

# Hopeless yet determined

By Derek Sambrook, FIB(SA), TEP,  
Managing Director, Trust Services, S.A.,  
Panama



**I**n last month's column (**Bat wings and BEPS**) I wrote about the eventual appearance of Basic Erosion and Profit Shifting (BEPS)-related blacklists. This will happen because the quixotic view of the Organisation for Economic Co-operation and Development that countries will fall into line is just that: foolishly impractical.

To say blacklists and politics in the same breath, particularly when it comes to the Basic Erosion and Profit Shifting Initiative, is as natural as pouring cream on hot apple pie. They are created primarily with self-interest in mind and not to grease the wheels of an increasingly global economy despite what claims are made; such considerations are secondary. Like the cliché goes at election time, all politics are local, and so are the principal motives behind blacklists. In the process the sovereignty of countries can be trampled on by more powerful nations.

The only thing we can say about blacklists is that they are not the threat to life and limb they once were. Historically, the word originated with a list made by Charles II of 58 judges, including court officers, who sentenced his father to death in 1649. When Charles II was restored to the throne in 1660 he executed 13 of them, sentenced 25 to life imprisonment while others escaped. No one today on a blacklist is in danger of losing his life, however, over tax evasion, except perhaps in China.

Since then its meaning has moved with the times. The word blacklist, however, is no longer used by the police of Scotland Yard because they say that its use is "inappropriate" over fears that it is racist. They now use a "Red list", apparently because it is "less sensitive". Much more so, no doubt, than it would have been in Senator McCarthy's day when Hollywood became the new Salem and the search for communists rather than covens was the priority.

Blacklists are even popular in Latin America in relation to tax issues, with Argentina and Venezuela listing a very large number of countries; far more than Brazil and Mexico. That said, we need to appreciate that blacklists have become an essential tool in the OECD's arsenal, and sometimes this tool has been wielded like a blunt instrument to either intimidate, coerce or compel compliance. In many cases (and we have seen this) there has been room for compromise, especially in the case of powerful countries such as the United States of America. In fact, often it is America's, and not the OECD's, special brand of blacklist that is the most menacing.

Because of the primacy of the US dollar, banks across the globe, in order to transact business in dollars, need to use American correspondent banks as conduits for dealing in dollars. Any foreign banks, however, who fall foul of the US can be shut out of the system. Correspondent banks, the conduits which I described, because of the perceived risks of money laundering and tax evasion have become nervous and some have withdrawn their services. A number of offshore banking jurisdictions have been shut out of the system even if the US Treasury Department has not tagged a jurisdiction as high risk and there is no evidence of high levels of illicit activity. Even the FATF, known to some as the Financial Contruction Task Force, has criticised such moves, quaintly referred to as de-risking by banks, saying that it is overkill in many instances.

In a bid to discourage excessive de-risking by banks, the FATF has issued new guidelines warning regulators to treat financial institutions' compliance failures in an "appropriate and proportionate" way and not come down on them like a ton of bricks with huge fines. The FATF emphasises that implementation of anti-money laundering/counter-terrorist financing measures by financial institutions "should be aimed at managing (not avoiding) risks". The FATF says that it is especially concerned with the withdrawal of correspondent banking and remittance services from some jurisdictions, and the "wholesale cutting loose of entire countries and classes of customer".

National blacklists (distinct from those of the European Union, the OECD and the FATF) can be discriminatory and, importantly, in a large number of cases, perhaps even the majority, are not compiled with any objective or consistently-applied criteria. So from the very start these blacklists

can be constructed on very weak foundations. And the problem is that blacklists may simply, arbitrarily, be copied between jurisdictions without separate judgement or debate.

We saw politics at work when the European Union announced its own blacklist, putting the OECD's blacklist to one side and deciding itself what conditions apply if a jurisdiction is to be classified as non-co-operative. Predictably, the OECD took umbrage at this and suggested that the EU list should be ignored. The OECD, in other words, blacklisted the EU's blacklist.

What a farce. In the case of the EU blacklist which derived its data from member states' lists, a proper analysis didn't take place. The director of the OECD Centre for Tax Policy and Administration said that the list featured jurisdictions already appearing on at least 10 EU countries' national blacklists and he described the result as being "very unfortunate". He was not alone in thinking so because many of the perceived most un-co-operative tax jurisdictions targeted, thirty in all, went public with their protests. Liechtenstein found the EU actions "wholly inexplicable"; Hong Kong was "puzzled" saying that the listing was "unilateral and procedurally unfair"; and Guernsey said that it appeared the list had been "hurriedly" put together "...using very arbitrary criteria". Inexplicable, puzzlement, unfair and arbitrary summarises the situation well. And that's just the EU's blacklist.

Now the World Bank, not just the FATF, in two surveys at the end of last year, has stated that large global banks are restricting or terminating relationships with other financial institutions unnecessarily. This reluctance strikes at the very heart of global financial business. Avoid rather than manage; that is precisely the problem. Banks in Latin America, including Panama, the region's banking centre, have fallen victim to this policy.

So financial services for local and regional banks, including remittance providers, and embracing cheque clearing, international money transfers, and trade finance, are being affected. Gloria Grandolini, Senior Director of Finance and Markets Global practice at the World Bank Group comments: "Now that we have evidence that large banks are reducing services to correspondent banks and remittance providers, the private and public sectors need to come

together to find practical and fact-based solutions. There is a real risk that turning away customers could actually reduce transparency in the system by forcing transactions through unrelated channels". She goes on to add: "Making banking services accessible, transparent and affordable is essential to achieving the goals of promoting financial integrity and universal financial access by 2020, which means that basic and legitimate access to the formal financial system should be possible for everyone". 2020? An optimism which rival's Dorothy's in the Wizard of Oz.

By the same token some foreign financial institutions have, for their part, shied away from taking on American clients because of the reporting complications and the risks this can entail. One of those risks is the pugnacious American legal system. The US has stretched its laws far beyond its borders and this is in part because of the country's financial pre-eminence and the global status of the greenback. Its justice department claims the right to go after anyone who uses its banking system. When applying its laws it is as creative as George Lucas of Star Wars fame and will discard the one which appears most relevant for one that is more likely to get a conviction. Such tactics can make foreign service providers nervous and question the wisdom of inviting trouble to their doorsteps.

But more germane to my blacklist theme is a growing anger felt towards society's elite with disgust at the level of corruption in and outside government being the backdrop. The charity Oxfam says that soon the wealthiest 1 per cent will own more than the rest of the world's population. A psychologist in a US court case has used the term "affluenza" in describing a very rich youth's sense of irresponsibility, saying that this is due to his affluent upbringing. I'm sorry, affluent upbringing comes to mind.

The mood is as global as the countries are diverse. CRS, FATCA and BEPS are crowd pleasers for the disadvantaged and Aladdin's Cave for revenue-starved governments. F. Scott Fitzgerald once wrote of the ability "to see that things are hopeless and yet be determined to make them otherwise". That's good advice for offshore practitioners.

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