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Will High Taxes Force the Rich to Leave America?

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Treasury Secretary Steve Mnuchin is promising the "biggest tax cut" in U.S. history. A drop in the corporate rate from 35 to 15 percent would indeed be transformative. But for wealthy individuals, who foot the bill for America's debt-fueled spending binge, Trump's plan offers little relief.

The latest IRS data reveals that the top 1 percent of earners pay over 39 percent of total personal income tax revenues, while the top 5 percent pay 60 percent. Trump's proposed reduction of the top personal income tax rate from 39.6 percent to 35 percent—the same rate that prevailed as recently as 2012 when Barack Obama and Nancy Pelosi were in charge—would not fundamentally change this equation.

What might change, however, is the willingness of the rich to keep paying their taxes in the first place. The fact that a Republican-controlled government will not even *propose* a rate below 35 percent sends an unambiguous message to the wealthy. America has arrived at a new national consensus: a populist Republican Party now agrees with the Democrats that a tiny sliver of Americans should pay for everyone else's entitlements.

This paradigm shift should concern even those who otherwise agree with White House chief strategist Stephen Bannon that "all this theoretical Cato Institute, Austrian economics, limited government…doesn't have any depth to it." There's nothing theoretical about the fact that the wealthy—and the aspiring rich—have unprecedented opportunities to move their money abroad, beyond the reach of the IRS. Whatever fantasies of "social justice" or "economic nationalism" Washington is dreaming up, the game is over once the wealthy take to the shores of other countries less enchanted with Robin Hood economics.

Tax evasion, as David Burg notes in his encyclopedia of tax rebellions, "has been rampant and widespread from antiquity to the present" and probably "the most common of all forms of tax protest." Already, the Congressional Research Service estimates that the United States could be losing up to $100 billion in tax revenues from individual tax evasion.

This figure could be a mere pittance compared to the amount of tax avoidance—much of it entirely legal—that could proliferate through international tax havens. The higher the government keeps its upper income personal tax rate, the more likely it is that a wealthy elite—

empowered by globalization, inspired by anti-statist ideologies, and enabled with technological innovation—will leave the United States behind.

Whatever strong-arm tactics the government might use to compel taxpayers, the system ultimately works because Americans voluntarily acquiesce to it. The United States' anti-tax heritage notwithstanding, American compliance with the federal income tax historically has been quite high.

Wealthy American families did begin to take advantage of international tax havens during the interwar years. In a 1937 report to President Roosevelt, Treasury Secretary Henry Morgenthau implicated wealthy industrialists such as the Mellon and DuPont families for exploiting tax havens in the Bahamas, Panama, and Newfoundland. In subsequent years, the issue generated headlines from time to time when high-profile tax refugees left the country, as when the famed investor John Templeton renounced his citizenship in 1962 and took off to the Bahamas, ultimately saving over $100 million.

But these were distinct exceptions. Indeed, the very term "tax haven" was hardly used in the United States before the 1950s. And even during the 1950s and early 1960s, when the rich paid a federal income tax rate of over 90 percent, "relatively few United States citizens" as *The New York Times* reported in February 1961, were "attempt[ing] to avoid all taxes on business profits through the use of tax havens."

The reason is that the United States has historically maintained high "tax morale."Due to Americans' "perceptions of the government's trustworthiness and competence", U.S. citizens have complied with a "quasi-voluntary" tax code without forcing the IRS to using the full brunt of its coercive authorities. Wealthy Americans have tolerated progressive taxation when, in Georgetown law professor Itai Grinberg's words, they feel that "they are not being taken advantage of." This is borne out by public opinion polls. During the late 1950s and early 1960s, three in four Americans told pollsters that they trusted the government in Washington "to do what is right" either "most of the time" or "just about always."

Attitudes of the American rich, however, have been changing since the rise of offshore financial centers in the 1980s, when tax havens became "the heart of globalization." According to an analysis by UC Berkeley economist Gabriel Zucman, offshore personal wealth is "growing fast" principally for the purpose of evading taxes. U.S. residents own an estimated $1.2 trillion abroad, amounting to some 4 percent of the country's financial wealth. Eliminating revenue losses from tax havens would produce the equivalent of an 18 percent tax hike on the top .01 percent of income earners.

Over the past two decades, Washington has resorted to tougher sanctions to deter Americans' use of foreign holdings. Penalties for failing to report foreign-related transactions or abide by tax return filing requirements have increased significantly. A year after world leaders declared at the April 2009 G20 summit an "end of bank secrecy," President Obama signed into law the 2010 Foreign Account Tax Compliance Act (FATCA). The law threatens foreign financial institutions with a 30 percent withholding rate for failing to report information on asset holders.

These efforts, by and large, have proven ineffective. Revenue projections do not predict any significant effect from FATCA's enactment.

Instead, higher taxes and more stringent enforcement efforts have spiked rates of expatriation. Between 2008 and 2016, the number of Americans renouncing U.S. citizenship or terminating their long-term U.S. residency jumped by more than 2,240 percent. Among them: entertainer Tina Turner, who went to Switzerland; Bitcoin angel investor Roger Ver ("Bitcoin Jesus") who resides mostly in Japan; and Facebook co-founder Eduardo Saverin, who settled in Singapore. This, despite the State Department's 2014 decision to raise the fee for renouncing U.S. citizenship by 422 percent, making the fee more than 20 times the average rate of other high-income countries.

Plodding tax bureaucracies simply cannot compete with the powerful incentives created by market competition. "Competition among national governments," as Milton Friedman explained, "in the taxes they impose is every bit as productive as competition among individuals or enterprises in the goods and services they offer for sale and the prices at which they offer them." And contrary to the "race-to-the-bottom" predictions of anti-globalization critics, Nobel Prize winning economist Gary Becker found that, "competition among nations tends to produce a race to the top rather than to the bottom by limiting the ability of powerful and voracious groups and politicians in each nation to impose their will at the expense of the interests of the vast majority of their populations."

The big winners of America's wealth exodus are countries that can attract the rich with low tax rates. Offshore assets managed in Luxembourg have jumped 20 percent since 2009. Precise numbers, while unavailable, are almost certainly higher in the Asia-Pacific, not only in Hong Kong and Singapore, but also in more obscure places like the Cook Islands where "geographical remoteness" and "strategic detachment" from international treaties provide advantages over landlocked European competitors like Switzerland. As capital becomes more globally mobile, thriving offshore financial centers, particularly former British territories, are well-positioned to develop as tax havens due to their low tax rates and legacy legal systems from the colonial era. A cosmopolitan wealth management industry has sprouted to help the rich navigate new regulatory terrains—an industry that is guided by both a "professional jurisdiction" that "treats national boundaries as a resource to be exploited rather than as a limiting factor", as well as "an ethic reminiscent of medieval knighthood: an aristocratic code…dedicated to the cause of defending large concentrations of wealth from attack by outsiders."

Billions of electronic transfers out of the United States each year make it "almost impossible" for authorities to distinguish tax evasion from legal payments. This reality will generate added difficulties for the government as global e-commerce proliferates. About a quarter of Americans already earn money online, a number on the rise. Participants in online labor platforms are disproportionately young adults and consider their online incomes to be "essential" or "important" to their financial situations. The well-off and well-educated meanwhile tend to sell on online capital platforms.

The U.S. government, in short, is proving no match for the competition posed by international tax havens. Under the current progressive tax system, Washington is at the mercy of a small class of wealthy taxpayers—a group that American society increasingly cannot compel and must persuade to stay in the country.

Not only do today's rich have a tempting array of options beyond U.S. boundaries, they are ideologically unencumbered by the same nationalistic considerations that tugged at the conscience of an earlier generation of wealthy Americans. In her recent book *Capital without*

Borders: Wealth Mangers and the One Percent, Brooke Harrington found that today's "stateless super-rich themselves cannot be prevailed upon to pay taxes" for reasons incidental to economic self-interest. Why? Because they "belong nowhere in particular and can move at will…ideological appeals to patriotism and or civic duty are meaningless."

Indeed, many of today's wealthy are not simply agnostic about the American nation-state; they are driven to tax havens out of principled opposition to the excesses of progressive taxation. "Ideological warriors of offshore" as Nicholas Shaxon calls them in his book *Treasure Islands: Tax Havens and the Men Who Stole the World*, represent a growing network of American intellectuals, many of them "fanatical supporters" of Ayn Rand, who make a moral case for tax havens as "valiant resistance against tyranny." They welcome the fact that anti-statist ideologies considered "beyond the pale" in the United States are "allowed to grow without restraint offshore."

Overlapping with these communities are the same libertarian and anarchist innovators that champion other even more disruptive forms of tax havens. Cryptocurrencies like Bitcoin, according to UC Irvine law professor Omri Marian, have already advanced to the point that they could soon "replace tax havens as the weapon-of-choice for tax-evaders." Plans for establishing sea-based city-states, long advocated by disillusioned libertarians, passed a significant milestone this year with the signing of a memorandum of understanding for the first seastead in a French Polynesian lagoon.

Anti-government enthusiasts of cryptocurrencies and seasteading may be on the fringes of American politics, but they also epitomize a broader lack of trust in government. From a high of 77 percent in 1964, trust in government has plummeted to around 20 percent today.

During the late 2000's, when the rich were paying an individual tax of 35 percent, over two-thirds of Americans earning $250,000 or more felt they were overburdened with taxes. This in fact was the only income group that believed the U.S. tax system was unfair.

America's rich may not be ready to leave in droves for Seychelles or St. Kitts. But this is in large part because of the country's non-monetary appeal—an exceptional culture that celebrates the wealthy in a world where economic ambition is too often the victim of class warfare and stifling government overreach.

In a global economy with abundant tax havens, maintaining the loyalty—and the largess—of America's rich will require a tax code that respects their liberties. Trump's paltry tax cut offers little consolation.