The Well-Kept Secrets of International Finance

About: Brooke Harrington, *Capital Without Borders. Wealth Managers and the One Percent*, Harvard University Press

by Anne Monier

In her exploration of the exclusive world of wealth management, Brooke Harrington dives into the heart of capital globalization. As pillars in the structure of international finance, wealth managers increase the capital of the world's richest people by circumventing government regulations.

Who are wealth managers? What does their job entail? At a time of growing global inequality, Brooke Harrington, Professor of Economic Sociology at the Copenhagen Business School, focuses on these key players in the system that controls the management, accumulation and circulation of capital.

The book provides a fascinating insight into a world of which there is little public awareness and on which few studies exist, given that it is particularly difficult to obtain information on these shadowy figures. This difficulty stems not only from the complexity of any enquiry into the upper classes, but also from the cult of secrecy that characterizes this profession, further increased in recent years by wealth managers' belief that they are under attack—from organizations such as the OECD, which is a vocal critic, and from the press, through the revelation of a series of financial scandals: the "Offshore Leaks" in 2012, "LuxLeaks" in 2014, the "Panama Papers" in 2016 and the "Paradise Papers" in 2017.

Although extensive field surveys in this area are rare on account of the prohibitive costs (in terms of both money and time), they do provide access to information that is otherwise difficult to obtain. Harrington has overcome these obstacles, conducting an ethnography—completing a two-year wealth management course in Switzerland and Lichtenstein, and investigating within the primary association for wealth managers, STEP (Society of Trust and Estate Practitioners)—as well as semi-structured interviews with wealth managers, whose profile is relatively uniform: male (71%), white (70%), and from diverse specialist areas (law, accounting, banking, etc.).

The role of wealth managers is to protect and increase their clients' wealth. To that end, they move money across different structures and countries in order to avoid detection by tax authorities, creditors, courts, and even heirs or anyone else likely to claim a share. The three key components of the profession are freedom, mobility and discretion. Through their work, wealth managers are contributing to the internationalization of global finance and the dawn of a new era: financial capitalism.

The Wealth Management Profession

The role of wealth managers is to seek out the most favorable fiscal, regulatory and political conditions for their clients' fortunes, depending on the type of assets and the clients' aims, and then to create complex structures made up of inter-linked entities (such as companies, trusts and foundations) often with varying purposes (reducing taxes, circumventing regulations, controlling a family business, etc.). Although some professionals have the numerous skills required for implementing these structures within a national jurisdiction, the international transactions being performed require the intervention of a team of specialized advisors.

An example: trusts

A structure that dates back to the Middle Ages and is based on interpersonal relationships.

Trusts originated in medieval England. When knights departed on a crusade, they had to leave their fiefdom and feudal rights in the hands of a trusted person, which gave rise to a legal procedure known as *use*, which later became a *trust*. Trusts were therefore based on interpersonal relationships and trust between two individuals.

Principle and characteristics of a trust

A trust is created when a person (the settlor) transfers his/her assets to another (the trustee) for the benefit of a third party (the beneficiary). A trust has two main characteristics: the transformation of property (1) and a particular legal status (2). First of all (1), the ownership and legal responsibility for the assets passes from the settlor to the trustee, but their use passes to the beneficiary: the trustee must manage the assets in the beneficiaries' interest and not for his/her own profit. Second, unlike other asset-holding structures such as foundations and firms, trusts are not separate legal entities in their own right (2): one consequence of this is that a trust cannot be sued or go bankrupt in the way a firm can.

Obscurity and flexibility: enjoying the benefits of property without the drawbacks

Most importantly, trusts are loosely regulated structures which grant the various parties almost total confidentiality. As these are not separate legal entities, they are not registered. Trusts are therefore an instrument that makes it possible to enjoy the benefits of assets ownership without any of the constraints and obligations involved.

Trusts, a key player in the story of financialization

The freedom that a trust gives from tax regulation and other forms of regulation makes it an ideal instrument for accumulating wealth, for both individuals and firms. That is why trusts, in addition to serving high-net-worth individuals, are used in international financial transactions between firms. Trusts thus contribute to the financialization of the economy in main three ways: by consolidating the power of the investor as the central figure in the global economy; by propagating the dominance of Anglo-American finance; and by increasing the autonomy of finance from the nation-state system. By facilitating the maximization of profit and the international movement of capital, trusts have helped to free finance from state control and accelerated the financialization of the economy.

Source: Brooke HARRINGTON, "Trusts and Financialization", *Socio-Economic Review*, 2017, Vol. 15, N°1, 31-63.

An analysis of the position of wealth managers in the hierarchy of finance professions is indicative of the standards that are specific to this industry. Wealth managers have relatively "average" salaries (around $200,000 p.a.) in comparison with other finance professionals, and suffer from a lack of prestige in the sector, since their activity is costly with a relatively low profit margin—since the hierarchy in finance is proportional to the profits generated. However, they enjoy symbolic perks: they believe themselves to be doing a creative and intellectually stimulating job (which is rare in finance) and find "meaning" in their profession from the feeling that they are "helping families" and from having contact with the elite, who are difficult to access and lead enviable lives.

The Key Role Played by Trust

Wealth managers build up a long-term relationship with their clients, which may last a whole lifetime or even longer, continuing with the children and grandchildren. This longevity can be explained by the fact that, like a family doctor, a wealth manager has access to information that is particularly private, personal and sensitive inasmuch as it can have an impact on the family's wealth. The intimate knowledge that wealth managers have of their clients gives them immense power, making them indispensable and difficult to replace.

The challenge for wealth managers lies in establishing and maintaining that relationship of trust with clients, made particularly difficult given the latter's tendency to be suspicious of others' intentions—be they outsiders, the state, or family—with regard to their money. To overcome that lack of trust, wealth managers seek to embody trust in a deeply personal way with each client. Their physical presence is vital—requiring numerous face-to-face meetings—and they must adapt their appearance, character and attitude to their client's cultural and socio-economic situation.

The Techniques Involved in Wealth Management

Two major developments resulted in the professionalization of wealth management: the increasing fungibility of capital, and the financialization that took place in the 1970s and 1980s, aided by a lifting of restrictions on the international movement of capital and a weakening of regulations governing the financial markets. In 1991, one of the main professional associations was created (STEP, which now represents over 20,000 members in 95 countries), accelerating the professionalization process, even if the boundaries limiting the activity remain hazy.

This process of financialization has led to the emergence of a new, highly mobile group of elites whose capital is dispersed across the globe: wealth managers must no longer simply do their best in one country according to the legal and financial opportunities, but instead exploit legal loopholes and conflicts between laws in different countries. This technique is known as "regulatory arbitrage". Wealth managers develop a financial and legal activity that "operates within the letter but against the spirit of the law", in a grey area. Tax evasion is only the tip of the iceberg: the primary goal is to protect the client's assets from any external dangers (taxes, regulations, creditors, etc.) and internal threats (ex-wives, heirs, etc.).

The Role of Wealth Managers in Perpetuating and Increasing Inequality

After the 2008 financial crisis, the issue of inequality took centre stage once again. According to Harrington, the growth of inequality should be considered partly through the prism of asset transformation. Assets are more stable than capital, creating social configurations that prevail from generation to generation, but obtaining data on them is not easy. They are often hidden, placed in unregistered structures and protected by a strategy of obscurity—in several countries, wealth managers may even face criminal sanctions if they divulge information on their clients' capital flows. The little data available is generally derived from lawsuits or revelations made by employees of these organizational structures.

While it may be difficult to determine the exact role played by wealth managers in the growth of inequalities, Harrington explains that wealth managers "intervene at three crucial points in their clients' asset accumulation cycles: they minimize dissipation due to taxes, debts and penalties, maximizing the surplus available for further growth. Next, wealth managers give their clients access to exclusive opportunities to reap significant profits at low risk. Third, carefully managed succession processes keep the wealth concentrated in a few hands [...]. The result is a kind of perpetual-motion machine of wealth creation: [...] these structures preserve and compound advantages over time."[1] Their work therefore helps to consolidate their clients' dynastic fortunes and fuels long-term frameworks of social stratification.

Finally, wealth managers and their clients exercise a certain amount of political power. By "lobbying onshore governments, writing new laws offshore, and influencing elections" (for example, by supporting certain candidates), they effectively block "legislation and policies that might interfere with this wealth concentration and its broader consequences." As Harrington explains, "the effect is not only to make the rich richer but also to undermine meritocracy, mobility, and political voice for others."[2]

An Ambiguous Relationship with the State

Unlike other liberal professions, wealth management is characterized by its independence from state authority, and the work thrives by exploiting states' loopholes and resources to the clients' benefit. Wealth managers are not anti-state or anti-law; in fact, as Harrington explains, the states, laws and regulations created by the Westphalian nation-state system are precisely what enable wealth managers to circumvent them. They play a game of cat and mouse with tax authorities around the world, a process made easier by the lack of

[1] Brooke Harrington, *Capital Without Borders. Wealth Managers and the One Percent*, Cambridge MA, Harvard
[2] Ibid.

international laws governing wealth and its movement, or any institution responsible for exposing the loopholes and conflicts between national laws. The state has not become irrelevant, but has instead been "hijacked" to serve the interests of the ultra-rich: wealth management has not established itself "against the state" but rather by "cozying up to the state" (Vauchez & France, 2017).

Furthermore, there is an ambiguous relationship between wealth managers and the offshore countries holding this capital. While the profession brings those countries a certain level of economic prosperity, at least in the short term, this seems to come at a very high cost, particularly considering that the clients of wealth managers often have no connection with these countries and therefore have little concern for their development: the laws and policies of such countries are often geared primarily towards these foreign elites, their economy is fragile and their political, educational and social institutions are weakened by this dependence on offshore finance.

Reviewed: Brooke Harrington, *Capital Without Borders. Wealth Managers and the One Percent*, Cambridge MA, Harvard University Press, 2016, 318 pp.

Further Reading

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