The Atlantic

The Intractable Problem of Tax Havens

Perhaps in theory there are ways to fix tax avoidance, but they aren't politically feasible.

Vaduz Castle in Lichtenstein

Arnd Wiegmann / Reuters

Libertarian anarchists used to say "taxation is theft." New research by economist Gabriel Zucman suggests that there is some truth to this—when tax havens are taken into consideration. In his new book *The Hidden Wealth of Nations*, he makes a persuasive case that the way taxes are levied now—whether on income, wealth, capital gains or corporate profits—allows tax havens to steal revenue from other nations. For ordinary people, this means extra money taken from their pockets, in the form of an increased tax burden, because the world's wealthiest individuals and firms aren't paying their fair share.

Zucman's main achievement in this slim volume is to have quantified these thefts: $200 billion in state revenues lost through private individuals' use of tax havens, plus another $130 billion in losses created by U.S. firms booking their profits offshore. While Zucman does not claim that his findings are comprehensive, he is rigorous and admirably forthcoming in explaining his methods and their limitations. He also makes a convincing case that despite these limitations, his findings represent a great leap forward in the effort—both by scholars and policy-makers—to grasp the effects tax havens have on the global economy.

Zucman showcases this remarkable feat in unusually lucid and elegant prose—particularly for an economist—complemented by an admirable grasp of history. His review of the ways that efforts to combat tax evasion have stalled for the past century makes the book a worthwhile read in and of itself. But perhaps the most ambitious aspect of Zucman's work is his claim that, despite the immense scale of the problem, there are ways to solve it and thereby put a stop to the recurrent economic and political crises triggered by the use of offshore finance.

His proposed solution involves three elements. One is the creation of a global financial register, modeled on existing information depositories such as Clearstream, to keep track of who owns all the financial securities in circulation throughout the world. This would include data on the ownership of mutual fund shares, as well as stocks and bonds. From what Zucman says, this part of the solution seems both technically and practically feasible.

The other two parts of his solution, however, seem strangely neglectful of the power relations and interests surrounding the use and governance of tax havens. His proposal would require international cooperation to impose a global tax on capital and to sanction tax havens through trade tariffs. For reasons alluded to in Zucman's own observations, this kind of coordination seems highly improbable.

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This is not so much a case of naïveté, the classic cheap-shot critique leveled at most proposals seeking to address what the book's subtitle calls (with Dickensian flair) "the scourge of tax havens." The problem is more one of incompleteness and oversimplification. While the "scourge" robs many states of crucial tax revenue, it also feeds many of these same states with revenues gained from hosting tax-avoidance activity. As many of the offshore financial centers have pointed out for years, countries like the U.S. and the U.K. are themselves among the biggest tax havens in the world. Through special tax shelters for foreign investors and innovations in trust and corporate law designed specifically to draw the business of high-net-worth individuals, Wall Street and the City of London are major players in an industry that the American and British governments publicly condemn. While their elected officials may bemoan revenue losses from tax evasion, these countries are playing a double game, facilitating that evasion through their own financial-services industries.

This creates a massive conflict of interest that would seem to doom any attempt to coordinate an international regime of sanctions against tax havens. For those two nations in particular, cracking down on international tax evasion would deal a serious blow to their economies. The interest groups representing finance wield a great deal of political power: This is one reason the policy landscape is littered with half-measures and failed initiatives like the European Savings Tax Directive—one of the policy "mistakes" Zucman analyzes in detail. But such instances should not be a surprise. As the political scientist Terry Moe observed more than 25 years ago, some policies are purposely designed to fail: They can be sabotaged *ab initio* by the interest groups that oppose them, simply because the democratic process often allows those opponents a significant voice in the policy-making process. Considering the political influence of the firms and professional groups who orchestrate tax evasion on a global scale, it seems very unlikely that an effective strategy could be developed through democratic means.

Until some method is devised to cut the Gordian knot of conflicted interests and countervailing political forces, the most likely future is one of more fatally flawed, unwieldy, and deeply unpopular policies like the widely loathed Foreign Accounts Tax Compliance Act (FATCA). Zucman's neglect of these conflicts of interest within nations, and his optimism about initiatives like FATCA—despite its lack of popular support—stand out as glaring anomalies in a text that is otherwise carefully considered and closely argued. Since Zucman is still at the beginning of what promises to be a brilliant career, there is every reason to hope that his future work will delve more deeply into the political side of political economy.

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