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Title of paper: Capital, Nationality, and State Sovereignty: New Links for the 21st Century

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Abstract

This paper investigates the link between capital, nationality and state sovereignty, both historically and in the context of our current globalized world. It challenges the conventional viewpoint that capital has no nationality, which implies limited state sovereignty with regards to fiscal policy and developmental strategies. I argue that while capital does not properly ascribe to a *de jure* nationality, it has always had a *de facto* nationality that follows the nationality of the capitalist, as testified by the history of economic policy and decision-making. But the political-economy paradigms within which this nationality has been manifested have changed over time and so have the tools for states to preserve their sovereignty. In the current environment of advanced information technology, fiscal competition and an increasing presence of tax havens, I motivate and evaluate various proposals to give capital a *de jure* nationality for the benefit of state sovereignty in the 21st century.

Keywords

Capital; Nationality; Globalization; State Sovereignty, Tax Havens.

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1. Introduction

This essay seeks to explore the connection between capital and nation-states in our current globalized world. It is motivated from three premises. First, conventional belief upholds the view that capital is without borders, increasingly without tax jurisdiction, often linked to 'transnational' corporations, more and more mobile due to progress in information technology and thus cannot possess a legal nationality. Second, the findings of Zucman (2013a) corroborate this view somewhat, by showing that a non-negligible portion of the global financial wealth of households is held offshore, escaping national jurisdictions. This is specifically damaging to the sovereignty of states with respect to their fiscal and developmental policies. Moreover, the stock of unrecorded assets is double the recorded net debt of rich countries, which is sufficient to make the U.S. and Europe net creditors, rather than net debtors to the rest of the world as is officially held. Third, these first two premises reflect an asymmetry in knowledge regarding the respective identity of sovereign debtors and private creditors. While the national identity of the former is easily known in financial contracts, that of the latter is much more difficult to verify. This matters because without effectively knowing the nationality of private capital, national tax systems are undermined and states are increasingly dependent on international capital markets for financing their domestic needs.

This essay challenges the first premise by arguing that, while capital does not fully possess a nationality *de jure*, it can be said to have a nationality *de facto*. This is essentially because the nationality of capital mirrors the nationality of the capitalist, although the economic and political environments within which this nationality is manifested have changed over time, as this essay shall explain. Within the current environment of increasingly unregistered capital located in tax havens and opaque information regarding ownership (premises two and three), this essay shall highlight some guidelines as to how capital can fully come to have a nationality *de jure*. The immediate effect will be to eliminate the existing knowledge asymmetry between public debt and private assets, by ensuring that the latter follow a similar international recording system as the former, given that they are two sides of the same coin.

The remainder of the essay is structured as follows. Section 2 will define the key terms of the essay – capital and nationality – and their relationship from a present perspective; section 3 will examine how capital came to have a *de facto* nationality, from a historical perspective, while section 4 offers proposals to effectively naturalize capital from a practical viewpoint before concluding.

2. The meaning of capital and nationality in a globalized world

To begin with it will be useful to properly define 'capital' and to offer a more concrete understanding of what is meant by 'nationality'. For the purposes of this essay, the concept of 'capital' is understood in broad economic and financial terms. Thus, it is the monetary value of all material and non-material wealth, encompassing all national assets, domestic and foreign, financial (equity, bonds, deposits, cash, pension funds, etc.) and non-financial (real estate, machinery, patents, etc.) held by private entities. The concept of 'debt' is anchored in that of capital, given that all financial (domestic and foreign) liabilities are somebody else's assets, as defined through double-entry bookkeeping. Indeed, the common definition of 'capital' between the thirteenth and late eighteenth centuries was 'the capital assets of a trading firm', including 'funds, stock of merchandise, cash and money bearing interest' (Braudel, 1979: 201) The fact that capital was often referred to as the 'principal of a loan' and

later as the 'sums of money or their equivalents brought by partners into a partnership of company' (Schumpeter, 1954: 322), reveals how capital is linked to the capitalist system of debt.[1] Not only is capital advanced to form or expand an enterprise, but capital assets also need to be used as collateral to obtain such money loans in the first place. 'Sovereign debt' works in similar ways. When the government creates more money it automatically creates a debt for itself and a corresponding asset (bond) for the investor. The government does not need to formally put up collateral for the loan, since it has a monopoly over legal tender, through the central bank, and over the collection of taxes.

A particular emphasis is placed in this essay on financial capital, for obvious reasons, namely, its almost instantaneous mobility from one side of the world to the other and its intangible nature, which make it difficult to track and regulate. The treatment of non-financial capital (i.e. the physical means of production) is placed mostly in the context of transnational corporations, given their multi-country location and production. These two forms of capital capture the essence of economic globalization in the present age. They also provide the premises to the argument that capital has no nationality. In this respect, they are worth examining a little closer.

It is plain to see that we no longer live in the post-War paradigm of national governments limiting the movement of capital across borders, but in one that intellectually urges free capital movements and the end of national regulatory and supervisory power. Paradoxically, the capital market liberalization we are so familiar with today in developed countries can be traced from the post-War period. Already in the 1950s, the creation of Eurocurrency markets allowed for easier and quicker conversions between major currencies (Tobin, 1978; Eatwell and Taylor, 2000). The 1960s and 1970s saw the definitive breakdown of the Bretton Woods system and the effective privatization of foreign exchange risk, as governments abandoned all intervention in exchange markets. Financial liberalization was given a more fertile ground on which to work during the 1980s, with the creation of global bond markets, and further during the 1990s, with the creation of global equity markets and the complete removal of the remaining capital controls left over from the Bretton Woods era (Eatwell and Taylor, 2000). These sequential events *appear* to have had the consequence of removing the national character of financial capital, such that it has become 'passport free', and thus obligation free. No longer does capital have any obligations to anybody other than its private owners, so the argument goes.[2]

Unlike financial globalization, the phenomenon of transnational corporations, as we know it today, does not have a historical antecedent. While, it is true that the globalization of trade during the 1870-1914 period pre-dates our current wave, the nature of the traditional manufacturing firm has drastically changed. In the world of yesterday, 'U.S. companies employed U.S. workers in the United States to manufacture tangible goods, which U.S. citizen-salesmen abroad sold in foreign markets' (Kirsch, 2007: 464). In the world of today, U.S.-based transnational corporations operate using segmented production structures in which manufacturing is produced at multiple worldwide locations using subsidiaries or

[1] This is firmly embedded in the system of money creation. Modern money is created by crediting and debiting money values on balance sheets, such that an asset and a corresponding liability of equal size are brought into being with a keystroke. When a debt is repaid both the asset and the liability are extinguished from the balance sheet. Hence, according to Hyman Minksy, 'A capitalist economy can be described by a set of interrelated balance sheets and income statements' (Minsky, 1992: 12). Thus, all references to 'capital' made in this essay should be understood as also encompassing debt, both private and public.

[2] It is noteworthy that our current age of financial globalization is not a historical anomaly. The period between 1870 and 1914, often described as the 'first globalization' of finance and trade, was as integrated as our 'second globalization' – it took until the early 21st century for developed countries to regain the same level of stock-market capitalization relative to GDP than had existed in the 1870-1914 period (Piketty, 2013). Similar to what we are used to, individuals back then could avail of sophisticated capital markets that served diversified portfolios of assets, both domestic and foreign, albeit not as complex as those existing today (ibid).

subcontractors. The answer then, to whether capital has a nationality should be in the name 'transnational' corporation (or 'multinational' corporation). With the capital used in production being spread across many countries, it cannot pledge allegiance to any particular nation-state, but only to a unifying transnational motive – profit maximization. Arguments like these reveal that the only thing that is truly 'free' in a *free market* – a political economy structure of one dollar one vote, where everything is commodified – is capital. Individuals are free insofar as they own capital (and insofar as they own their own labour power). But this argument should not be confounded with the argument that capital has no nationality. This would erroneously equate freedom of movement with having no nationality when, in fact, it is proof of nationality that gives license to move.

The concept of 'nationality' can be generally defined within the domain of international law, by which legal status is given to the attachment of an individual to a nation-state, via passports or national IDs (Weil, 2011). But being a national of a certain legally defined territory is also connected to two further features. It can be argued that having a nationality gives one the right to participate, up to further legally defined boundaries, in the political and civic life of the society one is a national of, for example by voting in elections and referenda or by volunteering in different kinds of social activities. It can also be argued that having a nationality affords one the psychological comfort of having a 'home', or a sense of belonging. These features all come under the definition of 'citizenship' (ibid). Yet given that they usually (but not strictly) require nationality, it is plausible to make use of them when exploring the concept of nationality.

Bridging the concepts of capital and nationality, it is not clear, *prima facie,* how they can be connected. Nationality, legally defined, pre-supposes that the link is between individual *persons* and nation-states. Capital, on the other hand, is an abstract concept – it is an aggregation of many different tangible and nontangible saleable assets. However, this should not detract us from the asymmetry concerning private assets and sovereign debts when it comes to identifying their respective nationalities. Government debt, issued in the form of bonds, has a *de jure* and *de facto* nationality – in practice, when investors and credit rating agencies have to assess the security of a government's debt, they are very aware of *where* that debt comes from, since countries can differ with respect to their policies and thus risk profiles. On the other hand, private entities and individuals, who are largely the bondholders of a state's sovereign debts, are less easily associated to a nationality by law or by standard practice. One can notice this asymmetry in the Greek government debt debacle, where the identity of its counterpart, namely the nationality of the investors in Greek bonds, remained opaque. This is by no apparent means a media-driven conspiracy. It simply reflects the lack of an integrated cross-national accounting system that would effectively determine who owns what.

Despite these limits, capital can be legally connected to national persons through enforced property rights or contract laws, at least in Capitalist societies.[3] By default, this means that capital is someway under the dictates of nationhood and its correlates, as defined above. By being under the mandate of its owner, capital usually finds its movements and ends directed towards the interests of this owner, which are usually defined in close proximity to the 'home' of the capitalist. And these interests are ruled by what capital affords. Economic capital is a statement of wealth. Wealth is both a stock of individual purchasing power and of national economic stability. In increasingly commodified societies like ours, where almost everything *can be* put up on the market for sale, economic capital is thus a means to social, cultural and political power. Exercising the power that capital affords, whether it is in the form of purchasing goods and services for domestic use, for maintaining a certain social

[3] On the other hand, capital in centrally planned Communist countries is, by definition, easier to connect to a nationality, since all capital is the property of the state.

status or for influencing the direction of national economic and cultural policymaking, requires the capitalist to be connected to a 'home' or a place of residence. This logic renders the globalization argument irrelevant, as open borders increase the speed and movements of capital, but do not alter its ultimate objective or destination. And it is an inherent aspect of human nature – dependency on a 'home' – that determines this destination.

In the case of transnational corporations, the treatment of capital as a national can be derived from the separate legal protection that incorporated businesses receive under most jurisdictions. In this exceptional case, one could interpret capital as having a nationality *de jure*. This protection, however, also reveals one side of capital's double standards upon exercising its nationality. When seeking protection under the law, for whatever reason, U.S.-based corporations are quick to be 'American'. They too like to display their nationality, when voluntarily contributing to social expenditures of any kind (infrastructure, donations for education, etc.) in the form of corporate philanthropy. Yet, they often forgo their nationality in as much as it is possible when made to contribute mandatorily, often towards the same ends, but through different means, namely public taxation. These trends are characteristic of transnational corporations in developed countries in general – examples of this strategy of tax minimization are plentiful today. Therefore, transnational corporations may have a *de jure* nationality but they only exercise it *de facto* when it is of their own private interest.

In general, therefore, capital's nationality is derived from the country where its owners permanently reside. Where nationality does not overlap with place of residence, it is the passport of the capitalist that overrides the place of residence in determining the nationality of capital, given that protection of property rights is of a more foundational interest to the capitalist than the economic, political or cultural ends this capital can facilitate (you cannot have the latter without the former). And as with financial capital, the nationality of corporate capital can be derived from the place of residence of its owners or top decision makers, which is usually the country where the corporation is registered.[4] Here the globalization argument for capital having no nationality is again redundant, and at most used as an excuse.

3. The origins of capital's *de facto* nationality

From the above logic we may conclude that capital is endowed *de facto* with a nationality (only in exceptional cases it can rely on some sort of *de jure* nationality). The roots of this relationship can be sourced from specific periods in the history of capitalism. Over time the relationship has evolved into new forms, but the organic link between capital and the nation continues to be maintained. According to the globalization argument, we have no reason to think so. Capital's interest is allied solely to profit, independently of where it must travel to achieve maximum return. In conjunction, it is mal-practice to regulate the foreign ownership of capital in a country, as used to be done by governments, since governments should only care about corporations creating jobs and domestic wealth, not whether they are owned by its citizens or by foreigners (Chang, 2011). Arguments like these are prone to portray that things have always been like this. History, however, tells us otherwise. In particular, there are two features linked to capitalism's history that are rarely emphasized, but which explain how capital came to acquire a *de facto* nationality. These are, the 'emulation principle' of national economic policy and the 'home bias' in capital investment.

[4] Similarly to the case of financial capital, if the owners change residence without applying for a new nationality, the capital of the corporation remains the nationality of the country where the corporation is registered, which is usually the original place of residence of the owners, as shall be argued below. The exceptions are cases where companies are registered *offshore* in tax havens (more on this below).

3.1 The 'emulation principle'

The history of economic policy from roughly the seventeenth century onwards is marked by a simple heuristic that held sway among national policymakers of different emerging nations. This heuristic is best described as the 'emulation principle' – 'the endeavor to equal or surpass others in any achievement or quality' (Reinert, 2009). In essence, the principle is about emulating 'the best in the class', and then relying on a comparative advantage at a higher stage of development than would have otherwise been possible without emulation. This simple strategy has been applied by all of the presently developed countries, with few exceptions. It starts off with the protection, nurture and promotion of those economic activities with the highest value-added for the domestic economy that can be attained at a given level of development.[5] This has commonly taken the path of upgrading economic capabilities from labor-intensive agricultural production and raw commodity extraction (sugar, coffee, fish, cotton, rubber, primary metals, etc.) to 'light' manufacturing industry (clothing, shoes, textiles) and subsequently to capital-intensive 'heavy' manufacturing industry (steel, washing machines, cars, ships, airplanes, computer technology, industrial machinery, medical equipment, etc.). The emulation that occurred on the production side was in a way satisfying a demand for emulation in consumption between individuals of different countries – what can be interpreted as a 'keeping up with the Joneses' mentality. An infant industry strategy thus bred specific state-managed policies, which were most successful when they were both import substituting and export promoting.[6]

The principle of emulation experienced vast popularity among policymakers, and can be seen in action in Britain's attempt to protect and nurture its industry to emulate the Dutch in the seventeenth century; with German and U.S. efforts to emulate the British in the eighteenth and nineteenth centuries; to East Asian countries like Japan and eventually South Korea to catch up the developed West in the 20th century, to all active industrializers in between not wanting to be left behind, including France, Italy, Scandinavia and evidently the Soviet Union. Only when their economies had sufficiently developed, were trade barriers, capital controls and financial regulations gradually abandoned from the strategy (Chang, 2007; Reinert, 2009). State sovereignty was thus closely managed and better preserved. Also, in this historical period, public debt was much more locally managed, depending largely on the capital of national individuals and companies. A prime example is the U.K from the late seventeenth century onwards, when the government granted royal charters to national companies that bought public debt, while various forms of bond and annuities (e.g. 'consols') were offered to the affluent classes of the country (Venture & Voth, 2015).

The ideology defining this early history of capitalism was rooted in mercantilist nationalism, whereby it was the wealth of the nation through its trade that was desired. This united national policymakers and domestic merchants towards the same cause (providing glory to the former and wealth to the latter). War remained (until the mid 20th century) a useful outlet through which the productive wealth of a nation could be enhanced, but as Albert Hirschman insightfully points out in his book the *Passions and the Interests* (1977), the birth of capitalism channeled human competitive instincts away from purely violent pursuits and into commercial activities of greater social use. For much of the emulation period of the developed West, capital was devoted to 'working' for the glory and power of the state. This thinking is nowhere more visible than from the minds of the *German Historical School*

[5] This strategy is sometimes referred to as the 'infant industry strategy' in the literature.

[6] This strategy had its most visible origins in Britain and the United States. British Prime Minister William Walpole is credited with being the first policy-maker to have implemented a comprehensive infant industry program in 1721, which influenced Alexander Hamilton, the first Treasury Secretary of the U.S. to be the first to present the theory of infant industry protection in his *Report on Manufactures* in 1791 (Chang, 2007).

of economic thought, which influenced thinkers on both sides of the Atlantic. Political economists like Friedrich List (1789-1846) and Gustav Von Schmoller (1838-1917) promoted mercantilist policies and the infant industry strategy as means to promote 'national economy-making' – 'a national economic program for modernization and power' – very much in the spirit of the emulation principle (Magnusson, 1994).[7]

Not only does the early history of capitalism provide us with instances of patriotic emulation policies, but the extent of the competitive drive between nations also bred 'anti-emulation' policies, especially in Europe. For example, the Venetian city-state prohibited the outward migration of her skilled glass workers with the death penalty, while England forebode the export of her industrial machinery for many years during her early industrialization period (Reinert, 2009). The English case is a perfect illustration of the *de facto* nationality that capital came to have upon the birth of capitalism and the Industrial Revolution. And characteristic of the economic strategy of the time, 'England only gave up her export prohibition of machinery, when the English machine producers themselves successfully argued that if they were restricted from competing in world markets they would lose ground to foreign machine producers' (Reinert, 2009: 21). There have been yet other, more explicit, cases where capital has carried a nationality. These have usually revolved around war. One of the clearest examples is The European Recovery Program of 1947, commonly know as the Marshall Plan, through which a destroyed post-war Europe received large inflows of U.S.-sourced capital so as to help rebuild the continent's economy, which was of vital importance to the developing U.S. economy. The Plan was probably the most successful economic development assistance program in human history, and it carried the U.S. seal on it (Reinert, 2009). Moreover, this episode also reveals how capital can be directed by national economic and political interest – the Plan not only helped to rebuild an important market for U.S. production, but it also successfully contained the spread of Soviet influence in Western Europe (ibid).

A further example relates to the reparation payments that the German state was forced under by the Allies in the aftermath of the First World War. The Peace Treaty crafted by the Allies included numerous provisions of German capital expropriation – the ceding of her mercantile marine (vessels, trawlers, fishing boats); her colonies; the retention and liquidation of her foreign investments (properties, rights and interests) therein; a payment of up to $5,000,000,000 to be given in-kind 'whether in gold, commodities, ships, securities or otherwise' (Art. 235); and the appropriation and exploitation of her coal-mines and iron-ore fields (Keynes, 2011 [1919]: 28-41). These provisions were explicitly geared at the destruction of Germany's oversees commerce and wealth, and her domestic industrial production (ibid). It effectively imposed a large sovereign debt on Germany that significantly curtailed her sovereignty. The Treaty can also be rightly interpreted as the most venomous form of emulation, given that Germany was at the time the Continent's first industrial power, to which her neighbors were playing catch up.[8] The Treaty essentially gave countries like France and Italy the time and supplies to emulate the industrial prowess that Germany had developed over the previous decades, apart from laying the ideological foundations for the

[7] The opposing school of thought was the 'Neoclassical' or 'Marginalist' School, whose economic maxim was *laissez-faire*, thus leaving the state out of economic affairs and promoting voluntary exchange between 'profit-maximizing' entrepreneurs and 'utility-maximizing' consumers. While over time this latter school has come out as the intellectual victor, history remains on the side of the Historical School, which viewed man as a historical creature molded by evolving institutions and social conditions, rather than as a hedonistically motivated rational economic agent (Magnusson, 1994). It is still debated into which school Adam Smith best fit in, but careful reading of his *Wealth of Nations* suggests that he thought there was a time and a place for each view to be put into practice.

[8] France was one of the three principal parties involved in the drafting of the Treaty, alongside Britain and the United States (Keynes, 2011 [1919], chapters III and IV).

Second World War. This historical excerpt portrays how capital can be understood to possess a nationality in practical affairs and how, when deemed appropriate, this nationality can be legally confiscated and replaced.[9]

3.2 The 'home bias'

The emulation principle offers one important link between capital and the nation, which is mediated by the *state,* as policymaker and national economic coordinator. The second feature of capital's rooted nationality moves us from the state to the individual capitalist and private corporation. It is represented through the 'home bias' of capital investment.

This home bias is most easily seen in the behavior of private corporations, for whom 'home' is defined as the countries where ownership of the corporation resides – that is, in the countries their top decision makers are nationals of. Therefore, one of the most visible examples of the home bias is in the appointment of top executives to the corporation. Even when companies are acquired by or merge with foreign firms, it is the nationality composition of the board of directors and principal shareholders that matters for determining the *de facto* nationality of a firm. For developed country corporations, the nationality of top decision makers then becomes important for determining the location of key productive activities, such as high-end research and development and high-skilled manufacturing. The home bias is strong for the former in shielding it from foreigners, while the latter answers to a home bias in a more political sense – when having to close down production units or lay-off workers, corporations are prone to it last at 'home'. The fact that still only around a third of the output of U.S.-based manufacturing firms is done abroad or that the figure is close to ten percent for Japanese firms, speaks for itself (Chang, 2011).

Some of these decisions may be more political (avoiding a backlash from unions, domestic citizens or governments) than economic, but this does not conceal the corporate drive to maximize global profits. Indeed, this motive is present in decisions to separate the legal domicile of a company from its operations headquarters, through 'holding companies' registered in low tax jurisdictions like Amsterdam, Dublin or Luxembourg. Despite the confusion that this adds to the calculation of a corporation's 'home', the bias can be tracked from following the income flows in national accounts. To take illustrative examples, the value of Ireland's national income is only about 80 percent of the value of its domestic production, while in Luxembourg the figure is roughly 66 percent (Zucman, 2013b). This means that approximately one fifth of Irish GDP and one third of Luxembourg's GDP leave the countries in repatriated income each year. This is income going to foreign expatriate workers, owners of foreign banks, foreign corporations, domestically registered holding companies of foreign corporations and foreign clients of domestically registered hedge funds, in other words capital flows that, instead of staying in these countries, return to *the home* of their owners.

The existence of a home-country bias is not a coincidence. It is likely to have deep moral, economic and historical motives. It is quite normal for capitalists to have moral sentiments towards the society that has allowed them to build their individual wealth or corporate enterprises. There is thus a temporal reciprocity, which is a proximate idea to that developed by Adam Smith in his lesser referred to book, *The Theory of Moral Sentiments* (1759). At the level of the transnational corporation, there is also an economic motive to the home bias, in that there is a certain category of capabilities and productive networks that require 'a conducive institutional environment', and thus 'tend to stay at home' (Chang, 2011:

[9] Concerning Germany's overseas possessions, Keynes writes: '…not only are German sovereignty and German influence extirpated from the whole of her former overseas possessions, but the persons and property of her nationals resident or owning property in those parts are deprived of *legal status* and *legal security*' (2011 [1919]: 29, emphasis added).

82). For most transnational corporations these usually relate to skilled workers, networks of suppliers, financial intermediaries, business networks, organizational routine and legal practice. For individual, risk averse, investors it is knowledge asymmetries related to legal practice, taxation, and institutional risk that seem to explain the observed home bias in the asset portfolios of developed country citizens, even when a foreign bias has been estimated to be more profitable (Coeurdacier and Rey, 2013). This is reflected by the popular investments in government bonds and U.S. treasury bills by own nationals or nationals of similar countries. Here, the 'home bias' can the understood as a portfolio bias towards the debt of 'safe' countries, which are usually those whose laws and economic climate one is familiar with. For citizens of the rich world, this is usually their home country or countries from similar geo-political regions.

These type of arguments were well understood back in the 18th century, when merchants preferred a home market to employ their capital because they had greater oversight of their investment, they were more acquainted with business networks of their home country and ultimately with the its laws. This was especially true in cases when merchants needed to seek redress for damages or malpractice of any kind. It was Adam Smith, writing in the 18th century, who understood this best. In his highly cited (but seldom read) book, *The Wealth of Nations*, Smith highlights how capital is drawn towards its equilibrium, which he defines to be the home of the capitalist:

> Home is in this manner the center, if I may say so, round which the capitals of the inhabitants of every country are continually circulating, and towards which they are always tending… (1976 [1776], IV ii: 455)

It is primarily in the context of capitalists favoring domestic industry that Smith uses his now famous metaphor of the 'invisible hand'. And it is by relying on the institutional safety and geographic proximity of the home market that produces the greatest gain for the capitalist and the national economy:

> 'By preferring the support of domestick to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other eases, led by an invisible hand to promote an end which was no part of his intention' (ibid: 456)

Smith was well aware of the economic benefits of patriotism in production and commerce. Indeed, a plausible interpretation of the context in which Smith uses the term 'invisible hand' is to validate the emulation principle discussed above (Reinert, 2009). The only time the term is employed for illustrative purposes in his book is to acknowledge a form of import substitution, characteristic of the mercantilist strategy. It could only have been possible for an English capitalist to derive the greatest value from supporting domestic industry if English consumers preferred domestically produced goods to foreign goods. And this could only be the case if domestic industry was adequately protected and developed so as to serve these local demands.[10] This evidences how the home bias and the emulation principle are intrinsically linked in uncovering the effective nationality of capital.

The home bias of individual capitalists and private corporations has its own history and motives. However, we should not forget the particular history of a state involved in institutionalizing the home bias of capital through citizenship-based taxation. This is the case

[10] Reinert (2009) argues that this logic may explain why Smith, deep down, regarded the Navigation Acts – a body of laws designed to protect the English shipping industry and foreign trade – as 'perhaps, the wisest of all the commercial regulations of England' (Smith, 1976, IV ii: 465).

of the government of the United States, which in principle taxes its citizens, whether they are residents or not, on their global income sourced from their financial/real estate capital and their labour (Kirsch, 2007). The history of this legislation provides an example of a national constitution recognizing the claim that a sovereign state has on the capital of its nationals, living at home or abroad. This was historically defended on the grounds that U.S. nationality continues to afford its beneficiaries protection over their person and property by the U.S. government, whether or not they reside in the country (ibid). It could be argued that all sovereign governments tax their citizens' capital income (through property taxes, capital acquisition taxes, capital gains taxes, wealth taxes, etc.), albeit not of nonresidents like the U.S. These governments thus legislate a national claim on the capital of private individuals residing in the country and thus grant capital a *de jure* nationality. Capitalists may change their place of residence, but their capital, as long as it is declared, retains the nationality of where they are living. But here, skeptics may still point to an auxiliary feature of the globalization argument, which is that there is a substantial and increasing portion of the world's financial wealth that is not declared by being registered in offshore accounts in tax havens. This capital escapes *de facto* any *de jure* claims for a nationality.

4. Naturalizing capital

Despite attempts to legislate the nationality of capital through the tax law or through property law, these are exceptions that largely prove that nationality remains *de facto* (whatever the arguments made by globalization enthusiasts). Once we recognize this, two questions then arise: should we care about giving capital a nationality *de jure*, and, if so, how should we go about it?

The above analysis revealed the motives, both historical and current, that have tended capital towards a nationality in practice. But in some instances, where these motives were once strong they are now weak. For example, the emulation principle is more a relic of history than a key pillar in current economic policymaking. Among the current advanced economies, it is evident that emulation saturation has kicked in some time ago. Tax competiveness is now the strategy of the period, which is fuelled by the emergence of tax havens, and ultimately leads to a 'race-to-the-bottom' mentality. Moreover, international organizations such as the IMF, the World Bank or the World Trade Organization – which are principally governed by the advanced economies – have been anti-emulation for much of their existence (see Chang 2007).[11] The policy advice thus imparted by these organizations to the developing world has been that the state should not seek to build up its claims on national capital through nationalizations or high taxation of any kind.

The strength of the home bias argument today is also compromised by the fact, already alluded to, that an increasing amount of national capital is unrecorded in tax havens. Currently, this hidden capital has been estimated to represent approximately 8 percent of the global financial wealth of households (Zucman, 2013a, see Figure 1 in Appendix). The estimated order of magnitude for Europe is 10 percent (see Figure 2 in the Appendix). This implies that national authorities cannot determine who owns the 5 to 8 trillion euros worth of wealth that is managed by hedge funds and investment societies in places like Switzerland, the Cayman Islands, Luxembourg, Singapore, etc. These are substantial sums of money. For example, Zucman's estimates equate to roughly twice the value of French GDP in 2013. This hidden wealth of nations has two direct implications.

[11] The psychology is self-evident: the idea that developing countries should be fostered to emulate the advanced economies does not sit well with the latter, for competitive reasons, given that they are at the technological frontier.

The first relates to a puzzle in international macroeconomics. In the official data, the rich world seems to be a large net debtor to the rest of the world, determined in large part by the negative net positions of Europe and the U.S, as depicted in Figure 1.[12] Yet the explanations for this imbalance remain obscure, despite efforts linking U.S. net debt with Chinese exports and savings. The emerging view is that external debts are in rich countries (with the exception of Japan) and that developing countries like China are increasingly 'owning the world' (Zucman, 2013a). However, accounting for the unrecorded wealth in tax havens, and making plausible assumptions of regarding the origins of this wealth, turns the Eurozone from the world's second largest net debtor into a net creditor, and significantly improves the U.S. net position. Given worries about the sustainability of global imbalances, these results would suggest that the necessary adjustment is not as large as the official data state (ibid).

The second implication relates to the annual cost of bank secrecy from a public finance perspective, and is in many ways more pertinent. The estimated annual loss in fiscal receipts to the world's governments is around 190 billion dollars, which represents the sum of the non-declared portion of the capital located in tax havens that avoids paying an income tax (on interests and dividends), an inheritance tax or a wealth tax (see Figure 3 in the Appendix). Again, to put this cost into perspective, without the tax evasion that such bank secrecy permits, in the case of France, its public debt in 2013 would not have been 94 percent of GDP, but 70 percent of GDP, the level observed before the recent financial crisis (Zucman, 2013b).[13] Here the issue of sovereign debt sustainability in Europe is turned on it head when the hidden wealth of European countries is made public.

In the face of the threat that tax evasion and bank secrecy pose for welfare states in the developed world as well as for the development strategies of currently developing countries (constrained by tax havens and policy conditionality by the international economic organizations), it would seem wise to consider proposals that seek to give capital a legally recognized and binding attachment to its country of origin, that is, a nationality *de jure*. Naturalizing capital in this way must go beyond considerations to legislate corporate personhood, or capital personhood. The U.S. has been one of the few countries to have legally interpreted 'corporate personhood' from its constitution (Bloch and Lamoreaux, 2014), yet it has apparently not prevented a continuous increase in the share of tax havens in U.S. total corporate profits and corporate profits made abroad, since the 1980s (See Figures 4 and 5 in the Appendix). States should instead pursue a plan that ultimately places a nationality on all capital, wherever it is located. This would help countries combat tax evasion as well as giving their development strategies more flexibility and sovereignty.

Although he does not phrase it thus, Gabriel Zucman's proposal for the automatic exchange of bank information – that is, the end of bank secrecy – to be encouraged through commercial sanctions by regional coalitions on non-cooperating countries and verified by a 'world financial registry' under the supervision of an international public organization has all the ingredients of a binding naturalization of financial capital. The proposal is realistic and adequate for its intended purpose of combating tax evasion (but also for its indirect purpose of giving capital a 'passport'). A world financial registry would in effect identify the owners and jurisdiction (i.e. nationality) of all global financial assets in circulation, allowing national

[12] This means that foreigners own more assets in Europe and the U.S. than what Europeans and North Americans own in foreign countries. Thus the net foreign asset position (foreign assets minus foreign liabilities) is negative.

[13] These figures should be treated as a lower bound, given that they exclude the indirect fiscal cost of the substantial reduction in rates that top income, capital and inheritance taxes have experienced over the previous decades in order to precisely ease the flight of national capital to tax havens (Zucman, 2013b). This is exemplary of the 'race-to-the-bottom' economic strategy highlighted above.

fiscal administrations to verify that their contributors have honestly declared all their financial assets inscribed in the registry.[14]

Legislating the nationality of capital through this registry would be facilitated by the creation of a global tax on capital, withheld at source by say the IMF on behalf of the individual countries. The rate of this tax could be around the 2 percent mark, or at least over and above the highest national rate observed. It would act as a sufficient constraint against financial opacity, since the tax would only be reimbursed to the proprietaries of the assets once they declare these assets on their tax form in their home countries, thus allowing states to preserve their fiscal sovereignty.[15] For countries that already have a wealth tax, as is the case of France, their taxpayers would be reimbursed the difference between what is withheld at source by the IMF and what is due to the fiscal authorities in their home countries[16] – in the case of France, for example, the wealthiest contributors subject to the highest rate of the national wealth tax (ISF) at 1,5 percent, would be reimbursed 0,5 percent, assuming that the global rate is 2 percent. The citizens not subject to any rate under the ISF would be reimbursed the entirety of the 2 percent. (Zucman, 2013b: 103-104). A global tax on capital may also facilitate or motivate countries that currently do not have a progressive wealth tax to create one, without fearing capital flight. Thus the complementary tools of a world financial registry and a global tax on capital have the opportunity to return to states the national sovereignty that they have increasingly lost to the financial industry. However, this would not prevent individuals, outside of U.S. citizens, from changing their place of residence to tax havens, so as to escape their national country tax burdens. In this case, countries could follow the U.S. by implementing citizenship taxation, whereby tax liability would follow the passport and not the place of residence. Under this legal framework, individuals would be taxed on their global income according to the rates and schedules applied in their home country, but would be compensated, via tax credits, the amount of personal tax paid to foreign governments in whose country they residence (Kirsch, 2007).[17]

Beyond proposals to naturalize financial capital, there are also proposals to naturalize nonfinancial (or corporate) capital. The present design of the corporate tax system among countries is such that corporations are able to optimize where they want their profits to appear by taking advantage of 'judicial subtleties', in an operation known as 'transfer pricing' (Zucman, 2013b: 107). This operation brings tax havens once more into the foreground, as they are often the preferred locations where corporations set up subsidiaries so as to overprice other subsidiaries located in high tax countries for products or services bought by the latter. In this way profits may appear on the books of the subsidiaries located in the Cayman Islands, in Bermuda, Luxembourg or in Ireland, instead of in France, Japan or the United States (Figure 5 illustrates this for the U.S.). As is evident, such a price manipulation can have substantial fiscal costs.[18] All this quasi-legal optimization is facilitated by the very design of a corporate

[14] Such a proposal is not necessarily 'utopian', as similar types of registries are already in existence, though managed by different private entitites, such as the Depository Trust Corporation in the U.S., Clearstream in Luxembourg, Euroclear France, etc. The aim would be to unite the dispersed registries that exist into a global registry supervised by an international public body like the IMF (Zucman, 2013b).

[15] This reimbursement clause would also be a constraint against the use of trusts, foundations and 'sociétés-écrans' by individuals in order to conceal their identity.

[16] Hence the importance of setting a global rate higher than the highest rate observed at any national level, so as to detract as far as possible individuals that desire to conceal their financial wealth.

[17] In effect, the tax due by the individual would be the difference between the tax liability of the country of nationality and the tax liability of the country of residence. This would also work for individuals with multiple legally recognized nationalities. The tax due would be the difference between the tax liability of the country of residence and all the countries the individual is a nationality of, in the case that they are different to the country of residence.

[18] Estimates on U.S. data suggest that transfer pricing reduce corporate tax receipts by 30 percent (Clausing, 2011).

tax system that seeks to tax each company's profits country by country. A more effective design would be to tax the *global* profits of corporations and distribute the receipts to the countries according to the proportion of sales they represent in the total sales of the corporation, or either according to each countries' weight in the payroll of the corporation or the capital used in production, which are plausible proxies for where most of the value-added is created. Each country would then be free to tax these profits at the rate they wish (Zucman, 2013b: 109).[19] With such a formula, a naturalization of corporate capital could effectively be achieved, whereby most of the tax revenues would likely flow to the countries whose corporate capital (i.e. corporation) is headquartered in, as was argued in section 3.2 above.

The proposals just described are clear indications of an implicit desire to give financial and corporate capital a *de jure* nationality in a world where financial opacity has threatened much of the viability of welfare state politics in developed countries and development strategies in developing countries.

5. Conclusion

This essay sought to scrutinize the question of whether capital really has a nationality and thus whether states really have sovereignty. It can be concluded from the preceding analysis that despite the best efforts by globalization enthusiasts to claim that capital operates with disregard to nations, and despite the growing relevance of tax havens, economic and financial capital (both assets and debts) has always been, and continues to be, deeply attached to nations – hence its *de facto* nationality. This nationality is filtered through the nationality of the owners and managers of capital. The history of capitalism, as portrayed in the acts and writings of its associated policymakers and scholars, provides illuminating examples of this logic at work – from the state-led development process of industrializing nations encapsulated in the principle of emulation, to the private capitalist's preference for the safety of and familiarity with his home country's laws and networks.

Therefore, capital has always come with a symbolic stamp of nationality attached to it, much in the same way as minted coins have always come with the mark of their home country on them. Even in our age of increased financialization and dissimulation, capitalists are still keen to hold a large bulk of their capital within the confines of their national jurisdiction – after all the share of tax havens in global financial wealth barely reaches double digits. Nevertheless, their increasing trends motivated this essay to suggest proposals to combat the harm that they pose to global balance sheet accounting and to the public finances. In their very nature, these proposals also end up 'naturalizing' capital. This is founded on the basis that capital has currently has no binding obligation to fully disclose its *de facto* nationality, whose organic roots have a long history but remain visible and relevant nonetheless.

[19] A world registry, similar to the one described for financial assets, could even be formed for the activity of transnational corporations, which would detail the global profits of corporations and the geographical distribution of their sales, payroll and value of productive capital. This registry could also be managed by an international public body like the United Nations.

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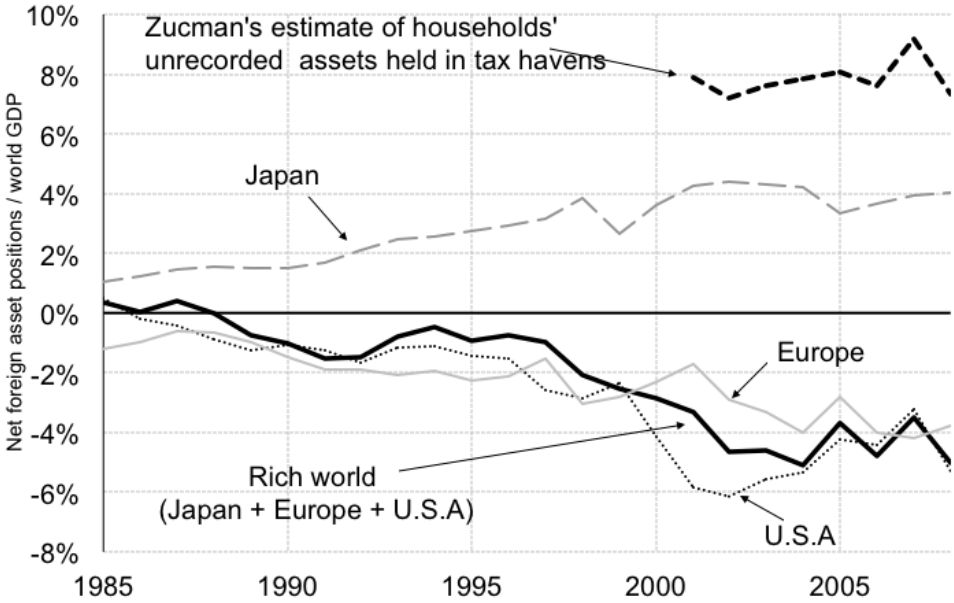
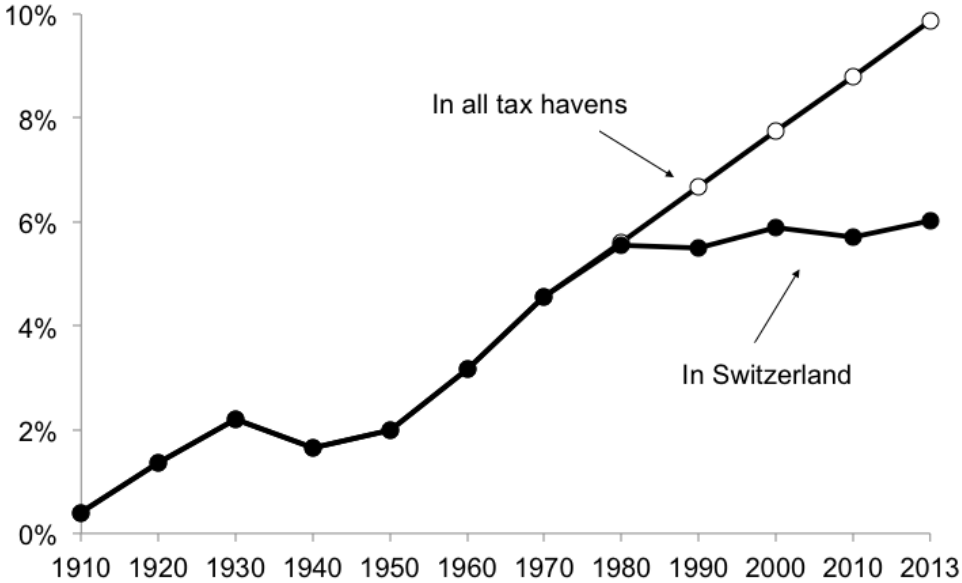
Appendix Figures and Tables

Figure 1. Recorded Net Assets of the Rich World and Estimated Unrecorded Assets Held in Tax Havens



Source: Zucman (2013a).

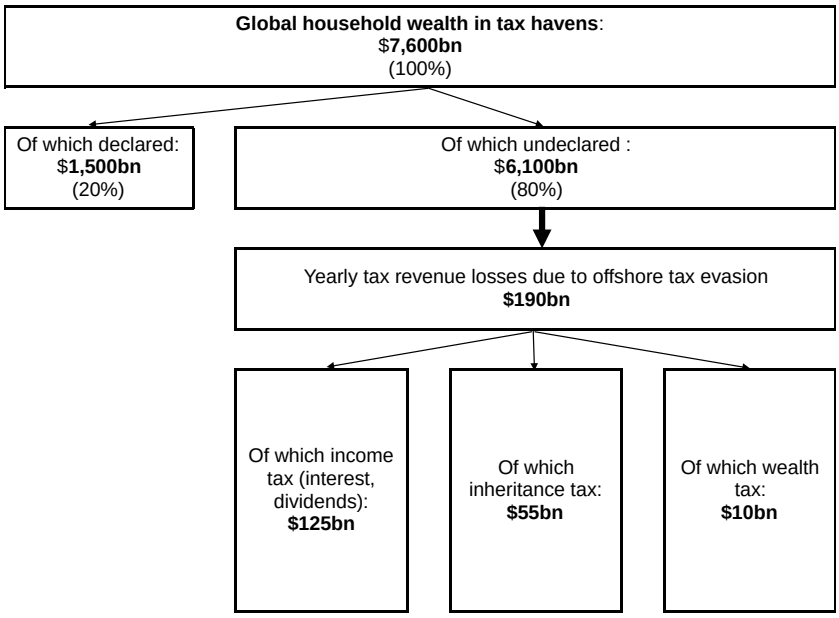
Figure 2. The wealth of Europeans held in tax havens (% European financial wealth)



Source: Zucman (2015).

Figure 3.

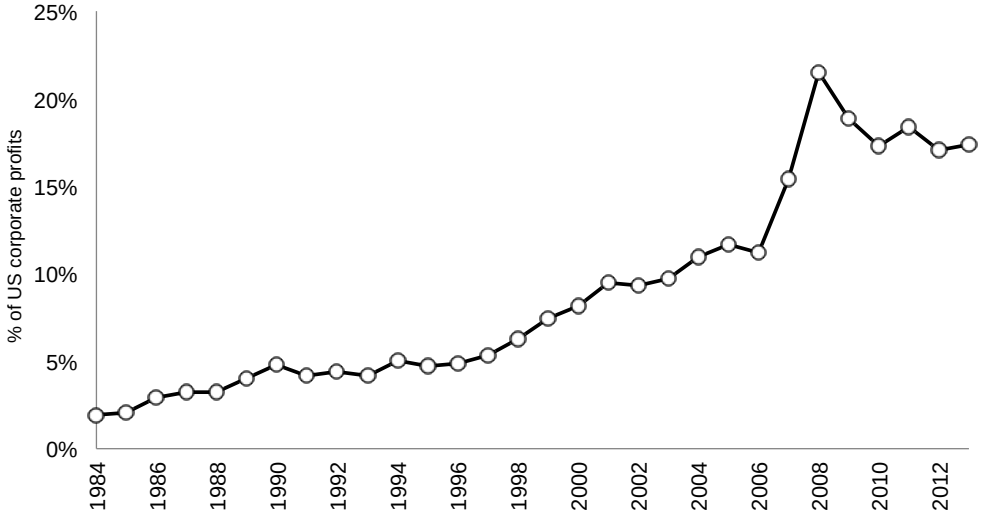
The global cost of offshore tax evasion (2014)



Source: Zucman (2015).

Figure 5.

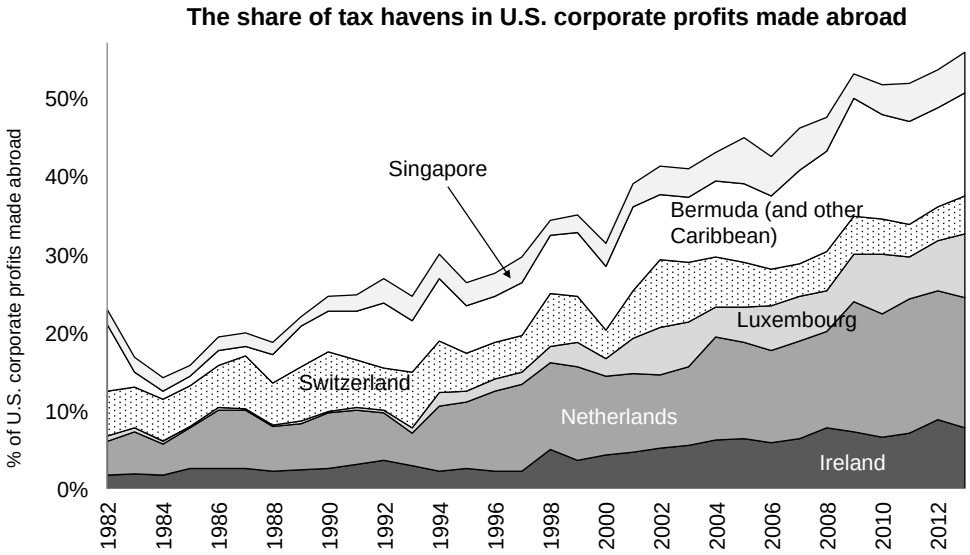
The share of tax havens in U.S. corporate profits



Notes: This figure charts the ratio of profits made in the main tax havens (Netherlands, Ireland, Switzerland, Singapore, Luxembourg, Bermuda and other Caribbean havens) to total US corporate profits (domestic plus foreign). Source: author's computations using NIPA and balance of payments data, see Online Appendix.

Source: Zucman (2014).

Figure 6.



Notes: This figure charts the share of income on U.S. direct investment abroad made in the main tax havens. In 2013, total income on U.S.DI abroad was about $500bn. 17% came from the Netherlands, 8% from Luxembourg, etc. Source: author's computations using balance of payments data, see Online Appendix.

Source: Zucman (2014).