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### De Curaçaoese offshore

*Ontstaan, groei en neergang van een belastingparadijs, 1951-2013*

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#### Publication date

2018

#### Document Version

Other version

#### License

Other

[Link to publication](#)

#### Citation for published version (APA):

van Beurden, M. J. C. (2018). *De Curaçaoese offshore: Ontstaan, groei en neergang van een belastingparadijs, 1951-2013*. [Thesis, externally prepared, Universiteit van Amsterdam].

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## Summary

### **The Curaçao offshore: Origin, Growth and Decline of a Tax Haven, 1951-2013**

Recently hardly a week passed or news about tax havens, also known as Offshore Financial Centres (OFC), made headlines. Successive revelations like Offshore Leaks, LuxLeaks, SwissLeaks, Panama Papers and Paradise Papers fed public opinion that multinational corporations and the wealthy succeeded to avoid taxes with offshore constructions and inspired debate about the acceptability of OFCs. Knowledge of how OFCs develop and function is therefore no luxury. This dissertation contributes to that by examining the evolution and structure of one OFC, Curaçao. Until now there are as far known, only four studies covering the entire history of a specific OFC, i.e. Jersey, the Bahamas, the Cayman Islands and Curaçao. Because the Curaçao offshore suffered, unlike the other centres, a strong decline, I chose to study the history of the Curaçao OFC with the research question: To which internal and external factors can we attribute the origin, growth and decline of the Curaçao offshore?

One previous study covering the Curaçao OFC's history was an article published by C. Boise and A. Morriss in 2009, analyzing its origin, growth and decline. However, the authors did no archival research and based their article entirely on interviews in Willemstad and literature in English, such as reports from hearings by the American Congress and general studies about the history of the Dutch Antilles. They hardly analysed the essential Antillean legislation, and gave little statistical substantiation. By contrast, this dissertation is based on extensive archival research in Dutch-language sources, including the archives of ABN-AMRO, ING, the National Archives of the Netherlands and the ministries of Foreign Affairs, Finance, and Interior and Kingdom Relations. When deemed necessary this dissertation gives statistical substantiation and analyses of relevant Antillean legislation.

The key facility offered by the Curaçao offshore was a lower tax rate for non-residents. That was made possible by special laws, rulings, tax treaties, and the *Belastingregeling voor het Koninkrijk* (BRK), a fiscal arrangement between the partners of the Kingdom of the Netherlands. Secrecy was also offered by a firmly guarded banking secret, secret tax rulings, and the bearer share system which rendered it impossible to identify an offshore company's ultimate beneficial owner. Moreover, avoidance of regulations was made possible due to the weak or non-existent supervision of offshore banks, captives and trust offices. The Curaçao OFC also facilitated money laundering. The combination of secrecy and weak supervision provided good shelter against inquiries by fiscal, legal, and supervisory authorities.

The evolution of the Curaçao offshore had five distinct phases: origins, construction, success and decline, temporary recovery, and decline. The OFC started in 1951 when the Antilles introduced legislation designed to attract offshore companies. That move was inspired by the Nederlandsche Handel-Maatschappij (NHM), a big Dutch bank, which wanted a tax haven in the Western hemisphere to facilitate European clients seeking a safe destination for their assets. In 1950 the bank chose Curaçao for the purpose because it was a small jurisdiction with political stability, but which also possessed fiscal autonomy. The NHM set up a trust office in Willemstad and, by pointing at the substantial tax income that an OFC could generate, succeeded in convincing the Curaçao elite that it was worthwhile to introduce special legislation. Thus the key external factors to which the origin can be attributed are the need for a tax haven in the Western hemisphere and the successful attempt from NHM to persuade the Curaçao elite to introduce special legislation. Internal factors were Curaçao's fiscal autonomy, its image of political stability, and the fact that it was a small jurisdiction.

The second phase, the construction of the Curaçao offshore, began in 1951 with the introduction of legislation concerning participation exemption, and ended around 1975 with the take-off, by which time the profit tax generated by the offshore already exceeded 25 % of government revenues. This success can be largely attributed to the 1955 tax treaty with the United States and the BRK. The tax treaty with the US exempted payments of dividend, interest and royalties from the US to the Antilles wholly or partly from the American withholding tax of 30 %. Those reductions boosted the establishment of offshore holding-, investment-, financing-, and royalty-companies in Willemstad. On the other hand the BRK, which came into force in 1965, exempted dividends paid from the Netherlands to a Curaçao parent company from Dutch dividend tax. That exemption helped in making the Netherlands a hub through which to route dividends originating in other countries to Willemstad.

The tie with the Netherlands was therefore essential for the Curaçao OFC, also because the US tax treaty would not have been possible without it. Moreover, the trust offices were for a great part owned by Dutch banks, and many accountancy firms and tax consultants had a Dutch background, and Dutch companies exercised a strong influence on legislation. The Dutch financial sector and the Curaçao offshore had a symbiotic relationship which benefitted both.

After the entering into force of the tax treaty with the US in 1955, the offshore activities grew fast. The rapid growth fostered in their turn the growth of trust offices and offshore banks and allied professionals, creating economies of scale and agglomeration effects. As a result a critical mass was reached, enabling the take-off to take place around 1975. At the

same time the expanding Eurodollar and Eurobond markets boosted OFCs generally, other OFCs such as the Cayman islands, Guernsey and Jersey showing rapid growth at the same time.

From the take-off to around 1984/1985 the offshore activities increased strongly. After that a decline occurred. In 1984 the offshore generated approximately half of the total government revenue and about one third of GDP. The growth can be contributed on the one hand to investment-, financing-, and real estate companies using the American-Antillean tax treaty to partially or completely evade the US withholding tax, and on the other to dividend payments from and via the Netherlands to Curaçao offshore companies.

Several measures by the Netherlands and the United States caused a decline of the offshore activities. This included a BRK-revision (imposed by the Netherlands), repeal of the American withholding tax and termination of the tax treaty with the Antilles by the US. The repeal of the US withholding tax on interest rendered Antillean financing companies set up by American corporations obsolete. The cancellation of the tax treaty followed the Antilles's refusal to sign a new treaty because of fears that the stricter rules about exchanging information would scare away offshore customers. The Antilles came to regret their refusal and tried twice to obtain a new treaty with the US, but in vain. The BRK-revision replaced the zero rate on dividends from the Netherlands with a 10.5 % tax to stem tax losses in the country itself, but was also prompted by complaints from third countries about tax losses due to the routing of zero-taxed dividends via the Netherlands to Curaçao. Even so this dividend routing remained attractive, since the current rate was 25 %, so the revision did not really harm the Netherlands' position as a financial hub.

From 1989 to 1995 a temporary recovery occurred which can be attributed to zero-tax rulings and the *pensionado* scheme. Antilles tax rulings gave mutual funds under certain conditions exemption from the offshore profit tax rate. The *pensionado* scheme was introduced to attract wealthy foreign pensioners (*pensionados*) by offering income tax rates as low as 5%. As a result many wealthy Dutch emigrated to Curaçao, for real or just on paper, including people with good pension entitlements who moved only to sell them in Curaçao and reap a substantial tax benefit compared to what they would have had to pay in the Netherlands. Many Dutchmen also transferred their personal pension schemes into a Curaçao offshore company.

From 1995 renewed decline set in, pushing down the government's offshore profit tax income from 47% of total revenue in 1988 to 17% in 1996 and forcing it to finance budget deficits by borrowing. The downturn was mainly caused by measures from the Netherlands

and the EU. The Netherlands introduced legislation subjecting lumpsum pension pay-outs from a foreign company holding personal pension schemes to 60 % corporate tax. The measure was meant to reduce tax losses and not specifically directed against the Curaçao offshore, but did have a negative effect on the offshore activities there. In 1997 the Dutch government imposed a BRK-revision, intended to reduce tax losses from the *pensionado* scheme, and also adopted legislation about group financing intended to bring the financing activities of Dutch corporations back to the Netherlands. Consequently many Dutch corporations ended their offshore financing activities in Willemstad. Meanwhile the EU Parent-Subsidiary Directive had entered into force in 1992. The Directive abolished withholding taxes on dividend payments between group companies residing in different EU member states. As a result it became more attractive to direct dividend via for instance Luxembourg instead of Curaçao. Therefore the routing of dividend to Curaçao via the Netherlands decreased significantly.

As a result the Curaçao offshore activities entered into a steady decline from 1999 to 2013. The Dutch banks left and the number of offshore companies, trust offices and offshore banks dropped. By 2013 the offshore contribution to GDP was only about one seventh from the 1999 level and the offshore-generated profit tax also dropped to circa one seventh. Several factors contributed to the decline: the introduction of the New Fiscal Framework (NFF), EU regulations regarding investment funds, competition from other OFCs, and the faltering cooperation between state and offshore sector in Curaçao. Under pressure of the Netherlands, the OECD and the EU, the Antilles implemented the NFF. As a result the special profit tax tariff for offshore companies was repealed, though with a very generous transition period of 20 years. In 2013 new European legislation concerning investment funds offered in the EU entered into force. As a consequence, funds moved from Willemstad to countries like Luxembourg, which possessed an advantage over Curaçao not only in EU membership, but also in being able to offer favourable fiscal facilities, political stability, and the availability of specialized professionals offering a high quality of funds value assessment. As for the cooperation between state and offshore sector in Curaçao, that had worked very well until it started to unravel around 2005 as a result of disagreement within the sector. One part wanted to raise profit tax rates to internationally acceptable levels so as to attract offshore companies with more substance, the other part stuck to less stringent substance requirements for offshore companies and low profit tax tariffs. As a result the cooperation between state and offshore sector faltered, reducing government policy to an ineffective wait-and-see attitude.

The history of the Curaçao OFC demonstrates that offshore activities created an attractive, but vulnerable source of government income and an equally attractive and vulnerable economic sector. Based as it largely was on opportunities created by the American withholding tax, the tax treaty with the US and the BRK, the Curaçao offshore declined after the repeal of the withholding tax, the termination of the tax treaty and the drastic revisions of the BRK. In all periods Curaçao's ties with the Netherlands were of crucial importance. The Curaçao offshore and the Dutch financial sector maintained a close, indeed symbiotic relationship which the Dutch government was keen to nurse, so keen that the government repeatedly showed more concern for maintaining that relation than about the tax losses resulting from that symbiosis. In other words, the interests of the Dutch financial sector took precedence over public revenue.