ASPECTS OF PUBLIC FINANCE IN A TAX HAVEN: THE CASE OF THE BAHAMAS

By

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In recent years, tax havens have become the centre of a great deal of attention. This attention, it should be pointed out, does not spring from any common interest. While, for example, tax havens do not arouse more than academic curiosity in some circles, for others there are more practical considerations involved. To many private individuals and corporations tax havens are seen as a means of reducing their tax burden and hiding their assets. To foreign governments, particularly those operating relatively high tax structures, the use of tax havens by residents often results in a loss of public revenue. To the country providing the facilities, tax haven business provides employment and income. In brief, tax havens affect different people differently, depending on their position and particular point of view.

In this paper we are concerned with only one small area of the whole subject, and this is the fiscal experience of one country offering tax haven facilities. Since there are many prevailing misconceptions about tax havens it might be useful to begin our discussion by stating what we mean by a tax haven, and outline some of their more popular uses. We shall then go on to discuss the particular fiscal structure of the Bahamas and some of the financial problems facing this particular country in the context of its tax haven policy.

Essentially a tax haven is a country offering certain financial facilities with the object of attracting foreign funds and encouraging the conduct of certain types of operations from within its shores. Generally, these facilities relate not only to tax arrangements as the term 'tax haven' implies, but also to exchange control regulations and certain other legal and administrative practices. It should be pointed out, however, that there is no standard tax haven and every centre tends to have its own peculiar attractions. For example, while some jurisdictions impose very low rates of taxes on income and profits, others refrain from any major form of direct taxation. There are some centres too, which are renowned for their numbered account facility, while others rely for a considerable part of their business on trust operations and the private company. There are also a few which operate laws with a view to attracting shipping registration. Besides certain financial facilities, some havens, of course, also offer a pleasant living climate. It should also be noted that factors like communication, transportation, financial infrastructure and political stability also help to discriminate between tax havens. Location can also be a very important consideration for institutions wishing to engage in offshore Euro-currency operations.

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Tax havens are used for a wide variety of purposes ranging from pure tax avoidance to outright illegitimate activity. Their proponents, of course, argue that they operate within the framework of law based on sentiments akin to what Lord Atkin expressed many years ago that "the subject, whether poor and humble or wealthy and noble, has the legal right so to dispose of his capital and income as to attract upon himself the least amount of tax".[1] In other words, a distinction is sought to be made between tax avoidance (a legal act by Atkin's interpretation) and tax evasion (which is the flouting of the laws of one's country). While undoubtedly a large part of the activities that take place in tax havens are what can be termed legitimate, there are countless instances which show that they are often put to illegal purposes.

To people making use of tax havens the benefits can be quite significant, particularly in the context of the rapidly increasing taxation and regulations of various kinds in many countries. To centres offering the facilities there are also, of course, benefits to be derived in terms of income and employment. The main sacrifice is in the area of public revenue. This sacrifice, it is often argued, has to be examined from the perspective that part of the total income and employment generated would not have been created without the tax haven facilities. There is undoubtedly some truth in this, and this has prompted some havens (e.g. Panama and Hong Kong) to operate a two-tier system under which income derived from local activities is subject to tax, while income arising from foreign sources is exempt from any form of taxation or regulation. Within this framework exceptions can be made in both spheres depending on existing conditions and the objectives which are sought to be achieved.

At this point there is another misconception which needs to be clarified, and it is this. When the term 'tax haven' is used in reference to any country, it does not mean that the particular country has no taxes at all. Generally what it implies is that certain forms of taxes are absent or the tax rates are very low. Tax havens, like other countries, also have public obligations to discharge. These might include the costs of administration, the provision of social services, and the maintenance and development of public infrastructure – areas for which private enterprise generally disclaims any responsibility. In the following section we shall examine the pattern of revenue and expenditure prevailing in the Bahamas (which is regarded as one of the world's leading tax havens) in an effort to highlight some of the fiscal problems that can emerge in a tax haven situation.

The Pattern of Revenue in the Bahamas

A look at Table I shows that in the selected years between 1969 and 1974 revenue from taxes ranged between 16 and 22 per cent of GNP. Though this proportion is not quite as high as those achieved by some of the more developed countries, it tends to reflect (on the surface) a much better performance than that attained by a number of other developing nations. The absence of income and profit taxes may appear to make the tax level in the Bahamas look even more remarkable. It is obvious, however, that the heavy reliance on import duties in a situation of extreme dependence on foreign trade[2] provides the major explanation. It should be borne in

TABLE 1 SELECTED GOVERNMENT FINANCES, 1969 TO 1975

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Items	1969	1971	1973	1974	1975	Average Per Cent Growth Rate of Rev., Exp. and GDP 1969-75	Rev. and Exp. Elasticities 1969-1974
1. Current Revenue[a]	74.572	77.503	108.794	115.361	119.067	7.8	0.9255
(Tax Revenue)[a]	(67.246)	(68.626)	(96.177)	(103.189)	(97.931)	(6.9)	(0.9041)
2. Current Expenditure	61.777	79.580	93.500	105.492	113.881	10.8	1.1993
3. = (1) – (2)	+12.795	–2.077	+15.294	+9.869	+5.186		
4. Capital Expenditure	16.639	12.479	13.532	35.387	22.231		
5. = (2) + (4)	78.416	92.059	107.032	140.879	136.112	9.6	1.3491
6. = (1) – (5)	–3.844	–14.556	+1.762	–25.518	–17.045		
7. GNP (at Current Market Prices)	308.000	430.000	440.000	490.000	n.a.	10.3[c]	
8. = (1) as a Per Cent of (7)	24.2	18.0	24.7	23.5	n.a.		
9. = (5) as a Per Cent of (7)	25.4	21.4	24.3	28.7	n.a.		
10. Tax Revenue as a Per Cent of GNP	21.8	16.0	21.8	21.0	n.a.		
11. Indirect Taxes[b] as a Per Cent of Total Tax Revenue	86.0	80.8	69.9	69.7	69.0		

a – These figures exclude refunds in respect of incentive Acts and other refunds and therefore are not comparable with the equivalent series presented in Table II.

b – Defined here to include only Customs Duties (including Emergency and Inland Taxes) and Excise.

c – 1969 to 1974.

Sources: Central Bank of The Bahamas, *Quarterly Review*, Various Issues; The GNP figures are World Bank estimates.

mind, too, that revenue from the casinos (which is largely an offshore activity) is also included in the tax figure. The casinos' contribution[3] to government income increased from $0.5m (1.2 per cent of current revenue) in 1965 to an estimated $9.3m (6.9 per cent of current revenue) in 1975.

While the primary purpose of a tax system is to bring the public authorities the revenues required for carrying out their functions, there are considerations which cannot be ignored in its imposition on the community. An important aspect here, which has long been recognised, is that there must be a certain amount of equity in the system, and this bears directly on the tax structure. There are no income, profit, capital gains, gift, inheritance estate or withholding taxes in the Bahamas. In Table 2 an attempt is made to show the main contributors (in broad terms) to government's income. As can be seen there, the largest single source is import duties which in recent years have been contributing over 50 per cent on average to current revenue and between 60 and 70 per cent to tax revenue. In absolute terms income from this source increased from $54.9m in 1970 to an estimated $71.9m in 1975 or by 40 per cent. A large part of the estimated increase between 1975 and 1976 is expected to come from the abolition of the preferential margins traditionally accorded imports from Commonwealth sources.[4]

The real property tax shown is levied on property improved by a value of $3,000 or more. The rate ranges from ½ of 1 per cent to 1½ per cent per annum, depending on the market value of the property. The tax does not apply to exclusively agricultural land, while a $20,000 exemption is allowed for owner-occupied property. Realizing this tax had the effect of encouraging speculation, the Minister of Finance in his 1976 Budget Communication indicated that the government proposed introducing a tax on undeveloped land owned by non-Bahamians and non-Bahamian companies both in New Providence and the Out Islands. He also pointed out that the principle will be extended to cover non-Bahamians and non-Bahamian companies owning developed land in the Out Islands. The figures relating to the 'Tourism Tax' comprise (as footnote c in Table 2 indicates) a departure tax, a passenger ticket tax and a hotel occupancy tax. Hotels in New Providence with more than 10 rooms (more than 25 rooms in the Out Islands) pay an annual licence fee of $3 per room. In addition they are also required to pay a tax of 17c per guest-day in the summer season, and 25c per guest-day during the winter. A large part of these charges is passed on by the hotels to the guests in the form of a toll.

The item 'Other Taxes' is broken down in Table 3. All companies registered in the Bahamas pay an annual fee of $250.[5] As from 1976 all companies which are not 60 per cent owned and controlled by Bahamians will be required to pay $1,000 instead of $250. Banks and trust companies pay fees ranging between $300 and $6,000 per year depending on the type of licence they hold. Exchange control privileges carry additional annual charges of between $15-30,000. Insurance operators pay an initial registration fee of between $1,000 and $3,000 depending on the kind of business they write as well as annual renewal fees based on the amount of new business written, the minimum payment in any one year required, however, being set at $500. As from 1976 insurance companies will be required to pay 1 per cent of their gross

TABLE 2 SOURCES OF GOVERNMENT CURRENT REVENUE, 1970-1976

	1970		1972		1974		1975[a]		1976[a]	
	$'000	%	$'000	%	$'000	%	$'000	%	$'000	%
Import Duties	54,864	59.9	50,782	49.0	70,990	55.4	71,900	53.8	80,380	54.3
Excise Duty	4,099	4.4	1,873	1.8	3,141	2.4	3,000	2.2	–	–
Real Property Tax	1,095	1.2	1,534	1.5	2,840	2.2	3,000	2.2	4,650	3.2
Motor Vehicle Tax	1,150	1.3	1,429	1.3	2,881	2.2	2,987	2.2	3,487	2.3
Gaming Taxes	6,730	7.3	7,820	7.6	8,898	6.9	9,290	6.9	9,278	6.3
Tourism Tax[c]	3,211	3.5	5,553	5.4	4,956	3.9	5,910	4.4	5,550	3.8
Stamp Tax	3,295	3.6	4,039	3.9	6,474	5.0	5,750	4.3	8,550	5.8
Other Taxes[d]	3,462	3.8	6,703	6.5	6,054	4.8	6,590	4.9	8,670	5.8
Total Tax Revenue	77,905	85.0	79,733	77.0	106,234	82.8	108,427	80.9	120.565	81.5
Fees and Services Charges	2,754	3.0	4,980	4.8	5,720	4.5	6,355	4.7	6,876	4.6
Revenue from Government Property	921	1.0	638	0.6	2,412	1.9	5,800	4.3	4,558	3.1
Interest	499	0.5	55	0.0	458	0.3	606	0.4	3,957	2.7
Reimbursement and Loan Repayments	2,813	3.1	10,574	10.2	5,881	4.6	2,071	1.5	1,478	1.0
Services of a Commercial Nature	6,733	7.4	7,550	7.4	7,548	5.9	10,625	7.9	10,559	7.1
Total Non-Tax Revenue	13,720	15.0	123,797	23.0	22,019	17.2	25,457	19.0	27,427	18.5
Total Current Revenue[e]	91,626	100.0	103,530	100.0	128,253	100.0	133,884	100.0	147,992	100.0

a – estimate

b – includes inland taxes on cigarettes, radio, T.V. sets, gasoline and fuel oils plus export duties.

c – hotel occupancy tax + passenger ticket tax + departure tax.

d – for a breakdown see Table 3.

e – these figures include refunds in respect of incentive Acts and other refunds.

Source: Official *Estimates of Revenue and Expenditure,* Ministry of Finance.

TABLE 3 CONTRIBUTION OF SELECTED TAXES TO GOVERNMENT'S REVENUE 1970-1976

	1970		1972		1974		1975[a]		1976[a]	
	$'000	%	$'000	%	$'000	%	$'000	%	$'000	%
Bank and Trust Co. Fees	484	14.0	1,841	27.4	1,556[b]	25.7	1,600	24.3	1,600	18.4
Insurance Co. Fees	67	1.9	91	1.4	91	1.5	120	1.8	500	5.7
Companies' Fees and Registration	1,436	41.5	2,096	31.2	1,967	32.5	2,000	30.3	2,000	23.1
Business Licences	–	–	–	–	3	0.0	1,000	15.2	2,000	23.1
Trade and Professional Licences	68	2.0	117	1.7	92	1.5	120	1.8	120	1.4
Immigration Fees	1,365	39.4	2,485	37.1	2,090	34.5	1,500	22.8	2,300	26.5
Sundry Taxes	42	1.2	73	1.1	257	4.2	250	3.8	150	1.7
Total	3,462	100.0	6,703	100.0	6,054	100.0	6,590	100.0	8,670	100.0

a – estimate

b – includes penalty charges of $6,000

Source: Official *Estimates of Revenue and Expenditure,* Ministry of Finance.

premiums into the public treasury. The stamp tax payable on property conveyances varies with the value of the transaction. The scale starts at .75 per cent on values up to $6,000 and increases up to 4.5 per cent on sums of $100,000 or over. As from 1976 the new rates applicable to conveyances of real and personal property to Bahamians and/or Bahamian companies are as follows:

(a) where the value of the conveyance exceeds $30,000, but does not exceed $50,000, 3½ per cent of the value;

(b) where the value of the conveyance exceeds $50,000, but does not exceed $100,000, 4½ per cent of the value;

(c) where the value of the conveyance exceeds $100,000, 5½ per cent of the value.

Where land is sold to non-Bahamians and/or non-Bahamian companies the rates are to be twice the rates applicable to land sold to Bahamians and/or Bahamian companies.[6] As from 1976, the distinction between real and personal property is to be abolished. Personal property will attract the same rates as real property. The stamp tax also includes levies on import and export entries. As from 1976 the existing import stamp tax of ¾ of 1 per cent of the value of all import entries (except those specifically exempted by any other Act) has been increased to 1 per cent. As for the stamp tax on export entries this has been changed from the specific rate of $1 on every set to an *ad valorem* rate of ½ of 1 per cent. In order to encourage greater employment of Bahamians or at least to accelerate their training for jobs held by expatriates, immigration fees have also been increased from 1976. These now range from $5,000 in the highest bracket to $100 in the lowest.

Even after all the 1976 tax adjustments are taken into account, import duties are expected to still account for over 50 per cent of total current revenue or for 67 per cent of tax income as a look at Table 2 shows. One reason for the continued heavy reliance on this source is that the authorities cannot significantly increase certain taxes without jeopardising the tax haven status of the country. Also, there are limits to the extent to which some others can be made to yield revenue without seriously affecting the activities to which they relate. There are other considerations, too, which the government cannot continue to ignore, and seems to be fully aware of.[7] The most important of these is perhaps the problem of equity. Import taxes have certain advantages attached to them, particularly in the context of developing countries where collection of income taxes pose certain problems. The most important of these is the ease of valuation and collection. They can also be used to help achieve certain policy objectives related to the balance of payments and domestic production. Like a number of other indirect taxes, however, import duties tend to be regressive in nature, i.e. they take a higher proportion of the income from the poorer classes than they do from the wealthy. True, some element of progressivity can be built into the system by structuring it in such a way that the rates on essential items are kept low while they are increased proportionately on goods which are considered less essential. Heavy dependence on import duties as a source of revenue, however, carries with it other

drawbacks. One is that in a revenue context rates cannot be increased to the point where they choke off imports which form the base of the tax. Secondly, it is likely to discourage serious attempts at an import substitution programme aimed at reducing imports. In other words government has a vested interest in encouraging a high level of imports, which of course also have implications for domestic savings. Heavy reliance on import duties as a source of revenue also has the effect of weakening this measure as an instrument in balance of payments policy. In the event of a foreign exchange crisis it is precisely the 'luxury' goods (which attract the highest rates) that are likely to be first curtailed.

The Growth and Pattern of Expenditure

As indicated earlier governments in tax havens have the same kinds of financial commitments as governments in other countries. They have to maintain a civil service system, build and maintain physical infra-structures provide medical and educational facilities, upkeep law and order and so forth. Even in countries with a broad and flexible tax system, these responsibilities tend to exert considerable strain on the public finances.[8] The problems, of course, become much worse in a situation with an inelastic tax system and rising public expenditures induced by a growing population and an expanding economy.

A look at Table 1 shows that tax revenue elasticity[9] tends to be of a fairly low order (0.9041 in the 1969-74 period) even when the gaming taxes are included. With the exception of 1973, total expenditure (current and capital) has consistently exceeded current revenue in the period shown in the table, and the difference is likely to get larger if government pushes ahead with its development programmes without a radical change in the tax structure. So far, borrowing has played a key role in the financing of its activities. The public debt increased from $15.2m at the end of 1965 to $61.4m at the end of 1970 and to $117.3m at the end of 1975 (see Table 4). In percentage terms this represents an increase of almost 700 per cent between 1965 and 1975 at an average annual rate of 22.7 per cent. In per capita terms the figure increased from $107 at the end of 1965 to $564 at the end of 1975.

As this debt is being repaid, there will obviously be increased pressure on revenue, given the inelasticity of the system. Further borrowing of course, can take place to repay past loans. Borrowing, however, in a situation of stagnating revenues has its limits. The government has often boasted that the willingness of the financial community to provide it with loan funds reflects the measure of confidence financiers have in the administration. It can also, of course, be looked upon as a measure of the government's inability to mobilise sufficient domestic resources to meet its development needs.

A glance of Table 1 shows that public expenditure has been increasing at a faster rate than revenue, particularly the tax component. An idea of the main areas in which government's efforts are being concentrated can be got from Tables 5 and 6. In 1975 items 2 to 6 (which can be regarded as social expenditure) took 46 per cent of the current budget and 13 per cent of the capital budget respectively. This latter pro-

TABLE 4 GROWTH OF THE NATIONAL DEBT, 1965 TO 1975 (END OF YEAR POSITION)

$'000	1965	1967	1970	1973	1975
DIRECT CHARGE					
EXTERNAL					
Govt. Sec.	–	–	–	–	–
Other	7,682	20,818	22,274	31,614	28,103
TOTAL EXTERNAL	7,682	20,818	22,274	31,614	28,103
INTERNAL					
Govt. Securities held by Central Bank	3,000	8,000	8,000	–	–
Treasury Bills	1,438	1,350	7,211	10,025	14,918
Other Govt. Securities	–	–	–	–	25,000
Local Loans	3,114	1,945	23,920	30,345	49,325
TOTAL INTERNAL	7,552	11,295	39,131	40,370	83,244
TOTAL DIRECT CHARGE	15,234	32,113	61,405	71,984	117,348
CONTINGENT LIABILITIES					
B.E.C.	9,809	8,743	10,610	16,213	8,752
BATELCO	–	6,753	11,126	20,869	16,214
TOTAL CONTINGENT	9,809	15,496	21,736	37,082	24,966
TOTAL NATIONAL DEBT	25,043	47,609	83,141	109,066	142,314

Source: Central Bank of The Bahamas, *Quarterly Review*, Various Issues.

TABLE 5 FUNCTIONAL CLASSIFICATION OF GOVERNMENT EXPENDITURE, 1969 TO 1975

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Category		1969 Current	1969 Capital	1971 Current	1971 Capital	1973 Current	1973 Capital	1974 Current	1974 Capital	1975 Current	1975 Capital
1.	General Public Service	15.2	0.8	18.4	0.4	22.7	0.5	25.5	0.2	28.0	0.2
	of which										
	(General Administration)	(8.6)	(0.0)	(9.9)	(0.0)	(13.0)	(–)	(14.7)	(–)	(15.6)	(–)
	(Public Order and Safety)	(6.6)	(0.8)	(8.5)	(0.4)	(9.7)	(0.5)	(10.8)	(0.2)	(12.4)	(0.2)
2.	Education	13.5	1.9	19.9	3.0	23.7	5.6	26.7	8.8	29.8	2.6
3.	Health	9.0	0.2	11.7	0.3	15.1	0.2	16.9	0.4	17.8	0.1
4.	Social Benefits and Services	3.0	–	3.6	–	4.3	–	3.8	–	4.4	–
5.	Housing	0.1	0.3	0.1	0.1	0.1	0.0	0.1	0.3	0.1	0.1
6.	Other Community and Social Services	0.2	–	0.2	–	0.0	0.0	0.4	–	0.1	–
7.	Economic Services:	16.8	13.2	19.4	8.4	20.6	7.2	23.0	25.6	23.4	16.3
	of which										
	(Agricultural and Fisheries)	(0.5)	(0.1)	(1.8)	(0.4)	(0.7)	(0.4)	(1.0)	(0.3)	(1.1)	(3.6)
	(Tourism)	(6.7)	(–)	(6.9)	(–)	(8.1)	(–)	(8.4)	(20.0)	(8.7)	(–)
	(Public Works and Water Supply)	(8.4)	(6.8)	(8.0)	(6.1)	(8.7)	(4.5)	(9.9)	(4.2)	(10.0)	(4.4)
	(Transportation)	(0.5)	(4.6)	(1.8)	(1.2)	(1.8)	(2.1)	(2.0)	(1.0)	(2.0)	(4.2)
8.	Other	4.2	0.3	6.2	0.2	6.9	0.2	9.0	0.2	10.2	2.9
	of which										
	(Interest and Public Debt)	(3.8)	(–)	(5.8)	(–)	(5.7)	(–)	(7.9)	(–)	(10.2)	(–)
Total		61.8	16.6	79.6	12.5	93.5	13.5	105.5	35.4	113.9	22.2

Note: Details may not add to total due to rounding.

Source: Central Bank of the Bahamas, *Quarterly Review*, Various Issues.

portion is much less than it was in previous years when education alone was taking an average of over 20 per cent of capital expenditure. While much of this expenditure is in the nature of a long term investment, it tends to have expansionary repercussions on the current budget. Besides the social obligations which government has assumed, it is also responsible for the development and maintenance of basic infrastructures to meet the expanding needs of the economy and society. In some cases (e.g. electricity, telephone, etc.), the provision of the service is associated with a charge. Whether or not this charge covers the cost of the service, ultimate financial responsibility is the government's, as it is in cases where there are no direct charges involved, e.g. sanitation services, law enforcement, etc. In circumstances like these where the private sector is not prepared to assume any obligations, the tax system has a crucial part to play in providing the government with a substantial part of the resources required to perform these functions, both as they relate to the provision of current services and the development of the capital base of the country.

From the above discussions it is clear that one of the major problems facing the authorities stems from the fact that the tax system is not geared (or is not structured) to recoup for government as large a part of the income generated by its activities as it required in a situation where it carries such heavy social responsibilities. For many countries, the income tax with its ability to incorporate a progressive incidence is a useful instrument in this context. Complementary measures normally include taxes on earnings of entities which benefit in one form or another from government's operations. Besides raising revenue these measures, of course, have other advantages. For example, they can be quite useful in influencing domestic demand conditions by either increasing purchasing power or skimming off excess demand pressures. In brief there would appear to be grave defects in taxation systems of the kind prevailing in the Bahamas from several points of view. Some of these defects, of course, give rise to greater concern in circumstances where there is limited scope for the use of monetary policy.

To be sure, the effects of a tax haven policy are not limited to the public finances or to government's policy instruments. It can also have implications for the disposition of capital funds mobilised through private channels. In some tax havens (and the Bahamas is a good example in this respect) there is the tendency to treat resources generated locally in the same way as foreign source income. The result of this policy is that funds that should be employed in domestic development are permitted to flow out of the country. Even such resources that remain tend to be put to uses in accordance with private objectives, without regard to national priorities and to the social imperatives of the situation. One suspects that failure to introduce any sort of direction in the use of local funds stems not only from the inability to properly articulate a strategy, but from a misconception that interference with the *laissez-faire* type atmosphere would damage the tax haven image of the country in a real sense.

Some Fallacies

In recent years there have been reports of governments in the region intent on establishing tax haven regimes as a means of solving their financial problems. On the face of it, this trend appears to be motivated not so much by a desire to alleviate the

TABLE 6 PERCENTAGE DISTRIBUTION OF GOVERNMENT EXPENDITURE BY MAJOR FUNCTIONS 1969 TO 1975

Category	1969 Current	1969 Capital	1971 Current	1971 Capital	1973 Current	1973 Capital	1974 Current	1974 Capital	1975 Current	1975 Capital
1. General Public Service of which	24.6	4.8	23.1	3.2	24.3	3.6	24.2	0.6	24.6	0.9
(General Administration)	(13.9)	(0.0)	(12.4)	(0.0)	(13.9)	(–)	(13.9)	(–)	(13.7)	(–)
(Public Order and Safety)	(10.7)	(4.8)	(10.7)	(3.2)	(10.4)	(3.6)	(10.2)	(0.6)	(10.9)	(0.9)
2. Education	21.4	11.4	25.0	24.2	25.4	40.9	25.3	24.7	26.2	11.7
3. Health	14.6	1.2	14.7	2.4	16.2	1.5	16.0	1.1	15.6	0.5
4. Social Benefits and Services	4.9	–	4.5	–	4.6	–	3.6	–	3.9	–
5. Housing	0.2	1.8	0.1	0.8	0.1	0.0	0.0	0.8	0.0	0.5
6. Other Community and Social Services	0.3	–	0.2	–	0.0	0.0	0.4	–	0.0	–
7. Economic Services of which	27.2	79.0	24.5	67.7	22.0	52.5	21.8	72.2	20.5	73.3
(Agriculture and Fisheries)	(0.8)	(0.6)	(2.3)	(3.2)	(0.7)	(2.9)	(0.9)	(0.8)	(1.0)	(16.2)
(Tourism)	(10.8)	(–)	(8.7)	(–)	(8.7)	(–)	(8.0)	(56.5)	(7.6)	(–)
(Public Works and Water Supply)	(13.6)	(41.0)	(10.0)	(49.2)	(9.3)	(32.8)	(9.4)	(11.9)	(8.8)	(19.8)
(Transportation)	(0.8)	(27.7)	(2.2)	(9.7)	(1.9)	(15.3)	(1.9)	(2.8)	(1.8)	(18.9)
8. Other of which	6.8	1.8	7.8	1.6	7.4	1.5	8.5	0.6	8.9	13.1
(Interest on Public Debt)	(6.1)	(–)	(7.3)	(–)	(6.1)	(–)	(7.5)	(–)	(9.0)	(–)
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note: Details may not add to total due to rounding.

Source: Table 5.

tax burden of their citizens as by the hope (no doubt fanned by foreign interests) that their countries would become centres for wealthy refugees and refugee capital capable of playing a crucial part in efforts at economic transformation. In this respect the experience of the Bahamas offers some important lessons.

The first is that by definition a tax haven situation is not likely to enhance the revenue position of the government either directly, or even to any significant extent indirectly by any extra economic activity generated. The difficulty that this raises has to be seen against the fact that government's public responsibilities tend to be no less heavy in tax haven conditions than they are in a situation where major direct taxes exist.

A second myth which needs to be exploded is that a tax haven does not have a capital problem. This arises from a basic misconception about the functioning of tax havens. To be sure there are some havens (e.g. Switzerland) which have a high level of domestic savings to provide the resources on a significant scale for local capital formation. There are also, however, a number of havens with underdeveloped economic structures where not only are domestic savings low, but desired investment opportunities in terms of risk and maturity are also scarce. In these circumstances the vast funds that are registered as being held in the tax haven tend to be invested abroad mainly in the developed countries with a record of political and economic stability. This explains why despite the enormous resources held by the banks and trust companies in the Bahamas, basic sectors of the economy remain short of capital and undeveloped. True, the Bahamas has been able to attain a standard of living that appears to be higher than that so far reached by many developing countries. This however, can be largely attributed to its tourist industry, rather than to its tax haven status *per se.*[10] In fact one has to wonder whether the latter (as currently operated) is not an obstacle to the development of a more vibrant and rationally planned tourist industry which can bring to Bahamians a relatively more secure means of livelihood, free from the intrigues and frequent scandals associated with the tax haven status of the country.

This brings us to another point, and this is the precariousness inherent in basing the future development of a country on a tax haven strategy to any extent. The laws of the countries from which the tax haven business originates are constantly changing in the attempt by these countries to close the loopholes which make tax havens possible. Tax haven activity tends to be a highly volatile business which can keep a country heavily dependent on it in a continuous state of anxiety. What is of even greater concern is that the effort required to maintain the tax haven image of the country can seriously interfere with decision-making affecting basis problems facing the society, in terms of both policy formulation and the implementation of particular measures designed to change existing conditions. This situation often stems more from the psychological re-action to which such decisions give rise rather than from the actual effects, which may have no fundamental implications in terms of the benefits to be derived by foreign persons and entities from the use of the haven.

Concluding Observations

In this final section we discuss briefly the possibilities for establishing a more rational tax system in the Bahamas, not only from the point of view of equity, but from the need for a greater degree of responsiveness to government's financial requirements as dictated by the organisation of the economy and developmental ambitions. As we indicated earlier, tax haven status implies a certain kind of fiscal structure, though in practice there can be great variation in individual regimes. The kind of regime adopted depends on a number of factors. The most important of these are: the type(s) of business the country is trying to attract; the perception of what is considered to be an effective fiscal structure in terms of the factor just mentioned; the level of the country's financial needs; the desire for some degree of equity in the fiscal system.

The Bahamian regime can in a sense be described as a very broad one. In other words it seeks to attract a wide range of business without putting explicit emphasis on any particular type.[11] Even within this approach, it should be pointed out, however, there can be variation encompassing differing degrees of 'liberalism' which would tend to depend partly on what is perceived to be the requirement for attaining stated tax haven objectives, and partly on the scope of governmental operations and obligations as defined by the particular situation. The effect of the equity factor on the fiscal structure would depend on the value placed on this problem in the existing scale of priorities. As we shall see later, the more restricted is the scope for levying tax measures, the more difficult it is to accommodate considerations of equity. Having said this, however, it needs to be pointed out that one reason for the high degree of inequity in the fiscal system of many tax havens stems from the fact that these centres emerged independent of any conscious planning or deliberate strategy. Taxes which at one time would easily have been tolerated from the point of view of social equity have in recent years become serious burdens on the community, as the systems of which they are a part are being made to yield revenue to meet increasingly new demands in situations where there has either been no corresponding growth in income or where the distribution of the latter has become more inequitable.[12]

It would appear from the above, therefore, that a tax haven policy *per se* does not necessarily imply a fiscal system with a low revenue generating capacity or one with a high degree of inequity. These qualities derive their direction and content from the particular approach taken, and the ability on the part of the authorities to guage the requirements for attaining particular objectives and the competence to operationalise these requirements within the framework of the fiscal structure.

As we indicated earlier, the present Bahamian system offers scope for rationalisation in both respects. One approach is to tax income generated from domestic activities while exempting (or taxing at very low rates) income derived from off-shore operations. The rationale for this distinction stems from the fact that income falling in the former category is created through local effort and facilities and therefore government has a claim to part of this income in the context of its functions and the nature of its responsibilities. This policy has two main advantages. The first and perhaps more important is that it provides a broader base for public revenue which should then become more responsive to changes in income. The second (which is directly related to the tax haven status of the country) is that would lend an element of certainty to the fiscal structure in terms of the elimination of the perennial speculation about changes in the latter stemming from pressure on the public finances, and therefore should enhance the image of the Bahamas as a tax haven instead of changing it, as some people believe. A stronger financial position also means that government would be better placed to deal with the social problems besetting the country, and in this way contribute to the formation of a healthier and more relaxed social climate.

The capacity of a tax system to generate revenue is not unrelated to equity considerations and this forms part of the dilemma facing the Bahamian authorities. Given the restricted capacity of the present system, the government is constrained to pay more attention to the revenue raising ability of fiscal measures (that are easily tolerated within the present policy framework) than to the equity implications of these measures. In an environment where there is more scope for raising revenue and greater freedom in the choice of measures, the government can afford to give more thought to questions of equity and reconcile these to its need for revenue.

As indicated earlier, the Bahamas relies heavily on import duties as a source of income and it is not easy to discriminate among income groups when applying this measure. This system of taxation, it should be pointed out, also has implications for the country's tourism industry which is the mainstay of the economy. There is a definite impact of the cost/price structure of the industry, which affects its competitiveness and hence its ability to grow and provide increasing income and employment. This is an aspect of the problem to which little attention has so far been given. Even the influence on the cost of living faced by residents has also so far not received serious study, and this no doubt partly contributes to the view that economic well being under a system based on indirect taxation is inherently superior to that associated with a system of direct taxation. The feeling is widespread that living under the latter necessarily means being worse off, since take-home pay may be less than it is under the former system. It is quite possible that a system based on direct taxation may result in a higher real income if the positive effect on the cost/price structure (resulting from a concomitant rationalisation of the tax system) can succeed in transforming the tourist industry into a more dynamic sector capable of generating the required level of income and employment. This would, of course, require the institution of policies and measures in other areas, and it is therefore extremely important that various sectors in the system be seen in proper perspective. This wo ' help considerably in the formulation of the relevant policy framework.

To summarise, then, it is clear that in view of the rapid increase in public expenditures brought about by various factors, urgent attention will have to be given to the existing tax structure which must be t...sformed to meet the larger role which government has assumed in recent years. One option, of course, is to hold the rise in expenditures within the limits of existing revenues. This policy, however, is clearly

neither desirable (given the stage of development of the country) nor politically feasible in the circumstances. There are some observers who seek to justify the present system on the grounds that it is not a burden on Bahamians, since the poorer strata of society contribute an insignificant part of the total tax collected. Whether one chooses to agree with this or not, the question of the scope of government's obligations and responsibilities still remains, and with it the need for funding. The two aspects cannot be viewed apart from each other in the present circumstances.

FOOTNOTES

[1] From judgement in Inland Revenue Commissioners vs Duke of Westminister, 1936, A.C.I.

[2] Excluding oil imported for refining and re-export, imports account for over 40 per cent of GDP.

[3] Since 1 January 1974, the casino tax structure has been as follows:

Basic Tax

$200,000 for each Casino

Winning Tax

On gross winnings in excess of $16m, up to and including $20m, 10 per cent.

On gross winnings in excess of $20m 5 per cent.

The minimum tax payable in any one year by a casino is $2m.

[4] As a signatory to the Lome Convention, the Bahamas was faced with the option of either abolishing the Commonwealth Preferences altogether, or extending them to all EEC and ACP countries. Given the revenue position of the country, it had little choice but to adopt the former course, even though this was likely to put further pressure on the cost of living.

[5] This is in addition to initial registration fees and stamp taxes.

[6] A Bahamian company is one which is at least 60 per cent is beneficially owned and controlled by Bahamians.

[7] In an interview carried in the *Nassau Guardian* of 22 June 1976, the Prime Minister, Mr. L.O. Pindling indicated his concern about the existing system of taxation which he said fell more heavily on the lower income groups. He pointed out the basic question was whether or not to implement direct taxation. "This" he said, "will have to come at some stage. Some future government will have to come to grips with this".

[8] This problem also has to be seen against the fact that the government owns an airline and a number of hotels. To the extent that these concerns operate on a profitable basis, this would take some of the pressure off the public revenues. In the event, however, that they have to be subsidised (as is the case at the moment) the strain on the government's purse is correspondingly increased.

[9] Our elasticity coefficient as used here reflects such changes in the tax base and/or rates as were made during the period.

[10] In the absence of a comprehensive study, it is difficult to say exactly what contribution tax haven activities make to the Bahamian economy. The IBRD has estimated that in 1970 the sector 'Finance, Insurance, Real Estate and Business Services' contributed about 13 per cent to GDP. According to census figures, this sector provided jobs amounting to about 9 per cent of the employed labour force in the same year. These figures have to be regarded as exaggerated in the sense that 'insurance' is largely a domestic activity, while 'real estate' is undoubtedly more connected with the tourism than with the tax haven status of the country.

In recent years with the stagnation in income and the increase in unemployment resulting from the problems faced by tourism and related activities, these proportions may have increased. It is unlikely, however, that the respective contributions have increased significantly in absolute terms.

[11] This statement remains true even in the light of the recent legislation designed to attract the registration of ships (*a la* Liberia and Panama) and the expressed intention to make the country a haven (*a la* Bermuda) for captive insurance companies.

[12] The distribution of income in the Bahamas is highly skewed. According to the 1970 Census the lowest 60 per cent of the country's households was receiving 27 per cent of personal income while the top 20 per cent was receiving 51 per cent.