

Offshorenness, globalization and sovereignty:
A postmodern geo-political economy?

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Introduction: Offshorenness and the geographies of globalization

The offshore phenomenon - the development of regulatory spaces beyond the reach of onshore regulation - and the reworking of sovereignty, are central to the contemporary restructuring of the international political economy and its geographies. In this paper I outline the phenomenon of offshorenness and explain its connection to processes of globalization and the reworking of sovereignty. By globalization I mean increases in the extensity (scale), intensity (volume), and velocity of social interactions (Held, McGrew, Goldblatt and Perraton 1999); by sovereignty I mean the principle which gives states the authority to set the rules for activities which take place within their borders¹; by offshorenness I mean the existence of jurisdictions beyond the regulatory reach of onshore regulatory authorities.² The paper begins by outlining recent work on the geographies of globalization, before introducing offshore and its development, and drawing out the themes and puzzles which the development of offshore throws up. Utilizing the idea of geo-regulatory change, the heart of the paper then seeks to explain these puzzles through the concept of the offshore “unbundling of sovereignty”, a

¹ This definition is crucial. Sovereignty is an ordering principle which confers regulatory powers rather than being in itself something which states do or do not possess. I use the term “sovereignty-derived regulatory powers” or “sovereign powers” to refer to the ability of states to set the rules within their territories.

² “Offshore” is relative to, and gets its meaning from, “onshore”. In this way, all places might be seen as off-some-shore, but in this paper my focus is on micro-state tax havens such as the Bahamas, Cayman, Jersey and Vanuatu which are offshore from the world’s most powerful and wealthy states.

concept which reveals why offshore matters in the changing relationship between the geographies of globalization and sovereignty.

The recent proliferation of research concerning processes of globalization by Geographers and other social scientists (see for instance: Boyer and Drache 1996; Cerny 1995; Cox 1997; Dodds 1998; Hirst and Thompson 1996; Kofman and Youngs 1996; Mittelman 1996; Sassen 1997), has begun to explain the ways in which the geographies of globalization matter, focusing on the ways in which the spatial organization of the international political economy makes a difference to its workings. The focus of this research has been to show the ways in which the geography of power alters the workings or modalities of power (Allen 1997, 1999). As part of this focus on the geographies of power, and after the work of Harvey (Harvey 1982, 1989), attention has been given to matters of mobility and fixity (Brenner 1998), deterritorialization and reterritorialization (O'Tuathail 1998a), scale and scaling (Swyngedouw 1997), and the role and dynamics of borders and frontiers (Newman 1998; Newman and Paasi 1998; Rosenau 1997; Yeung 1998).

A focus on such issues and concepts at the international level has led to some convergence between the work of Geographers and scholars of International Relations and International Political Economy (Agnew 1998; Agnew and Corbridge 1995; Hudson 1998a; Kofman and Youngs 1996; O'Tuathail and Dalby 1998; Rosow, Inayatullah and Rupert 1994; Youngs 1999). This convergence has taken place around the concept of sovereignty, a concept which has provided the foundation for the discipline of International Relations and which most social scientists have, until recently, taken as fundamental to the international political economy. In recent years, in the context of globalization, the sovereign assumptions of mainstream International Relations have come in for much criticism, with sovereignty increasingly seen as a socially constructed and historically specific socio-spatial institution which changes as social processes and their spatial organization change (Agnew 1994; Barkin and Cronin 1994;

Bartelson 1995; Biersteker and Weber 1996; Burch 1994; Camilleri and Falk 1992; Ferguson and Mansbach 1996; Lapidoth 1992; Philpott 1995; Ruggie 1983; Sassen 1997; Spruyt 1994a and 1994b; Taylor 1994 and 1995; Thomson 1994; Walker 1991 and 1993). That is, although sovereignty has played a central role in the organization of the international political economy over the last three centuries, it wasn't always so, and need not be so in future.³

Offshorenness provides a useful and important lens through which to look at the changing geographies of globalization and the reworking of sovereignty. The phenomenon of “offshore” - offshore financial centres (OFCs), export processing zones and special economic zones which are located legally, if not always physically, beyond the reach of onshore regulation – seems to play a central role in the restructuring of sovereignty as an ordering principle of the international political economy (Palan 1998a, 1998b, 1999; Ruggie 1993).

Placing offshore

Developing offshore

OFCs are places which host banking, insurance, and other financial activities, juridically away from onshore regulatory authorities.⁴ Such centres include the Bahamas and Cayman in the

³ International Relations scholars produce much material which considers the development of sovereignty, debates its importance and argues about whether or not it has changed; see the special issue of Political Studies on “Sovereignty at the Millennium” (Political Studies, 1999). Within this literature there is considerable debate about the importance of sovereignty relative to imperialism. However, this supposed opposition between sovereignty and imperialism seems to me to be overdone. Whilst imperialism has been an alternative spatial organization of power to sovereignty, it has actually resulted in the exporting of the principle and practice of sovereignty world-wide. In fact many offshore financial centres, which now rely on sovereignty for their development, are themselves relics of imperialism.

⁴ The following section briefly re-works previously published material (Hudson 1998a).

Caribbean, Gibraltar and Jersey in Western Europe, Bahrain in the Middle East, Singapore and Hong Kong in East Asia, and Vanuatu in the South Pacific. As small and apparently marginal places in the international political economy, until recently they have merited scant attention (although see: Hampton 1994 and 1996; Hampton and Abbott 1999; Hudson 1998a, 1998b, 1999; Johns 1983; Johns and Le Marchant 1993; Palan 1998a, 1998b, 1999; Palan and Abbott 1996; R. Roberts 1994; S. Roberts 1994 and 1995). However, their small size belies their importance in the workings of the international political economy. In 1991 the volume of international banking taking place in the top five OFCs - the Bahamas, Cayman, Hong Kong, Panama and Singapore – was \$1893 bn., or 15% of total international banking activity (Bank for International Settlements 1993). Indicating the greater volumes of financial activity which make use of OFCs in a more transient manner Kochen suggests that “as much as half of the world’s stock of money either resides in, or is passing through, tax havens” (Kochen 1991, 73). In addition, as this paper explains, offshoreness is central to the reworking of sovereignty as the ordering principle of international relations and, as such, is more important than even the large volumes of financial activity taking place offshore would suggest.

Two of the most dynamic OFCs over the last thirty-five years have been the Bahamas and Cayman; a brief examination of their development illustrates general trends in the development of OFCs.⁵ Their development as OFCs began in the 1960s as they offered a safe haven for US dollars seeking to escape US restrictions – chiefly interest rate ceilings and reserve requirements - on onshore banking activity (Aliber 1979; Hawley 1986; Johns 1983). For places with limited resources and small local markets offshore finance seemed to offer an

⁵ This paper extends my doctoral research which concerned the development of the Bahamas and Cayman OFCs. In addition to much archival research I conducted a postal questionnaire and 60 in-depth semi-structured interviews with bankers, politicians and central bankers in the Bahamas, Cayman, New York, Washington D.C. and London (Hudson 1996).

alternative path to development (Connell 1998), a path which could build on their reputation as tax havens, and their ability to shape their own regulatory environments. The Caribbean OFCs offered a cheap location, an attractive regulatory environment free of exchange controls, reserve requirements and interest rate ceilings, a New York time zone, and relatively stable political environments with increasingly good communications facilities. The number of overseas branches of US banks increased from 180 in 1965 to 732 in 1975; the Caribbean component increasing from 5 to 164 branches (Johns 1983, 29). Through the 1970s, with the collapse of the Bretton Woods system, the rise of the Eurodollar markets, the oil-price hikes and the increasing internationalization of economic activity, the Bahamas and Cayman OFCs developed rapidly and put the Bahamas and Cayman on the international financial map (Roberts 1994 and 1995). By 1991 the numbers of banks with a presence in the centres had reached 400 and 544 for the Bahamas and Cayman respectively, while the volumes of offshore banking hosted had reached \$287 bn in the Bahamas and \$442 bn in Cayman.

Offshore themes

Running through the historical geography of OFCs such as the Bahamas and Cayman are three themes which can help us to relate offshoreness to globalization and sovereignty: the regulatory construction of places; the relational nature of competing places; and the positioning of places within a wider regulatory landscape (Hudson 1996). Firstly, the regulatory construction of places. The Bahamas and Cayman OFCs operate by creating attractive regulatory environments for international finance (Roberts 1995). Two sets of legislation provide the fundamental regulatory building blocks for the construction of the Bahamas and Cayman OFCs. These regulatory building blocks are the tax and secrecy laws of each country. There are no direct taxes in the Bahamas or Cayman and the confidentiality of their financial systems is supported by strict secrecy laws. These two sets of laws work to make the Bahamas and Cayman OFCs attractive places or regulatory environments for

financial activity. The tax laws make them a potentially profitable place; the secrecy laws make them a private place where the tax laws can be skilfully used for evasion and avoidance. In providing the OFCs with the authority to enact low tax and high secrecy laws, the principle of sovereignty is central to their development.

A second theme is that the identity and position of each OFC is affected by how it relates to, and compares with, other OFCs. This is particularly apparent in the development of the Bahamas and Cayman as they are the key OFCs in the Caribbean, servicing the large North and South American markets. When the Bahamas became independent from the UK in 1973 it was Cayman⁶ which benefited, attracting financial activity away from the Bahamas. The competing jurisdictions have different characteristics and try to construct themselves as more attractive to offshore business than their competitors. In such a situation, offshore centres rarely co-operate with each other in the construction of their regulatory environments, for fear of losing their competitive edge. That said, there are limits to the ways in which the OFCs compete. OFCs have to retain the trust and confidence of their customers and onshore and international regulatory authorities, and so are unlikely to reduce their levels of regulation and supervision below acceptable levels (Hudson 1998b).

A third related theme is that OFCs are places in a wider regulatory landscape. Their identities, strategies and fortunes are shaped not only by the actions of competing OFCs (relational competing places), but also by the activities of powerful onshore regulators such as the US Federal Reserve Board, international regulators such as the Basle Committee on International Banking Supervision and Regulation, multinational banks and wealthy individuals. In

⁶ The Cayman Islands are a UK-dependent territory, but they are autonomous as regards their internal affairs and legislative framework.

particular, relations with the USA have been central to the development of the Bahamas and Cayman OFCs. Their development was stimulated by US restrictions on domestic banking activity in the 1960s, and through the 1970s and 1980s the USA - suspecting that the OFCs facilitated tax evasion/avoidance and money laundering - sought to restrict the operations of the OFCs and dismantle their strict secrecy laws (Hudson 1998a).

Offshore puzzles

An investigation of the development of the Bahamas and Cayman OFCs uncovers various puzzles, puzzles about places and puzzles about sovereignty. A first puzzle is apparent in the work of Roberts, which usefully situates the development of Cayman's OFC within wider processes of capitalist globalization. Roberts suggests that: "Offshore financial centres are at once on the margins and at the centre of global capitalism's displacement of crisis" (Roberts 1994, 111). Such a statement invites consideration of *the ways in which* such "fictitious spaces" are both on the margins and at the centre. In addition it remains puzzling that, in a context of globalization, hypermobile capital, and the supposed "end of geography" (O'Brien 1992), places remain important and, further, that small resource-poor micro-states such as the Bahamas, Cayman, Andorra, Gibraltar, Liechtenstein and Vanuatu seem to have assumed such important roles in the restructuring of the global economy.

A second set of puzzles relates to the role of sovereignty in the development of OFCs. On the one hand sovereignty seems to be crucial to their development. As explained above, the success of the OFCs in attracting financial activity to their shores is built on their distinctive regulatory environments (no-tax, high-secrecy), and their ability to create such environments stems from the principle of sovereignty which authorizes them to set the rules of the game within their own territories (see Dodd 1994, 100). On the other hand, by choosing to maintain a low or zero tax rate, the OFCs in effect surrender some of their sovereignty-derived

regulatory powers, or more precisely choose to use them in a particular way, to encourage non-local transnational actors - banks and individuals - to make use of their regulatory environment. An inevitable consequence of this, as the Bahamas and Cayman OFCs experienced through the 1970s and 1980s, is that onshore regulators, seeking to maintain control of financial activity which originates from their shores, try to gain access to information from within the OFCs. The USA sought to extend its regulations into the formally sovereign (i.e. governed according to the principle of sovereignty) Caribbean territories, interestingly by holding transnational banks accountable across borders, leading to conflicts of jurisdictional authority. The OFCs did not give up their regulatory powers in this respect without a fight, but as the OFCs were forced to come to some arrangement with more powerful onshore (US) regulators they ended up losing some of their sovereign powers and having to relax their secrecy laws (Hudson 1998a). It remains unclear what role sovereignty plays in the OFCs, whether sovereignty provides an important resource for the OFCs' development, or whether they have in fact lost their sovereign powers by becoming nodes in an interdependent global economy. These are the puzzles which any theory of offshore-ness must address.

Regulatory landscapes and geo-regulatory change

Globalization and space

Conceptualizing globalization as geographical process and sovereignty as territorial principle, it is necessary to outline a model of geo-regulatory change prior to explaining the role of offshore-ness in the changing geographies of globalization and the reworking of sovereignty. Globalization, for a variety of commentators, is best understood in terms of changes in the importance and meaning of space, place, distance and borders; the spatialities of power and social relations; geography (Giddens 1990; Held, McGrew, Goldblatt and Perraton 1999;

Rosenau 1997; Sassen 1997). Cerny, for instance, develops a spatialized political economy approach with his discussion of globalization and the changing logic of collective action (Cerny 1995). In this framework, globalization is about a shift in the appropriate scale for the provision of public goods. Political economies of scale are “particular historical matrices or patterns of imbrication between economic-organizational and political-institutional structures” (Cerny 1995, 598). These political economies of scale change over time as the nature and spatial mobility of the goods, assets and resources which are central to the international political economy change in a dynamic technological environment. As the scale of goods and assets produced, exchanged and used diverges from the scale of the state, the authority, legitimacy and effectiveness of the state as a regulatory authority is brought into question. Such processes of structural differentiation require new political economies of scale (see also Spruyt 1994a and 1994b).

Agnew and Corbridge develop a similar approach to understanding changes in the international political economy with their concept of “geopolitical order” (Agnew and Corbridge 1995). By order they mean “the routinized rules, institutions, activities and strategies through which the international political economy operates in different historical periods” (Agnew and Corbridge 1995, 15). They argue that orders are necessarily geographical, involving particular spatialities of power and social relations; that orders can be distinguished by their geographies (Ruggie 1983); and, that changes in the geopolitical order involve changes in the differentiation of the spatial fields of practice, that is, changes in the location, function and understanding of borders. It is this sort of approach which I develop with my concept of “regulatory landscapes”.

Regulatory landscapes

Regulatory landscapes⁷ are spatial organizations of economic activity and political regulation, which are geographically structured through the use of borders and territoriality, resulting in an uneven regulatory surface.⁸ Most importantly, regulatory landscapes are socially constructed or constituted (Burch and Denmark 1997), and scaled in particular ways (Harvey 1996). As Agnew puts it: “geographical scale is the focal setting at which spatial boundaries are defined for a specific social claim, activity or behaviour” (Agnew 1997, 100). Scale matters because scale is about boundaries and boundaries are about the power to include and exclude (Smith 1992; Swyngedouw 1992). The location, function and meaning of boundaries which separate different regulatory environments on the regulatory landscape is the result of, and basis for, social processes involving contests for power or authority. But, scales and the borders which constitute them change only intermittently because they are institutionalized, for a time, through the discourse and practice of law (Rosenau 1997, 217). The politics of globalization, then, is all about who has the power to draw boundaries around places and peoples, at what scale such boundaries are drawn, and, what the boundaries signify. If we neglect the politics of scale and boundaries we miss the central feature of processes of globalization, the reshaping of regulatory landscapes.

“Regulatory landscapes” are organized in terms of two dimensions or axes: the degree of boundedness of economic activity; and, the degree of boundedness of political regulation.⁹

⁷ This section briefly reworks previously published material (Hudson 1998a and 1998c).

⁸ I prefer “regulatory landscapes” to “regulatory spaces” in order to emphasize: their unevenness and dynamism; the interconnection of regulatory environments; and the fact that landscapes and the actors within them are mutually constitutive rather than regulatory space being a backdrop which actors do not themselves shape.

⁹ This is an **ideal type** model. I am not suggesting that economics and politics are in practice separate spheres, although their differentiation if not separation is a feature of contemporary capitalism (see Meiksins-Wood

Each of these axes stretch from “bounded” to “trans-boundary” poles. “Bounded” economic activity refers to the production, distribution and consumption of commodities within a defined territory, for instance the state; “trans-boundary” economic activity refers to situations where commodity flows cross (state) borders. The scale and hence boundedness of economic activity depends upon the technological environment and the characteristics - particularly the potential spatial mobility - of the commodities in question. “Bounded” regulation means that rules refer to specific defined territories or jurisdictions; “trans-boundary” regulation signifies that rules extend beyond national borders. The scale and boundedness of political regulation depends upon the technological environment and decisions made by national regulators about the optimal scale of political regulation for the commodities in question. Combining these two dimensions generates a typology of regulatory landscapes, or geo-political economies, as illustrated by Figure 1.

1997). In addition I am not suggesting that the complexities of a world in which there are many different types of economic accumulation and political regulation can be described in terms of a single regulatory landscape. Rather I am offering a conceptual framework which can be used to think about different types of economic accumulation and political regulation. Different regulatory landscapes, for, say, coffee and money, can and do, co-exist. Whether and how regulatory landscapes affect one another is a question for another day.

		<u>Political regulation</u>	
		Bounded	Trans-Boundary
<u>Economic accumulation</u>	Bounded	Domestic political economies (sovereignty and autonomy)	Political globalization (extra-territoriality)
	Trans-Boundary	Economic globalization (competitive deregulation)	Global political economy (borderless world)

Figure 1: A typology of regulatory landscapes

Regulatory landscapes can be identified through looking at the ways in which scales of economic accumulation and political regulation are combined. That is, in terms of the degree of boundedness or territoriality of activities and rules. In a regulatory landscape of “domestic political economies”, borders are all important. In a “global political economy”, borders are unimportant; this is a borderless world in which neither activities nor rules pay much attention to territorial limits. In the case of “political globalization”, rules transcend borders whilst commodity flows do not; this is a landscape characterized by extra-territoriality or efforts to apply rules to activities which do not take place within the territory of the regulatory authority which seeks to extend its rules. In the case of “economic globalization”, commodity flows cross borders whilst rules do not; this is a landscape characterized by tendencies towards competitive deregulation and regulatory underprovision. The development of Caribbean OFCs in the 1960s and 1970s when the centres were largely able to preserve their autonomy to regulate their own territories and the transnational banking which made use of them, provides a good example of this type of regulatory landscape. In short, regulatory landscapes are socially constructed spatial configurations or scalings of economic activity and political regulation in which borders are more or less important, particular spatialities of power and social relations, particular geographies.

The concept of “regulatory landscapes” emphasizes the dynamic nature of geographies of economic accumulation and political regulation. Because they are socially constructed, regulatory landscapes change as social processes change. In modernity sovereignty is the dominant ordering principle of regulatory landscapes. As Ruggie suggests: “The central attribute of modernity in international politics has been a peculiar and historically unique configuration of territorial space” (Ruggie 1993, 144). However, as the regulatory landscapes framework shows, other configurations are possible through the trans-boundary extension of economic accumulation and/or the trans-boundary extension of political regulation. Such dynamism is evident in the development of OFCs. The development of stateless monies and their movement from onshore to offshore is a trans-boundary extension of economic activity, whilst US efforts to pierce the secrecy of OFCs and follow the dollars exemplify the trans-boundary extension of political regulation. In fact OFCs seem to play a central role in processes of geo-regulatory change from a “modern” to a “postmodern” – less territorially bounded – regulatory landscape (Anderson 1996; Kobrin 1997; Newman 1999; Ruggie 1993).¹⁰ However, *the ways in which* offshore plays a central role remain to be explained.

The medieval to modern transformation

In seeking to develop a vocabulary for understanding a confusing contemporary world Ruggie returns to the middle ages, or more specifically to the transition from medieval to modern times in Western Europe (Ruggie 1993). Social systems and historical periods are best identified not through looking at the parts of society, but through uncovering the principles

¹⁰ The idea of a modern to postmodern transition is perhaps overused and, as with all concepts, imposes a relatively neat framework on a messy reality (see Meiksins-Wood 1997; O’Tuathail 1998b). Here, “postmodern” is used as a shorthand to refer to a world in which there are changes in the meaning and importance of territorial borders.

which provide the basis for the separation of constituent units (Ruggie, 1983). Examples of such principles include relations of class, kinship, religion or geographical location.

In medieval Western Europe the mode of differentiation, was “a nonexclusive form of territoriality”. The regulatory landscape was based on a variety of principles and lacked clear spatial boundaries of authority and regulatory power. The central characteristic of the transition from a medieval to a modern world was the development of a new ordering principle, a development which was based in material changes, strategic behaviours and epistemic changes (Ruggie 1993, 152-160). The transition to modernity sees the re-organization of power into territorially defined, fixed and mutually exclusive units. This is a reconfiguration of power/space, a reshaping of the regulatory landscape. In the medieval-to-modern transformation, the emergence of sovereignty as a new ordering principle resulted in certain problems; there was a tension between a modern ordering principle and a society which was in the process of becoming modern. With its units separated by borders how could the constituent parts of society communicate and deal with issues which extended beyond the borders of an individual jurisdiction?

This tension is clearest in the example of the “embassy chapel problem”: how could a Protestant nation be permitted to hold Protestant services in its embassy chapel in a Catholic state? This problem was dealt with by the (anti)territorial trick of unbundling territoriality. That is, in certain issue-areas the state would surrender its powers to regulate its territory, reducing the scope of its territorial powers. In the case of the “embassy chapel problem”, and diplomatic relations more widely, Ruggie explains that “having so fundamentally redefined and reorganized political space, states ‘found that they could only communicate with one another by tolerating within themselves *little islands of alien sovereignty*’ ” (Ruggie 1983, 279 - citing Mattingly 1964, 244 – my emphasis). Such an “unbundling” of territoriality became a widely used strategy for coping with changes to the principle of differentiation. In a phrase which

points the way to an explanation of the role of offshore-ness in terms of “unbundled territoriality”, Ruggie suggests that “this negation of the exclusive territorial form has been the locale in which international society throughout the modern era has been embedded. The terrain of unbundled territoriality, therefore, is the place wherein a rearticulation of international space would be occurring today” (Ruggie 1993, 171).

Globalization is a process of rescaling the regulatory landscape, a process of geo-regulatory change. To some extent mirroring the medieval-to-modern transformation, the unbundling of territoriality is central to the current phase of geo-regulatory change as it allows an increasingly borderless economy to co-exist with a political system based on borders and sovereignty (Palan 1998a). It is in this way, I will argue, that the role of offshore-ness in processes of globalization and the reworking of sovereignty can best be explained.

The offshore unbundling of sovereignty

Offshore unbundling: What is it?

The offshore unbundling of sovereignty refers to the reconfiguration of power/space, the “splitting up” of sovereignty over various activities, or more precisely the practice of varying the use of sovereign powers by issue area.¹¹ Offshore unbundling is part of contemporary processes of geo-regulatory change. Geo-regulatory change is fundamentally about changes to the principle of differentiation. As sovereignty is the dominant principle of differentiation in modernity, the reworking of sovereignty provide evidence of a transition to a “postmodern”

¹¹ In Sørensen’s terms the unbundling of sovereignty is about changes to the regulative rules of sovereignty, rather than the constitutive rule of constitutional independence (Sørensen 1999).

geo-political economy. It is in this way that offshore is central to the relationship between processes of globalization and transformations of sovereignty. As the regulatory landscapes framework makes clear, processes of geo-regulatory change introduce tensions between the scales of economic accumulation and political regulation. These tensions are manifest offshore in jurisdictional conflicts and contests over sovereignty.

Contests over sovereignty are about which/whose rules should rule in which space (horizontal allocations of authority) in relation to which activities (vertical allocations of authority); they are battles over the appropriate scale and scope of political regulation. Horizontally, is the USA or the Bahamas the appropriate regulatory authority for US-based transnational banks operating in the Bahamas? Vertically, does the USA have the authority to extract information about banking in the Bahamas and/or to tax financial activity taking place there, or should the USA respect the sovereign status of the Bahamas completely? Therefore, such jurisdictional conflicts may be resolved in two analytically separable ways, through the horizontal and vertical reallocation of authority and power.

Horizontal reallocations of authority take place through border skirmishes (Hudson 1998a). In modernity, geo-regulatory change is most apparent at the border because in this era power, communities and their values have tended to be horizontally organized into territorial parcels. Challenges to sovereignty as an historically specific spatial organization of power are most apparent at the margin; power may be everywhere, but it is most clearly contested at the margin. Borders are the dividing lines between cultures, communities and value-systems. As competing communities seek to extend their value-systems or rules they will eventually clash. For some commentators (Rosenau 1997) “frontiers” better captures the essence of these zones of conflict, but regardless of the label we attach to them, the important point is that they are socially constructed and hence are socially transformed. As Leitner makes clear: “a central aspect of the practice of the political construction of scale is the manipulation of relations of

power and authority between overlapping or mutually inclusive political territories, by actors operating and situating themselves at different geographic scales” (Leitner 1997, 125). In the transition from a modern to a postmodern regulatory landscape the margin is frequently a spatial border. As Rosenau puts it: “the political space opened up by the erosion of the boundaries between domestic and foreign affairs emerged as the frontier where most of the action on the global stage unfolds” (Rosenau 1997, xiv). Border skirmishes are central to processes of geo-regulatory change.

Vertical reallocations of jurisdictional authority or power take place through the unbundling of sovereignty. The offshore unbundling of sovereignty, along with border skirmishes, is part of the latest process of geo-regulatory change. Offshore, sovereignty is unbundled into power or authority over two activities which in modernity tend to be bundled together and controlled by a single state. These activities are: firstly, the enactment of laws which shape the regulatory environment of the territory in question; and, secondly the taxation of economic activity which takes place within the territory. We might call the sovereign powers over these two sets of activities, “legal sovereignty” and “fiscal sovereignty”.¹² Whilst modern states exercised their sovereign powers in both the legal and fiscal areas, offshore states, whilst retaining their legal sovereignty to determine the legislative framework - tax and secrecy laws - within their borders, surrender some of their fiscal powers by maintaining low or zero tax regimes to attract mobile financial activity.

Offshore unbundling: Why does it happen?

¹² Whilst some International Relations scholars – particularly those of a realist persuasion in the IR sense - might object to the adjectivization of sovereignty and prefer to speak of legal and fiscal autonomy or independence, the terms legal sovereignty and fiscal sovereignty are a useful shorthand.

The workings of the International Political Economy have, since the emergence of capitalism and the inter-state system with sovereignty at its core, been governed by two social processes or institutions with contradictory spatial logics (Chase-Dunn 1981). On the one hand there is capitalism with a natural tendency to extend itself across borders in order to maximize markets and profits. On the other hand is the inter-state system whose spatial logic is one of borders and fixed mutually exclusive territoriality. As Kratochwil explains: “while political systems are boundary-maintaining systems, markets - although dependent for their creation upon political power and economic networks - are not” (Kratochwil 1986, 42). In the transformation from a medieval to a modern regulatory landscape, property and property rights were central to both the separation and the articulation of capitalism and the inter-state system. As Burch explains: “the split in property (rights) established the conceptual division between the state system (real, tangible property) and the capitalist system (mobile, intangible property). The institution of property rights contributes to the generation and linking of capitalism and the interstate system as articulated structures; differences between real and mobile property contribute to the differences between the two structures” (Burch 1994, 47; see also Burch 1997). The development of mobile property rights alongside immobile property rights is fundamental to the development of capitalism, the inter-state system and their articulation. As Burch briefly summarizes: “Property was a wedge that split the spheres of society, yet it was also a tie that bound them” (Burch 1994, 54). In the modern-postmodern process of geo-regulatory change property and property rights remain central, with offshore unbundling the process through which understandings of property are transformed and tensions between the spatial logics of capitalism and the inter-state system are managed. In Palan’s terms offshoreness is an attempt by the state system to have its cake and eat it (Palan 1998a).

In the contemporary period of globalization, in which processes of economic accumulation increasingly extend across boundaries, the disjuncture between the spatial logics of capitalism and the inter-state system is amplified. The development of “stateless monies” (Martin 1994)

since the first Eurodollar deposits by a Chinese Government fearful of US seizure of their dollar assets in 1949, and particularly since US restrictions on onshore banking, was a key moment in the development of a postmodern international political economy. The development of stateless monies created an economic space, or in Castells' terms a "space of flows" (Castells 1989), partially separated and working at a different scale from the political space of states and places. As Leyshon puts it: "there emerged for the first time an essentially *de-territorialized* economic phenomenon, which possessed a logic and a dynamic completely at odds with the national-centric order of the international regulatory system" (Leyshon 1992, 260 - his emphasis). The geo-political economy of Bretton Woods was shattered by the development of new monies, new monies which had their own geographies, monies and geographies which undermined the power of state-territorial regulatory systems (Corbridge 1994; Helleiner 1994). The development of stateless monies reshaped the regulatory landscape, undermining the geography – a spatial organization of power and social relations - of fixed, mutually exclusive, territorial states. The regulatory landscape was transformed. Sovereignty as the dominant principle of differentiation was undermined, in Ruggie's terms as a result of increases in the "dynamic density" of society (Ruggie, 1983; see also Spruyt 1994a and 1994b).

The increased mobility of money and finance, as well as other forms of economic activity, produced further tensions between capitalism and the inter-state system of sovereignty. As Kratochwil explains: "On the one hand, we observe the virtually universal recognition of territorial sovereignty as the organizing principle of international politics. On the other hand, because of the growth of transnational relations and interdependencies, there is a tendency toward erosion of the exclusivity associated with the traditional notion of territoriality" (Kratochwil 1986, 27). The development of OFCs and the offshore unbundling of sovereignty articulates capitalism and the inter-state system. The offshore unbundling of sovereignty links the contradictory systemic logics in that, on the one hand, sovereignty – legal sovereignty or

autonomy - is maintained, whilst on the other, sovereignty - fiscal sovereignty or the power to tax offshore finance - is surrendered.

It is important to note at this point that I am not suggesting that processes of geo-regulatory change produce OFCs because they are functional for capitalism. The OFCs are functional for fractions of capital, particularly internationally mobile capital, but this is at best one half of an explanation for their development. A fuller account must include the decisions and actions of people, for instance, of elites in the Bahamas and Cayman in pursuing an offshore development strategy and international financiers in looking for an offshore location. A fuller account must include social practices, and explain *the ways in which* OFCs are functional for capitalism. In fact, a fuller account must be able to explain why OFCs have been important in the unbundling of sovereignty.¹³

We can explain why it is that OFCs have been important sites for the unbundling of sovereignty, with reference to the fact that they tend to be resource-poor micro-states, with small markets and few options for development. Baldacchino suggests that micro-states are treated as anomalous or deviant, and have been neglected by mainstream development theory (Baldacchino 1993). He describes the strategies of micro-states as “pseudo-development”, arguing that they adopt a rentier development strategy of insertion into the world economy. For micro-states “economic development is a problem of management - of timing, sequencing, and manipulating in an unending effort to perceive or create, and in any case to exploit, a multiplicity of little openings and opportunities” (Best 1971, 30 - cited in Baldacchino 1993,

¹³ My aim is to explain why and how, rather than simply to assert that, offshore-ness matters, in the same way as Burch (1994) improves upon Chase-Dunn’s (1981) assertion that there is a “structural articulation” between politics and economics, by explaining the role of the “properties” of the state system and global capitalism in this articulation.

37). For such places, sovereignty-derived legal powers are one of their best resources for development, so, if they wish to develop, they need to make use of them. The smallness and nature of micro-states' economies, lacking internal linkages and relying on imports, can also mean that "there is little difficulty in designing a set of tax advantages which not only do not weaken the domestic tax base but actually widen it beyond what the local economy itself could achieve" (Dommen and Hein 1985, 12). In such a situation, unbundling sovereignty - retaining legal authority to create an attractive regulatory environment, whilst surrendering some of their fiscal powers in order to attract international financial activity - is an attractive proposition. Although the offshore state lets slip its domestically-generated tax base, the income it generates through license fees paid by international financial activity which chooses to use offshore more than compensates for this. It makes financial sense to surrender fiscal sovereignty and miss out on tax revenues in return for a share (small in percentage terms but large by offshore standards) of the transnational flows which pass through offshore.

Offshore unbundling: How does it happen?

Having explained what the unbundling of sovereignty is, why it happens and why it particularly happens offshore, it remains to be explained how it happens, and what it is about sovereignty which gives it the potential to be unbundled. In her work on the emergence of the modern state-system Thomson outlines the changing relationships between mercenaries, pirates and sovereigns through which the state progressively monopolized violence within its territory (Thomson 1994). In outlining the processes through which the sovereign state managed to gain a monopoly on the use of violence, Thomson makes clear that sovereignty is socially constructed and is an historically specific way of organizing political space. Most importantly for our purposes Thomson shows that sovereignty, as a set of institutionalized authority claims, has two dimensions (see Figure 2).

		Constitutive Dimension	
		Smaller political space	Larger political space
Functional Dimension	Fewer activities	Spatially and functionally limited sovereign powers	Functionally limited sovereign powers
	More activities	Spatially limited sovereign powers	Full sovereign powers

Figure 2: The dimensions of sovereignty (after Thomson, 1994)

The first dimension of sovereignty is the constitutive dimension, the dimension in which a specific actor, the state in this case, is designated as the relevant authority for a particular geographical area (see also Sørensen 1999). Along the constitutive dimension of sovereignty the state made a claim to final authority in a particular political space, and, as such, established the boundary between domestic and international politics, inside and outside the borders of the state (Walker 1993). The second dimension of sovereignty is the functional dimension and refers to the set or scope of authority claims made by a state over a range of activities within its political space. As Thomson explains: “This dimension of sovereignty reflects the state’s penetration of the political space contained within its territorial boundaries” (Thomson 1994, 16), establishing the boundary between the political sphere in which state involvement is required and the economic sphere which is left largely to non-state actors.

Thomson provides empirical backing for Ruggie’s claim that: “The institutional framework of sovereignty differentiates units in terms of juridically mutually exclusive and morally self-entailed domains. However, the *scope* of these domains is defined not only territorially but also functionally, depending upon the range and depth of state intervention in domestic social

and economic affairs” (Ruggie 1983, 280). That is, sovereignty is about claims to authority which extend along constitutive dimensions - making the state the relevant authority for a particular political space, and functional dimensions - determining which activities within that space the state has authority over. In this way, changes to sovereignty as the ordering principle of the international political economy can involve changes in claims to authority along either or both dimensions, in my terms horizontal and/or vertical reallocations of authority.

In order to understand transformations in and of the international political economy, transformations such as that associated with globalization, we need to understand the relationships between changes along each of the dimensions of sovereignty. As Thomson puts it: “The key to a theory of global politics is an understanding of the relationship between these two dimensions of sovereignty” (Thomson 1994, 16). In practice, as we have seen with the case of offshore, reallocations of authority are likely to involve both horizontal (constitutive) and vertical (functional) reallocations of authority. Thomson begins to outline the relationship between changes on the constitutive and functional dimensions, explaining that: “While the constitutive dimension sets the boundary between domestic and international political space, the functional dimension establishes the boundaries between the economic and political spheres and between state and non-state realms of decision-making authority. These functional boundaries are not, however, established unilaterally in a geopolitical vacuum. Their positions are a matter of concern for other states or the world polity because they will have external effects. When a state claims authority over a specific range of activities, it at the same time disclaims authority over another set of activities. These specific claims made by a state are conducive to a particular pattern of domestic flows and transactions. But since these flows do not stop at the territorial borders, the individual state’s authority claims have implications for the international system” (Thomson 1994, 17). Although Thomson’s focus is the emergence of the modern state and its monopolization of violence, such an analysis clearly

has relevance for the current transformation from a modern to a postmodern geo-political economy and the position of OFCs and offshore-ness in this transformation. Decisions by the Bahamas and Cayman to relinquish their fiscal powers to tax international financial activity which takes place within their territories have repercussions well beyond the OFCs, repercussions which - although largely unintended - serve to transform sovereignty as the ordering principle of the international political economy.

Offshore unbundling: What makes it possible?

For Burch, property and property rights are the constitutive principles - sets of practices, rules and resources - which make the international political economy work in the way that it does, as the uneasy articulation of capitalism and the inter-state system. As we saw in the medieval-to-modern transformation, the source of changes to the nature of the international political economy is to be found in changes to its constitutive principles, changes in the understandings and practices of property and property rights. Although sovereignty describes the modern mode of differentiation, sovereignty is based upon the institution of property (Ruggie 1983; Burch 1994). Sovereignty is an institution which is based on the acceptance of rights to absolute exclusive private property. As Burch explains: "Sovereign states are first and foremost holders of property rights: holders of a grounded stake in the secular social realm. The crucial terrain is the sovereign state. Arguing that the global system is grounded upon the concept of sovereignty actually misses the fundamental point. Sovereignty is the physical manifestation of sovereign [exclusive] property rights to territorial property" (Burch 1994, 47-8). It is because of its basis in property that sovereignty can be unbundled. Just as property rights over a tree may be unbundled into rights to climb it, pick its fruit, and chop it down, offshore, sovereignty may also be unbundled.

In the OFCs sovereignty is unbundled into “legal sovereignty” and “fiscal sovereignty”, property rights over immobile property - the offshore territory’s legal regulatory environment - and mobile property - the international financial activity which makes use of the OFCs. With echoes of the embassy chapel problem, Palan explains that the offshore phenomenon involves the “bifurcating of the sovereign space into relative realms distinguished by degrees of regulation” (Palan 1998a, 626), a process which allows states to provide “less regulated and taxed spaces without undermining their claim to regulate and tax other areas of economic activities” (Palan 1998a, 627). Legal sovereignty is defended as it is through such powers that the OFCs retain the ability to construct themselves as tax-efficient, confidential and attractive places in the financial regulatory landscape. Fiscal sovereignty is willingly given up for the benefits which offshore financial activity and multinational banks bring to the OFCs. In Burch’s terms OFCs are a site where property rights over activities taking place in the offshore territories are unbundled into two sets of property rights. Along its constitutive dimension the OFCs defend their sovereignty, maintaining their legal claim to be the ultimate authority within their territory, but along the functional dimension OFCs relinquish their sovereignty, waiving their right to tax offshore international financial activity. In this way, offshore-ness does not eliminate sovereignty; rather, offshore-ness uses the principle of sovereignty and reworks its functional scope. Offshore states are still sovereign states but they have chosen to use their legal sovereignty to temper their fiscal powers by creating spaces with relatively low levels of regulation and tax. As sovereignty is based on the constitutive principles of property and property rights, changes to the mobilities of property and the understandings of property rights inevitably lead to transformations of sovereignty as the ordering principle of the international political economy.

Conclusion: A postmodern geo-political economy?

Our brief examination of the development of the Bahamas and Cayman OFCs threw up some puzzles. Firstly, it seemed odd that OFCs are both marginal and central to the workings and transformation of the international political economy, particularly given their small size. Secondly, there seemed to be something odd going on with sovereignty offshore in that the OFCs seem to both defend and surrender aspects of their sovereignty. The explanation offered in this paper helps us to solve these puzzles and to understand the nature of offshore. OFCs are marginal because they are small places away from the major industrialized economies. However, they are central as it is offshore that sovereignty, the ordering principle of the international political economy, is initially unbundled. In fact, it is largely due to the marginality and resource-poverty of the places where OFCs are found that sovereignty is initially unbundled offshore. The puzzle of sovereignty is explained by the fact that sovereignty, with its basis in property rights, is unbundled offshore into “legal sovereignty” which the OFCs defend and value highly, and “fiscal sovereignty” which the OFCs surrender, trading in their ability to tax the financial activity which makes use of offshore in return for a share of the massive transnational financial flows. The contemporary transformation of the international political economy involves the unbundling of sovereignty, an unbundling which occurred initially and most clearly offshore.

Offshorenness matters because contemporary processes of globalization problematize territorial sovereignty as the organizing principle of the international system, leading to a “re-articulation of international political space” (Ruggie 1993) which is achieved initially through the offshore unbundling of sovereignty. The unbundling of sovereignty facilitates the articulation of a global capitalism based on increasingly mobile property with an inter-state system based on immobile property rights or sovereignty. Hand in hand with the deterritorialization of property comes a deterritorialization of regulatory power. As Agnew puts it: “When increasing proportions of property are mobile beyond any one state’s boundaries, individual states provide only a partial and tenuous protection for absolute property rights” (Agnew 1999,

181). OFCs are one site where the unbundling of sovereignty, part of the process of geo-regulatory change, is practised, enabling the articulation of capitalism and the inter-state system despite their contrasting spatial logics. As with the “embassy chapel problem” in the medieval-modern reconfiguration of power/space, OFCs and offshorenness, by bracketing out the source of the tension, resolve a paradox. As Palan suggests, offshorenness allows the state to “carry on discharging its traditional roles as if nothing had happened, thus helping to alleviate some of the tension between globalization and the state system” (Palan 1998a, 627).

As Ruggie puts it, processes of globalization entail “a shift not in the play of power politics but of the stage on which that play is performed” (Ruggie 1993, 139-140). The spatial organization of power and authority into state-territorial units is increasingly undermined by the mobility of money and the space of flows such that “the modern state system may be yielding in some instances to postmodern forms of organizing political space” (Ruggie 1993, 144). The unbundling of sovereignty blurs territorial boundaries, confusing the relationship between territory and power. It is not only money that has become more mobile; the same is true for other commodities, types of information and pollutants. As properties change and become more mobile, understandings of property rights change too, leading to a reconfiguration of power and space. State-territoriality or sovereignty, the central principle of differentiation in modernity, is transformed. As social systems are best distinguished by their principles of differentiation and sovereignty is unbundled offshore, offshorenness is central to our efforts to understand contemporary processes of socio-spatial change. Along with Ruggie, “I have tried to show that unbundled territoriality is a useful terrain for exploring the condition of postmodernity in international politics” (Ruggie 1993, 174).

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