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# Tax and Regulatory Avoidance Through Non-Traditional Alternatives to Tax Havens

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NOEL COX

Lecturer in Law, Auckland University of Technology

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*To combat corporate regulation, and the burden of taxation, corporations and individuals attempted to avoid or minimise the effects of both. This was particularly so with respect to taxation. There has been increased interest in avoiding the regulatory requirements of States. One approach to the avoidance of taxation or regulation is to use traditional tax havens. Another, but more problematic option, is through the creation and use of micro-nations, or ephemeral political entities. Another option is a virtual State in cyberspace, but this perhaps faces even less chance of success. Difficulties beset all of these endeavours. This article assesses some of the possible alternatives to traditional tax and regulatory havens.*

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## 1.0 INTRODUCTION

In the face of growth in the scope of governmental regulation, and an increasing burden of taxation, corporations and individuals not surprisingly have sought to avoid, or at least to minimise, the effects of State intervention.<sup>1</sup> This was particularly important with respect to taxation,<sup>2</sup> both from the perspective of governments – which would lose revenue – and of corporations or individuals who sought to avoid payment of taxes.

One option that became available in this respect was the tax haven – a country that attracted overseas companies and individuals to register or otherwise obtain legal residence, in return for paying minimal tax. As States alone levied taxation, so States alone could offer taxation incentives to investors. There was a significant rise in the number of tax havens in the course of the 20th century. This has continued into the 21st century,<sup>3</sup> even though tax burdens have in many cases eased. Possibly half of all money in circulation throughout the world either resides in or passes through tax havens.<sup>4</sup> In very few of these cases do the investors actually physically reside in the tax havens. It is generally sufficient if their legal

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1 Financial Stability Forum, *Report of the Working Group on Offshore Centers*, Basel, 2000, p 11, available at <<http://www.fsforum.org/Reports/RepOFC.pdf>> (as at 17 July 2002).

2 J Prebble, "Criminal Law, Tax Evasion, Shams, and Tax Avoidance: Part 1 - Tax Evasion and General Doctrines of Criminal Law" (1996) Vol 2:1 *New Zealand Journal of Taxation Law and Policy* 3; J Prebble, "Criminal Law, Tax Evasion, Shams, and Tax Avoidance: Part II - Criminal Law Consequences of Categories of Evasion and Avoidance" (1996) Vol 2:2 *New Zealand Journal of Taxation Law and Policy* 59; R McIntosh and J Veal, "Tax Evasion and New Zealanders' Attitudes Towards It" (2001) Vol 7:2 *New Zealand Journal of Taxation Law and Policy* 80.

3 R Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151.

4 M Cassard, *The Role of Offshore Centers in International Financial Intermediation*, IMF Working Paper WP/94/107, Washington, IMF, 1994; N Kochen, "Cleaning up by Cleaning up" (April 1991) *Euromoney* 73.

residence is within the haven. If companies or individuals were required to relocate completely from one jurisdiction to another to take advantage of a tax haven, interest in tax havens would perhaps have remained relatively insignificant. Use of a tax haven usually requires only a legal move, the management of most companies – and private investors – remaining physically located elsewhere.<sup>5</sup>

However, traditional tax havens have come under increased pressure from established economic powers.<sup>6</sup> Although this pressure is unlikely to have significant short-term effect, in the longer term such tax havens may find themselves compelled to enact more stringent regulations on investors. This would obviously have an adverse effect on their utility as havens.

Another option for minimising taxation and regulatory burdens, more imaginative though more problematic than the tax haven, is the creation or use of micro-nations or ephemeral political entities. One example of such a “State” is the Duchy of Sealand, but there have been many others appearing since the late 19th century. The term “ephemeral political entities” is here preferred to micro-nations, since the great majority of such “nations” have no real existence beyond the imagination of their creators, and because most such entities have been short-lived.<sup>7</sup> The purpose of this article is to assess the viability of such ventures as tax havens.

One of the earliest examples of the deliberate creation of a new State by a private individual occurred in the South China Sea in the early years of the 20th century.<sup>8</sup> Morton Meads established two companies chartered in Manila for the purposes of exploiting the mineral resources and pearl beds of the Spratly Islands.<sup>9</sup> These islands were disputed territory, thus offering an opportunity for an enterprising individual or company to attempt to obtain title where none was already clear.<sup>10</sup> For various reasons, this venture to create a new private State suffered a similar fate as that of other self-proclaimed States before and since,<sup>11</sup> and was short-lived. Traditional tax havens offer many advantages to the investor, principally those of low or nil taxation. However, the added advantages of establishing and controlling one’s own micro-nation – including the ability to control the legal and fiscal policies of that State – mean that the notion of such “nations” continues to attract interest.

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5 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 151, p 163; W Diamond and D Diamond, *Tax Havens of the World*, New York, Matthew Bender Books, 1998.

6 D Spence, “Stepping Up the Pressure on Tax Havens: An Update” (2001) Vol 7:3 *New Zealand Journal of Taxation Law and Policy* 170; M Ngoy, “The Paradox of Tax Havens: Consequences of the Subjective Approach” (2001) Vol 7:3 *New Zealand Journal of Taxation Law and Policy* 154; B James, “Tax Havens Face OECD Threat of Sanctions” *International Herald Tribune*, available at <<http://www.iht.com/IHT/BJ/00/bj061400.html>> (as at 18 July 2002).

7 For an example of the many such imaginary States, which the internet has encouraged to proliferate, see “The Micronation Page”, available at <<http://www.execpc.com/~talossa/patsilor.html>> (as at 19 July 2002).

8 The exact circumstances, or even time, of the existence of the “State” is uncertain.

9 SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81, 85. The Spratly Islands consist of more than 100 small islands or reefs, of which about 45 are claimed and occupied by China, Malaysia, the Philippines, Taiwan, and Vietnam. All of the Spratly Islands are claimed by China, Taiwan, and Vietnam; parts of them are claimed by Malaysia and the Philippines; in 1984, Brunei established an exclusive fishing zone, which encompasses Louisa Reef in the southern Spratly Islands, but has not publicly claimed the island.

10 Michael Oliver, the philosophical mastermind behind what became known as the Republic of Minerva, was also an advocate of an extreme laissez-faire political economic philosophy; L Horn, “To Be or Not to Be: The Republic of Minerva - Nation-founding by Individuals” (1973) 12 *Columbia Journal of Transnational Law* 520, pp 525-526.

11 SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81.

The third option for avoiding or minimising taxation or regulatory burdens of traditional States is to utilise a “virtual” State, whose legal existence and residence is only in cyberspace. To be effective, however, this option will likely have to wait until the time, which may never come, when the internet itself is recognised as sovereign.<sup>12</sup>

The fourth option is not to avoid the imposition of State-imposed taxation by creating one’s own State – real or virtual – but to utilise existing sub-national entities such as special development regions or tribal reservations. If the principal opposition to tax havens is from governments unwilling to see their taxation revenues decline, it is perhaps incumbent upon these governments to offer incentives for investors to remain domiciled in their homeland and not seek tax havens abroad. This could be achieved through the establishment of special economic regions.

This article begins with an examination of some of the criteria for a successful tax haven. It then reviews the requirements for traditional statehood, and some exceptions to these. The various types of ephemeral States are then examined and assessed in light of the criteria for successful tax havens and for statehood.

## 2.0 TRADITIONAL TAX HAVENS

Palan has argued persuasively that tax havens were not simply a legitimate response to a surge in taxation and governmental regulation. They also developed as a consequence of the complex interrelationship of State sovereignty and economic globalisation.<sup>13</sup> Though they come in many forms,<sup>14</sup> traditional tax havens distinguish themselves by enacting legislation that provides corporations and individuals with a measure of anonymity and shelter from their own domestic governments.<sup>15</sup>

Palan also outlined the attributes of a successful tax haven.<sup>16</sup> According to him, most successful tax havens have political and economic stability, are supported by a large international market, or are equipped with sophisticated information-exchange facilities and are within easy reach of a major financial centre.<sup>17</sup> They also have agreements with larger countries to avoid double taxation and

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12 J Goldsmith and L Lessig, “Grounding the Virtual Magistrate”, available at <<http://mantle.sbs.umass.edu/vmag/groundvm.htm>> (as at 18 July 2002).

13 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 151.

14 Park identified four major types - those which have no income tax and where foreign corporations pay merely a licence fee; those with low taxation; those which only tax internal activities; and those which have special tax privileges for certain types of corporations or operations: YS Park, “The Economics of Offshore Financial Centers” (1982) 17 *Columbia Journal of World Business* 31. Most countries in the world will qualify under one or other of these categories (particularly the last), and perhaps it is a matter of degree and intent as to whether a particular State can be classified as a tax haven.

15 A Starchild, *Tax Havens for International Business*, Basingstoke, Macmillan, 1993; R Johns, *Tax Havens and Offshore Finance: A Study of Transnational Economic Development*, New York, St Martin’s Press, 1983; S Banoff and B Kanter, “States Compete to Save Taxes Owed to Other States” (1994) 80 *Journal of Taxation* 382.

16 Diamond and Diamond list 30 key characteristics of tax havens considered in order of priority, according to a survey of international companies operating in offshore financial centres. They include: guarantees against expropriation, fair treatment by government, investment concessions, low taxes, political stability, economic stability, tax treaties, minimal currency restrictions, freedom to import raw materials, minimal government controls, secrecy, free remittance of profits, local capital availability, good communications and transportation, security of property rights, and promotion by government. See W Diamond and D Diamond, *Tax Havens of the World*, New York, Matthew Bender Books, 1998.

17 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 151, pp 155-156.

regulation.<sup>18</sup> They are also untainted by scandals, and money laundering of the proceeds of criminal or drug activity.<sup>19</sup> Any alternative to a tax haven would have to offer these or commensurate advantages to achieve a measure of success in attracting investors.

The Cook Islands has long been a tax haven for New Zealand investors,<sup>20</sup> though some companies have transferred their legal domicile to more distant tax havens, such as Bermuda, which enjoy better access to the major financial centres of the world. Although there is a considerable degree of “shopping around” in locating a suitable tax haven,<sup>21</sup> none is likely to offer a perfect solution either for a company, or for a private investor. Tax havens must, as States operating within an increasingly interdependent global economy, adhere to certain norms of behaviour, and cannot disregard the legitimate concerns of other States.

### 3.0 STATEHOOD AND EPHEMERAL POLITICAL ENTITIES

A more problematic alternative for avoiding or minimising tax liability and regulation is the deliberate creation of micro-nations, or ephemeral political entities. One example of such a creation is the Duchy of Sealand, but there have been many since the late 19th century. These are “States” that have been created by small groups of people, usually motivated by economic or utopian ideals.<sup>22</sup> The question whether these are viable as nations, quite apart from their efficacy as tax havens, must be doubted. Yet it is important to recall that the notion of the State as the sole source of legal authority is comparatively modern, and many States have been created, amalgamated, and have disappeared over the course of time – even within the 20th century.

The notions of sovereignty and statehood were once among the most important aspects of public international law. The heyday of the notion of statehood was perhaps during the late 19th century, when States enjoyed almost unfettered independence of action. They were subject only to the regulation of their diplomatic and military actions, principally by the law of armed conflict (or the law of war).<sup>23</sup>

The traditional juristic theory of territorial sovereignty, with the king being supreme ruler within the confines of his kingdom, originated as two distinct concepts in western Christendom. The king

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18 See n 17.

19 A report to the French Parliament indicated that both Liechtenstein and Monaco actively sought suspect, if not criminal, funds; Amaud Montebourg, cited by SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81.

20 The Cook Islands have long been an offshore home for New Zealand money. But it may be too remote for most overseas companies; A Reyes, “The World’s Safest Safes: Many Are Also Tax Havens”, *Asiaweek*, March 8 1996, available at <<http://www.asiaweek.com/asiaweek/96/0308/feat8.html>> (as at 18 July 2002). Norfolk Island is also a tax haven favoured by Antipodean companies, though promoters of Norfolk Island’s tax haven status have seen its potential to become a major global offshore financial centre blocked by the Australian Federal Government; A van Fossen, “Norfolk Island and Its Tax Haven” (2002) 48 *Australian Journal of Politics and History* 210.

21 SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81.

22 “Utopia” refers to the State in the book of that name by Sir Thomas More (1516); Sir Thomas More, *Utopia*, Cambridge, Cambridge University Press, 1890. Other “States” are purely fictitious.

23 International law has been called “the sum of the rules or usages which civilized states have agreed shall be binding upon them in their dealings with one another”: *West Rand Central Gold Mining Co v The King* [1905] 2 KB 391 quoting Lord Russell of Killowen in his address at Saratoga in 1876. See also M Howard, GJ Andreopoulos and MR Shulman (eds), *The Laws of War: Constraints on Warfare in the Western World*, New Haven, Yale University Press, 1994; J Gillingham and J C Holt (eds), *War and Government in the Middle Ages*, Cambridge, Boydell Press, 1984.

acknowledged no superior in temporal matters, and within his kingdom he was emperor.<sup>24</sup> If the Holy Roman Emperor had legal supremacy within the *terrae imperii*, the confines of the empire, theories of the sovereignty of kings were not needed, for the latter had merely *de facto* power.<sup>25</sup> Sovereignty remained essentially *de jure* authority.<sup>26</sup> This was not merely power without legitimacy.<sup>27</sup> Medieval jurists cared not whether the emperor had jurisdiction and authority over kings and princes, but focused on his power to usurp the rights of his subjects. Whether this power was *de facto* or *de jure* was unimportant.<sup>28</sup> From this concept of pluralist authority, modern international law developed.

But not every political entity was necessarily sovereign, or even a State as that term is now understood. The Montevideo Convention of 1933 is generally regarded as articulating the modern requirements for statehood. A State must have a permanent population; it must have a defined territory; it must have a government; and it must have the capacity to enter into diplomatic relations.<sup>29</sup> No other entity could be regarded as a State, whatever its *de facto* power, and leaderless populations or ethnic groups within States generally lacked sovereign status and, accordingly, the recognition and protection of public international law.

Even if a territory meets the Montevideo criteria, it will not necessarily be recognised by the international community. An old debate, between declaratory and constitutive theorists, centred on the role of recognition in transforming communities into States. Declaratory theorists asserted that recognition by existing States merely acknowledged that a community possessed the empirical attributes of a State – territory, population, a government, and the capacity to engage in international relations. Under this view, the function of recognition was merely to acknowledge that the State has come into existence and to signal a willingness to enter into diplomatic relations with the new State. Constitutive theorists, by contrast, considered recognition necessary to the creation of a new State. They further believed that recognition was a matter within the discretion of the recognising State to extend or withhold. The effect of the constitutive view is to hold a community's right to statehood hostage to the discretion of existing States.<sup>30</sup>

24 W Ullmann, "This Realm of England is an Empire" (1979) 30 *Journal of Ecclesiastical History* 175.

25 In Roman law it was originally considered that the emperor's power had been bestowed upon him by the people, but when Rome became a Christian State his power was regarded as coming from God. In America, also, God had been recognised as the source of government, although it is commonly thought in a republican or democratic government that "all power is inherent in the people".

26 JP Canning, "Law, Sovereignty and Corporation Theory, 1300-1450" in JH Burns (ed), *The Cambridge History of Medieval Political Thought c.350-c.1450*, Cambridge, Cambridge University Press, 1988, pp 465-467. Emperor Frederick I Barbarossa saw the advantages of Roman law and legal science for his ambitions and his inception of absolutism. This led to the growth of royal absolutism, and eventually to the emergence of opposition to this, throughout Europe; see K Pennington, *The Prince and the Law, 1200-1600*, Berkeley, University of California Press, 1993, p 12.

27 See n 26, pp 467-471.

28 K Pennington, *The Prince and the Law, 1200-1600*, Berkeley, University of California Press, 1993, p 30.

29 *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, Vol 6, p 620, available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002); I Brownlie, *Principles of Public International Law* (5th ed), New York, Clarendon Press, 1998, ch 5. Although the application of the Convention is confined to Latin America, it is regarded as declaratory of customary international law. See also *Island of Palmas Arbitration Case* (1928) No xix (2) Reports of International Arbitral Awards 829; (1928) 22 *American Journal of International Law* 986; 4 Arbitration Decisions 3.

30 See C Hillgruber, "The Admission of New States to the International Community" (1998) 9 *European Journal of International Law* 491, available at <<http://www.ejil.org/journal/Vol9/No3/ab3.html>> (as at 11 September 2002).

Grant considers the declaratory theory to be the better view, but he argues that neither view accurately describes the emergence of new States. Recent State practice renders the debate between declaratory and constitutive theory all the more inadequate. Some scholars have amended existing constitutive and declaratory theories by proposing additional requirements that communities must fulfil before becoming States, such as democratic governance or respect for minority rights. These additional rules, which have yet to gain widespread acceptance, pose additional difficulties in that they threaten to enlarge the scope of State discretion with respect to recognition. Grant contends that the alternative is to focus on the process that governs recognition rather than the substance of statehood.<sup>31</sup>

It may be that there is scope for the creation of novel forms of new States, but such scope appears to be restricted. Statehood has hitherto been the necessary precondition of tax haven status. For only a State is able to impose – and repeal – taxation and regulatory laws.

Traditionally only a State was regarded as an international person, capable of having rights and duties under international law.<sup>32</sup> That entities other than States might be the subjects of international law is even today not a universally accepted idea,<sup>33</sup> and exactly which entities do have this status is an even more controversial topic. Early in the 20th century, Hall noted that international law primarily governs the relations of independent States, but “to a limited extent ... it may also govern the relations of certain communities of analogous character”.<sup>34</sup> At about the same time, Lawrence wrote that the subjects of international law were sovereign States, “and those other political bodies which, though lacking many of the attributes of sovereign States, possess some to such an extent as to make them real, but imperfect, international persons”.<sup>35</sup> Whereas these scholars tended to define subjects of international law as States

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31 T Grant, *The Recognition of States: Law and Practice in Debate and Evolution*, Westport, Praeger, 1999. The European practice of recognizing new States in Eastern Europe and in the former Soviet Union in 1991-1992 was based on the guidelines adopted by the European Commission Member States on 16 December 1991 (see (1992) 31 *International Legal Materials* 1486). The list of criteria lays down the conditions that had to be fulfilled before the Community was prepared to recognize the new States, and thus to agree to their admission to the community of States and to the international community. It has been claimed that the conditions listed in the guidelines are merely the criteria for the establishment of diplomatic relations - something which is in the political discretion of the States in any case - and not requirements for statehood in the sense of international law; M Weller, “The International Response to the Dissolution of the Socialist Federal Republic of Yugoslavia” (1992) 86 *American Journal of International Law* 569, pp 588 and 604. See also S Talmon, “Recognition of Governments: An Analysis of the New British Policy and Practice” (1992) 58 *British Yearbook of International Law* 231, pp 250-251.

32 The assumptions of international lawyers about the near-exclusive role of States seem to be largely shared by international relations theory. See K Abbott, “Modern International Relations Theory: A Prospectus for International Lawyers” (1989) 14 *Yale Journal of International Law* 335.

33 S Charnovitz, “Opening the WTO to Non-Governmental Interests” (2000) 24 *Fordham International Law Journal* 173; Legal Affairs Committee of the Parliamentary Assembly of the Council of Europe, *Legal Status of International Non-Governmental Organizations in Europe*, D Smith (ed), Brussels, Legal Affairs Committee of the Parliamentary Assembly of the Council of Europe, 1986; International Law Commission, “Status, privileges and immunities of international organizations, their officials, experts, etc” in *Analytical Guide to the Practice of the International Law Commission*, available at <<http://www.un.org/law/ilc/guide/gfra.htm>> (as at 10 September 2002). See also *European Convention on the Recognition of the Legal Personality of International Non-Governmental Organisations*, 24 April 1986, ETS 124, entered into force 1 January 1991.

34 WE Hall, *A Treatise on International Law* (8th ed), Oxford, Clarendon Press, 1924. Nor was he alone, similar views being expressed by other writers: G Schwarzenberger, *A Manual of International Law* (1st ed), London, London Institute of World Affairs/Stevens & Sons, 1947, p 48; W Friedmann, *The Changing Structure of International Law*, New York, Columbia University Press, 1964, pp 213-215.

35 TJ Lawrence, *The Principles of International Law* (7th ed), London, Macmillan, 1925, p 69.

and certain unusual exceptions, there are others who went further in opening up the realm of reasonable subjects of the law of nations. Notable among them was Sir Hersch Lauterpacht. In his view:<sup>36</sup>

“International practice shows that persons and bodies other than states are often made subjects of international rights and duties, that such developments are not inconsistent with the structure of international law and that in each particular case the question whether a person or a body is a subject of international law must be answered in a pragmatic manner by reference to actual experience and to the reason of the law as distinguished from the preconceived notion as to who can be the subjects of international law.”

Indeed, it has since been observed that “a look at history, however, tells us that conceptions of world order have by no means always been shaped by the model of sovereign co-equal actors with a territorial basis”.<sup>37</sup> The recognition of non-State entities has indeed become more pronounced since the 1960s.<sup>38</sup>

The status of organisations in international law is less controversial than the assumption of rights and duties by individuals or groups of individuals. In 1949, the International Court of Justice recognised the United Nations Organisation as an international person,<sup>39</sup> marking an important stage in the process whereby an ever-increasing number of modern international organisations are recognised as having personality in international law. That is not, however, the same thing as saying that such an organisation is a State, or that its legal personality and rights and duties are the same as those of a State.<sup>40</sup>

While it is possible for organisations and individuals to be subjects of international law, States remain the dominant agents in world politics and the dominant actors in international law. This dominance has led some theorists to distinguish “subjects” of the law from “objects” of the law, suggesting that although entities other than States may have rights and duties in international law, these rights are conferred upon them by States and, presumably, may be taken away by States.<sup>41</sup> It is possibly more correct now to regard international law as a body of rules that binds States and other agents in world politics in their relations with one another, and that is considered to have the status of law.<sup>42</sup>

There are now many organisations operating on an international plane. Whilst many such organisations, such as the European Union and the United Nations Organisation, receive ambassadors from member countries, the Sovereign Military Order of Malta almost alone among international organisations claims the right to send representatives to other States for the purpose of carrying on

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36 E Lauterpacht, “The Subjects of the Law of Nations” (1947) 63 *Law Quarterly Review* 444. See also C Schreuer, “The Waning of the Sovereign State: Towards A New Paradigm for International Law?” (1993) 4 *European Journal of International Law* 447, available at <<http://www.ejil.org/journal/Vol4/No4/art1.html>> (as at 11 September 2002).

37 See Schreuer, n 36.

38 See Schreuer, n 36; M Koskeniemi, “The Future of Statehood” (1991) 32 *Harvard International Law Journal* 397; N MacCormick, “Beyond the Sovereign States” (1993) 56 *Modern Law Review* 1.

39 *Reparation for Injuries Suffered in the Service of the UN* (1949) 4 ICJR 179.

40 “[The UN] is a subject of international law and capable of possessing international rights and duties, and ... it has capacity to maintain its rights by bringing international claims”; see n 39, pp 178, 179.

41 G Schwarzenberger and ED Brown, *A Manual of International Law* (6th ed), Milton, Professional Books, 1976, p 42.

42 H Bull, *The Anarchical Society: A Study of Order in World Politics*, London, Macmillan, 1977, p 127; E Lauterpacht, “The Subjects of the Law of Nations” (1947) 63 *Law Quarterly Review* 444; R Higgins, *The Development of International Law Through the Political Organs of the UN*, London, Oxford University Press, 1963, p 1; P Jessup, *A Modern Law of Nations*, New York, Macmillan, 1968; JG Castel, *International Law: Chiefly as Interpreted and Applied in Canada* (3rd ed), Toronto, University of Toronto Press, 1976, p 1.

diplomatic negotiations,<sup>43</sup> as well as to receive representatives from other States for the same purpose.<sup>44</sup> Most importantly, the Sovereign Military Order of Malta claims, and is sometimes acknowledged by States, to be a sovereign State in its own right.<sup>45</sup> This status has been claimed since at least the 14th century, well before international law began to accord legal personality to international organisations.<sup>46</sup> But the Order is not unique in such claims. Its own parent body, the Holy See, has for long been regarded as sovereign, apparently even when the papacy was without territorial possessions.<sup>47</sup> Territorial possessions gave both the Holy See and the Sovereign Military Order of Malta their status as sovereign States, but the loss of territory did not necessarily extinguish that status.<sup>48</sup>

The 20th century, and particularly the second half of that century, saw the growth of international organisations and other bodies now accorded recognition as subjects in international law. With the growth in both the extent and the reach of international agreements, treaties, conventions and codes, the extent to which individual sovereign States retain the final control over their national policies may have diminished.<sup>49</sup> This tendency is becoming more noticeable in the modern commercial environment, and especially in respect of the internet. The development of the internet has presented new opportunities for those keen to escape the shackles of government. As yet, however, only States and international organisations that have been recognised as analogous are exempt from taxation by other States.

The principal actor in international law is the State. If one cannot find a State whose fiscal and regulatory policies accord exactly with one's requirements, the option remains of creating one's own

43 The Holy See is in a similar position, though the existence of the Vatican City complicates the situation. It is important to realise that it is the Holy See which is recognised by the United Nations, and not Vatican City State (which fulfils the fuller requirements for State sovereignty). In United Nations documents, the term "Holy See" is used except in texts concerning the International Telecommunications Union and the Universal Postal Union, where the term "Vatican City State" is used. States do not entertain diplomatic relations with Vatican City State, but with the Holy See. The term "Holy See" refers to the supreme authority of the Church, the Pope as Bishop of Rome and head of the College of Cardinals. It is the central government of the Roman Catholic Church: Archbishop R Martino, "A Short History of the Holy See's Diplomacy", available at <[http://www.holyseemission.org/short\\_history.html](http://www.holyseemission.org/short_history.html)> (as at 11 September 2002).

44 The Order was also involved in the Geneva Conventions, and is a member of the International Red Cross. The European Communities also accredit some ambassadors. Both the Order of Malta and the International Red Cross have had permanent observer status at the United Nations since 1994. For a list of permanent members, non-member States with permanent observer missions at UN headquarters, and entities with a standing invitation to participate as observers in the sessions and work of the General Assembly and maintaining permanent offices at headquarters, see <<http://www.un.org/Overview/missions.htm#nperm>> (as at 10 September 2002).

45 For example, San Marino acknowledged the Order as a sovereign State in a treaty of amity in 1935; A Astraudo, "Saint-marin et l'Ordre de Malta" [1935] *La Revue Diplomatique* 7.

46 Though the canon law of the Church accorded recognition to certain organizations. See also N Cox, "The Acquisition of Sovereignty by Quasi-states: The Case of the Order of Malta" *Mountbatten Journal of Legal Studies* (forthcoming).

47 The best statement of this position - though dated - is that of J Hatschek, translated by C Manning, *An Outline of International Law*, London, Bell & Sons, 1930, p 56, cited in DP O'Connell, *International Law* (2nd ed), London, Stevens, 1970, pp 85-86; Archbishop R Martino, "A Short History of the Holy See's Diplomacy", available at <[http://www.holyseemission.org/short\\_history.html](http://www.holyseemission.org/short_history.html)> (as at 11 September 2002).

48 Many countries (the US and most Western European countries) did not recognise the incorporation of the Baltic States into the USSR in 1940, at least initially: United States Mission to the United Nations, "The United States reaffirms recognition of independence of Estonia, Latvia and Lithuania", 29 July 1983, available at <[http://web-static.vmeef/static/failid/182/President\\_Reagan\\_statement.pdf](http://web-static.vmeef/static/failid/182/President_Reagan_statement.pdf)> (as at 13 September 2002); cf G Marston, "The British Acquisition of the Nicobar Islands, 1869: A Possible Example of Abandonment of Territorial Sovereignty" (1998) 69 *British Yearbook of International Law* 245.

49 Though even in the heyday of State sovereignty, the late 19th century, the extent to which any State was truly independent depended much on non-legal factors, such as relative economic strength.

“ideal” State. Most of the attempts to create new States have been in oceanic or marine situations. The freedom and isolation of the open seas inhibit the control exercised by established powers, and encourage the formation of alternative political societies.<sup>50</sup> Menefee has identified four principal categories of territory that have been so used: the appropriation of apparently unclaimed islets (for example, Mead’s State in the Spratly Islands); the promulgation of sovereignty over reefs or low-tide elevations (for example, Grand and Triumph reefs); the creation of States in shallow waters by dumping or other means (for example, Abalonia); and the creation of States on totally artificial structures (for example, Sealand).<sup>51</sup> Each of these categories presents particular difficulties for the would-be State-builder, whether that person be motivated by notions of unbridled free enterprise or libertarianism, or by pure eccentricity.

#### 4.0 PROBLEMS FOR APPARENTLY UNCLAIMED ISLETS

Even if the whole of the land mass of the planet is claimed by existing States,<sup>52</sup> it may still be possible to find islands that have escaped the jurisdiction of States. One such possibility is the Spratly Islands – sometimes known as the “Kingdom of Humanity” and the “Republic of Morac-Songhrati-Meads”. Morton Meads never got as far as declaring independence. But had he done so it is likely that his country’s independence would have been short-lived. The principal requirement for the acquisition of sovereignty over an uninhabited island territory is effective occupation.<sup>53</sup> This requires possession and administration,<sup>54</sup> though this will be commensurate with the extent and nature of the territory. It does not necessarily mean actual settlement.<sup>55</sup> The emphasis has changed from taking physical possession and the exclusion of others,<sup>56</sup> to the manifestation and exercise of the functions of government over the

50 SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81.

51 See n 50, p 82.

52 Excepting Antarctica: *The Antarctic Treaty*, 1 December 1959, NZTS 1961, No 12, EAPub No 215; 402 UNTS 71, entered into force 23 June 1961.

53 *Island of Palmas Arbitration Case* (1928) No xix (2) Reports of International Arbitral Awards 829; (1928) 22 *American Journal of International Law* 986; 4 Arbitration Decisions 3; *Clipperton Island Arbitration Case* (1932) 2 Reports of International Arbitral Awards 1105; (1932) 26 *American Journal of International Law* 394; 6 Arbitration Decisions 105; *Minquiers and Ecrehos Case, France v United Kingdom* (1953) ICJ 47; *Gulf of Fonseca Case, El Salvador v Honduras* (1992) ICJ 351.

54 Sir R Jennings and Sir A Watts (eds), *Oppenheim’s International Law* (9th ed), London, Longman, 1992, vol 1, p 688; *Island of Palmas Arbitration Case*, see n 53; *Clipperton Island Arbitration Case*, see n 53; *Minquiers and Ecrehos Case*, see n 53; *Gulf of Fonseca Case*, see n 53.

55 *Island of Palmas Arbitration Case*, see n 53; *Legal Status of the Eastern Greenland Case, Denmark v Norway* (1933) Permanent Court of International Justice Reports Series A/B, No 53, p 46; 6 Arbitration Decisions 95; *Clipperton Island Arbitration Case*, see n 53; CHM Waldock, “Disputed Sovereignty in the Falkland Islands Dependencies” (1948) 25 *British Yearbook of International Law* 315; *Delgamuukw v British Columbia* [1997] 3 SCR 1010 (SCC); *Argentina v Chile* (9 December 1966), No xvi Reports of International Arbitral Awards 111, 115; (1969) 38 *International Legal Materials* 16, p 20.

56 Though the symbolic taking of possession can be important, as in the case of uninhabitable territories, such as the Island of Rockall. Rockall is an isolated, uninhabited, pudding-shaped sea rock situated in the middle of the North Atlantic Ocean. It is tiny, only 19m high, 25m across and 30m wide. Rockall is located 57°N, 13°W, about 300 nautical miles from the coasts of Scotland, Ireland, and Iceland. After being claimed variously by the United Kingdom, Ireland, Iceland, and Denmark, a British naval party claimed the island in 1955, and the Rockall Act 1971 further reinforced the British claim. However, in 1997 Greenpeace activists landed on the island, stayed for 42 days, and declared Rockall the sovereign territory of Waveland: “Rockall” at <<http://www.bbc.co.uk/dna/h2g2/A749630>> (as at 17 July 2002); “Welcome to Waveland” at <<http://www.waveland.org/>> (as at 17 July 2002).

territory.<sup>57</sup> “The continuous and peaceful display of territorial sovereignty (peaceful in relation to other States)” is as good as a title otherwise obtained.<sup>58</sup> “In many cases the tribunal has been satisfied with very little in the way of the actual exercise of sovereign rights, provided that no other State could make out a superior claim.”<sup>59</sup> The means by which possession by an individual could establish statehood is analogous to that by which an existing State obtains title.

Settlement of the Spratly Islands might have been sufficient to give Meads some title to the islands. But though it might be possible to *claim* sovereignty over a disputed island, it is unlikely that any established State would fail to use force, if necessary, to remove occupiers before they could obtain a perfect title.<sup>60</sup>

These entities (unclaimed islets) cannot be said to meet Palan’s requirements for success as tax havens.<sup>61</sup> They generally do not have political and economic stability. It is unlikely that they would be adjacent to and supported by large international markets, or be equipped with sophisticated information-exchange facilities and be within easy reach of a major financial centre. It is unlikely that any will have agreements with major countries to avoid double taxation and regulation. While such entities are not necessarily tainted by scandals, or by the laundering of proceeds of criminal or drugs activities, they lack international credibility. Indeed, since their status is disputed by existing classic sovereign States, they would present grave risks and disadvantages to investors.

## 5.0 PROBLEMS FOR REEFS OR LOW-TIDE ELEVATIONS

Even if one could not locate an existing island upon which to base one’s financial empire, it might be possible to use a reef or other low-tide elevation, such as what was known as the Grand Capri Republic (or alternatively Atlantis, Isle of Gold) – the Grand and Triumph reefs, east of the Florida Keys. This was chosen by Louis Ray, of Acme General Contractors Inc, for the development of a resort, although his ambitions apparently also extended to eventual independence. The same reef was also chosen by the rival Atlantis Development Corporation. The plans to develop Grand and Triumph reefs ended in protracted litigation.<sup>62</sup> It was unnecessary for the courts to consider in detail the international law precedents for establishing States, because the reefs were found to be seabed rather than islands. Both domestic<sup>63</sup> and international law<sup>64</sup> confirmed that the United States had a right to control the natural

57 CHM Waldock, “Disputed Sovereignty in the Falkland Islands Dependencies” (1948) 25 *British Yearbook of International Law* 315, p 317.

58 *Island of Palmas Arbitration Case* (1928) No xix (2) Reports of International Arbitral Awards 829; (1928) 22 *American Journal of International Law* 986; 4 Arbitration Decisions 3.

59 *Legal Status of the Eastern Greenland Case, Denmark v Norway* (1933) Permanent Court of International Justice Reports Series A/B, No 53, p 46; 6 Arbitration Decisions 95.

60 As was shown by the occupation by Spanish and Moroccan troops of the disputed island of Perejil: I Wilkinson, “Spain talks of peace but troops dig in on island”, *Daily Telegraph* (London), 19 July 2002.

61 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 1.

62 *United States v Ray*, 281 F Supp 876 (SD Fla 1965); *Atlantis Development Corporation v United States*, 379 F 2d 818 (5th Cir 1967); *United States v Ray*, 294 F Supp 532 (SD Fla 1969); and *United States v Ray*, 423 F 2d 16 (5th Cir 1970).

63 Outer Continental Shelf Lands Act 1953 (43 USC 1331-1356, PL 212, Ch 345, 7 August 1953, 67 Stat 462) as amended by PL 93-627, 3 January 1975, 88 Stat 2130; PL 95-372, 18 September 1978, 92 Stat 629; and PL 98-498, 19 October 1984, 98 Stat 2296 (US).

64 *Convention on the Continental Shelf*, 29 April 1958, NZTS 1965, No 2, EAPub No 307; 499 UNTS 311, entered into force 10 June 1964, art 2, paras 1, 2, 3. In 1969, the International Court of Justice declared that Article 1 of the 1958 Geneva Continental Shelf Convention (defining continental shelves) should be regarded as reflecting or crystallizing rules of

resources of the continental shelf.<sup>65</sup> Federal authorities could prevent Ray from developing his reef into an island. The development of a State could scarcely succeed in these circumstances.

It seems unlikely that a State would allow part of its seabed to be used in this way, but it may be possible to find an elevation that is unclaimed, such as the Republic of Minerva. This was based on the Minerva reef, between Tonga and Fiji, some 1,000 nautical miles north-east of New Zealand.<sup>66</sup> Most of North Minerva reef is less than 2 metres high at low tide, and the rest is never more than 1 metre uncovered. The entire reef is submerged at high tide. South Minerva reef is completely submerged at high tide, and uncovered at low tide.<sup>67</sup> Unlike the Grand Capri plans, the reefs were not within the territorial waters of another State – or on its continental shelf – being some hundreds of nautical miles from Tonga, the nearest State. The proposed development of the Minerva reef was led by the USA-based Ocean Life Research Foundation, and began in 1971.<sup>68</sup> The plan was for the formation of a 160 hectare island on the reef.<sup>69</sup> The developers claimed that their “Republic” was recognised by the Sultanate of Ocussi-Ambeno, East Timor – though the legal status that this recognition would confer was slight, given that the Sultanate was itself not a recognised State.<sup>70</sup> Whilst the constitutive theory of statehood might recognise this as a means of achieving *de jure* statehood,<sup>71</sup> *de facto* statehood did not endure (if it ever existed). The brief existence of the “Republic of Minerva” – whether it was ever a

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customary international law. Not all the remainder of the Convention might be so regarded: *North Sea Continental Shelf Case, Federal Republic of Germany/Denmark v Federal Republic of Germany/Netherlands* (1969) ICJR 3. Article 2(3) states that “[t]he rights of the coastal State over the continental shelf do not depend on occupation, effective or notional, or on any express proclamation”. The US is a signatory of the Geneva Convention on the Continental Shelf. The Geneva Convention is available at <[http://www.un.org/Depts/Treaty/final/ts2/newfiles/part\\_boo/xxi\\_boo/xxi\\_4.html](http://www.un.org/Depts/Treaty/final/ts2/newfiles/part_boo/xxi_boo/xxi_4.html)> (as at 12 September 2002).

- 65 SP Menefee, “Republics of the Reefs: Nation-Building on the Continental Shelf and in the World’s Oceans” (1994) 25 *California Western International Law Journal* 81, pp 86-95.
- 66 L Horn, “To Be or Not to Be: The Republic of Minerva - Nation-founding by Individuals” (1973) 12 *Columbia Journal of Transnational Law* 520.
- 67 See n 66. See also O Ruhen, *The Minerva Reef*, Sydney, Halstead Press, 1963.
- 68 P Du Bois, “Utopia on the Rocks: Or, the Short, Unhappy Life of the Republic of Minerva”, *Barron’s*, 26 March 1973, p 5.
- 69 L Horn, “To Be or Not to Be: The Republic of Minerva - Nation-founding by Individuals” (1973) 12 *Columbia Journal of Transnational Law* 520, p 521.
- 70 R Boragartz, “How to launch a country”, *Saturday Review of the Society*, vol 1, no 3, March 1973, 10, p 11; see n 66, p 526. It is also to be observed that the Sultanate is now part of the newly independent State of East Timor, though there is a shadowy “Sultanate” in existence on the internet, if not in reality. See “Sultanate of Okusi-Ambeno” at <<http://okusi1.tripod.com/>> (as at 10 September 2002).
- 71 See C Hillgruber, “The Admission of New States to the International Community” (1998) 9 *European Journal of International Law* 491, available at <<http://www.ejil.org/journal/Vol9/No3/ab3.html>> (as at 11 September 2002).

State or not – ended with its occupation by Tongan forces.<sup>72</sup> It is likely that further such States would founder due to invasion by the nearest established State claimant, or simply because of the high cost of development and the uncertainty of a return on investors' funds.

These reef-based entities also cannot be said to meet Palan's requirements for success as tax havens.<sup>73</sup> They generally do not have political and economic stability, and while they are not necessarily tainted by scandals and by the laundering of proceeds of criminal or drugs activities, they lack international credibility because of their very artificiality.

## 6.0 PROBLEMS FOR STATES IN SHALLOW WATERS CREATED BY DUMPING OR OTHER MEANS

Greater difficulties face States in shallow waters, created by sinking derelict ships or by dumping. One example is Abalonia in Cortes Bank, west of San Diego in California. Like the neighbouring Taluga, development ceased temporarily during the *Ray* litigation, and ended soon after the Grand Capri Republic failed to obtain court recognition.<sup>74</sup> Such projects are likely to be unsuccessful for economic reasons alone, and environmental considerations – which were also present in the *Minerva* case – would deny them support from many of the freer spirits of the environmentalist movement, who formed their own (virtual) Waveland.<sup>75</sup> They are also likely to be in territorial waters, and thus subject to the authority of existing States. This alone would prevent their development.

In respect of Palan's requirements,<sup>76</sup> these entities also would be unlikely to rank as successful alternatives to existing tax havens, for the same reasons as the other forms of "States" reviewed.

## 7.0 PROBLEMS FOR STATES ON TOTALLY ARTIFICIAL STRUCTURES

Perhaps ironically, in some respects the most successful option – or least unsuccessful – for an alternative to a traditional tax haven has been the creation of totally artificial States. For practical reasons these have usually been in coastal waters. They may be part of the seabed. In some cases they have been floating, moored or anchored, or free-floating – though the floating republics have generally been especially unsuccessful.<sup>77</sup> One of the first of these was New Atlantis, which was created by Ernest

72 L Horn, "To Be or Not to Be: The Republic of Minerva — Nation-founding by Individuals" (1973) 12 *Columbia Journal of Transnational Law* 520, p 528. The complete occupation of one State, so that its territory is absorbed into another State, may serve to extinguish that former State, though not necessarily the treaty obligations of the former State. See the *Vienna Convention on Succession of States in Respect of Treaties*, 28 August 1978, entered into force 6 November 1996; United Nations Conference on the Succession of States in respect of treaties-Official Documents-Volume III-Conference Documents (United Nations publications, Sales No F.79.V.10); United Nations Document A/CONF 80/31 of 22 August 1978, as corrected by A/CONF 80/31/Corr 2 of 27 October 1978; (1978) 17 ILM 1488.

73 R Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151.

74 SP Menefee, "Republics of the Reefs: Nation-Building on the Continental Shelf and in the World's Oceans" (1994) 25 *California Western International Law Journal* 81, 102-104; DP Stang, "Wet Lands: The Unavailable Resources of the Outer Continental Shelf" (1968) 2 *Journal of Law and Economic Development* 153.

75 Originally declared "sovereign" on the uninhabited islet of Rockall: see "Welcome to Waveland" at <<http://www.waveland.org/>> (as at 17 July 2002).

76 R Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151.

77 N Papadakis, *The International Legal Regime of Artificial Islands*, Leiden, Sijthoff, 1977, p 36.

Hemingway's younger brother, Leicester, in the 1960s. It consisted of a bamboo platform moored six nautical miles off the coast of Jamaica,<sup>78</sup> and was fated to sink in a storm.<sup>79</sup>

A non-American example is Iola Delle Rose, off the Port of Rimini, on the Adriatic coast of Italy, 300 metres outside Italian territorial waters.<sup>80</sup> The Italian Council of State, to which Rosa and Chierici (the co-founders of the "State") appealed a demolition order from the Rimini Harbour Office, said that the Geneva Convention on the High Seas,<sup>81</sup> like that of Territorial Sea and Contiguous Zone,<sup>82</sup> "only creates rights and obligations of an international character for the Italian State with respect to other nations of the international community. The appellants cannot deduce from it any rights worthy of protection either according to international law or under Italian municipal law."<sup>83</sup> The venture failed because, like Grand Capri, it fell within the territorial influence of an existing State, which simply ignored its claims to statehood.

The Principality, or Duchy, of Sealand<sup>84</sup> is perhaps the best-known example of a totally artificial structure that has pretensions to statehood – and the longest surviving. It is based on Roughs Fort, built in the winter of 1941-1942, 7 nautical miles off the coast of England, as an anti-aircraft post. It comprises two 20-metre high and 8-metre wide legs, which are joined at the top by a platform that originally housed the guns. The State began in the 1960s, at a time when numerous "pirate" radio stations were being established across the United Kingdom and continental Europe in contravention of national broadcasting laws.<sup>85</sup> Many of these were built in wartime sea forts.<sup>86</sup> Most were found to be subject to national broadcasting laws,<sup>87</sup> but the legal status of Roughs Fort at least was more problematic.<sup>88</sup> Indeed, a British court held in 1968 that Sealand was outside British territorial waters –

78 At that time outside the territorial waters of Jamaica.

79 SP Menefee, "Republics of the Reefs: Nation-Building on the Continental Shelf and in the World's Oceans" (1994) 25 *California Western International Law Journal* 81, 104-105; R Arias and M Weiss, "On the Job: George Demko, US Geographer - Keeps a Watchful Eye on States That Border on the Absurd", *People Weekly*, 30 May 1988, 101, p 103.

80 See Menefee, n 79, p 105; *Chierici and Rosa v Ministry of the Merchant Navy and Harbour Office of Rimini*, 71 ILR 258 (14 November 1969) partial English translation and fact summary (citing (1975) 1 *Italian Yearbook of International Law* 265) (Council of State).

81 29 April 1958, 450 UNTS 82, entered into force on 30 September 1962.

82 29 April 1958, 516 UNTS 205, entered into force on 10 September 1964.

83 *Chierici and Rosa v Ministry of the Merchant Navy and Harbour Office of Rimini*, 71 ILR 258 (14 November 1969) partial English translation and fact summary (citing (1975) 1 *Italian Yearbook of International Law* 265) (Council of State).

84 In German litigation, the State was referred to as the Duchy of Sealand, though the more common usage - and the current "official" usage - is the Principality of Sealand: *In re Duchy of Sealand* (1978) 80 ILR 683 (Administrative Court of Cologne), cf <<http://www.sealandgov.com>> (as at 18 July 2002).

85 Radio Noordzee and TV Noordzee were constructed in international waters off the coast of the Netherlands, for the purpose of evading national broadcasting laws: G Bishop, *Offshore Radio*, Norwich, Icen Enterprises, 1975, pp 80-82. See also HF van Panhuys and M van Emde Boas, "Legal Aspects of Pirate Broadcasting: A Dutch Approach" (1967) 60 *American Journal of International Law* 303.

86 Other forts similar to Roughs Fort included Knox John, Tongue Sands, and Sunk Head Forts. The latter housed Tower Radio, Radio Tower, and Tower TV during 1965-1967. It was subsequently demolished by the British army. Radio City, and later Radio Essex and bbms (Britain's Better Music Station), ran from Knox John Fort during 1965-1967: SP Menefee, "Republics of the Reefs: Nation-Building on the Continental Shelf and in the World's Oceans" (1994) 25 *California Western International Law Journal* 81, pp 106-112; G Bishop, see n 85.

87 As falling within British territorial waters; see G Bishop, n 85, pp 46, 57 and 115.

88 Sunk Head Fort may have been demolished for this same reason: SP Menefee, "Republics of the Reefs: Nation-Building on the Continental Shelf and in the World's Oceans" (1994) 25 *California Western International Law Journal* 81, p 139.

as then defined<sup>89</sup> – and therefore beyond the jurisdiction of British courts.<sup>90</sup> But though it may be beyond the territorial jurisdiction of the country to which it apparently belongs, a territory, however large, is not necessarily a State.

On 25 September 1975, “Roy of Sealand” proclaimed the Constitution of the Principality. In the mid-1970s the Administrative Court of Cologne, asked to determine the status of Sealand citizenship conferred upon a German national, the “Foreign Secretary and Chairman of the Council of State” of Sealand, held that the platform was not a State within international law, because it had neither territory, nor people, nor government.<sup>91</sup> The criteria of the Montevideo Convention<sup>92</sup> proved too resilient for the new “State”. As the Court observed:<sup>93</sup>

“A man-made artificial platform, such as the so-called Duchy of Sealand, cannot be called either ‘a part of the earth’s surface’ or ‘land territory’ and only structures which make use of a specific piece of the earth’s surface can be recognised as State territory within the meaning of international law.”

The Court however went beyond the guidelines of the Convention, and observed that:

“The State, as an amalgamation of many individuals ... has the duty to promote community life. This duty does not merely consist of the promotion of a loose association aimed at the furtherance of common hobbies and interests. Rather it must be aimed at the maintenance of an essentially permanent form of communal life in the sense of sharing a common destiny ...”<sup>94</sup>

“The so-called ‘nationals’ of the ‘Duchy of Sealand’ do not satisfy these criteria for community life. Apart from the 30 to 40 persons permanently living on the platform, who are responsible for its defence and the maintenance of its installations, the presence of the other so-called ‘nationals’ is limited to occasional visits. The territorial extent of the ‘Duchy’ of merely 1300 square metres does not satisfy the requirements for the permanent residence of all its ‘nationals’. The life of the State is not limited to the provision of casinos and places of entertainment. Rather a State community must play a more decisive role in serving the other vital human needs of people from their birth to their death. These needs include education and professional training, assistance in all the eventualities of life and the provision of subsistence allowances where necessary. The so-called ‘Duchy of Sealand’ fails to satisfy any of these requirements. Regardless of the material prerequisites which an entity must have in order to constitute a ‘people’ under international law, the ‘nationals’ of the ‘Duchy’

89 Territorial Waters Jurisdiction Act 1878 (41 & 42 Vict c 73) (UK); Continental Shelf Act 1964 (UK); Continental Shelf (Designation of Areas) Orders 1964 to 1982 (UK). The territorial waters were extended to 12 nautical miles by the Territorial Sea Act 1987 (UK); Continental Shelf (Designated Areas) (Extended Territorial Sea) Order 1987 (SI 1987/1265) (UK).

90 25 October 1968 at Shire Hall, Chelmsfort, Essex. This has apparently been confirmed by diplomatic correspondence by the Ministry of Finance of the Federal Republic of Germany of 14 June 1977, IV C5-S 1300-118/77, and the Ministry of Finance of Belgium of 25 May 1980, 1/3 R9 DIV/313.941. The difference in the approach taken in the *Ray* case is instructive. There, the emphasis was on the control of the continental shelf, rather than jurisdiction of courts beyond territorial waters - which the US then set at 3 nautical miles.

91 *In re Duchy of Sealand* (1978) 80 ILR 683 (Administrative Court of Cologne), cf <<http://www.sealandgov.com>> (as at 18 July 2002).

92 *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force on 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, vol 6, p 620, available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002).

93 *In re Duchy of Sealand* (1978) 80 ILR 683, 685 (Administrative Court of Cologne), cf <<http://www.sealandgov.com>> (as at 18 July 2002). It may be, however, that this was an unduly narrow interpretation.

94 See n 93.

themselves fail to satisfy an essential condition for their classification as a people. These ‘nationals’ have not acquired their ‘nationality’ in order to live with one another and handle all aspects of their lives on a collective basis, but on the contrary they continue to pursue their individual interests outside the ‘Duchy’. The common purpose of their association is limited to a small part of their lives, namely their commercial and tax affairs. This degree of common interest cannot be regarded as sufficient for the recognition of a ‘people’ within the meaning of international law.”<sup>95</sup>

However, despite this judgment, the United Kingdom authorities did little to assert their authority over the platform, though (perhaps unsurprisingly) they still do not recognise it as a State.<sup>96</sup> But the “State” continues to exist, albeit precariously.

On 30 September 1987, Prince Roy declared the extension of Sealand’s territorial waters to 12 nautical miles, pre-empting the declaration on 1 October 1987 that British territorial waters had been extended from 3 to 12 nautical miles.<sup>97</sup>

In 1999, Sealand began a resurgence, due to an alliance with HavenCo, providers of internet servers. Prince Regent Michael, who has acted for his father as ruler of the principality since 1999 – although he lives at Leigh-on-Sea in Essex, on the mainland of Britain – leased Sealand to HavenCo, an Antigua-registered firm run by husband and wife team Sean and Jo Hastings.<sup>98</sup> The aim is to avoid United Kingdom laws, and taxes on e-commerce activities.<sup>99</sup> According to the company’s own publicity material, “HavenCo has been providing services since May 2000 and is fully operational, offering the world’s most secure managed servers in the world’s only true free market environment, the Principality of Sealand”.<sup>100</sup> The claims continue thus:

“The Sealand Government is ideal for web business, as there are no direct reporting or registration requirements.”<sup>101</sup>

“HavenCo Limited is exploiting a unique opportunity to set up the world’s first real data haven. The initial showcase datacenter is the Principality of Sealand, the world’s smallest sovereign territory. It was founded over thirty years ago and has obtained a unique legal status as the only sovereign man-made island. Its claim to sovereignty has been tested and supported in several legal challenges.”<sup>102</sup>

“Sealand has no laws governing data traffic, and the terms of HavenCo’s agreement with Sealand provide that none shall ever be enacted.”<sup>103</sup>

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95 See n 93, pp 687-688. This is also arguably narrow, because the focus is on the whole body of citizens.

96 “Sealand offers online ‘data haven’”, USA Tech Report quoting Foreign Office spokesman Robin Twyman, available at <<http://www.usatoday.com/life/cyber/tech/cti162.htm>> (as at 15 July 2002).

97 See “History of Sealand”, available at <<http://www.sealandgov.com/history.html>> (as at 15 July 2002); Territorial Sea Act 1987 (UK); Continental Shelf (Designated Areas) (Extended Territorial Sea) Order 1987 (SI 1987/1265) (UK).

98 S Mathieson, “Prince Michael of Sealand cries freedom”, uk.internet.com (20 October 2000), available at <<http://www.vnunet.com/Analysis/1112812>> (as at 15 July 2002).

99 S Mathieson, “Pirate ISPs and the Sealand case”, (9 June 2000), available at <<http://www.vnunet.com/Analysis/1102943>> (as at 15 July 2002).

100 See <<http://www.havenco.com>> (as at 15 July 2002).

101 See n 100.

102 See n 100.

103 See n 100.

HavenCo's plan is to allow any type of internet services to be hosted at Sealand, with the exception of child pornography and the unsolicited mass broadcast of messages ("spam"). HavenCo has already agreed to host the internet presence of the Tibetan government in exile (Tibet Online<sup>104</sup>) from Sealand.<sup>105</sup> HavenCo claims that the combination of Sealand's declared independence from the United Kingdom, sophisticated encryption techniques, and the laissez-faire attitude of Sealand ruler Roy Bates will give customers unprecedented freedom and security.<sup>106</sup> The Home Office, the United Kingdom agency responsible for enforcement of internet laws, says that it expects Sealand and any business operating on it to follow British laws.<sup>107</sup> While the United Kingdom might have done little to assert jurisdiction over the offshore enclave in the past, any prospect of its use for digital money laundering, gambling or tax evasion might quickly result in a re-assertion (or assertion) of British sovereignty.<sup>108</sup>

The Government of the United Kingdom can assert that it owns the platform, which is on the continental shelf (on the *Ray* analogy). Sealand also lies within the United Kingdom's 12 nautical mile territorial water limit, though – perhaps crucially – it did not do so when the independence of the platform was first proclaimed. Ultimately, the existence of Sealand can be ended as easily as that of the Grand Capri Republic, or of the Republic of Minerva. The establishment of internet servers on the platform are no more a sign of statehood than the operation of pirate radio stations. As soon as significant regulatory issues arise the United Kingdom authorities are likely to act to end Sealand's de facto statehood. However, the longer this is delayed the stronger are claims that Sealand has de jure statehood, despite its artificiality and minimal population. It may be that, despite the finding of the Administrative Court of Cologne,<sup>109</sup> and in light of the passage of years,<sup>110</sup> Sealand has a sufficiently permanent population, government, and capacity to enter into diplomatic relations, and would meet the criteria of the Montevideo Convention.<sup>111</sup> However, difficulties remain with respect to the existence of a defined territory, for Sealand is nothing more than an artificial platform.

In terms of the attributes of a successful tax haven, Sealand is apparently equipped with sophisticated information-exchange facilities, and it is within easy reach of a major financial centre. But whether it has political and economic stability is another matter.<sup>112</sup> A platform or boat in international waters – if it were able successfully to establish statehood – could be both tax and regulation free. But these advantages are obtained also in the Bahamas, or any one of the existing land-based tax havens. As well

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104 See <<http://www.tibet.org/tibet.org/index.html>> (as at 19 July 2002).

105 See <<http://www.havenco.com>> (as at 15 July 2002).

106 See n 105.

107 "Sealand offers online 'data haven'", USA Tech Report quoting Foreign Office spokesman Robin Twyman, available at <<http://www.usatoday.com/life/cyber/tech/cti162.htm>> (as at 15 July 2002).

108 J Markoff, "Rebel Outpost on the Fringes of Cyberspace", *The New York Times*, 4 June 2000, available at <<http://www.nytimes.com/library/tech/00/06/biztech/articles/04have.html>> (as at 15 July 2002).

109 *In re Duchy of Sealand* (1978) 80 ILR 683 (Administrative Court of Cologne), cf <<http://www.sealandgov.com>> (as at 18 July 2002).

110 Which may give legitimacy to claims of both a permanent population and a government.

111 *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, vol 6, p 620; available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002).

112 Since 1978, a German group has claimed to be the Government-in-Exile of Sealand. They have an internet presence at <<http://www.principality-of-sealand.de>> (as at 18 July 2002). The "official" site is at <<http://www.sealandgov.com>> (as at 18 July 2002).

as tax and legal-haven advantages, companies in the Bahamas would benefit from an established legal system and infrastructure, which would not be the case on a platform or ship.<sup>113</sup>

As in the case of the previous structures examined, these artificial entities cannot be said to meet Palan's requirements for success as tax havens.<sup>114</sup> They generally do not have political and economic stability. Sealand may be equipped with sophisticated information-exchange facilities and within easy reach of a major financial centre. It is unlikely, however, that it will have agreements with major countries to avoid double taxation and regulation. Yet, so long as it operates on a relatively small scale it seems that the United Kingdom authorities have been unwilling actively to enforce domestic laws over Sealand. In such a situation could lie the seeds of future political recognition and eventual tax haven status. But success is at best uncertain.

## 8.0 REAL SMALL STATES OF DUBIOUS STATUS

If artificial platforms and islands are generally untenable, there remains the option of the Principality of Seborga. This is located in Liguria, on the Italian Riviera, close to the French border. The Principality's territory amounts to 14 square kilometres, and it has a population of 2000 inhabitants – of whom only 362 living in the 5 square kilometre capital are citizens.<sup>115</sup> This is not merely a would-be independent State declared by a lone eccentric. It is one that may have some historical claim to legitimacy.

In 954 AD, Count Guido of Ventimiglia bestowed the castle, the Saint Michael's Church in Ventimiglia, and a large portion of land on the monks of Lerins. In 1079, Seborga became a Principality of the Holy Roman Empire. Seborga remained a Cistercian State until 1729, when the principality was sold to Vittorio Amedeo II of Savoy, Prince of Piedmont and King of Sardinia. But this change was never, according to advocates for an independent Seborga, registered with the Kingdom of Sardinia, nor with the House of Savoy.<sup>116</sup>

At subsequent stages in the unification of Italy, Seborga was never mentioned by name. According to its advocates, the Principality of Seborga has never been considered part of the Italian Republic formed in 1946.<sup>117</sup> In view of this alleged status, in 1963 the people of Seborga elected a new Prince, Giorgio I. On 23 April 1995, Seborgans voted for the principality's Constitution.<sup>118</sup> It declared its independence in 1996. Seborga is successful as a tourist resort. But whether its independence will ever be more than just an attraction to tourists is doubtful. As a State situated between Italy and France – and a near neighbour of Monaco – Seborga has potential for development as a tax haven, provided its legal status as a State can be established, which is doubtful.<sup>119</sup> Currently the citizens of the putative State continue to pay taxes to Italy.

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113 S Mathieson, "Prince Michael of Sealand cries freedom", uk.internet.com (20 October 2000), available at <<http://www.vnunet.com/Analysis/1112812>> (as at 15 July 2002).

114 R Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151.

115 Principato di Seborga, "The Principality, Where is it?" at <<http://www.masterweb.it/seborga/eng-3.htm>> (as at 15 July 2002). The total population of the principality is approximately 2,000.

116 Principato di Seborga, "History of the Principality" at <<http://www.masterweb.it/seborga/eng-2.htm>> (as at 15 July 2002).

117 See n 116.

118 Principato di Seborga, "Why a Principality" at <<http://www.masterweb.it/seborga/eng-4.htm>> (as at 15 July 2002).

119 Though it may be possible for Seborga to utilise its near proximity to both France and Italy to its advantage.

Seborga, and similar potential States, enjoy several important advantages over artificial sea platforms. Seborga has a permanent population, and a defined territory. It may also possess a government, and possibly the capacity to enter into diplomatic relations. This would meet the criteria for statehood of the Montevideo Convention.<sup>120</sup> However, it may not meet the criteria laid down by the European Union for recognising new States in Eastern Europe and the former Soviet Union in 1991-1992, based on the guidelines adopted by the European Commission Member States on 16 December 1991.<sup>121</sup> This recognition may be denied it.

Compared with the artificial constructs examined previously, genuine States of dubious status do meet some of the requirements for a successful tax haven. They may well have economic if not political stability – they do at least have a settled population. Being physically based on land it is easier for them to achieve access to large international markets. While it is unlikely that any will have agreements with major countries to avoid double taxation and regulation, they have a better chance of achieving international credibility and recognition. The main difficulty would be that their status is doubtful, and they cannot simply be created as investors might wish, since they depend upon the vagaries of history. Indeed, they offer no advantage over existing tax havens, and present some additional disadvantages.

## 9.0 VIRTUAL STATES

The next example of a non-traditional alternative to tax havens is the newest and least orthodox. It is not a territorial State at all. The internet, or “cyberspace”, is an interconnected electronic communications network. It has no physical existence as a whole, though comprised of a large number of individual networks.<sup>122</sup> In essence the internet exists in a virtual world, rather than in the real, geographical, world.<sup>123</sup> The internet has no controlling body,<sup>124</sup> although it does have a common

120 *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, vol 6, p 620, available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002). Although the application of the Convention is confined to Latin America, it is regarded as declaratory of customary international law. See also *Island of Palmas Arbitration Case* (1928) No xix (2) Reports of International Arbitral Awards 829; (1928) 22 *American Journal of International Law* 986; 4 Arbitration Decisions 3.

121 “Guidelines on Recognition of New States in Eastern Europe and in the Soviet Union” (1992) 31 *International Legal Materials* 1486-1487. The list of criteria established the conditions that had to be fulfilled before the Community was prepared to recognize the new States, and thus to agree to their admission to the community of States and to the international community. It has been claimed that the conditions listed in the guidelines are merely the criteria for the establishment of diplomatic relations - something which is in the political discretion of the States in any case - and not requirements for statehood in the sense of international law.

122 The result being a conceptual confusion: see J Goldsmith and L Lessig, “Grounding the Virtual Magistrate”, available at <<http://mantle.sbs.umass.edu/vmag/groundvm.htm>> (as at 18 July 2002).

123 G Zekos, “Internet or Electronic Technology: A Threat to State Sovereignty” (1999) 3 *Journal of Information, Law and Technology*, available at <<http://elj.warwick.ac.uk/jilt/99-3/zekos.html>> (as at 10 September 2002); DG Post and DR Johnson, “‘Chaos Prevailing on Every Continent’: Towards a New Theory of Decentralized Decision-Making in Complex Systems” (14 June 1999) Social Science Research Network Electronic Library, available at <[http://www.papers.ssrn.com/paper.taf?ABSTRACT\\_ID=157909](http://www.papers.ssrn.com/paper.taf?ABSTRACT_ID=157909)> (as at 23 July 2002). See also D Burk, “Federalism in Cyberspace” (1996) 28 *Connecticut Law Review* 1095; J Reidenberg, “Governing Networks and Rule-Making in Cyberspace”, in B Kahin and C Nesson (eds), *Borders in Cyberspace*, Cambridge, MIT Press, 1996, pp 84, 85-87.

124 Though the Internet Corporation for Assigned Names and Numbers (ICANN) regulates some aspects of the net. This is the non-profit corporation that was formed to assume responsibility for the Internet Protocol (IP) address space allocation, protocol parameter assignment, domain name system management, and root server system management functions previously performed under United States Government contract by Internet Assigned Numbers Authority (IANA) and other entities. That no single country can regulate the internet is seen in the internationalisation of ICANN. See for instance, JS

language, allowing different operating systems to speak to one another.<sup>125</sup> A State created on the internet would have no corporeal existence, yet it may be no less real for that. Such internet States could conceivably be used to avoid taxation liability, particularly in an age of electronic money.

There has been a tendency to claim that the changes we observe in notions of sovereignty, the State, jurisdiction, and law in general are caused by the internet.<sup>126</sup> But, as has been observed by various writers, globalisation of commerce is not a new phenomenon.<sup>127</sup> Our existing international law is predicated on the existence of the sovereign State. The notions of sovereignty and statehood were once among the most important aspects of public international law.

But to be a State, a territory must have a permanent population,<sup>128</sup> it must have a defined territory,<sup>129</sup> it must have a government, and it must have the capacity to enter into diplomatic relations.<sup>130</sup> No other entity could be regarded as a State, whatever its *de facto* power. This definition remains politically important, though additional factors have increased in relevance and importance.

The notions of sovereignty and statehood are not easily defined or explained. To a large degree this is because they are principally political concepts, rather than merely legal principles. With the growth in both the (horizontal) extent and (vertical) reach of international agreements, treaties, conventions and codes, statehood is becoming a less dominant feature. This tendency is becoming more noticeable in the modern commercial environment, and especially in the context of the internet as the level at which economic decisions are increasingly taken, though States remain the level at which taxation is levied.

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Fishkin, "Deliberate Polling As a Model for ICANN Membership", study paper from the Berkman Centre for Internet and Society at Harvard Law School, available at <<http://www.cyber.law.harvard.edu/rcs/fish.html>> (as at 23 July 2002).

125 At its highest level coordinated by the Internet Assigned Numbers Authority (IANA) and a central Internet Registry (IR); DR Johnson and DG Post, "And How Shall the Net be Governed? A Meditation on the Relative Virtues of Decentralized, Emergent Law", draft paper at Cyberspace Law Institute Papers on Cyberspace Law, available at <<http://www.cli.org/emdraft.html>> (as at 23 July 2002).

126 It has been said that the very nature and growing importance of the internet requires a fundamental re-examination of the institutional structure within which rulemaking takes place: see Johnson and Post, n 125.

127 The analogy between the rise of a separate law of cyberspace and the Law Merchant has been observed: see IT Hardy, "The Proper Legal Regime for 'Cyberspace'" (1994) 55 *University of Pittsburgh Law Review* 993, p 1020; N Cox, "The Regulation of Cyberspace and the Loss of National Sovereignty" (2002) 11(3) *Information and Communication Technology Law* 241.

128 See the judgment of the International Court of Justice in the *Western Sahara*, Advisory Opinion, International Court of Justice Reports 12, 63-65 (1975); 59 ILR 30, 80-82.

129 Which may however be very small, or even of varying extent: *United States v Ray*, 281 F Supp 876 (SD Fla 1965); *Atlantis Development Corporation v United States*, 379 F 2d 818 (5th Cir 1967); *United States v Ray*, 294 F Supp 532 (SD Fla 1969); and *United States v Ray*, 423 F 2d 16 (5th Cir 1970); *Chierici and Rosa v Ministry of the Merchant Navy and Harbour Office of Rimini*, 71 ILR 258 (14 November 1969) partial English translation and fact summary (citing (1975) 1 *Italian Yearbook of International Law* 265) (Council of State); *In re Duchy of Sealand* (1978) 80 ILR 683 (Administrative Court of Cologne), cf <<http://www.sealandgov.com>> (as at 18 July 2002).

130 This was expressly outlined in the *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force on 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, vol 6, p 620; available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002). Although the formal application of the Convention is confined to Latin America, it is regarded as declaratory of customary international law. The Arbitration Commission of the European Conference on Yugoslavia, in Opinion No 1, declared that: "The state is commonly defined as a community which consists of a territory and a population subject to an organised political authority." (See 92 ILR 162, 165). On the Arbitration Commission generally, see M Craven, "The EC Arbitration Commission on Yugoslavia" (1995) 66 *British Yearbook of International Law* 333.

The jurisdiction of national courts is based upon the domestic laws of individual countries.<sup>131</sup> Similarly, the legislative jurisdiction of a State is limited to its territory.<sup>132</sup> The advent of cyberspace has not meant the decline of domestic law. But it has “pushed the boundaries”.<sup>133</sup> Border controls on the internet are not impossible to develop and implement.<sup>134</sup> Many governments already regulate cyberspace.<sup>135</sup> It may be that the most effective means to achieve this is to regulate the architecture of cyberspace.<sup>136</sup> But for the most part the internet is international; nor are its users adequately served by existing laws with respect to conflict of laws.<sup>137</sup> And global computer-based communications cut across territorial borders,<sup>138</sup> creating a new realm of human activity and undermining the feasibility<sup>139</sup> – and legitimacy<sup>140</sup> – of applying laws based on geographic boundaries.<sup>141</sup> Furthermore, the internet threatens

131 DR Johnson and DG Post, “Law and Borders: The Rise of Law in Cyberspace” (1996) 48 *Stanford Law Review* 1367.

132 See I Brownlie, *Principles of Public International Law* (5th ed), New York, Clarendon Press, 1998, p 301; R Jennings and A Watts (eds), *Oppenheim’s International Law* (9th ed), London, Longman, 1992, vol 1, p 456; FA Mann, “The Doctrine of Jurisdiction in International Law” (1964) 111 *Recueil des Cours* vol 1, 9, pp 10-13; FA Mann, “The Doctrine of Jurisdiction in International Law Revisited After Twenty Years” (1984) 186 *Recueil des Cours* vol 3, 9, p 20.

133 See, for example, T Puurunen, “The Legislative Jurisdiction of States over Transactions in International Electronic Commerce” (2000) 18 *John Marshall Journal of Computer and Information Law* 689.

134 *United States v Montoya de Hernandez*, 473 US 531; *The Chinese Channel Limited* <<http://www.chinese-channel.co.uk>> (as at 10 September 2002). See also A Wells Branscomb, “Jurisdictional Quandaries for Global Networks”, in LM Harasim (ed), *Global Networks: Computers and Informational Communication*, Cambridge, MIT Press, 1993, pp 83 and 103.

135 “Framework for Global Electronic Commerce”, available at <<http://www.ecommerce.gov/>> (as at 13 September 2002); “Management of Internet”, available at <<http://www.ntia.doc.gov/>> (as at 10 September 2002). Their legal right to do so is undoubted: *US v Smith*, 680 F 2d 255 (1st Cir Mass 1982). See also President’s Working Group on Unlawful Conduct on the Internet, “The Electronic Frontier: The Challenge of Unlawful Conduct Involving the Use of the Internet” (March 2000), available at <<http://www.usdoj.gov/criminal/cybercrime/unlawful.html>> (as at 23 July 2002).

136 G Greenleaf, “An Endnote on Regulating Cyberspace: Architecture vs Law?” (1998) 21 *University of New South Wales Law Journal* 593, available at <<http://www.austlii.edu.au/au/other/unswlj.OLD/thematic/1998/vol21no2/greenleaf.html>> (as at 18 July 2002).

137 The efficacy of the concept of “closest and most real connection” (*McConnell Dowell Constructors Ltd v Lloyd’s Syndicate* 396 [1988] 2 NZLR 257 (CA)) is also reduced, in that no part of the world is any more directly affected than any other by events on the web, as information is available simultaneously to anyone with a connection to the internet; DR Johnson and DG Post, “Law and Borders: The Rise of Law in Cyberspace” (1996) 48 *Stanford Law Review* 1367. Nor, in terms of the protection of intellectual property rights: DL Burk, “Muddy Rules for Cyberspace”, (25 May 2000) Social Science Research Network Electronic Library, available at <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=204188](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=204188)> (as at 23 July 2002).

138 Location remains important, but it is virtual location, rather than physical location. There is no necessary connection between an internet address and a physical location. For a general description of the Domain Naming System, see DL Burk, “Trademarks Along the Infobahn: A First Look at the Emerging Law of Cybermarks” (1995) 1 *University of Richmond Journal of Law and Technology* 1.

139 Something which may be related to the relative length of the virtual border: see DR Johnson and DG Post, “Law and Borders: The Rise of Law in Cyberspace” (1996) 48 *Stanford Law Review* 1367.

140 With the dominance of democratic concepts of government, it might be thought that if the people believe that an institution is appropriate, then it is legitimate: PB Cowen, “Neo Liberalism” in R Miller (ed), *New Zealand Politics in Transition*, Auckland, Oxford University Press, 1997, p 341. But this scheme leaves out of account substantive questions about the justice of the State and the protection it offers the individuals who belong to it. This point is illustrated by the study of the application of the model to Mummah Qadhafi’s Libya: Saleh Al Namlah, “Political Legitimacy in Libya Since 1969”, PhD thesis, Syracuse University, 1992. It is generally more usual to maintain that a State’s legitimacy depends upon its upholding certain human rights: J Rawls, *Political Liberalism*, New York, Columbia University Press, 1993; T Honerich (ed), *The Oxford Companion to Philosophy*, Oxford, Oxford University Press, 1995, p 477 “Legitimacy”; M Swanson, “The Social Contract Tradition and the Question of Political Legitimacy”, PhD thesis, University of Missouri-Columbia, 1995.

141 DR Johnson and DG Post, “Law and Borders: The Rise of Law in Cyberspace” (1996) 48 *Stanford Law Review* 1361.

traditional political institutions and perhaps even the very concept of sovereignty itself.<sup>142</sup> As Zekos has written, the real jurisdictional novelty of cyberspace is that it will give rise to more frequent circumstances in which effects are felt in multiple territories at once.<sup>143</sup> Traditional international legal rules on jurisdiction do not fit the internet context, nor do they facilitate cooperation on international regulation. The limits of national control of the internet are perhaps exaggerated. Principally that is because nations are increasingly acting in concert to deal with the borderless nature of cyberspace by creating both relatively uniform laws across jurisdictions, and agreements for international cooperation in surveillance and investigation.<sup>144</sup>

As well as being a threat to sovereign authority, the internet may allow new opportunities for an increase in surveillance<sup>145</sup> and authority<sup>146</sup> – or for an increase in public participation in government. Increasingly, private, non-State parties are regulating cyberspace.<sup>147</sup> But this does not yet equate to “sovereignty”, nor can one avoid tax liability by utilising a virtual residence, since money requires a physical abode – even if only for juridical purposes.

Internet-based entities could not be said to meet Palan’s requirements for success as tax havens.<sup>148</sup> They would not have political and economic stability, since they could be created and abolished by the actions of an individual computer operator. Since they would be virtual rather than real they would be within easy reach of any major financial centre. But they would lack international credibility, and they may never emerge from the virtual world of cyberspace.

## 10.0 SPECIAL DEVELOPMENT REGIONS AND TRIBAL AUTHORITIES

One of the principal reasons for the upsurge in criticism of tax havens has been the perception that they illegitimately deprive governments of the taxation revenue which they are due.<sup>149</sup> The desire to protect and enhance revenue is as much a social policy objective as it is economic. The alternatives to

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142 W Lash, “The Decline of the Nation State in International Trade and Development” (1996-97) *Cardozo Law Review* 1001; B Sanford, “Teaching an Old Dog New Tricks” (1995-96) 28 *Connecticut Law Review* 1137, p 1170; D Buck, “Patents in Cyberspace: Territoriality and Infringement on Global Computer Networks” (1993-94) 68 *Tulane Law Review* 1; WB Wriston, *The Twilight of Sovereignty*, New York, Scribner, 1992 (examining the challenges to sovereignty posed by the information revolution).

143 G Zekos, “Internet or Electronic Technology: A Threat to State Sovereignty” (1999) 3 *Journal of Information, Law and Technology*, available at <<http://elj.warwick.ac.uk/jilt/99-3/zekos.html>> (as at 10 September 2002).

144 See AB Overby, “Will Cyberlaw be Uniform?: An Introduction to the UNCITRAL Model Law on Electronic Commerce” (1999) 7 *Tulane Journal of International and Comparative Law* 219; G Greenleaf, “An Endnote on Regulating Cyberspace: Architecture vs Law?” (1998) 21 *University of New South Wales Law Journal* 593, available at <<http://www.austlii.edu.au/au/other/unswlj.OLD/thematic/1998/vol21no2/greenleaf.html>> (as at 18 July 2002).

145 See Greenleaf, n 144.

146 See, for instance, J Linchuan Qiu, “Virtual Censorship in China: Keeping the Gate between the Cyberspaces” (1999/2000) 4 *International Journal of Communications Law and Policy* 1.

147 PS Berman, “Cyberspace and the State Action Debate: The Cultural Value of Applying Constitutional Norms to ‘Private’ Regulation” (2000) 71 *University of Colorado Law Review* 1263.

148 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 151.

149 D Spence, “Stepping Up the Pressure on Tax Havens: An Update” (2001) Vol 7:3 *New Zealand Journal of Taxation Law and Policy* 170; M Ngoy, “The Paradox of Tax Havens: Consequences of the Subjective Approach” (2001) Vol 7:3 *New Zealand Journal of Taxation Law and Policy* 154; B James, “Tax Havens Face OECD Threat of Sanctions”, *International Herald Tribune*, available at <<http://www.iht.com/IHT/BJ/00/bj061400.html>> (as at 18 July 2002).

the traditional tax haven outlined above are no less a threat to this revenue, and are therefore just as likely to face the opposition of governments.

There is, however, one way around this apparently unavoidable difficulty. There have been a number of tribal authorities and special development regions that have been permitted to become, if not tax havens, at least areas where special tax benefits may be obtained – with the blessing, or at least acquiescence, of government – for the furtherance of social and political objectives. These have developed as a consequence of a resurgence of the interests and rights of tribal and indigenous peoples in western countries in particular.<sup>150</sup> For example, in some States of the US, native American tribal authorities own and operate casinos and other commercial ventures, largely unfettered by ordinary State taxes.<sup>151</sup> While such authorities do not present a complete answer – and they will likely be subject to regulation – they at least usually have the support of governments. Unlike in many tax havens, such privileges are seen as serving worthwhile social objectives, rather than allowing rich people and companies to avoid paying taxes on their already ample assets.

These entities often meet Palan's requirements for success as tax havens.<sup>152</sup> They generally have political and economic stability. They may be supported by a large international market, or equipped with sophisticated information-exchange facilities, and within easy reach of a major financial centre, depending upon the nature of the region. They will often have agreements with their national government to minimise taxation and regulation. They are not necessarily tainted by scandals and by the laundering of proceeds of criminal or drugs activities. Finally, their international credibility stems from their official or quasi-official nature. They offer the best alternative available to the traditional tax haven.

## 11.0 CONCLUSION

Tax havens cannot simply be abolished, as they are a manifestation – and a consequence – of State sovereignty.<sup>153</sup> A State may obtain benefits from offering taxation advantages to certain non-residents. But they do not suit every investor. However, non-traditional tax havens, based on non-State entities or quasi-States, offer no real alternative.

There are serious difficulties facing ephemeral States such as Sealand, which are unlikely to be given the opportunity to develop fully as alternatives to tax havens. States with some claim to sovereignty, such as Seborga, may have better prospects of success. But even here they will offer few if any advantages over traditional tax havens. Even special development regions and tribal authorities offer only partial answers – though they are more viable. Political and economic stability are essential, as is

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150 S Krasner, "Sovereignty: An Institutional Perspective" (1988) 21 *Comparative Political Studies* 66.

151 Despite the clear legal obligation of Indian tribes to collect and remit State taxes imposed on commodities sold by tribes to non-Indian consumers, many tribes evade this responsibility. Unfortunately for the States and for non-Indian retailers, little can be done to prevent this. States lack the jurisdiction to enforce the collection of taxes on Indian reservations, and sovereign immunity shields Indian tribes from any legal challenge which States or non-Indian businesses may initiate to compel the tribes to collect and remit the taxes they owe. See *Washington v Confederated Tribes of Colville Indian Reservation*, 447 US 134, 160-161 (1980); *Moe v Confederated Salish & Kootenai Tribes of Flathead Reservation*, 425 US 463, 475-476 (1976); *New York Dept of Taxation & Finance v Milhelm Attea & Bros*, 114 S Ct 2028, 2031 (1994).

152 R Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151.

153 See n 152, p 173.

international credibility. These have generally been denied the newly-created States, which rarely satisfy even one of the requirements for statehood,<sup>154</sup> let alone those of a successful tax haven.<sup>155</sup>

The future may lie in space. Article II of the 1967 Treaty on Principles Governing the Activities of States in the Exploitation and Use of Outer Space provides that:<sup>156</sup>

“Outer space, including the Moon and other celestial bodies, is not subject to national appropriation by claim of sovereignty, by means of use or occupation, or by any other means.”

Perhaps some latter-day Morton Meads may claim the Moon as his private kingdom, and thereby bewilder the taxation and governmental authorities on the earth?

*This revised article was accepted for publication on 31 July 2003*

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154 *Montevideo Convention on the Rights and Duties of States*, 26 December 1933, 49 Stat 3097; USA Treaty Series 881, entered into force on 26 December 1934, in MO Hudson (ed), *International Legislation*, Washington, Carnegie Endowment for International Peace, 1931-50, vol 6, p 620, available at <<http://www.yale.edu/lawweb/avalon/intdip/interam/intam03.htm>> (as at 12 September 2002).

155 R Palan, “Tax Havens and the Commercialization of State Sovereignty” (2002) 56 *International Organization* 151.

156 *Multilateral Treaty on Principles Governing the Activities of States in the Exploration and Use of Outer Space, including the Moon and other Celestial Bodies*, 27 January 1967, 610 UNTS 205, entered into force 10 October 1967.