

**HIGH LEVEL CONSULTATION ON THE OECD'S HARMFUL TAX  
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**Promoting a more inclusive dialogue**

**By Hon George A McCarthy, OBE JP  
Financial Secretary, Cayman Islands**

An 18<sup>th</sup> Century French political advisor, writing at a time during the ascendancy of imperialism and colonialism, is reputed to have described taxation as an art rather than a science. The analogy which he chose for his description, loosely translated, was that the art of taxation is the art of extracting from the goose the maximum number of feathers with the minimum amount of hissing. Of course in those times, claims in regard to the legitimacy of taxation were largely circumscribed by geography, and no one (except the goose) expected the goose to either choose which farmyard to inhabit or whether to partake in any dialogue prior to being deprived of her feathers.

In those times, expanding one's tax base generally meant expanding one's empire through colonialism or other more overt aggression, and the view expressed subsequently by the German tactician Clausewitz to the effect that war was merely the continuation of diplomacy by other means, prevailed.

We are now at the beginning of the 21<sup>st</sup> century. The goose has become sentient and acquired the ability to analyse which farm yard offers the best value for feathers plucked. Furthermore the goose has new abilities to move from one farmyard to the next in order to minimize the extent of plucking. The operators of the modern farmyards have realized that if they can send the goose to someone else's yard to feed and then later demand the return of the goose or at least the goose's feathers, they have effectively expanded their own farms at little or no cost.

International relations have also evolved to the point where there is a legitimate expectation in the international arena that differences in perspective can be discussed and common ground found in order to resolve disputes and competing claims.

Those who have organized this conference are to be commended for creating a new forum in which the search for such common ground can go on.

The Cayman Islands recognises that globalisation and the global competition among public sectors that is part of it, present both potential opportunities and potential threats for all jurisdictions. All jurisdictions are moving to optimize the opportunities and minimize the threats.

Recent trends toward globalisation have accentuated a number of concerns in regard to the viability of 19<sup>th</sup> and 20<sup>th</sup> century taxation regimes, and in particular concern over whether current expectations of future transnational tax bases and future government tax revenues can be fulfilled in the globally competitive environment of the 21<sup>st</sup> century.

Many of the concerns over tax related economic competition are not new. Jurisdictions have long competed in the international arena for investment and economic activity in order to provide employment and wealth for their peoples as well as the tax revenues for governments. Tax related economic competition among governments is documented as far back as the 3<sup>d</sup> century BC when the Romans created a special economic zone in Delos to promote the relocation of trade from Rhodes (which Rome did not rule), to Roman controlled Delos.

The academic literature on modern tax related economic competition similarly goes back almost 100 years. Such competition has taken many forms over time. In some cases it has involved the active creation of various types of reduced rate direct tax regimes for potential investors. In other cases it has involved various tax expenditure regimes and the direct payment of subsidies for specific types of investment. In still other cases, jurisdictions have been essentially passive, as is the case where multi-national enterprises have sought out existing fiscal regimes based on indirect taxation rather than direct taxation.

The focus of this conference and a great deal of other international activity is on the perceived need for the creation of a new set of universally applicable rules for international tax related economic competition. This will likely be a process of constructive and vigorous negotiation. It is natural for jurisdictions, whether acting singly or collectively, to attempt to set the rules of economic competition, including those involving international tax, so as to achieve the greatest level of benefit for themselves. In the area of tax related economic competition, as in all others in which nations compete, there is a need for all jurisdictions to behave responsibly in accordance with accepted international law and standards. Engaging in meaningful dialogue is a vital element in this process, as is creating a non-confrontational environment in which dialogue can occur.

The Cayman Islands has long recognised that it is better to be part of any meaningful dialogue than to be excluded from it. In this regard, the Cayman Islands welcomes the opportunities that have arisen to engage in such meaningful dialogue in regard to tax related economic competition. We applaud those who have created such opportunities, through the OECD Global Forum on International Taxation and through the good offices of the Commonwealth Secretariat, to mention just two. We welcome any bilateral or multilateral contact with any jurisdiction willing to join in the process of meaningful dialogue on this subject.

### **Creating an environment for dialogue**

The Cayman Islands would like to suggest that the way forward in the search for a greater degree of consensus in matters of international tax related economic competition involves a number of components, of which three key components are:

- The facilitation of more inclusive dialogue;
- Enhancing transparency through the articulation of a broad set of shared assumptions; and
- Enhancing transparency through the promulgation of a broad set of guiding principles for the process as it moves forward.

The achievement of these three components will go a very long way to creating the international understanding necessary for the process to achieve its optimal outcome. It will also go a long way towards eliminating any existing misunderstandings and preventing new ones from arising. Finally, it will refute any perception that “might makes right” and confirm the legitimacy of the process in which we are now engaged. It will also confirm to the international community that it is the rule of international law rather than “the rule of the big stick” that determines the outcome of the process.

### **The Facilitation of More Inclusive Dialogue**

A clear invitation to participate in meaningful dialogue is critical to the process. The Cayman Islands is pleased to have received such an invitation and to have taken it up. The facilitation of more inclusive dialogue will also involve:

- Mutual education and a shift in focus toward a more broad recognition of the concerns of individual jurisdictions, the legitimacy of the various types of fiscal regimes that exist within the international community, and the legitimacy of economic competition within defined boundaries,
- The use by all participants of inclusive rather than exclusive language and an avoidance of the use of pejorative and discriminatory emotive language, and
- The use of many means and many fora, both new and established.

Addressing the last of these three points first, this multilateral conference hosted by the Government of Barbados in association with the Commonwealth and the OECD is one example of a new forum that provides a very valuable opportunity to facilitate more inclusive dialogue. I would like to once again commend all of those who have given of their time and effort in the organization of this conference.

Recent dialogue among the non-OECD jurisdictions that have joined the international process commenced by the OECD, is another example of a new forum in which all such jurisdictions that have joined the process and those who are contemplating joining the process are welcome. The Cayman Islands would

be happy to share information on this emerging process with any delegation wishing further information.

### **Mutual Education**

Mutual education is vital. There has been a great deal of misunderstanding, seemingly fuelled by narrow self-interest and rhetoric, both in regard to what are the legitimate expectations of individual nation states in regard to transnational taxation, and in regard to what each state may reasonably expect of other states in the international arena. Much of this misunderstanding will be eliminated once there is a common understanding of the political economics and jurisprudence of each participant and the legitimate expectations of each participant.

If you will indulge me, I would just like to give a simple example from our experience of the type of misunderstanding that can inhibit dialogue. Most of you will know that the fiscal regime that has evolved in the Cayman Islands employs indirect taxes rather than direct taxes. The Cayman Islands has never had direct taxes on income, capital gains, wealth, or any of the other direct taxes that have appeared for various reasons in the industrialized states over the past hundred years or so.

Our culture has always favoured taxes based on consumption, as such taxes are more consistent with the fundamental beliefs of our people and our desire to protect our fragile environment. It has also been the experience of the Cayman Islands that the academic models are quite correct in their prediction that consumption taxes have a very low compliance cost for business and individuals. It is also well established that if properly implemented, consumption based taxes are as equitable and broad based as any other model, and can be efficiently administered by a relatively small and inexpensive public sector agency.

Despite the fact that our fiscal regime is both simple and transparent, there are some we have encountered in the international arena who have the completely muddled and misguided impression that the Cayman Islands somehow recently created a fiscal regime specifically to attract international business, whereas in reality the Cayman Islands simply never adopted direct taxation measures that international business finds somewhat less than appealing at times.

### **The Use of Inclusive Language**

Language is very powerful. The Book of Proverbs (Chapters 12 & 18) teaches that words can play a decisive role, whether for good or evil. They can be as destructive as sword thrusts or the means of healing.

Temperate language is essential in the process we are now engaged in, if there is to be progress. Intemperate language is rarely constructive. Vilification and demonisation are well known techniques which may seem to be expedient in regard to the mobilization and shaping of domestic public opinion or some other narrow political objective when simple facts are not helpful or sufficient.

However, these methods do not contribute to international harmony and they are rarely effective in the long term, as history has ably shown.

### **The Articulation of Assumptions**

There may be much yet to be established in terms of achieving a fair playing field that is accessible to all in the international arena of tax related economic competition. However, there are things that we all share such as adherence to the rule of international law. We can choose to build upon these shared beliefs.

Articulation of our respective assumptions can also help to identify areas for discussion and consensus building. The generation of, and response to, various position papers and other public documents over the past few years has been very useful in bringing to the fore subjects which require international debate and consensus building.

Some of the academic and in some cases pragmatic questions that have emerged and re-emerged in regard to these subjects include:

- What assumptions define certain forms of tax related economic competition as “harmful” and other forms acceptable? The perception of some on the outside of the current processes is that the focus and scope of recent initiatives indicates that these initiatives are merely a means for large rich countries to preserve and project forward the existing global economic order at the expense of smaller less developed countries.
- What are the legitimate limits of state sovereignty in regard to international taxation in general and the extra-territorial application of fiscal regimes in particular? The perception of some on the outside of the process has been that the limits proposed by the large developed states are just another case of might attempting to define right.
- What is “fair” in terms of allowing for economic diversification in smaller states? The perception of some on the outside of the process has been that no economic diversification is to be tolerated if it potentially competes with the interests of large developed states.
- To what extent is it appropriate for the rich and developed nations to restrict the movement of investment capital to small less developed states which offer investors the potential for diversification and a higher after tax rate of return on their investments? This question is often coupled with the parallel question regarding investment incentives offered by large states that have distorting effects on international investment activities.
- To what extent are historical events and current aspirations for the future relevant? The perception of some on the outside of the process appears to be that the historical removal of people and wealth from what are now

the developing regions for the benefit of the now rich and developed regions is relevant. The question that is asked is that if wealth started out, for example in the West Indies and went to Europe, when did it stop being wealth to which the now developing nations have a claim? Similarly, when does money leaving the now developed world cease to be money on which the developed world has an ongoing claim?

- To what extent is there a relevant question of proportionality in regard to international taxation? The extra-territorial application of fiscal regimes, for example through Controlled Foreign Companies regimes, results in the potential for arguably disproportionate taxation of non-monetary inputs, that is the taxation of inputs arising from the natural and human resources of another jurisdiction. Some may ask whether an international convention could be developed which would define the scope in respect of which the jurisdiction which was the most recent source of the money, only has a tax claim in respect of a portion of any income or gain in wealth proportionate to that jurisdiction's relative contribution to the creation of new wealth.

It is highly unlikely that consensus in respect of the answers to even these few semi-rhetorical questions can be achieved during the course of this conference. However, if we can openly identify what the questions and assumptions are, then we will be able to establish working groups or other forms of communication to enable us to build consensus and work towards an acceptable outcome.

### **Developing a set of guiding principles to take the process forward**

Achieving transparency in regard to the principles which are to be followed in the process, as well as in the mechanisms of the process itself, will go a long way to encouraging dialogue and achieving a workable outcome. The Cayman Islands would like to suggest by way of illustration, that the guiding principles that participants in the dialogue may wish to consider and adopt could include the following concepts in one form or another:

- Acceptance of the general principles of public international law including the defined sovereign rights of states,
- Acceptance of the general presumption against the validity of the extra-territorial application of laws of individual states,
- Acceptance of the legitimate expectation of consistency and equitable treatment,
- Acceptance of the right of individual jurisdictions to negotiate the terms of international tax arrangements and to determine whether that particular state wishes to enter into bilateral or multilateral arrangements, or similarly whether any arrangements should take the form of double taxation agreements or otherwise,

- Acceptance of the general proposition in favour of the right to privacy of the individual in respect of personal information including financial information,
- Acceptance of the right of all individuals to due process before the law,
- Acknowledgement of a general presumption in favour of following the format of existing international conventions and practice to the extent applicable and practical, except where there is a clear international consensus for change to a specific new format which is consistent with the other principles listed above.

It may be that for one reason or another, one or more of the concepts set out here are not acceptable to one or more participants in the dialogue. If so, even that information would assist in the dialogue. Similarly, there are likely to be suggestions for modifications to those general principles listed here, or additions which one or more jurisdiction might wish. The Cayman Islands welcomes any suggestions in this regard and would be glad to participate in any forum in which these principles can be further developed and articulated.

## **Conclusions**

Having begun with one agrarian analogy in regard to farmyards and geese, I would like to end with another, this time having to do with water.

On our planet water in its liquid form often defines our borders. It moves internationally in rivers and oceans. It leaves its liquid form in evaporation, travels the winds across international boundaries in clouds, returns to liquid form in condensation and falls as rain, whether close to where it originated or in distant lands. Having fallen as rain, it again begins the life-giving process of flow, nourishment and evaporation. In all of these forms and with all this movement it is what gives us life. If we stop its movement it becomes stagnant and fetid. If we conserve its natural cycle and use it wisely, it will sustain us all.

Perhaps in regard to the international economic flows that are the focus of the discussions here, there are analogies that will give us perspective. The potential wealth of this planet is a resource we all share. We would hopefully all agree that no upstream nation would be justified in unreasonably depriving its downstream neighbours of life sustaining water by virtue of the geographic or historical accident that put them upstream.

Similarly, no nation should pollute waters that move internationally making them unhealthy or unproductive for their neighbours. Further, there are internationally accepted limits to which a nation may go in causing water to deviate as it flows internationally. Finally, conservation is to be applauded in all jurisdictions.

The approach of the Cayman Islands is to participate fully and constructively in the international process of establishing new international law and norms in regard to tax related economic competition. The Cayman Islands encourages all

jurisdictions to participate in this process and would be pleased to engage in dialogue with any jurisdiction in this regard. The Cayman Islands commitment to the OECD is part of our involvement in the process. The terms of our commitment to the OECD is a matter of public record and we would be happy to share the full text of this commitment with any of the delegations gathered here.

I would once again like to thank those involved in the planning and organization of this conference for allowing me this opportunity to speak and to extend an invitation to dialogue to any jurisdiction not currently engaged in the process.