



City Research Online

City St George's, University of London

Citation: Palan, R. (2015). The Second British Empire: The British Empire and the re-emergence of global finance. In: Halperin, S. & Palan, R. (Eds.), *Legacies of Empire Imperial Roots of the Contemporary Global Order*. (pp. 40-68). Cambridge, UK: Cambridge University Press. ISBN 1107521610

This is the accepted version of the paper.

This version of the publication may differ from the final published version. To cite this item please consult the publisher's version.

Permanent repository link: <https://city-ref-test.eprints-hosting.org/id/eprint/12698/>

Copyright and Reuse: Copyright and Moral Rights remain with the author(s) and/or copyright holders. Copies of full items can be used for personal research or study, educational, or not-for-profit purposes without prior permission or charge, unless otherwise indicated, provided that the authors, title and full bibliographic details are credited, a hyperlink and/or URL is given for the original metadata page and the content is not changed in any way. For full details of reuse please refer to [City Research Online policy](#).

**The Second British Empire:
The British Empire and the re-emergence of global finance**

Ronen Palan

The British Empire was a remarkable empire for many good reasons. First, it belonged to that very rare club of empires, which included as far as I can tell only two (the Spanish ‘empire’) in which the sun never sets. Indeed, at its peak, the British Empire was the largest formal empire the world had ever known. True to size, the British empire extended its power and influence in the 19th century over very large tract of lands mostly in Latin and Central America which was formally sovereign but colloquially known as the ‘informal empire’. Second, considering its size and wealth, the rapid and generally speaking orderly collapse of the British Empire after WWII was even more remarkable. By the 1980s, the largest empire the world has ever seen shrank down to contain very few remnants and debris, including the United Kingdom, three adjacent Crown territories, Jersey, Guernsey and the Island of Man, and fourteen dependent territories, since 2002 called ‘overseas territories’ which include some small Caribbean islands, the Malvinas/Falkland Islands, Gibraltar. Collectively these overseas territories encompass a population of approximately 260,000 people and a land area of 1.7 million square kilometer, the vast majority of which constitutes the British Antarctic Territory.

A third remarkable fact about the British Empire is that while it disappeared completely from most contemporary maps of the world, it remains very much alive in one crucial such map, the map of contemporary international finance. Indeed, the contemporary map of the international financial markets is configured principally around two poles. One pole has a distinct British Imperial flavor. It consists, first and foremost, of the City of London and includes, in addition, the British Crown dependencies of Jersey, Guernsey and the Isle of Man, as well as British Overseas Territories of which the most significant are the Cayman Islands, Bermuda, British Virgin Islands, Turks and

Caicos and Gibraltar, and recently independent British colonies such as Hong Kong, Singapore, the Bahamas, Cyprus, Bahrain and Dubai.¹ This British imperial pole accounted for 39.9% of all outstanding international loans and 37.3% of all outstanding international deposits by March 2009 (see table 2). The other pole consists of a string of mid-size European states known uniquely for their welfare provisions as well as for serving as tax havens. This pole includes the Benelux countries, Belgium, Netherlands and Luxembourg, Ireland, Switzerland, and Austria. This pole accounted for 17.3% of all outstanding international loans by March 2009 and 19.4% of all outstanding international deposits by March 2009.² Combined, the two poles account for approximately 57% of all international banking assets and liabilities by March 2009. The U.S., in contrast, during the same period accounted for 12.4% and 12.9% of all outstanding international loans and deposits respectively, and Japan for 4.5% and 3.8%.³

The unusual geo-political configuration of the international financial market has so far attracted little attention for reasons that are difficult to fathom.⁴ This is despite the fact that Cayman

¹ This pole includes in addition Bermuda, which is the largest captive insurance centre in the world, but contains a relatively small banking center, and the more numerous but less significant in terms of impact former British colonies in the Pacific. For discussion of Bermuda's financial center see Crombie, 2008. Pacific offshore centers and their relationship to the UK see Sharman and Mistry 2008.

² A Survey the eleven best known and most authoritative lists of tax havens of the world found that Switzerland is considered as a tax haven by nine of them, Luxembourg and Ireland by eight, the Netherlands by two and Belgium and Austria was considered a tax haven until it repealed its stringent bank secrecy law in 2001 under enormous pressure from the European Union. Nevertheless, Austria is included in this list because its financial center grew primarily during the years it served as a tax haven. Switzerland and Liechtenstein share a custom union as well as strong political links. Observers tend to treat the two countries as a linked financial center. See Kuentzler 2007 for discussion.

³ The figures are for all international loans and deposits, e.g., which are the figures used commonly for ranking international financial centers. See discussion in section one. Aggregate figures for loans and deposits in financial centers, which include domestic and international loans and deposits yield very different picture. According to McKinsey report the leading centers in terms of aggregate bank deposits in 2008 were the emerging economies with US\$ 14.3 trillion, followed by the Eurozone with US\$ 13.1 trillion and the U.S. \$12.5 trillion and Japan US\$ 11.5 trillion. The McKinsey report does not even devote a separate entry for the UK which is classified as one among 'other mature economies'. See Roxborough et.a., 2009.

⁴ The literature on international financial centers typically considers only the UK, US, Japan, Switzerland, Germany, France and sometimes Caymans among the leading financial centers. See, for instance, See Goetz 2007 and Yeandle et. al., 2005. For an historical analysis of the emergence of the British imperial network of financial centres see author.

Islands, for instance, ranked consistently among the largest international financial centers since the Bank of International Settlements (BIS) began to produce locational statistics on international lending and deposit taking in 1982, and ever since the small islands of Jersey and Guernsey have never been too far behind. One possible explanation for the lacunae is that the BIS tends to treat British Crown Dependencies as well as British Overseas Territories as independent jurisdictions separate from the UK—which they are not, and hence underplays the British link.⁵

In this chapter I discuss the exceptional case for resurrection of this ‘Second’ British financial Empire out of the ashes of the first. I begin with a broad discussion of the development of financial centers, followed by an explanation of how the legacy of the British empire survived in modern finance.

I. Theories of International Financial Centers

⁵ The relationship between the British state and its various dependencies is complex, fluid, and appears to have evolved on the basis of tacit understandings between the two sides. Yet, none of them possess anything approaching full sovereignty. Indeed, reports in the British press suggest that the UK may have to bail out a number of these tax havens. Jersey, Guernsey and the Island of Man are Crown dependencies. They are possessions of the British Crown and, strictly speaking, are not part of the UK or the EU. Executive power in the three Channel Islands is exercised by the representatives of the British Crown, and hence primarily through the British Home Office. The relationship between the islands and the British state has evolved over time and the Islands today possess greater autonomy – although that trend may have gone into reverse during the current financial crisis. Le Hérissier 1998 describes the relationship between the British State and the Channel Islands as pragmatic, with the UK exercising prudence. In financial matters, however, the British Treasury exercises far greater control over the islands than is normally admitted. For discussion see also Mitchell and Sikka 2002; Hampton and Christensen 1999. In addition, the UK retains responsibilities for fourteen Overseas Territories, 11 of which are permanently populated and remain under British sovereignty. The territories are not constitutionally part of the UK, but the UK government maintains responsibilities towards them, and the Foreign and Commonwealth Office is the department mainly responsible for dealing with them. Among these Overseas Territories, the Cayman Island, Bermuda and British Virgin Islands have emerged as very significant OFCs, while Turks, Caicos and Gibraltar are medium-size centers and Anguilla, Montserrat, and Pitcairn Islands possess insignificant offshore financial centers. See NAO 2007 for detail. During and after the G-20 meeting in London, April 2008, the UK government has acknowledged its responsibilities for regulation these OFCs.

Over the past three decades the concept of the international finance center has been going in and out of fashion, but still remains highly contested. Predictably, conceptual debates in this area have tended to spill over into empirical arguments about the measurement and ranking of financial centers and vice versa. One popular methodology of ranking financial centers is based on the headquarters count formula. The theory is that banks and other financial institutions are likely to locate their headquarters near where the action is, and hence, headquarter location is indicative of the importance of a financial center (Gehrig 2000; Choi, Park and Tschoegl 1996). The headquarter formula was particularly popular before the Bank of International Settlements introduced locational data in the second quarter of 1982. The data first alerted observers to the importance of offshore financial centers, in particular the Caymans Islands, and has been used ever since as the principle source of data for measuring and ranking international financial centers.

Table 1 is based on BIS locational statistics as of March 2009. In addition to the unassailable position of London, the table shows that the Cayman Islands, which were in fifth position in 2006, were ranked fourth by 2009. The table also shows the importance of other tax havens such as Jersey, Guernsey and the Bahamas as international financial centers. Table 2 regroups Table 1 on a thematic basis. The exercise reveals a number of interesting trends that are obscured by the conventional method of ranking financial centers. The most obvious among them is the role played by the UK's financial center in international finance. The UK consists of the famous Square Mile, Canary Wharf, Mayfair and the Home Counties, as well as subsidiary financial centers located on the British Isles, such as Edinburgh and Manchester (Yeandle et. al., 2005). UK figures exclude British overseas territories which, according to all available reports, are still closely linked to the City of London. If we add jurisdictions that are under British control, then the British State accounts for 31% of all outstanding international loans and 29.6% of deposits by end-March 2009. With the addition of

former colonies such as Singapore, Hong Kong and the Bahamas, the share of British Imperial jurisdictions rises to 39.9% and 37.3% respectively.

Table 2 contains a significant amount of double counting. I submit, however, that it offers a more accurate and honest depiction of the character of the international financial market than Table 1. Table 2 reveals the overwhelming significance of what I call, the Second British Empire in shaping international financial activities. It also reveals, more generally, that the international financial market — the market that is supposed to be the most advanced, sophisticated and modern — exhibits a preference for small and often somewhat anachronistic polities including the British Empire and its remnants, city-states, or European dukedoms and monarchies. Existing theories provide little explanation for this. Why is that?

The modern study of international financial centers may legitimately be considered to have originated with the publication of Charles Kindleberger's seminal study, *The Formation of Financial Centers* (Kindleberger 1974). Kindleberger represents large financial centers as a variant of the Marshallian district theory. According to the theory, large financial centers like London or Amsterdam, and in the twentieth century, New York and Tokyo, develop organically around the major trading centers. In time, the agglomeration of know-how and skills presents centers with an unassailable competitive advantage. Nonetheless, in increasingly internationalized financial markets, other centers can develop if their governments are prepared to offer alternative methods of cost reduction, including liberalized regimes of regulation and taxation. Kindleberger explains, therefore, the development and the geographical spread of international financial centers in terms of a trade-off between two competing tendencies, market efficiencies and scale economies and geographical and informational and discriminatory business practices.

By the early 1980s, Y.S. Park observed the growth of new types of financial centers developing in conjunction with the traditional centers. Park identified four types of international

financial centers which he described as ‘primary centers’ such as London or New York. ‘booking centers’ such as the Bahamas or the Cayman Islands specializing as ‘registration havens’ for Euromarket transactions (Park 1982); ‘funding centers’, such as Singapore or Panama, that tend to channel Euromarket funds into regional financial centers, and ‘collection centers’ like Bahrain that are engaged primarily in channeling regional funds into the Euromarket.

A less elegant, if somewhat more popular theory suggests that OFCs are still primarily ‘booking centers’, and serve merely as conduits for transactions that are conceived and organized elsewhere.⁶ This may explain why the literature on international financial centers has opted, by and large, to ignore the OFC phenomenon, on the grounds that they represent little in terms of genuine banking or capital market activity. The view is mirrored by a considerable and growing literature on tax havens, which on the whole, has ignored their role and function in the financial system.

Until recently theories of international financial centers were predicated on the assumption that financial centers are in competition with each other. But from the late 1950s, the focus of banking shifted from retail to wholesale activity (Lewis and Davis 1987), and subsequently from intermediation to risk trading, the relationship between financial centers became more complex and competition was supplemented by cooperation. A study commissioned by the Bank of England has

⁶ Thirty years on, there is still a debate whether leading OFCs such as the Cayman Islands, or Jersey have developed genuine financial centers or remain largely booking centers. Many OFCs maintain that they have matured into fully functioning financial centers. Yet available data does not lend support to their claims. The Cayman Islands’ assets and liabilities are roughly one third of the UK financial center’s (Table 2). Yet while the Corporation of the City of London reports 338,000 people working directly in the Square Mile, the UK’s National Audit Office reports that only 5,400 people work in the Cayman OFC. The disparity between the two figures suggests that either Caymans is exceedingly efficient, or it is still largely a booking center with relatively little ‘real’ banking activity. See NAO 2007. The U.S. General Accounting Office’s study into the activities of the largest legal firm on the Caymans Islands, Maples and Calder, made famous by Barack Obama’s remark: ‘You’ve got a building in the Cayman Islands that supposedly houses 12,000 corporations. That’s either the biggest building or the biggest tax scam on record’(Obama may have given an underestimate. GAO reports that ‘the sole occupant of Uglad House is Maples and Calder, a law firm and company-services provider that serves as registered office for 18,857 entities it created as of March 2008’ Gao 2008, 2.GAO concluded that at least 96% of these were effectively of the ‘brass plate’ type of virtual entities. In the Netherlands, one building in Amsterdam serves as registered office for 18,857 entities as of March 2008. See also Lewis and Davis 1987.

demonstrated that many OFCs were oriented in their business model to serve London and New York's banking community (Dixon 2001). Similarly, a BIS study acknowledges the increasingly cooperative nature of modern international finance arguing that the large international financial centers serve nowadays as global hubs of financial activities.

None of the above offers an explanation for the geo-political character of the international financial system as shown in table 2. Aggregative measures and the use of techniques such as regression analysis or even more sophisticated statistical techniques in the economist toolkit so far provide at best a fuzzy picture. Nevertheless, the consensus appears to be that the traditional model of financial centers as agglomerations of banking and financial activities serving the needs of an economy has been supplemented by a model of financial centers serving one another. Since such behavior does not conform to an idealized notion of the efficiency and utility of financial markets, an explanation for such behavior must be sought elsewhere, in externalities such as regulatory competition or geographical location, which is where political economic theories come into the picture.

Alternative theory for the rise of the British pole in the international financial markets is based on different interpretation of the techniques of construction of geo-political alliances which stresses not universal economic logic, but rather parochial technique of institutional constructions that are often driven by opportunistic cost/benefit analysis. According to this perspective, actors encounter the world largely as set of opportunities, penalties and rewards. They seek to take advantage of opportunities that open to them, and yet avoid penalties in doing so. A rapidly collapsing trading empire such as the British left behind a bloated financial center in the City of London that has been traditionally politically powerful. The City contains many competing financial institutions, including banks, insurance companies, accounting and legal companies, now left stranded without the geo-political umbrella that the British Empire offered them. They were now

desperately searching for new business opportunities, and when one of those opportunities was discovered –almost by mistake in 1957 with the emergence of the Euromarkets – then like a pack of hyenas, they all poured into the new markets. They soon learned that as British law was applicable in other remnants and debris of the empire, in the Caribbean and the pacific islands, they could introduce Euromarke operations in these localized communities. City financiers developed these remnants into a second British empire not because of a sense of patriotism or even having some grand strategic perspective. Rather, they develop these colonies as financial-colonial outposts for two related reasons: first, while the City of London was largely unregulated, it was still taxed, and heavily so. Crown and overseas territories offered great opportunities for avoiding British tax while taking advantage of the British lack of regulation (known euphemistically as ‘self-regulation’). Second, as befitting financial actors that have evolved in an empire where the sun never sets, the remnants of the former empires in the Caribbean, Asia and the Pacific, offered logistical advantages in terms of sharing time zones with other crucial trading centers in the U.S. and Asia. Thus, the City of London could become through the British colonial outposts, a 24 hours integrated financial center present everywhere in the world.

II. The Rise of the Euromarket

These opportunistic, sets of considerations are borne out by the history of the modern international financial system. It appears that the significant spark, or the historical institutional disturbance, that began the process of differentiation among financial centers took place in the late 1950s in London in what Philip Cogan described as ‘probably the single most important development in the international financial markets since the Second World War’, namely, the Euromarket (Cogan 2002, 102).

Despite its importance, a great deal of confusion surrounds the Euromarket, or as it used to be called, the Euro-dollar market. Some very distinguished economists believe that the Euromarket is any wholesale financial market, or an inter-bank market, trading in non-resident denominated currencies and assets. According to this view, the Euromarket evolved as a system trading in US dollars in European markets and took off on the European continent in the mid 1950s (Schenk 1998; Bryant 1983). In time, the Euromarket has come to denote any market trading in non-resident 'hard' currencies, such as the British Sterling, the Yen, the Swiss Franc, the Deutsche Mark and the euro.

There is a different theory, however, suggesting that the Euromarket is a very specific type of market that emerged in late 1957 in London, ironically, for reasons that are directly linked to the collapsing empire (Burn 2005). Faced with mounting speculation against the pound after the Suez Canal crisis, the British government imposed strict restrictions on the use of sterling in trade credits with non-residents. But many City banks, primarily commercial banks, which evolved for more than a century as specialists in international lending particularly to British Imperial outposts and the so-called British informal empire in Latin America, saw their core business disappear overnight. They responded by using US dollars in their international dealings arguing to a receptive Bank of England (whose deputy, John Bolton, was a banker who headed one of the successful commercial banks specializing in central American trade only few years before) that such transactions have no bearing on UK balance of payment issues. At this point, the precise policy and legal steps that gave rise to the Euromarket become somewhat vague. It appears that the Bank of England has decided without consulting the Treasury that it will not intervene in transactions between non-residents and in a foreign currency, at that time dollar, but subsequently other currencies entered the same pool. These sorts of transactions were interpreted then in the context of the English common law to imply that the Bank accounted for certain types of financial transactions between non-resident parties

undertaken in foreign currency as if they did not take place in the UK. As these transactions were taking place in London, they could not be regulated by any other regulatory authority and ended therefore in a regulatory vacuum, which is called the Euromarket, or the offshore financial market (Burn 2005; Altman 1969; Hanzawa 1991).

The Euromarket was therefore an opportunistic development that emerged to sort out a specific problem that City banks were facing. Because it was not a planned policy outcome, it remained small and practically unknown for about three or four years. By the early 1960s, however, US banks, hemmed in by series of New Deal financial legislations, discovered the opportunities that London offered them to escape their own financial regulations, and began to set up branches in London specializing in Euromarket operations. It soon became clear that the market could be employed not only to circumvent an Act of the Bank of England in 1956, but also, crucially, to circumvent the very strict capital control regulations that were imposed under the Bretton Woods regime. In addition, American banks flocked to the market where they could avoid Regulation Q that was introduced in the 1930s. Regulation Q placed an interest rate ceiling on time deposits in U.S. banks.⁷ It kept bank interest rates on time deposits very low, a situation that met with little objection from the banks for a long time, but as the world economy began to flourish in the late 1950s, American banks found themselves at a disadvantage.

By the early 1960s, the flow of money to the Euromarket became a veritable flood. Then crucially, in 1963 the Kennedy administration proposed a tax that achieved exactly the opposite of what it intended. It introduced the Interest Equalization Tax, a 15% tax on interest received from investments in foreign bonds, in order to make investment in such bonds unattractive to U.S.

⁷ Regulation Q prohibits member banks from paying interest on demand deposits. See Electronic Code of Federal Regulations (e-CFR). The National Recovery Administration, which was set up under the New Deal, sought to fix prices in industry in order to eliminate “ruinous” competition, and Regulation Q attempted to do the same thing in the banking sector.

investors. The tax was supposed to stem the flow of capital out of the United States. In practice, American corporations refused to repatriate capital, to avoid paying the interest equalization tax, and in the process fueled the growth of the Euromarket.

III. The Euromarket and the Channel Islands

London was able to reduce one crucial fixed cost dimension of trading in incorporeal assets, namely, regulation. London seized, in effect, the initiative in the development of the international financial markets, to which other states had to respond. That the initiative lay with London, or rather with London-based actors, can be seen very clearly in subsequent developments. Contrary to popular perception, the US Treasury initially objected to the rise of the unregulated market in London and put forward proposals for a new regulatory framework (Kapstein 1994). Failing that, and with the active encouragement of the New York banking community, particularly Citibank and Chase, the US Treasury came to the conclusion that rather than fight the onset of an unregulated market, the US stood to gain by encouraging a domestic variant of the offshore market. A swift volte-face took place culminating in the establishment on 3rd of December 1981 of the New York offshore market, the New York International Banking Facilities (IBF), which is a more restricted type of London offshore. The IBFs were set up as a defensive measure representing ‘an attempt by U.S. government regulators to ‘internalize’ the Euromarkets into the U.S. banking system. Japan then followed suit in 1986 by establishing its own IBF, the Japanese Offshore Market (JOM) (Moffett and Stonehill 1989; Hanzawa 1991).

London’s however, was by then already in the lead. The success of London was built around two pillars of strength: an historical concentration of professional and technical know-how in international business combined with the rise of the Euromarket in the early 1960s, propelled the

City of London into the position of the world's premier international financial centre. London had, however, some disadvantages. First and foremost among them was that while the market was largely unregulated or 'offshore', banks were subject to corporate taxation. Furthermore, British banks and corporations, as opposed to foreign banks, were paradoxically at a disadvantage vis-à-vis foreign institutions because they could not pose as non-residents for taxation purposes, whereas American banks could take advantage of transfer pricing to ensure low taxation. Third, as the market grew in size, the cost of conducting business in London became an issue as well.

For all or any of these reasons, and since London had in effect emerged as a large and flourishing OFC, or a conduit through which bankers, increasingly of American, Japanese and German origins, have learned to register financial transaction to avoid various regulations, the idea of using other, closely related jurisdictions sharing British law and regulations but with the added advantage of low taxation seemed logical. At this juncture it appears that the expansion of the Euromarket throughout the globe followed four time-honored institutional precepts:

- A. The process was driven from the centre, by London and New York's financial, legal and accounting firms searching for alternative low-tax locations to 'book' transactions in order to obtain tax savings;
- B. In their quest for alternative locations, these financial operators, appear to have followed a clear geographical path, beginning from those islands nearest to the UK mainland, namely, the Channel Islands, soon followed by the British-held Caribbean jurisdictions, then Asia and lastly British-held Pacific atolls. The process took about ten years to complete.
- C. In expanding operations internationally, London institutions appear to have sought the path of least resistance, selecting British imperial polities that broadly resembled the City

of London's unique political structure. As a result, the Euromarket never developed in the larger British imperial possessions or dominions such as Canada, India, or Australia, but in typically quasi-feudal polities such as the Channel Islands, and other small British dependencies. This resulted in a network of British—dominated financial centers with close links between them.

IV. Institutional Affinities and the Development of the Euromarket

The remaining bits of empire offered other advantages, including institutional affinities. The City of London is a unique political entity, described invariably as quasi-feudal or quasi-democratic. It is noteworthy that the City shares many attributes with other remnants of the British Empire, such as the Channel Islands, the Caribbean British possessions, Hong Kong (until 1997) or British Pacific Islands. The City of London, which used to be called, the Corporation of London, describes itself rather modestly as the oldest local authority in England. It plays the role of a local authority within the Square Mile, and is responsible for services such as housing, refuse collection, education, social services, environmental and health but much, much more. The Corporation of London runs, in fact, its own police force, but also two of London's best loved parks, Epping Forest and Hampstead Heath, which are not within the square mile. Most importantly, the voting structure in the City is dominated by what is called non-residential business vote.⁸ The City of London Corporation was not reformed, like other UK municipalities, by the Municipal Corporation Act of 1835. As a result, eligible voters in the borough are either residents who are 18 years old and citizens of the UK, the

⁸ The City of London Corporation was not reformed by the Municipal Corporation Act of 1835. Eligible voters are either residents, 18 years old and citizens of the UK, the Commonwealth or the EU, or sole traders or partners in an unlimited partnership or appointees of qualifying bodies. Each body or organization, whether incorporated or unincorporated, whose premises are within the City may appoint a number of voters based on the number of workers it employs. In fact, qualified voters can vote twice, while residents of the City can only vote once.

Commonwealth or the EU, or - and this is where the difference with other boroughs comes to light - are sole traders or partners in an unlimited partnership or appointees of qualifying bodies. Each body or organization, whether incorporated or unincorporated, with premises in the City may appoint a number of voters based on the number of workers it employs. As a result qualified voters can vote twice, while residents of the City can only vote once. The City has greatly increased the business franchises in 2002 – not sure what this means. Consequently, for all intents and purposes, the City of London is run more like a guild in the control of the financial and business interests resident in the Square Mile.

The City elects a Lord Mayor, who plays a significant diplomatic role negotiating both with the British State and overseas heads of state, and is supported by a committee of Alderman, nearly all of whom are representatives of financial, legal and accounting firms located in the City. The Lord Mayor, the committee of Alderman and the entire political structure of the City unashamedly is the representative of corporate financial interests.

The spillover from London to other centers began in early 1960s and followed what appears to be a quest for institutional affinities in other centres. Hence the spillover began most naturally with British jurisdictions adjacent to the UK, sharing British law, and whose political and institutional organizations shared many of the unique political attributes of the City. The Island of Jersey was the first to develop as a Euromarket outpost, and is a typical case in point.

Jersey seemed an obvious starting point for the expansion of City Euromarket operations: it shared the UK common law, was protected under the UK's security umbrella, and used the British pound. Labor and real estate costs were much lower than London at the time, although the situation has changed dramatically since not least because of the success of Jersey as an offshore financial center. Jersey was also known since the 1930s as a tax haven for UK tax exiles. Mark Hampton demonstrates very clearly that 'the emerging offshore centre [in Jersey] was driven by international

financial capital, merchant banks, which set up in the island to service certain wealthy customers' (Hampton 2007, 4). London banks took the lead and began to set up subsidiaries in Jersey, Guernsey, and the Isle of Man in the early 1960s. By 1964, the three big American banks - Citibank, Chase Manhattan and the Bank of America - arrived on the scene as well (Toniolo 2005, 454).

The Channel Islands proved attractive, in addition, not least due to their unique semi-feudal type of politics, more akin to the politics of the Corporation of London than to modern democracy. Austin Mitchell and Prem Sikka described Jersey as a 'town government writ large, with all its intimacies and inefficiencies' (Mitchell and Sikka, 1999, 40). The island became a possession of the British Crown in 1204, the last of the French possessions retained by the British Crown. Executive authority resides with the Lieutenant-Governor, who acts as the Crown's representative on the island. In reality, the Lieutenant-governor consults with the States of Jersey and both executive and legislative powers lie primarily with the States of Jersey. In that sense, it is largely autonomous.

V. Second and Third Wave Expansion of the Euromarket

We also know from various reports that faced with the high infrastructural costs of a London base, some of the smaller American and Canadian banks 'realized that the British Caribbean jurisdictions offered cheaper and equally attractive regulatory environment – free of exchange controls, reserve requirements and interest rate ceilings, and in the same time zone as New York' (Hudson 1998, 541). The Caribbean booking centres had the further advantage of sharing New York's time zone and they were not subject, crucially, to the Act of 1948 – what Act?. They were developed by the North American banking community to serve as conduits for Euromarket transactions.

The OFCs in question were British-held territories. The early spillover into territories such as the Bahamas and the Cayman, reckons Sylla, 'was, like the London Euromarket, not motivated by

tax advantages, but because it was cheaper to set up branches in these locations' (Sylla 2002, 53). Bhattacharya also makes an argument based on costs. In 1980 'the average annual wages for a bookkeeper in the Bahamas are a meager \$ 6,000, and the annual fee for an offshore banking (Category "B") license in the Cayman Islands is only \$6,098.7 The total cost of operating a branch in these islands is much lower than in the primary centers of Eurocurrency operation (Bhattacharya 1980, 37.)

Three Caribbean centers, the Caymans, the Bahamas and Bermuda benefited in particular from the rapid expansion of the Euromarket, while Bermuda chose a somewhat separate developmental path as the world's premier captive insurance centre. By the late 1970s, the Caribbean basin accounted for one fifth of the gross size of total Eurocurrency operations. By the 1980s, US bank branches in the Caribbean comprised more than one-third of the assets of all US Foreign bank branches in the American region. Yet both Panama and the Bahamas have declined since, while the Cayman Islands forged ahead. The reasons are very obviously the British link (Bhattacharya 1980, 37). The Bahamas opted for independence and was tainted by political scandal and began its decline.

The theory of social and political affinities may help explain the development of the Asians OFCs with strong British links as well. As the widening Indo-China war in mid 1960's increased foreign exchange expenditure in the region, a tightening of credit occurred in 1967 and 1968, contributing to rising interest rates in the Eurodollar market. Tapping existing dollar balances in the Asia-Pacific region became attractive for many banks. The Bank of America was the first to hit on the idea of setting up a specialized facility for Eurodollar operations in East Asia.

Initially the Bank of America approached the one jurisdiction that shared many of the characteristics described above, namely, Hong Kong. The Hong Kong colonial government, however, was not particularly forthcoming. It had placed restrictions on the financial sector as far back as the early 1950s.

Having failed to persuade the Hong Kong government, the Bank of America turned to the next available jurisdiction that shares many of the above characteristics. This time an ex British colony, Singapore, proved far more accommodating. Singapore responded by setting up in 1968 facilities, called the Asian Currency Unit (ACU), that provided incentives for branches of international banks to relocate to Singapore. Singapore licensed the first branch of the Bank of America to set up a special international department to handle transactions for non-residents. As with all other Euromarket operations, the ACU created a separate set of accounts in which all transactions with non-residents are recorded. Although the ACU was not subject to exchange controls, banks were required to submit to the exchange control authority detailed monthly reports of their transactions. In that sense, the ACU is a more restricted type of an offshore financial centre.

The moratorium on the establishment of new banks in Hong Kong was lifted in 1978 and proved a great success. In February 1982, the interest withholding tax on foreign currency deposits was abolished. In 1989, all forms of tax on interest were abolished. With the government becoming more proactive, by 1995-96, Hong Kong had soon become the second largest OFC in the Asia-Pacific region, and between the sixth and seventh largest IFC in the world (Jao 1979).

CONCLUSION

The British 'second' empire emerged partly as an accident of history, partly because of the traditional role of the City in the first empire. Once an unregulated financial market developed in London, it became clear that trading through the small remnants of the empire gave London a distinct advantage. The UK was never too keen on making political capital out of these

developments, maintaining relatively low key profile in the international arena but always insisting on maintaining London's system of financial self-regulation.

Whether intentionally or not, the City of London went about dispersing its assets among closely linked offshore financial centers – largely in order to achieve what is nowadays euphemistically described as 'tax neutrality', but in the process it also diffused somewhat the perception of power accumulating in London. This has resulted in British-centered networks specializing in trading in incorporeal assets that together quietly have shaped and defined the international financial market. That the Euromarket proved to be the most significant development in international finance in the post-war period is well-known and accepted among scholars on the two sides of the Atlantic – yet the link between these developments and theories of state structural power and hegemony are somehow missing. Many scholars still believe that the U.S. was the key agent driving the trend towards international financial deregulation, which is clearly not the case.

References

.....

- Albert, Michel, 1993. *Capitalism Against Capitalism*. London: Whurr.
- Altman, Oscar L. 1969. "Eurodollars." in Chalmers Eric B. (Ed.), *Reading in the Euro-Dollar*. London: W.P. Griffith.
- Arrow, Kenneth J. 1962, 'The Economic Implications of Learning by Doing,' *Review of Economic Studies*, 29:155-73.
- Axelrod, Robert. 1984. *The Evolution of Cooperation*. NY: Basic Books.
- Baldacchino Godfrey, 2006, Managing the hinterland beyond: Two ideal-type strategies of economic development for small island territories. *Asia Pacific Viewpoint*, 47:1, 45-60.
- Bazzolim Laure, 2000, Institutional Economics and the Specificity of Social Evolution : About the Contribution of J.R. Commons in Perlman, Louca F., M. (ed), *Is Economics an Evolutionary Science?* Edward Elgar.
- Bhattacharya, Anindyak, 1980, Offshore Banking in the Caribbean. *Journal of International Business Studies*. 11:3, 37-46.
- Bianchi, Patrizio and Labory, Sandrine, 2004, The Political Economy of Intangible Assets in Bianchi, Patrizio and Labory, Sandrine (eds.) *The Economic Importance of Intangible Assets*. London: Ashgate.
- Brinkman, Richard L. and Brinkman, June E., 2006, Cultural Lag: In the Tradition of Veblenian Economics. *Journal of Economic Issues*, XL (4) 1009-1028.
- Bryant, Ralph C., 1989. The Evolution of Singapore as a Financial Centre, in Singh Sadhu xx
- Burn, Gary, 2005, *Re-Emergence of Global Finance*. London: Palgrave.
- Choi, SR, Park, D, Tschoegl, A, 1996, Banks and the World's Major Banking Centers, 1990, *Review of World Economics*, 132(4), 774-793
- Cogan, Philip, 2002, *The Money Machine: How the City Works*. London: Penguin. 5th edition.
- Commons, John R. 1959 [1924] *The Legal Foundations of Capitalism*. Madison, Wis: The University of Wisconsin Press.
- _____ 1961. *Institutional Economics*. Madison: University of Wisconsin Press.
- Corporation of London, 2005, *The Competitive Position of London*, Z/ yen, St. Helen's Place: London
- Crombie, Roger, 2008, Bermuda in-Depth Series Part I: Lighting and Fire' *Risk and Insurance*, January 1st.

Dharmapala, Dhammika A. & Hines, James R. 2006, Which Countries Become Tax Havens? *NBER Working Paper* No. W12802.

Dijk, Michael Van, Weyzig, Francis & Richard Murphy, 2006, *The Netherlands: A Tax Haven?* Amsterdam: Somo.

Dixon, Liz. 2001. "Financial Flows Via Offshore Financial Centers." *Financial Stability Review*, 10: 104-115.

Dumenil, Gerard and Levy, David, 2004, *Capital Resurgent*. Cambridge. Mass: Harvard University Press.

ECOFIN, 1999, Code of Conduct Business Taxation Council of The European Union. Brussels. . http://ec.europa.eu/taxation_customs/resources/documents/primarolo_en.pdf

Financial Stability Forum (FSF). 2000. *Report of the Working Group on Offshore Centers*. www.fsforum.org/Reports/RepOFC.pdf.

Foster A., and Rosenzweig, M., 1995, Learning by doing and learning from others: human capital and technical change in agriculture. *Journal of Political Economy* 103: 1176–1209

G Murray, G and Pereira A., 1996, *Singapore: The Global City-State*. Palgrave Macmillan.

Gehrig, Thomas, 2000, Cities and the Geography of Financial Centres in Huriot, Jean-Marie and Thisse, Jacques-François eds. *Economies of Cities: Theoretical Perspectives*. Cambridge: Cambridge University Press.

Goetz, Von Peter, 2007, International Banking Centres: A Network Perspective, *BIS Quarterly Review*, December, 33-49.

Goodfriend, Marvin, 1998, 'Eurodollar' in Cook, Timothy Q. and Laroche, Robert K. Eds. *Instruments of Money Market*. 7th edition. Federal Reserve Bank of Richmond Richmond, Virginia.

Government Accounting Office (GAO), 2008, *Cayman Islands: Business and Tax Advantages Attract U.S. Persons and Enforcement Challenges Exist*. Report to the Chairman and Ranking Member, Committee on Finance, U.S. Senate. July 2008.

Gowa, Joanne, 1995, *Allies, Adversaries and International Trade*. Princeton: Princeton UP.

Gowan, Peter, 1999, *The Global Gamble: Washington's Faustian Bid for World Dominance*. London, Verso.

Guex, Sebasiten, 1998, *L'argent de l'état: Parcours des finances publiques au xxe siècle*. Lausanne, Réalités sociales.

Hall, John and Oliver Whybrow, 2008, Continuity and Continuousness: The Chain of Ideas Linking Peirce's Synechism to Veblen's Cumulative Causation, *Journal of Economic Issues*, vol. XLII: 2, 350-4

- Hampton, Mark, 1996, *The offshore interface : tax havens in the global economy*. Basingstoke : Macmillan.
- _____.2007, Offshore Finance Centers and Rapid Complex Constant Change, Kent Business School, Working Paper No.132.
- Hanzawa, Masamitsu. 1991. 'The Tokyo offshore market' in *Japan's Financial Markets*. Foundation for Advanced Information and Research, Japan
- Harvey, David, 2007. *A Brief History of Neoliberalism*. Oxford: Oxford University Press.
- Heyvaert, Werner, 2006, ECJ Ruling Extends Belgian Coordination Center regime, *Tax Notes International*, July 10, p 105.
- Hudson, Alan C. 1998, reshaping the regulatory landscape: border skirmishes around the Bahamas and Cayman offshore financial centers. *RIPE*, 5:3, 534-564.
- IFSL, 2007, International Financial Markets in the UK. www.IFSL.org.uk/research
- Jao, Y.C., 1979, The Rise of Hong Kong as a Financial Center, *Asian Survey*, 19,7:674-694.
- Jin, Jim Y., Perote-Pena, Juan, and Michael Troege, 2004, Learning by doing, spillovers and shakeouts. *Journal of Evolutionary Economics*, 14: 85–98
- Johns, R.A. & Le Marchant, C.M. 1993. *Finance Centres: British Isle Offshore Development Since 1979*. Pinter Publishers: London and New York.
- Kapstein, Ethan B. 1994, *Governing the Global Economy: International Finance and the State*. Camb. Mass. Harvard University Press.
- Kindleberger, Charles, 1974, *The Formation of Financial Centres: A Study in Comparative Economic history*. Princeton: Princeton University Press.
- Konings, Martin, 2008, 'The Institutional Foundations of US structural power in International finance: From the re-emergence of global finance to the monetarist turn. *RIPE*, 15(1), 35-61.
- Kuenzler, Roman, 2007, *Les paradis fiscaux*, university of Genève, Master thesis
- Le Hérissier, Roy, 1998, Jersey: Exercising Executive Power in a non-party system', *Public Administration and Development*, 18, 169-184.
- Lewis Mervyn K. and Davis, Kevin T. 1987, *Domestic and international banking*. Cambridge, Mass.: MIT press.
- Lipietz Alain, 1987 *Mirages and Miracles: The Crisis of Global Fordism*. London: Verso.
- Low, L. 1998, *The Political Economy of a City-state: Government-made Singapore*. USA: Oxford University Press.
- Marshall, Don D. 1996. Understanding Late-Twentieth-Century Capitalism. *Government and Opposition*

Roxburgh, Charles, Lund, Susan, Atkins, Charles, Belot, Stanislas, Hu, Wayne W. and Moira S. Pierce, 2009, *Global Capital Markets: Entering a new Era*. McKinsey Global Institute. McKinsey & Co.

Mitchel, Austin and Sikka, Prem, 2002, Jersey: Auditors' Liabilities versus People's Rights, *Political Quarterly*, 70: 3 – 15.

Moffett Michael H.& Stonehill, Arthur, 1989, International Banking Facilities Revisited. *Journal of International Financial Management and Accounting* 1:1 1989

Mutti, John and Grubert, Harry, 2006, New Development in the Effects of Taxes on Royalties and the Migration of Intangible Assets abroad. NBER/CRIW Conference on International Service Flows, Washington D.C. April 28, 2006. http://www.nber.org/books_in_progress/criws06/mutti-grubert8-4-06.pdf

National Audit Office NAO, 2007, *Managing Risk In The Overseas Territories*, Report By The Comptroller And Auditor General | HC 4 Session 2007-2008 | 16 November 2007 Foreign And Commonwealth Office. London: The Stationery Office.

Naylor, R.T. 1987. *Hot Money and the Politics of Debt*. London: Unwin Hyman.

Orren, Karren and Skowronek, Stephen, 2004, *The Search for American Political Development*. Cambridge UP.

Panitch, L, and Gindin, S. 2005, 'Finance and American Empire' in L. Panitch and C. Leys (Eds.) *Socialist Register 2005*, London: Merlin.

Papke, Leslie E., 2000, One-Way Treaty with the World: The U.S. Withholding Tax and the Netherland Antilles. *International Tax and Public Finance*, 7: 295-313.

Park YS, 1982, The Economics of Offshore Financial Centers, *Columbia Journal of World Business*. 17:4, 31-36.

Peillon, V., and A. Montebourg. 2001. La Cité de Londres, Gibraltar et les Dépendances de la Couronne: des centres offshore, sanctuaires de l'argent sale. *Rapport d'information de l'Assemblée nationale*, no. 2311. 52/2001

Preinreich, Gabriel, 1936, The law of Goodwill. *The accounting review*, XI, December, 4, 21-35.

Ragin, Charles 2000, *Redesigning Social Inquiry: Fuzzy Sets and Beyond*. Chicago and London: Chicago University Press.

Reed, H.C. 1981, *The Preeminence of International Financial Centers*, New York: Praeger Publishers.

Regini, Marino, 2000, Between Deregulation and Social Pacts: The Responses of European Economies to Globalization, *Politics & Society*, 28:5, 5-35.

- Regnier, P, 1991, *Singapore, City-State in South-East Asia*. University of Hawaii Press.
- Roberts, R, and Kynaston, D., 2002. *City State: A Contemporary History of the City of London and how Money Triumphed*. London: Profile.
- Ruggie, J. G. (1982) 'International Regimes, Transactions and Change: Embedded Liberalism In The postwar economic order', *International Organization* 36: 397-415.
- Schanble, H. 1991, Agenda-Diffusion and Innovation: A Simulation Model. *Journal of Evolutionary Economics*, 1:65-85.
- Schelling, T.C., 1978, *Micromotives and Macrobehaviour*. New York: W.W. Norton and co.
- Schenk, Cathrine R., 1998, "The Origins of the Eurodollar Market in London 1955-63." *Explorations in Economic History*, 21: 1-19.
- Seabrooke, Leonard, 2001, *US Power in International Finance: The Victor of Dividends*. New York: Palgrave.
- Sharman, Jason and Mistry, Percy S., 2008, *Considering the Consequences: The Development Implications of Initiatives on Taxation, Anti-Money Laundering and Combating the Financing of Terrorism*. London: Commonwealth Secretariat.
- Spruyt, Hendrik 1994. *The Sovereign State and Its Competitors: An Analysis of Systems Change*, Princeton, NJ: Princeton University Press.
- Steward, Jim, 2005, Fiscal Incentives, Corporate Structure and Financial Aspects of Treasury Management. *Accounting Forum*, 29:271-288.
- Stiglitz, Joseph, 2002, The Roaring Nineties. *The Atlantic Monthly*. October.
- Strange, Susan . 1988. *States and Markets: An Introduction To International Political Economy*, New York: Basil.
- Swank Duane, 2006, Tax Policy in an Era of Internationalization: Explaining the Spread of Neoliberalism, *International Organization* 60: 847-882.
- Sylla Richard, 2002, United States Banks and Europe: Strategy and Attitudes in Stefano Battilossi and Youssef Cassis eds. *European Banks and the American Challenge: Competition and Cooperation in International Banking Under Bretton Woods*. Oxford UP.
- Tesfatsion, Leigh, 2001, Introduction to the special issue of agent-based computational economics. *Journal of economic Dynamics & Control*, 25: 281-293.
- Thelen, Kathrin, 1999, Historical institutionalism in comparative politics, *Annual Review of Political Science*, Vol. 2: 369-404.

- Toniolo, Gianni, 2005, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973*, Cambridge University Press, Cambridge.
- Tschoegl, Adrian E. 1989, The Benefits and Costs of Hosting Financial Centres, in Park, Yoon S & M Essayad (Eds.). *International Banking and Financial Centres*. Amsterdam: Kluwer
- Van de Ven, Andrew, 1993, The Institutional Theory of John R. Commons: A Review and Commentary. *The Academy of Management Review*, Vol. 18, No. 1, 139-152.
- Veblen, Thorstein, 1961, 'On the Nature of Capital' reprinted in Veblen, Thorstein, *The Place of Science in modern Civilization and other essays*. Russle & Russel, New York.
- Wade, Robert and Frank Veneroso, 1998, The Asian Crisis: The High Debt Model Versus The Wall Street-Treasury-IMF Complex, *New Left Review*, 228: 3-24.
- Warner, Philip, J. , 2004, *Luxembourg in Intenational tax planning*, IBFD publication
- Weichenrieder, Alfons J and Mintz, Jack, 2006, What Determines the Use of Holding Companies and Ownership Chains? Unpublished paper.
http://www.buba.de/download/vfz/konferenzen/20070329_cambridge/paper_weichenrieder.pdf
- Weichenrieder, Alfons, 1996, Fighting international tax avoidance: the case of Germany. *Fiscal Studies*, 171 37-58
- Yeandle, Mark, Mainelli, Michael and Berendt, Adrian, 2005, *The Competitive Position of London as a Global Financial Centre*. Corporation of London. www.cutyoflondon.gov.uk/economicresearch

.....

Table 1 International Financial Centers, 2010

External loans and deposits of banks in all currencies vis-à-vis all sectors
 In individual reporting countries, in billion of US dollars, Mar 2010

Reporting Countries		Amounts outstanding		combined	% share of total
		External loans	deposits		
All countries		21,497.0	22,883.9	44,380.9	
1.	UK	4,417.2	4,691.3	9162.5	20.6
2.	US	3,274.2	3,364.5	6638.7	14.9
	(IBF)	705.6	629.2	1334.8	3.0
3.	Germany	2,965.9	1,262.1	4228.0	9.5
4.	Caymans	1,554.7	1,617.9	3172.6	7.1
5.	France	1,434.4	1,705.8	3140.2	7.1
6.	Japan	867.5	932.5	1800.0	4.0
	(JOM)	518.0	199.5	717.5	1.6
7.	Switzerland	780.8	851.8	1632.6	3.7
8.	Netherlands	694.8	825.2	1520.0	3.4
9.	Ireland	464.3	892.8	1357.1	3.0
10.	Singapore	702.2	659.8	1362.0	3.0
11..	Luxembourg	567.3	538.2	1105.5	2.5
12.	Belgium	514.2	514.8	1029.0	2.3
13.	Spain	309.3	683.1	992.4	2.2
14.	Hong Kong SAR	497.0	465.0	962.0	2.2
15.	Bahamas	467.5	483.7	951.2	2.2
16.	Italy	239.4	585.9	825.3	1.8
17.	Canada	386.2	328.3	714.5	1.65
18.	Austria	311.8	184	495.8	1.1
19.	Jersey	287.4	189.8	477.2	1.0
20.	Sweden	224.8	184.6	409.0	0.92
21.	Denmark	163.9	215.1	379.0	0.85
22.	Bahrain	179.9	174.1	354.0	0.79
23.	Guernsey	137.7	141.8	279.5	0.63
	Isle of Man	75.3	57.0	132.3	
	Cyprus	57.5	95.0	152.5	

Source: BIS 2010

Table 2 International Financial Centers

	COMBINED	% OF TOAL
ALL COUNTRIES	44,389.0	
British Empire + European Havens	23,648.6	53.3%
British Empire ¹	17,006.4	38.3%
British State ²	13,224.1	29.8
European Havens ³	6,642.2	14.9
City-States ⁴	8,719.8	19.6
US	6,638.7	14.9
4 big European ⁵	9,185.9	20.7

Source: BIS 2010

¹ Figures for the British Empire include the UK, Caymans, Singapore, Hong Kong, Bahamas, Jersey, Guernsey, Isle of Man

² UK, Caymans, Jersey, Guernsey, Isle of Man

³ Switzerland, Netherlands, Ireland, Belgium, Luxembourg, Austria.

⁴ Caymans, Singapore, Hong Kong, Luxembourg, Bahamans, Jersey, Guernsey, Bahrain, Isle of Man

⁵ France, Germany, Italy, Spain