The Importance of Being South Dakota

by Michael Curtis

I could cry salty tears… tell me now how long has this been going on.

It has become increasingly evident that while most Americans and other people at some point fly over the state of South Dakota, some land their money there. This is startingly revealed in the Pandora Paper, the extraordinary leak of tax haven files that indicate the relationship between people in powerful positions and secret offshore finance. The Papers reveal current and former leaders who have owned secret companies and trusts: King Abdullah II of Jordan, the prime ministers of Cote d'Ivoire and the Czech Republic, the presidents of Ecuador, Kenya, and Gabon, and the former presidents of El Salvador, Panama, Paraguay, and Honduras, as well as a host of others. They include a motley assortment: criminals, business giants, cult leaders, Hollywood actors, soccer stars, mistresses of the famous, movie directors, famous singers.

The Papers also include documents from 206 U.S. trusts in 15 states and Washington, D.C. and 22 U.S. trustee companies. The U.S. has become an increasingly attractive home for hidden wealth. In the U.S. the biggest tax haven is South Dakota, a thinly populated state.

The state of South Dakota is mildly familiar from two former residents: Laura Ingalls Wilder, author of the Little House on the Prairie series of children's books; and Senator George McGovern, the Democratic candidate in 1972 for the presidency who obtained only 37% of the national vote and won one state, his own, The main tourist attraction in the state is Mount Rushmore, the colossal national monument of the faces of four U.S. presidents, built 1927-41, in the Black Hills, the land of the Sioux. The 60 foot heads of the presidents which represent the nation’s birth, growth, development, and preservation, attract two million visitors a year who park to see the monument. But increasingly since the 1990s South Dakota has been the place where wealthy people and businesses park their wealth, mostly in trusts.

Trusts are ancient and complex financial bodies that own assets. In the past, since a dynasty trust was immortal, property remined in the family that owned it forever. But because of this fact, that property was thus locked up, British judges in the 17th century created the rule against perpetuities, limiting the duration of trusts to around a century. This rule was imported into North America.

Until the mid 1980s the length of trusts in South Dakota were thus limited to about a century, a limit intended to curb the intergenerational power of the wealthy. However, in 1981 Governor William, Wild Bill, Janklow, former U.S. marine and son of a Nuremberg prosecutor, abolished laws that set an upper limit to credit card interest rates that lenders could charge. These rules were a legacy of the New Deal era which protected consumers. As a consequence, the Citibank based its credit card business in Sioux Falls, the most populated city in the state, and could charge borrows any interest rate it wanted. Credit cards became profitable, and SD evaded the restrictions imposed by the other states. SD thus had and still has a financial service industry.

In 1983 the state abolished the rule against perpetuities. The rule created by British judges was erased by a few words. SD became the first state to allow perpetual trusts, money that continues untouchable in perpetuity. It attracted the Pritzker family of Hyatt Hotels, and the head of Wrigley

Chewing Gum who set up private trusts in Sioux Falls .

Abolishing the rule against perpetuities opened the flood gates in SD, a state which has no income tax, no inheritance tax and no capital gains tax, or tax on withdrawals from retirement accounts, and a relatively low state tax.

Other states, Alaska, Delaware, followed by abolishing the rule against perpetuities. To keep ahead of these competitors, Janklow in 1997 created the "trust task force" to search for more legal innovations that could work, "establishing and maintaining SD's stature as the premier trust jurisdiction in the U.S."

Unlike most jurisdictions, where trusts have to benefit someone other than the benefactor, in SD clients can create a trust for the benefit of themselves, and one that is secret as court documents relating to it are kept private. A trust becomes immune from any creditor claiming a share of the assets.

Increasingly, wealthy individuals have been taking advantage of one type of trust the grantor -retained annuity trust, a special type that allows a grantor to pass a considerable amount of wealth to the next generation with little or no gift tax cost. Among those involved are former NYC Mayor Michael Bloomberg, private equity mogul Stephen Schwartzman, Facebook CEO Mark Zuckerberg, Laurene Powell Jobs, widow of Apple founder Steve Jobs, and the industrialists Charles and David Koch.

SD has continued to pass rules making trusts more attractive, allowing trusts where the settlor and beneficiary can be the same person. All documents involving a trust are sealed., making it impossible to know who has one, including those created to benefit themselves rather than a third party. Other states have devised methods by which wealth can be hidden. Delaware has a limited liability corporation. Florida has an all cash condo purchase system. But since 1981, SD can be regarded as the most open state for financial services, offering the best privacy and asset protection laws in the country, and maybe in the world.

Besides trusts, SD has shell companies, a business corporation with no economic substance whose sole purpose is to avoid taxes or other laws. In SD, a wealthy individual can give assets to a trustee who then invests the assets for a beneficiary , often a relative of the rich person. Those establishing trusts can list themselves a beneficiary and do not need to visit the state.

SD has increased its role as a tax haven for both Americans and foreigners, such as Ecuadoran president Guillermo lasso who has transferred millions, the Chinese real estate billionaire Sun Hongbin, the head of the sugar company in the Dominican Republic, the executive of the Brazilian orange juice firm. The largest law firm in the U.S., Baker McKenzie, has been active in creating the offshore system.

In 2010, SD trust companies had $57.3 billion in assets. Today it is said to be over $360 billion. One company, Trust Company has international clients from 54 nations. Of the 201 trusts in the U.S., 81 are based in SD.

Critics of the offshore system argue that companies, whose ownership is legal, can hide gross abuses, money laundering, rackets, bribery, and, at worst, finance terrorism , criminals, and human trafficking. They may cause disproportionate harm to poorer nations and increase national and global inequality by allowing the wealthy to avoid paying their fair share of taxes, and the costs of government, infrastructure, and education.

Can the four presidents on Mount Rushmore offer any advice on any changes to be made in preventing gross abuses of the U.S. legal and tax system?