Gabriel Zucman, *The Hidden Wealth of Nations* (Chicago, University of Chicago Press, 2015)

The labyrinthine world of shell companies and international tax havens is a fascinating—and often infuriating—part of global capitalism today. Gabriel Zucman's book, *The Hidden Wealth of Nations*, shines powerful new light on contemporary tax evasion by the rich. Zucman offers rigorous and creative empirical digging with a light touch of economic theory, making it a compelling read for scholars of inequality, economic sociology, globalization, and public policy. Once upon a time, ill-gotten gains and other dark monies were hidden in safety deposit boxes. The content of these boxes was never disclosed to tax authorities, but they were simply iron mattresses that left hidden cash hard to use. In the modern era of globalization, shell companies and offshore accounts allow the rich to invest at home and abroad under a shroud of anonymity, allowing the rich to grow their fortunes while evading taxes on their capital income. Welcome to the 21st century.

Zucman provides the first serious effort to gauge how much money is hidden in the global economy today. This book summarizes Zucman's massive undertaking of pouring through the byzantine world of offshore financing. The technical details are published elsewhere, including a high-profile article in the *Quarterly Journal of Economics*, but the curious can spend days clicking through Zucman's online appendices that document the hidden flow of funds in and out of offshore tax havens.

How does one study an industry—offshore finance—whose job it is to make things invisible? When rich people hide big money overseas, it creates anomalies in international financial accounting statistics. These anomalies leave a signature trace that Zucman uses to reveal the hidden economy. When Europeans buy stock in US companies, these purchases are recorded both in the US as a sale overseas, and in the EU as a purchase abroad. The international accounts record both sides of the transaction. However, when someone sets up an anonymous shell company in the Cayman Islands and then buys US stock through a Swiss bank account, only one side of the transaction is recorded. US companies report that stocks were sold to a foreign entity. But, because the buyer is an anonymous shell company, the

Cristobal Young, Stanford University [cristobal.young@stanford.edu]
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purchase is not recorded in any other country's financial accounts. Thus, in global statistics, more stock and bonds appear to be sold than are purchased. When companies make dividend payments to their foreign owners, more dividend payments are made than are "officially" received. These imbalances are the signature of money disappearing into the offshore economy. Globally, these anomalies amount to staggering figures. They suggest that roughly $7.6 trillion are hidden in the offshore economy. By comparison, the global stock of financial wealth is about $95 trillion. So, as Zucman modestly concludes, about 8 percent of the world's financial wealth is hidden overseas. That is probably a conservative estimate—the real figure might be as high as 10 percent.

Why does the offshore economy exist? Zucman argues that "the main reason to deposit securities in a Swiss bank is and always has been for tax evasion" [17]. Zucman estimates that, worldwide, governments lose about $200 billion in revenue from offshore tax evasion. And the beneficiaries of this game are highly concentrated among the super-rich. While most anyone could figure out how to set up an anonymous shell company, using it to safely evade taxes requires elaborate shell structures maintained by extensive legal and accounting advice. People using these accounts for serious tax evasion are the top tenth of the "one percent." Offshore tax havens are helping to drive the soaring wealth inequality that Zucman has documented in other research (e.g., Saez and Zucman 2016).[1] For the top fraction of the highest income earners (the 0.1 percent), the offshore economy is providing a do-it-yourself tax cut approaching 20 percent of what they owe.

However, the offshore economy is not all about tax avoidance. Surprisingly, the most intensive users of the offshore economy, Zucman finds, are Middle Eastern oil countries such as Saudi Arabia, Kuwait, and the United Arab Emirates [53]. Some 57 percent of these countries' financial wealth is held offshore—even though these countries do not have an income tax, and most of this wealth belongs to the royal families that maintain absolute rule in their countries. Zucman argues that, for Saudi princes, the offshore economy primarily offers anonymity—the ability to operate abroad, purchasing assets, land, and companies in the West without attracting unwanted attention [22].

Also strikingly high in offshored wealth is Russia, where 52 percent of financial wealth is hidden abroad. Russia has low income taxes and,

[1] Saez Emmanuel and Gabriel Zucman, 2016. "Wealth Inequality in the United States since 1913: Evidence from Capitalized Income Tax Data", *Quarterly Journal of Economics*, 131 (2): 519-578.

by Zucman's estimate, Russian offshoring saves the oligarchs hardly anything in taxes owed. In Africa, 30 percent of financial wealth is hidden offshore. In contrast, in Western Europe, 10 percent of wealth is hidden offshore, and in the US, only 4 percent. These figures by country and region are some of the most arresting facts in the book. Zucman produced these estimates, and used them to calculate overall tax revenue losses due to the offshore economy, but had surprisingly little to say about these international differences in offshoring. Of course, one of the drawbacks of a shorter book like this is that not all great leads can be pursued in depth. But these international differences in offshoring wealth shine light into what motivations drive the offshore economy, and a comprehensive analysis would be extremely valuable. It seems that a significant part of the offshore economy is not about tax avoidance, but more about corrupt elites concealing ill-gotten gains, seeking protection from autocratic dictators like Vladimir Putin, and anonymously investing or consuming their wealth in high-status Western cities like New York and London. Of course, it is not clear if these motivations are any less genteel than tax evasion—but they are interestingly different.

Zucman finishes the book with some compelling arguments about how to put a stop to tax evasion and enforce transparency in the global economy. Tax haven countries and secrecy jurisdictions benefit from aiding and abetting in the tax evasion of the rich, but the benefits are smaller than the costs and revenue losses they impose on other countries. Indeed, because tax havens do not directly tax the money they help conceal, most of the benefits flow simply to bankers and wealth managers in countries like Switzerland, Luxembourg, or the Cayman Islands—not to the general public of these countries. Moreover, a general feature of tax havens is that they are small jurisdictions highly dependent on international trade for their standard of living. This means that tax havens are remarkably vulnerable to trade sanctions for having abusive bank secrecy rules.

If the US imposed a 30 percent trade tariff on the Cayman Islands (a notorious tax haven), the country would be quickly forced to abandon its bank secrecy laws: remaining as a tax haven under trade tariffs would be far more costly than coming into compliance with international transparency rules. Similarly, if a coalition of France, Germany and Italy agreed to impose a 30 percent tariff on Swiss exports, the cost to Switzerland would likely outweigh its gains from being an international bank secrecy hub. The world is not helpless in the face of small nations seeking to undermine the laws and revenues of other countries. No country has the legal right to help foreigners evade the taxes of their home countries. Nations engaged in such opportunistic services can and should face trade sanctions in proportion to the harm they cause other countries.

In practice, the US and the IMF have made significant progress in recent years towards transparency in international banking, backed by sanctions against non-compliant countries. Hiding large sums of money in the global economy is becoming more difficult, but there is much work left to do, and Zucman offers additional proposals to limit the potential for tax evasion. The fight against tax havens, Zucman concludes, is "above all a battle of citizens against the false inevitability of tax evasion" and a rejection of the supposed "impotence of nations" [116].

The last time I reviewed a book in economics was in 2004. My review was to critique chalk-board economics as a discipline of fact-free policy prescriptions that hides its moral values behind complex mathematical formulae that few can understand [Young 2004].[2] The ideology of frictionless supply and demand, rather than actual evidence, was the currency of economics in my own graduate training and in much of the literature. Twelve years later, it is remarkable how much the discipline has changed. Zucman represents a new generation of economists, focused on empirical evidence and stylized facts rather than distillation of neoclassical theory. Zucman uses economic theory, not to dictate policy conclusions, but to guide his empirical inquiry—to know where to look for anomalies. His final product is not regression analysis or causal inference, but simply astute and careful observations about the size of the offshore economy. If Zucman were a sociologist, someone would probably criticize his work as "merely descriptive." This is a long way from the chalk-board economics of the past, and reflects a field much more open to interdisciplinary research.

The new economics cares more about discovering important and insightful facts than whether a study is "descriptive" or "inferential." Quantitative sociologists can learn a lesson here about what should matter most in their research: cultivating new evidence and creating tangible new knowledge, rather than running stale and uninteresting significance tests on pre-packaged data sets. Zucman offers deep evidence and insight without a single significance test or regression

[2] Young Cristobal, 2005. "The Politics, Mathematics, and Morality of Economics: a Review Essay on Robert Nelson's Economics as Religion." *Socio-Economic Review*, 3 (1): 161-172.

command in either the book or the initial *QJE* article. Zucman is part of a group of economists—including Emmanuel Saez, Tomas Piketty, Raj Chetty and others—producing groundbreaking research with minimal use of the classical hypothesis test (eg, Piketty and Saez 2003; Chetty *et al*. 2014).[3] Significance tests are fine, but they are not an especially good way of conveying what is informative and interesting in the data. Often a well-thought out descriptive analysis is more compelling and insightful than a significance test.

In this light, I especially recommend Zucman's book to graduate students in sociology for a fresh view of what cutting-edge empirical analysis can look like. They might even find some intriguing stones left unturned for their own research pursuits.

CRISTOBAL YOUNG

[3] Piketty Thomas and Emmanuel Saez, 2003. "Income Inequality In The United States, 1913-1998", *Quarterly Journal of Economics*, 118(1): 1-39.
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