COGS IN THE MACHINE: SMALL STATES, FINANCIAL CRIME, AND GLOBAL CAPITALISM

An Interview with Michael Hudson

Michael Hudson is a senior editor at the International Consortium of Investigative Journalists. He worked as a reporter, writer, and editor on ICIJ's Pulitzer Prize-winning Panama Papers investigation and on ICIJ's FinCEN Files probe, which was named a Pulitzer finalist. He has also served as a staff writer for the Wall Street Journal *and as global investigations editor at The Associated Press. The* Journal of International Affairs *spoke with him to discuss the roles small states play in the offshore financial system, agency and power in an era of globalized capitalism, and the ever-changing nature of international finance and taxation.*

A note from the editors: this interview was recorded and has been edited and condensed for clarity.

Journal of International Affairs (JIA): *You're a Senior Editor for the International Consortium of Investigative Journalists (ICIJ). Can you describe for readers what ICIJ is currently working on?*

Michael Hudson (MH): As long as we're around, ICIJ is going to continue to report and write about the offshore financial system. But we also have other kinds of stories that we're doing, some of which aren't necessarily about offshore, but are maybe still about smaller states. Stay tuned for those. As you may have seen this year, we've done a series of stories about the telecom giant Ericsson and its problems with illegal payments around the world, especially in the Middle East.[i] In July, we came out with a new project about Uber and its lobbying and influence operations around the world seeking to change laws or even evade laws.[ii] The Uber story reflects

[i] International Consortium of Investigative Journalists, "The Ericsson List," https://www.icij.org/investigations/ericsson-list/.

[ii] International Consortium of Investigative Journalists, "The Uber Files," https://www.icij.org/investigations/uber-files/.

the themes of everything we do, which is ultimately about creating transparency and fighting corruption and exposing the people and systems who enable it.

We're also going to continue to follow up on all our offshore projects. There are new developments all the time: there's always new legislation and new scandals, so we continue to follow up because the offshore system is entrenched, the system is powerful, the system is smart and adaptable. And the only way to bring about change is to just keep pushing and hacking away at these issues. As Teddy Roosevelt once said: "There is mighty little good in a mere spasm of reform."[iii]

JIA: *On ICIJ's homepage today are stories involving a bribery case in Djibouti, a profile on Delaware as a "low profile tax haven," and a tax evasion scheme run through Mauritius, among others. Is it fair to say that small states and jurisdictions are at the center of financial crime?*

MH: I would say no, in the sense that I don't think they are at the center of the system. They are key cogs; they are very important parts of the offshore system. They're part of the connective tissue, and the offshore system would not operate, or would operate much differently, if they didn't exist and weren't part of it.

The thing about the offshore system is that people often say, "So-and-so moved their money offshore." That doesn't necessarily mean the money resides in Belize or the British Virgin Islands or Seychelles. That means the money is probably in a Western bank, because if you have money, you want to be able to spend it. But first, if the money involves ill-gotten gains, you need to launder it to disguise its ownership. You might have a trust in Belize that is controlled by a shell company in Cyprus that in turn is controlled by a shell company in Hong Kong whose directors are not human beings but rather another shell company created in Seychelles, and on and on. But eventually, if you're, say, the son or daughter of a corrupt dictator somewhere in the world, you're going to want to be able to spend that money shopping in London and New York. So you're going to have a US bank account, or a bank account in London. And often one of the key steps in money laundering is turning local currency into US dollars, because the US dollar is the de facto global currency. That conversion helps make dirty money appear cleaner and makes it easier to spend, easier to move.

The key here is that the offshore system is truly a global system, not just a hodgepodge of far-flung island hideaways. It's a machine that's all about interconnection, all about linking together multiple jurisdictions. Financial

[iii] Theodore Roosevelt: "There is mighty little good in a mere spasm of reform." Speech given April 14, 1906.

secrecy is a product that is bought and sold. The more secrecy you want, the more you pay. If you just want basic secrecy, you can have a bank account in New York that, on paper, is controlled by an anonymous shell company in the British Virgin Islands. That's pretty simple. But that's an easier trail for investigators and even ex-spouses or tax authorities to follow, so you might want to have what's called "layering." The more layers of companies and trusts between you and your bank account, the more secrecy there is. And that's why all of these smaller jurisdictions, in particular island nations, are so important to the system. They provide the puzzle pieces, the building blocks of hard-to-trace shell companies and trusts, that make layering possible.

The small states play another important role in the offshore system. They draw much of the blame for offshore financial sleaze and direct attention away from the big players, the big Western nations.

After so many years of reporting on these issues, one of the axioms that I've come to embrace is that the smaller and less powerful a jurisdiction is, the more likely it is to be condemned for its role in the offshore system. These smaller, less politically-powerful jurisdictions have been traditionally the fall guys for the offshore system. Almost always the focus in the media, government, and multinational organizations is on the island paradises: the Caymans and the British Virgin Islands in the Caribbean, the Cook Islands in the Pacific Ocean, or the Seychelles in the Indian Ocean. The idea is:

> "They're bad. They're at fault in this. We, the greatest powers on earth, the United States, the United Kingdom, the European Union and its member states, are shocked—shocked—that such a thing is happening. And we're going to work to reform the system and make sure that the British Virgin Islands and the Caymans and all the rest of the bad islands behave."

JIA: *If small states aren't at the center of the offshore system, then who is?*

MH: The most powerful players in the offshore system are really the big Western countries, where all the money is and all the big banks are. A tax expert once said, "The biggest tax haven in the world is an island, and it's either Manhattan or the United Kingdom." They are the central hubs that tie together all the jurisdictions that make up the offshore system—and the vast majority of offshore-flavored cash moves through them or resides with them.

Say you're in the Democratic Republic of Congo and you want to move money and put it in a bank in Switzerland. As we've said, you probably want it to be in dollars. But you can't move dollars around the world in a direct line—you can't move money directly from the DRC or Angola to Switzerland or Belgium, if it's in dollars. It has to first go through a New York bank, one of the big banks that has a license from the U.S. government to move dollars around the world. The dollars have to go from country A to New York and then out to country B.

Many of the biggest banks in the world make substantial profits from these transactions. It's a profit center, through which billions and billions of dollars are passing and a small percentage for each transaction is earned as profit, just for being a middleman for each of these transactions. They make lots of money without putting any of their own capital at risk. This creates a disincentive for them to look too closely at who's moving this money and whether the money might be the proceeds of crime and corruption or is fleeing oversight from law enforcement and tax authorities. Our 2020 FinCEN Files investigation,[iv] in partnership with BuzzFeed News and other media outlets, found that five global banks—JP Morgan Chase, HSBC, Standard Chartered Bank, Deutsche Bank, and Bank of New York Mellon—profited from suspect transactions, even after they paid fines to U.S. authorities for previous anti-money laundering failures and in some cases signed deferred prosecution deals. The fines that these banks were forced to pay were basically the cost of doing business.

Meanwhile, the United States, and to some degree the UK and the EU, have set themselves up as the global cops responsible for fighting offshore-enabled financial crime. Since they are not necessarily going to go after themselves or go after each other, they're going after the smaller players. It's the little guys who are met with threats of economic blacklists and sanctions. There's a really great paper by Steven Dean at Brooklyn Law School and Attiya Waris at the University of Nairobi called "Ten Truths about Tax Havens: Inclusion and the 'Liberia Problem.'"[v] They call the US a "superhaven:" it's a state that can combine secrecy and attractive rates of investment return. That's really a quantum leap over what other tax havens offer, especially smaller tax havens that are offering secrecy alone. When you go back to 2000, to the beginning of the global community making noise about doing something about global tax evasion, the big countries that controlled the Organisation for Economic Co-Operation and Development were searching, as Dean and Waris put it, "for an explanation for the failures of the international tax system" that the OECD had overseen for decades. Liberia was put on a blacklist, along with a handful of others—but none were the big players. As Dean and Waris note, the OECD did not see war-

[iv] International Consortium of Investigative Journalists, "FinCEN FILES," https://www.icij.org/investigations/fincen-files/.

[v] Steven Dean and Attiya Waris, "Ten Truths About Tax Havens: Inclusion and the 'Liberia' Problem," *Emory Law Journal* 70, no. 7 (2021), Brooklyn Law School, Legal Studies Paper No. 670, https://ssrn.com/abstract=3822421.

ravaged Liberia as a state spiraling into more years of brutal killing, it "saw a 'gangster' willfully engaging in 'harmful tax competition'."

Their argument is that this is simply a scapegoating of smaller countries, smaller jurisdictions. When I spoke to Dean about his paper, he said that the big nations, the rich nations, don't actually want the system to change in a way that harms their own economic self-interests. He said that offshore secrecy and tax avoidance are "not a breakdown in the system: this is a machine operating as it is supposed to work."

JIA: *You describe the system as a "machine." Is it correct to think of this all as a system, a club, a network? What's the proper framework for understanding these reports and discussing financial crime more generally?*

MH: The "machine" analogy isn't perfect. I guess a machine is often an agglomeration, a series of connected systems that are put together to create the machine.

It certainly is a global system, a global machine that allows money laundering and tax dodging to flourish. The best estimates are that only a fraction of 1 percent of dirty money—money that's being laundered, money that's being hidden, money that would be considered ill-gotten gains—actually gets intercepted and caught by the world's law enforcement authorities. This means the vast flow of dirty money flows around the world essentially unhindered.

When there are crackdowns against specific jurisdictions, and the United States or the EU or the UK go after, for example, the British Virgin Islands, these big nations will demand change: "You need to tighten up, you need to have better financial transparency, and the financial and corporate gatekeepers within your borders need to get better about knowing who their customers are when they're selling them offshore trusts and shell companies."

But once this happens, the machine adapts. The first offshore money investigation by ICIJ was back in 2013 and simply called "Offshore Leaks." Much of it focused on the British Virgin Islands. There was some action based on our reporting but also generally based on what was going on in the world. The BVI is a British Overseas Territory, so the U.S. and other European countries put some pressure on the UK, and the UK then put some pressure on the BVI to do a better job: be more transparent and demand tough anti-money laundering checks for clients buying offshore companies and trusts.

Other tax havens have used this as a marketing point. We saw that in the Panama Papers, our later investigation into a giant offshore-focused law firm based in Panama with satellite offices around the world. Offshore operatives in Panama and elsewhere reached out to people with BVI shell companies, telling them, "There's a real crackdown in the BVI. Money's not going to be safe there anymore. Your offshore company is not going to be as secret as it once was. The perfect solution to that is a Panama offshore company." And then later, after we released the Panama Papers and exposed the law firm and Panama in general for their roles in a lot of offshore chicanery, operatives in other offshore jurisdictions started saying to potential clients, "Panama is basically over. You don't want to have your money controlled by a company based in Panama, because you're not really safe. The only safe place is to come to us. Come to Belize. Come to Singapore. Wherever." It's a whack-a-mole problem, especially if your main strategy is trying to force small microstates, the island havens, to clean up their acts. You slap down one and another one increases its market share, or newer havens rise up to grab part of that business.

If the goal is really to interdict the money, consider the old line from famed American bank robber Willie Sutton: "Why do you rob banks?" "Because that's where the money is." If the goal is really to interdict dirty money, going after these small havens is only going to be a partial, or extremely incomplete, solution. The real way to do that would be to make sure that big U.S. banks and big UK banks are conducting real anti-money laundering checks and investigating their customers. That entails making sure that customers aren't, for example, politicians involved in corruption scandals; or members of criminal networks; or fraudsters running Ponzi schemes.

Almost all the money moving around the world goes through these big U.S. and UK banks, along with German or French banks. That's the choke point: that's where almost all the money's going and where you there could actually have a pretty significant impact. But despite a few efforts in the United States and the UK to slap banks on the wrist for not doing enough to stop money laundering, it's been pretty ineffective, and the show goes on. Dirty money keeps flowing.

JIA: *You previously described small states and jurisdictions as "cogs" in the system: is this function specific to offshore financial services or broader economic dynamics as well?*

MH: With many of the smaller states we've been talking about, the offshore system is the main way they interact with the world economically. But that doesn't mean they don't have a significant role within the global economy. The offshore system isn't a mere sideshow: it's a powerful part of the overall world economy.

As Nicholas Shaxson, a journalist and offshore expert who wrote an insightful book, "Treasure Islands,"[vi] puts it, we'll never truly understand the economic history of the modern world without understanding the offshore system: "Tax havens are now at the heart of the global economy. Their tentacles have curled their way into pretty much everything."[vii]

JIA: *What is the origin of the offshore system? How did we get here? To what extent is the construction and maintenance of this system accomplished by individual actors and their agents, financial institutions, or governments themselves—or is it not possible to make meaningful distinctions among these three?*

MH: Governments definitely played a role in the construction of the system. The laws and regulations they create can allow or impede the marketing of corporate financial structures that enable financial secrecy, money laundering, and tax avoidance.

But of course, a lot of the initiative for passing these laws and rules, and for the development of the infrastructure of the system, comes from non-governmental players: lawyers, accountants, bankers, company incorporation agents, and many others. Among other things, these operatives use their wealth and connections to influence governments to pass laws and regulations that allow them to operate in the manner they desire.

It's important to remember that the offshore system is always an evolving thing. The impresarios and operatives of the offshore system, people outside of government who play a big role, are always inventing new kinds of transactions, new kinds of corporate structures—often in response to attempts to crack down, to limit what they can do. Thus, they come up with new ideas to help them find loopholes, get around new laws, and respond to the pressure.

In terms of the origin of the offshore system, I should note that ever since money and taxes have existed, some humans have tried to avoid taxes and keep their money hidden. Maybe even in civilizations that operated with the barter system, there were those who were hiding or laundering their chickens and spices and bushels of wheat.

Many trace the dawn of the modern offshore system to incorporation laws that passed in New Jersey and Delaware in the late 19th century. As Ronen Palan, professor of international politics at City, University of London, has written,[viii] New Jersey and Delaware were not necessarily tax havens at this time, but they were "the originators of the technique of 'easy

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[vi] Nicholas Shaxson, *Treasure Islands: Uncovering the Damage of Offshore Banking and Tax Havens* (New York: Macmillan, 2011).

[vii] Jeremy Hodges, "Offshore Tax Havens in Spotlight After 200-Year History," *Bloomberg*, May 3, 2013, https://www.bloomberg.com/news/articles/2013-05-03/offshore-tax-havens-in-spotlight-after-200-year-history.

[viii] Ronen Palan, "History of tax havens," History and Policy, October 1, 2009, https://www.historyandpolicy.org/policy-papers/papers/history-of-tax-havens.

incorporation,' which is used by all modern tax havens." In this way, New Jersey and Delaware "invented the technique of attracting non-resident companies by offering amenable regulatory environments." Later in the 1920s, some Swiss cantons copied this practice and brought it to Europe. Then, in 1934, Switzerland passed a law that, for many decades, set the gold standard for banking secrecy and made the term "Swiss account" synonymous with well-hidden wealth.

By the 1960s, Palan writes, British banks were "the principal force behind the development of an integrated global offshore economy centered on London, including remnants of the British empire." UK banks first began expanding their offshore activities in Jersey, Guernsey, and Isle of Man. By 1964, they had been joined by three American megabanks, Citibank, Chase Manhattan, and the Bank of America, in the push to create offshore infrastructure. Chase Manhattan was an early player in the 1960s in the growth in the Bahamas as an overseas financial center. Consequently, it was one of the banks of choice for people with pools of dark money to protect, moving a lot of suspect money and holding a lot of suspect money for powerful figures. Chase was a go-to bank for Philippine president Ferdinand Marcos and the Shah of Iran: strongmen who looted their countries' treasuries during their decades in power. In fact, it's been said that relations between Chase officials and the Shah were so close that in the 1960s and 1970s, Chase chairman David Rockefeller was essentially "the Shah's private banker." Chase even played a cameo role in an offshore money laundering thread of the Watergate scandal, serving as a conduit for an illegal $55,000 campaign contribution that American Airlines laundered through foreign sources and funneled into President Nixon's reelection campaign. Federal authorities fined the airline but apparently took no action against Chase.

JIA: *Chase Manhattan was an early player in the Bahamas. Where do other small states come in?*

MH: In 1966, the Cayman Islands enacted a set of laws that embraced, according to Palan, the "classical tax haven model." The success of European and Caribbean tax havens soon inspired a series of Pacific Island nations to join this offshore gold rush. As Jason Sharman, a Cambridge political scientist, has noted,[ix] between 1970 and roughly 1990, Vanuatu, Nauru, the Cook Islands, Tonga, Samoa, and the Marshall Islands followed one another in copying legislation from the successful havens, offering zero or near-zero taxation for non-residential companies and Swiss-style bank secrecy laws. By the early 1990s, there were something like 60 to100 tax havens around the globe, depending on the definition.

[ix] Palan, "History of tax havens."

Now, in 2022, the Financial Secrecy Index, compiled every couple of years by the NGO Tax Justice Network, lists 141 offshore secrecy jurisdictions worldwide.[x] This includes some small jurisdictions but also some very large ones. The index takes into account both the level of financial secrecy that a jurisdiction has in its laws and the jurisdiction's relative share of the offshore financial market. The index's top ten enablers of financial secrecy in the world currently are, in reverse order: Guernsey, British Virgin Islands, United Arab Emirates, Germany, Japan—as I said, there are some big countries in here—Luxembourg, Hong Kong, Singapore, Switzerland, and the United States. The UK, by the way, is ranked 13th in the index, so while its colonial legacy has helped it maintain a large offshore footprint, its former colony, the U.S., is the biggest player in the offshore system. Tax Justice Network also notes that if you combined Britain with all its affiliated satellite havens around the world, it would be the world's biggest offshore jurisdiction.

Again, that's why I keep bringing up the United States and UK: they really are the biggest influencers, the biggest players, one way or another, in the offshore system worldwide. They also provide a lot of the customers. Many Americans, as well as many Brits, are using the offshore system to move money, hide money, or dodge taxes.

JIA: *It's worth exploring the relationships between financial institutions from large states set up in small states and the governments of the small states themselves. What is that relationship, and just how much power does the government of a Cayman Islands or a Seychelles have in mediating financial institutions or legal frameworks?*

MH: Occasionally, there will be a Western bank that has a branch in one of these jurisdictions, but that's not really how the system works today. Now, Western banks are where they are: they're in New York, they're in Frankfurt, they're in London. What the governments of small offshore havens have control over is the creation of offshore companies and offshore trusts, which are the tools that are used to create the layers of secrecy which then protect bank accounts.

Each individual offshore haven could put a dent in money laundering, financial secrecy, and global tax avoidance by making sure that offshore operatives—the trust companies, the lawyers, and the accountants who operate in their jurisdiction—are actually doing anti-money laundering checks and screening their clients. Some jurisdictions, like the British Virgin Islands, have started to get better at this, although the jury's out as to how much better.

The truth is, most jurisdictions, just like the United States, have eco-

[x] "Financial Secrecy Index 2022," Tax Justice Network, https://fsi.taxjustice.net/.

nomic incentives to only go so far when it comes to oversight and regulation: they want the business. The money that's coming into these smaller jurisdictions isn't necessarily bank deposits: it's the accumulation of fees that clients pay to set up and maintain offshore companies or trusts—a steady flow of money that boosts government budgets and the bottom lines of accountants, lawyers and other offshore operatives.

JIA: *You mentioned that the U.S. states Delaware and New Jersey were among the first to develop incorporation laws, and it is well known that Delaware remains the de facto capital for U.S. corporations. Are individual U.S. states getting in on the business of appealing to wealthy clients, including individuals and corporations?*

MH: Over the past decade or more, while the United States has put pressure on the Caymans, Switzerland and other foreign havens, U.S. states have gotten into the offshore game in a big way. ICIJ's Pandora Papers investigation documented how South Dakota, Nevada, and more than a dozen other U.S. states have transformed into offshore havens peddling shell companies and trusts to people around the world. Customer assets in secrecy-cloaked South Dakota trusts more than quadrupled over a decade, topping $360 billion as of last year.[xi]

The United States has forced other countries to share information about American citizens with money in overseas accounts. But the United States hasn't returned the favor by sharing information with other nations whose citizens have moved money into U.S. bank accounts, shell companies and trusts. The United States has refused to join a 2014 global agreement supported by more than 100 jurisdictions, including the Caymans and Luxembourg, that would have required American financial institutions to share information they have about foreigners' assets.

JIA: *Are states like South Dakota and Wyoming learning from the case study of the British Virgin Islands, for example, and are they drawing in the same clientele?*

MH: They certainly are using many of the same techniques. Have they learned from them? I would think so. And the clientele is essentially the same: people and companies that want to move, hide, protect large sums of money.

There are some Americans who use South Dakota trusts and Wyoming limited liability companies, but Americans seeking financial secrecy often prefer to use overseas providers. They use the British Virgin Islands, the

[xi] Debbie Cenziper, Will Fitzgibbon, and Salwan Georges, "Pandora Papers: a Global Investigation: Foreign Money Secretly Floods U.S. Tax Havens. Some Of It Is Tainted," *Washington Post*, October 4, 2021, https://www.washingtonpost.com/business/interactive/2021/booming-us-tax-haven-industry/?itid=lk_inline_manual_15.

Cook Islands, and other small island nations to help protect their assets. Many of the customers using the United States for financial secrecy are likewise from outside the United States.

JIA: *Smallness, then, whether it's inside the United States or out, seems to be a necessary, but not sufficient, condition. What else leads to a small state joining the system: is it individual initiative on the part of some officials in the country, or is it something else?*

MH: How a jurisdiction becomes part of the offshore system involves a lot of factors. One factor that's often present in these origin stories is the initiative of Western professionals—lawyers, accountants, and others—who come to an island nation and offer to help it create an offshore financial center. They tell local officials: "You got a really nice country here. We could show you how to improve your economy: here's how you do it." In many of these microstates and island nations that we've looked at, it's Western professionals who have come in and literally written the laws: "Here's model legislation that, if you pass it into law, will provide a real boost to your economy, as well as a boost to your government budget."

JIA: *Most people have likely heard of the Cayman Islands and have some idea that wealthy people store assets there. Maybe to a lesser degree Switzerland. But what distinguishes the illegal from the merely unethical?*

MH: That's a good question. It's illegal to slash your taxes if you're hiding income from your country's revenue authorities. It's illegal to benefit from money tied to corruption or criminal enterprises. By definition, moving around money that's the proceeds of illegal activity is money laundering, a criminal act.

What may be legal but is still unethical is another matter. Corporations, for example, have been able to exploit tax structures that have set up the illusion that income is being earning in a certain jurisdiction, a low-tax jurisdiction like Ireland, Switzerland or Luxembourg. This allows them to avoid paying more in taxes than in their own jurisdiction. Sometimes tax authorities or courts find that these write-offs are illegal. But often these kinds of tax shelters fall into the category of "legal but really sketchy, unfair, unethical."

JIA: *Part of the problem is that large corporations are composed of many different departments and types of employees. By what mechanisms do corporations use or abuse the system?*

MH: A 2014 investigation by ICIJ called "Luxembourg Leaks" really illustrates this. We found that Pepsi, Ikea, FedEx, and 340 other international companies had secured secret deals from Luxembourg, allowing many of them to slash their global tax bills while maintaining little presence in this tiny European duchy. We got hold of secret tax rulings called "comfort letters" that Luxembourg provides to corporations seeking more favorable tax treatment. In some instances, the leaked records showed that companies had enjoyed effective tax rates of less than 1 percent on the profits they had shuffled into Luxembourg. This is the sort of thing that's on the line between illegal and unethical. It all depends on what tax authorities permit.

Big companies use microstates to make their tax bills go away, almost disappear. They've got huge armies of accountants and lawyers and experts and lobbyists who will fight for them and against changes in the law that would tighten things up and make it harder for them to do this kind of thing. Much of this is the power of illusion: to create the idea of doing business, of headquartering and generating profits in this jurisdiction, when, in fact, they have very little business there.

While that clearly raises real ethical considerations, it only raises legal considerations if the governments of the world and the international community want to ensure this kind of thing isn't happening. One of the experts that we talked to for the Luxembourg Leaks, Stephen Shay, a former tax official in the U.S. Department of the Treasury, said, "A Luxembourg structure is a way of stripping income from whatever country it comes from"—making it "like a magical fairyland" for any corporation that wants to make its tax bills go to virtually nothing.

JIA: *Corporations pay their lawyers and accountants and lobbyists a lot of money to access the system. But for individuals or families, if the child of a former head of state, for example, is implicated in a shell company for tax evasion, should we assume this was done willingly or nefariously, or is this more likely a consequence of relying on financial advisors who, again, are merely exploiting the system as it is?*

MH: There are a lot of professionals involved in marketing offshore hideaways to clients. In the U.S., they include professionals here onshore: tax advisors and attorneys who link them up with other professionals offshore who will then help them.

In the 1980s and1990s, there was a so-called malpractice crisis causing great concern for American medical doctors. Tax advisors, tax lawyers, accountants, and others approached plastic surgeons and other physicians, saying, "There's this huge medical malpractice crisis, and you're in danger. You know what you can do? You move all your assets (or most of your assets) into a trust in the Cook Islands in the South Seas, in the South

Pacific. If you do that and get sued and lose a big judgment, the money is controlled, even though it may be here in the United States, by your trust in the Cook Islands."

Cook Islands law didn't recognize foreign court judgments, so the plaintiffs would actually have to travel to the Cook Islands—which is thousands of miles from the California coast—and retry the case there with rules that were not very favorable to plaintiffs and with a very short statute of limitations. If someone got sued for malpractice and they had a Cook Islands trust, they wouldn't even have to wait until after the case was decided in court to invoke the trust. Their lawyers would write to the plaintiffs lawyers: "By the way, here's where all this money is." The trust had simply created this fiction that the money was being controlled, was essentially domiciled, in the Cook Islands. The lawyers would say, "Here are the laws in the Cook Islands, and here's what you would have to do to actually collect." That would create a situation in which the plaintiff's attorneys would either have to drop the case or settle for much, much less than they would in a normal situation.

JIA: *Now for a few questions about the specific investigations either undertaken by or publicized through ICIJ. First, Mossack Fonseca & Co. was a Panamanian law firm at the center of the Panama Papers, released in April 2016. How did it rise to become one of the largest providers of offshore financial services in the world, and what role did the government of Panama play in that rise?*

MH: There's a good story, involving a very tangled web of characters, about the creation of Mossack Fonseca & Co. The father of one of the founders had been a member of the German Nazi Party's SS corps during World War II, our reporting showed.

Our investigation found that Mossack Fonseca & Co. prospered in the offshore system in large part because it was willing to serve some of the dirtiest clients in the world: mobsters, narcotraffickers, corrupt politicians, major tax evaders. It was able to operate as it pleased for decades because it was headquartered in one of the world's busiest offshore havens—a country where powerful lawyers routinely moved back and forth between government posts and law firms providing offshore secrecy. Until just before the Panama Papers investigation was released, one of the co-founders of Mossack Fonseca & Co. was a top advisor to then-President Juan Carlos Varela. So many offshore industry players were part of Varela's government that critics referred to his top aides as his "offshore cabinet."

Varela later complained that it was unfair to call the leaked documents that underpinned the investigation the "Panama Papers" because they came from just "a single law firm" that happened to be based in Panama.

But our reporting at the time and more recently has shown that many other Panamanian law firms were also deeply involved in the offshore industry. Just last year, for example, ICIJ's latest offshore investigation, the Pandora Papers, exposed the internal workings and client list of another big Panamanian law firm: Alemán, Cordero, Galindo & Lee.[xii] The records revealed that over the years, Alcogal, as the law firm was also known, had created more than 14,000 offshore entities in Belize, the British Virgin Islands, and other tax havens on behalf of more than 15,000 customers. The Pandora Papers showed the firm had provided services to figures tied to the most notorious corruption scandals in recent Latin American history, as well as more than 160 politicians and public officials from around the world.

JIA: *The Paradise Papers, released in November 2017, seem more concentrated on the machine in Europe. Can you talk about how this part of the offshoring system is different in, say, Ireland and Luxembourg, than in the Caribbean or Pacific?*

MH: Many Caribbean jurisdictions and other island havens around the globe structure their offshore financial industries around the selling of financial secrecy: the use of offshore companies and secret trusts to hide flows of money and disguise the true owners of bank accounts and other assets. This secrecy can facilitate both tax evasion and money laundering.

Ireland's and Luxembourg's offshore industries, in contrast, are built less on secrecy and more on feats of accounting sleight-of-hand. These accounting tricks allow megarich individuals and corporations to shift profits and assets, at least on paper, from the places where they're earned or domiciled to low-tax jurisdictions like Luxembourg and Ireland. The people who control these pots of money don't necessarily want their involvement with these jurisdictions to be totally secret: in fact, they want to be able to claim financial ties, however fictitious and accomplished through accounting maneuvers, to these geographic domains so that they can reap tax benefits by arbitraging one jurisdiction's tax laws against those of another, more hospitable jurisdiction.

JIA: *The list of the founding office locations for offshore service providers revealed in the Pandora Papers, released in October 2021, consists almost entirely of small former British colonies or territories: Seychelles, Belize, British Virgin Islands, Hong Kong, United Arab Emirates. Just how much of this phenomenon is a contemporary manifestation of colonial dynamics? And is it actors in the UK tapping into those old*

[xii] Brenda Medina, Jesús Escudero, and Emilia Díaz-Struck, "When Latin America's elite wanted to hide their wealth, they turned to this Panama firm," International Consortium of Investigative Journalists, October 3, 2021, https://www.icij.org/investigations/pandora-papers/alcogal-panama-latin-america-politicians/.

colonial-era networks or just taking advantage of size and common language?

MH: The fall of the British Empire did not end the UK's exploitation of the rest of the world. Even if Britain no longer dominated large swaths of the planet militarily and politically, its network of overseas territories and former colonies allowed it to profit from offshore machinations that kept huge amounts of money flowing into and through the largest British banks.

The UAE is a good example of a major offshore jurisdiction that was formerly under the rule of the UK, in the form of a British protectorate. But while the UK still has some sway with the Emirates, the United States also has close ties with the UAE. As Maggie Michael and I wrote in ICIJ's Pandora Papers piece about the UAE, the Emirates promotes itself as a forward-looking ally of the U.S. and the other Western powers in an unstable region.[xiii] The UAE has purchased massive amounts of American-made military hardware and deployed F-16 fighter jets to back U.S. operations in Afghanistan. Some U.S. generals have nicknamed the country "Little Sparta."

Because of the role the UAE plays in American national security and economic interests in the region, the U.S. hasn't put the kind of pressure on the Emirates that it has on many other offshore havens. As part of our FinCEN Files investigation in 2020, ICIJ revealed that the U.S. Treasury Department had declined to take enforcement action against a company that refines almost half of Dubai's gold imports, despite a finding by American investigators that the firm was buying gold from sellers suspected of laundering money for drug traffickers and other criminals. Former Treasury officials told ICIJ that the United States pulled back out of fear of damaging its relationship with the UAE.[xiv]

JIA: *Do locals use these offshore services? For example, do wealthy Emiratis tap into that offshore infrastructure within the UAE, or do they generally park their wealth elsewhere? Is the paradigm something like "Everywhere is offshore to somewhere else?"*

MH: The UAE is mainly an offshore haven for people from outside the UAE. If you're in the UAE, you're using other offshore havens outside the country. By definition you want to go offshore, you don't necessarily want to be onshore. In our reporting in the Pandora Papers, we saw high-level

[xiii] Maggie Michael and Michael Hudson, "Pandora Papers reveal Emirati royal families' role in secret money flows," International Consortium of Investigative Journalists, November 16, 2021, https://www.icij.org/investigations/pandora-papers/pandora-papers-reveal-emirati-royal-families-role-in-secret-money-flows/.

[xiv] Kyra Gurney, "US Treasury Department abandoned major money laundering case against Dubai gold company," International Consortium of Investigative Journalists, September 21, 2020, https://www.icij.org/investigations/fincen-files/us-treasury-department-abandoned-major-money-laundering-case-against-dubai-gold-company/.

members of Emirati royal families and government officials, who are often one and the same, moving assets through British Virgin Islands companies and other offshore havens far from the Emirates. For example, the Pandora Papers revealed one prominent royal family member was a business partner in an offshore investment deal with billionaires from the UAE and Singapore.

The UAE's status within the world's offshore financial secrecy system has grown markedly in the last decade or so. In 2009, when Tax Justice Network first created its Financial Secrecy Index, it ranked Dubai as the 31st most important offshore jurisdiction. By 2020, the UAE ranked tenth. This year, in 2022, the UAE now ranks eighth.

JIA: *ICIJ has put forward, among others, the Offshore Leaks, the Panama Papers, the Bahamas Leaks, the Paradise Papers, and now the Pandora Papers. While there is certainly more information out there about states and jurisdictions already implicated, do you think there are more havens or financial centers that have yet to be identified? Moreover, what are the known unknowns of the current system?*

MH: I think we generally know all the offshore financial centers that are out there right now, thanks to a decade of reporting by ICIJ and its partners, as well as through fine work by NGOs, government investigators, and other media outlets. Of course, the system is always evolving, so there's a chance that newer havens will emerge in the next few years.

JIA: *What can small states and jurisdictions do to counteract the system? How much agency do they have, and do they have a place in a more equitable, less unequal global capitalism?*

MH: Small states can clean their own houses and play a role in fighting the offshore machine's worst abuses. They can wipe their books of laws that allow anonymous shell companies and hyper-secret trusts and make sure that their banks and other financial gatekeepers do rigorous anti-money laundering checks on their clients and their clients' assets.

In fact, the British Virgin Islands has already begun to do this, in part because of reporting from ICIJ and its partners, and other news media. As a result of pressure from the United States and the UK, the BVI has started to do a better job of making sure that the company incorporation agents who operate there conduct real checks on customer backgrounds and the sources of their wealth. Whether these changes will be truly transformative remains to be seen.

Ultimately, it's the biggest players in the offshore system—the United States, the UK, and the EU—that have the most power to upend the offshore machine and make serious inroads against money laundering and cross-border tax evasion. Their dominance over the global financial system puts them in a position to make a real difference.

JIA: *From a small state perspective, what is the disincentive from participation in the offshore financial system? Is it only the threat of one of those big players cracking down?*

MH: The disincentive is very modest. Right now, there's pressure to do better, but while the United States and the UK have made lots of promises about cracking down on offshore centers, the results have been modest so far. The system abides. It has the ability to adapt and adapt quickly, creatively, and aggressively. Some offshore strategy, tool or jurisdiction is targeted, and by the time legislation is passed or international pressure takes effect and has an impact, people have moved on to something different.

JIA: *Does the intrinsic agility of many small states contribute to systemic churn? There has been some theorizing around advantages in small states, focusing on their ability to innovate in governance and remain flexible when confronted with external challenges. Is the tax haven and financial crime system merely an unfortunate consequence of this dynamic?*

MH: A smaller state, a smaller entity, often does have the ability to move quicker, to innovate. That's contributed to the ability of the offshore machine to keep fighting off pressure to repent and reform. And that's why it's crucial that the big Western powers, the United States, the UK, and EU countries, clean up their own acts and follow through on their promises to end offshore secrecy and fight for a fairer, more transparent, less corrupt financial system. ♚