

The internet and international financial centres

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THE INTERNATIONAL FINANCIAL centres (IFCs) have always been innovators. They are less burdened by status quo expectations, and are subject to fewer regulations that inhibit innovation. IFCs succeed simply by being successful at what they do – not erecting barriers to capital flow and innovation. IFCs break down barriers put in place by other nations using the flexibility provided by their political environment.

The reason for the end of a financial centre is also very clear. Throughout history the demise of an IFC occurs in the face of contracting markets and restrictive rules that make other centres more attractive.

IFCs are the logical places for an International Internet Based Business (IIBB) to develop gateway services and banking relationships. What can we do to promote these advantages? First, recognise that the internet is no longer a 'new frontier'; it is a proven business conduit that dominates several markets and is making inroads in all others. The solutions which will attract more

IIBBs to an IFC must address issues of sovereignty, payments, and support services.

Sovereignty

Miss Scarlet in Canada places an order for one of Colonel Mustard's Indian baskets on a server hosted in Singapore by Mrs Peacock, pays in euros at Mr Green's bank in the Netherlands, and the product is drop-shipped from Miss White's Guatemalan factory (since we know that's where India has offshored its basket manufacturing). So, do you have a clue where the transaction is domiciled?

The textbook concept of a sovereign nation, denoting full autonomy, freedom from constraint, and independence, is a definition lacking any real-world application. All nations of the world possess what we now call interdependent sovereignty. As globalisation accelerates the flow of goods, people and currencies across sovereign borders, it also erodes state sovereignty.

We need a better framework of sovereignty to develop international

commerce, and that is the concept of a sovereign as the "supreme authority that enforces the law and adjudicates conflicts". This is what we will call domestic sovereignty, and is part of the logic of statehood. Further defining domestic sovereignty requires a recognition of domestic territoriality, and the exclusion of external actors from this domestic authority structure. In short, it is called non-intervention. This assumes that each and every sovereign nation is a hard shelled entity whereby its territory and its sovereignty is respected as well as mutual pacts of non-intervention. While this is the model that most nations agree defines a sovereign, nations violate it on a regular basis, of their own free will, through treaties, compacts, accords, and other legal arrangements. It is thought that nations enter into these agreements of their own free will, but often there are elements of coercion as economically stronger nations force the more interdependent nations' hand. Essentially, the strong do what they can and the weak suffer what they

must. These conformity-by-consequences agreements are occurring all over the world, in wholesale form such as in the European Union (EU), and in smaller piecemeal treaties.

Weaker nations have had some successes in recent years by collaborating and using their collective power to take on stronger nations, particularly on issues of trade. This is an example of a collective assertion of multiple nations' common goals.

With this knowledge an IIBB needs to choose a host jurisdiction that respects its own sovereignty and is strong enough (independently or collectively) to stand up to external challenges. The host needs to possess a framework for resolving disputes in an efficacious manner free of judicial whim. Ideally it is a jurisdiction that has drafted specific laws to enable IIBBs to defend their rights as well as the rights of their customers. To the IIBB, it is no longer acceptable to apply laws designed for static transactions in sovereign nations to multinational simultaneous electronic transactions. Just as electrical and mechanical technology has evolved through the twentieth century, our legal framework needs to evolve as well. Above all the legal system needs to be free, fair and open, providing near immediate access through an arbitration system or injunctive relief.

With this host jurisdiction in mind, the IIBB needs to concentrate their 'mind of management' and 'loci of operations' on it to the greatest degree possible. A very clear agreement, whether it be a purchase agreement, terms of use agreement, or end user licence agreement, needs to clearly state the choice of jurisdiction that the IIBB and its customer choose for the settlement of the transaction and for any disputes.

The host jurisdiction should aggressively seek to protect its IIBBs from extra territorial attacks and enable the IIBB's prosperity through a legal framework of efficacious rules, regulations and enforcement.

Payments

A payment is an exchange of value between two consenting parties for the provision of goods or services. The payment can be any medium of exchange that is acceptable to the parities of the transaction. The internet provides us more forms and choices of payment options than any community

has ever possessed in the history of the world. Miss Scarlet's Canadian dollars are converted to euros and deposited into Mr Green's bank in the Netherlands while payment is made in quetzals to Mrs White's Guatemalan account. All of this takes place in a matter of minutes or hours – not days.

The guardian of these many varied payment systems is the banking community. While the community has done very well at creating faster and more efficient payment systems that encircle the globe, these services are not yet available in all locations or by all institutions. The United States (US) and their Automated Clearing House (ACH) and Check 21 systems have nearly real time settlement, as does the United Kingdom (UK) with its Faster Payment Scheme (FPS), and the EU with its model for the Faster Payment Scheme. All of these networks need to be accessed by the banks providing services to an IIBB. It's no longer just about credit cards and debit cards – it's about integrating the ACH FPS models into payment services for the IIBB served by the IFC's banking community.

Support

While this is hardly a new frontier, it is a challenging frontier, and the participants need support.

Physically, there needs to be excellent connectivity to the Internet. Telecommunications need to be first world order and need to be scalable. This physical requirement is not just for the IIBB, but also for the banks and processors. To any host jurisdiction, the lack of proper physical telecommunications infrastructure is a fatal flaw. To those jurisdictions with access, it's an advantage that can be measured in years.

Professionals of all disciplines are required, but specifically the location will need support experts specialising in:

- web hosting and network maintenance;
- experienced and aggressive banking professionals;
- treasury experts to aid in the operation of the IIBB treasury functions;
- legal professionals trained in IIBB commerce and banking;
- experienced and independent arbitrators; and
- enforcement of real anti-fraud measures against IIBB and clients.

It's not enough to have the game board

and the pieces – you need knowledgeable players to make it a game.

The Future

Not one country has it all correct, yet. The US, EU and UK have excellent hosting and payment systems in place – with horrible legal systems. The legal systems are antiquated, ruled by fiat, and administered by automatons. These are victim-driven systems of retribution against the IIBB, but the IIBB has no ability to go after fraud committed on them by customers or third parties. A legal system must be a level playing field between all parties. Some jurisdictions have workable legal systems, but lack the necessary infrastructure or the level of sophistication needed to provide professional support.

The evolution of financial centres echoes these observations. Financial deepening, the consolidation of services, skills and technology, are required antecedent events to the building of a financial centre. These are not random events but are supported by three basic pillars:

- innovation in financial institutions, instruments and markets;
- an institutional mechanism where debtors cannot repudiate their debt; and
- the presence of a facilitating banking system.

These forces combine to allow a location to become a harbour and hub for finance. Once the centre is established, gains from this centralisation work in its favour. The financial deepening creates strong economies of scale that are realised by financial centres and can be so compelling as to overcome foreign hostile political cultures and legislation. The conditions are right for an IFC to create an IIBB-based environment. The improvements in communication and information technology favour the erosion of sovereign financial borders and the development of a host jurisdiction dedicating itself to the transparent expansion of the IIBB.

Not one country has it correct, but it will occur in time – either by the builder's design or the buyer's intent. Since as business owners we are less and less bound to geographic sovereignty, we are allowed to choose that combination of legal sovereignty, fiscal integration, and technical infrastructure that is most advantageous to us. And we will. ■