

THE FUTURE OF INTERNATIONAL FINANCIAL SERVICES AND REGULATIONS



*By Archon James Smith
Delta Lambda Boulé*

Over the next several years offshore financial-services centers in the Caribbean will be under increasing pressure from international regulators, led by the OECD countries, to dramatically change the manner in which services sectors are operated. The clamping down began about a decade ago with the publication of OECD's "Harmful Tax Competition Initiative," which originally called for tax harmonization among the major European countries, most of which were faced with large public-sector deficits and growing public debt. At that time wealthy tax evaders were the principal targets; however, many of them held accounts outside of Europe in the fifty or so offshore financial centers around the world, including some in the Caribbean. The need for more tax revenue, particularly by the OECD countries, has been further exacerbated by the continuing global economic crisis that has devastated public finances everywhere – huge public deficits, negative economic growth, high unemployment, falling revenues and escalating costs for bailout programs, stimulus packages and increased demand for health and social-welfare services.

It is generally thought that only wealthy individuals and large corporations are to bridge the widening gap between government revenue and expenditure, and plans are already under way to raise taxes on the wealthy. The UK proposes raising rates from 40 to 50 percent on annual

incomes exceeding \$250,000; the United States proposes rolling back the Bush-era tax cuts for the rich; and tax increases on the wealthy have already been imposed in The Netherlands, France, Italy, Belgium, Ireland and several other countries. This is happening at a time when taxpayers have lost a sizeable amount of income through decreases in real-estate values, stock prices and returns on savings and other investments. Judging from discussions at a recent G20 meeting in Pittsburgh, there is to be an all-out effort to increase banking regulations and the compensation package paid to bankers. All those initiatives are likely to affect financial services in general globally, and particularly in the Caribbean offshore sectors.

To increase the tax burden on the rich at a time when they are under financial strain is not likely to yield the desired results. In the past, when the tax burden has been perceived as too heavy, the rich have responded by moving as much of their savings and investments as they legally can outside their country of residence. Therefore, there could be an increase in the demand for the services in offshore jurisdictions deemed compliant with international standards for transparency.

At the same time, as the wealthy seek tax shelters for their assets, governments, particularly the OECD members, are likely to increase pressure on offshore centers to cooperate in tax matters either by coaxing or coercion. It was rumored at the G20 meeting that offshore centers that have made no effort to comply with the OECD standards may be subject to sanctions.

Sanctions and other regulatory changes proposed over the last few years and since the global recession have ranged from the simple request that each center execute a minimum of twelve bilateral tax-information exchange agreements or a similar number of double-taxation treaties to the establishment of complex regulations and costly institutions to implement the new laws. Failure to comply could result in being blacklisted at the least, or worse, subjected to draconian provisions outlined in the draft of the Stop Tax Haven Abuse Bill, cosponsored by President Obama when he was in the Senate. That bill would allow the U.S. Treasury Department to impose harsh measures against financial centers preventing enforcement of U.S. laws. The measures are similar to those in the Patriot Act and include prohibiting the use of correspondence-banking relationships in the United States and restricting the use of credit and debit cards and other instruments issued by foreign institutions.

Given the current environment, characterized by a firm belief on the part of most OECD members that the financial crisis was caused in part by inadequate regulatory oversight along with the dismantling of controls set in place to address financial crises, we can expect more stringent oversight in both onshore and offshore jurisdictions. Caribbean centers will have to play by the new rules as these financial services contribute anywhere from 15 to more

than 50 percent of the GDP in some countries; economic disaster would ensue if such an important sector were to fold. Reform proposals sponsored by the Financial Stability Forum, the OECD, the Basel Committee on Banking Supervision, the International Accounting Standards Board and the International Organization of Securities Commissions have called for increased oversight of financial institutions with respect to capital adequacy and risk management, more transparency in financial transactions and improved corporate governance. Above all, they have called for initiatives to curb tax evasion, eliminate taxation treaty abuses, and regulate the currently unregulated parts of the industry such as hedge funds.

If Caribbean offshore centers are to remain in business it is critical that they take seriously threats posed by the OECD countries, which are much more determined since the UBS case in Switzerland, the Julius Baer case in the Cayman Islands and the German government's tax matter with Liechtenstein. To the extent that the developed countries are convinced that billions of their tax dollars are lying offshore – dollars that could be used to close their fiscal deficits – they will continue to attack and, if necessary, dismantle offshore centers.

Governments in those jurisdictions must avoid being placed on the so-called blacklist by instituting those measures that would make them compliant with international standards of transparency and effective tax-information exchange. Practitioners must develop more tax-compliant products and services, while at the same time denying use of their institutions to clients who may be breaking the laws of their home countries. Upon achieving compliance, every effort should be made to become active participants in the decision-making bodies introducing the new rules.

It should be remembered that in spite of our efforts to adopt reforms, we can expect regulations will continue to become more intrusive, more frequently applied and, above all, more targeted against offshore financial-services centers.

Delta Lambda Archon James Smith, the former minister of finance and Central Bank governor of The Bahamas and chairman of Colina Financial Advisers, delivered this address in October at the Caribbean Economic Conference.

LOST IN THE ARCHIVES

**ARCHIVED IN CRUMBLING PARCHMENTS
OF REFINED IDEALS,
LOST IN THE RECEDING MISTS THAT
ONCE CLOAKED POWER IN MYSTERY,
TIMELESS IDEAS LANGUISH FORGOTTEN,
SAVE THE FADING MEMORIES
OF A FEW FADING GREEKS.**

**REMEMBER DISCRETION?
ONCE A HALLMARK
OF DISCRIMINATING MEN
BEFORE TELL-ALLS AND TELEVISION
REPLACED REAL LIFE WITH REALITY SHOWS.
THERE WAS A TIME WHEN STRANGERS
COULD BE CALLED TO THE TEST.
NOW THE SENATE BABBLES LIKE THE HOI POLLOI
AND THE SILENCE OF THE SPHINX
MAY JUST TOKEN HER DESPAIR.
HOW WOULD WE KNOW IF THE DIN
HAD DEAFENED OUR SENSE TO HER COUNSEL?**

**THE WISE MAN, THEY SAY, NEVER TELLS
ALL HE KNOWS. THE FOOL TELLS ALL
AND KNOWS NOTHING.
I ONLY KNOW THAT FOR ALL THE TALK
INFLATION DEVALUES THE WORD'S WORTH TOO
AND ONLY AN EAR'S DIFFERENCE STANDS
BETWEEN IMPORTANT AND IMPOTENT.**

KHEPHRA BURNS

GEORGE QUICK: ON THE CUTTING EDGE IN PUBLIC FINANCE



Archon George K. Quick

*By Archon Wendell M. Davis
Grapter, Alpha Tau Boulé*

Successfully managing public finances during the worst economic recession since the Great Depression demands a steady hand on the tiller, especially for local governments that are responsible for constructing major public projects in a fluid and uncertain banking and financial environment. For Durham County, North Carolina, Archon George K. Quick of Alpha Tau Boulé is such a steward. As the chief financial officer for county government, he has had his financial acumen tested time and again, and time and again he has creatively maneuvered in a challenging financial arena to save Durham's taxpayers real money.

Lehman Brothers vanished, Merrill Lynch was purchased by the Bank of America, and AIG was on the brink of collapse as Archon Quick was in the throes of locating institutional investors to purchase more than \$250 million of public debt in order to construct schools, libraries, a courthouse and a human-services structure. In a conventional public finance environment, simple general obligation (GO) bonds or certificates of participation (COPs) are the preferred instruments of choice. However, these instruments for construction financing typically require that the total project debt is issued up front, with repayment of the debt beginning immediately. Because of the considerable uncertainty in the banking and finance arena, securing financing for these projects did not favor the traditional methods, although COPs were used.

Amid this grave uncertainty, Archon Quick developed a strategy using short-term variable-rate debt, and he subsequently reduced the overall interest rate to less than 2 percent for the human-services structure (\$117 million)


and less than 1.25 percent for the courthouse (\$124 million). The two projects combined represented the lion's share of the debt issue. The financing plan for the courthouse incorporated variable-rate short-term debt, with the flexibility of drawing down the funds as needed. Durham's courthouse project will be the first in North Carolina to use this financing method. Each project's original interest rate projection was between 4.5 and 5 percent, and Archon Quick's skillful negotiation resulted in a savings of five cents on the tax rate. The result was that Durham residents enjoyed more than \$15 million in tax savings.

Notwithstanding Archon Quick's most recent cutting-edge financing strategy, he is no stranger to pinching a penny on behalf of Durham's residents. Prior to his financing maneuvers during the recent banking meltdown, back in 2004 he also managed to save county residents \$5 million by entering into a municipal swap arrangement. The swap transaction was executed by Rice Financial, a full-service municipal investment-banking firm that specializes in the development and implementation of bond transactions.

The swap instrument is based on the relationship between the tax-exempt rate (SIFMA) and the taxable rate (LIBOR). Coincidentally, the president and CEO of Rice Financial is Archon J. Donald Rice of Zeta Boulé, New York City.

Staying on the cutting edge in the public-finance arena does not come without challenges and often comes with anxiety. Archon Quick, in concert with Archon Kenneth W. Lewis of Alpha Tau – the legal counsel on the transaction – and Archon Rice, successfully worked with the state treasurer and the Council of State to execute the first municipal-swap transaction in North Carolina. At present the Durham County swap is the only swap in North Carolina that has not experienced a period of dissavings, in spite of the current economic downturn. In fact, the Durham swap is generating in excess of \$2 million for Durham County residents in the current fiscal year. As a result of Archon Quick's leadership, Standard & Poor's and Moody's have consistently given the county a triple-A bond rating. Furthermore, Durham County is one of only forty-four counties in the nation that enjoy this distinction.

Although he has been the county CFO for the past eight years, Archon Quick's expertise is a result of his many years of experience in the banking industry. He is the former president and CEO of Mutual Community Savings Bank, and he worked for First Union in commercial lending in Charlotte and Raleigh. He is a firm believer in going the extra step and is not afraid to ask the difficult questions when confronting resistance about employing cutting-edge strategies. Financially, his persistence has proved good for all Durham residents.

A graduate of South Carolina State University with a degree in business administration and an M.B.A. from Atlanta University, he is married to Archousa Gloria Grainger Quick. They have two children: a daughter, Erica, a third-year resident in obstetrics and gynecology at Pitt Memorial Hospital, and a son, Jeffrey, a real-estate broker. 



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