



**FINANCIAL SERVICES  
COMMISSION**

## VIABILITY OF INTERNATIONAL FINANCIAL SERVICE CENTRES: OPPORTUNITIES AND CHANGE

Remarks by Oliver Jordan, FSC Board Chairman, on occasion of  
the 2022 BIBA Global Business Week Conference

## **Viability of International Financial Service Centres: Opportunities and Change**

Good morning, ladies and gentlemen. I have been invited to speak to you about the changes and opportunities for **International Financial Service Centres**, what we refer to as IFSCs.

These centres typically represent a significant part of the economic drivers for many of the economies in which they reside. As such, the viability of these sectors is critical for the long-term sustainability of these economies.

Unfortunately, in recent times, there have been significant questions raised about the role of these centres and the suggestion that they present a risk to the global financial markets and to the countries of origin of their clients (from a tax and financial crime perspective.)

These questions and views on the broad-reaching potential adverse impacts of IFSCs on the global markets have in turn led to questions of viability. However, the reviews conducted by the international standards setters have largely shown evidence that these sectors are largely well run with strong regulatory regimes and oversight.

In resolving this specific question of viability, I will provide an overview of the challenges facing the sector as well as the potential opportunities.

Before doing so, however, I provide a short overview of the benefits of IFSCs. IFSCs are an integral part of the global economy, mobilising investments, facilitating estate planning, and protecting assets from political and fiscal risks. They provide opportunities for companies to enhance risk management, reduce costs and facilitate global financial intermediation and investment. As such, these centres provide value creation for their clients, increasing financial market efficiencies and enabling companies (and individuals) to gain access to financial markets outside of their domestic jurisdictions.

While the value of IFSCs to the global economy is not quantified in the literature, the growing stature and importance of these centres speak to their value in the global financial sector. In some cases, these centres also serve as an innovation hub for the development of new financial products and services. As can be seen in the development of the fintech sectors, these centres can be nimbler and more responsive to emerging financial innovations. Their ecological niche

positions in the respective jurisdictions and importance to these economies allow for faster creation of legislative regimes - rules, regulations, guidance, and other enabling requirements

Barbados' reputation as a well-regulated IFSC is well-established. Although composed primarily of banks and insurance firms, this sector includes other non-bank financial institutions and more recently, we have seen significant interest from the Fintech sector. Barbados offers a favorable investment climate with a responsive regulatory environment. Its double taxation agreements and numerous bilateral agreements, supported by strong regulatory frameworks serve to enhance its attractiveness as an investment hub. Further, the introduction of the Economic Substance Regime has moved the jurisdiction away from a passive IFSC to a more active, all-encompassing position of being a Global Services Centre providing a range of services.

From the non-banking perspective, the specialised segments within the Barbadian market are mainly insurance and wealth management companies. This preference for Barbados by this business can be attributed to the talented and experienced local workforce, ease of business incorporation and licensing, and appropriate regulation and governance. Other key contributors include the presence of leading global accounting firms, in addition to other service providers who ensure that the best investment structures are pursued to accomplish favorable portfolio activity. The government is also an active participant in the creation of a favorable business environment through modern business legislation, efficient security, and regulation.

The challenges facing IFSCs can be grouped largely around four main themes:

- The adverse perception of these centres
- Slow growth in the global economies
- Increased competition and,
- Increasing regulatory complexity.

## **1. Adverse perception**

The term IFSC has over time been associated with the belief that these jurisdictions attracted criminal elements and had weak or lax regulatory regimes. This is in fact not correct.

As many of you know, in the late 1990s, developed nations, concerned with collecting tax revenues and issues of money laundering led to several initiatives that sought to assess the regulatory regimes of these centres, and set standards for the basis on which countries should tackle money laundering, and terrorist financing. In 1990, the Financial Action Task Force first issued its 40 recommendations which became the standard for the assessment of the extent to which an IFSC was so structured that it could facilitate money laundering.

The key aspects of the recommendations relate to:

- (i) the criminalisation of money laundering,
- (ii) the facilitation of international cooperation in the investigation and prosecution of such crimes
- (iii) the strengthening of supervisory policies and practices such as “know your customer rules” and
- (iv) the facilitation of the international exchange of information regarding suspicious activity

These standards have since been revised but they remain the gold standard by which financial centres such as ours are assessed.

Compliance with these standards has presented a significant cost to IFSCs. Firstly, in terms of the reputational damage to host governments and economies arising from being placed on the “lists” associated with non-compliance and the loss of business but also from the direct cost to implement the corrective measures. As these standards do not make provision for the size or resource base of an IFSC, it results in the transfer of knowledge and skills away from other productive enterprises and legislative priorities to implementing the changes.

The scrutiny of IFSCs has remained unabated and in the aftermath of the 2008 financial crisis, the role of the IFSC in facilitating financial intermediation and increasing leverage-taking was again criticised. The resulting de-risking activities, placed significant pressure on host jurisdictions, limiting economic growth and development.

Woodward in his 2009 paper on the impact of the initiatives on small states describes the attitude of the international community toward IFSCs as “hostile.<sup>1</sup>” but notes that while the rules were set by developed nations and vested in new “Bretton Woods” institutions, it was

unlikely to result in the eradication of these centres given the pivotal role they play in the global financial market.

He further pointed to the weak transparency in the US and many OECD countries and the lack of appetite for tackling similar concerns within their own borders. As the Economist remarked in an article “Haven hypocrisy: The G20 and tax.”, *“the most egregious examples of banking secrecy, money laundering, and tax fraud are not found in remote alpine valleys or on sunny tropical isles but in the backyards of the world’s biggest economies.”*

Many of the studies on the regulatory effectiveness of offshore financial sectors have noted contrary to the perception that these jurisdictions have lax regulatory regimes allowing for fraud and criminal activity that the converse was true. The underlying assumption that regulatory and tax arbitrage were the active ingredients in the success of IFSCs has been proven incorrect and while the changing standards and reviews present a real economic cost to host jurisdictions, they cannot undermine the success of the IFSCs.

Like other IFSCs Barbados was adversely impacted by the global outcry against IFSC. Concerns about blacklisting and other reputation challenges present challenges to firms doing business with Barbados. In response, in addition to strengthening its regulatory and supervision regimes, through legislative, supervisory practices, and structural changes, there was the dismantling of all preferential tax regimes and converging to an across-the-board regime and the introduction of an economic substance regime. Reviews of its regulatory regime by the international standards setters have been largely positive.

## **2. Slow growth in the global economies**

The second challenge to IFSCs is that global economic challenges such as the Covid-19 pandemic have negatively affected major economies. The daunting economic conditions heightened by the pandemic reduced investor confidence and diminished the appetite for businesses to engage in the activities provided by IFSCs. This coupled with the slow-down seen in other major sectors such as tourism would have created a significant challenge for IFSC host jurisdictions. The cost of the pandemic was significant worldwide and governments report rising debt levels and reduced revenues. This has been equally true for IFSC host jurisdictions such as Barbados, where the steep decline of the tourism sector resulted in the need to augment

social services to provide for the number of persons who were without traditional sources of income.

Notwithstanding the challenges presented by the financial markets during the pandemic, our market numbers remained relatively strong. Some of this could be attributed to the regulatory response – exercising elements of regulatory forbearance to reduce pressure on the sector as well as maintaining much of its functions throughout the period - effectively adapting and working from home.

The pandemic, however, unlike other recent global challenges has opened new opportunities for IFSCs. We have seen the emergence/growth of new and innovative financial products and increased demand by service providers to register in our jurisdictions. The nimbleness of IFSCs allows for the faster development of regimes to govern the area. The advantage of small size and access to the regulators allow for a quicker understanding of the regulatory expectation by the new service providers and the strong tradition of skilled workforces and highly developed economy with good infrastructure continues to make the IFSCs desirable.

### **3. Increased competition**

The third factor that has the potential to adversely impact the sustainability and long-term viability of the sector is the heightened competition. Many of the jurisdictions with established IFSCs boast high income, well-developed financial markets, and highly educated and knowledgeable workforces.

As a result, more countries have sought to develop their own IFSCs as a pathway to growth. There has been the growth of new financial centers in the Middle East, Asia, and Africa in line with the shift in the geopolitical landscape. We have seen the emergence of IFSCs in Dubai, Mumbai, Shenzhen, and Cape town. Additionally, there has been increased competition between the established centers, and IFSCs moving into new areas outside of their traditional niche. While it may be challenging for new IFSCs to compete with established jurisdictions in their established niches, it is not impossible. This emphasises the need for jurisdictions to focus on their service delivery - increased efficiency, faster turn-around times, and heightened responsiveness – if they are to maintain their competitive edge.

#### **4. Regulatory Landscape**

Regulation can be an expensive and challenging undertaking. The cost to surveil the regulatory perimeter to ensure that all requisite businesses are captured in the regulatory ambit, the cost of developing, reviewing, and improving the legislative regime and associated rules, regulations, and guidelines so that the jurisdiction remains well regulated, the cost to training and upskilling and retaining staff. These are all significant but critical.

Changes in assessment methodologies, and the introduction of new standards such as IFRS17, also heighten the cost of compliance. This is equally true for the regulator as it is for the regulated. These costs may narrow margins, but the benefits of maintaining a well-regulated jurisdiction, being able to withstand global shocks, and changing regulatory initiatives speak for themselves. A good regulatory regime also provides a competitive advantage as it instills confidence in the investor and reduces the risk of adverse impacts from black and grey-listing.

#### **So, What is the Way Forward?**

As has been seen from the evidence of the past 20 years, IFSCs are integral to the global economy and are here to stay. Without the ability for investment to flow, countries will not be able to make the necessary investments in social and economic goods. However, the evidence also suggests that successful IFSCs are the ones that balance meeting the requirements of the continually changing regulatory landscape while competing effectively in an increasingly crowded space.

The IFSCs of the future will have to offer a larger range of services so that they are more diversified and able to withstand specific shocks (regulatory and economic) directed to niche areas. The changing global standards and the evolving needs of market participants will create a new paradigm for the IFSCs and demand considerable investment in foundational infrastructure – staffing, and regulatory regimes – to keep pace with the changes.

According to an article in the IFC review, IFSCs of the future may not be recognisable by the standards of today. It suggests that the utility of the double taxation agreements and other niche areas will continue to be eroded as new standards of economic substance and transparency emerge. It forecasts that by 2030 IFSCs will be:

1. Tax neutral (allocating the taxing right to the investor or parent entity's home jurisdiction).
2. Have a strong legal framework and regulatory standards. (This will inspire confidence in the market as investors want to know that their funds are safe, and the legal system is fair and transparent)
3. Committed to global standards. (Committed to making the requisite changes to the regulatory regime to align with global standards)
4. Lead in fintech and emerging financial technologies. (With an understanding of the new technologies and innovations as well as achieving the balance between innovation and investor protection).

In summary, IFSCs will need to remain nimble. They must continue to capitalise on their ability to adapt quickly, identify gaps or openings and surmount challenges.

The opportunities lie in our adaptability, the strength of our regulatory regimes which have been boosted and tested over the last 20 years, our investment in education and developing a strong knowledgeable domestic workforce but also being open to attracting international talent, our investment in infrastructure and telecommunications to support business and quality of life. The Covid-19 pandemic provided an opportunity for us to utilise alternate work modalities and to shake up the way we conduct business. We need to leverage this change to prioritise our digital evolution, improve our systems and embrace innovation. The technical evolution and innovation seen over the last two years provide an opportunity for us to leapfrog our competitors, work collaboratively with the best in the field and improve the effectiveness of regulation.

Other emerging opportunities that provide a competitive advantage include focusing on Environmental, Social, and Governance (ESG) investment and creating new and innovative instruments. As nations seek to focus on the impact of climate change and meeting Sustainable Development Goals, it is critical for the investment community to look for the resulting niche opportunities. We need to capitalise on our regulatory competence, our strong industry knowledge, and best practice models to set the standards for others to follow.

At the FSC, we have been making the necessary improvements to our regulatory infrastructure. We have conducted a comprehensive review of the legislative regime governing the non-banking sector. Legislative change as we all know takes time, so in the interim, we have been



working to improve our guidance to the sector and provide greater clarification of our expectations.

Additionally, over the last few years, we have worked to reduce our application times and become more responsive to the industry – and yes, we acknowledge that more needs to be done!

Strong stakeholder engagement is one of the key tenets by which we operate. So important is this mandate, that the Board of the FSC has established a Stakeholder Engagement Committee (Chaired by none other than former BIBA Executive Director Henderson Holmes) – giving prominence to the relationships between the FSC, service providers, existing registrants, and new applicants, our partners in government and other regulatory frameworks, and the public.

We work collaboratively with stakeholders to understand the needs of the sector as this allows us to better understand the opportunities emerging in the space and the regulatory response required. To this end, you would be delighted to know that we are ready to issue a consultation paper on digital assets to the industry to share an overview of our proposed approach to regulation of this sector.

Fintech is only one area in which we as regulators are actively seeking your input. The FSC will issue in the coming weeks, consultation papers on corporate governance, updates on fitness and propriety, cyber security, and business resilience.

What is clear ladies and gentlemen, is that maintaining relevance in this sector will require the resources of the government and industry working together. While the government can put in place the necessary infrastructure to facilitate development, the industry must also play its part in determining and developing new growth areas and value propositions.

Competition and regulatory changes, and tax initiatives must be anticipated and become a routine part of the business. The better we anticipate the changes and move quickly to respond will ensure the longevity of the jurisdiction.

We also need to be at the forefront of financial innovation. The speed of change seen with the emergence of fintech signals the intensity and speed with which change is being demanded by the market. Other emerging opportunities or niche areas must be similarly anticipated and explored.

In summary ladies and gentlemen let's continue to collaborate as it is through this collaboration that we will maintain Barbados as a jurisdiction of choice.

I would like to thank BIBA for hosting this conference and trust that you enjoy the remaining sessions.

Wednesday, October 26, 2022