

**OFFSHORES ONSHORE:
NEW REGULATORY SPACES
AND REAL HISTORICAL PLACES**

by

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“In creating a global financial market-place the banks altered the geography of the world system. The basic geographical dimensions of space and time were warped to suit the banks operating needs. ... Nations attempted to control the system through regulation or taxes: tax havens, dots in geographic space but substantial territories in the bankers’ world, enabled such restrictions to be by-passed. ... Time and space in the bankers’ world were pliable, moveable, profitable constructions which might or might not correspond with the mundane geography of national territories” (Daly and Logan, 1989, p.103).

INTRODUCTION: MONEY FLOWS AND REGULATORY SPACES

This is a story about regulatory spaces. Drawing on research conducted in London, New York City, Washington D.C., the Bahamas and Cayman, this chapter is an historical geography of money and the links between ‘offshore’ and ‘onshore’ financial regulatory spaces. As an historical geography, this chapter focuses on the socio-spatial dynamics of money, the ways in which the development of new monies relates to the development of new spatialities of power and social relations, and, the development of regulatory spaces. Substantively, my focus is the development of International Banking Facilities (IBFs) in the USA, and the relationship of this legally-offshore-but-physically-onshore space with the offshore financial centres (OFCs) of the Bahamas and Cayman.

‘Regulatory spaces’ provide the link between money and the space-economy. As particular spatialities of power (Allen, 1997), they are the reason why geography matters in matters of money. Regulatory spaces, or jurisdictions, can be more or less territorial. Rules may refer to a particular set of activities and/or to a particular geographical territory. As the activities in question slip across regulatory borders, rules which are strongly territorial are increasingly challenged. This is what O’Brien means by ‘the end of geography’, a situation in which, “*financial market regulators* no longer hold full sway over their regulatory territory: that is, rules no longer apply solely to specific geographical frameworks, such as the nation-state or other typical regulatory jurisdictional territories”

(O'Brien, 1992, p.1). Leaving aside debates about the newness of globalization (Hirst and Thompson, 1996) or whether geography can be reduced to sovereignty (Agnew, 1994), globalization is usefully understood as an increasing mismatch between the spatial extent of activities and the spatial extent of the rules which govern them, a shift from a modern state-centric geo-political economy towards a more post-modern, less territorial world order (Ruggie, 1993; Agnew and Corbridge, 1995). Money and finance occupy a key position in processes and accounts of globalization. Money flows through space, crossing borders, linking places. As a universal equivalent, money translates value from place to distant place, arguably, dissolving the difference between places (Harvey, 1985; Leyshon, 1996; O'Brien, 1992). So, bounded financial spaces always have a precarious existence; their boundaries may be undermined, and their fortunes linked through flows of money. In the financial sphere particularly, scales of regulation are temporary fictions. As Dodd argues, "the conceptual convenience of the distinction between international and national monetary systems should not be allowed to disguise its analytical weakness" (Dodd, 1994, p.101).

We begin this chapter by looking at the role of money in the shift from a modern to an increasingly postmodern geo-political economy, placing the development of OFCs within the wider context of processes of financial globalization and the collapse of the Bretton Woods international monetary system in the early 1970s. This is a story about the changing geo-political economy of money; new monies go hand in hand with new geographies. Examining the links between onshore and offshore, I show that the development of OFCs was, in part, a response to increased onshore restrictions, and describe how US regulatory authorities subsequently sought to regain control of 'their' offshore dollars. Extra-territoriality, the projection of the USA' legal power beyond its territorial borders was part of the strategy (Hudson, 1998), but in this chapter I focus on efforts to develop an attractive onshore regulatory environment - IBFs - to entice the offshore dollar back home. I consider the initial proposals for IBFs, the predictions which were made as to their impact on the OFCs, and their actual impact, before explaining why IBFs were not as successful as many expected.

My explanation for the failure of IBFs, as new regulatory spaces, to attract the offshore dollar back onshore, revolves around the fact that money is **still** a social relation, and places are **still** peopled and have histories which matter. As a social relation which links distant creditors and debtors, money and finance - particularly when the value of money is uncertain (see Harvey, 1982, on 'fictitious capital') - depends upon trust, trust which is backed up by legal regulations. In the world of international finance, laws are still overwhelmingly territorial, and so places - bounded territorial regulatory spaces - matter. However, IBFs failed because it is very difficult to create anew a new regulatory space. These new regulatory spaces were established in real historical places, which, over time, had acquired particular reputations; reputations which, to potential depositors, were not very trustworthy. Money is more than economic; places are too. Flows of money are not solely determined by potential profits; places cannot be created by legislation. Although money flows link spaces, they do not dissolve difference. Places and peoples are more or less trusted; their past is remembered in their present. To develop Massey's (1984) geological metaphor, it may be possible to shift around the topsoil, but the underlying strata continue to shape the characteristics of places.

GEO-POLITICAL ECONOMIES: MODERN AND POST-MODERN

Monies have geographies. Different monies have different geographies. Or, as Leyshon and Thrift put it: "Each monetary form has its own geography, and the transformation from one monetary form to another has important geographical implications" (Leyshon and Thrift, 1997, p.23). As one monetary form is replaced by another, one spatial arrangement of power and social relations is replaced by another. This is what we see with the early 1970s transformation from the Bretton Woods international monetary system of fixed (if supposedly flexible) exchange rates, to floating rates. The geography of the Bretton Woods system was one of bounded national financial spaces, and managed interactions between these spaces. However, as has been well documented (Corbridge, 1994; Helleiner, 1994a; Leyshon, 1992; Strange, 1986 and 1994), the Bretton Woods system was inherently contradictory and doomed to collapse right from the start.

In part, its collapse was due to its geography. Finance was going global whilst the Bretton Woods regulatory framework remained inter-national with the US dollar at the centre. Processes of

financial globalization challenged territorial regulation as the organizing principle of the modern international political economy. The dynamism of economic activity and money flows was in tension with the stasis and state-centrism of the existing geo-regulatory framework (Leyshon, 1992, p.258). The development of new monies divorced from their national spaces - so-called 'stateless monies' - contributed to the collapse of the Bretton Woods geo-political economy. 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, p.260). As a result, "the postwar model of an international order comprised of a set of interrelated but economically sovereign nation states was finally exploded by an invigorated ... increasingly mobile international financial capitalism" (Leyshon, 1992: 261). 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. An economic space of flows emerged, apparently divorced from the political space of states (Castells, 1989, 1996 and 1997). The development of stateless monies reconfigured power/space, undermining geographies - spatialities of power and social relations - organized into fixed, mutually exclusive, territorial states (Agnew, 1994). Global finance was, and is, a geographical project (Swyngedouw, 1996).

As the Bretton Woods international monetary system collapsed, new geographies were created. Offshore financial centres were a crucial part of this new geography; their development cannot be understood apart from processes of financial globalization and the production of stateless monies (Hudson, 1996; Martin, 1994; Roberts, 1995). The importance of OFCs derives from their role in unbundling sovereignty - property rights over territory - a practice which articulates the economic space of flows and the political space of states (Burch, 1994; Ruggie, 1993; Hudson, 1996 and 1997). The OFCs "hold down the global" (Amin and Thrift, 1994), providing a gateway which links a seemingly abstract and uncontrollable space of flows with the productive economy and the space of politics. The development of OFCs is a key moment in the transition from a modern to a postmodern geopolitical-economy, a geopolitical-economy in which the organization of space and

power into state-territorial units is increasingly undermined by the mobility of money and the space of flows (Anderson, 1996).

ONSHORE - OFFSHORE RELATIONS

As the above analysis suggests, the development of OFCs cannot be understood without looking at onshore developments, and, vice-versa. Onshore and offshore financial spaces are linked by flows of money. 'Onshore' and 'offshore' may define distinct financial spaces, but money flows blur the distinction. From their very beginning OFCs have developed, in part, as a result of onshore regulation. 'Offshore' means beyond the regulatory reach of the onshore authority. As Wise argues, "in the age of instant telecommunications, insularity is not determined by geography. Today, offshore banking centers are not necessarily physical islands set off by the oceans; rather, they are islands surrounded by a sea of regulation" (Wise, 1982, p.300). For the Caribbean OFCs, the USA is the most significant onshore regulatory authority. The initial development of the Bahamas and Cayman OFCs was very much tied up with US efforts to defend the Bretton Woods geo-political economy, a state-territorial regulatory framework with the dollar at the centre.

As Triffin pointed out in 1960, the Bretton Woods international monetary system was bedevilled by a dilemma: how could the dual goals of lubricating increasing volumes of international trade, and maintaining confidence in the dollar as the international measure of value be achieved when the dollar was backed by a relatively inelastic stock of gold? (Triffin, 1960). This dilemma was heightened by the increasing internationalization of business, dollar investments abroad, US expenditures on the Vietnam war, and the resultant growth of dollar holdings outside the regulatory reach of the USA.⁰ The US faced the related problems of an increasing balance of payments deficit⁰ and doubts about the stability of the dollar. To finance the balance of payments deficit, more dollars were printed; this made holders of dollars more doubtful that their holdings could and would be

⁰ By 1964 the value of foreign holdings of US dollars exceeded the value of US gold reserves (Volcker and Gyohten, 1992).

⁰ By current standards the balance of payments deficits of around \$2 bn per year may seem insignificant, but at the time they were large and a threat to the stability of the international monetary system and the position of the US within it (Volcker and Gyohten, 1992).

redeemed for gold. These trends threatened to undermine the role of the dollar and the Bretton Woods international monetary system. In an effort to tackle these problems and defend the Bretton Woods system the US introduced a series of capital controls and financial regulations. By restricting the outflow of dollars the US hoped to regain control of its currency, address its balance of payments deficit, and restore confidence in the dollar.

The first measure considered, by the Kennedy administration in 1961 and 1962, was a tax reform. This was intended to strengthen US trade and goods exports at the expense of capital export growth by eliminating foreign tax credits. However, it was strongly opposed by US multinationals and never implemented. The second measure, enacted in 1963, was the Interest Equalization Tax (IET). The IET acted as a tariff, influencing the supply and demand of capital indirectly through the market by increasing the costs of new US issues of foreign equities in an effort to minimize capital outflows. The IET was intended as a temporary measure but was renewed every two years until 1973, with vigorous opposition from the transnational banks at each renewal. In his pioneering but neglected book *Dollars and Borders*, Hawley explains that:

“The IET stimulated the initial rapid growth of the Eurocurrency system in 1963, promoting the internationalization of finance. In so doing the IET aided in denationalizing the Eurocurrency system by placing it beyond the effective control of national governments and international agencies, ultimately creating a financial structure which was instrumental in the downfall of the dollar in 1971” (Hawley, 1986, p.62).

Hawley goes on to describe the capital controls program which was instituted on a voluntary basis by President Johnson in 1964 and made mandatory in 1968. The capital controls program aimed to limit US foreign direct investments, US deposits in foreign banks, and the holdings of foreign assets by US transnational banks and the largest US transnational corporations. These capital controls shaped the development of international finance from the mid-1960s until they were cancelled in 1974 in belated realization that the regulations had been circumvented. As one commentator wryly observed, “banks did not invent the Euromarket. Governments created it by seeking to control the

natural flow of money” (Aliber, 1979, p.19). Johns explains further how “national friction structures and distortions” in the US regulatory environment stimulated the development of the Euromarkets and offshore finance (Johns, 1983). Prohibitions on inter-state banking (McFadden Act, 1927), the divide between commercial and investment banking (Glass-Steagall Act, 1933), and the existence of interest rate ceilings (Regulation Q) and reserve requirements (Regulation D), hindered the on-shore competitiveness of major US banks and pushed them off-shore. So, the Euromarkets, dollar-denominated offshore business based chiefly in London, developed rapidly, and were given a further boost when OPEC’s inflated petrodollar earnings were deposited in, and recycled through, the Euromarkets after the 1973-4 oil shock (Helleiner, 1994b; Martin, 1994).

Some of the smaller banks, faced with the high infrastructural costs of a London base realized that the Caribbean OFCs offered a 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 - and moved their Euromarket operations to the emerging Caribbean OFCs. In addition these centres offered a secure, politically stable environment, 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 five to 164 branches (Johns, 1983, p.29). The development of the Bahamas and Cayman OFCs has always been influenced by regulatory practices in the USA. In fact, as Edwards laments, “the remarkable development of offshore dollar banking is at bottom a history of regulatory myopia, together with a good bit of regulatory mismanagement” (Edwards, 1981, p.6).

As the dollars flowed offshore, the US lost control of its currency and ultimately had to abandon its commitment to the Bretton Woods international monetary system, cutting the promised link between the dollar and gold, or, “closing the gold window” (Gowa, 1983). However, the US has never abandoned its desire to control or regulate its dollars and/or the offshore spaces through which its dollars flow. The dollars’ escape from the regulatory and supervisory clutches of the US authorities, although initially for reasons of profitability and competitiveness, led to further problems for the US, particularly as the activities hosted by the OFCs were largely hidden by strong secrecy

laws. The USA, particularly the Treasury and Justice Departments, has long been opposed to the development of the Bahamas and Cayman OFCs.⁰ The OFCs have undoubtedly facilitated tax evasion and avoidance by US citizens, and the laundering of money from narcotics trafficking and organized crime. As one commentator suggested: “The Bahamas [and other OFCs] must do things which are not allowed in the US because to do things which are allowed in the US is non-competitive, since in every instance the US does it better than the Bahamas do. The Bahamas are therefore compelled in banking and trust operations to appeal to unallowable activities and by inference to appeal to activities disallowed in the US” (Blum, 1984, pp.144-5).

So, the US has tried to limit the role of OFCs, to regain control of its dollars, and to boost the competitiveness of US-onshore banking. The US strategy has had two parts: trying to entice the dollars back onshore; and, trying to regulate the offshore territories. As Wise puts it, when regulations are undermined “policymakers are presented with just two options. Either they must seek to mitigate regulations in the direction of conditions existing in the external market, or, conversely, they must seek to gain control over the external market” (Wise, 1982, p.312). US agencies have tried, with some success, to regulate the offshore territories by reshaping the regulatory landscape, extending US legal power extra-territorially into the offshore jurisdictions (Hudson, 1998). However, in this chapter, my focus is on US efforts to entice the offshore dollar onshore.

OFFSHORES ONSHORE: INTERNATIONAL BANKING FACILITIES

Given that the major attraction of Bahamas and Cayman OFCs is their relatively ‘unregulated’ environment, and that financial capital is potentially highly mobile, OFCs’ development is necessarily intertwined with developments elsewhere in the financial regulatory landscape. One might expect onshore deregulation to erode the competitive advantage of offshore jurisdictions. As the Governor of the Central Bank of The Bahamas commented: “technological advances together with global deregulation and liberalization of financial markets have undoubtedly intensified competition and may

⁰ This simplifies things somewhat. US banks, US companies who receive inward investment via the OFCs, and US citizens who make use of them, are clearly not opposed to their existence. However, the US Government and its agencies have certainly sought to restrict the development of OFCs (Hudson, 1996).

well reshape the contours of offshore financial activities permanently” (Smith, J., 1990). The OFCs’ positions as places in a relational regulatory landscape are modified by regulatory changes elsewhere.

Since the mid-1970s and the ‘Mayday’ deregulation of the New York Stock Exchange, a deregulatory trend has swept across international financial markets leading to, for instance, London’s ‘Big Bang’ of 1986. Also, in 1986 a Japanese Offshore Market was established, offering a liberal regulatory environment based in Tokyo. This facility proved to be attractive to international financial business attracting \$400 bn of funds in its first two years (Johns and Le Marchant, 1993, p.77), but in terms of impact on the Caribbean OFCs a similar move to establish International Banking Facilities (IBFs) in the USA was of greater importance, a move which was described by the Financial Times as a ‘carrot’ to entice offshore business to US shores (Financial Times, 28/11/83). As Wise suggests, “the United States threw a lasso around the Bahamas and the Cayman Islands, in order to pull the operations transacted there back to the American shore” (Wise, 1982, p.300).

IBFs came into existence on the 3rd of December 1981 and permitted the establishment of banking entities, in reality another column in a spreadsheet rather than a physical bank, in the United States, which would be subject to less stringent regulations than international banks in the US were used to. Specifically, there would be no reserve requirements (in contrast to the 3% imposed by regulation D), no interest rate ceilings, and banks would be exempt from the 48 hour ‘notice-of-withdrawal’ requirement. Foreign banks and official institutions were permitted to place ‘overnight funds’ in IBFs to take advantage of short term interest-rate differentials. As two officials from the Federal Reserve Board recalled: “the purpose was to allow these banking offices to conduct a deposit and loan business with foreign residents, including foreign banks, without being subject to reserve requirements or to the interest rate ceilings then in effect” (Key and Terrell, 1988). IBFs offered an escape from some of the regulations that had pushed banking offshore in the 1960s and 1970s. In order to ensure that the IBFs remained an international wholesale banking market, individual and small-scale clients were discouraged from using them; a minimum withdrawal/deposit limit of \$100000 was set; and individual clients had to give 48 hours notice of withdrawals; and, most significantly, US citizens were not permitted to use them.

Developing Offshores Onshore

The idea of facilitating ‘offshore’ banking onshore, complicating the relationship between territorial states and their regulatory jurisdictions, had been around for a long time before the establishment of IBFs in 1981. A ‘foreign window’ for international banks based in New York had been proposed by one Governor of the Federal Reserve Board in 1969 as a way of avoiding the restrictions imposed by the capital controls programme, but this was rejected by the Federal Reserve Board due to concern about the potential effect on monetary policy (Key and Terrell, 1988; Johns, 1983). In 1977, the Chairman of Citibank, Walter Wriston, revived the idea of IBFs and in 1978 the idea received the support of the New York Clearing House Association and the New York State and City authorities who agreed to free international banking from their taxes if the Federal Reserve Board would approve IBFs. Approval was given in 1979, and detailed legislation was drawn up and passed in June 1981.

This brief history of the IBFs proposal hints at the complexity of negotiations, actors, and motives that led to their establishment. Prior to 1981 no agreement could be reached between the interested parties - the Federal Reserve Board, international banks, and City and State authorities - but eventually all parties felt that they could get something out of IBFs. Hawley describes the mixture of motives behind the IBFs, saying that “while transnational banks wanted to use the IBF as a wedge for deregulation, Federal Reserve officials saw it as a way to make the best out of a bad Eurocurrency situation” (Hawley, 1986, p.139). An official of the Federal Reserve Board, when asked why IBFs were set up, responded:

“Briefly, the large US money center banks had been down here for five years previous asking us to do it. They had this grand vision that London was going to migrate to New York, and all the jobs. We didn’t quite see it that way and kind of dragged our heels on it. We thought, you know, we’d lose control of the monetary aggregates if you had all this reserve free banking going on in the US. Ultimately they wore us down ... New York State passed some tax legislation, contingent on us approving IBFs. To give the banks relief they would basically say

that IBFs are not a part of New York's tax base. And that pushed us a little harder. You know, if New York State was going to go that far it was hard for us to stand in the way" (Simons, Personal Interview, Washington D.C., 1994).

The US banks, and particularly the New York-based ones, supported the IBFs proposal as they wanted to maintain their competitiveness and that of New York as a financial centre. They wanted to be able to conduct international banking business from the US rather than having to go overseas. The motive of the New York State and City authorities in supporting the IBFs proposal was to generate employment. An interview with one of the architects of the IBFs illustrates this:

"In New York State it was a fairly simple proposition. Who was behind it? The State was behind it because the burdens of operating in New York State, the taxes etc., were very high compared to say Chicago. By creating an IBF you lower the tax structure, and all kinds of things happen. So in this case it was a desire to keep New York the centre of the financial community in this time zone, and to make the cost structure as reasonable as possible for the participating banks. That's really what happened. There were lots of other reasons but that's what it came down to. It was thought that there would be benefits ... employment, keeping the banks here instead of moving offshore. You see, for example, if you're a foreign bank here, with the taxes and all the other costs that are involved, you might say 'whoa, I don't do that much business, I'll use the Cayman Islands or go to the Bahamas.' So it's employment, taxes, and so forth. There are a lot of benefits" (Hughes, Personal Interview, New York, 1994).

A banking regulator at the Federal Reserve Board also talked about the motives of New York State in supporting the IBFs proposal. He said: "Well there was first this notion that you could attract this business here onshore. The Federal authorities were basically ambivalent although supportive of the notion of these IBFs. The effort was really driven by the States, especially the State of New York, who believed that this would lead to increased employment, increased business" (Lane, Personal Interview, Washington D.C., 1994). Other interviewees argued that the Federal Reserve Board

eventually supported the proposal as a way to enhance their regulatory powers. A representative of the American Banking Association argued that:

“The feeling was that US banks were going outside the US, were escaping oversight and regulation, so there was concern by the bank regulators that maybe there were things going on that were being pushed outside the US, out of the view of their safety and soundness attempts, that it was better to loosen the regulations in the US, on a restricted entity basis, so you can keep a closer watch on them. So for that it had to be the regulators that were driving these moves” (Thompson, Personal Interview, Washington D.C., 1994).

A further regulatory motive was assigned to Federal Reserve support for IBFs, with some interviewees suggesting that they were intended to sort out the offshore wheat from the chaff, as legitimate business would now have no reason to use the OFCs. A Federal Reserve official explained that:

“We installed in the US an international banking programme about five, seven, maybe ten years ago, which was designed to provide the benefits of an offshore centre as it relates to taxes, reserve requirements, and depository insurance relief, under the mis-guided belief that we could attract all this business right here in the US. It would then differentiate between those conducting legitimate, loosely, versus illegitimate business” (Lane, Personal Interview, Washington D.C., 1994).

Hawley suggests that the Federal Reserve Board’s shift of position to supporting the IBF proposal in the late 1970s was linked to negotiations with the UK about the international regulation of banking; the Federal Reserve Board hoped to use the IBFs proposal to pressure the UK to accept internationally coordinated banking supervision. The development of IBFs was certainly a complex process, and a somewhat bizarre situation. One commentator asked rhetorically: “how do we find ourselves in the extraordinary position of having to create special banking facilities to repatriate to the US a gigantic financial market whose principal commodity is none other than our own currency?”

(Edwards, 1981, p.6). The answer to this question lies in the de-linking of US dollars from US territorial regulation since the development of the Euromarkets.

The End of Offshore?

Many commentators predicted that the introduction of IBFs would result in the return of much of the Eurodollar business that took place in London and the Caribbean to the US. Ashby estimated that by 1990 London's share of the Eurodollar market would decline from 32% to 20%, that of the Bahamas/Cayman would fall from 11% to 2%, and New York's share would increase from 0% to 18% (Ashby, 1981; Johns, 1983, p.235). Such quantitative predictions of the decline of offshore centres were complemented by the gleeful hopes of many US commentators. Ashby suggested that "the main effect of the introduction of IBFs ... will be to dull the shine on those brass plates, as US Banks will shift their Eurocurrency operations back home" (Ashby, 1981, p.97), and Ireland remarked that "the US Federal Reserve Board's decision to grant permission for the establishment of offshore banking facilities in New York has sent a small frisson through those Caribbean central banks which currently host the Eurocurrency operations of US banks" (Ireland, 1981, p.51). Another commentator, (obviously not accepting the argument that all markets are regulated institutions!), argued prematurely that "this result is not surprising since the Caribbean markets are more the result of US regulation than the result of market forces" (Campbell, 1982, p.537). While many US commentators predicted and hoped that IBFs would signal the end of OFCs, financiers in the Bahamas, although worried, did not entirely accept such views. The Governor of the Central Bank of the Bahamas, William Allen, told the Financial Times that "New York clearly poses a threat. But at present we are more worried by Miami. In any event a big hole could be knocked in our offshore banking business as we know it today. And we are well aware of the need to respond to a changing situation" (Financial Times, 17/3/81).

The Nassau Guardian reported Allen's comment that "the position that the international banking facility spells doom for offshore activity in the Bahamas appears, however, not to be substantiated". Backing up this assertion he explained: "It seems therefore that foreign banks operating in the Bahamas are hardly likely to be keen on moving their operations from their Bahamian

locations to US offices where they would deny themselves the advantages and benefits which motivated them to establish operations in the Bahamas in the first place” (Nassau Guardian, 28/1/81).

Not the End of Offshore

Many IBFs were established in a short time from the 3rd December 1981, the first day when they were permitted. By the 1st of September 1982, 395 IBFs had been established in the USA, of which 176 were in New York (Johns and Le Marchant, 1993, p.76). The initial rapid growth of IBFs, with assets of \$63 bn by the end of the first month, was due to the repatriation of funds from London, Luxembourg and Nassau (Walmsley, 1983). Walmsley estimates that US banks’ funds deposited in London and Caribbean branches fell, respectively, by 11% and 40% between November 1981 and July 1982 (Walmsley, 1983, p.85). But this initial rapid growth did not continue. Figure 1 compares the amount of international banking activity (external assets) taking place in IBFs from 1981 to 1991 with that hosted by the Bahamas and Cayman from 1977-1991. By December 1987, 540 banking institutions had established IBFs, with external assets of \$281 bn. New York IBFs accounted for 75% of IBF activity. This compared with London’s \$428 bn and the combined Bahamas/Cayman external assets of \$241 bn (Key and Terrell, 1988; BIS International Banking Statistics, 1993). In contrast to Ashby’s prediction of 18% of Eurodollar business being based in New York by the end of the decade, by 1988 IBFs hosted only 7% of total international banking, with New York IBFs hosting less than 6% (Key and Terrell, 1988). From 1989 to 1991 the volume of IBF external assets actually decreased from a peak of \$343 bn to \$291 bn, whilst activity in the Bahamas and Cayman increased from \$297 bn to \$362 bn.

The IBFs neither persuaded the London Eurodollar market to migrate to New York, nor spelled the end for traditional offshore centres. However, there was certainly some loss of business from the Bahamas and Cayman. Representatives of the Bahamas offshore financial community accepted that “unquestionably US banks, and possibly some others, have transferred part of their external positions from the books of their Nassau branches to the books of their IBFs, preferring central administration of assets and liabilities from a base such as New York” (Central Bank of the Bahamas and AIBT, 1986, p.10).

The transfer of business by some of the major American banks with Eurodollar booking centres in the Caribbean was described by an ex-Governor of the Central Bank of The Bahamas as a ‘political’ move. He explained that:

“One of the banks that played a very important role, an important political role, in the development of IBFs, was Citibank. Citibank was in the Bahamas. Once the legislation was approved Citibank had almost to make a political response to it, to move to New York from the Bahamas. It did this and as a result some of the American banks pulled their offshore operations back to the US. Certainly the New York banks did that to a great extent, and so obviously the footings changed. But the Swiss banks and the other non-American financial operations, they didn’t feel the need to respond to the IBFs” (Talbot, Personal Interview, Bahamas, 1994).

The impact of the IBFs on the OFCs was far from simple; in fact, as US residents were not permitted to use them it resulted in a rather strange situation. As a Federal Reserve Board publication noted: “the current regulatory situation has produced a paradox: non-US residents are now encouraged to conduct their banking transactions in the United States, while US residents have incentives to book their transactions, particularly their deposit accounts, offshore” (Terrell and Mills, 1983, p.12). Therefore, even though many US banks established IBFs they tended to retain their Caribbean entities too. As a central banker in London put it: “lots of IBFs were set up but few banks closed their Caribbean presence. In many cases IBFs and the Caribbean operations were both operated from New York anyway, by the same people as two books, so the entities were used selectively depending upon the specific case” (Gilling, Personal Interview, London, 1993). Without exception, interviewees in London, the US and the Caribbean centres acknowledged that the impact of the IBFs had been less than expected. Key and Terrell conclude that “IBFs have not turned out to be the dramatic innovation that some had predicted and that IBFs simply provide another center for booking transactions with foreign residents in a regulatory environment broadly similar to that of the Euromarket” (Key and Terrell, 1988).

Why Not the End of Offshore?: The path-dependence of place

The IBFs failed for a variety of reasons: economic, political, social, and, historical. Economically, in terms of their potential profitability and flexibility, they were at a competitive disadvantage in relation to the OFCs. A Federal Reserve report acknowledged that the IBFs still impose more restrictions on international banking than other Euromarket centres do. These restrictions include: the fact that IBFs cannot do business with US residents; a minimum maturity period of 48 hours for non-bank foreign residents; a minimum transaction of \$100000 for non-bank customers; and the fact that IBFs cannot issue negotiable instruments (Key and Terrell, 1988; see also *Financial Times* 29/5/84). A regulator in the US explained to me that “banks can do more things and they have more flexibility in the Bahamas” (Evans, Personal Interview, Washington D.C., 1994).

A second set of reasons for the IBFs’ failure related to the fact that potential investors did not see US ‘country risk’ as particularly advantageous. One of the supposed key attractions of IBFs was that they would avoid restrictive onshore regulations (which we have seen to be only partly true), and yet offered US country risk, a risk which was assumed to be lower than that experienced in the Caribbean OFCs. However, a Federal Reserve Board report explained that in an age of consolidated banking supervision ‘sovereign risk’ has lost much of its meaning:

“The view that depositors would perceive clear advantages in the sovereign risk associated with deposits subject to US law does not seem justified. Sophisticated international depositors do not appear to perceive a significant difference in sovereign risk between deposits at branches of a US bank located in other major international financial centers and deposits at that bank’s IBF in the US; in both cases the deposits are backed by the US bank, which is supervised on a worldwide consolidated basis by US bank regulatory authorities” (Key and Terrell, 1988, p.28).

However, the most important reasons for the failure of the IBFs to bring the offshore dollar back home were social and historical. A particular issue was concern about US authorities’ access to account information. A representative of the Central Bank of The Bahamas explained that “the idea

behind the IBFs was to bring onshore the offshore dollar. It has not worked. It has not worked for a very simple reason. The banks don't want full disclosure. The banks don't care about the money being back onshore, the Federal government want it back onshore. They want to be able to control that money" (Johnston, Personal Interview, Bahamas, 1994). As Key and Terrell put it, "some nonbank customers may want to keep their accounts outside the United States for reasons of secrecy because they view such accounts as subject to less scrutiny by US and other authorities than an account at an IBF" (Key and Terrell, 1988, p.21). More colourfully, Miller contrasted the offshore centres with the IBFs: "In the Caymans, the banks work for you. In the US, they work for the IRS [Internal Revenue Service], your ex-wife, and whoever else wants to know your financial position" (Miller, 1981, p.41). Offshore money has always been about secrecy and confidentiality as well as profitability.

The impression gained from interviews in the Bahamas and Cayman was that clients, particularly those from Latin America who are familiar with the heavy-handed approach of the US, were very wary of placing funds in the US, even if for regulatory purposes they were supposedly offshore. A Bahamian lawyer clearly described why a client might not wish to use an IBF:

"If people are looking at moving away from their regulatory authorities they don't go in the same country to set up entities. If you're within their borders you're still subject to their control, their disclosure, and to their ability to penetrate the system. You're literally right in their yard. So those who are still looking to have funds which are coming from international sources, not be subject to possible disclosure or knowledge of their [US] authorities, will not use the IBFs. They will use the OFCs or other countries outside of the US" (Young, Personal Interview, Bahamas, 1994).

Although legislation is necessary in the creation of an attractive space for international finance, it is not sufficient. Legislation could not change the fact that IBFs were still in the USA. Legislation could not erase the memory of previous efforts by the US to access confidential account information (Hudson, 1998). Although the IBFs were supposed to provide 'offshore' facilities from

New York and other US cities, a regulator in Cayman clearly explained the fear that other US regulatory and enforcement authorities would gain access to account information:

“It didn’t work because people don’t have confidence in the US system in being able to separate out different zones. They don’t have confidence in the fact that they can have an IBF that can have information in it that can’t go to other sections. If the Department of Justice has something then of course the IRS has it etc. Unfortunately the US doesn’t have that good a record with being able to streamline and isolate their different departments” (Fry, Personal Interview, Cayman, 1994).

A representative of the Central Bank of The Bahamas explained another concern, namely the reversibility of the IBFs legislation: “Some of them would open an IBF but they kept their same operation offshore because if one government brought in the legislation, another government could take it out, and that has been the history of banking legislation” (Johnson, Personal Interview, Bahamas, 1994). Legislation could clearly be altered in the OFCs too, but the point is that the legislative history of the offshore centres does not include such swings in policy. As Yassukovich suggested, “it is perhaps too early to assess the degree of commitment of the US authorities for the IBF concept. Abrupt regulatory changes in the United States are not unknown” (Yassukovich, 1981, p.253). The past history and reputation of the US and its regulatory authorities meant that banks and customers lacked confidence in the IBFs. Situated within a jurisdiction remembered for regulatory changes and an inability to resist looking into the financial affairs of people and institutions, IBFs and their regulatory authorities were not trusted. As Wise suggested, “although the US is recognized as a low political risk, it may be regarded as a significant regulatory risk. The past capital and credit restraint programs and more recently the freezing of Iranian assets held in US banks are examples of such regulatory actions. This history may be the most significant determinant of whether International Banking Facilities are able to attract the degree of the external market that many proponents claimed” (Wise, 1982, pp.328-9).

A regulator at the Federal Reserve Board in Washington D.C. got to the heart of the matter, explaining that IBFs are purely fictional entities created by legislation:

“Well banks had been operating the Nassau books, or the Cayman Islands books, or the Netherlands Antilles books on premises for years. I mean they already had a structure in place to do this. All you offered them is a different title on top of the spreadsheet, computer run, listing of customer business. So for these banks they didn’t need a whole cadre of people to come in and do something they were already doing” (Lane, Personal Interview, Washington D.C., 1994).

A representative of the American Bankers Association described the IBFs as “no big deal” and, invoking a path-dependence argument, said that “these bases have been well established for international monetary flows and, perhaps if we’d always had IBFs in the US they wouldn’t have started in these OFCs, but since we haven’t they’ve been very functional” (Thompson, Personal Interview, Washington D.C., 1994). The (financial) genie was pushed out of the (US regulatory) bottle in the 1960s and could not now be persuaded to return.

CONCLUSIONS: MONEY RULES OR PLACING TRUST?

The development of IBFs played an important part in the development of the Caribbean OFCs, spurred on processes of financial globalization and liberalization and contributed to the construction of a post-modern geo-political economy. New monies and new geographies were created together. Money flows, linking the fortunes of onshore with offshore. Jurisdictions may seek to attract these flows through the construction of attractive regulatory environments. For some commentators, the resultant processes of place competition lead to the ‘end of geography’ (O’Brien, 1992). Even for Harvey, whose Marxist political position is in stark contrast to O’Brien’s free-marketeering preferences, “commodity exchange and monetization challenge, subdue, and ultimately eliminate the absolute qualities of *place* and substitute relative and contingent definitions of places with the circulation of goods and money across the surface of the globe” (Harvey, 1985, p.11). Harvey and O’Brien both suffer from an excess of economic reasoning. Although I find Harvey’s

analysis of uneven capitalist globalization more persuasive and useful than O'Brien's homogenization thesis, I would argue that although money flows link the fortunes of places they do not dissolve their differences. Places are not purely economic nodes⁰ and, as long as they are peopled, never will be (see also Thrift, 1994 and Leyshon and Thrift, 1997 on the 'social and cultural determinants of international financial centres'). The history of places is not easily transferable, and their more or less trustworthy reputations cannot be legislated away.

The development of IBFs illustrates this, both in the attempt, and, in the failure, to bring the offshore dollar onshore. The attempt shows that places can be partially constructed through legislation. The failure however, is more interesting, illustrating that money and the places between which it flows are social and historical, as well as economic. The IBFs failed for economic, political, social and historical reasons.⁰ Economically, the US regulatory authorities - clinging to a disappearing dream of sovereignty - were unwilling to construct the IBFs as truly offshore centres. Financial activity in these onshore offshores remained more restricted and less potentially profitable than in the Caribbean centres, which, in contrast, made fruitful use of their remaining legal sovereignty. As Dodd puts it: "Offshore transactors rely on the strength and consistency of the monetary and fiscal sovereignty of individual states. It is from differences between individual regulatory environments - which are based on the sovereign right of each state to legislate independently - that commercial incentives are derived" (Dodd, 1994, p.100). In addition, in a globalizing political-economy with globally consolidated banking supervision, US 'sovereign risk' provided little incentive for offshore dollars to return to the USA. However, it is the social and historical reasons for the failure of IBFs which are the most illuminating. Offshore money has always been about secrecy or confidentiality as well as profitability. Many banks and their wary customers did not trust the US regulatory authorities, fearing that they would continue - as they had historically - to pry into their financial affairs, and to pass this information around government departments. Neither, in memory of the historical record, did banks and customers trust the USA to retain the IBFs over time; as a legislative decision, it could

⁰ The development of cyber-space banking may well provide an interesting arena in which to explore this idea further!

⁰ We might opt, alternatively, to totally deconstruct 'the economic', lumping everything together as 'the social'. But, although it is impossible to draw clear fixed boundaries around aspects of social life, temporary conceptual boundaries seem to me to be important for the practice of critical social science (compare Thrift and Olds, 1996).

be reversed. Finally, and again because of historical path-dependence, once banks and their customers had grown to trust the Caribbean OFCs they were reluctant to switch their allegiance to the IBFs. If OFCs had never existed it might have been different, but they had, so it wasn't.

The failure of IBFs illustrates that financial space is made up of social and historical places rather than abstract timeless nodes in an economic network. Money flows and the development of financial spaces are only partially explained by economics. Money is more than economic; flows of money are not solely determined by potential profits. As Dodd puts it: "it is not at all clear that international monetary networks mark the emergence, teleologically as it were, of a market stretching across geopolitical boundaries whose operation approximates more and more closely to a perfection derived from economic reasoning" (Dodd, 1994, p.102). In suggesting that, "as a universal equivalent, money becomes a form of communication about economic value, which can link social actors separated by vast tracts of space and time" Leyshon (1996, p.65) marginalizes, but does not erase, the sociality of money. Money remains a social relation; the communicating actors are social. Their reasons and actions are communicative rather than purely economic and instrumental. For their communication to succeed there must be trust. Places and peoples are more or less trusted; their past is remembered in their present. Money is a socio-historical geography.

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