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SALUTATIONS!

SLIDE 1: BACKGROUND & CONTEXT

My presentation will explore the metamorphosis of the trade in cross-border financial services in and from The Bahamas, touch on the rules being rolled out for international tax cooperation and share some thoughts on how The Bahamas may respond to these conditions. Our traditional strength has been in the private banking/trust arena, which has undergone foundational shifts due to cross-border cooperation initiatives. The model of financial services on which our success grew is now obsolete. We must now adjust to the new realities of financial services, with fundamental shifts in how the business is best managed, in order to gain traction in a dynamic space.

SLIDE 2: PANGEA 2.0

How many of you are familiar with the concept of Pangea, the super continent?
It seems to me that with globalisation & information and communications technologies, the countries of the world are in a virtual Pangea (which I dub "Pangea 2.0"). BUT this version has the imprint or memory of the era of the nation state.

(Screen shows (1) actual Pangea 270 mill years ago; (2) the separated continents with political representation of the world today with nation states and (3) finally what I deem the reversion to a Pangea, but a virtual Pangea, the cradle-cap over the globe represents the borderless world of cyberspace.)

SLIDE 3: NEW WORLD CHALLENGES

The European University Institute, Academy of Global Governance has characterised the challenges of Pangea 2.0 thus:

"In the post-1989 period, important changes have occurred in the organisation of the world economy and of world politics more broadly. The new global (dis)order is characterised by both interdependence and mutual vulnerability among world regions and nation-states. The

intensification of linkages and connections driven by technology, trade, investment, aid, and the mobility of people and ideas is transforming states and societies around the world.

……A new multipolar international system is emerging, underscored with the eclipse of the G7/G8 of western powers, by the G20. The growing weight of countries such as China, India and Brazil points to a relative decline in the power and influence of the 'West'.

….. Demands for the supply of public goods/[services] at both the regional and international level are rising, but significant – and in some cases rising – barriers to their provision confound policymakers.

The European Union (EU) is drawn into a web of global governance as it tries to shape – and is also shaped by – international regimes, bilateral and multilateral agreements that comprise today's patterns of transnational governance."

Small economies have drawn into the same web of global governance and are also being shaped by the new international regimes etc. The big difference is that they are not playing any meaningful part in the shaping of these regimes. A situation that creates a substantial imbalance for the sustainability of these economies.

The Academy of Global Governance provides space for multi-national, multidisciplinary and multi-cultural think-tanking.

Whilst attending one of the meetings, colleagues from Latin America gave assurances that offshore financial centres in this region were vitally important to the foreign trade agenda of Latin American economies. They indicated that so long as transparent tax information exchange mechanisms were in place and abuse of the centres for illegal activities were demonstrably discouraged, these OFCs provide a very necessary service to Latin American multinationals, that use the centres to structure their global operations. Since such services are generally not available in their home countries; the service offerings of the OFCs gave Latin American multinationals a competitive edge and were considered a distinct value added to global trade in and from this region.

This was an epiphany me, as I realized that in addition to attending the OECD GF and CFATF battlegrounds, there was a need to engage directly with trade officials of other jurisdictions on trade facilitation that would INCLUDE cooperation on tax matters. The two areas of cooperation had become de-coupled, or disconnected, in the case of smaller OFCs, creating an imbalance.

The very clear positive message of my Latin American colleagues had also somehow been overshadowed by the muddied cacophony coming from the activities of the multilateral agencies, some OECD governments, NGOs, the international press and in some case, the local press.

I fear that many small OFCs became so distracted and consumed with this cacophony, that they, perhaps unwittingly contributed to the imbalance, by failing to simultaneously pursue the trade and investment dimension of international tax cooperation.

The net effect of these imbalances oftentimes was counterproductive messaging, business uncertainty, over-reaction, and general confusion.

The greatest travesty remains that the companion discussion on cross-border activities between States in the context of trade and investment opportunities; and how this might best be facilitated between the States concerned (especially in a rapidly changing global landscape), has not been happening.

SLIDE 4: ECONOMIC & POLITICAL BLOCS

I want to highlight the integrated relationship of the main players behind the initiatives.
The top matrix contains the membership of the OECD.
It should be noted that Colombia became an OECD member in 2018 - though it is not reflected here.
The members highlighted in red are the members of the EU (22 of 29, but EU is also a member in its own right).

The asterisk indicates members of FATF (includes EU as a separate member). Israel became an FATF member in 2019.

The second matrix represents the members of G-20. - includes G7, BRICs and 11 OECD members.
I have also identified the members of FSB, which includes Switzerland, HK and Singapore. (EU also a member of FSB)

SLIDE 5: ICEBERG ANALOGY

This is another perspective on how the blocs work as a common inter-related force and are synergistic in their pursuits.

I have used the iceberg analogy to illustrate the importance of understanding what the root causes or source are of the initiatives. I have found that it is very important to not become so preoccupied with the tip of the iceberg that is visible above the water line, that there is a failure to appreciate the thousand-fold mass that is nurturing it beneath the water.

Above the waterline are the bodies and initiatives that The Bahamas is engaged with. Those identified in green are the ones in which The Bahamas holds direct membership. However, beneath the waterline is found the source of these bodies and their activities.

It should be noted that in elation to BCBS, IOSCO and IAIS, The Bahamas has membership through its relevant financial regulators.

SLIDE 6: CORPORATE INCOME TAX

Amid the intricacies of the web of transnational governance, all countries are being forced to adjust. One of the areas that the IMF has been promoting for countries without direct taxation systems, is to consider introducing Corporate income tax. Such advice has been given to The Bahamas and to the UAE.

In looking at adapting its business model to capitalize on the new substance requirements, The Bahamas' international business focus is shifting to attracting multinational corporations (MNCs) to establish operations here. This means that the issue of corporate income tax takes on greater significance.

Corporate income tax is normally payable in one or two ways. Either, based on residence of the person entitled to receive the profits (the residence-based system) or based on the source/territory of the income or profits (the territorial or source-based system). For many countries, under the residence-based system, a resident Company pays taxes on its worldwide profits. In contrast, a non-resident company is only taxed on profits earned in, or remitted to, the territory in the non-resident company is located.

Some countries have a pure territorial tax system, in which both resident and non-resident companies are charged <u>only</u> on profits generated in (or remitted to) those countries. It is considered to be the simplest, most business-friendly approach, and can be found, notably, in Hong Kong, Singapore and Panama.

Double taxation agreements or DTAs address the conflict that arises for an MNC, over competing taxing rights, by providing for the apportionment of taxing rights in its cross-border trade. This is achieved mainly through a system of credits and exemptions applicable to taxes paid as a non-resident in another jurisdiction.

DTAs ALSO help countries to facilitate competitive market access for their multinational corporations. Tax cooperation remains, for most countries, an important facilitator of cross-border trade and investments. The entire BEPS initiative confirms this.

Multinationals, for their part, also took advantage of the variation in tax systems around the world, to structure their global activities, including in locations that had no direct taxation system and which therefore fell outside the DTA network. This enabled them to minimise their overall tax liabilities. The OECD has acknowledged that the activities of the MNCs were largely legitimate.

Over time the larger economies grew concerned that the tax minimisation structuring by many MNCs were harmful to their respective tax bases, and by extension, their national development. They (the larger economies) put in train plans to tackle the problem. Ecommerce and the digitalisation of the economy presented a greater urgency to revise the international tax rules and close the "loopholes" that allowed MNCs to avoid and/or minimise their tax liabilities through structuring.

SLIDE 7: AEOI & BEPS

The loophole closing is being accomplished through the AEOI (including FATCA & EU initiatives) and the BEPS projects, with the aim of involving all countries irrespective of their individual tax system.

Amongst other features, to ensure that there is no backsliding, inclusive frameworks and peer review processes have become entrenched. These mechanisms allow the OECD secretariat the ability to monitor and conduct periodic assessments of the implementation of the measures, and to act or react accordingly. It also enables them to conduct on-going analysis on the data collected as part of the initiatives. Other initiatives contain similar oversight and audit style features.

The work underway on Action 1 of the BEPS framework which focusses on the tax challenges of the digitalisation of the economy, will result in further reconfiguration of the international tax landscape. This is to ensure that the inherent characteristics of the digital economy (mobility, data, virtual nature, intangible assets) do not prevent States from enforcing taxing rights on their taxpayers.

BEPS, through its fundamental re-write of international tax rules, has placed enormous pressure on smaller OFCs, vis-à-vis the worldwide operations of MNCs.

In order to attract the corporate business and other key operations of MNCs, jurisdictions must offer advantages that will ultimately ensure that the MNC can find commercial value in those locations without falling afoul of the new rules or being exposed to reputational risks.

Whilst none of the tax initiatives claim to be dictating what type of tax system or tax rate a jurisdiction should adopt; in the absence of other substantial revenue generating streams, there are few choices left for smaller OFCs to meet critical and growing public needs. One such choice is to conform to the global tax system standard, i.e. income tax. I do see 2 important benefits of corporate income tax in light of recent developments: -

1. MNCs & Tax administrations understand it;

2. Jurisdictions will be better situated to benefit from the new rules expected from BEPS 1; having regard to -

a. its emphasis on taxing rights being tied to the jurisdiction where the value has been created by an MNC and where their markets are located; and

b. the ability to participate in a broader international network in support of efforts to collect their fair share of taxes that may be due from non-resident businesses that offer digital goods and services within their markets.

Today's reality is that the tax aspect of global business is converging and being standardized.

Should The Bahamas consider introducing corporate income tax?

First, I caution placing too much value on corporate income tax by itself as a competitive draw. There are many more compelling considerations that give an OFC a competitive edge in global business. Further, global structuring for MNCs is driven more by commercial and operational considerations, rather than on tax minimisation as an overriding factor.

We can see from the March 2019 Global Financial Centres Index (GFCI) report as well that taxation as a competitive indicator is not prominent. We can see high performance amongst countries that do not have a general CIT in place e.g UAE with Dubai and Abu Dhabi, Cayman Islands and Bermuda. On the other end of the spectrum we see OFCs with direct taxation system also fall considerably in the ranking e.g. Mauritius which has residence-based direct taxation.

My second caution is that the considerations for The Bahamas in deciding whether to introduce corporate income tax go well beyond the financial services sector, so the discussion must be much broader.

I do support a thorough analysis of the issue in the context of, not only the external pressures and global interdependence, but also whether the current tax system is fit for purpose. Clearly the external activities (tax and otherwise) pose distinct economic and social risks for the country. These risks require thorough, in-depth analysis by stakeholders and academia.

If, the decision is taken that The Bahamas tax system will be changed to implement CIT then, my recommendation would be for a territorial tax system for both resident and non-resident companies.

SLIDE 8: BENEATH THE ICEBERG

We have seen that sovereign independence is waning in importance. The new paradigm for national growth is "interdependence". The most powerful nations are aligning in one bloc or another to shore up their influence where it is likely to have the greatest positive outcomes on their respective national development.

Strategic political and/or economic alliances are critical to national development. Countries that have not pursued such engagements, are inevitably dragged into one mix or another as fringe dwellers; or suffer marginalisation.

In taking note of countries that have fallen considerably in the March 2019 GFCI rankings as OFCs: (Bahamas, Mauritius) - what stood out to me was that they are small sovereign countries, relatively. A similar trend is evident in FATF rankings.

As for the UN, it is heavily influenced by the large global blocs. They take full advantage of UN mechanisms to advance their own programmes. So, in my opinion, the UN machinery is not enough to ward off the torrential pressures of globalisation on smaller sovereign nations in Pangea 2.0.

At a more granular level, it is so very important to view these various initiatives as inextricably interrelated; each engaging in activities that support the outcomes of the others. History has shown that their timing is well coordinated. Consequently, any viable response strategy must be more purposefully integrated.

The mechanisms to deliver the initiatives (i.e. the secretariats) have become perpetual, more sophisticated, coordinated and elaborate, and are generally no match for what is ostensibly weaker, disjointed, incoherent opposition. The initiatives are also converging to deliver optimum impact that benefits their members.

SLIDE 9: THE ROAD AHEAD

Panning back in our interest in attracting more MNC activity, I offer the following observations.

Despite my conviction that breathing new life into our OFC industry requires a deep-dive, multi-pronged approach, I believe our biggest immediate concern must be tackling the reputational deficit from the FATF listing. It is highly problematic, with grave consequences for the general economy.

SLIDE 10: FATF MER CONSOLIDATED RESULTS FOR IMMEDIATE OUTCOMES (as at Aug 2019)

Foreign banks, including our correspondents, are obliged to comply with their home regulators rules or face sanctions. Many of those rules require that due risk weighting must be given to countries appearing on an FATF list. Unfortunately, the harsh reality is that the assessment of

AML risk is largely now a function of Artificial Intelligence; the fact of being on the list is often all that matters. This presents issues for clients who rely on cross-border transactions. They face greater scrutiny of their activities which in turn may adversely impact smooth commercial operations.

SLIDE 11: THE COMPETITION

SLIDE 12: MARCH 2019 GFCI AREAS OF COMPETITIVENESS

Competitiveness of IFCs depends very much on ecosystems with highly sophisticated, flexible, mature smart, business environments, including active Fintech industries; highly skilled workforce with range and diversity; good connectivity & airlift, good reliable infrastructure (especially ICT), political certainty, relatively safe and secure environments, a coherent, user-friendly regulatory framework; and good reputation (or demonstrated resilience in the face of allegations of impropriety – the comeback factor).

Trust and confidence in the information network privacy and security frameworks of jurisdictions are also important factors.

I am very optimistic that The Bahamas can again become a major centre for international business. Being armed with a better understanding of the global dynamics at play and how they interplay though, is key.

I believe that the following attributes are in our favour, (in addition to the 3 SSS (sun, sand & sea))-

1. Location (a bridge between and among continents)

2. History as an int'l business centre

3. Freeport (logistics centre)

4. Talent (inside and outside) – may be not enough, but we are recognised as having talent.

UAE has 2 "purpose-built" financial freezones. In that region there are others on the drawing board or in play: Astana in Kazakhstan, Baku in Azerbaijan and Gujarat in India. In the western hemisphere, Freeport is best situated to establish a similar type of centre.

To realise such a revival, however, requires committed central Government leadership in the business development side of the industry to: -

1. tackle challenges in a holistic way and from the perspective of global interdependence in trade and investments - e.g. moving Bahamas from just a specialist centre to an international one;

2. ensure a proper alignment of business development, promotion and regulation of financial services within a coherent, collaborative, simplified, business-friendly, model;

3. maintain strong adequately resourced technical secretariats within central government to support business development and regulation (e.g. analysts, project managers, risk professionals, asset & wealth management specialists, tax specialists, legal experts, financial crimes experts, data specialists, innovation experts, techies, etc.)

4. involve UB more in research and analysis of trends (domestic, regional, global)

5. involve Foreign Offices more as monitors in global activities (UN, EU, etc.) and provide important intelligence on global trends back to the home country.

6. I especially encourage a re-visit of the challenges being faced through trade and investments prisms – and avoid falling into the trap of segregating them from the tax cooperation debate. To do so risks losing the proper perspective on the underlying motivations which should be mutual.

The theme of the conference is: Evolution: Substance, Transparency, Opportunity.

There are no guarantees in life. Success is best realized by those that are informed, adaptable and agile.

Opportunities in the global services industry abound, waiting to be exploited. It will require effort, but the returns can be substantial.

I encourage the use of this transition period to re-invent our model as an international business centre.

SLIDES 13 – 16: MAJOR INTERNATIONAL BUSINESS CENTRE RANKINGS (March 2019 GFCI Report)

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