The Offshore World According to FATCA:
New Evidence on the Foreign Wealth of U.S. Households

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Introduction

- Globally, households hold an estimated $7 trillion in offshore accounts (Zucman, 2013):
    - **Loss of tax revenue**: offshore assets are largely untaxed
    - **Regressivity**: offshore assets are highly concentrated among the very wealthiest (e.g. Alstadsæter et al, 2019, Guyton et al 2021)

- Policy innovation: FATCA requires all foreign banks to report U.S.-owned accounts to the IRS
    - Extends third-party information reporting to foreign financial income and assets

This Project

- U.S. administrative data: **FATCA forms**, income tax returns, business-owner links (K-1 information reports)

- **Questions:**
  1) What do FATCA reports reveal about offshore holdings?
  2) Does automatic third-party reporting on foreign accounts induce tax compliance?

- Today, descriptive analyses from the micro data (linked **F8966**)
  - Aggregate asset reporting: amount, where and how they are held (households or entities)
  - Who holds the assets: where in the income distribution

- Causal analysis of the effect of FATCA on tax compliance is in progress.

FATCA Reporting Regime

- Foreign financial institutions (FFIs) are required to:
  - **Identify accounts** ""beneficially owned" by U.S. taxpayers (thorough background check searching for U.S. indicia)
  - **Convey information** about assets and income to the IRS
  - Some exceptions (ex. reporting threshold of $50K in assets)

- Key differences to previous enforcement initiatives:
  - Beneficial (rather than immediate) ownership
  - Automatic (rather than on-request) information exchange

- Non-cooperating foreign banks are subject to 30% witholding on U.S. source income

Reporting of Offshore Wealth

Overview: Totals from FATCA Reports

	TY 2016	TY 2017	TY 2018
Assets (billion USD)	3,648	3,233	3,981
No. reporting FFIs	36,056	41,829	45,308
No. of accounts	3,703,159	4,225,689	4,566,774
No. of identified U.S. owners	1,223,115	1,296,462	1,477,183
No. accounts w/out identified owners[1]	1,318,291	1,594,459	1,664,587

[1] See TIGTA (2018)

FATCA Reports by Owner Type (2018)

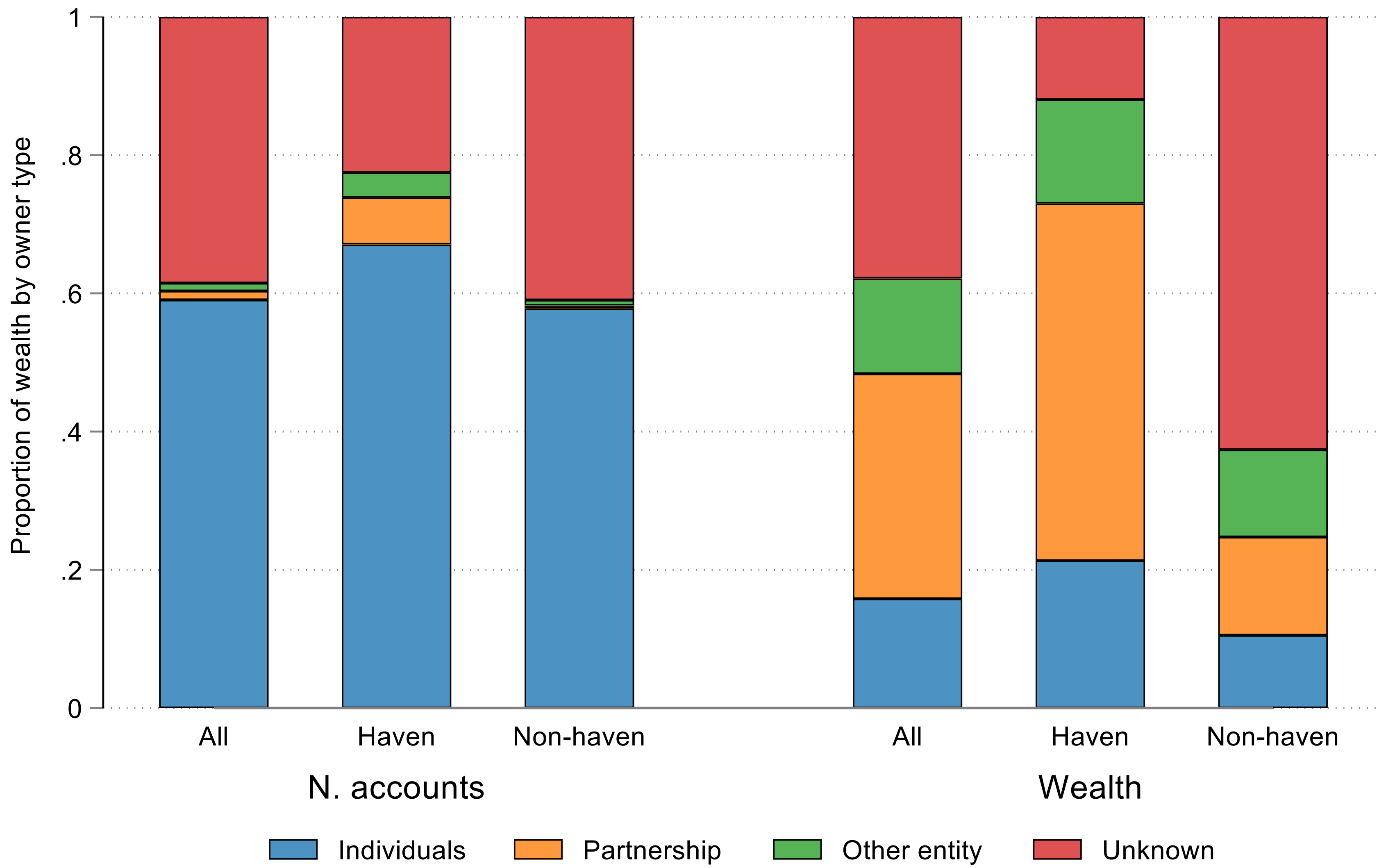
	Account Balance		No. of accounts	
	Total (Billions USD)	Share	Total	Share
Partnership	1,291.64	32.4 %	55,548	1.2 %
Individual	618.49	15.5 %	2,401,217	55.7 %
C Corp	400.64	10.0 %	18,206	.4 %
Tax exempt entity	48.59	1.2 %	8,777	.2 %
Trust	47.27	1.1 %	9,198	.2 %
Foreign corporation	20.64	.5 %	6,304	.1 %
S corporation	37.18	.9 %	8,041	.1 %
Missing TIN	1,017.58	25.5 %	1,578,472	36.6 %
Unmatched entity	278.78	7.0 %	12,306	.2 %
Ambiguous match	153.74	3.8 %	6,663	.1 %
Unmatched TIN	60.01	1.5 %	62,376	1.4 %
Unmatched individual	7.21	.1 %	143,141	3.3 %

FATCA Reports by Location of Accounts (2018)

	Havens*	Non-havens	Share in Havens
Wealth (billion USD)	1,940	2,041	49%
Accounts	612,406	3,954,216	13%

- * "Havens" is used as a shorthand descriptor of a set of countries that are low tax jurisdictions and serve as financial centers, as is commonly used in the literature
- The **IRS does not have any official designation of haven v. non-haven countries** and there is no such definition in FATCA law or administration. In line with previous literature, we use the list from Johannesen et al. (2020), which is the OECD (2000) list plus, Switzerland, Singapore, Hong Kong, and Luxembourg.
- Future work should refine the countries and institutions that potentially facilitate offshore tax evasion post-FATCA

Reported accounts and wealth by owner type and location (2018)



Comparisons to Previous Literature

- Larger wealth in tax havens than suggested by prior US estimates
  - Our data: **$1.94 trillion/10% of GDP in tax havens in 2018**
  - Alstadsæter et al. (2018): $1.1 trillion in havens/7% of GDP in havens in 2007.

- Comparable rates of ownership of offshore wealth at the top to Scandinavian data
  - Our data: 62% of those in top 0.01% own foriegn assets, 57% own haven assets
  - c.f. 60% of 0.01% of wealth distribution in Scandanavia (Alstadsæter et al. 2019))
  - Other data from leaks/amnesties: dispropotionately number of top-income recipients, but smaller shares of top-income/wealth individuals appearing in data

- Ownership of offshore wealth via partnerships modestly more concentrated than all partnership income
  - 46% of reported offshore partnership assets held by top 0.01%, 80% by the top 1%
  - c.f. 69% of total partnership income received by top 1% (Cooper et al 2016))

What Can We Learn About Rates of Return? (2018)

- Challenges in estimating (nominal taxable) rates of return in offshore accounts:
  - Missing income information for 45% of accounts/41% of wealth
  - Some items are not net taxable income amounts (e.g. "gross proceeds")

- We estimate "quasi-" rates of return, e.g. $\frac{\text{Total Int+Div}}{\text{Total Acct Bal }|\text{Non}-\text{Missing Int or Div}}$

Sub-population	Total reported wealth (billions USD)	Share of wealth with reported interest or dividends	Quasi-rate of return: interest + dividends only
All accounts	3,982	37.7%	2.8%
Non-haven country	2,042	51.3%	1.8%
Haven country	1,940	23.4%	5.0%
Individual owners	626	33.6%	4.6%
Partnership owners	1,292	19.8%	6.4%
Other entity owners	279	37.7%	1.1%
Unmatched owners	1,510	49.9%	1.6%

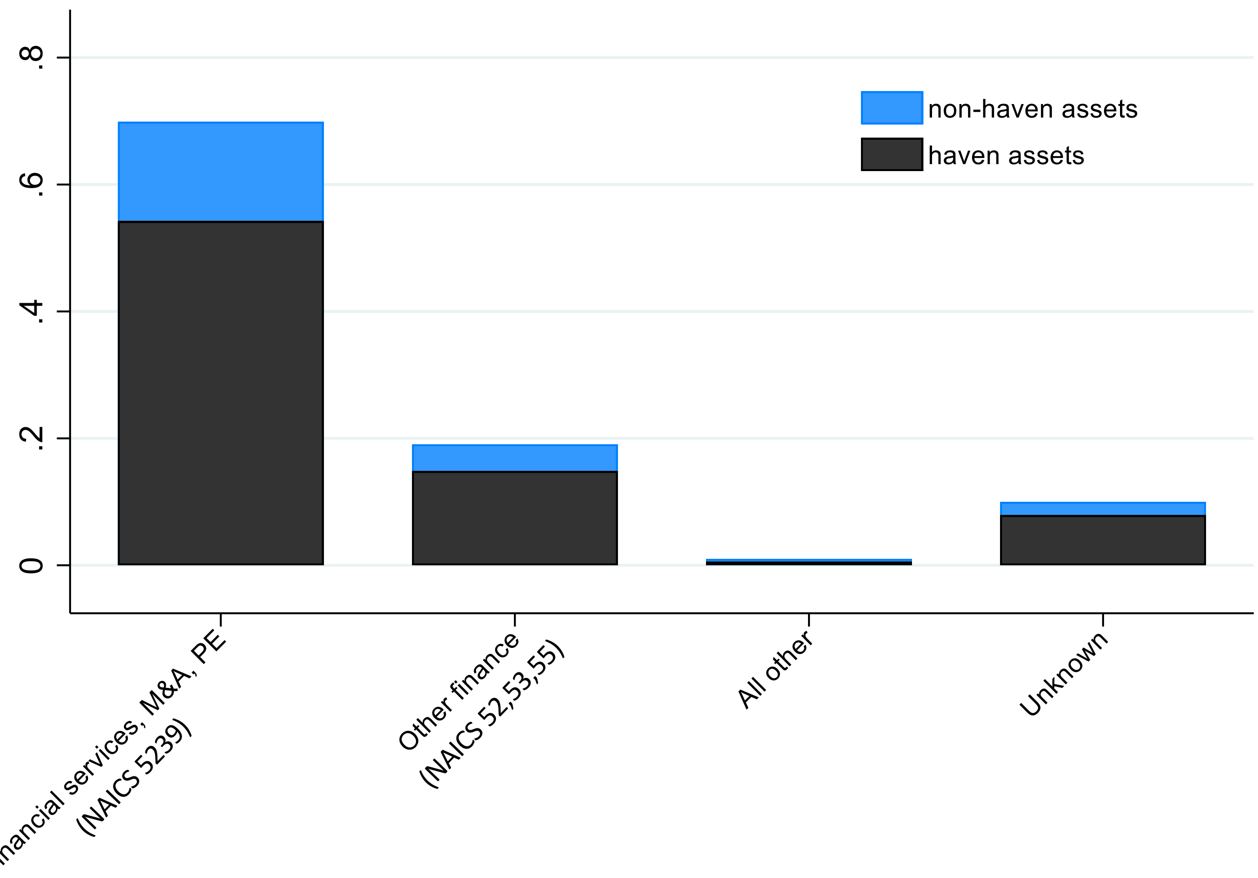
Partnership account owners and their shareholders

Partnerships hold the plurality of offshore assets, 78% of which are in havens. Using the micro data, we can learn about taxable owners

1. Link partnership account owners to the entity income tax return (Form 1065) for partnership information

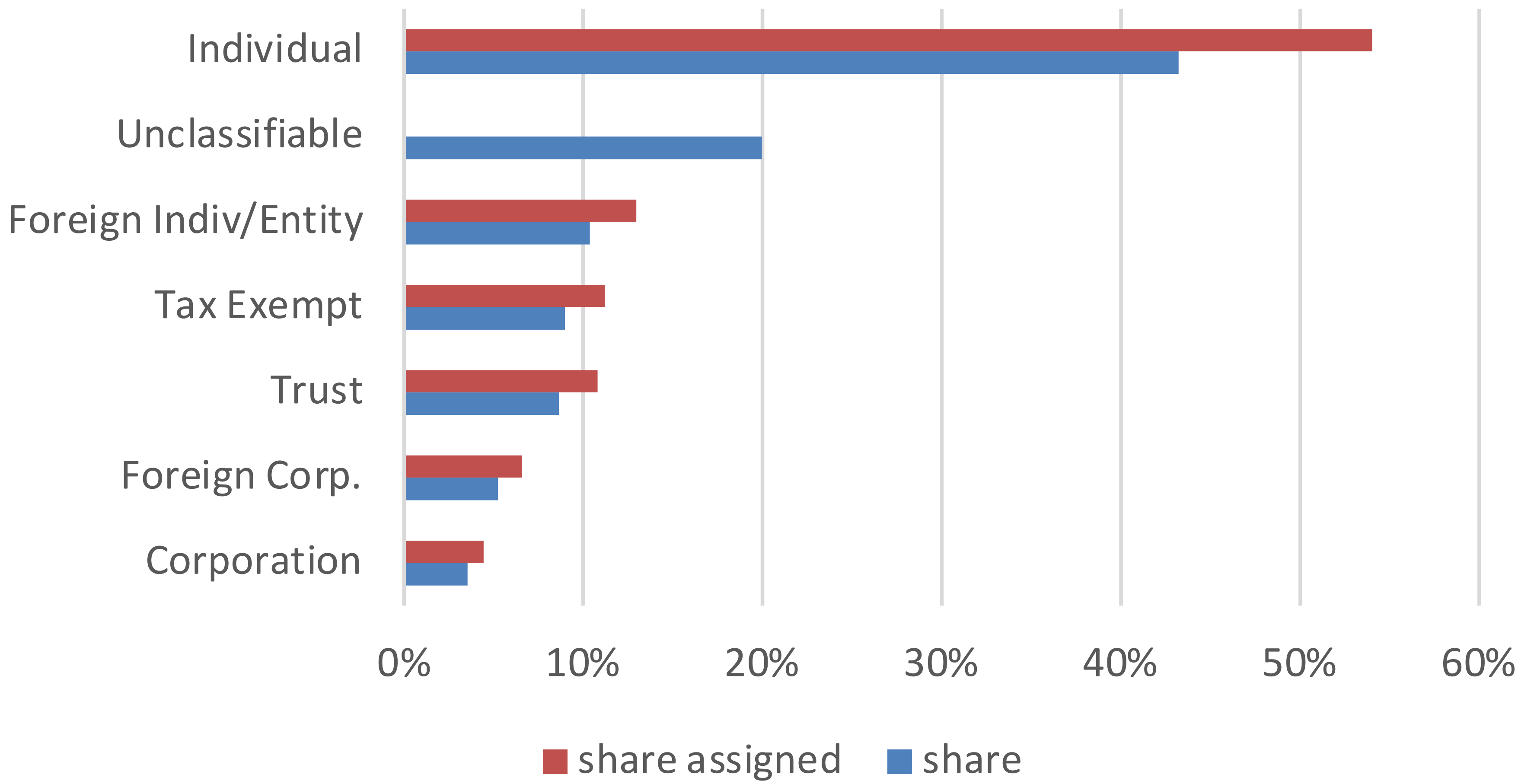
2. Link shareholders to the partnership
   - Distribute foreign assets and income to the shareholders (based on their share of total income distributed on K-1s)
   - Look through levels of pass-through ownership to ultimate taxpayer (Cooper et al. 2016)

Shares of partnership assets by industry and location (2018)



Compare to partnership income from all partnerships in 2011 (Cooper et al 2016): 70% Finance, 11% professional services

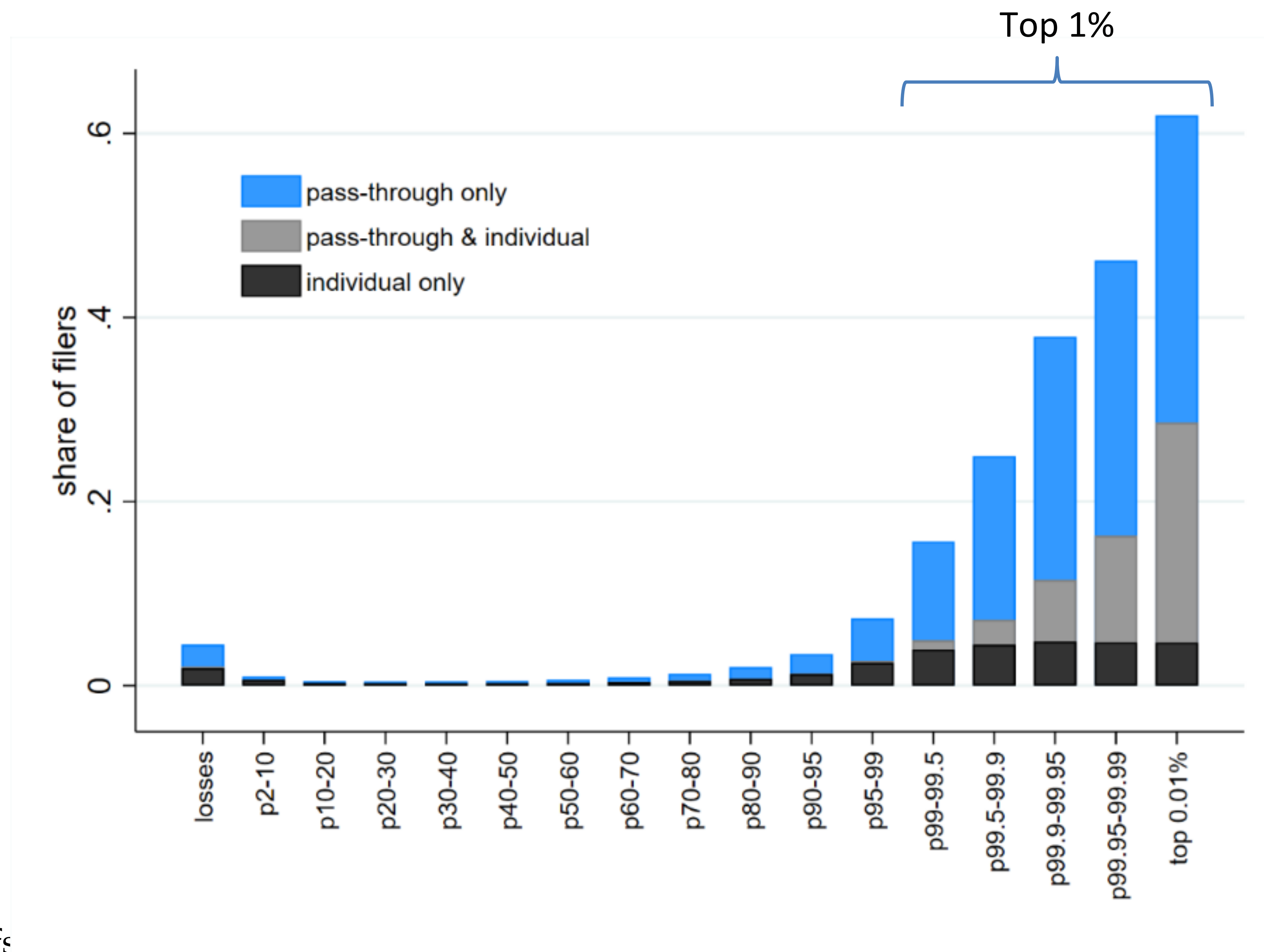
Shares of Partnership foreign assets by beneficial taxable owner type (2018)



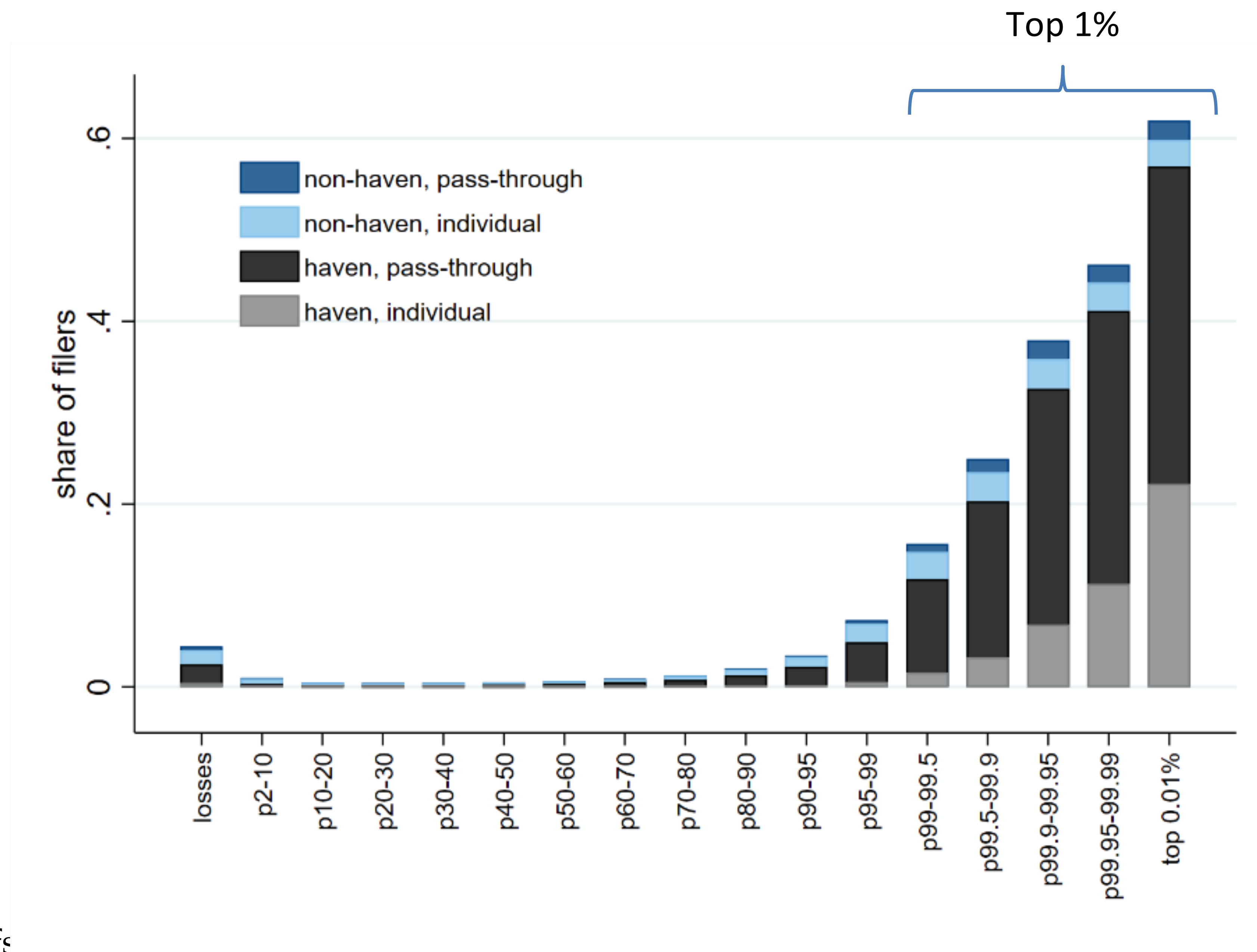
Compare assigned share of partnership foreign assets (red bars) to shares of all partnership income from in 2011 (blue bars, Cooper et al 2016): 20% unclassifiable, 43% individual, 5% tax exempt, 9% foreign, 7% trust, 10% corp

Beneficial individual owners of foreign assets across the income distribution

Share of taxpayers with a foreign account by position in the income (AGI) distribution (2018)



Share of taxpayers with a foreign account by position in the income, haven v non (2018)



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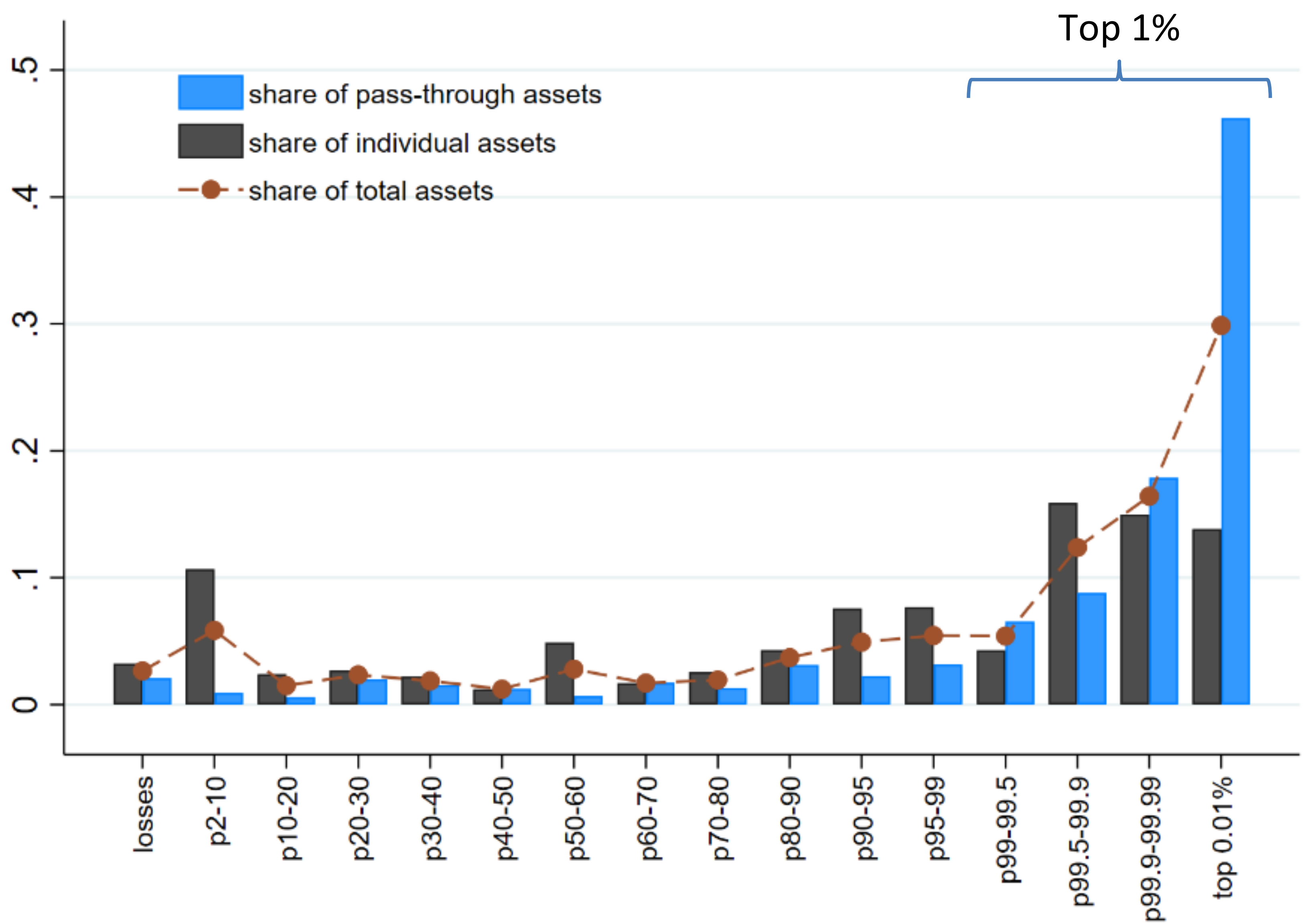
Distribution of assets held directly and held through pass-throughs (2018)



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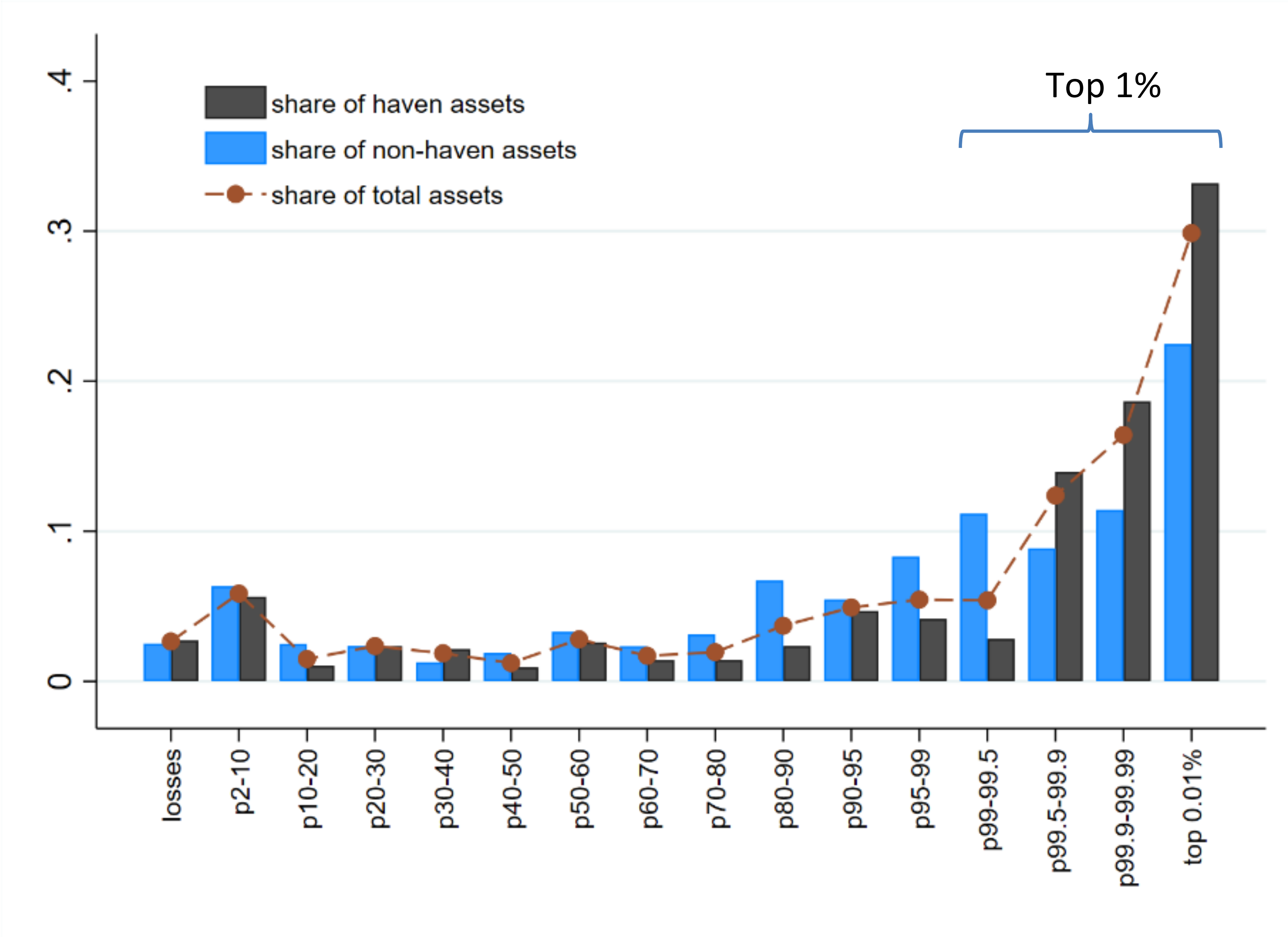
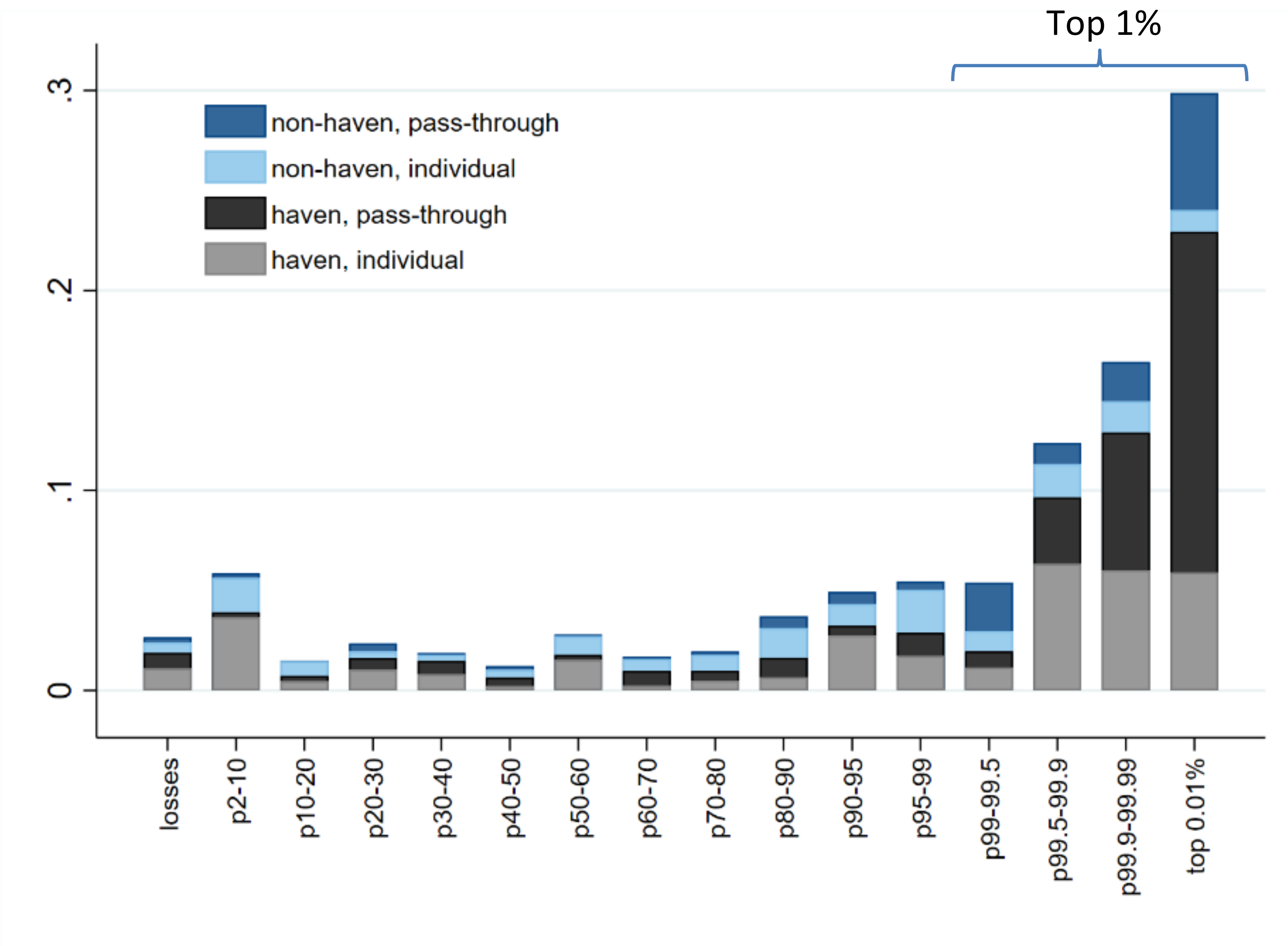
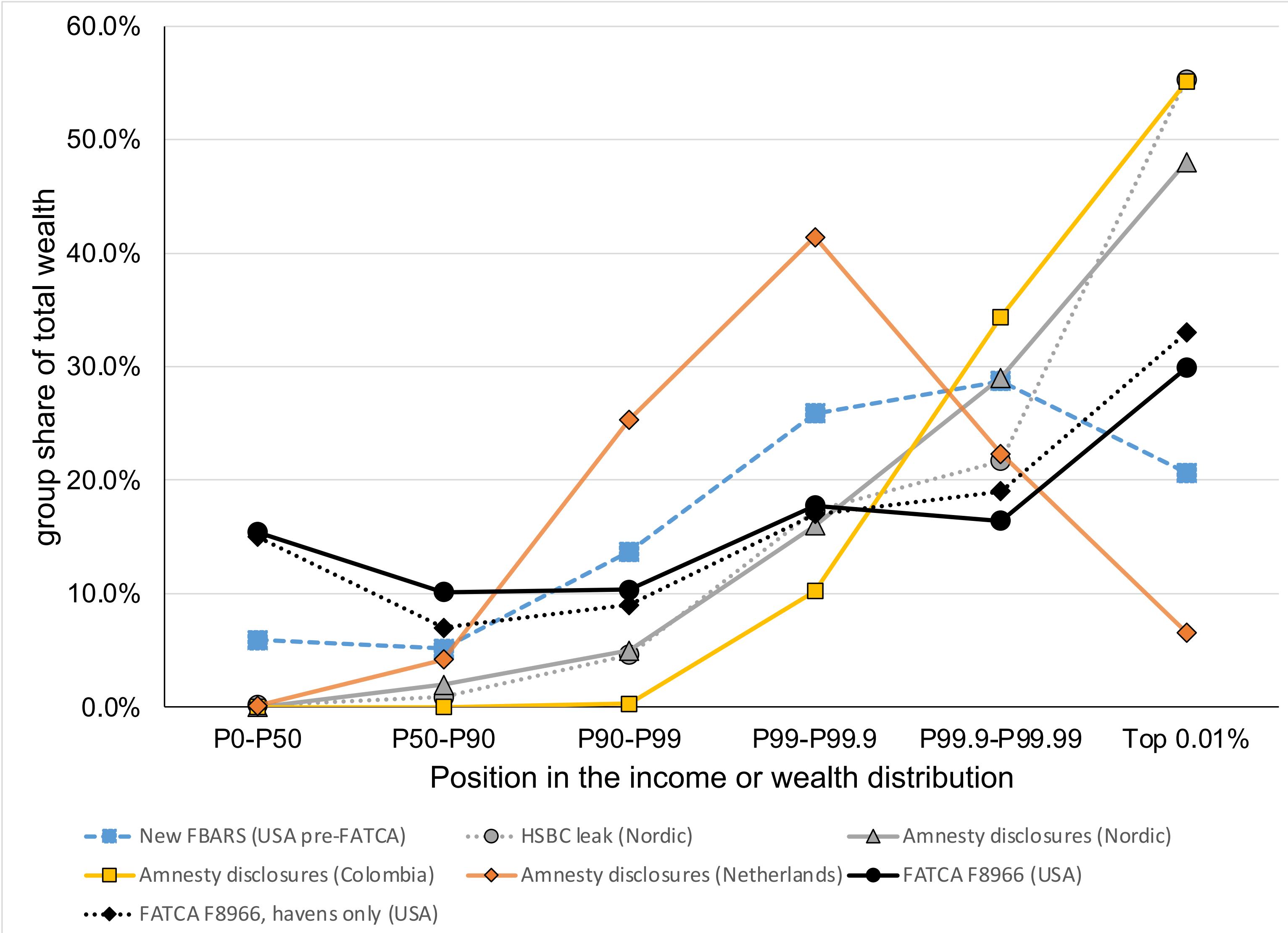
Distribution of assets held in havens and held in non-havens (2018)



Distribution of total assets (2018)



Comparisons: Concentration of Offshore Wealth



- All non-US data rank by wealth; US data rank by income (AGI)
- Sources: Johannesen et al 2020 (USA pre-FATCA), Alstadsæter et al 2019 (Nordic), Londoño-Velez & Ávila-Mahecha 2020 (Colombia), Leenders et al 2020 (Netherlands)

Takeaways + Next Steps

Takeaways

- FATCA reports provide new micro evidence on offshore holdings
    - $3.98 trillion of financial wealth.
    - $1.94 trillion in tax havens (49%), larger than previous estimates

- A large share of offshore wealth is held **indirectly through entities** (at least 46%), particularly partnerships (at least $1.3 trillion, 32%))
    - <u>Implication</u>: Effects of tax or enforcement policy depend significantly on how they affect these entities and how they respond

- FATCA accounts, and especially offshore wealth, are **highly concentrated**
    - 62% of households in the top 0.01% of the income distribution have an account identified by FATCA reports
    - 64% of foreign assets are owned by the top 1% and 30% by the top 0.01%
    - 77% of top 0.01% for. assets held through pass-throughs (61% of top 1%)
    - 77% of top 0.01% foreign assets held in havens (74% of top 1%)
    - <u>Implication</u>: Tax or enforcement policy disproportionately affect assets held by extremely high-income taxpayers

Further Research/Work In Progress

- Find scope for a substantial compliance response ($4 trillion held at top of the distribution, mostly in havens and through partnerships)

- **Open question**: To what extent do the income and assets reported through FATCA yield <u>new</u> tax compliance?
  - i) Are they tax compliant post-FATCA?
  - ii) Were they tax compliant pre-FATCA?
  - iii) Was there an additional compliance effect from those who chose to repatriate?

- Challenges: (i) Long lead-up b/w announcemet (2010) and full FFI reporting (2016). (ii) Control group

- Cost-Benefit Debate: FATCA has received public criticism for additional compliance costs on foreign banks and Americans abroad (e.g. Taxpayer Advocate, 2016, Oei, 2018).

Appendix

Insights from the literature

- **Pre-FATCA enforcement caused modest increase in compliance**
  - Increase in reported foreign accounts around U.S. enforcement efforts in 2008-2009 (Johannesen, Langetieg, Reck, Risch and Slemrod, 2020)
  - Decrease in offshore deposits and the value of offshore banks around leaks of customer data (Johannesen and Stolper, 2017)
- **…as well as actions by evaders to circumvent enforcement**:
  - More indirect ownership through offshore corporations (Johannesen, 2014; Omartian, 2016)
  - Relocation of assets to non-cooperating havens (Johannesen and Zucman, 2014)
- **Indirect evidence that FATCA / CRS boosted tax compliance**
  - Decrease in the use of offshore holding companies around implementation of FATCA (Omartian, 2016)
  - Drop in foreign-owned assets at activation of automatic information exchange (Menkhoff and Miethe, 2017; Casi et al., 2018; De Simone et al., 2018)

Pre-FATCA enforcement initiatives

Global battle against offshore tax evasion in the past decade:

- Legal action against offshore banks
  (U.S.: case against UBS starts in July 2008)

- Treaties with tax havens: case-by-case information exchange on request
  (U.S.: treaties with Switzerland, Luxembourg, Panama in 2008-2010)

- Automatic Exchange of Information (AEOI) agreements with specific set of countries

- Temporarily reduced penalties for voluntary disclosers of offshore assets
  (U.S.: OVDP starts in March 2009)

- Whistleblowers in offshore banks and tax haven law firms
  (U.S.: Brad Birkenfeld's whistleblowing triggers the case against UBS)

Matched and unmatched owner types (2018)

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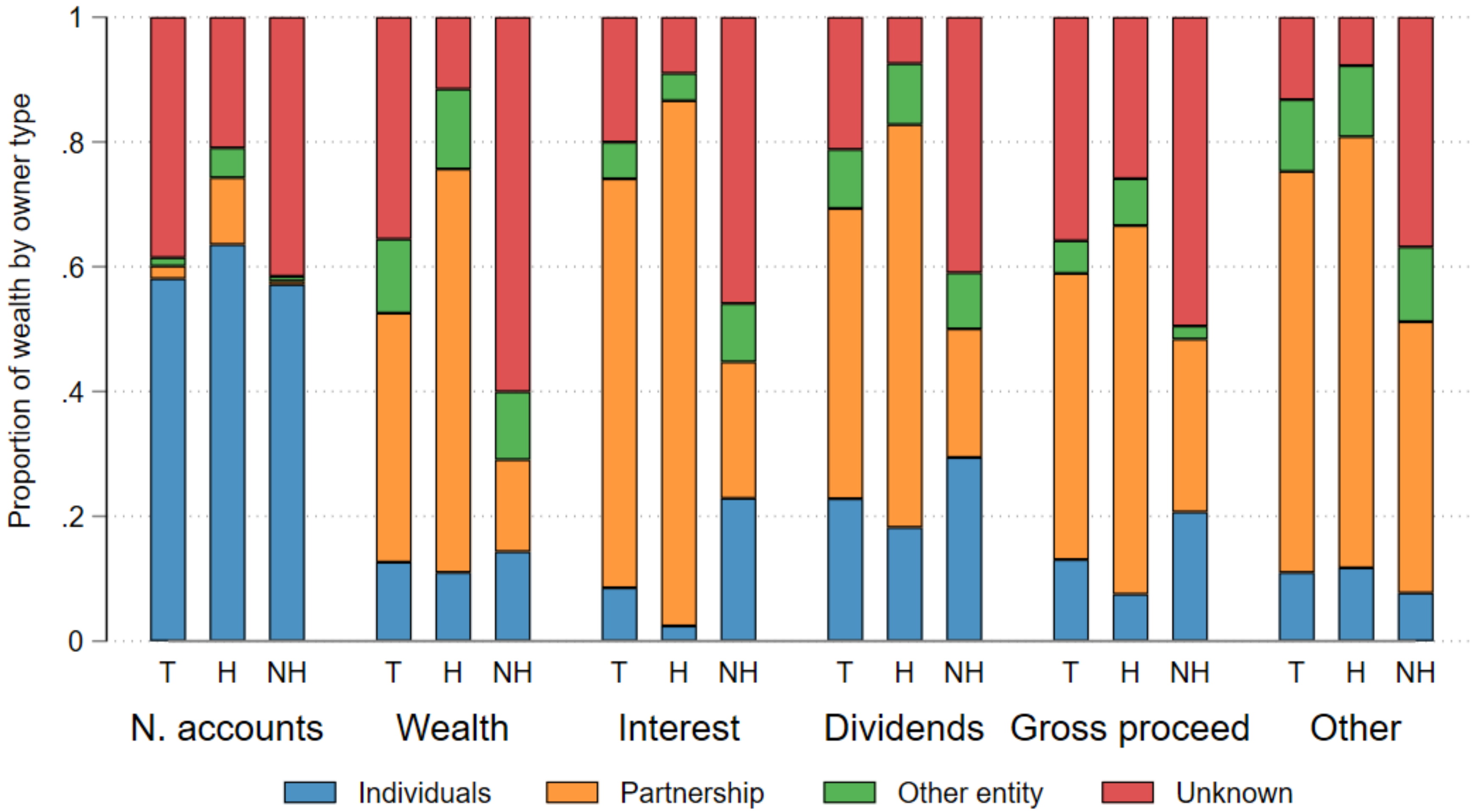
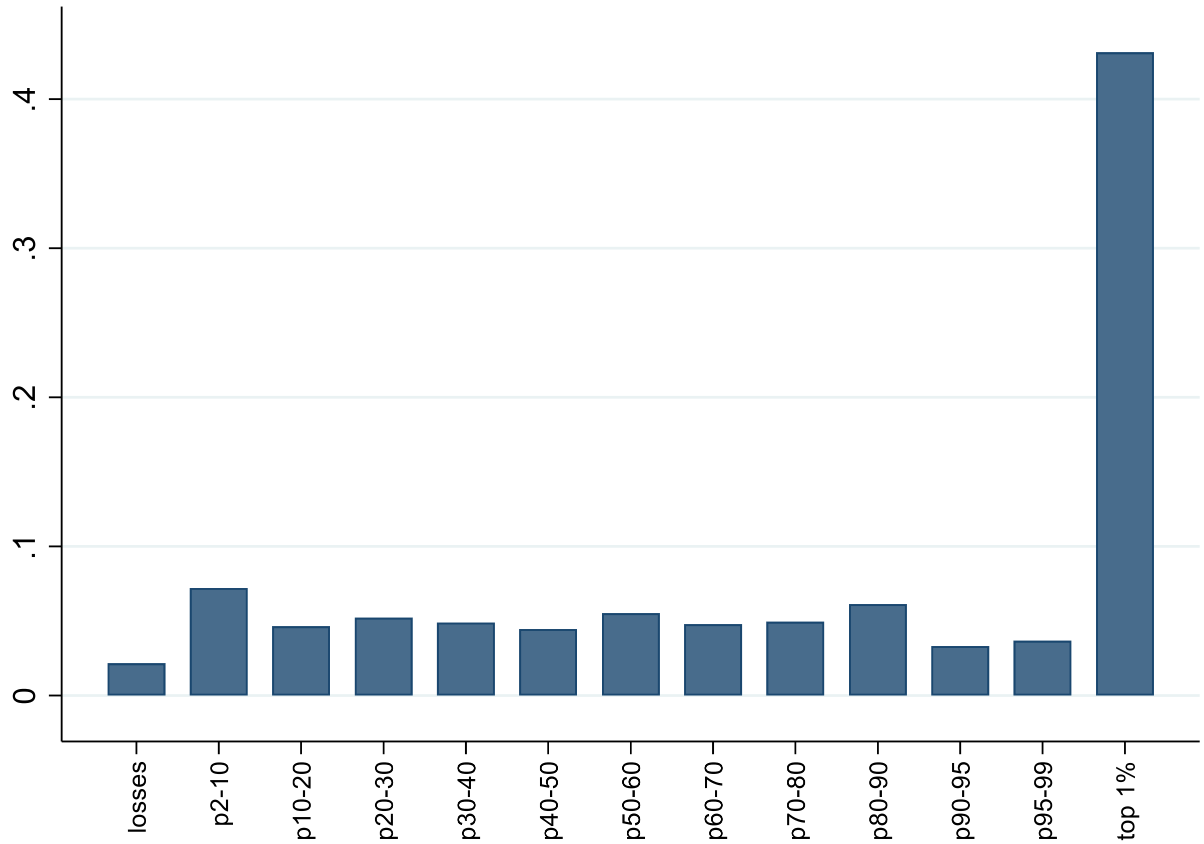


T = total, H= haven, NH = non-haven

(Ad hoc) Robustness to $50K reporting threshold



Hypothetical distribution of foreign assets assuming 10% of households below 90th percentile have $40,000 in foreign assets (i.e. just below the FATCA reporting threshold)

- 42% of assets held by top 1%, relative to observed 64% on FATCA reports (21% by top 0.01% relative to 30%)