SOVEREIGN VENTURES?
Transborder Corporations and the Politics of Offshore

by

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ABSTRACT

This paper seeks to analyse the challenges that the offshore finance/economy causes to the modern state sovereignty. The offshore finance consists of tax havens, flags of convenience registers, export processing zones, offshore financial centres and international banking facilities, and has grown to such an extent that if we want to understand the international political economy the offshore simply cannot be left unnoticed.

I approach the concept of sovereignty by adopting Giorgio Agamben's idea of the close link between sovereignty and the ability to issue a state of exception. Agamben argues that sovereignty is defined by the ability to issue a state of exception and that in contemporary world the exception takes increasingly often the form of a camp.

Albeit Agamben's theory focuses mostly on his idea of biopolitics, I find it imperative to extend its reach. Ronen Palan has shown how offshore jurisdictions commercialise their sovereignty by turning the right to draft legislation into a tradable asset. I will analyse the phenomenon of commercialised sovereignty by using Agamben's theory. The question is who has the *de facto* power to issue and control the commercialised states of exception within the offshore world? Can we see some kind of shift of sovereignty from states to non-traditional actors of politics?

My methodological approach to this question comes from international relations' constructivism. In line with Nicolas Onuf's constructivist method that operates around the concepts of structures and agents, I start by setting focus on how different types of offshore jurisdictions (structures) establish and use the states of exception. I will then analyse role of the agents that benefit from the special legislation, with particular focus transborder corporations.

Onuf argues that the relationship between agents and structures is not mechanical or rigid relation. I agree with him on this. I will take Onuf's point into account by presenting the connections that the politics of offshore has with larger trends of contemporary economical and financial globalisation Susan Strange's theory of the competition state will be extremely helpful in this research process.

After focusing on some empirical case studies I conclude that control of the state of exception within the offshore has, at least in some cases, partially shifted to transborder corporations. Therefore, there are some grounds for analysing transborder corporations as participants in politics

and bearers of sovereignty. I argue that these kinds of corporations should be called transnational, while their competitors that do not have significant offshore businesses are essentially multinational. Too often these terms are used interexchangeably and without proper definitions.

I end my paper by suggesting that our fixation on modern state sovereignty is badly outdated in face of the tremendous rise of the offshore world. In the final part I introduce one solution for overcoming the difficulties in combining national regulation with increasingly transnational corporations: the new accounting standards proposed by accountant Richard Murphy. The proposed standards would tax transborder corporations as global entities, thus making the regulatory or tax shopping in offshore by and large useless.

List of Abbreviations

BIS	Bank for International Settlements
CSR	Corporate social responsibility
EPZ	Export processing zone
EU	European Union
FOC	Flags of convenience
HNWI	High Net Worth Individual
IBF	International banking facility
IMF	International Montary Fund
IRS	Internal Revenue Service (of the US)
MNC	Multinational corporation
OECD	Organisation for Economic Co-Operation and Development
OFC	Offshore financial centre
TBC	Transborder corporation
TNC	Transnational corporation
UN	United Nations

1. Introduction

(1) “Taxes not only helped to create the state. They helped to form it. The tax system was the organ the development of which entailed the other organs. Tax bill in hand, the state penetrated the private economies and won increasing dominion over them. The tax brings money and calculating spirit into corners in which they do not dwell as yet, and thus becomes formative factor in the very organism which has developed it. The kind and level of taxes are determined by the social structure, but once taxes exist they become a handle, as it were, which social powers can grip in order to change this structure. However, the whole fruitfulness of this approach can here only be hinted at.” *(Schumpeter 1991 [1918], 108)*

Taxation is relatively rarely discussed topic amongst political scientists. Yet taxes are, as Joseph Schumpeter noticed nearly 90 years ago, a formative component of modern states. We cannot adequately address the functional logic of modern states without analysis of taxation’s role in shaping its structures. In most countries, taxes bring majority of the money that keep the state’s organs running. Taxes determine the size and scope of the state. And most importantly from the viewpoint of political science, once taxes exist they become a Schumpeterian “handle” for different powers in society to change state’s structures. Consequently, the decisions on tax rates and the nature of tax system turn out to be highly significant, contested and political issues. The agents in position to make decisions related to taxation obviously exert significant power in society.

Traditionally these decisions have been sole responsibility and right of the sovereign states. States have issued taxes and secured their collecting. This system has recently been challenged by two intertwined phenomena. First is a direct result of the economical and financial liberalisation of recent decades: countries around the world are turning to competition states that bet each other out for transborder corporations’ investments. Taxation is an important part of states’ competitive strategies, and so is regulation. Second, only rarely noticed phenomenon is the dazzling rise of the offshore economy. The offshore world consists of tax havens, export processing zones, offshore financial centres and flags of convenience registers–all are small (semi-)independent jurisdictions or juridically isolated areas within onshore states. These offshore structures have created a myriad of possibilities for avoiding or evading regulation and taxation for wealthy individuals, transborder corporations and international criminal networks. The offshore jurisdictions have commercialised parts of their sovereignty, and many market agents are more than willing to exploit these possibilities for their own advantage.

The offshore-onshore dichotomy is an important division throughout this dissertation. The dividing line is, however, partially artificial. One of

the most fundamental characteristics of offshore is its fictiveness: the offshore businesses take place within a 'legal fiction'. Transactions are often merely booked in offshore jurisdictions or areas within onshore states, while functional organs of these organisations may reside onshore on the other side of the globe. Onshore means here states where most of the economic activity has connection with the people or firms located there, i.e. most of the major developed and developing countries. Their characteristic feature is that principally transactions are booked, taxed and regulated in a jurisdiction where the businesses actually take place. We shall see later various examples on how offshore actually penetrates onshore economies in increasing number of ways, which is the primary reason why the onshore-offshore dichotomy has become increasingly problematic.

Finding a robust definition for two other important concepts, sovereignty and politics, is difficult as well. They are burdened with meanings that often contradict each other. I will begin this paper (part two) with inquiry to interrelated concepts of politics, political and sovereignty, relying on the writings of Carl Schmitt and Giorgio Agamben. According to Agamben, the ability to control the state of exception defines sovereignty and only sovereign has the capacity to engage in politics. I think that Agamben's ideas help us to grasp something very essential on what it means to do politics or act politically in the contemporary world– much better than if we would define politics, for example, as some sort of governance. The discussion about sovereignty will be weighed against ideas of competition state phenomenon. This will help us to differentiate the role of active political agency and politics from competitive pressures arising from economical and financial globalisation processes.

In part three I set my focus on how we could understand the offshore structures with help of the theory of the state of exception. I will introduce the ways how offshore jurisdictions rely on use of the state of exception case by case. This will help us to understand what parts of sovereignty are being commercialised when offshore jurisdictions create legislation tailored to suit investors' or corporations' needs. This enquiry is a necessary precondition for further analysis on the active political agency, i.e. in answering who actually has the capacity to control these exceptions after they have been commercialised and during the process of commercialisation? Finding answers to this question is the purpose of part four and also my main research question. I will start the analysis by introducing the limits that onshore governments' and international organisations' activities create for offshore jurisdictions. These two limitations are important for understanding the whole picture, but will be covered as shortly as possible. The reason for this is that it is self-evident that states exert sovereignty over others, and the role of international organisations in framing the world politics has also been studied before. My main purpose is to examine how transborder corporations can partake in creation and control of the state of exception.

The terminology for addressing contemporary corporate giants is not a straightforward issue. The reason why I have decided to address them with a general category of 'transborder' instead of multinational or transnational–two frequently used categories in both academic and popular literature–is intentional, as the 'multinational' and 'transnational' will, in the fourth part, be given contents according to their relation to the concept of sovereignty. It is not insignificant whether one speaks about multinational or transnational corporations, even though these two categories are usually mixed even in academic literature. Even though the term transborder corporation is not that common, it has been previously used for example by Jan Aart Scholte.[1]

There are relatively few existing books on offshore. This has had its own impact on the composition of my empirical material. I have been collecting the background material widely from different official documents (UN, IMF, OECD etc.) because of scarcity of this kind of up-to-date information, especially in a compact form that overcomes the different fractions of offshore. Therefore this work has also general educational purposes. I will rely largely on examples and case studies in my analysis. While the case studies are far from comprehensive sample of the offshore world, they are more than sufficient as archetypes for testing the validity of my arguments. I have chosen them in order to illustrate how the state of exception, offshore and commercialised sovereignty are being bundled together in different areas of offshore. Doing interviews and other on-site research in offshore jurisdictions would have been better way for collecting empirical material, but that would have been out of my reach–especially as my research questions require to focus on all aspects of the offshore world, not only to e.g. tax havens. The data and examples I use places this thesis to the field of international political economy. The international political economy is, however, a stepping-stone for gaining some insight into some of the political science's fundamental concepts.

The most important reference point for weighing the importance of empirical examples is the astounding size and scope of the offshore phenomenon. Albeit this issue will be covered in part 3, it is worth hinting here that more than half of world's money flows pass through tax havens, and that high net worth individuals possessing more than US$1 million in easily liquidated assets have deposited US$11.5 trillion in tax havens (a conservative estimate). The use of offshore financial structures by transborder corporations and international criminal networks is also a widespread phenomenon. International shipping industry is dominated by the use of vessels registered in flags of convenience jurisdictions, and significant proportion of world's industrial production takes place in export processing zones, especially in developing and transitional economies. All this has been made possible by the offshore and the fictional nature of state sovereignty.

[1] *Scholte 1997*

I have chosen international relations' constructivism as my methodology. It has been developed especially by Nicholas Onuf.[2] His constructivism is an attempt to find answer to age-old question of politics: should we focus our attention on political agents' action or to the structures in where they act? Agents include corporations, states, and so on. Inter-state system and global economical/financial systems are examples of structures. Onuf's constructivism proposes a third way that combines agents and structures. The relation between these two is a two-way process, Onuf argues. Agents act *on* structures. They shape those structures as they act, but their limits of action are also shaped by structures in this two-way process. Onuf's smooth division between agents and structures stems with the structure of this dissertation, as I start with introducing the offshore structures and continue with focus on agents operating in offshore.

2. Sovereignty and the State of Exception

2.1. The History of Sovereignty

The concept of sovereignty is burdened with meanings it has acquired during centuries.[3] It has been understood in relation to the definition of state, in relation to state's actual powers, and as a concept that defines the international system. Despite of these definitional difficulties, sovereignty has not turned into a meaningless idea. Even with all the talk about globalisation, states and sovereignty they possess do matter. As Camilleri and Falk note, "[s]overeignty, as both idea and institution, lies at the heart of the modern and therefore Western experience of space and time". If our conceptions of space and time are undergoing transformations, as Manuel Castells suggests,[4] these changes are inevitably either influenced by changes in the way sovereignty is being used or are caused by these changes in the first place. Understanding the foundations of sovereignty is therefore necessary in order to grasp what is happening to the state.

The history of sovereignty is also history of modern states. Strict territorial boundaries, absolute rule of the sovereign within its territory, and mutual recognition of other states' sovereignty within the inter-state system are all relatively modern products. The modern state sovereignty emerged only when these inventions became bundled together. As Ruggie notes, "[w]hile all states have made claims to territories, it is only with the modern nation-state system that exact borders have been gradually fixed."[5]

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[2] *Onuf 1999*
[3] *Camilleri and Falk 1992, 11*
[4] *Castells 2000 [1996]*
[5] *Held et al. 1999, 45*

The modern state sovereignty started to emerge in the medieval Europe, where a "non-exclusive form of sovereignty" prevailed. People were subject to different set of rules within same territory depending on their birth, residence and status.[6] Europe was divided into various kingdoms, duchies, principalities and semi-autonomous areas, all entangled in a complex web of alliances, dependencies and antagonisms. By the end of the 15th century, the number of these units had risen to approximately 500. This myriad of governance systems was connected by the 'divine law of God' and the all-reaching political influence of the Church. Even though kings were able to make contracts with their vassals and the vassals had power to make alliances with others, the authority of the Church transcended these kinds of local concerns. "[T]he law was not thought of as the creation of the political order" in the divine hierarchy.[7] The divine law was seen as external to the daily politics. It formed an objective set of values which made it possible to derive duties and rights in society.

As the age of feudal order coming to its end in the 16th century, the divine order of things started to tremble. The shockwaves and unrest caused by the Reformation was the hardest blow in face of the old system. In the Newtonian world that emerged to replace it, all things under the sky (and the sky itself) were ordered according to same principles. This was in stark contrast with the hierarchical order of the medieval world. An important consequence of this change was that the law itself became a relative concept. The states were no longer bricks in the carefully designed pyramid that created the divine order of things, but profoundly similar yet competing entities which inhabited and stretched their borders all over the globe. This mental shift was essential to emergence of the modern state sovereignty. The unity of subject that defined medieval thinking was being questioned by relativity that would later on become a familiar characteristic of international law. And the relativity of law became later an important factor as the first offshore jurisdictions started to surface.

The international system that emerged from the ashes of the European wars over religion differed markedly from medieval times. Instead of the decentralised political arrangements of the feudal Europe came out a system of strictly demarcated sovereign states with monopoly on the legitimate use of violence within their borders.[8] The law became linked with territory. Emerge of the capitalist market based on contractual relationships brought inevitable changes to the structure of state, society and sovereignty in turn of the 19th century. Before that time, the purview of the natural law was limiting the absolute control of the sovereignty, even though the rulers had, in theory, sovereign authority over their territories. The negation of the natural law system removed the last

[6] *Ruggie 1993 in Hudson 2000, 15*
[7] *Benn and Peters in Camilleri and Falk 1992, 13*
[8] *Camilleri and Falk 1992, 14*

shackles of the transnational ethics and the states became insulated and separated from each other.

It was not until the 19th century, then, before sovereignty started to express ”the exclusive, unique institutionalized and strictly public dominance over a territorial national ensemble and the effective exercise of central power without the extra-political restrictions of juridical or moral order which characterized the feudal state.”[9] With the absence of moral and ethical responsibilities, it was possible to locate the sovereign people as the bearer of rights and duties. Consequently, this shift made the more or less artificial group of “the people” also bearer of law. Sovereignty was transformed from the exclusive privilege of the monarch into an instrument of the government: to an issue that was open to debates, debacles and renovations.

National borders and practices that regulate international relations developed during the 19th century in forms of bi-lateral treaties and with emerging international law. This development resulted in contemporary system of insulated sovereign jurisdictions and created heated disputes over limits of sovereignty. Clear separation between national and international territories was introduced as a principle to the international law. As for example, the right to separate a ship’s source country and the country of residence became gradually acknowledged. However, disputes between national frontiers and international territories were common, and these debates were loaded with practical problems in attempts to overcome the tensions caused by overlapping powers.

The maritime legislation was used as a model for other disputes over sovereignty, but the development of technology brought constantly new challenges. The sea borders were first extended from the cannonball’s reach of 3 sea miles to 12 miles in the 19th century. With the introduction of zeppelins, hot air balloons and airplanes, the sovereign territory was transformed into a ‘three-dimensional cage’ and the upper limit of sovereignty was fixed to 50,550 miles. The altitude became known as Von Kármán’s line. Underground the ‘cage’ spanned all the way to the centre of the earth. Palan refers to Kish and claims that creation of this ‘cage’ marked the last step in the process where sovereignty spanned gradually the entire globe.[10] But contrary to this, some cracks remained. The last frontier (apart from space) for new territorial claims of sovereignty was actually not closed until in 1982, when emergence of the Sealand, a micronation[11] that declared sovereignty over a World War II

[9] *Poulanzas 1973 in Palan 2003, 92*

[10] *Kish 1973 in Palan 2003, 97*

[11] *The offshore world is indeed full of definitional fuzz and problems. Especially on the edges of offshore world one is confronted with terms like micronations,quasi-states, statelets, or bogus-states. I would refrain from calling Sealand a tax haven proper because of its very limited*

missile hull just outside the British waters, prompted the government of UK to lobby in UN for an agreement that became the Convention of the Sea. This convention "of all coastal countries of the world prohibited artificial structures becoming independent countries once and for all", thus constituting the final part in a process addressed as "closure of the map".[12] The cage was finally complete.

Through these kinds of debates and their compromising solutions in the latter part of the 20th century we have finally entered in endless discussions over source and residence countries of international money transfers and transborder corporations' activities. The end of these conflicts is unforeseen as long as the concept of sovereignty will not go through a serious transformation. This does not seem like a plausible option at the moment, but the corrosive forces within the system of state sovereignty mark possibility for change in the years to come. The important thing to notice, however, is that even though the modern sovereignty was perceived as absolute both in relation to states' internal matters and to sovereignty's geographical reach, this absolutism was largely a fictional product. If we want to find out whether modern state sovereignty has changed, it is against this background that the possible changes need to be weighed.

2.2. The State of Exception

The sovereign is defined by its ability to create and control the state of exception. This Giorgio Agamben's definition of sovereignty will serve as the theoretical starting point for my inquiry. Too often sovereignty is defined ambiguously as potentiality to exert power within particular territory or in some other way that leaves open *how* the sovereign establishes and maintains its power. Defining sovereignty from its outcomes and not from its foundations means that we go around in circles. Today, increasing number of struggles over power and authority are fought over issues that are not really located in any particular territory, or are located in many territories simultaneously. Sovereignty should be defined separately from its territorial limits, and Agamben's approach helps us to accomplish this task.

There are two immediate questions we have to tackle. First, what does the state of exception mean? And second, how is it created and controlled? To begin with the first question, it was Carl Schmitt who first discovered and conceptualised the connection between sovereignty, politics and the state of exception in the 1930s in the context of the modern 'total state'. The total state penetrates its power into its citizens' private lives: as a result, all domains the state has infiltrated become

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authority over anything, with only couple of inhabitants and lack of international acknowledgement.

[12] *Kochta-Kalleinen 2003, 44*

potential sources of political conflicts.[13] The division between politics and political is an important one. Doing *politics* is the exclusive right of the sovereign, but all issues that the state penetrates have potentiality to enter the *political* by becoming publicly contested topics. My focus in this dissertation is on politics, not political. Schmitt illustrates this division by stating that in the formation of total state "what had been up to that point affairs of state become thereby social matters, and, vice versa, what had been purely social matters become affairs of state–as must necessarily occur in a democratically organised unit."[14] Politics means neither some kind of model for governance nor an all-encompassing term for issues that become publicly contested, e.g. in a sense that "personal is political". What it does mean is potentiality for autonomous, creative and unconstrained action. In the modern world Schmitt saw that this freedom was fundamentally limited to sovereign states. For him, the ultimate manifestation of the sovereign power was the decision upon war and peace.

Plenty of time has passed since Schmitt created his theory of the state of exception. The way world has changed has led many authors to question the relevancy of some of his basic presumptions, especially the central role given to war as the ultimate state of exception. The state of exception that manifested earlier overtly as special legislations or decrees has become, by and large, embedded in the normal functioning of contemporary states. The authorities do not necessarily need to overtly declare a state of exception, because in many cases this can be done as a mere administrative order. The role and nature of the state has changed as well, because globalisation processes and rise of the so-called competition state change the international environment where states operate. In many cases war is not necessarily even a viable option for states that wish to expand their influence or gain power, as other (often economical) concerns have replaced it.

Giorgio Agamben has traced the use of the state of exception from the French revolution to the major European conflicts in earlier part of the 20th century. The state of exception has been a definitive element in the European politics during the 20th century and after. It was explicitly used in Weimar Germany for hundreds of times, and as a regular tool in other European states as well. Internal unrest, as well as economical hardships, served as a justifiable cause for claiming a state of exception.[15] Throughout the 20th century, the state of exception became gradually an inherent part of our legal systems. Agamben notes that "[u]nder the pressure of the paradigm of the state of exception, the entire politico-constitutional life of Western societies began gradually to assume a new form, which has perhaps only today reached its full

[13] *Schmitt 1976 [1932], 22*
[14] *ibid.*
[15] *Agamben 2005, 14*

development."[16] The state of exception that was first used primarily as an emergency measure covers today a wide number of areas.

The status of refugees is the most striking example and proof Agamben gives for his claims. He argues that Schmitt was wrong when he raised the capacity to issue war as the ultimate state of exception. Instead of war he stresses states' capability to issue a 'camp'–a place where normal human rights and constrains for the state's coercive power do not apply. Agamben says that the novelty of concentration camps was in dehumanisation and violence directly mediated through the state's legal structure. The horrifying results of this connection were seen in their full scale in Nazi Germany. The persons that were put into concentration camps–irrespective of whether the camps were in Germany, Russia or elsewhere–were "*excluded from the scope of law and included to the legal system through this exclusion*".[17] This definition forms the ultimate test of sovereignty. Mundane maintenance of laws and legal order can not be the meter of sovereignty. The important thing to ask is who has the power to decide when these laws *do not* apply. War is one example of this kind of situation and the camp is another.

Agamben claims that today camps take many forms, including temporary detention centres, airports' international areas and other similar places. The camp is present every time when something is excluded from the scope of law through law's own mechanisms, and included to the system through this exclusion. As a result, "what emerges in this limit figure [of the state of exception -MY] is the radical crisis of every possibility of clearly distinguishing between membership and inclusion, between what is outside and what is inside, between exception and rule."[18] Something is taken out from the sphere of seemingly universal and all-encompassing law and paradoxically included to the legal system through this exclusion.

I think the possibilities for practical application of Agamben's theory of the camp are much wider than in his own analytical field, biopolitics.[19] Focusing only to camps that are created for 'illegal aliens' gives us a tilted image of sovereignty. It leaves out other important areas where states exert their sovereignty, especially the sphere of economics and finance. As a result, the theory of sovereignty will remain powerless in coping with many of the contemporary globalisation processes. Fine, the relationship between state and citizenship has changed as more and more people are excluded from the basic rights guaranteed by seemingly universalistic

[16] *Agamben 2005, 13*
[17] *Agamben 1998, 17-18*
[18] *Agamben 1998 ,134*
[19] *Agamben's idea of biopolitics owes much to the works of Foucault, but his texts often lack clear references. Being through and through philosophical writer, it is difficult to clearly categorise Agamben in wider paradigm of biopolitical approach.*

declarations of rights, but what about the challenges that states' changing roles and options in world economy has created to sovereignty? Could we find examples of similar camps in world economy as well? We need to step out of the empirical examples of biopolitics and challenge Agamben's thoughts in macro levels of world economy and finance.

In order to do this, some questions need to be answered. What it takes to issue a state of exception; control it; and to dismantle or cancel it? Could these operations be measured with same standards, or do they require different analytical treatment? For a state to be completely autonomous and sovereign it needs to have genuine monopoly in each one of these fields. Making a special legislation for a detention centre with limited possibilities to control it or close it can not be a sign of full sovereignty. Neither can one be fully sovereign by having a capacity to stop a war that some other sovereign has started but no power to decide when or how to start one. It is possible to think of a situation where a partially occupied state drafts special legislation for allowing a foreign country to set up military bases in its territory. Drafting the legislation is a sign of sovereignty, but inability to control its outcomes means that this sovereignty is not absolute. Occupied Iraq is one example of this kind of situation. Afghanistan is another contemporary case where central government controls the capital and is able to hand over some of its area for foreign troops to secure. Much of the country is, however, under *de facto* sovereignty of local warlords. Contemporary sovereignty is, then, something that can be given, taken and negotiated, just as the short inquiry to the history of sovereignty suggested. Issuing the state of exception, controlling it, and cancelling it should be viewed as separate processes.

The world's economical and financial context for this inquiry is that of the competition state. Introduced first by Philip Cerny in 1990 and developed later by Susan Strange, this theoretical framework gives the best tools for connecting the economical globalisation processes with the theory of the state of exception. Together these two approaches help us to avoid the trap of examining economical globalisation processes merely in quantitative terms (increased trade flows, investments etc.) or by referring to vague and ambiguous changes in how global businesses are re-organising themselves (the network enterprise etc.). These kinds of approaches would tell us little about what is happening to the state. On the other hand, narrow focus on active political agency and sovereignty would ignore the indirect impacts of the competitive pressures of economic and financial globalisation. Both sovereignty and the economical globalisation (competition state) should therefore be taken into account. We need to set the focus on both the active political agency shaping these processes (sovereignty) and on the structures where this happens (competition state and the offshore structures). This approach stems well with Onuf's constructivist methodology, helping us to look at the relationship between agents and structures as an interactive two-way process.

Strange argues that as states have lost their monopoly of politics and their ability to intervene in many economical processes, they have been transformed to competition states that can and need to negotiate agreements with transnational corporations (TNCs).[20] This is a result of corporations' growing ability to affect the structures where they operate and persuade individual states (especially developing countries) into favourable agreements. What is new and unusual in this power shift "is that all–or nearly all–states should undergo substantial change of roughly the same kind within the same short period of twenty or thirty years."[21] TNCs (to use Strange's terminology) have become central organisers of the world economy, transferring some powers from civil society to corporations and creating some "no-go areas where authority of any kind is conspicuous by its absence."[22]

Strange's book is a vivid analysis on how corporations' bargaining power over states has increased. However, her narrow conceptions of power and politics reduce its usability. First, Strange defines politics in very loose terms as "common activity," thus ending up with statements like "they (TNCs) themselves are political institutions, having political relations with civil society."[23] While this statement is presumably accurate, we would need different set of tools for analysing TNCs internally as a political institution on the one hand, and analysing TNCs' relations with outside world on the other. Second, Strange divides power in political economy in two rather narrow categories: structural power and relational power. Relational power refers to power between political agents, manifested when one political agent attempts intentionally to affect the behaviour of another agent. Structural power, on the other hand, means literally power over structures, thus shaping all power relations within the affected structure (security structure, financial structure and so on).

What is missing from Strange's analysis is the viewpoint of sovereignty and law. Even though she notes that transnational corporations' activities have created no-go areas which are characterised by absence of any authority, she neither asks what kind of authority this absence creates nor ponders how the politics of these "no-go areas" is different from, say, intra-firm political contestations. It is evident that no power vacuum within social relations can remain void for long time because all structured social relations necessarily imply some kind of power relation. Therefore we need to ask what kind of authority has occupied these "no-go areas".

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[20] *Strange 1996, 85-86. The term TNC will be used here for retaining consistency with Strange's text. Strange does not clarify why she has chosen the term over MNC or other alternatives.*

[21] *Strange 1996, 87*

[22] *Strange 1996, 46*

[23] *Strange 1996, 13, 44*

Strange's approach can, of course, be a deliberative choice. Describing the larger structural currents that shape the world economy is an ambitious task in itself. Whatever her motives were, however, I think that through the analytical lens of sovereignty we can gain an insight on how the relational power can actually become structural power. This might happen in cases where use of power helps to gain access in the control of the state of exception–this is an issue that Strange's division of power does not cover. In order to analyse this kind of phenomenon we have to concentrate on the relationship between law, sovereignty and these "no-go areas" where transborder corporations presumably operate. If we are able to prove existence of the link between the power to control the "no-go areas" and transborder corporations it would mean that the corporations actually operate in the sphere that has traditionally been monopoly of the states–not only in terms of power, but also in terms of politics. This is a crucial part of the connection I am analysing here.

Let's take bit closer look on how the competition state phenomenon could relate to the state of exception and sovereignty. Strange shows how transborder corporations have become central organisers of the world economy because they are able to compete states against each other for favourable agreements. Another, less important issue is that this change has shifted the "limits of cooperation, and the competition, between states and thus to shifts of power as well as wealth between states."[24] From the viewpoint of state sovereignty this means that states have, besides of starting to compete with their general business environments, began to create special legislations that reserve the most favourable treatment to foreign investors or companies. That is, they have commercialised their sovereignty[25] by creating states of exception suited for the age of the competition state. This is the reality especially for less developed countries that struggle with their attempts to attract foreign capital.

On the other hand, it is possible to claim that the only new thing with this development is its enormous scale. States have attracted foreign investments with special exemptions earlier as well. This is indeed the case if we assume that the special exemptions are still controlled solely by the states and companies are mere 'customers' who merely decide whether to accept state's offers or not. Within the assumed modern state system where sovereignty is the exclusive right of the state, corporations should not be able neither to control the exceptions created for them nor to decide how and when they are cancelled. They may be making tough choices between employment, tax revenues and other factors, but nevertheless options for discarding the exceptions do exist.

[24] *Strange 1996, 46*
[25] *Palan 2003*

Or do they? Could we think of a situation where states would no longer have either the monopoly for issuing a state of exception, to control it, or to decide when and how it is cancelled? When the use of the state of exception becomes increasingly commonplace and, at the same time, the competition state phenomenon blurs more and more the line where voluntary adaptation to the "race to the bottom" actually becomes the only option for at least to the weaker and less developed states, this could indeed be the case. It is already difficult to accurately point out who effectively controls the sovereignty in take-it-or-leave-it negotiations between International Monetary Fund (IMF) or World Bank and developing nations. At the heart of many of these negotiations are questions of how to create a 'favourable business environment' for foreign investors and corporations.

It is often fruitful to examine transition phenomena at their 'outskirts' in extreme situations. We may not know whether the mainstream development actually proceeds towards the extreme, but in any case it reveals what is possible and what can become mainstream current in the future if the marginal phenomenon is allowed to nourish and grow. Doing politics is all about understanding what is possible in given situation and how to stretch or reduce the limits of possible. In world economy the extreme playground for the competition state and experiments with sovereignty is undeniably the offshore finance–or offshore laboratory, as Christopher M. Le Marchant has quite illustratively addressed it.[26] Therefore, I believe that focus on offshore and transborder corporations can reveal us something important on the nature of sovereignty, politics and their connections with contemporary economical and financial globalisation.

3. The Offshore Structures

3.1. Introduction to the Offshore Finance

"There was the "European Union Bank" of Antigua, which operated on the Internet on a license from the corrupt government of Antigua. The computer server that handled the bank was in Washington, D.C. The man who was operating the computer server was in Canada. And under Antiguan law, the theft of the bank's assets was not illegal. So now the problem is, where is the crime committed? Who committed it? Who is going to investigate it? And will anyone ever go to jail?" *(Investigator Jack A. Blum in a U.S. congressional testimony,* Tillman 2001, 21*)*

Antigua is a pleasant tourist resort located in the midst of Caribbean. It neighbours a couple of other small islands that few people know about, such as Barbuda, Montserrat and St. Kitts & Nevis. Antigua's land area extends to barely 280 square kilometres, and the state of Antigua and Barbuda has no more than 68 000 citizens. According to Antigua's tourist

[26] *Le Marchant 1999*

office's homepage, it is "the Caribbean you've always imagined".[27] The definition is illustrating, but in a different sense than the tourist office probably had in mind: Antigua and its neighbouring islands make a brilliant example of the common image of tax havens. The island has all the necessary qualities for meeting the popular standards; such as thickets of shady palm trees, empty beaches that stretch to the horizon, eye-catching coral reefs, and pleasant climate for that final touch. U.S News and World Report noted that in the late 1990's it also had "a virtually unregulated banking industry, no reporting requirements and secrecy laws that punish violations of bank clients' confidentiality. --- [A]nyone with $1 million can open a bank, and many consist of nothing but a brass plate or a room with a fax machine". [28] Antigua has since then introduced some new anti-avoidance legislation, making it bit classier and more up-market tax haven. The example could, however, be from many other havens as well.

When we discuss the world of tax avoidance or criminal tax evasion,[29] focusing merely on distant paradise islands such as Antigua (or its counterparts like Aruba, Montserrat, Cayman Islands, and Vanuatu) would be misleading. Albeit they are and have been playing an important role in the processes of financial liberation and intensifying tax competition, the global framework for avoiding taxes and/or regulation is much greater in both scope and intensity. Tax havens such as Antigua and their better known predecessors like Switzerland, Luxemburg and Monaco are major players. But there is also enormous number of loosely regulated and monitored financial transactions conducted 24 hours a day in Offshore Financial Centre (OFC) Euromarket in London and International Banking Facitilies (IBFs; located in different cities of U.S., Singapore, Frankfurt, Malaysia's Labuan, Tokyo etc.). We should also take into account Export Processing Zones (EPZs), designed for often low-tax, lightly regulated production of industrial products; and Flags of Convenience (FOC) which are used for similar purposes by international shipping industry.

The instruments of low or zero taxation and/or regulation are made possible by so called "legal fictions"[30] of tax havens, offshore financial centres, international banking facilities, EPZs and FOCs, all characterised by reliance on the state of exception in one way or another. The whole

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[27] *Antigua and Barbuda Tourist Office*

[28] *U.S. News and World Report quoted in Blum* et al. *1997, 47*

[29] *Tax avoidance means "seeking to minimise a tax bill without deliberate deception." Tax evasion, on the other hand, means "[t]he illegal non payment or under-payment of taxes, usually by making a false declaration or no declaration to tax authorities; it entail criminal or civil legal penalties." (Tax Justice Network 2005b) In this dissertation my interest will be mainly on tax avoidance, because I want to explore how offshore can be exploited in legally acceptable ways.*

[30] *Picciotto 1999*

phenomenon of these legal fictions goes under the umbrella term offshore finance. Prem Sikka argues, referring to Hampton, Abbott and Christensen, that offshore financial centres "play a key role in facilitating growing mobility of finance and shaping complex webs of interactions and relationships involving the nation-states, multinational corporations, a wealthy elite and ordinary citizens."[31] Indeed, the sheer magnitude of financial flows and economic effects associated with offshore is staggering:

- According to IMF, over half of the cross-border transactions are passing through offshore financial centres and tax havens[32]
- According to the Global Tax Justice Network's research, based on cross-comparison of three independent sources, approximately US$11,5 trillion of assets are held offshore by high net-worth individuals who possess more than US$1,000,000 in easily movable assets[33]
- Major tax havens comprise of less than one percent of the world's population and 2.3 percent of world Gross Domestic Product (GDP), but host 5.7 percent of the United States' foreign employment and 8.4 percent of foreign property, plant and equipment of American firms[34]
- In US, 61% of domestically owned companies paid no federal taxes at all in 1996-2000. With foreign-owned firms the figure was even higher.[35] The numbers are remarkably high, more so because the period of 1996-2000 was time of economical boom. The offshore facilities play key role in companies' tax avoidance schemes.
- Capital outflows from Africa to U.S. resulting from transborder corporations' explicit mispricing of imports and exports added up to more than US$31 billions total in years 1996-2005. This equals 7.7% of all the trade between African countries and U.S and includes only the most exaggerated mispricing cases.[36]
- The number of tax havens has risen from about 30 in 1980's to more than 70 according to some estimates[37]

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[31] Sikka 2002, 3; Sikka uses term Offshore Financial Centre to address both OFCs and tax havens. This terminological confusion exemplifies how new and not yet established subject of academic study the offshore finance is.

[32] Errico and Musalem (1999), 10

[33] Tax Justice Network 2005a; on high net-worth individuals Capgemini & Merrill Lynch 2004

[34] Hines 2004, 16

[35] General Accounting Office 2004, 6

[36] Pak 2006

[37] Sikka 2002, 3 – The inaccuracy is result of difficulties in finding a consistent and commonly agreed meters for defining a tax haven

Many of these figures are estimates because of the lack of reliable statistics and the strict secrecy laws and practices that characterise offshore. The purpose of these figures is to give hint about scale of the phenomenon–and it is indeed enormous. There are few international institutions that gather data on international finance, such as OECD, IMF and the Basle Committee, but their scope of action is limited by the role that states and market self-regulation leaves to them. When it comes to offshore jurisdictions, the co-operation tends to be limited to some work against money-laundering and other financial crime. And even in these fields finding a consensus is difficult, as EU's internal struggles over contents of the Savings Directive and the Third Directive on Money Laundering have shown. Business groups do not want see their profits or services to be curbed, and nations that can benefit from unregulated financial services, such as UK or Luxemburg, can act as watchdogs against broad international agreements. All these issues make it more difficult to gather information.

Many of the impacts that offshore jurisdictions cause to onshore states and world economy are related to the competition state phenomena. It can easily be seen, without any references to states of exception or to sovereignty, that the competitive pressures and loopholes offered by offshore jurisdictions push onshore states to lower their level of regulation and tax rates in order to compete for firms, rich individuals and investments. These competition state effects will not be analysed here through and through, but it is nevertheless important to get grasp of the phenomenon in order to understand the effects of commercialised sovereignty and the uses of the state of exception in context.

The relationship between competition state and offshore is first of all related to changes in income distribution. The governments in both global North and South are losing massive amounts of tax revenues because of tax avoidance and evasion by both wealthy individuals and corporations. Were offshore finance not to exist, these activities would become much more difficult, not even to mention that many possibilities for lowering the tax burdens would become unavailable permanently. The increased tax revenues would open more political windows to states. For corporations that avoid taxes it would mean less profits, for wealthy individuals smaller rates of return from their investments, thus levelling the competition and bringing all market agents closer to the same competitive ground. International criminal networks would find it much harder to launder their profits.

The impact that tax avoidance, tax evasion and tax competition is currently causing to the global South is particularly remarkable. In developing countries the cost of lost tax revues caused by transborder corporations and lost interest income is estimated to be about US$50 billion, which accounts to about half of the world's development aid.[38] In

[38] *Oxfam 2000, 10; OECD 2006*

addition to this, it has been estimated that the capital flight from developing and transitional countries tops up to US$500 billion, of which about US$200 billion is result of transborder corporations' tax avoidance, US$50 billion comes from corrupt practices, and US$250 billion from other forms of capital flight.[39] As developing countries lack competent bureaucracy, including sufficient number of tax inspectors, it is naturally much easier to conduct aggressive tax avoidance schemes there than in developed countries. The discrepancy between highly paid corporate tax advisors and accountants, and developing countries' often under-staffed, under-resourced and at times corrupted administration is evident. Raymond Baker claims that "I have never known a multibillion-dollar, multiproduct corporation that did not use fictitious transfer pricing in some part of its business to shift money between some of its entities."[40]

International effects of offshore finance are also related to income re-distribution between countries. While the distributive effects arise partly from developing countries' innate corruption and mismanagement that makes it possible to shift enormous sums of potential tax revenues abroad, they have also very much to do with large onshore nations' legislation and with major intermediary companies operating in big financial centres of London, New York, Paris, Tokyo etc. This should be called the dirtiest side of the competition state phenomenon. Many industrialised countries, with U.S. in forefront, accept money that as been laundered abroad as a legitimate investment in their country.[41] Furthermore, banking interest groups in both U.S. and European Union have strongly opposed all new initiatives to tackle money laundering if they have included any extra responsibilities for banks.[42] There are also many examples on accounting giants' role as facilitators of tax avoidance

The giant corporations and wealthy individuals benefit from the existence of offshore finance because expensive expert services required for exploiting the offshore facilities are easily available for them. This creates a competitive edge for those who are already in good market positions because of economics of scale. The result is even bigger boost to competition state as business detaches itself increasingly from limitations of location and enters the legal fictions of offshore. This self-feeding circle is constantly shaping offshore structures, market agents who use offshore services, and in larger scale the whole competition state phenomenon. The states' and international organisations' responses to the challenges of the offshore world are likely to be reactions to the social and economical costs of these larger trends, not to conceptual changes in sovereignty or erosion of the state.

[39] *Financial Times 2004a, Tax Justice Network 2005b*
[40] *Baker 2005, 30*
[41] *Baker 2005, 189*
[42] *Baker 2005, 179, 189*

All these effects have their impacts on the competition state phenomenon. As the number of HNWIs and transborder corporations increase, so does the demand for offshore services. Therefore the competition state effects of offshore have thus far worked as motors in further extending the offshore world's scope and reach. This development is not, however, inevitable, and it is also possible that the international and national competition state phenomena may lead either to 'comeback of the state' (in comparison to Strange's retreat of the state), some form of global politics, or even a combination of these two.

3.2. Introduction to Earlier Studies on Offshore

Save for several discussion papers and some prominent books, the social scientific literature on offshore is scarce. The offshore was, after all, conceived largely as a minor aspect of world economy for several decades. The first important account on tax havens as an issue that has impacts outside the economics was Richard Anthony Johns' work "Tax Havens and Offshore Finance" in the beginning of 1980s. After him there was a long pause before literature on offshore started to be published in greater number in the last half of the 1990s. The first book I will cover here is Mark Hampton's doctoral thesis "The Offshore Interface".

Mark Hampton introduced the term offshore interface to address the various manifestations of offshore that, bundled together, create a system that undermines national governments' abilities to impose higher taxes, facilitates money laundering and hampers efforts to regulate financial capital.[43] The term is quite illustrating. Offshore is essentially an interface that smoothes the difficulties in overcoming the national legislation and divided nature of transborder corporations that as such do not exist as law, as we shall see later in this dissertation. It is no wonder that many corporations have so-called coordination centres in tax havens. Their purpose is not (at least only) to lower tax burden but function as nodal points for international operations that always require compromises and adaptation to varying legal environments in different countries. An interface could not exist on its own, without a relation to at least two outside entities. Neither could any of these coordination centres.

Alan Hudson approaches offshore from other perspective. He uses term "offshore unbundling" to describe the changes in sovereignty that offshore finance has initiated. Hudson notices that because "sovereignty is the dominant principle of differentiation in modernity the reworking of sovereignty provide evidence of a transition to a 'postmodern' geo-political economy."[44] Hudson argues that power is most likely contested on its margins because "borders are the dividing lines between cultures, communities and value systems" and that offshore is one significant

[43] *Hampton 1996, 1*
[44] *Hudson 2000, 16*

margin for contemporary shifts in power. This idea has much in common with the concept of offshore interface.

The offshore unbundling means basically shift from undivided, modern state sovereignty to a world system where ability to exert power in particular territory has become separated from capacity to tax economic activity within that territory. Hudson titles these two aspects as legal sovereignty and fiscal sovereignty. He sees that emerge of "stateless monies" (the Euromarket, will be dealt with later) was one important symptom of this shift towards postmodern geopolitical economy. Today, the tax havens still possess their legal sovereignty, but they have surrendered the fiscal sovereignty to tax the economic activity taking place within their terrain. This development that was initiated in tax havens is ultimately leading us to the world of postmodern political economy.

I think that albeit Hudson's theory helps to explain some important characteristics of offshore, it is still bit too straightforward in regard to its conceptions on sovereignty. Furthermore, it focuses too much on ability to tax, whereas regulation is an important aspect of offshore, too. Hudson sees sovereignty as "the principle which gives states the authority to set the rules for activities which take place within their borders."[45] There seems to be a background assumption here that these rules would be uniform in the 'normal' state of affairs, but as Schmitt and Agamben has shown to us, this is not the case. Tax havens are not surrendering half of their sovereignty, because in giving up their authority to tax certain economic activities they are precisely using the most essential feature of the sovereignty–the ability to create a state of exception. It is a whole another question to ask how easily this state of exception could be cancelled and who has the *de facto* power for it.

Ronen Palan is an author whose ideas are cited more or less throughout this dissertation. He stresses that the roots of offshore are very much onshore, albeit there is no single reason why offshore emerged.[46] Sovereignty has not undergone a radical change because of globalisation. Rather the aspects that have been a central part of sovereignty for decades–the ability of having competing claims for international activities and the fictional nature of citizenship–are increasingly being exploited by tax havens and their users. The world's changed political and financial architecture allows them to do so better than before. Palan thinks that the growing influence of offshore finance can be captured with term 'commercialised sovereignty', which indeed is an illustrative conception. I think that instead of commercialising only part of their sovereignty, as Hudson suggests, the ability to issue a state of exception has become commercialised.

[45] *ibid. 2*
[46] *Palan 2003, 8-9*

Palan endorses the holistic approach to offshore exploitation of sovereignty by noticing that "[a]s sovereignty is packaged and commodified, it is turned into a service commodity whose price can be reckoned with some accuracy."[47] This development is a result of the inherent contradictions between national, insulated sovereignties and internationalising capital. The capital operates in *inter-national* space, not in some homogenous legal system. Therefore the birth of offshore was partly an unintended consequence of the insulation of state sovereignty. The offshore finance was formed when this structural background was combined with different political factors.[48]

3.3. Tax Havens

I will start the inquiry on how offshore structures are intertwined with the state of exception by focusing on tax havens. The most popular definition of a tax haven comes from the OECD. According to the organisation, tax haven is a jurisdiction that levies no or nominal taxes, with at least one of the additional characteristics: it lacks effective exchange of information; it lacks transparency; and/or it hosts many businesses that have no real economic activities in the jurisdiction (so-called ring-fencing).[49] There are many other definitions as well,[50] but I think that OECD's version is particularly illustrative and useful. It is not only established and widely appreciated, but helps us also to distinguish tax havens from offshore financial centres and international banking facilities. The terminological confusion with tax havens and OFCs is widespread even in academic literature, with interexchangeable use of the terms being common.

There are currently about 70 tax havens in the world, and their number has more than doubled since the 1980s. The intensifying competition between tax havens has resulted in specialisation and widening portfolio of services offered to individuals, banks, and other corporations. Some tax havens are making money with niche 'products' like rerouting of international sex calls, sale of citizenship, and internet gambling. As quoted in the introduction of this part, IMF estimates that more than half of world's financial flows pass through tax havens and a conservative estimate is that US$11,5 trillions have been deposited to tax haven bank accounts by wealth individuals. Corporations' use of tax havens in tax avoidance and mispricing schemes is also widespread, as for example Simon Pak's research (section 3.1.) suggested.

History of the relationship between tax havens and the state of exception is closely linked with the general history of sovereignty and development of the modern welfare states. The fundamental characteristics of tax havens arose from three different strands:

[47] *ibid. 61*
[48] *ibid. 86-88*
[49] *OECD 2001a, 4*
[50] *Sikka 2002, 3; Hampton 1996, 15; Starchild 1994,1*

development of the modern banking secrecy laws; emerge of the corporate tax havens in the U.S.; and development of banking havens for wealthy individuals. These episodes took place in the time span between 1890s and 1930s, i.e. much before tax havens started to attract wider popularity (apart from Switzerland with its long history as a financial centre).

Switzerland is home of one important characteristic of tax havens–the modern banking secrecy. Albeit this Alpine country has been a significant financial and banking centre for centuries, there was something new in the banking secrecy legislation established in the 1920s. The earlier banking secrecy was a legacy from an era before strong, centralised states. Faith argues that it was merely a variant of the professional secret present in Roman law, binding doctors, lawyers and clergymen.[51] Fehrenbach follows similar line of thinking as he notes that "the principle of bank secrecy is far older in law and custom than non-secrecy". Opening up of the private financial affairs to authorities is actually "a by-product of the modern 'national' society". Up to the eighteenth century this kind of secrecy was taken for granted everywhere in Europe.[52]

As the modern 'national' society emerged, things changed so much that in the beginning of the 20th century, before the First World War, Switzerland's banking secrecy had become a major boon for investors. The great flood of gold into Switzerland began into 1920s, because "Europe changed and Switzerland did not."[53] In other words, majority of European states started to build state infrastructure and welfare state structures relying on higher tax rates and wider tax base, but tax havens decided this path was not for them. In order to strengthen its credibility as a reliable financial centre, Switzerland established the Banking Code in 1934, marking the birth of the modern banking secrecy. The code was unique compared to all other bank secrecies in that it "was written into *penal law*, and it was *specifically and deliberately applied to all government*."[54] Law stated that only two or in most three bank officials were allowed to know the identity of number account holder, and that by breaking the law one could be sentenced into imprisonment.

Did Switzerland commercialise its sovereignty with the Banking Code? Did it create a exception that would start to erode the basis for its legal unity? The answer is simple: no. The Swiss law was universal in its scope, and bound all government officials and customers alike. The secrecy laws and practices became part of the state of exception that characterises tax havens so well only in later decades, when copy-cat jurisdictions started to challenge Switzerland's status as *the* tax haven. Albeit the Swiss banking secrecy marked birth of the first characteristic of

[51] *Faith 1983, 79*
[52] *Fehrenbach 1966, 74*
[53] *ibid. 49, 62*
[54] *Fehrenbach 1966, 75*

tax havens, the beginnings of the connection between offshore and the state of exception have to be sought elsewhere.

Another strand behind emerge of tax havens–and behind emerge of the modern tax competition as well–can be traced back to the United States of the end of the 19th century. When it comes to corporate taxation, the first tax havens were the states of Delaware and New Jersey. They created corporate legislations that enabled corporations to create fictional headquarters with no genuine economical links to these states. Advised by a New York lawyer, the New Jersey's government decided to impose a franchise tax on all corporations incorporated in New York. This happened in 1890s. According to the scheme, New Jersey was to "liberalize her laws regarding corporate regulation to an extent that would make it advantageous for all corporations to be organized under her protection."[55] In 1898, Delaware decided to follow New Jersey's example, thus creating the famous concept of Delaware Corporation. In period of 1902 to 1919 the number of corporations incorporated in Delaware rose from 1407 to 4776.[56] Today the state claims in its website that 58% of Fortune 500 companies reside there.[57]

The novel thing with New Jersey's and Delaware's legislation was that they were the first ones to exploit the divided nature of corporate citizenship (an issue that will be elaborated in ch. 4) as a tool for tax competition. The corporations in Delaware did not need to have physical presence in the state–maintaining a registered agent was enough. This created an exception that enabled corporations actually residing in other states to create fictional headquarters there. *As for corporate taxation, the erosion of Schumpeter's "tax state" began at this moment*. It was not a state of exception from the viewpoint of the state of Delaware, as the law was applied to all corporations. But the sovereignty that enabled Delaware to introduce its corporate law created an exception within United States. From the viewpoint of sovereignty, the status of Delaware and New Jersey is therefore somewhere between tax havens and export processing zones, depending on the angle from which one examines the issue.

The policies of New Jersey and Delaware marked one important milestone in the emerge of corporate tax havens, but the Channel Islands played an equally important role in development of tax havens' banking facilities. As the U.K's business lobby managed to get the co-operation requirements for the Channel Islands watered down, the islands became tax havens for private investments in the 1920s-1930s.[58] They still lacked the banking secrecy laws, but the U.K decision was nevertheless one significant step towards the rise of modern tax havens. The British

[55] *Lindholm 1944, quoted in Palan 2003, 101-102*
[56] *Palan 2003, 101*
[57] *State of Delaware 2005*
[58] *Picciotto 1999, 51*

attempts to enforce taxes on British citizens abroad were often hampered by non-compliance of foreign countries, which apparently created a incentive for jurisdictions like Jersey to continue developing their tax haven policies. The sovereignty to tax individuals and especially corporations was therefore a contested issue already in the 19th century. The state lost many important battles in regard to rights and abilities to tax its newly created corporate citizens.

Delaware and New Jersey were tax havens for non-local corporations, not for home-grown entrepreneurs. Similarly the Channel Islands' tax exemptions were not available for local citizens (not that majority of them would have had any significant assets to invest anyway). This clarifies an important characteristic of offshore jurisdictions, namely ring-fencing. Basically it means that different set of laws is applied to domestic and foreign individuals or enterprises. The access to zero tax rates, lax business regulation or low capital adequacy requirements is very often restricted to non-nationals. One example of this method of allowing corporations to do business abroad, but not in the host country, can be found from the insurance industry. A number of Caribbean countries allow insurance companies to sell their policies abroad with minimal or even zero capital reserves. In 1993 in Turks and Caicos alone there were 1,488 of these licensed insurance companies.[59] Banking industry would offer strikingly similar examples, not even to speak about masses of dummy or 'brass-plate' corporations registered in tax havens.

Ring-fencing is *the* mechanism for tax haven jurisdictions for issuing a state of exception. After part of the legislation that regulates economic activities have been ring-fenced outside the legislative framework of domestic regulation, the control of this ring-fenced part can, if desirable, be further outsourced to market agents either as an administrative order or under veil of secrecy. The ring-fenced tax and regulatory vehicles equal in economic and financial spheres Agamben's concept of camp. Examples of the ring-fencing principle can be found all over the offshore world. Important thing to remember is, however, that ring-fencing is not equal with the state of exception. The state of exception covers the ring-fencing, but can take more subtle, administrative forms as well.

This leads us to two other points mentioned in the OECD's definition: lack of transparency and problems in exchange of information. As countries' ability and right to tax or regulate economical or financial activities depend much on whether they are taxed or regulated by other countries, masking the real identity of a person or corporation is a key step in reaping benefits from offshore business operations. If the onshore government is not aware of the real nature or identity of particular transactions or businesses, it is often easy to avoid taxes or other responsibilities. Usually secrecy is connected with high banking secrecy laws, but they are actually only one component in the veil of secrecy. For

[59] *Tillman 2001, 20*

example tax havens' international business corporations include bearer shares, or registered shares but no public register for identifying the shareholders.[60]

The letter of law and its application are two different things. Therefore it is not only the level of banking secrecy but also the way it is imposed and monitored that counts. Furthermore, banking secrecy is involved only in transactions and deposits where bank accounts are used. Masking the identity of corporation's shareholders or board can be equally important in an attempt to obtain redemption from taxes or regulation. Individuals use trusts and charities besides of well-known numbered bank accounts, and corporations rely on International business companies, captive insurance companies or other vehicles. To sum it up, flaws in exchange of information between tax havens and foreign authorities enables the ongoing tax evasion and avoidance, while lack of transparency within the tax haven helps to establish and maintain the state of exception–either as an overt ring-fencing legislation or through more subtle forms of the state of exception, possibly involving government corruption.

The importance of low taxation for tax havens might seem self-evident. As Schumpeter notices, taxation is the formative component of states. Taxation is also a fundamental relationship linking individuals and corporations to societies, and consequentially eroding that connection has most fundamental results to both states and state-citizen relationship. Offshore jurisdictions have always offered low taxation or exemption from taxes–this history stretches from the turn of the 20th century–but the critical thing is the phenomenal growth of the phenomenon. Today, growing number of tax havens offer even zero taxation for corporate income, which has major implications for tax burdens not only in onshore nations but also in tax havens. They offer vehicles such as captive insurance companies[61], trusts, foundations, and limited liability partnerships. All can be used for purposes of tax avoidance/evasion. International business corporations are also popular, with tax exemptions "from all taxes on profits, capital gains, and other income as well as stamp, gift and other taxes."[62] The first IBCs were set up in 1926 when Liechtenstein began its post-war development into a modern tax haven.[63]

We should not, however, fix our attention solely to tax breaks. Low level of regulation is also an important aspect luring corporations to incorporate in tax havens. There are numerous ways to help corporations in reducing their regulative responsibilities, much more than with taxation. Regulation is an inherent part of all business activities, while taxes are directed only to some economic transactions or assets. Therefore the impact of either reduced regulation or more favourable regulation is

[60] *IMF 2000, 3*
[61] *Hampton 1996, 31*
[62] *OECD 2001b, 24*
[63] *Hurst 2003*

significant not only to tax revenues and income distribution, but also in redefining the boundaries that dictate what market agents can and can not, or should not do. The application of these rules affects the market risks and system risks,[64] as well as other states' abilities to regulate these corporations. The regulative vehicles tax havens offer include for example international business corporations and captive insurance companies.

Tax haven jurisdictions have created a myriad of states of exceptions not available for their local citizens or companies. This has been done by ring-fencing parts of their legislation and tailoring it to suit the needs of investors and corporations. The diversity of these exceptions has increased with specialisation amongst tax havens, and the scale of the phenomenon has grown together with increase in the money flows passing through tax havens and increase in the number of tax haven jurisdictions. These ring-fenced parts of the legislation have then been commercialised. There would be no incentive whatsoever for great majority of vehicles of tax and regulatory avoidance apart from needs of the foreign investors. What the focus on tax haven structures does not tell to us, however, is whether the sovereignty to draft and maintain ring-fenced parts of the legislation is in hands of the tax haven governments, or whether it has been transferred partially or completely to market agents. This will require further analysis on the political agency.

3.4. Flags of Convenience

Flags of convenience registers have existed for approximately as long as tax havens. In 1920s, US shipowners flagged ships to Panama in order to avoid liquor laws. In the following decade, major companies such as United Fruit and Standard Oil reflagged their ships as well. The first notable period of growth in registrations was in 1950s.[65] However, the biggest expansion in the number the FOC registers happened during the 1980s and the trend only accelerated during the next decade. In 1980 there were only 11 FOC registers, which means that their number today is roughly three times larger. "The result", notes William Langewiesche, "was a sudden expansion in flags of convenience, and a corresponding loss of control".[66] The general deregulative wave that began to gain power in 1980s was thus expanded into shipping industry. The ship owners "found that they could choose the laws that were applied to them,

[64] *Market risk meaning the risk firm faces when operating in markets. The knowledge on the severity of this risk can often be spread unequally among the different stakeholders, such as management, board or the shareholders. The collapses of Enron and Parmalat were perfect examples of how astoundingly high risks remained hidden for years before the violent collapse. Systemic risk means risk towards the market as whole.*

[65] *Picciotto 1999, 54*

[66] *Langewiesche 2004, 5-6*

rather than haplessly submitting to the jurisdictions of their native countries." Economical gains were so high that even "the most conservative and well-established shipowners" had no choice but to follow the trend.[67] Simultaneously overtonnaging drove shipping companies to cut costs with whatever means available. Increasing the use of FOCs offered an easy way for meeting this goal.[68]

Just as tax havens, flags of convenience jurisdictions exploit the divided nature of corporate citizenship by offering shipping industry companies a possibility to book their profits and adhere on regulation of a flag of convenience jurisdiction, while the actual profits may come from any part of the globe. Ship registries are maintained in such distant land-locked places as Mongolia and Switzerland. Mongolia operates an FOC with help from a company called Sovereign Ventures, based in Singapore. The same people involved in Sovereign ventures operate the FOC register of North Korea and Cambodia.[69] FOCs blur the distinctions between offshore and onshore, as registers can locate in land-locked places, be operated by servers in other 'onshore' state (Liberia's register has been outsourced to U.S. based firm), which in turn may have their legal residence elsewhere.

According to the definition of International Transport Federation, in flags of convenience vessels "the nationality of the owner is different from the country of registration."[70] In past decades the working definition used to be more detailed, but just as with tax havens, defining a flags of convenience jurisdiction has become increasingly difficult. At the moment, seven out of the ten largest merchant fleets in the world are FOCs, with Panama as obvious number one and war-thorn Liberia as second. Major onshore countries like France and Germany have also been issuing "international ship registries". Just as tax havens' services and banking secrecy laws can be found from countries that are not usually associated with them (like banking secrecy laws of Austria, surmounting even its better known tax haven neighbour Switzerland), the maritime regulation and standards are also been pushed down by regulatory competition.

The total tonnage of Panama alone exceeds the combined non-FOC tonnages of Singapore, China, United States, Japan, India, United Kingdom, Italy, South Korea, Denmark and Iran, which are all included in top-20 countries. Panama is in its own class also when compared to other OFCs, surmounting Liberia's tonnage levels more than threefold.[71] The countries that offer FOC facilities can also operate as tax havens. Because FOC jurisdictions' services are targeted for niche markets of

[67] *ibid.*
[68] *Bloor et al 2000*
[69] *New York Times 2004*
[70] *ITF 1998, 14*
[71] *Lloyd's 2004 in U.S. Maritime Association 2005*

maritime businesses (and increasingly for aviation industry) the potential markets for FOCs is consequently more limited. This is reflected by the smaller amount of FOCs, 32, when compared to the number of tax havens. The list includes following jurisdictions:

Table 2 *Flags of Convenience Jurisdictions*

Antigua and Barbuda	Equatorial Guinea	Mauritius
Bahamas	French International Ship Register (FIS)	Mongolia
Barbados	German International Ship Register (GIS)	Netherlands Antilles
Belize	Georgia	North Korea
Bermuda (UK)	Gibraltar (UK)	Panama
Bolivia	Honduras	Sao Tome and Príncipe
Burma	Jamaica	St. Vincent
Cambodia	Lebanon	Sri Lanka
Cayman Islands	Liberia	Tonga
Comoros	Malta	Vanuatu
Cyprus	Marshall Islands (USA)	

Source: ITF 2002

The reasons for outflagging ships to FOC registers are related to taxation, secrecy, environmental standards and work legislation–or in short, regulation. The first point, taxation, is an obvious one and bears close resemblance with tax havens. Just as banking secrecy laws hide the true owners of equities or savings, the secrecy laws of FOC jurisdictions–for example the possibility to use international business corporations and bearer shares–hide the beneficiaries of maritime corporations.[72] The low environmental standards often results in poor condition of vessels. The condition of ships has been shown to be worse in recently founded FOCs and better in more established ones, illustrating the race to the bottom that bears resemblance to tax havens' development.[73] Low labour standards imposed in most FOCs have led into heavy reliance on workers coming from developing countries.

Albeit FOCs and tax havens have much in common, the magnitude of the state of exception and possibilities for its exploitation have been visible for a longer time in FOCs. Maritime trade has been a globalised

[72] *OECD 2003, 8-10*
[73] *Alderton and Winchester 2002*

industry much longer than global finance. The absurdity of a tax haven isle of Sark (population 545) boasting more than 15,000 nominee directed companies matches the absurdity of war-torn Liberia being a world shipping superpower, but in FOCs the paradoxes of divided corporate citizenship are easier to grasp. Shipping goods from one place to another is, after all, extremely tangible business when compared to sale of bonds, currencies or derivates. It may not a source of much astonishment today if derivates are being traded en masse in a Caribbean diving paradise. But it is more difficult not to get astounded by hearing that shipping fleets are operated from land-locked Mongolia of Switzerland.

Flags of convenience registers are interesting because results of the state of exception are experienced directly and sovereignty's shift from governments to private corporations is evident. At one point the Ahmad Yahya of the Cambodian Ministry of Public Works and Transport said that "we don't know or care who owns the ship or whether they're doing 'white' or 'black' business --- it is not our concern."[74] In 1999 the former prime minister of Belize, Manuel Esquivel, made a remark that did not share the Ahmad Yahya's approach to maritime regulation. Esquivel responded to the complaints on illegal fishing by Belize registered vessels by saying that "[t]here was little we could do. These people aren't responsible to anyone. The ships are never seen in Belize. The Belize shipping industry has been privatised. There should be proper accountability."[75] What is notable in both statements is that the state of exception created by Cambodian and Belize governments effectively removed the power to regulate and monitor shipping industry from the government, at least for the given time period. This relationship will be analysed in greater detail in part four.

Many of the conclusions said about tax havens hold true with FOCs as well. The whole idea behind offshore shipping registries is a state of exception created by ring-fenced legislation. But amongst world's industries, the shipping businesses operate at the extreme end of regulative void. The enormous popularity of FOC registers suggests that offshoring is actually standard norm in shipping even much more than in global finance. In other words, what started as a single exception to get around liquor prohibition laws has become the norm in the ways how commercial vessels are being operated. These exceptions are issued by the governments setting up FOC registers, but the effective control of them is a complex issue. More discussion on this problematic will follow in part four. The competition state phenomenon is also strongly present both in the internal competition between FOC jurisdictions and between onshore ship registers and FOCs.

3.5. Export Processing Zones

[74] *Fairplay 2000 in ICFTU 2003, 6*
[75] *ICFTU 2003,13*

The International Labour Office defines export processing zones as "industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being (re)exported again".[76] Proctor and Markman define EPZ as "a delineated, enclosed and policed area of a country which has an industrial estate specialising in the production of manufactured goods for export".[77] The word 'zone' implies an area within a nation, separated by legislative means, offering special incentives that can be anything from tax concessions to lower labour standards. The definition stresses the single most important characteristic of EPZs–their importance as assembly sites of world's industrial products–but it has become in parts considerably outdated.

Today export processing zones, free trade zones, *maquiladoras*, special economic zones, boarded warehouses, free ports (the phenomenon goes under many names and variations in different countries) include several areas in addition to simple manufacturing or assembling of products. High tech zones, finance zones, coordination zones and even tourist resorts are operated under principles of EPZs.[78] Further examples include zones for medical diagnosis, architectural or engineering services.[79] Their physical form can be anything from traditional enclave-type zones, that is territorially located areas within states, to "single-industry zones (such as the jewellery zone in Thailand or the leather zone in Turkey); single-commodity zones (like coffee in Zimbabwe); and single-factory (such as the export-oriented units in India) or single-company zones (such as in the Dominican Republic). Amongst the most extreme examples are Mauritius and Namibia, where any single factory can be established as a new EPZ.[80]

The diversification in both physical forms and services tells something about expansive growth of EPZs. Since the modest beginnings of contemporary export processing zones in 1950's (free ports and other similar areas have existed already in medieval Europe, but their operating logic has been different), the number of EPZs have grown in a tremendous pace. Today there are more than 3,000 free trade zones in the world. Even though EPZs exist in different parts of Europe and other developed countries, most are founded in developing countries. In developing countries their economic significance is highest as well. The electronics, garments and other products assembled in free trade zones can be found from any supermarket, and it takes effort to find a major industry that would not exploit EPZs.

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[76] *TMEPZ 1998 in ILO 2003a*

[77] *Proctor, Markman 1995 in Labour Resource and Research Institute 2000, 12*

[78] *ILO 2003a, 2*

[79] *United Nations 2004, 35*

[80] *ILO 2003a, 2, Jauch 2002*

There has been phenomenal period of increase in number of EPZs especially from year 1997 to 2002, as the following figure illustrates:[81]

Table 3 *The Growth of world's EPZs*

	1975	1986	1995	1997	2002
No. of countries with EPZs	25	47	73	93	116
No. of EPZs	79	176	500	845	3000
Employment (millions)	n.a.	n.a.	n.a.	22.5	43
- of which China	n.a.	n.a.	n.a.	18	30[82]
- other countries for which data were available				4.5	13
Total countries for which date were available (108)					

Source: ILO calculations based on a variety of sources including zone administrations, national statistics, web sites, published articles, estimates and responses to ILO surveys, updated to Dec. 2002.

The growth of China's EPZ market during recent years has been remarkable. There were 456,892 firms operating from Chinese special economic zones in 2003, plus additional 4,747 located in Hong Kong. Much of the increase in number of different kinds of EPZs comes from China with its 2000 zones in 2003.[83] The Chinese zones have grown in a pace that has brought troubles to some competitors in other developing countries. For example in Mexico the number of people employed in local export producing zones dropped from 1,285,000 in 2000 to 1,086,000 in May 2002, "partly owing to growing pressure of competition from the Chinese EPZs"[84]. China offers reduced tax rates for investors, but most likely the biggest reasons for incorporating in Chinese EPZs are the importance of its' market area together with cheap and submissive labour. Tremendous growth of EPZ industry has led to a competitive situation where successful entrance to the market is really difficult.[85]

The logic of tax exemptions in EPZs differs from tax havens' policies, albeit some tax havens offer EPZ services as well. In EPZs, countries often provide 'tax holidays'–reduced or zero tax levels–that can last for couple of years. The original idea has been that this period will lead to established investments and technological spill-overs. However, the over-supply of EPZs has led to a situation where it is easy to arrange manufacturing or other business in a way that most of the income can be cashed in with remarkably low tax rates. Transferring production to

[81] *ibid.*

[82] *Estimates vary from 20,000,000 to 40,000,000; ILO uses 30,000,000 for purposes of calculation, see ILO 2003b, 8 and 15*

[83] *ICFTU 2003, 8*

[84] *ibid., 10*

[85] *Labour Resource and Research Institute 2000, 13*

another location is not difficult as most of the work conducted in EPZs is relatively simple manufacturing and assembling. Technological parks and other specialised and more sophisticated zones are, of course, another issue.

Taxes are only one factor in manufacturing. Submissive labour, low wages and lax work legislation are important means in keeping the expenses low. In this field some EPZs could be characterised at least as innovative, often in a way that has grave social consequences. Labour laws are being dismissed systematically, and obtaining information from outside is often impossible because employees' contacts to outsiders are under tight scrutiny.[86] Countries hope that by establishing export processing zones they will be able to attract investments, create employment, increase exports and generate foreign exchange. Products originating from EPZs make as much as 80 percent of foreign exports for example in China, Czech Republic, Hungary, Kenya and Philippines. EPZs have helped some countries, like Mauritius and today China, to move from basic assembly production towards more sophisticated and knowledge-intensive industries, thus helping development and economic growth.[87]

There are not many developing countries with enough economical and political significance to follow the Chinese or Mauritanian way. India can probably make it with its recently introduced export processing zone program. Transition countries like Checz and Hungary are also attracting big investments from e.g. car industry, which have had significant impacts on employment and FDI. Their national asset is skilled workforce, geographical location and working infrastructure. The darker side of intensifying competition amongst EPZ countries is visible in politically and economically less significant developing countries, most notably in sub-Saharan Africa. Competitive pressures make it difficult to raise tax levels or labour standards because for corporations, relocating production to other countries (with other EPZs) is easy. United Nations has addressed this threat as "a race in the use of incentives"[88].

In essence export processing zones bring the offshore right at the doorsteps of the nations that suffer most from the existence of tax havens–namely developing countries. But EPZs undermine also OECD countries' efforts in tackling harmful tax competition, as double-standards erode consistency of attempts for global governance. In EPZs the ring-fenced parts of the legislation cover not only economical and financial issues, but environmental and work legislation as well. With EPZs this extension is more remarkable than in FOCs because of the enormous scale and importance of the EPZ industry. At the matter of fact, EPZs are the major link between Agamben's biopolitical states of exceptions and

[86] *ICFTU 2003, 11*
[87] *ILO 2003a, 2*
[88] *United Nations 2004, 35*

offshore. Just as detention centres or other instances of Agamben's camps, the EPZs are territorially located areas that create separate set of rules on how people's private lives are being arranged. In the poorest assembly halls the special legislation is not limited solely to some safety condition, but to tiniest aspects of workers' lives as well. Over 40 million people around the world, mostly young women, go work every day to areas where normal labour and environmental legislation is not necessarily applied, i.e. they are excluded from the scope of application of their labour laws or obedience to laws is not enforced. Just as with FOCs, state is the ultimate issuer of an EPZ, but its control is far more complicated issue.

3.6. Offshore Financial Centres and International Banking Facilities

Albeit offshore financial centre is usually used as a general category (often including also tax havens), in my opinion there are actually two kinds of offshore financial centres: 'spontaneous' OFCs of London and Hong Kong, and deliberately created international banking facilities in Tokyo, New York, Frankfurt and many other cities. Common denominator is that both 'spontaneous' OFCs and intentionally created IBFs are located within onshore states; are often (but not always) significant financial centres even if the offshore facility is taken out of consideration; and most importantly trading in them is reserved for non-citizens of the countries where they are located. Consequently OFCs and IBFs share similarities with both tax havens and EPZs. The financial industry connects OFC and IBFs with tax havens. The geographically framed boundaries within onshore states has conceptual similarities with EPZs.

The early history of OFCs is not a straightforward story. The formation of the first OFC, London's Euromarket, began around 1955-1963, albeit some authors claim that the period was shorter and started in 1957.[89] Euromarket arose from several strands, including both structural factors and conscious decisions by both market and governmental agents. For example, one reason for Euromarket's (or euro-dollar market, as it is sometimes called) emerge was result of British court decisions, other was related to political factors in United States, [90] while the third reason bounded from sterling crisis of 1957[91]. Schenck has also stressed role of the market agents–especially the Midland bank–as a motor behind the increasing dollar trade in London. [92] Kane has traced the earliest factors behind emerge of the Euromarket all the way back to the Soviet Union's camouflage banks operating in Europe.[93] Palan underlines the role of Suez crisis in 1957.[94] I will not go through these explanations in detail: it

[89] *Schenk 1998, 1 (for latter point see Kane 1983)*
[90] *Kane 1983, 5-7*
[91] *Palan 2003, 27-28*
[92] *Schenck 1998, 5-7*
[93] *Kane 1983, 1*
[94] *Palan 2000, 27-28*

suffices to say that as a result of these overlapping phenomena, the dollar trade in the City of London increased markedly and the British courts had to decide how to deal with it. As a surprise even for the government of UK, the courts concluded that in a juridical sense transactions in Euromarket were not subject to UK's laws and regulations in case that both lenders and borrowers were non-British. If they were not under British law while the trade took place in British soil, the consequence was that they were under no regulation and under no law whatsoever!

Implications of the emerge of a currency market free from restrictions on currency exchange, interest rates, maturity periods and forms of investments was quickly understood by banks and investors. The financial markets of late 1950's and were rigidly regulated, which made emerge of the Euromarket to seem almost like revolutionary. The unregulated markets for currency trade had been created, and they seemed to have come to stay. The Eurocurrencies were followed, within a couple of years' time-span, by Eurobonds (1962) and Euroequities.[95] This combination was to create pressures to national attempts to regulate financial markets until during the deregulative that we have currently witnessed all over the world.

But before things emerged this far, many political contestations took place. During the years, several governments in United States wanted to curb or shut down the Euromarkets, as they distracted their Keynesian economic policies. Intensive lobbying in several periods bore little fruit, and in 1980s things started to change. As Reagan government came into office the shift in political mood affected attitudes towards Euromarkets. After several decades of fight against the windmills, U.S. decided to start compete against Euromarket instead of insisting its better regulation or dismantling.

This development resulted in establishment of New York's international banking facility system in late 1981, targeted for international wholesale banking market. Its intention was to be a direct response to Euromarket with hope of repatriating many of the dollars deposited offshore. The most important features included no reserve requirements or interest rate ceilings for banks.[96] Financial Times described it as a 'carrot' to entice business back onshore.[97] Initially it did succeeded to lure much capital to New York but in the longer run the development was less successful. Albeit New York IBFs were 'freed' from much regulation, it nonetheless could not match the London's OFC. Further cause for doubts was created by political risks investors associated with IBFs. As it was created by separate law, it was possible that following governments might have abrogated it. A Representative of Bahamian Central Bank stated

[95] *Schenck 1998, 10*
[96] *Hudson 1998, 10*
[97] *Financial times 1983, quoted in Hudson 1998, 10*

that "[s]ome of them would open an IBF but they kept their same operation offshore because if one government brought in the legislation, another government could take it out, and that has been the history of banking legislation".[98] Other people were concerned about privacy protection, as they feared that information gathered by US authorities might have been used elsewhere as well. Some of these concerns were captured in a remark made by Bahamian lawyer:

> "If people are looking at moving away from their regulatory authorities they don't go in the same country to set up entities. If you're within their borders you're still subject to their control, their disclosure, and to their ability to penetrate the system. You're literally right in their yard. So those who are still looking to have funds which are coming from international sources, not be subject to possible disclosure or knowledge of their [US] authorities, will not use the IBFs. They will use the OFCs or other countries outside of the US" *(Young, Personal Interview, Bahamas, 1994).*[99]

Now that the political window for IBFs was opened, the number of newcomers increased rapidly. By September 1982, 395 IBFs were introduced, of which 176 were in New York.[100] Others were located in smaller financial centres which also started to offer similar services. And soon after the establisment of the New York's IBF system, Japanese started to delve into possibilities to create a similar system in Tokyo. After couple of years, in 1986, they opened Japanese Offshore Market (JOM), which operated on a similar basis with American IBFs. It managed to attract 400 billion USD during its first two years, which can be considered as a success.[101] After this, similar facilities have been created in i.e. Singapore, Malaysia's Labuan and Frankfurt. At the moment London enjoys still its number one position but Japan's JOM has been overcome by Singapore. year 1999 85 per cent of international banking and bond issuance took place in offshore financial centres.[102]

Tax havens have had an important role as facilitators of OFCs. They have helped investors to mask their transactions as 'foreign' and therefore benefit from the lax regulation of OFCs. Major currencies and bonds are traded also in tax havens, which means that there is certain overlapping in their services. These similarities have resulted in conceptual confusion over whether different financial centres should be called OFCs, tax havens, international banking centres or something else. In my opinion the ultimate test that distinguishes an OFC from a tax haven is a simple yet crucially important one: tax havens facilities are booking devices created by tax haven government, applying within the

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[98] *Johnson, Personal Interview, Bahamas, 1994, in Hudson 1998, 20*
[99] *Hudson 1998, 19*
[100] *Johns and Le Marchant 1993 in Hudson 1998, 15*
[101] *Johns and Le Marchant 1993 in Hudson 1998, 10*
[102] *Lewis 1999, 81*

whole jurisdiction; while OFCs are territorially framed areas within a nation that host similar services. *Tax havens create a state of exception for finance industry to exploit, whereas OFCs are states of exception created by their host states.* Creation of the Euromarket had significant consequences for states' capabilities to exert their sovereignty, as the chances for imposing controls on trade in bonds, equity and capital diminished. The regulatory vacuum that was first built in London in 1950s set the state sovereignty over financial markets into decline.

Both OFCs and IBFs are states of exceptions created within onshore states. It is often said that this made U.S., UK and Japan tax havens. I think it is more accurate to say that these states brought offshore within their territories by following the logic of export processing zones. This was done by creating ring-fenced legislation for their financial hubs. With Euromarket's origins being partially in mist and the early histories of prominent IBF's still waiting to be written, it is impossible to say how big role financial firms played in their formation. It was certain that IBFs were created at least partly because of the competition state pressures, but whether the initiative came from the government or from the business circles is not certain. Therefore I have to exclude the OFCs and IBFs also from the case study section in part four.

3.7. Conclusions

As the previous pages showed, the world's 70 tax havens, two offshore financial centres, various international banking facilities, 32 flags of convenience registers and about 3,000 export processing zones have created a complex network of states of exception within the world economy. This offshore world is an essential factor in hastening the competition state processes. But it is also important in the sense that as a result of these exceptions, the state has retreated from regulation and taxation of economic activities in a length that at least US$11,5 trillions of assets owned by the world's super-rich are now held offshore. In addition to this, much of the transborder corporations activities operate under principles low tax, low regulation and high secrecy. One should also remember the offshore's role as the world's money laundering platform.

If we look offshore jurisdictions through the lens of their formal governance structures, many reasons that explain how this anomaly was born and is maintained will be explained only partially or remain permanently clouded in mist. We would perhaps end up concluding that through parliamentary processes offshore jurisdictions use their sovereign right to draft. We could continue by stating that in the age of contemporary globalisation this fundamental characteristic of sovereign state causes clashes with other sovereigns that need to be reconciled.

If, on the other hand, we examine offshore with focus on how they commercialised their sovereignty with states of exception, the results will differ greatly. As we have already seen, the states of exception can be

drafted as administrative orders, and the secrecy and technicality surrounding them can work as a silencer for public discussion. The ring-fenced legislation has usually only small effects within the particular jurisdiction, and therefore the scale of the states of exceptions can be seen only from far–or, from onshore. Giorgio Agamben has stated in his book *State of Exception* that "as a figure of necessity, the state of exception therefore appears (alongside revolution and the de facto establishment of a constitutional system) as an 'illegal' but perfectly 'juridical and constitutional' measure that is realized in the production of new norm (or of new juridical order)."[103] The offshore's states of exception might, at least in some cases, indeed be called as new juridical orders within the particular jurisdiction.

In light of how offshore jurisdictions have sliced their sovereignty into bits that are tailored for the needs of different foreign customer groups, it seems implausible to argue that right for self-determination would justify the tax havens' and flags of convenience jurisdictions' activities. Introduction to the history of sovereignty showed that albeit sovereignty is often perceived as absolute rule within some territory, in practice this can never be the case. Tax havens' activities as facilitators of state sovereignty's erosion put them into position where argumentation centred on defence of national sovereignty seems more than odd. But the host governments of EPZs, OFCs and IBFs–especially those of powerful OECD countries–are in even more difficult position. Defending national sovereignty in front of one audience and disdaining it in front of another might be successful in terms of real-politik, but in longer run it will almost certainly affect negatively the credibility of states in front of their electorate. This hastens the commodification of sovereignty, which some libertarians might actually see as a positive development. Its most fundamental flaw is just that it has nothing to do with democracy.

Democratic power is fundamentally constrained power. In parliamentary states the sovereignty that enables state to do *anything* within its borders (in the limits arising from its international status and power) has been scattered across wide range of institutions and state organs. Ideally democratic use of power is characterised by transparency, openness, and accountability. Undemocratic power, on the other hand, operates behind secrecy and without constraints. Therefore in autocracies sovereignty is used by one person, whereas in democracies it is used by the state, a non-personal and complex entity. What happens within 'camps', or states of exceptions, is that in certain area the values of transparency, openness and accountability lose their meaning, and in the most extreme cases anything becomes possible. The most notorious tax havens, such as Belize or Nauru in the 1990s, are not far from this position.

[103] *Agamben 2005, 28*

In case of 'illegal aliens', removal of citizenship is a sign that they have, at least in certain extent, been removed from the normal legal order and are facing state's coercive power directly. Needless to say, removal of basic rights is a bad thing to them. In offshore, however, the removal from normal legal order is not done in order to take away rights, but in order to grant new rights to corporations and individuals that *choose* to reside, in a legal sense, within a particular tax haven or other offshore jurisdiction. The contrast with 'illegal aliens' is most dramatic in the market for citizenship: the passport and citizenship of various tax havens has been marked with a price tag so that super-rich individuals can reside, in legal sense if not as actual residents, in a jurisdiction that offers suitable legislation. If we are to correct these kinds of undemocratic abnormalities, the answers can neither rely on defending state sovereignty nor commercialising it further. Instead, it seems that we need genuinely global solutions. But before saying anything certain about that we should take a look on transborder corporations' role in offshore's states of exception.

4. Political Agency and Offshore

4.1. Introduction

There are four important groups that should be taken into account as we look the offshore world through the lens of sovereignty. They include offshore jurisdictions' governments (tax havens and FOCs); onshore governments (OFC, IBF and EPZ host governments, but also other onshore states); international organisations (e.g. OECD); and finally transborder corporations. It is self-evident that states are participants in politics. This group includes also offshore jurisdictions' governments, in a length that they are independent from their existing or former host jurisdictions. Many of them are, after all, former colonies. It has also been noticed that international organisations have increasing power in shaping the agenda of world politics.[104] However, I have not seen a case where any state would have *commercialised* its sovereignty and handed it down to an international organisation. The traditional international relations simply do not work this way. The UN's and NATO's operations in some war-torn areas could be possibly be analysed as extension of sovereignty, but it has nothing to do with the offshore world. Therefore my main concern here will be in clarifying the relationship between transborder corporations and sovereignty, in order to conclude whether we can learn something new about sovereignty by focusing on offshore.

Nevertheless, all aforementioned categories include elements that frame the offshore jurisdictions' possibilities for independent decisions. They add up to the pressures that the competition state phenomenon– internal competition between offshore jurisdictions and competitive pressures from outside as onshore states engage in tax competition– causes to offshore jurisdictions. Therefore their influence on the offshore

[104] *See for example Cable 1999; Keck and Sikkink 1999*

world should be introduced, even if only superficially. Otherwise we fail to see the offshore in its context and end up with a view on vacuum instead. That can not result in anything else but bad research.

Onshore governments have a twofold role in affecting the framework where offshore jurisdictions operate. On one hand, some onshore governments want to tame the harmful tax competition and the offshore structures that accelerate and maintain it. On the other hand, many 'onshore' governments actually either promote harmful tax competition (Ireland is one example) or participate in it by maintaining some offshore centre, such as international banking facility or an export processing zone. The governance of parliamentary states is by its nature packed up with conflicting or even contradictory forces, and therefore one state can simultaneously be both promoter and opponent of the offshore world. One important example of this is the U.S., where Internal Revenue Service (IRS) and some people in the Senate are doing much work against tax havens, while some other state's organs are strong proponents for it. United Kingdom is another example. It could have a great impact on many of the tax havens that are former Crown Dependencies. In practice, the London's Euromarket has made the UK to oppose reforms tackling harmful tax competition within the EU.

International organisations can, at best, have a great impact on offshore jurisdictions. The most important example is OECD and especially its blacklist of non-cooperative tax havens. The existence of this list (that has been updated and shrank as some listed tax havens have shown compliance) has led to improvements in cooperation against financial crimes and money laundering. OECD has also been doing work against misuse of corporations' transfer pricing schemes. The work that trade unions have been doing against malpractices of EPZs and FOCs should also be mentioned. Putting pressure on tax havens by either international organisations or larger states can, in other words, lead to reconsideration of the gains and losses arising from some pieces of legislation.

All these forces shape the limits where tax havens and other offshore jurisdictions can operate as they draft the ring-fenced legislation or other states of exceptions. In other words they shape what is feasible, but not necessarily what is possible. Very few outside forces can actually restrict offshore jurisdictions to create states of exceptions for business, as this would be a grave insult against their sovereignty. Therefore much more interesting thing is to look at what happens to sovereignty after it has been voluntarily commercialised. In order to accomplish this task, we need to set our focus on the transborder corporations as possible participants in creation and control of the states of exceptions that offshore jurisdictions initiate.

4.2. Transborder Corporations

Corporations are "everywhere and nowhere in our society."[105] First and foremost, they are everywhere because significant amount of economic activities is conducted in corporate form. This is the case especially in developed countries where majority of economic activities operate within the formal, developed economy based on contractual relationships. Many of the organisations and institutions that used to be operated by states–universities, churches, hospitals, and non-profit organisations among others–are now being organised as corporations in various countries. But it is indeed possible to say that "corporations are nowhere" as well. The contractian theory on corporations points out that "corporations do not really exist: they are merely a convenient connection point for a bundle of relationships between shareholders, bondholders, employees, and customers, to name the most important stakeholder groups." According to this view, any useful analysis on the corporation needs to begin by looking at it through viewpoint of the various groups that interact through it.[106] Furthermore, the law does not generally recognise an entity called transborder, multinational, or transnational corporation. In front of law they exist only through their subsidiaries.[107]

Corporations can be examined as bearers of political power separately from particular corporation's decision making procedures, composition of the stakeholders, and the ownership structure (all these issues can create political conflicts, but in a different sense.) The modern corporation, as an entity and via its representatives, has power to sign binding contracts. This makes corporations much more than mere connection points for different groups. In this part I am going to demonstrate how transborder corporations' ability to partake in the control of the state of exception within offshore and, at certain extent, possibility to even issue new kinds of states of exception within the original exception 'rented' to them by states (the commercialisation of sovereignty) makes the analysis of corporations *as entities* and *as participants in politics* (in a sense illustrated in part 2) not only plausible but also necessary in order to understand how politics and sovereignty are maintained and conducted within the contemporary world economy.

My focus will be broadly on transborder corporations. Transborder corporation is one of the four labels used for defining corporations that have businesses, in one form or another, in more jurisdictions than one. The two other widely used terms are multinational corporation and transnational corporation. Even term global corporation is occasionally used, but I see that as a sign of lazy use of terminology. At times, the label enterprise is used instead of corporation, especially when the legal form and status of the corporation is not a major concern. The language of social science and economics can never be value-neutral, and should

[105] *Avi-Yonah 2004, 1*
[106] *Avi-Yonah 2004, 3-4*
[107] *Robé 1997*

therefore be chosen carefully and with self-reflection.[108] Different ways to address corporations not only deliver rather different images (with *multi-* meaning more or less same than plural and trans- meaning a thing that goes beyond something) but should also be differed from each other conceptually. When it comes to state system, it is definitely different thing to speak about corporate activity that is located simultaneously in various countries (multinational) on the one hand, and to locate the same activities in the supposed space between states (transnational) on the other. Finally, to use term global corporation implies that there is a uniform global platform where the corporation operates, or that the corporation can be conceptualised as an entity on a global scale. At the moment we have neither a uniform global platform for corporate activities nor juridically global corporations. And, at least if the offshore is not taken into account, the corporations operate in multinational, not transnational space.

Transborder corporations' role in globalisation have been noticed and analysed primarily from economical standpoint. Comparisons between states' GDPs and corporations' profits appear frequently in literature on globalisation.[109] Furthermore, the growth of foreign direct investments (FDI), foreign subsidiaries and intra-firm trade are seen as indicators of economical globalisation that increases the general power of economics and more specifically corporations, vis-à-vis states.[110] The background assumption in these kinds of analyses seems to be that economical muscle brings also political affluence, but without further considerations on *how* exactly the economical power is transformed into political power the explanatory value of comparisons remains limited. This task is not possible without defining first what one means with politics and the political (part two). The enormous magnitude and importance of offshore finance and tax avoidance means also that analysis of the larger trends in economical and financial globalisation will be biased if the offshore is not taken into account.

There has not been much academic discussion on corporations as potentially political or sovereign agents. Susan Strange's theory of the competition state, discussed in part two, puts a strong emphasis on corporations' role in international politics, but, as noted before, it lacks the viewpoint of sovereignty. Jean-Philippe Robé is another scholar whose work should be mentioned. He examines corporations from a standpoint of transnational law. Robé claims that "[w]hat is new, in its relative importance, is that the control of fragmented production processes, spread all over the world, is now exercised by *organizations* which have themselves spread beyond state frontiers."[111] The organisational change

[108] *McCloskey 1986*
[109] *Held et al. 1999, 236*
[110] *ibid.*
[111] *Robé 1997, 46*

affects not only legal theory but also political science[112] and economics, where the national level seems to be principal, almost 'natural' framework for thinking about the economy. The result of this 'national' fixation has been that the international analysis of economics has mostly been part and parcel about *inter-national* economic relations.[113] Robé sees that state's monopoly on law creation is being challenged first by "extraterritorial effect of norms adopted by certain states" and, second, "the self-regulation of civil society."[114]

Robé rejects the monistic conception of the state as a sole bearer of sovereignty by referring to the legal pluralism of which corporations are one example. To Robé, the state consists not only of the ultimate state law, but also of diverse set of contracts, conventions and practices. He notes that *if* we think state's sovereignty in rigid terms of having the final decision over events, conventions, contracts and practices within particular territory, the trans-state level would indeed have no legal existence. This ultimate primacy of state law should be rejected, Robé argues, because in such framework there would be "no law in societies without a state," such as in medieval societies.[115] And indeed, if law is conceptualised as any organised means of maintaining order and regulating social/economic/political life, then Robé's approach is valid.

What is missing also from Robé's analysis is, however, distinction between *power* to do something and *sovereignty* to do something. Sovereignty is, as the history of the concept illustrated, a particular system of governance and tied closely to the modern state. The medieval societies were organised, but not according to the principle of modern sovereignty. It is possible to claim that there is a legal pluralism so that "each enterprise constitutes a legal order,"[116] but this pluralism still exists within the framework of sovereign states. Here, the theory of the state of exception shows its full potentiality. Yes, the states may have partially become devoid of actual power to affect their subjects because of the competition state phenomenon and other impacts of economical and financial globalisation, but nevertheless the sovereign state system is the ultimate structure upon which the *lex mercatoria* (the regulative system developed for corporations and by corporations themselves from the eighteenth century onwards)[117] and the competition state phenomena rest. Even today there are states like North Korea that have simply rejected to participate in the open world economy, and there seems to be little that other agents, whether states or non-state actors, can do about it. Thus, the pluralistic conception of the state works fine if we are interested in finding out and describing the power relations within the

[112] *Robé refers to Strange (1996) here*
[113] *ibid. 47*
[114] *ibid. 49*
[115] *Robé 1997, 54*
[116] *ibid. 56*
[117] *Robé 1997, 49-50*

state. It falls short, however, as soon as we enter the field of relations based on politics and sovereignty.

My interest here is not in possible transnationalisation of corporate culture, and neither it is in focusing on meters of foreign direct investments, number of subsidiaries, or other purely quantitative indicators in defining corporation's 'multinationaliness' or 'transnationaliness.' Rather, I am posing a question of whether transborder corporations (meaning any corporation that operates, in some meaningful capacity, outside the borders of its host country) could, in particular situations, be called transnational in terms of sovereignty? Should a purely transnational corporation exist, it would not be affected by the normal legal order of the nations where it operates, or, in other words, it would do its businesses in a permanent state of exception that it would also control. In an international system based on sovereign states this is not possible, but nevertheless it could be possible to find something quite close to it.

We need criteria for judging whether this hypothesis holds true in particular cases. Although it is impossible to draft clear quantitative test for measuring the possible sovereignty of corporations, it is feasible to put together a set of indicators by drawing from the knowledge and conclusions of the earlier parts. The important indicators are:

1. does the corporation exploit one or more the states of exception (or in some offshore structure(s);
2. does these states of exceptions form a central part of corporation's businesses;
3. has the corporation participated in creation of one or several states of exceptions;
4. is the corporation capable to affect and change the internal functional logic (i.e. effective legislation) of the states of exceptions; and
5. can the corporation operate independently within the state of exception (degree of secrecy) or does it have to share the power with the jurisdiction that has originally issued it?

The first point is obvious. If the corporation is neither incorporated in tax haven nor has significant offshore subsidiaries, accounts or other facilities, there is not much reason to call it transnational. The corporation can be active and aggressive within the framework of competition state, negotiating subsidies with host governments and relocating from one onshore state to another(s), but in conceptual terms it means simply multinationalisation phenomenon with a twist of the competition state. The second point's question is much more difficult to answer. If the corporation operates within the offshore state of exception, it does not necessarily mean that it would be in transnational relation to sovereignty. This is the case if the corporation merely exploits the offshore services with no considerable impact on how the corporation's operations are constructed or maintained. Against this background the three last

questions turn out to be truly meaningful in judging whether a particular corporation falls more in the category multinational or transnational.

If we are dealing with a corporation which operates offshore in the state of exception, either through subsidiary, headquarter, or other facilities, one issue to consider is whether the corporation has participated in creation of the state of exception. While being insignificant question with established offshore financial centres, this is a relevant concern in many areas of offshore. Flags of convenience registers, tax haven vehicles and export processing zones can be set up on ad hoc basis, based on wishes or explicit suggestions of some corporation that will benefit from establishing the offshore facility. There are various real-life examples of these kinds of activities, some of which will be dealt with in the case study section below. Corporations can, for example, get an export processing zone legislation tailored to their needs; purchase or lease a flag of convenience register; or, as in case of some accounting firms, help tax haven governments to draft ring-fenced legislation that enables them to sell tax/regulatory avoidance services.

The fourth question is a matter of control capacities. It helps in differentiating the creation of the state of exception from its effective control. As for example, there can be a situation where an accounting firm has participated in creation of legislation for some tax avoidance vehicle, and that it can easily update the legislation in order to meet challenges arising from changing international or foreign regulation. Same could apply to export processing zones especially in relation to immaterial rights, where pace of regulative development spurred by IT innovations has been rapid. A corporation operating in an EPZ designed for IT work could have an important role in updating the legislation in this kind of situation.

The last, fifth, indicator is related to the previous question of control capacities. It helps us to distinct the sovereignty to control a state of exception from the power to control it. We need to bear in mind that the things taking place within the state of exception do not necessarily have to follow written contracts or laws. Therefore offshore jurisdictions can hand down the power for controlling the state of excpetion not only explicitly, but also implicitly by turning consciously a blind eye to internal activities of the state of exception. This is a relevant point especially with export processing zones, where the nature of control is by and large biopolitical power over workers (in addition to power over environment and larger regulative questions related to EPZs). Even though host government might not explicitly allow exploitation of EPZs' factory workers, intentional leaks in monitoring and control of EPZs can have same results.

These indicators need case studies for back-up. I will take few prominent examples that shed light into each one of these points, related to tax havens, export processing zones, and flags of convenience

registers. Same kind of analysis could be used to market agents shaping the IBFs as well.

4.3. Case studies

4.3.1. Flags of Convenience Registry Firms

Recall from the part 3 what the former prime minister of Belize, Manuel Esquivel, said on illegalities surrounding the Belize's FOC register: "[t]here was little we could do. These people aren't responsible to anyone. The ships are never seen in Belize. The Belize shipping industry has been privatised. There should be proper accountability."[118] But who are, then, "these people" that Esquivel grumpily dismisses? From all the places in the earth, the answer can be found from Singapore. The people responsible for Belize's ship registers are actually working for a subsidiary of a Singapore-based multi-industry company called–perhaps with a sense of irony?–as Sovereign Ventures. The corporate group Sovereign Ventures handles everything from oil exploration to real estate and e-commerce, but the relevant subsidiaries here are "Sovereign Ventures Pte Ltd", "International Ship Registries Pte Ltd", and "Mongolian Ship Registry Pte Ltd". Together they serve as registration agent for Mongolia, Tuvalu, Panama, Belize, Honduras, and "many more worldwide".[119] And not only as an agent–the services of Sovereign Ventures seem to span from marketing to legal advice and handling of everyday businesses, at least in the cases of Tuvaluan and Mongolian registries. Details of the contracts between Sovereign Ventures and the governments are not public, but some interesting information can be found from their website:

(2) The Mongolian Government appoints the Mongolia Ship Registry Pte Ltd, Singapore (MSR) as the exclusive principle agent to process registration applications for ships flying the Mongolian flag. MSR is fully authorised to issue all the necessary documents and certificates and to administer the whole registration system. To facilitate the conveniences of international shipowners, MSR is based in Singapore, which offers efficient telecommunications, financial and legal services easily and accessibly. It is staffed by qualified professionals and well placed to take on the challenge of providing efficient and quality services to shipowners who choose to have their vessels fly the Mongolian Flag. *(International Ship Registries 2006)*

Elsewhere, in a newspaper interview, the deputy registrar of the MSR stated that "[w]e are not a fly-by-night company or flag of convenience which are all out to make money --- we are a very strict regime because this ship registry is run directly by the government." Thus, in the formal chain of command, the Mongolian state seems to be the ultimate authority, but the reality might be more ambiguous. In light of Mongolia's

[118] *ICFTU 2003, 13*
[119] *International Ship Registries 2006*

land-locked situation and the fact governmental experience in seafaring business before establishing the ship registry in 2003 was virtually zero, it is probable that in the end it is MSR's word that counts in drafting the required regulation and in keeping it up-to-date. The only imaginable reason for a land-locked country to set up a ship register is potential revenue, and that is the field where MSR knows how to deliver. As an onshore state Mongolia is actually in odd company, because it is the tax havens-turned-FOCs such as Belize and Tuvalu to whom this kind of revenue logic is more familiar. The state of exception of the Mongolian ship registry was most likely set up in co-operation of the Mongolian government and the MSR corporation, the control of the state of exception being in the hands of the MSR. The public documents do not show whether the contract has been drafted for limited period or for time being.

The MSR decided to contact Mongolian government shortly after the state of Cambodia had decided to cancel its own contract with another privately operated ship registry, Cambodian Shipping Corporation. The move came about after the French Navy had seized a Cambodia-based vessel for alleged cocaine smuggling.[120] This is an example on how the state can have authority over its outsourced FOCs in a different extent than above cited Esquivel's comment on Belize's situation hinted. Everything depends, however, on terms of the contract and possible sanctions for breaking its rules, in addition to functional capacities and corruption of the concerned FOC government. Apparently are no precedents of cases where FOC host state has broken its contract with the corporation that manages its registry.

One better-documented example on outsourcing of FOC registries can be found amongst the giants of world's commercial fleets: Liberia. The corporation that runs Liberia's register is called "Liberian International Ship & Corporate Registry". Based in Reston, Virginia, it offers everything from Limited Liability Corporations to ship registry services, maintaining also the registry of Marshall Islands.[121] Its history stretches back to 1948, when the International Trust Company, based in Monrovia, capital of Liberia, was founded. Since then, the Liberian registry has gone through series of transformations from International Trust Company to International Registries Inc of Virginia, and in 1999 to Liberian International Ship & Corporate Registry (LISCR) for a ten-year period. Astounding thing is that, as a 'refugee' in U.S., the ship registry was fully functional even during the Liberian civil war of 1990-1996, during which the revenue from registry accounted for 90 per cent of the total state budget! Even today, the revenues represent 25 to 50 percent

[120] *Shipping Times 2003 in International Ship Registries 2006*

[121] *Liberian International Ship & Corporate Registry 2006; Palan 2003, 53*

of Liberia's budget (the Bureau of Maritime Affairs and the Ministry of Finance give confusingly different figures).[122]

The Liberian case differs from the Sovereign Ventures in the sense that the state has always been significant owner of the company that handles the registry. This is not the case, however, with Mauritius. As a renter of LISCR's services, it is in a role of merely providing a legal platform for FOC registry, and collecting part of the revenues arising from registrations. This exemplifies the diversity of the possible states of exception and the competencies for issuing and controlling them: when Mauritius rents FOC services from a corporation based in U.S., with offices around the world, owned by Liberian state (albeit, during the history of Liberian FOC registry, parts of the ownership have been in private possession) in a situation where political responsibility of the ship registry is in the hands of the Liberia's Commissioner of Maritime Affairs, the situation could not be much more complex. The essential things to notice are, however, that Liberia has commercialised part of its sovereignty by transforming the FOC register to U.S. based firm; the result of this procedure is conceptually in creation of a state of exception; and that the Liberian International Ship & Corporate Register Ltd controls this state of exception. Yes, Liberia could cancel the corporate structure, as could Mauritius, but nevertheless certain amount of sovereignty has been shifted to corporate control for a certain period of time. These FOC case studies fill first four criteria well, and partially also the fifth criterion.

In light of this background it is clear that both Sovereign Ventures and LISCR exploit states of exceptions as a fundamental part of their businesses; are capable to change the rules of these states of exceptions; and even that they can operate relatively independently as regulators and rule-makers within these states of exceptions. Therefore, Sovereign Ventures and LISCR seem to be more transtnational than multionational corporations.

4.3.2. The Big Four Accounting Firms

In 1996, Susan Strange began her case study on the political effects of major accounting firms by noting that "[t]he big six accountancy firms – Price Waterhouse, Peat Marwick McClintock, Coopers & Lybrand, Ernst and Young, Deloitte Touche Tohmatsu and Arthur Andersen – play an important part in the world economy", adding that "[f]ew academics outside accountancy realise how big they are".[123] While the last two remarks are still true–accounting and auditing is a crucial part of determining the tax and regulatory responsibilities of corporations–much has changed in only a couple of years. The big six accountancy firms have, by now, become the Big Four: KPMG (successor of the Peat Marwick–Strange's list is badly outdated and based on the market

[122] *United Nations 2001, 84-86*
[123] *Strange 1996, 135*

situation in the 1980s); PriceWaterhouseCoopers (formed after merge of the Price Waterhouse and Coopers & Lybrand); Ernst and Young; and Deloitte Touche Tohmatsu.

The accounting firms have internationalised by following their clients' expansion abroad from their host countries especially from 1970s onwards.[124] During this process–and through several mergers and acquisitions–the number of big accounting firms has been on decline, while the size and importance of the remaining accounting giants has respectively increased. The reach and know-how of the Big Four firms is global, at least in relation to relevant markets. They have subsidiaries in a large number of countries, including all important tax haven jurisdictions. This background enables the Big Four firms to advocate not only multinationalisation of corporations, but, potentially, also facilitate their transnationalisation. The Big Four's triple role as accountants, auditors, and tax advisors (one could add to the commonly presented list a fourth role as advisors for governments, especially to tax havens) is an advantage in designing complex schemes for tax and regulatory avoidance. In some cases, they have been convicted of assisting in tax evasion and money laundering operations. Together the annual global income of these four corporations goes up to US$55 billions (2003/2004).[125] It is no exaggeration to say that the Big Four accounting firms are, together with banks and other financial intermediaries, oil in the wheels of transborder corporations' offshore activities.

As the Arthur Andersen was prosecuted and convicted of obstruction of justice for shredding documents related to its audit of Enron, the world of accountancy suddenly began to appear in breaking news. In turn of the millennium, Enron became to be the biggest and most astonishing corporate scandal ever. These headlines were followed few years later with major tax avoidance investigations and trials in U.S., with KPMG as the main target. Many other investigations involving all of the Big Four accountancy firms have been conducted in various countries, including also the infamous crashes of Barings Bank and BCCI in 1980s (BCCI) and 1990s (Barings). These two financial catastrophes sent shockwaves through markets and created claims that the auditors–and not only regulators–should have been much more vigilant.[126] I will not give here a comprehensive account on the Big Four's operations around the world, but concentrate on the evidence of their role within offshore instead. Much of the information available is related to some sort of misbehaviour or scandals, but it is important to remember that the generally disreputable examples are only one part of the picture. Bubbling under is a constant flow of everyday decisions related to use of tax havens, mis-transfer pricing and other actions that exploit either the mechanisms of the competition state or offshore's states of exception.

[124] *Strange 1996, 137*
[125] *Cousins et al. 2004, 8*
[126] *Strange 1996, 137*

Because of the secrecy which is so central to the working of offshore economy, it is also difficult to find comprehensive accounts on how the dynamics of accounting giants and the tax haven jurisdictions they advise have worked out. An exception to the rule is, however, the tax haven State of Jersey, which has been studied rigorously during past ten years or so by especially Mark Hampton, John Christensen, Prem Sikka, Jim Cousins and Austin Mitchell. Located near the French coast with other Channel Islands, Jersey is a Crown Dependency that is neither part of the U.K. nor a member of the European Union. The U.K. has negotiated a special trading position for Jersey with EU countries. Jersey passports even have text "European Union" peculiarly printed on them. The government of Jersey "neither separates the functions of legislature, executive and judiciary nor has a formal 'opposition' in parliament in its single chamber Parliament, the States of Jersey, which consists of 53 elected members (12 Senators, 29 Deputies and 12 Connétables), plus representatives of the UK Crown, the Bailiff (i.e. Speaker of parliament who in his capacity as President of the Royal Court also acts as a judge), the Lieutenant Governor (resident representative of the Crown), the Dean of Jersey, the Attorney 25 General and the Solicitor General (both appointed by the Crown)." [127]

With a population of less than 90 000 people, the island has a finance sector worth £400 billions (about US$700 billions in April 2006 rates) and part-time members of the State of Jersey meeting in average of 6-7 days month to oversee its regulation. They are "poorly resourced and lack researchers to support them in their efforts to scrutinise the policies of the executive." Furthermore, the Jersey is a non-party state with no formal cabinet, prime minister or president. Everyday governmental tasks are in the hands of a series of Executive Committees, in most cases with no formal definition of their responsibilities and the public cannot attend their meetings or access the minutes.[128] Obviously this combination of insufficient know-how and poor capacities, bundled with the lack of public scrutiny, creates a fertile ground for outside interest groups to advocate legislative changes that suite their needs and demands. And, as we shall shortly see, the accounting firms have been eager to try. The following case study is, unless otherwise explicitly stated, based on Mitchell et al. (2002) pp. 47-55.

The concept of liability is central not only to the responsibilities of corporate directors in general, but perhaps even more to the accountants and auditors. They are, after all, responsible that the financial reports of the giant corporations are reliable, trustworthy and accurate. If the liability laws of the accountants are smoothened, the accounting firms can take more risks and use fewer resources on securing the prudent work. This was one of the central issues as major accounting firms hired lobbying

[127] *Mitchell et al. 2002, 39*
[128] *Mitchell et al. 2002, 24-25, Hampton 1996, 137*

firm Ian Green Associates to “find ways of securing liability concessions” in 1995. The objective was to enact a suitable limited liability partnership (LLP) legislation in Jersey. Subsequently, a member of local law firm, Mr. Ian James, met the Director or Jersey’s Financial Sector Department in order to discuss the proposal. James told in his letter to the Finance and Economics Committee that he had been working with Price Waterhouse for finding a suitable location for LLP legislation. It “would give the partners of a partnership registered under that law limited liability whilst permitting them to take part in the management of the Special Limited Partnership”. He added that “PW with its advisers has investigated a wide number of jurisdictions for this purpose” and that also “Ernst & Young have a strong interest in registering under the provisions of a Special Limited Partnership Law if it was passed in Jersey”.

Drafting of the law was soon under its way. The Director of Jersey’s Financial Services Department reported to the president and members of the FEC that “law drafting would be undertaken entirely at the expense of Price Waterhouse (together, possibly, with Ernst & Young) and what the Committee is being asked to do at this stage is to confirm that it is prepared to sponsor legislation in the States”. The legislation proceeded soon to the powerful Policy and Resources Committee (PRC), which “considers broader issues of desirable policies and resources (including money) devoted to laws”. The PRC voted on the issue, and decided to accept the proposed legislation with one member dissenting. The Committee “had no papers on which to base its decision” but relied on a presentation from its Vice-President. On May 1996 the draft was finally published, ending the principle of ‘joint and several liability’ and replacing it with a principle which declared that “individual partners would not be personally liable for the liabilities of the LLP unless the actually caused the loss in the course of their work”. Other features included that the LLPs were not required to publish audited accounts; there was “no dedicated regulator and no policies or procedures for investigating the conduct of errant auditors; and LLPs registered in Jersey would be exempt from all corporate/income taxes.

Senior politicians expected that the Bill would be passed quickly and quietly–but the case was far from closed. The proposed legislation “encountered unexpected resistance” from “Jersey’s senior law draughtsman, some members of the Jersey States and politicians and academics from the UK”. The law was finally passed in September 1996, and amended with revisions in 1998. In the end, none of the accounting firms registered in Jersey. This is interesting because all along the debates surrounding the issue, the Price Waterhouse and Ernst & Young reaffirmed their intentions to move to Jersey. Mitchell et al. suppose that this was, in fact, a measure for putting pressure on UK legislators in order to get more suitable legislation there, i.e. accounting corporations’ attempt to accelerate the competition state phenomenon. In April 2001, Ernst & Young announced that it will register as an LLP in the UK, and

the PriceWaterhouseCoopers made same decision next year. Mitchell, Sikka and Austin conclude by stating that these

(3) "two accountancy firms bought legislation in Jersey to advance their narrow economic interests. Despite some local resistance, Jersey enacted the law designed and drafted by accountancy firms. However, the firms did not eventually migrate to Jersey. They used Jersey as a lever to squeeze concessions from the UK government with the naked threat that if their demands were not met they would migrate and cause economic and social turbulence. They used their economic and political networks to threaten elected governments." (*Mitchell et al. 2004, 40*)

Indeed, this seems to be the case. To sum it up: according to the words of their representatives, the firms first compared several tax haven jurisdictions in order to find the most suitable one for a piece of legislation that would enable them to avoid their onshore responsibilities, and then drafted the required legislation on their own expense and with their in-house resources. Finally they managed to get the involved State of Jersey's committees to accept the proposed legislation even without relevant background information, relying merely on oral presentation. The public distress that followed the draft came apparently as a surprise to the senior politicians of the island, who had all seen the introduction of several similar pieces of legislation during the years. This is a brilliant example of both the competitive pressure that drives tax haven jurisdictions to find yet unexplored market niches (the competition state), and of the ways how incompetent and poorly resourced tax haven governments rent their sovereignty (the right to issue a state of exception) to accounting firms that draft legislation suited either for their own purposes or for the purposes of their clients.

In 2002, The Guardian newspaper investigated the level of scrutiny in tax haven Belize. The reporter introduced himself as a potential customer, willing to buy there un-audited, anonymous off-the-shelf company, with a Visa card that would have enable withdrawing clandestinely money from ATMs around the world. This was not only endorsed, but the local office of the KPMG also promised that "it would not have to disclose the owner's true identity to the Belize government".[129] What is more, the KPMG had been contracted by the UK's Department of International Development to audit the tax-exempt Bank of Belize, which operates the registry of the offshore companies "to investigate claims that the debt-ridden Caribbean country was failing to collect enough tax revenue because of its extravagant tax exemptions". This is another example of the conflicts of interest that can arise as a private company that markets tax consultancy and other financial services is hired to audit or regulate governmental branches in concerned jurisdiction. Again, the control–here in a sense of overseeing the business–of the state of exception in tax haven jurisdiction was rented to

[129] *The Guardian 2001*

a firm whose resources outnumber tax haven jurisdiction's capacities by far. The Jersey case study fills the first three criterion in the test list of transnationaliness, even though the proposed legislation raised unexpected resistance. The KPMG's actions in Belize could have partially filled the last points as well because of its dual advisory role.

The aforementioned triple role of accounting firms (accountants, auditors and advisors), in addition to their wide range of activities in tax havens, puts them in the heart of the transnationalisation phenomenon. As such, they can be called partially transnational. The most important thing is, however, that the Big Four corporations help other multinationals to adapt the logic of offshore and turn from multinationals to transnationals. If we follow Hampton and address offshore as an interface, then accounting firms are amongst the constitutive building blocks in that interface.

4.3.3. Export Processing Zones: The Case of Namibia

Namibia is a newcomer in the export processing zone business. As one of the first African state to pass national EPZ laws in 1995, it created an example for other South African states to emulate. It was not the first one, though, as Zimbabwe had launched the trend with its EPZ program one year earlier.[130] The Namibian Labour Resource and Research Institute claims that Namibian government is "riding many horses" in adhering to neo-liberal fiscal and monetary policies while promoting the job creation prospects of the SME sector and the informal sector as well.[131] As a part of Namibia's intentions to become internationally competitive and attracting, it established the EPZ act in 1995 with high hopes of creating 25,000 new jobs. Perhaps as a result to the difficult competitive situation in world's EPZ markets, it decided to adopt a highly flexible EPZ system. With both territorially framed zones and single-unit zones being offered, companies can either choose to locate in industrial parks near ports and harbours or establish a zone in a single production site with other advantages (e.g. proximity to natural resources or suitable labour).[132] Namibia's EPZ laws were tailored not only for industrial production but also for high-tech industry. The purposes for setting up the EPZ legislation were "to attract, promote or increase the manufacture of export goods; to create or increase industrial employment; to create or expand export earnings; to create or expand industrial investment, including foreign investment; and to encourage technology transfer and the development of management and labour skills"[133].

The EPZ act faced strong resistance because of its loopholes in health and social issues. Albeit Namibia's Social Security Act applies fully

[130] *Jauch 2002, 101-104*
[131] *Labour Resource and Research Institute 2000, 40-41*
[132] *Labour Resource and Research Institute 2000, 19*
[133] *Ayoade 1997 in Labour Resource and Research Institute 2000, 42*

in EPZs, this is not the case with the Labour Act. For example, a provision outlaws the right to strike.[134] The EPZ legislation allows Ministry of Trade and Industry, in consultation with the Minister of Labour and Human Resources Development, to make "regulations regarding basic conditions of employment, termination of employment and disciplinary actions, as well as health, safety and welfare conditions".[135] In other words, the state of exception in Namibian EPZs allows the basic level regulation of employment, health and safety to be tailored case-to-case by mere administrative decisions. Here we see a brilliant example on how control and issuing of the state of exception turns into mundane everyday activity. Within the Ministry of Trade and Industry "potential investors in the EPZ contact a special body, the Offshore Development Company (Pty) Ltd (ODC)". Interestingly ODC "is a private company with a minority share (15%) owned by the Namibian government". It is responsible of implementing the EPZ scheme on behalf of the Ministry of Trade and Industry.[136] This means that the situation is very much alike with previous examples on corporations that operate the commercialised ship registries of sovereign nations. Here, again, the company does the legislative task of controlling the governance of the state of exception–albeit in framework set by the state and in co-operation with the state–and can therefore be called partially sovereign.

For corporations the Namibian EPZ is amongst the most favourable ones in the region. It offers the following basic incentives (with some restrictions, such as a limitation that only 30% of the production can be sold in Namibian market):[137]

- Corporate tax holiday
- Exemption from import duties on imported intermediate and capital goods
- Exemption from sales tax, stamp and transfer duties on goods and services required for EPZ activities
- Reduction in foreign exchange controls
- Guarantee of free repatriation of capital and profits
- Permission for EPZ investors to hold foreign currency accounts locally
- Access to streamlined regulatory service ('one stop shop')
- Refund of up to 75% of costs of pre-approved training of Namibian citizens
- No strike or lock-outs allowed in EPZs
- Provision of factory facilities for rent at economical rates

[134] *Labour Resource and Research Institute 2000, 19*
[135] *Labour Resource and Research Institute 2000, 53*
[136] *Labour Resource and Research Institute 2000, 44*
[137] *Ayoade 1997 in Labour Resource and Research Institute 2000, 44*

In light of the first five years after the EPZ act was issued the Namibian EPZ experiment has been a limited success.[138] The Offshore Development Company claimed that in 1998 over 35 companies were "engaged in the manufacturing of various products, --- over nine companies --- engaged in the processing industry --- while six companies --- engaged in re-export warehousing activities". However, the Labour Resource and Research Institute's research group found only nine operational companies during their field work in 2000. These companies were: toy-producing company Johanna Haida Teddy Bears; automobile component producer Namibia Press and Tools; acrylic bathroom ware manufacturer Libra; rope producer Marine Ropes International; Namibian state's and diamond firm De Beer's joint venture NamGem Diamond Polishing; ostrich meat producer Ostrich Production Namibia; cooking ware producer New Sun Household Namibia; furniture firm Tax Free Warehouse; and multi-field producer Goran Enterprises. In addition to these, Labour Resource and Research Institute notes that few other firms had recently launched firms with EPZ status. Most of the firms are subsidiaries of foreign, often European firms. Closure of EPZ firms is common, with many companies operating for only few months. Only taxed income is that coming from EPZ employees' salaries, but only 10% of employees earn enough to fall into taxable income group.[139]

Jauch introduces some recent examples from Namibia's EPZ sector: "Desperate to show some success for the EPZ programme, the ministry has started to grant EPZ status to a poultry plant in Karibib (western Namibia) as well as to mining companies such as Ongopolo (a copper mine in Tsumeb, northern Namibia) and the Skorpion zinc mine and refinery in southern Namibia, which is currently being developed by the Anglo-American Corporation". He continues by stating that "[a]lthough Ongopolo and Skorpion obtained EPZ status only for their processing operations, it is likely that they will use the EPZ status to gain complete tax exemption from their profits" with simple accounting tricks like misuse of transfer pricing. As such, this broadening of the EPZ sector illustrates competition state phenomenon which relies on government-initiated states of exception. The active political agency is reserved to the Offshore Development Company, which enjoys a high level of independence in decisions over how the EPZ is managed and administered. Therefore the ODC seems to fill all criterions of transnationality quite well, even though it is not that big company in world scale.

Ramatex is the undeniable leader of the Malaysian textile industry. It produces garments for companies like Nike, Adidas and Wal-Mart with subsidiaries in Mauritius, China, Namibia and South Africa. It has also three investment holding companies, with one in Singapore and other in

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[138] *Labour Advisory Council 1999 in Jauch 2002, 105; Labour Resource and Research Institute 2000, 46*

[139] *Labour Resource and Research Institute 2000, 46-49*

tax haven British Virgin Islands.[140] These kinds of tax haven investment holding companies are typically used for tax avoidance purposes with help of a method called 'thin capitalisation'.[141] The decision on setting up the Namibian production site was made in 2001 after a fierce competition between Madagascarian, South African and Namibian governments. The deal was not cheap for the government of Namibia. It was achieved by promising Ramatex even greater concessions than those provided to other EPZ companies. "Drawing in the parastatals providing water and electricity (Namwater and Nampower) as well as the Windhoek municipality, the Ministry put together an incentive package which included subsidised water and electricity, a 99-year tax exemption on land use as well as over N$100 million to prepare the site including the setting up of electricity, water and sewage infrastructure."[142] This is another example of merge of the competition state phenomenon and transformation of sovereignty: as a result of the competition state trend, Ramatex was able to gamble three states against each other for an investment, which was secured by issuing another *ad hoc* state of exception in addition to the original EPZ legislation. This means that Ramatex fills the first three transnationality criteria well, and it is more than probable that it would pass the fourth test, too.

4.4. Conclusions

The above examples are far from comprehensive account on the users and ways for exploiting the offshore's states of exception. The secrecy that surrounds the structures and users of offshore would prevent success from any attempt to grasp the full picture of offshore. I could have drawn more examples, but from theoretical viewpoint they would have brought little additional information. I have already provided archetypes that prove the need to take corporations into account in discussions on sovereignty. The more offshore penetrates into everyday business practices and the more it becomes a normal trait of the onshore states, the more common sights will the above-like examples become.

As I noticed earlier, the IMF estimates that already more than half of world's financial flows go through tax havens. Moreover, the gathered evidence showed that use of tax havens, export processing zones, flags

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[140] *Labour Resource and Research Institute 2003, 8*

[141] *Thin capitalisation is, just as mis-transfer pricing, a method for transferring profits from production host countries to low-tax jurisdictions. In a typical thin capitalisation scheme the subsidiary that organises production in onshore state does not own its facilities, but rents them from an investment holding subsidiary located in a tax haven. As a result the profits are shown in tax haven while the balance sheet of the subsidiary that organises production suffers from high rents it pays to the holding company.*

[142] *Jauch 2002, 106; Labour Resource and Research Institute 2003, 6-7*

of convenience registers and offshore financial centres have become an integral part of global business. Therefore, albeit the above examples are only narrow sights into the whole offshore economy, they nevertheless are important. It is clear that tiny FOC jurisdictions find it easier to outsource the creation and operational tasks of their ship registers. It is evident that Namibian example is not an anomaly, but rather an illustrating sight into workings of not only competition state phenomenon but also the EPZ states of exception. And, with combined US$55 billion annual income, accounting, auditing and advising the major transborder corporation is definitely big business where the obedience of law and corporate social responsibility–even in its minimum conceptions–have not been on a high course. As William Brittain-Catlin observes, the major brands we all know have internalised the logic of offshore carefully:

(4) "A quick look behind the leaders of the Fortune 500 top corporations shows the significance of the Caribbean offshore circuitry alone. General Motors aggregates its sales and leasing revenues in Cayman and its revenues from reinsurance and finance subsidiaries in Barbados. ExxonMobil had eight holding companies in the Bahamas and Cayman alone. The Ford Motor Company's reinsurance group is split between Cayman and Bermuda, while IBM has holding companies in Bermuda, the Bahamas, the British Virgin Islands, and Barbados. --- Each Caribbean subsidiary is essential to the competitive financial enterprise of these $100 billion corporate giants." (*Brittain-Catlin 2005, 44*)

Held et al. notice that "geography still matters: MNCs cannot simply locate anywhere or everywhere".[143] While this is, in principle, true, it can easily lead us into misconceptions on what does it mean for an MNC to locate somewhere. For today's transborder corporations location is a multi-faceted issue, as Brittain-Catlin's examples illustrated. It is one thing to headquarter in a jurisdiction, another thing to produce tangible things or services, and yet another thing to decide where to show profits and pay taxes. Therefore, even though a particular corporation might seem like its located in particular country, in fact its tax burden there might be significantly low. The traditional indicators of the extent of foreign direct investment or company headquarters[144] are thus only a partial and potentially misleading indicator of the extent of corporation's multinatoinaliness or transnationaliness. As the currents of world trade shift more to sale of services and rights instead of industrial production, the fictional and highly mobile type of transactions within corporations are likely to become increasingly common.

Therefore the division between multinationalism and transnationalism is not only plausible but also essential to grasp. This is the case especially if we are interested in the ways corporations use power, act

[143] *Held et al. 1999, 269*
[144] *Held et al. 1999, 236-282*

politically, or relate to sovereignty. Even difficulties in measuring the 'transnationaliness' of any transborder corporation do not downplay the justification of this conceptual distinction. It is erroneous to speak about transnational corporations without defining the relationship between the corporation and the aspect of nation-state system it can or should be seen as transnational. I think that offshore is an interface worth reserving for this purpose. The offshore is, basically, a complex web of states of exception. One could even speak about globalised state of exception, in a sense that the vast majority of these exceptions would make little or no sense in genuinely national level.

Developing exact measures for estimating the transnationaliness or multinationaliness of a corporation is not, in my consideration, amongst the main concerns here. If we accept that the workings of offshore finance create spaces for transnational action, the next logical step would be to ask a) whether this development is desirable; and b) how we could and should govern it. Transforming a single firm into more accountable and transparent ('multinationalising it') with help of some meters measuring the transnationaliness or multinationaliness of a corporation would mean relying on corporate social responsibility, and, as has been seen in various corporate scandals, CSR can be a wobbly construction. Of course there are many corporations do relatively good job with their CSR programs, but, as with any voluntary action, in larger scale there is always someone who does not want to adhere to the commonly agreed rules. Therefore, the questions of governance and acceptability of the commercialisation of sovereignty need to be answered.

In the debate on corporate social responsibility (CSR), a common reply from corporations' side to claims for extending CSR is that they are operating according to the laws drafted through democratic and parliamentary processes, and everything else would actually neglect democracy. In some cases this is indeed true. In principle, the governments set up the rules for minimum behaviour, and after that point it is up to the company management and shareholders to decide what goals they want the company to pursuit. But in case of more transnational corporations. the above argumentation is on weak grounds. If corporations negotiate special exemptions from their most fundamental responsibilities in fields of taxation, labour rights and environment, this process can hardly be called democratic. The problem is more persistent if these exemptions are conducted offshore and under the veil of secrecy.

Any shift of constitutional powers–no matter how the constitution has been drafted in particular countries–should require vast and throughout public discussion and a majority decision. For the most part this has not happened even in the case of competition state processes. But competition state is essentially about shifts in power from one group of actors (states) to another (corporations and investors). The transnationalisation phenomenon, on the other hand, is about shifts in sovereignty and politics, which is even more serious threat to democracy.

Power can be used in democracies in various ways and with various methods, but the constitutional mandate for authority in politics is, even in the age of contemporary globalisation, in the hands of national parliaments. The threat to this authority is the most urgent issue surrounding offshore finance and transnational corporations, and dealing with comprehensively would be a lengthy account. In the next, final part, some modest openings are discussed.

5. Conclusions

(5) ”If the tax state were to fail and another form of providing for the wants of the community ensued, this would --- mean much more than that a new fiscal system replaces the prewar one. Rather, what we call the modern state would itself change its nature; the economy would have to be driven by new motors along new paths; the social structure would not remain what it is; the approach to life and its cultural contents, the spiritual outlook of individuals – everything would have to change.” *(Joseph Schumpeter 1991 [1918], 100)*

The tax state is in crisis. Every day, billions of dollars are being transferred around the globe with the sole purpose of avoiding or evading taxes that democratically elected governments have found wise to impose to their citizens. Both wealthy individuals and transborder corporations have managed–in varying degrees–to detach themselves from taxation and regulation surrounding different business activities and ownership of financial assets. Results of the rampant tax avoidance and evasion are seen as governments struggle to maintain even basic standards of living or structures of the welfare state. But just as tax avoidance and evasion is not the sole reason for the crisis of the tax state (competition state is, as was demonstrated in part 4, another side of the phenomenon, in addition to trade policy issues etc.), this crisis does not manifestate in mere monetary terms. The poverty and tilted income distribution (tilted especially because it is not decided in parliamentary fashion) that the structures of offshore generate create various social and systemic effects, described in earlier parts. But, perhaps even more importantly, the offshore is in crucial role in shaping our understanding of such questions as what is the state; what is sovereignty; and who has the capacity to engage in politics? Answers to these questions were sought in the previous part especially from the narrow viewpoint of transborder corporations. What emerged was that there indeed are examples of new kinds of transnational spaces. In these offshore’s states of exceptions, transnational corporations can not only avoid normal onshore regulation but also be in partial or total control of the regulation that sets limits to their actions.

From today’s perspective, Schumpeter’s important insight to the importance of taxation as a formative component of the modern state creates some confusing questions. Few important changes that form the background for the crisis of the tax state seem evident. First, the modern

state has already changed its nature. Sovereign states–including at least the developed, capitalist countries of Europe and elsewhere–used to be able to decide their tax levels and social systems relatively independently within the Keynesian trends of the world economy, as the mobility of both corporate and natural citizens was lower. It was not that long time ago when, as for example, the major corporations in U.K. were nationalised and privatised in various occasions depending on which party–Tories or Labour–was in power. Today, this would be unthinkable in vast majority of states. The reason why the political horizons of the governments have narrowed has very much to do with the global competition state phenomenon.

Second, the concept of citizenship is undergoing a profound change. Many concerns over effects of limited liability and separated corporate citizenship were raised as the modern incorporation laws, together with practices that guarded them, were drafted in turn of the 20th century. The people who took part in these discussions and law-making processes did not and could not, however, predict the 'shrinking' of the world as a result of developments in travel and communications technologies that created the material basis for contemporary corporate globalisation. Neither could they predict that this technological revolution coincided, in significant length, with retreat of the state from several of its regulative and political functions, many of which it had only begun to acquire at the time when these corporation laws were drafted. Lastly, third thing that understandably escaped the imaginations of the creators of the modern corporation was the rapid 'corporatisation' as many of the traditional state or welfare state functions–health care, education, internal security, even military–were privatised in various countries around the world. The 'schizophrenic' corporations could reside in one jurisdiction, pay taxes in other, while doing majority of their business elsewhere. And as the state retreated, many of the voids in markets were filled with transborder corporations that grew constantly through domestic and transborder mergers and acquisitions.

This inherent fiction of citizenship has become visible in other way as well. Not only are Agamben's 'illegal aliens' or stateless persons shaking the foundations of how we conceptualise and grasp what it means to be a citizen of a state, but we are also witnessing a phenomenon of super-rich who have, in a sense, begun to act like transborder corporations. Not paying ones taxes is already an old trick, as tax haven accounts and off-the-shelf companies are advertised broadly in world's major business newspapers. I do not want to undermine the significance of this rupture in the tie between a citizen and a tax payer, but the market for citizenships is even more interesting issue. Several tax havens are selling their passports, together with a citizen status they provide, to anyone who has the required amount of hard currency, and/or is willing to invest in the country. Some onshore states, Ireland at least, have had similar practices–only that the price tag for an Irish citizenship was much more

expensive.[145] Only investors willing to make large scale productive investments were welcomed to this VIP club. And, states especially in rich Middle East, but also in Europe, have offered lucrative deals for sport stars coming from developing countries if they have been ready to change their nationality and compete under a new flag. Many have agreed. These kinds of headlines bring inevitably the absurdities and contradictions of citizenship in the face of the public. Not overnight, but little by little. States can slower this citizenship shopping by building their tax systems so that new nationality will not help in tax avoidance–and many countries, especially U.S., indeed have strict legislation in this sense–but it will not stop the erosion of the concept of citizenship.

Third, in the age of contemporary globalisation, the economy has been and is driven "by new motors along new paths". With help of the present day communications technologies the production processes have been separated in different locations while retaining the unity of the process.[146] Thus, viewed from the firms' side, the production of tangible goods has been separated from strict locational restrictions. Furthermore, the processes of financialisation (measuring the value of tangible goods with financial assets that can be bought, sold and speculated with globally) and shift from industrial production to trade in services and other intangible goods has fundamentally changed the way world economy works. This shift has been matched with the general transformation from hierarchical, pyramid-like corporations to "network enterprises" that are built around flexible decision-making chains, mobile structures and the logic of autonomous systems of goals networking both at intra-firm and inter-firm levels.[147]

Fourth, states have aided in this process by liberalising their economies.[148] Liberalisation of trade policies, capital markets and many other regulative fields in 1980s and 1990s were essential building blocks enabling transborder corporations to free themselves from the shackles of national regulation, turn into "network enterprises" and to start full-scale offshore businesses. Many of the recent mergers and acquisitions have crossed the industry boundaries that used to limit business activities, creating firms that span diverse set of industries, with their own investments subsidiaries and so on. Examined from the viewpoint of the competition state, the sheer big size brings major advantages to giant transborder corporations over states in negations with them. Furthermore, the growing importance of transborder corporations' own investing companies–for some traditional industrial firms they are already the most important profit-generating assets–smoothes the shift from onshore production to the world of offshore fiction. The case of Enron was definitely the most illustrating example of this. The company that

[145] *Doggart 1997, 93*
[146] *Castells 2000, 417*
[147] *Castells 2000, 187*
[148] *Castells 2000, 101; Singh 2000*

began by producing energy begun to 'financialise' every part of its businesses, turning everything possible into financial instruments that could be traded and speculated with. Little before Enron's violent fall from grace the company had 692 subsidiaries in Cayman Islands alone.[149]

With all this said, it would still be exaggeration to claim that the tax state has failed. We still live in a world built around states that gather great majority of their income from taxes. But the issue is not straightforward: we cannot answer to the questions Schumpeter posed with blunt yes or no response. Drawing from the conclusions of the previous parts we know that there is already a new fiscal system operating in different parts of the world under logic that is different from both the state-centred, Keynesian economy, but also from the conceptions of *laissez-faire* economy. This system is offshore. Its novelty is not in lack of regulation–we can find convincing examples of that from the imperial era's East India's Trading Company etc.–but in the ways the relationships between corporations, states and citizens are being construed. The offshore jurisdictions have commercialised their sovereignty and transferred parts of it to transnational corporations. Simultaneously they have helped wealthy citizens to detach themselves, in varying length, from their responsibilities to pay taxes and thus from the states where the live in. Therefore, the offshore is indeed much more than a new fiscal system.

The modern state has, indeed, changed. The change that offshore brought happened first in small jurisdictions of Jersey, Panama, Switzerland and the state of Delaware. From these offshore 'islands' it expanded its reach into nearly all micro-states of the world, lurking more and more often to become part of the larger states as well. And, especially as the export processing zone phenomenon started to gain momentum in 1970s and 1980s, the offshore became increasingly embedded in the structures of the onshore states. This is the situation we are facing at the moment. Only time and our own responses of national, international or global governance will tell where the demarcation line between onshore and offshore will be drawn in the future. The states are not entirely without tools for dealing with the problems. What is essential, however, is whether we accept the logic of offshore and competition state as permanent phenomena that we should get adjusted to or that we should even endorse. For the reasons related to democracy, accountability and social justice I think that we definitely need more robust system of governance. It seems like only genuinely enduring option would be to admit the fictiveness of citizenship and state sovereignty, and start to look after new kinds of politics. This is precisely the project Agamben is into, but it is not an easy one. The developments need to progress in steps, because, as Schumpeter already noticed, "the approach to life and its cultural contents, the spiritual outlook of individuals – everything would have to change".

[149] *Brittain-Catlin 2005, 55*

Changing the approach to life is clearly not a matter of one or two political reforms, and neither is it a process that could really be governed or predicted. Nevertheless, there are possibilities for seeking alternatives that are more politically plausible and would, if completed, open new political horizons for even more ambitious projects. No matter what position is primary endorsed in the national-regional-international-global continuum, I think that all forms of governance should be considered as possible and non-exclusive options. There is no space here to ponder the myriad of options and combinations available, and therefore I intend to highlight briefly one extremely interesting proposal that falls into the category of global governance. It is the proposed international accounting standard, drafted by Richard Murphy on behalf of the Association for Accountancy and Business Affairs.[150]

The basic idea behind the Murphy's accounting standard is that transborder corporations (transnational corporations in Murphy's vocabulary) should be dealt with as entities and not as a network of headquarter and its subsidiaries. The idea is that transborder corporations would have to report their turnover and tax by location of their genuine business activities. The TBCs' should publicly disclose information on:

- which entities make up the TBC
- where those entities are located
- what those entities do
- what value of sales they make in each state in which a member entity of the TBC is located split between:
    - sales to independent third parties
    - sales to other entities within the TBC
- what value of purchases from other entities within the TBC are made by each member of the TBC
- how much added value each member of the TBC generates
- how much profit each member of the TBC makes in the locations in which it operates
- what tax each member of the TBC pays in the states in which it is located

This information would assist those seeking information of a TBC with regard to its corporate social responsibility; investments risk; tax risk; its contribution by way of value added to the societies in which it operates; and its contribution to national well-being by way of tax payment within those locations. One of the central objectives of the accounting standard would be to ensure that "the taxes on corporate profit paid by the reporting entity and its related parties in each state in which they operate".

[150] *Murphy 2005, 145-173*

The Murphy's proposed accounting standard is interesting for many reasons, but I find the departure from the bond between nation-states and transborder corporations as its most intriguing aspect. In a way, Murphy's accounting standard would finally admit that transborder corporations are neither multinational, nor they should be transnational, but that they are global instead. What follows is that these global corporations should pay their taxes according to the parts of the globe where they make their profits. This is an extremely intresting aspect not only because it would ensure (together with the transparency that the accounting standard demands) that corporations would pay their share of taxes, but especially because it would shake the foundations of state-centred politics. Perhaps for the first time it would be admitted in this scale that corporations that undeniably act globally should also *be* global. If applied, this mental change could later on arise further questions about the nature of bonds between persons (be they natural or corporate) and nation-states, and help us to find new solutions for the crisis of citizenship.

Of course, there are also many other, more or less ambitious ways for tackling the problems of offshore. European Union Savings Tax Directive is one regional attempt to tackle tax evasion of individual bank-account holders. Introduced in July 2005, it created an automatic system of information exchange between authorities of EU countries on savings held in other EU countries. Albeit the directive was, in practice, full of loopholes (many investment forms were excluded from the scope of the directive and some countries negotiated a lengthy transition period for themselves), the significant thing was that many tax haven jurisdictions both inside, and–remarkably–also outside the EU agreed to implement the directive. The Cayman Islands, as for example, was amongst them. Despite the flaws of the directive it is an important opening for more ambitious proposals. And just as the Savings Tax Directive has targeted the demand side of tax haven services, OECD's black list of tax haven has helped to create better standards for the supply side, urging tax havens to close at least their most notorious loopholes. Neither of these initiatives have effect on transbordrer corporations, but nevertheless they are steps to the right direction.

One thing is sure. If the problems that the clash of national (or at its best inter-national) regulation with increasingly transnational corporations will not be dealt with, the crisis of the tax state will escalate. Coupled with the crisis of the citizenship, it is no wonder that citizens' interest and trust in both national and regional (such as the European Union) authorities is in decline. The offshore has become an embryo for transnational spaces in spheres of economical and financial globalisation, just as internet has been a ground for culturally transnational spaces of communication. Unlike culture, however, the way we regulate the world economy and finance has serious material impacts in virtually all states. These impacts are then mirrored in level of communities and individual households. Therefore the unstable, undemocratic and unequal economy based on

transnational speculative finance and exploitative production can not be justified. It is clear that the transnational spaces of offshore cannot be nationalised and therefore the onshore has to be globalised. Only by doing this we can bring an end to the exploitation of offshore's states of exception.

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