

THEY'RE NOT TAX HAVENS ... THEY'RE SECRECY HAVENS

Citing a GAO report I linked to in January, Joe Conason had a much noted article on "tax shelters" this week. He argues we should focus on finding all the unpaid taxes in the tax shelters these companies are using, rather than focusing on AIG's measly bonuses.

In the article, Conason asks "what other reason" businesses would have for using the tax shelters, concluding that it must be the taxes.

According to the Government Accountability Office, nearly all of America's top 100 corporations maintain subsidiaries in countries identified as tax havens. As the GAO notes, there could be reasons other than avoiding the IRS to set up branches in places such as Singapore, Luxembourg and Switzerland, where taxes are light or nonexistent and keeping clients' illicit secrets is considered a matter of national pride.

But what reason other than evasion could there be for Goldman Sachs Group to set up three subsidiaries in Bermuda, five in Mauritius, and 15 in the Cayman Islands? Why did Countrywide Financial need two subsidiaries in Guernsey? Why did Wachovia need 18 subsidiaries in Bermuda, three in the British Virgin Islands, and 16 in the Caymans? Why did Lehman Brothers need 31 subsidiaries in the Caymans? What do Bank of America's 59 subsidiaries in the Caymans actually do? Why does Citigroup need 427 separate subsidiaries in tax havens, including 12 in the Channel Islands, 21 in Jersey, 91 in Luxembourg, 19 in Bermuda and 90 in the Caymans? What exactly is going on at Morgan Stanley's 19 subs in Jersey, 29

subs in Luxembourg, 14 subs in the Marshall Islands, and its amazing 158 subs in the Caymans? And speaking of AIG, why does it have 18 subs in tax-haven countries? (Don't expect to find out from Fox News Channel or the New York Post, because News Corp. has its own constellation of strange subsidiaries, including 33 in the Caymans alone.)

I pointed out in my January post the other point of these tax havens:

What Levin didn't say, of course, is that these tax havens allow them to avoid financial oversight, too.

And wrote another post giving a scary example of what those other reasons might include.

Masaccio pointed me to these two passages in AIG's 10K, which sound like they may describe what Gober is talking about:

Various AIG profit centers, including DBG, AIU, AIG Reinsurance Advisors, Inc. and AIG Risk Finance, as well as certain Foreign Life subsidiaries, use AIRCO as a reinsurer for certain of their businesses, and AIRCO also receives premiums from offshore captives of AIG clients. **In accordance with permitted accounting practices in Bermuda, AIRCO discounts reserves attributable to certain classes of business assumed from other AIG subsidiaries.** (10)

AIRCO acts primarily as an internal reinsurance company for AIG's insurance operations. This facilitates insurance risk

management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks. [my emphasis]

So AIG admits that its got a company, AIRCO, that is reinsuring its own insurance, and AIRCO is using a Bermuda accounting trick to limit the reserves it holds for this reinsurance.

AIG is almost certainly using a Bermuda subsidiary to engage in an incredibly risky practice that makes the "healthy" insurance companies we're counting on to get repaid a house of cards, because the reinsurance on the insurance they offer probably aren't backed by the amount of reserves they should be.

And here's another example of AIG using a secrecy haven to engage in risk and avoid regulation.

AIG is claiming that it overpaid taxes related to activities of an AIG-linked Panamanian corporation chartered in tax haven Panama.

[snip]

At issue is AIG-linked **Starr International Company, Inc. (SICO)**, which, it turns out, is AIG's largest private shareholder. It is also the manager of a compensation fund for AIG employees, who are paid, you guessed it, in AIG shares. Oh, and SICO's chairman is former AIG chairman Maurice "Hank" Greenberg.

Why is SICO, which is so extensively connected to U.S. firms and individuals, based in Panama? Well, the country applies low to no regulations and taxes on foreign firms registered there, of which there are 350,000 – second only to Hong Kong.

You see, these companies are robbing us blind by using these countries as tax havens. But that's not the most troubling aspect of the growing use of secrecy havens. As part of a very dangerous game, companies are using them to pick and choose when they want to be a big holding company and when they want to hide an incredibly risky venture somewhere where no one will account for it in stock valuations of the holding company or find it when suing the company. That limits the ability of consumers and investors to hold the company responsible, yet it's not clear it really mitigates risk.

And, in the case of companies like AIG and Citi, it means taxpayers bear a great deal more risk than we're talking about.

Now, I raise this not to take anything away from Conason's point—they **are** robbing us blind. But because the issue of tax and secrecy havens will be a key issue at the G20 meeting. And it looks like a key dispute will be how to enforce such new regulations.

The 20 largest economic nations in the world are expected to produce a new set of rules for oversight, transparency and conduct for offshore tax havens next week as part of a broader effort to overhaul the regulatory structure of the world economy, White House officials said Saturday.

The new "rules of the road" for Caribbean and other tax havens will be included in a communiqué issued by the Group of 20 nations at a much-anticipated London economic summit on

Thursday, said Michael Froman, a deputy White House national-security adviser for international economic affairs.

[snip]

On the tax-haven question, Mr. Froman acknowledged that there were no major offshore havens among the nations of the G-20. But, he said, the summit leaders have conducted "a series of dialogues" that will be reflected in the road map for clamping down on tax cheats.

The U.S. remains somewhat divided from Germany and France, which are pushing to blacklist tax-haven nations that don't go along with the emerging G-20 prescriptions.

This is likely going to be an answer where Europe tries to push us further than we're willing to go. We'd do well to understand the scope of the issue as that debate happens.