The Washington Times
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Learning from What Works

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Published March 31, 2010

Low taxes and financial privacy laws should be emulated

ZURICH

Economists, political scientists, reporters and pundits spend too much of their time looking at dysfunctional societies and trying to explain why there are poverty, joblessness and hopelessness. In many ways, Haiti is easy to explain - no rule of law and 200 years of corrupt and incompetent governments. Switzerland is the polar opposite. It has almost no corruption and has the rule of law with honest, competent judges and government administrators. The question should be, "What can we learn from the Switzerlands of the world about how to do things right" rather than, "What is wrong with the Haitis of the world?" Switzerland manages to run a smaller government as a share of gross domestic product than the United States and most other countries while providing a higher level of service, security, prosperity and freedom. How does it do that?

In many ways, Switzerland seems unlikely to be such a long-term global success story. It is a small country with religious and language differences; nevertheless, the Swiss have managed to live peaceably together for a long time. It has few natural resources, yet it has managed to have one of the highest per capita incomes in the world. It has a world-class health care system, which is privately run. Health care insurance is subsidized, and everyone has access regardless of income, but there is no "public option."

Switzerland is not perfect, but it is clean, prosperous, well-managed, pleasant, humane and very free. In the more than three decades I have been coming to Switzerland, I have been convinced that the United States and the rest of the world can learn from many things the Swiss have done. The Swiss are practical rather than ideological, but they do revere liberty. They protect private property and free markets and restrain themselves from rampant deficit spending. The Swiss maintain a sound currency, which has been rising against the euro, dollar and pound. Capital, goods and services, with few exceptions, move freely into and out of the country.

Long ago, the Swiss understood that most things government needs to do and constructively does are at the local level. So, unlike in most modern nation-states, local government has the bulk of the resources and activities, while the central government remains relatively small and less important in the daily lives of the people. In the U.S., roughly two-thirds of government is at the federal level, and one third is at the state and local level. Switzerland is just the opposite, with roughly two-thirds of government being at the state (canton) and local level. Both the United States and Switzerland are federal republics. If one reads the Federalist Papers and the other works of the American Founding Fathers, it is clear they envisioned a nation that operates much more like Switzerland than one with the large central government the U.S. now has.

The maximum marginal tax rate at the federal level in Switzerland is about 11.5 percent, while in the U.S., it will be more than 40 percent as a result of Obamacare and the planned expiration of the George W. Bush tax-rate cuts at the end of this year. In Switzerland, maximum income tax rates in the cantons range from 10.9 percent in Zug to about 30 percent in places like Geneva. In the U.S., state and local income tax rates range from zero in places like Texas and Florida to roughly 12 percent in New York City and California. Thus, the overall maximum income tax rate in Switzerland ranges from roughly 20 percent to 40 percent, depending on location, while in the U.S., the maximum rate ranges from 40 percent to 51 percent.

Switzerland also does not impose a capital gains tax, and most cantons allow large deductions for interest and dividends. On the negative side, Switzerland imposes a value-added tax (VAT) and a very small wealth tax. On the positive side, the average combined federal-canton corporate tax rate is 21.3 percent (and may be as low as 11.8 percent in some places) while in the U.S., the average combined federal-state rate is more than 40 percent.

One of the things most misunderstood about the Swiss is their financial privacy laws, which they view as a human rights issue. Pierre Bessard, executive director of the Institut Constant de Rebecque in Lausanne, noted: "These laws are a relevant part of the Swiss tax system in that tax authorities do not have access to any financial information not expressly declared by taxpayers. However, there is an anonymous withholding tax levied on interest and dividend income paid to residents (and now EU nonresidents), who have the option of claiming a full refund when filing their tax returns. Bank secrecy laws in Switzerland underscore the principle of self-declaration in a contractlike relationship between citizens and government and reflect a moral imperative that individuals have a right to privacy. Indeed, the laws were significantly strengthened in 1934, helping German Jews protect their assets from Nazi expropriation. Today, bank secrecy performs the same role, providing a safe refuge for victims of religious persecution, ethnic discrimination, political harassment, fiscal oppression, government instability and crime."

Without Switzerland, the world would be a far less prosperous and more repressive place. The Swiss and other low-tax states provide the necessary tax competition to keep the high-tax states from totally oppressing their citizens. Financial privacy stops evildoers, whether criminal gangs or criminal governments, from totally expropriating the assets of innocents. It is ironic that many of the countries criticizing Switzerland are engaged in fiscal mismanagement, including the United States, and abuse of the basic human right of privacy.

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