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A Historian Looks at Tax Havens **by Charles Adams**

The recent attack on tax havens by the Organization for Economic Cooperation and Development (OECD) has depicted about 20–30 countries, called tax havens, as destructive of the high tax systems of the world, especially Europe.

The OECD argues that its members should gang up on these nations and shut down their financial centers unless their banking facilities are made “transparent” (a word of art they use, which means to place their banking information at the disposal of the national tax authorities of the world).

For those centers that will not do so, the OECD plans to place a banking embargo on their banks, preventing them from doing any banking with the OECD. This is a bold, aggressive move that would put an end to the ancient principle of English liberty that a “man’s castle is beyond the surveillance of the king.”

The OECD argues that “tax havens” are financial cesspools teeming with dirty money, crooks, and tax evaders, having no redeemable value for civilization.

That view needs to be corrected.

To put tax havens in proper perspective, we have to go back 3,500 years to the Book of Joshua, even to the Books of Moses, where the Lord ordered the Israelites to set aside cities of refuge, where a person could gain asylum from the punitive laws of Moses.

Hawaiian kings on the big island of Hawaii set aside a city of refuge. In the recent past, young Americans who had conscientious scruples against the Vietnam War fled to Canada and other Western countries as asylums against America’s draft laws.

A tax haven is somewhat similar. It is a kind of economic sanctuary, a modern city of refuge for those oppressed by the fiscal laws of their homeland. People can bring their wealth to a tax haven and avoid government confiscations by tax or exchange controls or just plain confiscations like those of Castro and other totalitarian rulers. These oppressive acts by their governments are as much an evil to them as political oppression.

Margaret Thatcher is remembered for cutting most British taxes in half, but she should be remembered most of all for getting rid of Britain's insidious exchange controls, one of Britain's worst contributions to civilization — an embarrassment to the Crown in principle and in practice.

In March 1972, the tax ministry's chief enforcement officer for exchange controls, Stanley Little, was reported on the front pages of the newspapers in London to have offered a bribe to Swiss bankers to obtain records of British subjects violating exchange controls. The Swiss government notified Little that he was *persona non grata* for Switzerland, and if he ever set foot in Switzerland he would be arrested.

The Jamaica Shuttle

Consider Jamaica, where exchange controls have ruined one of Britain's former colonies. In the 1960s Jamaica became independent and issued a new currency, the Jamaican dollar, worth US\$1.20. That is, it cost \$1.20 (or half a pound sterling) to buy one Jamaican dollar. Jamaica, unfortunately, had British-style exchange controls, meaning that all Jamaicans were locked into the Jamaican dollar.

No one could own foreign currency without the central bank's permission. Jamaica, as with most exchange-control nations, charges a huge fee to acquire foreign currencies for investments. Today, for example, in the Bahamas, the fee is 25 percent, meaning that your investment must increase by that amount for you to break even. After 30 years of exchange controls, the value of the Jamaican dollar is not US\$1.20, but 2¢. The Jamaican dollar lost 99 percent of its value. Today, it costs \$48 Jamaican for just US\$1. In Jamaica, as in other former colonies, "exchange controls" became the government's phrase for stealing.

When Michael Manley (a buddy of Castro) became prime minister, he was determined to crack down on Jamaicans with even harsher exchange controls than those in force. Many enterprising Jamaicans were not willing to sit by idly and watch their money become worthless. They took action and looked to a tax haven for help.

There followed a mass exodus of money from Jamaica to the Cayman Islands on small single-engine Cessna airplanes picking up bundles of Jamaican dollars on small roads and fields in Jamaica and flying 250 miles across the ocean to the Cayman Islands. This exodus was so extensive that the banks in Jamaica ran out of currency and made frantic calls to their sister banks in Cayman to return the currency. Jamaicans with their new accounts in a tax haven quickly converted their money to sound currencies. I think you could call the Jamaica Shuttle justifiable money laundering.

The virtues of tax havens

Protecting people from abusive exchange controls is one of the many virtues of tax havens — ask any Jamaican who used the Jamaica Shuttle. You cannot fault people for taking whatever steps they can to protect their wealth from plunder by governments. It is as instinctive as resisting a robber. Indeed the robbery label has been applied to taxation that borders on plunder since the days of the Roman Empire, with its tax system often called by both modern and ancient historians “organized robbery.”

OECD nations should look within — not at the havens — to see whether their systems of taxation qualify as a modern day “organized robbery.” Or perhaps as a “scaffolding for plunder,” as British historian James Coffield in 1970 described Britain’s graduating system of tax rates from 1 percent to 80 percent.

The protection of wealth

Governments and especially the OECD seem to believe that all citizens have a patriotic duty to pay any tax, no matter what the rates. U.S. presidential candidate George McGovern advocated 100 percent rates for the wealthy. Many objected (as did the voters), but no one touched on the moral issue. In Sweden, Astrid Lindgren the famous writer of children’s stories, published an open letter to the government complaining about her 102 percent tax rate. Her letter brought down the socialist government that had ruled for decades.

Taxpayers throughout history have made it clear, they have a patriotic duty, not to pay, but to resist an unfair tax — for there is an iron law of history that when governments tax too much or unfairly taxpayers will respond in some way for relief. It may be violence, as in the American and French Revolutions; or it may be fraud, as in the notorious evasion of the “royal fifth” by Spanish

galleons in the 16th and 17th centuries; or it may be flight to avoid taxes — today, flight to the havens.

Certainly, throughout history flight to avoid taxes has been taxpayers' first choice among ways to avoid intolerable taxation. It is not dangerous, like violent rebellion or fraud. But it puts a taxpayer's wealth beyond the reach of his government, for no government will aid another government to collect a tax. Not even the OECD can change that.

The ancient Greeks' solution to tax evasion was to make the rates so low that evasion was not worth the trouble. When President Reagan reduced the top tax rates to 28 percent (from 70 percent), many CPAs were confronted with taxpayers in the underground economy wanting to get back into the tax system and pay what they considered were acceptable rates.

In the 1920s, Andrew Mellon, U.S. secretary of the treasury, tried to put through a constitutional amendment that would put a cap on tax rates. Studies at the Treasury indicated that a 25 percent tax rate would produce the most revenue. Once the rate exceeded 25 percent, revenues would mysteriously decline. At that rate, taxpayers would pay without resorting to tax planning, and as the rates went up, tax planning kicked in, and revenue went down.

This discovery was not new. In ancient China, more than 2,000 years ago, the emperor consulted a sage or "wise one" on how to generate more tax revenues. The sage told him to reduce the tax from 20 percent to 10 percent and thereby stimulate the economy and generate more tax revenues. It worked.

Today most governments have lost sight of that truism. If the OECD would just learn that one lesson, they could put an end to the use of tax havens for tax avoidance. As for exchange controls, tax havens are needed. Once exchange controls are abolished, the need for tax havens will disappear.

Finally, a very insightful editor at *The Times* foretold the rise of tax havens on May 17, 1894, when Britain first adopted graduated rates:

Single out the big and moderately big properties for attack, and very soon as if by magic they will begin to evade you and disappear, as all things in the world very reasonably do when singled out for attack. Even the half starved crow will not wait to be continuously shot at.

Can the OECD succeed? First, we should be reminded that money owes no allegiance except to safety and profits. The "transparency" project will cripple many tax havens. To that extent, the

OECD will succeed, but the money will not end up in the tax coffers of the OECD nations as hoped, but will disappear “as if by magic.”

People know financial privacy is an absolutely essential key to protecting their wealth, and havens that join in the OECD’s transparency game can say goodbye to their tax-haven business. Already, in the Caribbean havens, many European banks are cutting staff, and one major Swiss bank in Cayman is reported to have shut down. Business is certain to move to those financial centers that will protect privacy — this is as certain as that the sun rises in the east.

Where will the accounts go?

To almost any country not playing the OECD’s transparency game. Switzerland most likely will be the recipient of many of the accounts that have taken flight. While a member of the OECD, they will not play their game; in fact, they cannot. Banking privacy in Switzerland is unlike the privacy laws in the tax havens of recent origin, where privacy laws were enacted to bring in business.

In Switzerland, banking privacy is for the Swiss people and has been so for centuries. Foreigners benefit because the laws apply to anyone who uses the banking system.

And, most significant, there is the democratic root of Swiss banking privacy laws. These laws can be repealed only by a national referendum. There is no doubt that such a referendum would not be approved by Swiss voters. If Hitler, with Panzer divisions at the border, couldn’t penetrate Swiss banking secrecy, how can the OECD believe they can?

As noted German classical liberal Wilhem Röpke put it,

Banking secrecy is a major component of the wall of discretion that must protect the individual and his privacy if liberty is to be defended with success against the dominance of the State. This and no less, is what is at stake. The frightening thing is that it should be necessary to state it.

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