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Sovereignty, Taxation and Social Contract

Allison Christians*

I. INTRODUCTION

Tax policy creates and reflects relationships between the market, the citizen, and the state. As a result, traditional tax policy discourse centers around the premise that decisions about taxation should be made exclusively within nations, independent of outside concern and interference. But this view of sovereign autonomy over taxation is increasingly inconsistent with a global economic reality in which market and regulatory relationships have been and are being fundamentally reformulated. Major theoretical developments in tax policy are now arising not through solely national political and legal processes but through the interactions of nongovernmental actors in transnational settings. Working together in networks, especially the Organization for Economic Cooperation and Development (OECD),[1] these transnational actors are gradually redefining the connection of taxation to sovereignty.

The OECD, long prominent as a central global institution for technical tax policy design,[2] is an increasingly important

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* Assistant Professor, University of Wisconsin Law School. I would like to thank Professors Hugh Ault, Dorothy Brown, Howard Erlanger, Tom Ginsburg, Mitchell Kane, Michael Livingston, Michael McIntyre, Diane Ring, and Gregory Shaffer, as well as the participants of the 2007 Law and Society Annual Meeting in Berlin, panel on Transnational Transformations of the State, and the faculty of the University of Minnesota School of Law who participated in a workshop over an early draft, for their thoughtful comments and suggestions. This project benefited from a generous research grant from the Wisconsin Alumni Research Foundation.

1. Thirty of the world's largest economies, including the United States, Japan, Germany, and the United Kingdom, but not China or India, are OECD members. *See* OECD, Ratification of the Convention on the OECD, http://www.oecd.org/document/58/0,3343,en_2649_34483_1889402_1_1_1_1,00.html (last visited Sept. 12, 2008).

2. *See, e.g.*, Arthur J. Cockfield, *The Rise of the OECD as Informal 'World Tax*

focal point for theory development because it is breaking with conceptual traditions that hold tax law sacrosanct to the state. The development is perhaps most evident in the OECD's work to curb harmful tax competition,[3] a project which has led it to articulate a version of sovereignty that prioritizes responsibility to the international community over the individual autonomy of nations. The OECD does not seek to instill this priority through a traditional mode of international cooperation, such as a multilateral treaty. Instead, the actors in this network tacitly seek a fundamentally different type of cooperation, according to which nations will voluntarily and unilaterally abstain from tax legislation, even that produced through democratic processes, if it fails to conform to the OECD's articulated vision of what constitutes appropriate tax competition.[4]

Though unstated and perhaps even unexamined by those in the OECD itself, this idea of cooperation depends for its coherence on the existence of an implicit global social contract. The OECD's articulated position is therefore consistent with a view of the relationships among nations that is based in one of

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Organization' Through National Responses to E-Commerce Tax Challenges, 8 YALE J.L. & TECH. 136, 139 (2006); *see also* Reuven S. Avi-Yonah, *International Tax as International Law*, 57 TAX L. REV. 483, 497–501 (2004) (stating that rules and norms developed at the OECD constitute customary international tax law); John F. Avery Jones, *Are Tax Treaties Necessary?*, 53 TAX L. REV. 1, 2 (1999) (stating that the OECD is the "world body" for international tax matters). Other sources of influence on tax law include traditional, "hard" types of law such as the GATT and related WTO agreements, as well as less traditional and less hard influences similar to the OECD, such as the European Union. *See, e.g.*, Michael Daly, *WTO Rules on Direct Taxation*, 29 WORLD ECON. 527, 529–30 (2006) (discussing WTO restriction of state autonomy in tax legislation); Claudio M. Radaelli, *The Code of Conduct Against Harmful Tax Competition: Open Method of Coordination in Disguise?*, 81 PUB. ADMIN. 513 (2003) (discussing how EU developments in taxation resemble the ostensibly voluntary mechanisms becoming popular in other forms of EU governance). National tax systems are also influenced to various degrees by norms and rules developed in other international institutional settings such as the United Nations, the Inter-American Center of Tax Administrations (CIAT), the IMF, and the World Bank, as well as national and non-governmental institutions such as the Harvard Law School International Tax Program's Southern African Tax Institute. For an analysis of the influence of various state, non-state, and international actors on tax reform, see Miranda Stewart, *Global Trajectories of Tax Reform: The Discourse of Tax Reform in Developing and Transition Countries*, 44 HARV. INT'L L.J. 139 (2003).

3. This is referred to as the "Harmful Tax Practices" project, but its main focus has been on the practices engaged in by countries that are typically identified as tax havens, such as Lichtenstein. *See* OECD, Harmful Tax Practices, http://www.oecd.org/topic/0,3373,en_2649_33745_1_1_1_1_37427,00.html (last visited Sept. 12, 2008).

4. *See infra* Part II.

the oldest and richest philosophical attempts to explain the existence of the nation-state itself.[5] But who is the OECD, and why should its envisioned social order bind legislative activity in the United States or anywhere else? Can and should principles and standards articulated by a relatively small and elite group of individuals frame the taxing rights of sovereign nations? The OECD's work on harmful tax competition demonstrates that this kind of framing is in fact occurring, even though it may not be explicitly articulated or understood as such.

The essential tension in the OECD's work to curb harmful tax competition arises from the intersection of the idea that nations are entitled to self-determination in most regulatory matters, including taxation, with the reality of a global marketplace. By articulating standards for appropriate tax competition, the OECD is signaling a major conceptual shift away from the conventional view that equates sovereignty with complete state autonomy over tax matters. The OECD's work evidences an emergent vision of sovereignty that entails positive obligations or duties of nations in exercising the power to tax—what I refer to herein as a nation's "sovereign duty"[6] to other

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5. Social contract theory attempts to explain why and how people organize into political societies, exchanging personal autonomy and independence for greater certainty and security. *See, e.g.*, THOMAS HOBBES, LEVIATHAN 89, 117 (Richard Tuck ed., Cambridge Univ. Press 1996) (1651) (describing life without the state as "solitary, poore, nasty, brutish, and short" and laying out the "laws of nature" which will remain unfulfilled in the state of nature because they "are contrary to our naturall Passions, that carry us to Partiality, Pride, Revenge, and the like," such that persons submit all of their rights to the sovereign in order to ensure their fulfillment); JOHN LOCKE, THE SECOND TREATISE OF GOVERNMENT ¶¶ 87–89 (J.W. Gough ed., Blackwell 1966) (1689) (analyzing what it means to consent to law, *i.e.*, government with the consent of the governed); JEAN-JACQUES ROUSSEAU, *Of the Social Contract*, *in* THE SOCIAL CONTRACT & OTHER LATER POLITICAL WRITINGS 39, 50 (Victor Gourevitch ed., Cambridge Univ. Press 1997) (1791) (positing that people need social order in order to preserve their innate freedom through cooperation, and stating that the theory of social contract can be reduced to the idea that "[e]ach of us puts his person and all his full power in common under the supreme direction of the general will; and in a body we receive each member as an indivisible part of the whole."). Hundreds of scholarly works have followed and expanded on these works, with major contributions by John Rawls and, more recently, Martha Nussbaum. *See generally* JOHN RAWLS, A THEORY OF JUSTICE (1971); MARTHA C. NUSSBAUM, FRONTIERS OF JUSTICE: DISABILITY, NATIONALITY, SPECIES MEMBERSHIP (2006).

6. Sovereign duty is not a term of art. Indeed, the duties attendant to sovereign status could properly be encompassed in the core term sovereignty alone, as is common in the political philosophy and international law/international relations literatures. *See generally* Robert Jackson, *Introduction: Sovereignty at the Millennium*, 47 POL. STUD. 423 (1999); Alan James, *The Practice of Sovereign Statehood in Contemporary International Society*, 47 POL. STUD. 457 (1999); Georg

nations under an implied social contract.[7]

This view of sovereignty could have powerful implications for national taxation. Recognizing ourselves as parties to a global social contract would require a fundamental reassessment of the conventional standards of tax policy design. Instead of focusing on national tax policy as appropriately reflecting only or even primarily the needs and wants of national constituents, a global social contract would require national policy to reflect outward as well, to consider the needs and wants of the worldwide community.

Accordingly, this article examines the OECD's work on harmful tax competition from a political philosophy perspective in order to identify the existence of a global social contract for taxation and to assess its content and implications. A contractarian approach demonstrates the inadequacy of traditional tax policy analysis tools that are applied as if any given tax system is bound to the demands and authority of the nation-state, when global integration and interdependence is the social, institutional, and economic reality. If nations have sovereign duties in accordance with a global social contract, current and future national tax policy choices can only be

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Sørensen, *Sovereignty: Change and Continuity in a Fundamental Institution*, 47 POL. STUD. 590 (1999). More specifically, in the context of international law generally, the idea is commonly held that states have some positive obligation to cooperate with each other. For example, UN Charter Resolution 2625 provides that "States have the duty to co-operate with one another, irrespective of the differences in their political, economic and social systems, in the various spheres of international relations, in order to maintain international peace and security and to promote international economic stability and progress, the general welfare of nations and international co-operation free from discrimination based on such differences." Declaration on Principles of International Law Concerning Friendly Relations and Co-operation among States in Accordance with the Charter of the United Nations, G.A. Res. 2625, at 123, U.N. GAOR, 25th Sess., Supp. No. 18, U.N. Doc. A/8018 (Oct. 24, 1970). Exactly what this resolution requires in terms of positive action is a matter of extensive debate within international law scholarship. For an introduction see, for example, A. V. LOWE, INTERNATIONAL LAW 110–113 (2007). For the purposes of this article, I extract the idea of sovereign duty from the larger concept of sovereignty itself in order to distinguish sovereignty from autonomy, as these two concepts are often conflated in legal scholarship that addresses the connections between sovereignty and taxation. *See infra* Part II.A.

7. The approach of this article is by no means the only analytical framework for examining the OECD as an institution and its influence on national law in the U.S. and elsewhere. The same issues could also be analyzed from a law and economics, utilitarian, game theoretic or international relations approach, among others. *See* Allison Christians, Steven Dean, Diane Ring & Adam H. Rosenzweig, *Taxation as a Global Socio-Legal Phenomenon*, 14 ILSA J. INT'L & COMP. L. 303, 306 (2008) (arguing that more analysis of tax policy from these various lines of inquiry would help clarify the role of law in regulating global economic activity).

coherently assessed in the context of these global obligations.[8]

It therefore seems imperative to understand what sovereign duty comprises and to determine what demands an international social compact might imply for national tax policy. That is the aim of this article. Part II describes the concept of tax sovereignty and its historically powerful role in shaping tax policy. In Part III, I make the case that through its work to curb harmful tax competition, the OECD is developing an expansive theory of sovereign duty in tax system design according to which the sovereign state, as a member of international society, is obliged to adhere to certain universal principles in exercising the right to tax.

Part IV contextualizes these observations within existing frameworks of political philosophy and international law/international relations literature to build a foundation for the OECD's implicit social contract theory and provide a means of critique. This part shows that while the OECD's official statements evoke the major themes of social contract theory, they may fail to fully explain the implications of asserting the existence of a social contract. A contractarian analysis of the OECD's work demonstrates the need for a deeper analytical examination of the interrelationship of sovereignty, taxation and social contract. Part V concludes that to the extent the OECD's work demonstrates that sovereign status carries certain requirements for domestic tax system design, we must find ways to assess the OECD's conception of what is required and what countries may expect of each other as a result of their shared membership in international society.

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8. This view accords with those held by many international law scholars. *See, e.g.*, Terence C. Halliday & Bruce G. Carruthers, *The Recursivity of Law: Global Norm Making and National Lawmaking in the Globalization of Corporate Insolvency Regimes*, 112 AM. J. SOC. 1135, 1173 (2007) ("national law reforms can no longer be purely national"). However, the perspective contradicts some well-respected views in tax scholarship. *See, e.g.*, Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 54 TAX L. REV. 261, 282 (2001) ("denying that a worldwide perspective is the proper lens for U.S. international income tax policy"). Graetz's perspective is specifically a response to the question of whether a country should design its tax system with the goal of seeking global distributive justice, a question that I argue can be most coherently addressed after determining whether states have any duties toward each other in the context of a social contract.

II. SOVEREIGNTY CONVENTIONS IN TAX POLICY

Understanding what tax sovereignty means is the logical starting point for this discussion, since ideas about sovereignty fundamentally inform ideas about the kinds of constraints sovereign duty might imply for domestic regulatory policy. Although it is not often explicitly defined, to speak of tax sovereignty is generally to suggest that taxation is an inherent or essential component of sovereign status.[9] Since taxation is typically the main means by which governments support themselves and provide public goods, the ability and need of the state to tax is easily conflated with the concept of sovereignty—it is difficult to conceive of a modern nation-state that could sustain itself and protect its people from physical or economic harm without raising revenue through taxation of some kind.[10]

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9. Scholars often assume that the right to tax is intrinsically associated with sovereign status, occasionally citing Hobbes for the proposition, but often offering little or no theoretical grounds for the statement. *See, e.g.*, Graetz, *supra* note 8, at 277 ("No function is more at the core of government than its system of taxation."); Deborah Bräutigam, *Building Leviathan: Revenue, State Capacity, and Governance*, 33 IDS BULL. 10, 10 (2002) (quoting Hobbes that "[t]hese are the rights which make the essence of sovereignty . . . the power of raising money"); Miranda Stewart, *Introduction: New Research on Tax Law and Political Institutions*, 24 LAW IN CONTEXT 1, 1 (2006). A few scholars have made an explicit case for the right to tax as indelibly lodged in the relationship between citizens and governments, an inquiry that is complicated by such international tax customs as the taxation of residents, non-resident citizens, and even former residents and citizens. *See, e.g.*, Nancy H. Kaufman, *Fairness and the Taxation of International Income*, 29 LAW & POL'Y INT'L BUS. 145, 148, 169 (1998) (arguing that the right to tax on the bases of source, residence, and perhaps citizenship constitutes "customary norms" if not quite customary international law); Michael S. Kirsch, *Taxing Citizens in a Global Economy*, 82 N.Y.U. L. REV. 443, 469 (2007) (highlighting the problem of reconciling standard tax practices with a theory of the state that links governments and people by reference to citizenship); Peggy B. Musgrave, *Sovereignty, Entitlement, and Cooperation in International Taxation*, 26 BROOK. J. INT'L L. 1335, 1336 (2001) (arguing that "international law" recognizes "national entitlements to tax"). However, the case has not been persuasively made for why taxation should be or is in fact any more inherent or essential to sovereignty than any other form of regulation such as currency control, bankruptcy, anti-trust, or securities laws. For a discussion, *see* Diane M. Ring, *What's at Stake in the Sovereignty Debate*, 49 VA. J. INT'L L. 155 (2008).

10. Though, of course, it is not atypical to raise revenue by means that might not be considered "taxation" per se. For instance, few would argue that a country that finances its government wholly via profits earned by state-owned enterprises is somehow not a sovereign state. In addition, a state may raise revenues through a state monopsony (such as a national agricultural board that serves as the sole intermediary between domestic producers and foreign markets), or via feudalism (under which the state claims sole ownership to land and mandates rent, as in Hobbes' form of sovereignty, discussed *infra* at note 12). To the extent these and other revenue-raising mechanisms (such as fees, licenses, etc.) might be seen as

As a result, taxation seems plausibly identifiable as an inherent right or entitlement attaching to sovereign status. Further, some argue that taxation is so essential to sovereignty that autonomy in designing the tax system deserves greater protection than autonomy in other regulatory areas.[11] The conflation of autonomy in designing the regulatory machinery of taxation with the political institution of sovereignty itself may not be universally supported by theory or historical fact,[12] but

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imposing taxation in the form of higher costs for consumers or lower profits for producers, the link between sovereignty and taxation may seem that much more indelible.

11. *See, e.g.*, Rajiv Biswas, *Introduction: Globalisation, Tax Competition and Economic Development*, *in* INTERNATIONAL TAX COMPETITION: GLOBALISATION AND FISCAL SOVEREIGNTY 1, 1–2 (Rajiv Biswas ed., 2002) (claiming that "fiscal sovereignty" was so important that its pursuit drove the American Revolution and Ghandi's Non-Cooperation Movement against the British). *But see* Musgrave, *supra* note 9, at 1349 (arguing that states are losing control over corporations and that this "will compel the transfer of national responsibility for the corporation income tax to an international authority"). The debate between those who fear that globalization prompts a loss of state control and those who see globalization as empowering the state is vigorously debated in the international relations literature but this literature is largely overlooked in tax scholarship. For a discussion, see GEORG SØRENSEN, THE TRANSFORMATION OF THE STATE: BEYOND THE MYTH OF RETREAT 107–12 (2004). To the extent that taxation for some reason mandates greater state autonomy, it diverges from the trend in other regulatory areas, "as nation-states seek to conform to global universals in areas as diverse as voting rights, immigration, women's rights, environmental policies, and citizenship." Bruce G. Carruthers & Terence C. Halliday, *Negotiating Globalization: Global Scripts and Intermediation in the Construction of Asian Insolvency Regimes*, 31 LAW & SOC. INQ. 521, 522 (2006).

12. For instance, it may be accurate to invoke Hobbes in support of the idea that the sovereign status of kings includes the right to raise money from his subjects, but this supports the idea that feudalism and the right to collect rent by the ruling class is essential to sovereignty as much as or more than it supports the idea that taxation is essential to sovereignty. By contrast, Jean Bodin, whose work on sovereignty predates Hobbes by almost a century, is never invoked to defend the link between taxation and sovereignty even though he explicitly claimed that "[t]he right of levying taxes and imposing dues, or of exempting persons from the payment of such, is also part of the power of making law and granting privileges." JEAN BODIN, SIX BOOKS ON THE COMMONWEALTH 47 (M.J. Tooley trans., Blackwell 1955) (1576) (for Bodin a principal mark of sovereignty). Bodin is less citable perhaps because he explicitly noted that "the levying of taxation" was *not* "inseparable from the essence of the commonwealth, for as President Le Maître has shown, there was none levied in France till the time of Louis IX." *Id.* at 48. Bodin realized that persons other than the king were levying taxes of various kinds, and abhorred this fact—he, perhaps more clearly than Hobbes, argued that if revenues were needed, the right to raise them should rest in the "sovereign authority" alone. *Id.* For a classic explanation of why arguments for the divine right of kings, owing to their sovereign status, to raise money from "their people" (however definable and enforceable) may not apply effortlessly to the connection between the right to tax

the principle is generally accepted in the literature: sovereign status seems to include a right to tax in some form, so that infringing on the right of taxation is an infringement on sovereignty itself.[13]

Defining what the right to tax entails is thus embedded in the concept of sovereignty, and is as susceptible as that term to differing—and evolving—interpretations.[14] In the traditional view, states were said to have "supreme . . . and exclusive rule" within their own territorial borders and over their own people, as they defined them.[15] Tax scholarship often appears to advance this view,[16] though international law scholarship describes concerns for exclusivity and uncompromised autonomy as "traditional, and thankfully outmoded."[17] The latter view focuses instead on the state as the locus of political authority in a territory, where decisions about economic autonomy will be made.[18] As such, sovereignty might be generally defined to

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and the concept of sovereignty as embodied in the nation-state, see Joseph A. Schumpeter, *The Crisis of the Tax State, in* INTERNATIONAL ECONOMIC PAPERS No. 4, 12 n.11 (Alan T. Peacock et al. eds., MacMillan & Co. 1954) (1918) (outlining the emergence of the modern state and noting that, while "[o]ccasionally we find something which could be compared to modern taxes," the concept did not fully emerge "until the end of the 15th century").

13. *See, e.g.*, Cockfield, *supra* note 2, at 167 (stating that nations are unlikely to adopt international tax laws unless they preserve tax sovereignty); Jinyan Li, *Tax Sovereignty and International Tax Reform: The Author's Response*, 52 CAN. TAX J. 141, 144 (2004) (arguing that "any tax reform that requires a high level of international coordination or cooperation must deal with the sovereignty hurdle," and suggesting that nations "give up" their tax sovereignty when they enter into treaties or respond to market forces). However, defining sovereign right and infringement is subject to broad and varied views. For a discussion, see RAMON J. JEFFERY, THE IMPACT OF STATE SOVEREIGNTY ON GLOBAL TRADE AND INTERNATIONAL TAXATION 43 (1999).

14. The literature on sovereignty is vast. The discussion here does not attempt to encompass the complexities and the enormous amount of thought and debate that have been invested in the concept, but only to provide a broad synthesis of the most important components needed to give structure and content to the term in the context of taxation.

15. JAN AART SCHOLTE, GLOBALIZATION: A CRITICAL INTRODUCTION 135, 135–37 (2000).

16. *See supra* note 9.

17. Joel P. Trachtman, *Welcome to Cosmopolis, World of Boundless Opportunity*, 39 CORNELL INT'L L.J. 477, 479 (2006).

18. States are thus viewed as global actors that negotiate globalization through both domestic and international political processes. *See* Carruthers & Halliday, *supra* note 11, at 523 ("the locus of a country in a global matrix of power affects the structure of interactions between the global and national, which in turn influences variations in the terms of globalization that are negotiated between global institutions and nation-states."); *see generally* Halliday & Carruthers, *supra* note 8 (showing that norms and laws are the product of national recursive cycles between

mean that "other entities have no political authority within the states' territory," but this definition does not assume or require economic or perhaps even legislative autonomy as a fundamental precept. Obviously, states can and routinely do choose to trade economic and legislative autonomy in exchange for greater economic, legislative or geopolitical strength.[19]

States may also make tradeoffs between autonomy and cooperation when it is difficult to authoritatively claim a realm of exclusive jurisdiction, such as over economic matters. For instance, tax experts recognize that it may be virtually impossible to say with certainty that a particular transaction or item of income is definitively related to one state and not another, especially with the digitization of finance and commerce.[20] States therefore must make some arbitrary decisions about their jurisdictional reach, and they often do so according to international consensus.[21] But since activities and people overlap territorial boundaries, more than one state may make what is readily recognized by other states as a legitimate claim to tax with respect to the same person or in a given territory.[22] For instance, few would dispute the legitimacy of simultaneous claims by two countries to impose a tax on a dividend paid by a company in one of the states to a shareholder from the other.[23]

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the law as written (in statutes, regulations and cases) and law as implemented (through actors such as legal professionals, officials, and private persons), global iterative cycles between international norm creation (through guidance, recommendations, national reports, etc.) and national implementation, and the interaction of these national and global cycles).

19. A quintessential example is the WTO, a multilateral agreement which states may enter provided they voluntarily cede certain legislative rights, such as the right to freely impose discriminatory taxes on imports or the right to freely subsidize exports, in exchange for the promise of greater economic rewards through cooperation. The same kinds of tradeoffs are routinely made in free trade agreements and tax treaties.

20. *See, e.g.*, Philipp Genschel, *Globalization and the Transformation of the Tax State*, 13 EUR. REV. 53, 60 (2005) (The traditional idea that "all taxable events have a clearly identifiable place in space" within one jurisdiction or another "has always been a fiction.").

21. *See, e.g.*, REUVEN S. AVI-YONAH, INTERNATIONAL TAX AS INTERNATIONAL LAW 27–28 (2007). It is perhaps a truism to suggest that states often make decisions about whether and how to tax a particular person or activity according to domestic political tradeoffs or exigent revenue needs rather than economic theory.

22. For a classic description, see Richard A. Musgrave & Peggy B. Musgrave, *Inter-nation Equity*, *in* MODERN FISCAL ISSUES 63, 64 (Richard M. Bird & John G. Head eds., 1972).

23. A number of justifications may be invoked, but in general terms the right to

Consistent with the general international law principles laid out above, a state's right to tax is generally accepted as not exclusive but conjunctive.[24] The best evidence of this recognition is that countries do not generally attempt to prevent other countries from taxing their people or within their territory, so long as the other country can claim some plausible connection to the item or person being taxed.[25] This suggests that countries have a strong respect for sovereign entitlements, including those to taxation, held by other countries.[26] This respect for tax sovereignty may also be articulated as a recognition of sovereign duty—i.e., states have a duty to respect the sovereign right of other states to tax, even to the extent of not interfering with extra-territorial claims based on currently-accepted jurisdictional connections.[27]

Commensurate with this strong respect for tax sovereignty,

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tax the dividend may be said to arise from each nations' right to control activities within its territory (the nation that provides the market in which the earnings giving rise to the dividend economically take place is justified in its taxation as the "source" or "host" country) and over its people (thus the nation that comprises and provides the social, political, and legal structure for its people is justified in collecting revenues from all of their income, from wherever derived, as the "residence" or "home" country). The claims of the source-based jurisdiction and the residence-based jurisdiction are equally recognized as valid, thus giving rise to cooperation when cross-border activity is valued above economic autonomy. For an argument that the legitimacy of source and residence-based tax jurisdiction is based in customary international law, see Avi-Yonah, *supra* note 2, at 484.

24. The principle may be embedded in the international law concepts of comity and reciprocity. *See, e.g.*, F. A. MANN, FURTHER STUDIES IN INTERNATIONAL LAW 4 (1990) (stating that "[s]ince every State enjoys the same degree of sovereignty, jurisdiction implies respect for the corresponding rights of other States.").

25. The idea that the right to tax has limits (i.e., that connections be plausible) is not universally embraced, however. *See, e.g.*, BRIAN J. ARNOLD, TAX DISCRIMINATION AGAINST ALIENS, NON-RESIDENTS, AND FOREIGN ACTIVITIES: CANADA, AUSTRALIA, NEW ZEALAND, THE UNITED KINGDOM, AND THE UNITED STATES 7 (1991) ("A country's legal authority to levy tax is effectively limited only by practical considerations of enforcement and collection. Rules of public international law or domestic constitutional law restrict a country's jurisdiction to tax only in narrow, relatively insignificant ways."); *see also* SOL PICCIOTTO, INTERNATIONAL BUSINESS TAXATION 307 (1992) ("From the point of view of formal sovereignty, there is no restriction on a state's right to tax, and it may be exercised without regard to its effects on other states.").

26. Most probably out of a sense of reciprocity—each wants its own actions to be equally respected.

27. This leaves open the possibility, however, that a particular state's extra-territorial reach may be seen as justifiable by one but not another, according to each state's interpretation of prevailing international norms. Reuven Avi-Yonah has argued that what is deemed appropriate changes over time through the universal acceptance of practices by key states, especially the United States. AVI-YONAH, *supra* note 21, at 34–37 (outlining key changes in approach to jurisdictional reach in the taxation of income earned by United States persons through foreign entities).

many countries are currently expanding their tax reach, further complicating the coordination of mutually legitimate claims.[28] The recognition that multiple jurisdictions have simultaneously legitimate claims evinces a basic respect for the commonly-held idea that sovereign states are accorded legally equal status in international society by virtue of being treated as sovereign by other states.[29] This respect could mean a lot of things, but it at least means that barring extreme circumstances, no state may send military troops into another's legislative body and force the legislators to adopt certain tax measures; the courts of one state cannot deem the tax laws of another to be unconstitutional or illegal; one state's legislators cannot legislatively override another's statute or judicial opinion, etc.[30]

More practically, overlapping tax sovereignty is so respected that states go to extraordinary lengths to relieve

28. An example is China's recent tax reforms, which are designed to increase its claim over the profits of multinational companies operating within its borders. In addition, the OECD's efforts to coordinate transfer pricing may be strained by the increasing assertiveness of states attempting to claim jurisdiction over the income of multinational companies operating within their territories.

29. J.D.B. MILLER, THE WORLD OF STATES: CONNECTED ESSAYS 16 (1981). This is the "juridical core" of constitutional independence that is described as the essence of sovereignty by some international scholars. *See, e.g.*, IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 4 (1990). This does not mean that states have equal power or resources, but only that they are equally sovereign.

30. However, nothing prevents states from contracting to cooperate in the design of their tax systems and in so doing give away some of their autonomy in decision making—globalization is negotiated. *See* Carruthers & Halliday, *supra* note 11. Quintessential examples include the GATT and the European Union, two forms of legal and political institution under which nations agree to forego or undertake certain taxing measures and give up some of their autonomy over tax policy by agreeing to be evaluated and bound by decisions made at the supranational level. To be sure, if a state's law is found to be in violation of its GATT undertakings, the WTO does not force the state to change the law, but only allows other states to retaliate. For example, when the WTO found that U.S. tax laws were inconsistent with its undertakings under the GATT, the United States was free to redesign its own laws to comply with its obligations or not, but, if not, it faced economic sanctions in the form of retaliatory tariffs by the opposing nations. For a discussion, see Daly, *supra* note 2, at 537–41. The right to impose sanctions is obviously of more use to some nations than to others. *See, e.g.*, Joel P. Trachtman, *The WTO Cathedral*, 43 STAN. J. INT'L L. 127, 128–129 (2007) (arguing that since WTO sanctions are of little use to less developed countries, developed countries may breach their obligations at little cost). But, to the extent it has any impact, the right to impose sanctions might be seen as introducing a limit on autonomy, rather than sovereignty. For example, a state is free to exit the GATT and revoke its WTO membership according to the terms of its participation agreement. *See, e.g.*, Uruguay Round Agreements Act, Pub. L. No. 103-465, §101(a), 125 Stat. 4883–4834 (1994) (providing a mechanism for withdrawal by the United States from the WTO).

double taxation.[31] They do so unilaterally, through domestic statutes,[32] bilaterally through tax treaties,[33] and multilaterally through consensus building on best practices in tax base allocation, such as through coordinated transfer pricing.[34] None of these efforts represents a loss or diminishment of any state's sovereign status in the sense that all of these activities are voluntarily entered into by states and each can terminate its efforts at will.[35] Each represents deliberate and negotiated tradeoffs states make between exercising complete economic autonomy and achieving other goals.[36] Some of these efforts, especially unilateral ones, may evidence a contract between particular states, voluntarily adhered to in "a cooperative venture for mutual advantage."[37] Thus if tax sovereignty means anything, perhaps it is the idea that governments have a non-

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31. Respect for sovereignty seems evident in the way states attempt to resolve double taxation even when it does not actually occur, for example, in the case of so-called "double non-taxation," or the simultaneous non-taxation by multiple jurisdictions. In such cases each country may refrain from exercising an otherwise appropriate jurisdiction to tax, either out of deference to the other (arguably respecting the other's sovereign entitlement) or to attract foreign investment (arguably respecting its own sovereign entitlement not to tax—see discussion *infra* pp. 110–111).

32. The principal mechanism is the foreign tax credit, initially introduced by the United States when it was deemed to be a "present of revenue to other countries," for which source-based taxation was preserved. *See* EDWIN R. A. SELIGMAN, DOUBLE TAXATION AND INTERNATIONAL FISCAL COOPERATION 169–74 (1928); *see also* ELISABETH A. OWENS, THE FOREIGN TAX CREDIT; A STUDY OF THE CREDIT FOR FOREIGN TAXES UNDER UNITED STATES INCOME TAX LAW 20 (1961) (stating that "[w]hile one or two countries had used the tax credit device prior to [the United States] for taxes paid to their colonies, the United States was the first country to apply the foreign tax credit on a world-wide basis as a means of relieving international double taxation of income"). Virtually no countries today exercise residence-based taxation without some means of relieving double taxation, whether by credit or exemption. *See, e.g.*, HUGH J. AULT & BRIAN J. ARNOLD, COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS 372–77 (2nd ed. 2004).

33. *See, e.g.*, Allison D. Christians, *Tax Treaties for Investment and Aid to Sub-Saharan Africa*, 71 BROOK. L. REV. 639, 650–51 (2005).

34. *See, e.g.*, OECD, TRANSFER PRICING GUIDELINES FOR MULTINATIONAL ENTERPRISES AND TAX ADMINISTRATIONS P-3 to -6 (2001).

35. *See, e.g.*, Robert Jackson, *Sovereignty in World Politics: A Glance at the Conceptual and Historical Landscape*, 47 POL. STUD. 431, 449–54 (1999) (arguing that sovereignty is not a resource to be held or carved up and given away—a nation either is sovereign, and therefore a member of the international society of states, or it is not sovereign, and therefore not such a member).

36. For example, achieving reciprocal restraint or assistance in tax administration from another country.

37. RAWLS, *supra* note 5, at 4, 126. For example, a country may enact a unilateral foreign tax credit in the hopes that other countries will follow suit. This may have been the impetus for the adoption of the credit in the United States, as discussed *supra* note 32.

exclusive right to decide through political means whether and how to tax whatever activity occurs within their territories and whomever can be considered to be their "people," and that they recognize a reciprocal right in all other states.

This principle could require fairly little in terms of positive action by states. Recognizing a reciprocal right might mean little more than refraining from initiating war in the event of double taxation (obviously an enormously remote possibility in any case). The principle is challenged, however, by the very real possibility that the same respect for sovereignty that protects the right of states to tax must equally protect the sovereign right *not* to tax.[38] When goods and capital move easily around the world, a state can use its tax and regulatory regimes to attract people wishing to avoid the exercise of tax sovereignty by other states.[39] Does respect for sovereignty imply that states can design their tax systems as they please, and that other states cannot compel adherence to any baseline of cooperation (for example, that states have no duty to assist each other in tax law enforcement), or, conversely, that they are not so free and can be so compelled (for example, that a duty to assist exists)? These kinds of questions demonstrate the basic tensions that are informing policy development within the OECD (as well as within and among individual nations).

The institutional language emanating from the OECD, especially in the context of their project to stop certain tax practices, suggests that the idea is developing that nations have a sovereign duty to comply with global community tax policy standards. The need for policy development seems particularly acute as the international effects of exercising the right to tax become more pronounced in the context of increasing economic interdependence among nations. In this environment, non-compliance with community standards by some nations has been identified as the main contributor to a global environment of tax evasion and a critical erosion of every nation's ability to

38. *See, e.g.*, Hugh J. Ault, *The Importance of International Cooperation in Forging Tax Policy*, 26 BROOK. J. INT'L L. 1693, 1695 (2001) (stating that a treaty "can limit taxing rights [voluntarily], but it can't force the country to impose a tax").

39. *See* OECD, HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE 14 (1998) [hereinafter 1998 REPORT] ("Globalisation has, however, also had the negative effects of opening up new ways by which companies and individuals can minimize and avoid taxes and in which countries can exploit these new opportunities by developing tax policies aimed primarily at diverting financial and other geographically mobile capital.").

implement their sovereign right to tax.[40] It is therefore perhaps not surprising that the OECD's work, especially in the area of harmful tax competition, appears to shift the focus on tax sovereignty toward identifying an affirmative duty in the tax system design as a necessary element of respect for sovereignty itself.[41]

It should be clear that the claim is not made herein that anyone at the OECD or elsewhere is explicitly promoting the idea of sovereign duty as the binding tie of a global social contract. Any such claim would be virtually impossible to prove since the motivation and ideology of OECD insiders, as well as the range and depth of their influence, defies measurement. The OECD is not a supranational body like the WTO but an unelected, non-governmental network.[42] OECD work is carried out by experts, with input from member country representatives and other non-government individuals according to internally determined parameters.[43] The main interaction of OECD

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40. *See, e.g.*, Council of the OECD, *Ministerial Communiqué*, OECD OBSERVER, June/July 1996, at I, III [hereinafter Council of the OECD]; 1998 REPORT, *supra* note 39, at 7 ("[G]lobalisation is creating new challenges in the field of tax policy. Tax schemes aimed at attracting financial and other geographically mobile activities can create harmful tax competition between States, carrying risks of distorting trade and investment and could lead to the erosion of national tax bases." (quoting Communiqué issued by heads of state of G7 countries at their 1996 Lyon Summit)); 1998 REPORT, *supra* note 39, at 13–14 ("tax policies in one economy are now more likely to have repercussions on other economies," while historically, "the interaction of domestic tax systems was relatively unimportant, given the limited mobility of capital."); OECD, THE OECD'S PROJECT ON HARMFUL TAX PRACTICES: THE 2001 PROGRESS REPORT 4 (2001) [hereinafter 2001 REPORT] (reiterating that in an open and competitive environment, one country's tax practices can undercut another's).

41. The inquiry, relatively unexamined in tax literature, has long been a topic of debate in other fields.

42. Since it materialized as part of the reconstruction effort in the post-war era, the OECD has served as a forum for consensus-building among the members rather than a body for creating laws with which its members are expected to comply. As such, it operates more as a transnational network than as a supranational organization such as the WTO. *See* ANNE-MARIE SLAUGHTER, A NEW WORLD ORDER 11–13, 145 (2004) (distinguishing a transnational network as a horizontal network of national officials that builds consensus among the members but which may be "decentralized and dispersed, incapable of exercising centralized coercive authority," from the more familiar supranational, or vertical network which is used by "states to delegate their sovereignty to an institution above them with real [coercive] power."). It is not necessarily clear that the OECD lacks the ability to exercise centralized coercive authority, and even though it does not issue "law" as such, many of the OECD's declarations in tax matters may be accepted by some as largely equivalent to binding law. *See* Allison Christians, *Hard Law, Soft Law, & International Taxation*, 25 WIS. INT'L L.J. 325, 325–29 (2007).

43. *See* Human Resources Management at the OECD, http://www.oecd.org (follow "Human Resources" hyperlink) (last visited Sept. 12, 2008).

committees with the general public is through anonymously authored institutional reports which are the most accessible—perhaps the only realistically accessible—public accounting of the work of the committee members.[44] These reports are the product of discussions, negotiations and personal relationships about which the general public can claim no special knowledge or insight.[45]

Even so, the rhetoric emanating from and surrounding this institution has an observable influence on those who are concerned with tax policy, including government officials, academics, practitioners and other interested parties.[46] The explanatory language chosen by the OECD to describe its work thus provides a logical starting point for identifying evolving theories about sovereignty, taxation and social contract, and how these theories may impact national tax policy and lawmaking.[47]

The following part therefore focuses on the language of the OECD, presented to the public through its official reports, as an appropriate way to learn about its chosen principles, its institutional process and the reasons its committee members believe their ideas should be embraced by independent nations.[48]

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44. The general public knows what it knows about the OECD by reading what is posted on the official website or otherwise made generally available, which is mostly in written form. *See* Frequently Asked Questions, How does the OECD communicate with the public?, http://www.oecd.org/document/11/0,3343, en_2649_33487_2482699_1_1_1_1,00.html (last visited Sept. 12, 2008). Of course, personal interaction with some OECD representatives is possible. For example, various OECD tax experts are present at tax conferences and other meetings, sometimes presenting information in their capacity as OECD representatives, sometimes in their individual or other professional capacities. In addition, the OECD consults with certain business organizations, such as the Business and Industry Advisory Committee to the OECD (BIAC) and the Trade Union Advisory Committee to the OECD (TUAC). For most non-experts, the best access to the OECD is through its Website, www.oecd.com.

45. It should thus also be clear that while inquiring into the philosophical underpinnings of the OECD's tax policy work is inherently difficult and uncertain, the exercise seems critical for meaningful debate about their work.

46. *See* sources cited *supra* note 2.

47. This is not to suggest that no theory of sovereign duty has ever existed in international taxation, but to explore how existing theories of sovereign duty may be changing in light of the special problems states are currently encountering in designing their tax systems. *See* discussion *infra* Part III.

48. Rhetorical analysis, like most empirical approaches, admits of inherent limits. For instance, ideas or principles may not necessarily be discerned simply by observing the language people use, or for that matter, the outcomes of norm or law-making processes. Still, I presume that written statements reflect at least some of the ideas that took part in shaping them. An issue of concern for this approach is, of

The principal objects of this analysis are the five official reports issued to date by the OECD to explain its ongoing efforts to curb harmful tax competition.[49] This project is the focus of the present analysis because the theories it evokes about sovereignty, taxation and social contract are, while implicit, nevertheless very palpable and public.[50] The words chosen in these reports give us clues about what these rule makers, and those who reflect on the rules, think is important and appropriate, or at least what they think is important and appropriate to say about their efforts.[51]

III. IDENTIFYING SOVEREIGN DUTY: THE ROLE OF THE OECD IN SHAPING GLOBAL TAX POLICY

While discussion of tax sovereignty as autonomy is usually fairly explicit even though the underlying assumptions are not so, the inverse is true in the case of sovereign duty. Few expressly articulate any concept of sovereign duty in the design

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course, whose ideas are at work. *See, e.g.*, BOAVENTURA DE SOUSA SANTOS, TOWARD A NEW LEGAL COMMON SENSE: LAW, GLOBALIZATION, AND EMANCIPATION (2002) (arguing that values emanating from international organizations represent "globalized localisms" of key players and do not necessarily reflect widely-held views). For an argument that rhetorical analysis is a critical component of examining substantive claims, see DEIRDRE N. MCCLOSKEY, THE RHETORIC OF ECONOMICS (2d ed. 1998).

49. 1998 REPORT, *supra* note 39; OECD, TOWARDS GLOBAL TAX CO-OPERATION: REPORT TO THE 2000 MINISTERIAL COUNCIL MEETING AND RECOMMENDATIONS BY THE COMMITTEE ON FISCAL AFFAIRS (2000) [hereinafter 2000 REPORT]; 2001 REPORT, *supra* note 40; OECD, THE OECD'S PROJECT ON HARMFUL TAX PRACTICES: THE 2004 PROGRESS REPORT (Mar., 2004) [hereinafter 2004 REPORT]; OECD, THE OECD'S PROJECT ON HARMFUL TAX PRACTICES: 2006 UPDATE ON PROGRESS IN MEMBER COUNTRIES (2006) [hereinafter 2006 REPORT]. In addition to these five reports, the OECD has issued several other documents, including press releases, presentations, speeches, related guidance, and proceedings from meetings held in 2004 and 2006. All of these items are available on the OECD Website at www.oecd.com. Many of these documents contain language that is consistent with and in many cases virtually identical to that of the official reports. However, I have focused here on five reports that represent the formally documented outcome of OECD deliberations, and appear to be the most definitively representative of the OECD's position as an institution regarding the purposes of its harmful tax practices work as it has evolved over the life of the project.

50. Other projects of the OECD tax policy committees, such as transfer pricing and treaty negotiation evoke many of the same issues, but the harmful tax practices project has most clearly raised the specter of sovereignty within tax policy debate.

51. It is worth noting that ideas about what is and is not appropriate change over time and particular individuals, especially from key countries like the United States, may heavily influence evolving policy directions. *See* AVI-YONAH, *supra* note 21.

of tax systems, yet underlying assumptions about duty are often implicit in the language used to describe international tax norms and practices.[52] This seems especially true in the context of international collaboration and cooperation over tax matters.[53] For example, the OECD never explicitly discusses sovereign duty arising from membership in a global community to justify its recommended tax competition guidelines to national officials. Yet it implicitly evokes these ideas, especially when directing its attention to non-member states, who may have had little or nothing to say in forming the consensus.[54]

Since the OECD cannot expressly purport to determine policies and dictate their implementation by member countries, let alone non-member countries,[55] its official rhetoric may simply reflect what insiders think will either encourage compliance or provide a palatable justification of the imposition of consequences in the event of non-compliance.[56] As a result, official OECD rhetoric is susceptible to interpretation as little more than a means to mask or legitimize what is essentially an

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52. Again, this discussion refers to the relationship among states. Duty is occasionally explicitly invoked in the context of relationships between states and what they determine to be their peoples. *See* OECD, THIRD MEETING OF THE OECD FORUM ON TAX ADMINISTRATION: FINAL SEOUL DECLARATION 3 (Sept. 15, 2006) (stating that once national tax laws have been enacted, they need to be enforced because "[i]t is our duty as heads of our respective countries' revenue bodies to ensure compliance with our national tax laws by all taxpayers . . . through effective enforcement and by taking preventative measures that deter noncompliance."); Graetz, *supra* note 8, at 280–81 (arguing that national authorities have obligations to pursue national goals as evidenced by democratic processes).

53. *See* Carruthers & Halliday, *supra* note 11, at 534 ("[G]lobal actors sustain their expansive reach by discursive claims to universality.").

54. *See generally* Sol Picciotto, *International Law: The Legitimation of Power in World Affairs*, *in* THE CRITICAL LAWYER'S HANDBOOK 13–29 (Paddy Ireland & Per Laleng eds., 1997). Indeed, the OECD appears to recognize this need, in particular in the context of "associating non-member countries with its analytical and policy discussions on harmful tax competition." 1998 REPORT, *supra* note 39, at 10.

55. *See, e.g.*, 2000 REPORT, *supra* note 49, at 5 (stating that the OECD works through mechanisms such as persuasion and peer pressure to convince countries to adopt particular positions). It is of course arguable that by using its collective economic and political resources, the OECD does in fact decide and dictate, and its lack of power to make binding law is only nominal or formal rather than actual. *See* Christians, *supra* note 42, at 326–33.

56. Rather than searching for the tax practices that would be the best for everyone in the world and not just for its member states, the OECD is perceived by some as an institution dedicated solely to achieving advantages for its member countries, even at the expense of non-member states. *See, e.g.*, Vaughn E. James, *Twenty-First Century Pirates of the Caribbean: How the Organization for Economic Cooperation and Development Robbed Fourteen CARICOM Countries of Their Tax and Economic Policy Sovereignty*, 34 U. MIAMI INTER-AM. L. REV. 1 (2002).

illegitimate use of political or economic force to achieve the aims of the powerful against those of the weak.[57]

But this factor itself makes a strong case for searching for a theory of duty in the rhetoric emanating from this institution. To the extent the OECD's project derives from an authentic analysis of sovereignty and duty, national legislators might choose to adopt OECD recommendations to the extent they agree with these ideas.[58] On the other hand, to the extent the OECD is perceived as using ideology merely to achieve self-interested economic goals, its attempt to legitimate its use of economic and political pressure opens up its reasoning to intense public scrutiny.[59] This suggests at the very least that the individuals serving on the OECD's Committee on Fiscal Affairs must perceive a duty to justify their recommendations when they might be seen as attempting to interfere with the desires or goals of states not represented on the Committee (especially non-OECD member states) in exercising (or not exercising) taxation. At a minimum, the justification process provides a starting point for further analysis of sovereign duty.

A. BACKGROUND—HARMFUL TAX PRACTICES INITIATIVE

The OECD's work on harmful tax practices began in 1996 when an OECD Ministerial Communiqué called upon the organization to curb the rise of tax havens, which were seen as

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57. *See* Halliday & Carruthers, *supra* note 8, at 1140 (discussing a "narrative that, in the case of champions of 'globalization,' may serve to disguise or mask power," so that power is expressed not through physical control over a territory but "through control of consciousness.") (citing Susan S. Silbey, *1996 Presidential Address: "Let Them Eat Cake": Globalization, Postmodern Colonialism, and the Possibilities of Justice*, 31 LAW & SOC'Y REV. 207, 207–34 (1997)).

58. Thus national lawmakers might recognize and embrace the duty without much need for convincing from the outside community. As in the case of unilateral adoption of the foreign tax credit by the United States, the duty would be acknowledged and acted upon, even if it eroded the revenue-raising capability of the initial adopter. As a further analogy, the initial adopter would then set about trying to inculcate the duty in other states. U.S. tax officials arguably pursued double tax treaties in order to accomplish such an inculcation. *See* Michael J. Graetz & Michael M. O'Hear, *The "Original Intent" of U.S. International Taxation*, 46 DUKE L.J. 1020, 1043–45 (1997); H. David Rosenbloom & Stanley Langbein, *United States Tax Treaty Policy: An Overview*, 19 COLUM. J. TRANSNAT'L L. 359, 361 (1981).

59. This is to suggest that from a procedural justice point of view, if the theory is clearly wrong (*i.e.*, duty does not exist), then the outcome (*e.g.*, duty will be enforced through economic coercion), while not necessarily unjust, ought to be in question. Similarly, taking a more consequential view, if the outcome may be perceived as unjust, then the theory that allowed it is likewise subject to further inquiry.

eroding the revenue-raising ability of capital-exporting countries.[60] Two years later, the OECD published a report that "developed criteria to identify harmful tax competition" and recommended counteractive solutions.[61] This report was followed by a series of subsequent progress and related reports that named regimes deemed harmful by the OECD, called for defensive measures against and sanctions for uncooperative member and non-member states,[62] and later reported on compliance.[63]

Since the OECD's work does not represent a traditional, "hard" type of international tax law-making (in the sense of customary international law or treaty), the reasons it gives for countries—especially non-members—to abide by its recommendations are of interest.[64] Because of the economic

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60. *See* Council of the OECD, *supra* note 40, at IV (asking the OECD to "analyse and develop measures to counter the distorting effects of harmful tax competition on investment and financing decisions, and the consequences for national tax bases . . . ."). At a meeting in September of that year, the Heads of State of the G-7 countries stated that "[t]ax schemes aimed at attracting financial and other geographically mobile activities can create harmful tax competition between States, carrying risks of distorting trade and investment and could lead to the erosion of national tax bases," and they "strongly urge[d] the OECD to vigorously pursue its work in this field." Statement of G7 Finance Ministers and Central Bank Governors (Sept. 20, 1997), http://www.g8.utoronto.ca/finance/fm970920.htm. *See Lyon Summit Communiqué: Making a Success of Globalization for the Benefit of All*, 7 U.S. DEP'T OF STATE DISPATCH SUPPLEMENT 1, 5 (June 1996).

61. OECD, More Information on the Harmful Tax Practices Work, http://www.oecd.org/document/49/0,2340,en_2649_33745_33995569_1_1_1_1,00.html (last visited Sept. 12, 2008); *see also* 1998 REPORT, *supra* note 39, at 4.

62. The 2000 Report explained its review process, named states in violation of its harmful tax practices criteria, explained the commitments necessary to avoid being named as uncooperative, and set out "defensive measures" member states were to take with respect to uncooperative states, including imposing penalties and other economic sanctions, cutting off "non-essential economic assistance," and other non-tax measures. 2000 REPORT, *supra* note 49, at 26. The 2001 Report reiterates that member states may use "defensive measures" against states with tax regimes deemed to be harmful. 2001 REPORT, *supra* note 40, at 13. Some practitioners suggest that the real threat presented by the OECD was "unplugging the offshore tax centers from the global financial grid." Patrick Tracey, *Harmful Tax Competition Furor Raises Specter of Global Tax Forum*, 19 DAILY TAX REP. G-4 (2001).

63. *See* 2004 REPORT, *supra* note 49, at 7–9 (discussing regimes that had been labeled as harmful but that had been abolished or were otherwise no longer deemed to be so); *accord* 2006 REPORT, *supra* note 49, at 5–6.

64. For a discussion of why I do not believe the OECD's initiatives constitute customary law, see Christians, *supra* note 42 (distinguishing "hard" tax law from other forms of law and rule promulgation). *But see* Avi-Yonah, *supra* note 2, at 484. (arguing that the legitimacy of source- and residence-based tax jurisdiction is based in customary international law).

power of the thirty member countries of this institution, the simple answer may be that the recommendations are not voluntary at all but really demands backed by significant coercive capabilities.[65] These coercive capabilities bear close scrutiny because their invocation may signal something about sovereignty and social contract as conceived by those working through the OECD to achieve their goals.

The OECD proceeded carefully in this regard, laying the groundwork for economic sanction yet scrupulously avoiding official authorization. For example, a report issued in 2000 first sets out a list of "defensive measures" member states "may" take with respect to uncooperative states.[66] The report "invites" governments "to take into account that a jurisdiction is listed as an Uncooperative Tax Haven in determining whether to direct non-essential economic assistance to the jurisdiction."[67] It "reminds" governments that they should sever links with tax havens that contribute to harmful tax competition. It states that governments "should consider" using their ties with tax havens to reduce harmful tax competition (but does not suggest how to use these ties).[68] The 2001 report reiterates that "the adoption of defensive measures is at the discretion of individual countries" and states that the OECD "strongly prefers an approach that promotes change through dialogue and

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65. Failure to comply with OECD wishes was to result in real consequences, including the possibility of economic sanctions, as the Reports make clear. The degree to which consequences for noncompliance are essential for a rule or norm to constitute a law is a subject of debate. *See, e.g.*, Richard Bilder, *Beyond Compliance: Helping Nations Cooperate*, *in* COMMITMENT AND COMPLIANCE: THE ROLE OF NON-BINDING NORMS IN THE INTERNATIONAL LEGAL SYSTEM 65 (Shelton ed., 2000). I focus here not on whether economic coercion could make the statements of a non-legal institution "law" in some sense, but rather on whether such coercion forecloses the possibility that the institution is developing ideas about duty.

66. 2000 REPORT, *supra* note 49, at 24. Uncooperative states are those that "choose not to eliminate their harmful tax practices." *Id.* at 7. The OECD was careful to preserve state autonomy in enforcement, stating that "each country may choose to enforce the defensive measures in a manner that is proportionate and prioritised according to the degree of harm that a particular jurisdiction has the potential to inflict . . . ." *Id.* at 24.

67. *Id.* at 26.

68. *Id.* Perhaps diplomatic pressure was one intended mechanism, but nothing is said here to rule out more forceful means. It is difficult to imagine that military intervention would be appropriate, but hinting at economic sanctions might be seen to violate principles of nonintervention so a retreat to general principles of international law does not help much in this analysis. The issue is surely worthy of further exploration, but not necessary to the analysis of whether duty exists—we may find that a duty exists without determining what to do about it in the case of breach. See discussion in Part III, *supra*.

consensus" over coordinated defensive measures.[69]

Nuanced and careful though these statements may have been, critics of the OECD's efforts saw the reports as clearly endorsing economic coercion[70] rather than encouraging voluntary association as the reports suggested.[71] Commentators identified the threat presented by the OECD as real and unprecedented, with the potential to unplug offending countries "from the global financial grid."[72] What the OECD calls "encouraging" and "assisting" is interpreted by some as an unjustified use of force purely for self-interested ends.[73] If this is true, the OECD activity itself would be susceptible to a charge of violation of what many would recognize as a major tenet of sovereignty, *i.e.*, the right states have against intervention by other states, or, stated in terms of duty, the obligation states have not to intervene in the affairs of other states.[74]

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69. 2001 REPORT, *supra* note 40, at 13.

70. *See, e.g.*, Bishnodat Persaud, *The OECD Harmful Tax Competition Policy: A Major Issue for Small States, in* INTERNATIONAL TAX COMPETITION: GLOBALISATION AND FISCAL SOVEREIGNTY, *supra* note 11, at 17, 19 ("[d]efensive measures . . . are a polite usage for sanctions").

71. 2000 REPORT, *supra* note 49, at 22 (committing to "encourage non-member economies to associate themselves with the 1998 Report and to agree to its principles" as well as "encourage and assist" these countries to remove regimes the OECD determines are harmful or potentially harmful).

72. *See* Tracey, *supra* note 62; *see also* Richard Hay, *OECD Report on 'Level Playing Field' Imminent*, 9 MANAGING PARTNER 1, 1 (2006) (stating that the OECD's project threatens to "shut non-cooperating international financial centers out of the world's banking and securities markets" in violation of "[a] longstanding principle of international law [that] limits taxing rights to those which a country can enforce without the need for assistance from others.").

73. *See, e.g.*, James, *supra* note 56, at 28; Lawrence Speer, *Conservative Think Tanks Attack OECD on Offshore Tax Scrutiny During Forum*, 219 DAILY TAX REP. G-3 (2005) (reporting description of the anti-tax havens campaign as "hypocritical," "a thinly disguised move by industrialized countries toward forced harmonization of tax policies at the global level," and an attempt to create "a new tax cartel"); Daniel J. Mitchell, *An OECD Proposal to Eliminate Tax Competition Would Mean Higher Taxes and Less Privacy*, 1395 BACKGROUNDER 1, 18 (Sept. 18, 2000) http://www.heritage.org/Research/Taxes/upload/10525_1.pdf (2000) (OECD project "an attack on sovereignty").

74. The right of nonintervention is perhaps the most straightforward and familiar principle to be extracted from the concept of sovereignty, but that is not to say that it is without nuance or complexity. Scholars debate, for example, what level of violation of human life or dignity should be tolerated before one state should intervene militarily to restore order or save lives. For a discussion of views ranging from Grotius to Rawls, see NUSSBAUM, *supra* note 5, at 256–257 (noting that even in cases of human rights violation, some of which have been extreme, forcible intervention and economic sanction have been used "in a very small number of cases."). Some of the resistance to the OECD's work thus arises from its perception

On the other hand, use of encouragement *qua* coercion, to the extent the charge is accurately applied to the OECD's efforts, might not violate the principle of nonintervention if sovereignty has already been breached and the force is appropriately applied to prevent further breach.[75] In other words, to the extent the OECD's actions are unjustifiably coercive, anyone who thinks that sovereignty as an institution is under threat and ought to be preserved would be interested in preventing this unwarranted violation of the right of non-intervention.[76]

As the OECD reiterates in virtually every report it issues, its expressed commitment to sovereignty, and indeed tax sovereignty (however undefined), is of foremost importance and underlies every development in its harmful tax practices initiative.[77] It therefore seems plausible to suggest that the OECD's language was chosen carefully to signal that its proposed measures are meant to address a breach of sovereign duty and not to themselves constitute such a breach. This does not necessarily mean that their actions do not breach the non-intervention or any other international norm or custom; it only suggests that given the possible charges of such a breach, the OECD's justifications of its actions uncover an implicit theory of duty.

B. DEVELOPING IDEAS OF DUTY

Throughout the OECD's harmful tax practices work, the authors seem aware of the need to justify their actions by framing them as being in direct response to some wrongdoing. Defining just what that wrong is—and why it is wrong to do it—forms a major part of the project. Themes of countering "distortion" and promoting "fair competition," consistent with the initial charge of preserving revenue raising capability in

as unprecedented or extreme in the given context. *See, e.g.*, James, *supra* note 56, at 28.

75. There are few instances in which such intervention is justified, so it is perhaps not surprising that the United States demurred from the project to focus on less invasive measures (though the retreat is often ascribed to the differing political perspective of the incoming administration), and the measures ultimately taken were less drastic than those initially suggested. See discussion *infra*.

76. *See, e.g.*, Li, *supra* note 13, at 6 ("External forces may make a country give up its sovereignty. One example is the OECD-led harmful tax competition campaign."); Speer, *supra* note 73; Mitchell, *supra* note 73.

77. *See* 2000 REPORT, *supra* note 49, at 5; 2001 REPORT, *supra* note 40, at 4; 2004 REPORT, *supra* note 49, at 4; 2006 REPORT, *supra* note 49, at 3.

capital exporting countries, permeate the language.[78] But the OECD has significantly revised its stated goals over the life of this project, and the nature of these revisions suggests that the issue of sovereignty has become fundamentally important for framing and implementing the organization's goals.

In its first report, the OECD's stated goals were to strengthen international tax policies and reduce "the distortionary influence of taxation" on location decisions involving financial and service activities.[79] Two years later, in its 2000 report, the emphasis shifted towards supporting "effective fiscal sovereignty" by addressing issues that "unfairly" erode tax bases and distort location decisions.[80] By 2004, the project had coalesced around the goal of promoting a "level playing field," upon which "to achieve high standards of transparency and information exchange in a way that is fair, equitable, and permits fair competition between all countries."[81]

There is arguably a theory of sovereign duty in tax system design embedded within these goals, but it seems important to understand why the goals might have been framed this way before advancing such a theory. The differences between protecting revenue raising capabilities, addressing distortion and promoting fairness may not be obvious. But the change in language is purposeful and significant. Over the course of several years of discussion, of monitoring and evaluating practices, and of issuing reports, the OECD edited and condensed a relatively broad swath of potential international obligations down to a relatively simple statement regarding what could be interpreted as its current standard of sovereign duty in tax system design.

I outline here a number of the harms claimed by the OECD and some possible interpretations of these harms that could be framed as a search for sovereign duty. Among the many possible risks of doing so is the risk that some or all of these

78. See Council of the OECD, *supra* note 40, and see discussion *supra*, text at notes 60–61.

79. 1998 REPORT, *supra* note 39, at 9. In addition, the OECD sought "to safeguard and promote an open, multilateral trading system and to encourage adjustments to that system to take into account the changing nature of international trade, including the interface between trade, investment and taxation." *Id.*

80. 2000 REPORT, *supra* note 49, at 5 ("The [OECD] project . . . support[s] the effective fiscal sovereignty of countries over the design of their tax systems.").

81. OECD, A PROCESS FOR ACHIEVING A GLOBAL LEVEL PLAYING FIELD 2 (June 4, 2004); *accord* 2004 REPORT, *supra* note 49, at 4.

statements in which I identify an implicit sense of duty are less indicative of duty than of some other phenomenon.[82] And of course I am relying here on explicit, official rhetoric promulgated by the OECD. Still, starting with the OECD's own language and observing how it has changed and narrowed over time provides a framework for further analysis of what the OECD suggests national lawmakers might be required to consider in designing and assessing their tax systems.[83]

1. *Harmful Practices and Duty*

For example, in the 1998 report, the OECD lists over a dozen instances of what it calls harmful behaviors, for which it arguably implies some sort of sovereign duty exists to refrain from such behavior.[84] It implies this sovereign duty in attempting to define some key concepts that will later be pivotal to implementing actions against countries that are deemed to be non-compliant with OECD wishes.

In defining tax havens, the OECD suggests that these countries appeal to investors as "money boxes" for holding passive investments, for booking paper profits, and for shielding affairs from tax authorities of other countries. As such, the OECD argues, tax havens "potentially cause harm to the tax systems of other countries as they facilitate both corporate and individual income tax avoidance and evasion."[85] This language implies that states should not facilitate tax avoidance and evasion by taxpayers from other countries, even though no explanation is offered regarding whether or why causing harm

82. The risk of omission is present as well; I cannot claim to have uncovered every possible source of inference regarding sovereign duty in the OECD's harmful tax practices work.

83. One may well inquire why the OECD's statements about sovereignty should guide the discussion since, to the extent their rhetoric is chosen to support the self-interested goals of an exclusive group of countries, the resulting principles may not necessarily be expected to be inclusive of other perspectives. As others have pointed out, the very exclusivity of the OECD may indelibly mar its claims to legitimacy in promoting universal principles. *See, e.g.*, Cockfield, *supra* note 2, 183–86 (arguing that the OECD's membership and participation mechanisms should be more inclusive in order to legitimize its work in creating international tax norms). However much organizations such as the United Nations may be more inclusive in membership and participation and therefore might seem to be the more logical choice for pursuing and promoting universal principles, the OECD's prominence in tax norm creation and diffusion provides the primary rationale for closely examining the principles advanced by this organization as a starting point for analysis.

84. 1998 Report, *supra*, note 39, at 25–34.

85. *Id.* at 22.

to other countries should be avoided.[86] The potential for harm is presented as if the action is self-evidently egregious and therefore should be understood as a violation of sovereignty.

Similarly, in defining tax preference regimes, the OECD notes that countries use these to provide a favorable location for holding passive investments or booking paper profits, perhaps to route capital flow across borders.[87] Identifying a number of particular practices, the OECD argues that "there are good reasons for the international community to be concerned" because these practices "will have an adverse impact only on foreign tax bases," will allow host countries to "bear little or none of the financial burden of its own preferential tax legislation," will allow taxpayers to benefit from host country infrastructure without bearing its cost, and will have "harmful spillover effects" on other countries while protecting the domestic market from the competition.[88]

In stating these various harms, the OECD reports suggest that sovereign states might have a duty to refrain from adversely impacting foreign tax bases, from creating externalities that allow host countries to bear little of the cost of their preferential tax regimes, or from allowing people to benefit from public goods without contributing to them. Certainly, the

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86. The same duty seems to be invoked in the definition of rules that create or contribute to an "artificial . . . tax base," such as unconditional foreign tax credit rules "that go beyond the ordinary scope...to avoid double taxation," rules that allow deductions on top of exclusions, rules that contradict or fail to adhere to the OECD 1995 transfer pricing guidelines, the use of advance rulings to override statutory rules, the use of purely territorial taxation (*i.e.*, failure to tax foreign income earned by domestic persons), rules that allow taxpayers to negotiate rates or base, bank secrecy rules, and the conclusion of too many treaties. *Id.* at 30–33. The OECD finds these practices to be especially problematic when they are non-transparent, since non-transparency "can...distort the competitive position of countries." *Id.* at 32. The OECD suggests that advertising one's national regulatory system as tax friendly is not a prerequisite to being found to have harmful tax practices, but it "may provide a useful indication of whether a regime is seen and used primarily as a means of engaging in international tax avoidance and evasion." *Id.* at 34. Along the same lines, the 1998 Report states that "[g]overnments cannot stand back while their tax bases are eroded through the actions of countries which offer taxpayers ways to exploit tax havens and preferential regimes to reduce the tax that would otherwise be payable to them," *id.* at 37, instead "governments must take measures...to protect their tax bases and avoid the world-wide reduction in welfare caused by tax-induced distortions in capital and financial flows." *Id.* at 18.

87. 1998 REPORT, *supra* note 39, at 25.

88. *Id.* at 26–28. The 2001 Report retreats from this position by stating that there is no prohibition against failure to impose a tax. 2001 REPORT, *supra* note 40, at 9–10.

analysis of the good reasons for concern over adverse impacts are not directly linked to a breach of sovereignty, and none of these duties are explicitly stated or discussed in the OECD reports. Even so, the intent seems clearly to make some implicit connection.

Similarly, in defining transparency and effective information exchange as two pillars of sound tax policy, the OECD notes that countries with tax systems that lack these attributes "will make it harder for the home country to take defensive measures,"[89] which "may result in inequality of treatment of taxpayers in similar circumstances,"[90] and therefore create non-neutrality in the international tax system.[91] The chosen language again seems to imply that sovereign nations may have a duty not to frustrate other countries' audit procedures, but here there is also a sense that nations may have a sovereign duty to pursue equity and international neutrality in their tax policy. Identifying such a duty could require significant policy change in many countries, both within and beyond the OECD membership. But if any of these duties exist, defining the terms will be difficult, since, for example, economists and tax experts have long agreed that there are several competing and mutually exclusive neutrality and equity norms.[92]

2. *Unfair Competition and Duty*

As in the case of its identification of specific harms associated with certain tax practices, the OECD's attempt to define standards for appropriate inter-state tax competition evokes a vision of sovereignty that poses important conceptual challenges to conventional views. The 2000 report specifically discusses how various tax practices are used by countries to pursue an "unwarranted" competitive advantage.[93] OECD and non-OECD countries are seen as being "exposed to significant

89. 1998 REPORT, *supra* note 39, at 27.
90. *Id.* at 28.
91. *Id.* at 30.
92. *See, e.g.*, JAMES R. HINES JR., INTERNATIONAL TAXATION AND MULTINATIONAL ACTIVITY (2001); Musgrave & Musgrave, *supra* note 22; Keith Engel, *Tax Neutrality to the Left, International Competitiveness to the Right, Stuck in the Middle with Subpart F*, 79 TEX. L. REV. 1525 (2001); Joel Slemrod, Carl Hansen & Roger Procter, *The Seesaw Principle in International Tax Policy*, 65 J. PUB. ECON. 163 (1997).
93. 2000 REPORT, *supra* note 49, at 22.

revenue losses as a result of harmful tax competition," which "can be a particularly serious threat to the economies of developing countries."[94] Harmful tax practices are thus defined as "major distortions" that "will cause a shift of the targeted activities to economies outside the OECD area, giving them an unwarranted competitive advantage and limiting the effectiveness of [the OECD's whole cooperative] exercise."[95] As in the discussion of the harms of certain tax practices, the discussion of competition suggests that the OECD identifies a sovereign duty to refrain from pursuing an "unwarranted" competitive advantage, but does not explain why such a duty might exist, nor what principles guide the analysis.

The 2001 report more explicitly suggests that sovereign status might imply that states are obligated to refrain from impeding a country's autonomy in the design of its tax system. As the report states, "some tax and related practices are anti-competitive and can undercut the gains that tax competition generates. This can occur when governments introduce practices designed to encourage noncompliance with the tax laws of other countries."[96] These practices "undermine the ability of each country to decide for itself the allocation of tax burden among mobile and less mobile tax bases, such as labor, property and consumption."[97] This report appears to signal a subtle shift in emphasis: rather than focusing on the need to protect the tax base in other countries, it frames harmful tax competition as anti-competitive and obstructive to the ability of other countries to exercise autonomy in choosing tax policy.

The report implies that anti-competitive behavior may violate a country's sovereignty, but it stops short of explicitly claiming that there is a sovereign duty not to impede tax autonomy. By choosing language that describes some countries' practices as impediments to other countries, the OECD implies that some international obligation not to create such impediments has been breached. But the OECD does not set forth the case for recognizing such a duty, nor does it offer guiding principles. As in earlier reports, the egregious behavior or result implies its own curtailment. Rhetorical shifts in subsequent OECD reports may reflect the theoretical tensions

94. *Id.*
95. *Id.*
96. 2001 REPORT, *supra* note 40, at 4.
97. *Id.*

raised but essentially unresolved in these discussions.

For example, the 2004 progress report shifts away from delineating harms and focuses instead on articulating standards for a "level playing field among all countries and jurisdictions."[98] Stating that adoption by all countries of these standards is critical, the OECD suggests that individual countries should encourage other countries to adopt the standards, using methods that are "consistent with fairness, equity and proportionality."[99] For example, the OECD suggests countries "could consider how they could use other organizations to which they belong, fora in which they participate, and communication with their business communities to encourage the adoption of these practices."[100] The recommendation implies that a sovereign duty exists not only to adhere to certain standards, but also to disseminate these standards via international networks. However, the duty and its underlying principles are again to be inferred by the reader—the theoretical tension between autonomy and sovereignty remains unresolved.

The examples I have outlined here suggest a number of different themes worth exploring in the OECD's work. At minimum it seems significant that in the OECD's many documents there is little use of the standard measurements by which tax systems are typically assessed—namely, efficiency, equity and simplicity within a nation-based system.[101] When equity and efficiency are discussed in OECD reports, they are globally conceived.[102] But the development of ideas over the

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98. 2004 REPORT, *supra* note 49, at 4.

99. OECD, *supra* note 81, at 5.

100. *Id.*

101. See discussion *supra*, note 8.

102. *See, e.g.*, 1998 REPORT, *supra* note 39, at 18, 28 (governments must act to avoid worldwide reduction in welfare caused by harmful tax practices; certain state practices "may result in inequality of treatment of taxpayers in similar circumstances" that cannot be alleviated without global cooperation); 2000 REPORT, *supra* note 49, at 5 (initiative "is about ensuring that the burden of taxation is fairly shared" among people and among countries); 2006 REPORT, *supra* note 49, at 2 (arguing that one of the challenges governments face is "ensuring that their tax systems remain competitive and do not act as a barrier to increased productivity," and that despite a "wave of tax reform that has swept through" countries and reduced tax burdens toward this goal, "the global economy will not reap the full benefits of this more competitive environment unless the competition between countries is based upon transparent and internationally accepted standards including standards of international cooperation in tax matters necessary to counter the increased cross-border opportunities to unlawfully avoid or evade national taxes enacted by democratically elected legislatures."). Simplicity, or ease in administration, is not advanced as a universal problem or goal *per se* in the OECD reports, but the difficulty in administering national systems due to globalization is a

course of the OECD's continuing project seems consistent with the idea that notions about sovereign rights or entitlements of taxation may be embracing some ideas about sovereign duty, so that an analysis of efficiency and equity cannot be confined to the nation-state but will require a global inquiry. If there is sovereign duty in tax system design, then a synthesis of the OECD's developing views may help to identify and define its scope and impact.

C. PRINCIPLES OF SOVEREIGN DUTY IN TAX SYSTEM DESIGN

From its starting point in 1996 through its latest progress reports, the OECD shifted its emphasis from a principal concern for protecting the tax base of OECD countries toward a principal goal of creating a level playing field for all countries. This shift demonstrates a deliberate effort to resolve practical issues but it also reflects the unresolved tension of simultaneously trying to cement the sovereign right to tax and identify the contours of a positive sovereign duty to protect that right. The OECD stated its consensus in 2004 that "[a]ll countries, regardless of their tax systems, should meet [certain] standards so that competition takes place on the basis of legitimate commercial considerations rather than on the basis of lack of transparency and lack of effective exchange of information."[103] To that end, the OECD stated that "all jurisdictions, OECD and non-OECD . . . , should act in a manner consistent with the concept [of the global level playing field] in their bilateral relationships *and more broadly*."[104] In other words, the OECD is suggesting that countries should follow these community standards on a unilateral basis.

This suggestion signals that those at the OECD believe that countries have a duty to comply with certain community standards, such as those having to do with transparency and information exchange, whether or not they volunteer to do so in formal international agreements.[105] A progress report issued in

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pervasive theme. *See* 1998 REPORT, *supra* note 39, at 28 (arguing that lack of transparency "will make it harder for the home country to take defensive measures" against foreign tax practices that divert revenue sources out of national tax bases).

103. OECD, *supra* note 81, at 2.

104. *Id.* at 3 (emphasis added).

105. As such, one might argue that the OECD is suggesting either that there is a customary international law that requires affirmative practices, or that the OECD is promulgating a soft law to the same end. Either way, it seems important to determine whether the standards and recommendations produced by the OECD are

2006, which focused on developments within OECD countries, reiterated the commitment to "create an environment in which all countries, large and small, OCED and non-OECD, those with an income tax system and those without, can compete freely and fairly thereby allowing economic growth and increased prosperity to be shared by all."[106] To achieve this goal, the OECD argues that "competition between countries [must be] based upon transparent and internationally accepted standards, including standards of international cooperation in tax matters necessary to counter the increased cross-border opportunities to unlawfully avoid or evade national taxes enacted by democratically elected legislatures."[107]

As in the earlier reports, this progress report does not address the possibility that community standards are coherent only under a theory of sovereignty that includes duty to other countries. Yet the choice of language, such as the reference to internationally accepted standards, suggests that the OECD has identified a sovereign duty to protect the sovereign right to tax, at least when this right is exercised by democratically elected legislatures, and that the content of that duty includes the abandonment of laws that facilitate or encourage illegal tax evasion.[108] Framing its goals as the pursuit of a global level playing field or "fair tax competition,"[109] or even "fair but fierce tax competition,"[110] is thus a means of describing both the

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appropriate. Such a determination might include questions about legitimacy and participation, about who the key players are and whether and how they advanced personal agendas, about the benefits and drawbacks of this kind of norm creation and diffusion in comparison with other kinds (e.g., a multilateral treaty and the administration that accompanies it), and similar inquiries.

106. 2006 REPORT, *supra* note 49, at 3.

107. *Id.* at 2.

108. The strategies or expectations for such pursuit are discussed below. The protection of the right for only democratically elected legislatures may be too narrow; even Rawls thought that "decent hierarchical" societies could be counted as participants in the making of an international social contract. JOHN RAWLS, THE LAW OF PEOPLES: WITH "THE IDEA OF PUBLIC REASON REVISITED" 62–64 (1999). Further reflection might expand the OECD's conception to include all sovereign states, whether their lawmakers are democratically elected or not. At least we may note that the inclusion of these words suggests that political philosophy may be very important in shaping the ideas and norms emanating from international institutions.

109. 2001 REPORT, *supra* note 40, at 4.

110. Jeffrey Owens, Dir. of the OECD Ctr. for Tax Policy & Admin., Presentation at the INEKO International Conference on Economic Reforms for Europe, Fair Tax Competition: A Pillar of Positive Economic Reform (March, 18 2004). *See also* Jeffrey Owens, Fair Tax Competition: A Pillar of Positive Economic Reform (PowerPoint), http://www.oecd.org/findDocument/

existence of a social contract and some of the duties that form the content of that contract.[111]

The OECD reports thus implicitly raise the increasingly complex issue of sovereign duty, but they do not resolve the fundamental theoretical tensions illuminated by their discussion. Whether the sovereign duty implicitly identified by the OECD is authentic, legitimate or appropriate remains an unresolved issue. Some frame of reference is needed to effectively evaluate the bare skeleton of duty implicitly articulated by the OECD. The next part proposes a contextualization of these ideas within political philosophy scholarship as a starting point for such an evaluation.

IV. POLITICAL PHILOSOPHY AS AN ANALYTICAL FRAMEWORK

Having identified a baseline theory of sovereign duty in tax system design from the OECD's harmful tax practices initiative, how does this theory compare to theories of duty laid out in other contexts? What do people think states generally owe each other as fellow members of an international society of states, and how does taxation fit with these ideas? The potential analytical approaches are myriad, but social contract theory is particularly appropriate in this context both because it specifically explores how and why a duty arises between people at all, and because there is a (perhaps surprising) amount of affinity between the language the OECD uses to explain its views on harmful tax practices and the core concepts of this

0,3354,en_2649_33745_1_119835_1_1_1,00.html (click on "Fair Tax Competition - A Pillar of Positive Economic Reform") (last visited Oct. 24, 2008).

111. As defined in various reports. For example, "[s]ecret rulings, negotiated tax rates, or other practices that fail to apply the law in an open and uniform way are examples of lack of transparency," as are "inadequate regulatory supervision." 2001 REPORT, *supra* note 40, at 5, 11. Transparency "requires financial accounts to be drawn up in accordance with generally accepted accounting standards and that such accounts either be audited or filed." *Id.* at 11. Effective exchange of information is defined as having the legal mechanism allowing information to be given to tax authorities in another country in response to requests, enacting safeguards to ensure information is used for the purpose sought (protecting rights and confidentiality), not having rules requiring criminality in order to allow information transfer, and being able to have the information exchange mechanism monitored. *Id.* The standards currently offered by the OECD to evaluate a country's adherence to this duty are now encapsulated in a model tax information exchange agreement that requires "transparency" and "effective exchange of information." *Id.*

theory. The contractarian approach thus provides a structure for thinking about duty in tax system design that is already implicitly at play in the attempts of OECD officials to create an international consciousness regarding tax policy. This article is primarily an inquiry about duty, and not about justice per se (of which sovereign duty may be, but is not necessarily, a component). By providing a framework for thinking about justice, social contract theory demonstrates the complexity involved in determining whether a theory of sovereign duty in tax system design is coherent, defensible or workable.

In employing a contractarian approach, a first instinct may be to turn to the work of John Rawls, whose work on social contract theory is both seminal and so well-known that he is sometimes cited almost perfunctorily in contractarian inquiries.[112] Many analyses start with Rawls because his version of justice is thought to represent the most developed conceptual framework: if the case for Rawlsian social contract theory fails, it precludes the success of any lesser theory.[113] And, specific to the OECD work, Rawls's *The Law of Peoples*, first published in 1993[114] and revised in book form in 1999,[115] explicitly invokes ideas about sovereign duty in searching for a theory of international justice.[116]

However, as Part A demonstrates below, Rawls's view of social contract theory ultimately fails to provide a coherent framework by which we may judge the OECD's implicit social

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112. For example, Michael Graetz cites Rawls for the proposition that "we regard our obligation for the well-being of our fellow citizens as more pressing than for people in need elsewhere in the world." Graetz, *supra* note 8, at 277–78. This proposition has been severely criticized by Rawls's critics, who have contested both that there is no morally sound foundation for making such a claim, and that the claim itself is contradicted in Rawls's own writings. *See, e.g.*, THOMAS POGGE, JOHN RAWLS: HIS LIFE AND THEORY OF JUSTICE (Michelle Kosch trans., 2007).

113. Nussbaum particularly emphasizes this view. NUSSBAUM, *supra* note 5, at 3 (Rawls's theories "are probably the strongest theories of justice we have"). For example, Nussbaum particularly eschews utilitarianism for its averaging effect that measures justice in a way that allows the misery of the worse off to be offset by the happiness of the better off. Since her view is that any theory of justice necessarily requires the consideration of every person, utilitarianism offers a much less satisfactory basis than social contractarianism with its more individualistic view. *See, e.g.*, *id.* at 342–43. For a similar argument in tax policy assessment, see Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CAL. L. REV. 1905 (1987).

114. John Rawls, *The Law of Peoples*, 20 CRITICAL INQUIRY 36 (1993).

115. RAWLS, *supra* note 108.

116. Rawls, *supra* note 114, at 38 (stating that "every society must have a conception of how it is related to other societies and of how it is to conduct itself towards them."); *see also* RAWLS, *supra* note 107.

contract.[117] The Rawlsian theory fails because it relies on a procedural approach to justice and does not provide any means for evaluating the actual principles chosen via the apparently just procedure.

Even if Rawls's view is ultimately unsatisfactory (as it seems to be), his procedural justice approach provides some vocabulary and a context for understanding some of the ways in which states have behaved.[118] Further, so many of his core concepts are reflected in the OECD's explanations of its work, it seems a Rawlsian analysis would be critical in any attempt to understand this work from a contractarian perspective. By demonstrating why a Rawlsian approach does not answer the questions raised by the OECD's harmful tax practices work, I hope to show both why this project has prompted much polarized reaction but very little coherent debate on the principles, and why more and better analysis is needed.

While a Rawlsian analysis does not answer the critical questions here, another approach to social contract theory taken by political philosophers provides a better framework for analysis because it directly attempts to answer the question of how we assess the principles themselves, apart from the issue of assessing whether the procedure in ascertaining them was just.

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117. His theory has been criticized mainly for its failure to adequately extend the principles of *A Theory of Justice* to a single global social contract among individuals, and for relying on an often-flawed view of the state as a rational and representative actor, capable of principled and deliberative action. *See infra* Part II.A. Much of the criticism emerges from the cosmopolitan perspective, which rejects the two-stage contract and its vesting of rights in state agents as inconsistent with *A Theory of Justice.* This literature argues that a conception of a single global social contract among all people would be more consistent with Rawls's earlier work because it would involve the rights of all persons directly rather than via representatives who may be subject to self-dealing and political capture. *See, e.g.*, ANDREW KUPER, DEMOCRACY BEYOND BORDERS: JUSTICE AND REPRESENTATION IN GLOBAL INSTITUTIONS (2004) (criticizing Rawls's state-centric position as violating the original principles of *A Theory of Justice* and arguing that these principles would support a global theory of justice with the individual as the epicenter); *see also* Tomer Broude, *The WTO/GATS Mode 4, International Labor Migration Regimes and Global Justice* (21 Hebrew Univ. Int'l L. Research Paper No. 7-07 2007) http://papers.ssrn.com/sol3/papers.cfm?abstract_id=987315 (discussing Rawls's theory in the context of migration and criticizing its nationalist view as "justification of the unilateral and restrictive immigration policies of the affluent states who define the meaning of liberalism and 'decency'.").

118. At least, the affinity between Rawlsian concepts and the OECD's actions may provide a theoretical basis for evaluating competing views of the OECD's proposals to curb harmful tax practices. A framework may assist in creating dialogue between polarized views currently developing in tax scholarship on this issue.

This is the approach of cosmopolitan scholars such as Martha Nussbaum, whose *Frontiers of Justice* explicitly confronts the weaknesses of Rawls's theory in *Law of Peoples*.[119] Nussbaum's approach not only critiques the unsatisfactory result of the Rawlsian analysis outlined above, but it also furthers the analysis of the OECD's work by providing a means for assessing the OECD's vision of sovereign duty. Each of Rawls's and Nussbaum's analyses is discussed below, and each is compared to the theory of sovereign duty in tax system design that I argue is being advanced by the OECD.

A. THE FAILURE OF A RAWLSIAN APPROACH

Rawls's work in *Law of Peoples* is built upon his earlier work in *A Theory of Justice*, in which he developed what are now fundamental principles for understanding the kind of rules people would universally choose for a just society.[120] To briefly summarize, Rawls posited that people in a hypothetical pre-political "original position" would form a just social contract among themselves if they were ignorant about what their ultimate position would be in that society.[121] The resultant contract would require every person to have equal rights to a list of basic liberties and would allow for social and economic inequality, beyond those basic rights, only on conditions of equality of opportunity[122] and of maintaining or bettering the lot of the least-advantaged.[123] Rawls concluded that since all

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119. NUSSBAUM, *supra* note 5; RAWLS, *supra* note 108.

120. RAWLS, *supra* note 5, at 92.

121. *Id.* Rawls conceptualized a hypothetical "veil of ignorance" as a way to prevent people's views of justice to be colored by their actual position in society. He suggested that the coherence of the social contract theory rests on the idea that persons in the original position would be subject to the "circumstances of justice" as outlined by Hume and Rousseau—in general, everyone has a need to form a social contract because resources are relatively scarce, everyone has something with which to bargain, and no one has too much. *Id.* at 137; *see also* DAVID HUME, A TREATISE OF HUMAN NATURE (Selby-Bigge ed., Oxford Univ. Press 2d. 1978) (1739).

122. Because no one would want positions of power and resources to be locked in forever, it is assumed that people would seek equal opportunity in a fair competition rather than equal distribution of all resources. RAWLS, *supra* note 5, at 83. As will be discussed more fully in the next part, the work of the OECD in curbing what it deems "harmful" tax competition in the name of striving for "fair" competition reflects this type of opportunity rather than an equal results-centered view.

123. *Id.* at 14. That is, a move that would improve the lives of some at the expense of others, while it might produce an overall net gain that would be acceptable under a utilitarian view, would not be acceptable to a rational person constructing a contract in the original position since no one would risk being worse off only to make someone else better off. *Id.*

rational people would want to pursue these same ideals, all societies should center around these principles in an effort to become what he called "well-ordered."[124]

In *The Law of Peoples: with "The Idea of Public Reason Revisited"*, Rawls develops an international version of his theory by expanding the themes of *A Theory of Justice*, to analogize states[125] as parties in a second[126] original position in which they determine a just way of ordering international society by forming a second-level social contract.[127] Embodying states in their officially appointed representatives,[128] Rawls argues that rational representatives will opt for an international system that prioritizes independence and non-interference among states while subscribing to a short list of essential rights for all people.[129]

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124. *Id.* at 453–62. Thus, in Rawls's view, societies that do not pursue equal basic liberties for all, that tolerate inequality of opportunity, or that pursue social or economic gain at the expense of the least-advantaged among them, are illiberal, and therefore unjust, societies. *Id.*

125. In this work, Rawls explicitly rejects the use of the term "nation" or "state," preferring to place political authority in "peoples," which he attempts to define as groups of persons aligned by "common sympathies," and a "willingness to live together under the same set of democratic principles." However, as Nussbaum and others have shown, the departure is "confused and confusing," as well as possibly indistinguishable from current conceptions of statehood in any event. NUSSBAUM, *supra* note 5, at 246. In a world in which the state is unchallenged as the primary locus of political power, the abstraction to peoples is also unhelpful in assessing the OECD's work, to the extent it means anything other than people as they are currently organized in states. *See, e.g.*, STEPHAN LEIBFRIED & MICHAEL ZURN, TRANSFORMATIONS OF THE STATE? (2005); SØRENSEN, *supra* note 11. Relying on Nussbaum and others' criticism of the approach, I therefore leave aside the concept of peoples and apply Rawls's account as if between states. Rawls's argument appears ultimately unsatisfactory in any event, so this gloss should not by itself be fatal to the interpretation of Rawls's thinking.

126. The first being the parties to the original position that formed the state as the means to achieve justice among persons in the first instance. RAWLS, *supra* note 108, at 30.

127. *Id.* at 63.

128. Analogizing to the original contract, Rawls envisions that in the original position of states, the "veil of ignorance" prevents representatives from knowing the size, wealth, etc. of their states, so they "will develop a system that ensures their political independence, civil liberties, and self-respect as a people." Mike Wiser, Book Review, 14 HARV. HUM. RTS. J. 299, 299 (2001). *See also* RAWLS, *supra* note 108, at 32.

129. RAWLS, *supra* note 108, at 106. (Rawls's short list of duties includes a just war theory and a theory that people will want states to honor a bare minimum of human rights and help people living under conditions that preclude the existence of a just (national) social regime (what he calls "burdened societies.") The list is shorter than the list of basic liberties he outlines in *A Theory of Justice*. RAWLS, *supra* note 5, at 61.).

Although official OECD documentation never cites Rawls, many of his ideas about a second-level international social contract appear to be firmly embedded in the OECD's work of curbing harmful tax practices. Thus, whether one agrees with Rawls's perspective or not, it seems important to delve further into his theory, at least to examine evidence of its instrumentalism.

For example, the Rawlsian international social contract is created first by persons seeking to form a liberal state[130] for their mutual advantage, then seeking, among an inner circle of such duly-formed liberal states, a social contract to establish foreign relations among them. This second-level contract is then joined by "decent hierarchical" (but not necessarily liberal) states that accept the principles determined by the liberal states to be just.[131] Though the terminology presents some line-drawing problems, this sequence is approximated by the OECD's strategy toward developing international consensus on key principles. First, each of the OECD member states is probably a "liberal" state in the Rawlsian sense, so that we can generally assume each is itself the product of a social contract that adequately values the basic rights of its members and can therefore act as representatives of its people.[132] Second, representatives from a small group of such liberal states[133] came together and formed a second-level social contract among themselves[134] which they subsequently invited other "reasonable" (*i.e.*, as measured by their willingness) societies to

130. By liberal, Rawls roughly means democratic states that in general terms embrace the ideas of justice as fairness outlined in *A Theory of Justice*. *See* RAWLS, *supra* note 5, at 12–14.

131. *Id.* at 62–64. By "decent hierarchical," Rawls referred to states that were not democratic but that agreed to conform to the constraints and standards advanced in the contract. Nussbaum argues that Rawls's explanation is poorly conceived, but may have derived from his desire that states should "respect the sovereignty of any nation that is organized in a sufficiently accountable way, whether or not its institutions are fully just." NUSSBAUM, *supra* note 5, at 256. This stance protects Rawls's central focus on respecting state sovereignty by theorizing very few instances in which intervention would be justifiable.

132. *But see* NUSSBAUM, *supra* note 5, at 256 (critiquing this representative ability); *see also* Steven A. Dean, *Philosopher Kings and International Tax: A New Approach to Tax Havens, Tax Flight, and International Tax Cooperation*, 58 HASTINGS L.J. 911 (2007) (providing a critique of states as unitary actors in the context of international taxation).

133. Namely, the foreign ministers who wrote the original Communiqué to the OECD and the members of the Committee on Fiscal Affairs who participated in drafting the 1998 Report. *See* Council of the OECD, *supra* note 40, at I.

134. As outlined in the 1998 REPORT, *supra* note 39.

join.[135]

In addition, the OECD's work in naming, shaming, and placing pressure on noncompliant states to induce them to adopt the guidelines reflects Rawls's view of "outlaw regimes," or states that "refuse to acknowledge a reasonable law of peoples."[136] Rawls suggests that the parties abiding by the contract are in effect in the state of nature with respect to those not abiding by the contract, and therefore law-abiding societies can "at best establish a modus vivendi" with these states.[137] Evoking the related idea that it is immoral for anyone to want to stay in the state of nature,[138] Rawls states that the first duty of liberal states is to leave the state of nature themselves (by forming the international social contract), and the second duty is to bring all other states out of the state of nature as well, so that every person can live in a society that respects and promotes basic rights.[139] The OECD's recommendation that "Participating Partners" (states that adopt the OECD's guidelines and recommendations for fair tax competition because they are "Committed to Improving Transparency and Establishing Effective Exchange of Information in Tax Matters")[140] engage in coordinated defensive actions against "Unco-operative Tax Havens"[141] tracks this mechanism rather

135. The OECD terms these the "Participating Partners," namely, the thirty-five countries that have been designated as "committed jurisdictions" because they are working together to "develop the international standards for transparency and effective exchange of information in tax matters." *See* OECD, *Jurisdictions Committed to Transparency and Effective Exchange of Information*, http://www.oecd.org/document/48/0,3343,en_2649_33745_29874096_1_1_1_1,00.html (last visited Sept. 12, 2008).

136. Rawls, *supra* note 114, at 60.

137. *Id.* at 61.

138. IMMANUEL KANT, *The Metaphysics of Morals*, *in* POLITICAL WRITINGS 131, 132–36 (Hans Reiss, ed., 2d ed. 1991) (1797) (stating that the first political duty of humans is to leave the state of nature and submit to the rule of a reasonable and just law).

139. Rawls, *supra* note 114, at 61 (The "law of peoples" specifies that those in the social contract must aim to "bring all societies to honor eventually that law, to be full and self-standing members of the society of well-ordered peoples, and so to secure human rights everywhere.").

140. OECD, *35 Jurisdictions Committed to Improving Transparency and Establishing Effective Exchange of Information in Tax Matters*, at http://www.oecd.org/document/19/0,3343,en_2649_33745_1903251_1_1_1_1, 00.html (last visited Sept. 12, 2008).

141. OECD, *List of Unco-operative Tax Havens*, http://www.oecd.org/document/57/0,3343,en_2649_33745_30578809_1_1_1_1,00.html (last visited Sept. 12, 2008) (These are defined as states "which have not yet made commitments to transparency and effective exchange of information."). The use of the word "yet" implies that the

closely. Subsequent OECD reports become increasingly clear in describing a broad and all-inclusive plan to bring all countries to the principles of fair competition as laid out and agreed to by the OECD member countries.[142]

Rawls further posits that states representing the will of the people should favor political independence and non-interference.[143] This idea also seems to be strongly reflected in the work of the OECD.[144] The OECD repeats its defense of state independence in decision-making and control over tax policy in virtually every report it issues; in proposing a set of coordinated defensive measures it repeats the statement that countries must decide whether and how to participate; it repeats as a mantra that "[c]ountries should remain free to design their own tax systems as long as they abide by internationally accepted standards in doing so."[145] The OECD's work implicitly embraces Rawls's ideas about the importance of deferring to the state when people have (freely and fairly) ceded individual authority to this institution.

However, the term "as long as" may give us pause in applying Rawls's analysis, because the OECD has asserted a right to intervene by means of economic sanction in the case of a state that violates the condition of adherence to global standards. In Rawls's analysis, the OECD's implementation of this claim may constitute interference when non-interference should be the norm.[146] If the OECD has a duty[147] to bring all countries out of the state of nature, and if its expressed mission is to do so by bringing all countries up to its standards,[148] then

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OECD fully intends that these states will ultimately be brought out of the state of nature and into the international social contract.

142. *See, e.g.*, 2004 REPORT, *supra* note 49, at 12 (The OECD's goal is to make "further progress . . . so that all countries can reach the high standards which the Participating Partners wish to see achieved.").

143. RAWLS, *supra* note 108, at 37.

144. Rawls, *supra* note 114, at 41–42. (Rawls expresses a theme, familiar in tax scholarship, that the "familiar powers of sovereignty," including "the right to do as it likes with people within its own borders[,]" have become increasingly challenged and limited under international law as developed since World War II. But he ultimately affirms the essential status of the sovereign state by granting that institution the status as participant in the original position, rather than allowing for a single global social contract among all people.).

145. 1998 REPORT, *supra* note 39, at 15.

146. RAWLS, *supra* note 108, at 37 ("Peoples are free and independent, and their freedom and independence are to be respected by other peoples. . . . Peoples are to observe a duty of non-intervention.").

147. Whether Rawlsian, Kantian, or otherwise. *See* KANT, *supra* note 138.

148. *See, e.g.*, 2004 REPORT, *supra* note 49, at 12.

how are its efforts to impose economic or political pressure and sanctions to be understood? The imposition of pressure and sanctions either violates or protects the noninterference norm, depending on one's view. That is, "outlaw" states may need to be brought out of the state of nature, but Rawls explicitly demurs on the question of just how this should be done, leaving the matter to "foreign policy" because "these things call for political wisdom, and success depends in part on luck."[149]

Without a set of principles for determining whether the imposition of economic sanctions by the OECD is a violation of the duty of non-intervention or a just means of fulfilling a duty to bring outlaw states out of the state of nature, Rawls's social contract theory is ultimately unsatisfactory. It does not explain what sovereign duty in taxation may imply for states within or without the contract. It is therefore perhaps unsurprising that the OECD's position on its initiative evokes strong positions on both sides of the issue in tax scholarship while providing little frame of reference for a principled solution.[150] We need more to help assess and evaluate what the behavior explains about sovereign duty in tax system design. Since Rawls's theory does not (and perhaps cannot) provide such an analysis, I turn to Nussbaum for a different view.

B. THE STRENGTH OF A RIGHTS-BASED APPROACH

In *Frontiers of Justice*, Nussbaum argues that Rawls's second-stage social contract theory is inadequate to explain why states do or should cooperate, principally because the major premise is flawed: states will not contract unless it betters their position relative to what they can achieve in the Hobbesian state of nature.[151] She suggests that poorer or weaker states will be excluded from the second original position because wealthy states are better off dominating them in the state of nature than bargaining with them for a just international order.[152] The "circumstances of justice" so critical to the social contract

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149. Rawls, *supra* note 114, at 61.

150. *Compare, e.g.*, Lorraine Eden & Robert T. Kudrle, *Tax Havens: Renegade States in the International Tax Regime?*, 27 L. & POL'Y 100 (2005), *and* Papali'i T. Scanlan, *Globalisation and Tax-related Issues: What are the Concerns?*, *in* INTERNATIONAL TAX COMPETITION: GLOBALISATION AND FISCAL SOVEREIGNTY 43 (Rajiv Biswas ed., 2002), *with* Hugh J. Ault, *The Importance of International Cooperation in Forging Tax Policy*, 26 BROOK. J. INT'L L. 1693 (2001).

151. NUSSBAUM, *supra* note 5, at 248–49.

152. *Id.* at 249.

theory—that resources be relatively scarce, that everyone have something with which to bargain, and that no one have too much[153]—are thus not coherent when applied to states instead of people.[154] As such, social contract theory cannot explain why strong states cooperate with weak ones—there must be some other explanation why states would undertake behaviors that might not inure to their own benefit.

To go further into Nussbaum's theory, we need to determine where the burdens and benefits of tax competition lie, in order to determine whether it can be said that all states are under Humean circumstances of justice in matters of tax policy. The central message of the OECD's work is that each state, regardless of economic size and strength, has the potential to undermine the fiscal efforts of the others. The OECD suggests that states with large budgets (welfare states) are potentially disadvantaged in the state of nature, susceptible, for instance, to poaching by tax havens via predatory practices such as bank secrecy.[155] To the extent that they cannot reliably achieve cooperation by means of force and violence in the state of nature, it serves the interest of such welfare states to enter into a contract for mutual advantage—even, perhaps especially, with poorer and weaker states.[156]

But for the social contract theory to hold, non-OECD states must also seek advantage through bargaining rather than staying in the state of nature through unfettered competition. The OECD suggests that one potential advantage for some small states in an international social contract is the promise of continued financial assistance from OECD countries.[157] Whether that or some other promise is better than that which is achievable in the state of nature is a question each state determines.[158] For those who associate and comply with the

153. *See* RAWLS, *supra* note 5, at 126–30.

154. NUSSBAUM, *supra* note 5, at 255. Nussbaum deems the analogy to be "deeply flawed." She explains that Rawls's theory depends on an original position in which all the contracting parties are free, equal, and independent, so that anyone not free, equal, or independent is not eligible to strike the bargain (since they can simply be dealt with through domination later). As such, disabled persons are necessarily excluded from the original position and poor or weak states are necessarily excluded from the second stage original position. *Id.* at 240–55.

155. *But see* Scanlan, *supra* note 150, at 45–46 (pointing out that the OECD's claims of the potential harms of tax competition have not to date been supported by empirical evidence).

156. Thus, the OECD's emphasis on information-exchange agreements.

157. 2000 REPORT, *supra* note 49, at 20–21. Of course there are many other reasons as well, ranging in type and importance from country to country.

158. For example, a number of Caribbean countries decided to cooperate with

OECD recommendations, this social contract may seem to offer mutual advantage. To those who refuse, the state of nature might seem better.[159]

Understanding compliance with OECD guidelines requires further analysis of Nussbaum's theory, because, as the OECD points out, harmful tax competition is a global issue that cannot be solved without global compliance—all countries apparently must agree.[160] If there are states for which the advantage through bargaining does not clearly exceed the advantage of staying out of the social contract,[161] is there any notion that would support a theory of duty in tax system design that requires those states to acknowledge something called sovereign duty? For example, are those states obligated to "secure the integrity of tax systems by addressing . . . issues . . . that unfairly erode the tax bases of other countries and distort the location of capital and services," as the OECD suggests is a duty owed by all states?[162] In other words, going back to the analysis that was left unanswered by Rawls's theory, (how) can we identify sovereign duty, so that we can know whether the OECD's suggested measures are themselves a violation of sovereignty or instead a reaction to such a violation?

Nussbaum's approach brings us closer to an answer. A procedural approach such as Rawlsian social contract theory, she argues, will always leave questions unanswered because it assigns duties before it defines rights.[163] Since duties "are never generated in a vacuum . . . the idea of needs, and of entitlements based upon needs, always enters in to inform us why the duty is a duty, and why it matters."[164] This does not, however, mean that we inevitably return to both defining

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the United States in tax compliance matters in exchange for the promise that they would be included on a list of countries with respect to which certain business-related expenses would be deductible for United States federal tax purposes. *See* Interest and Dividend Tax Compliance Act of 1983, Pub. L. No. 98-67, tit. II, 97 Stat. 369 (codified at 19 U.S.C. §§ 2701–06 (1988)).

159. *But cf.* NUSSBAUM, *supra* note 5, at 51 (noting that, in Kantian terms, states should not want to stay there).

160. 2004 REPORT, *supra* note 49, at 4.

161. As, apparently, there are. *See* OECD, *List of Unco-operative Tax Havens*, *supra* note 141.

162. 2000 REPORT, *supra* note 49, at 5.

163. NUSSBAUM, *supra* note 5, at 276.

164. *Id.* at 276. Further, "[t]o put the problem in terms of duty first, asking what duties we have to people in other nations, is likely to make our ethical thinking stop short when we reach a problem that seems difficult to solve." *Id.* at 280.

sovereignty and the conundrum of locating a right to tax in the very nature and character of the institution of the state. Instead, Nussbaum argues that an outcome-based approach that seeks to determine what people need and are entitled to must inform the inquiry; only after this list has been drawn up may the duties be assigned.[165] She argues that, to the extent that we believe all people have certain basic entitlements, we must believe that all people similarly have the duty to promote and preserve these rights in others.[166] However, people acting individually may neglect their duties, overlap in them, or otherwise fail to meet needs as they arise.[167] Nussbaum therefore argues that people must, and do, turn to institutions to assign the task of seeing that duties are met collectively.[168] One of these institutions, though not the only one, is the sovereign institution of the state.

Thus Nussbaum presents a view of sovereignty that is close to that propounded by many international law and international relations scholars, namely, that the state is one possible institution in which people may locate various powers and

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165. *Id.* at 276. Since this article involves a search for duty and not a broad search for international justice, I do not dwell too heavily on the list of individual rights themselves or the route to justice provided by Nussbaum's outcome-oriented approach (what Nussbaum terms the "capabilities approach," in order to emphasize that justice requires that everyone be allowed to strive for opportunities, rather than being given some pre-determined minimum bundle of items). *Id.* at 280. Instead, I focus here on how this approach is already reflected in international tax norms and practices via the work of the OECD. As such, the approach itself seems worthy of further contemplation in understanding the limits and potential of a theory of sovereign duty as initiated by the OECD.

166. *Id.* at 278–80 ("[T]he 'basic capabilities' of human beings are sources of moral claims wherever we find them . . . we are all under a collective obligation to provide people of the world with what they need. Thus the first answer to the question 'Who has the duties?' is that we all do."). The capabilities approach offers a threshold of rights: "for each important entitlement, there is some appropriate level beneath which it seems right to say that the relevant entitlement has not been secured." *Id.* at 291–92.

167. *Id.* at 280.

168. *Id.* ("We may . . . find some good reason for delegating this obligation to a subgroup of human beings."). Because of collective action, fairness, and capacity issues, Nussbaum suggests that it is appropriate to vest some of the duty in institutions including states, non-governmental organizations, multinational corporations, etc. *Id.* at 307–08. This view accords with international relations scholars who see the state as a dynamic repository of ideas about social, political, and geographic identity and community, which changes (albeit sometimes quite slowly) according to changing ideas about what the state can and should do in influencing people's lives. *See, e.g.*, Stephan Leibfried & Michael Zürn, *A New Perspective on the State: Reconfiguring the National Constellation*, 13 EUR. REV. 1 (2005).

obligations, according to ideas that are developing in new ways as a result of economic globalization.[169] According to this view, sovereignty is an institution that is shaped by our changing needs as persons living in a politically separated but economically linked world.[170] Nussbaum's approach, viewing duty as articulated by individual persons who delegate it as needed or desired to particular institutions for particular purposes, seems not only more accessible and applicable to what is happening at the OECD and elsewhere in tax system coordination, but also more reflective of the broader reality of dynamic and complex rulemaking that may be witnessed in many areas of international governance.[171]

Like Rawls, in addition to adhering to Nussbaum's posited process by which ideas are implemented through delegation, some of the major details of Nussbaum's theory of duty are reflected in the work of the OECD. For instance, Nussbaum outlines "ten principles for the global structure," in reference to which she states that "multinational corporations have responsibilities for promoting human capabilities in the regions in which they operate."[172] Nussbaum states that corporations could be "controlled by domestic laws in each country," which would presumably require them to promote human rights, including equal social and economic opportunity, throughout the world.[173] However, like the OECD and others, Nussbaum recognizes that "the difficulty is that all countries want to

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169. *See, e.g.*, SLAUGHTER, *supra* note 42; Jackson, *supra* note 35. Nussbaum may be sympathetic to the retreatist, or liberal perspective, which sees the state as threatened by the forces of economic globalization. *See*, NUSSBAUM, *supra* note 5, at 225 ("the power of the global market and of multinational corporations has considerably eroded the power and autonomy of nations."); *see also* MATHEW HORSMAN & ANDREW MARSHALL, AFTER THE NATION-STATE: CITIZENS, TRIBALISM, AND THE NEW WORLD DISORDER (1994) (arguing that the traditional nation-state is under threat and realigning traditional relationships between states, citizens, and the international economy); SUSAN STRANGE, THE RETREAT OF THE STATE: THE DIFFUSION OF POWER IN THE WORLD ECONOMY (1996) (arguing that the domain of the state's authority is shrinking).

170. *See* Leibfried and Zürn, *supra* note 168; Sorensen, *supra* note 6, at 602–03.

171. For example, as illustrated in the growing volume of empirical study in the area of global governance. *See, e.g.*, JOHN BRAITHWAITE & PETER DRAHOS, GLOBAL BUSINESS REGULATION (2000); Gregory Shaffer & Kalypso Nicolaidis, *Transnational Mutual Recognition Regimes: Governance without Global Government*, LAW & CONTEMP. PROBS., Summer/Autumn 2005, at 263.

172. NUSSBAUM, *supra* note 5, at 315–318. Nussbaum outlines some of the ways in which multinationals can accomplish this, such as promoting fair labor standards and good environmental conditions.

173. *Id.* at 318.

attract [multinationals], and there is sometimes a race to the bottom as each one seeks to offer cheaper labor and less burdensome environmental regulations than its competitors."[174] Nussbaum does not explicitly mention taxation in this race to the bottom, but the parallel seems justifiable and has been made in other contexts.[175]

Because of the problem of state-level competition, Nussbaum leaves it to multinational corporations themselves, together with their lawyers and their consumers, to enforce compliance with their duty to promote basic rights, such as the right to pursue economic opportunities.[176] But to the OECD, this right cannot be pursued unless there is a "level playing field"—*i.e.*, unless countries adhere to certain basic tax system design elements to prevent the possibility that economic opportunities will be lost due to unfair competition.[177]

The OECD seems to accept it as a given that the responsibility to create and maintain a level playing field (by promoting equal rights to pursue economic opportunities) lies squarely in the hands of states, rather than corporations, their lawyers, and their consumers. Although the OECD's work is focused, for now, on the impact of financial flows, and Nussbaum appears to have in mind only the potentially irresponsible activities of firms seeking to engage in offshore manufacturing at the lowest cost, the two forms of activity should impact the same rights and the same attendant duty.[178] The OECD has suggested as much, albeit indirectly. The

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174. *Id.* For the OECD's corollary, see the 1998 Report, stating that: "Globalization has, however, also had the negative effects of opening up new ways by which companies and individuals can minimize and avoid taxes and in which countries can exploit these new opportunities by developing tax policies aimed primarily at diverting financial and other geographically mobile capital. . . . Pressure of this sort can result in changes in tax structures in which all countries may be forced by spillover effects to modify their tax bases, even though a more desirable result could have been achieved through intensifying international co-operation. More generally, tax policies in one economy are now more likely to have repercussions on other economies. These new pressures on tax systems apply to both business income in the corporate sector and to personal investment income." 1998 REPORT, *supra* note 39, at 14.

175. *See, e.g.*, Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1586–1603 (2000); Avi Nov, *The "Bidding War" To Attract Foreign Direct Investment: The Need for a Global Solution*, 25 VA. TAX REV. 835 (2006).

176. NUSSBAUM, *supra* note 5, at 318.

177. 1998 REPORT, *supra* note 39, at 9, 14.

178. NUSSBAUM, *supra* note 5 (arguing that basic human rights cannot be achieved without considering how the international economic order impacts people's choices and resources).

OECD's focus on creating a level playing field for all, though it appears to take a procedural approach (if the conditions are fair, the outcome will be fair), is simultaneously an outcome-based approach (everyone should have a fair shot at attracting capital).[179] The OECD's goal to ensure "that the burden of taxation is fairly shared and that tax should not be the dominant factor in making capital allocation decisions"[180] evokes the idea of a universal duty placed in the hands of the state for implementation.

Employing Nussbaum's approach where Rawls left off may help explain why the OECD might be suggesting that states have more of a responsibility for promoting economic rights than might be expected under a mutually advantageous contract scenario. The explanation might be that, at least among many of the most powerful actors on the international tax stage, the belief is growing that the sovereign right to tax is a liberty that cannot be enjoyed by any one state without a single, global social contract under which every person in the world agrees to vest in their states a duty to protect that right, by preventing individuals from engaging in behavior that, while potentially advantageous to the individual, and even to the state, may cause others in the world to be worse off.[181]

This approach potentially still leaves unanswered the question whether the OECD's suggested economic sanctions should be seen as an appropriate response to a breach of duty by "outlaw" states or a violation of sovereignty. Nussbaum argues that absent grave violations of human rights, intervention,

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179. *See* 1998 REPORT, *supra* note 39, at 9 (stating that the OECD seeks to promote "fair competition for real economic activities"); 2000 REPORT, *supra* note 49, at 5 (stating that the OECD seeks to "secure the integrity of tax systems by addressing . . . issues . . . that unfairly erode the tax bases of other countries and distort the location of capital and services."); 2001 REPORT, *supra* note 40, at 4 (stating that the OECD "seeks to encourage an environment in which free and fair tax competition can take place."); 2004 REPORT, *supra* note 49, at 4 (stating that the OECD seeks "to establish standards that encourage an environment in which fair competition can take place."); 2006 REPORT, *supra* note 49, at 3 (stating that the OECD seeks to "create an environment in which all countries . . . can compete freely and fairly, thereby allowing economic growth and prosperity be shared by all.").

180. 2000 REPORT, *supra* note 49, at 5.

181. For instance by unfairly shifting the burden of taxation to those unable to employ the same tax avoidance strategies. *See, e.g.*, 1998 REPORT, *supra* note 39, at 14 (harmful tax practices "can erode national tax bases of other countries, may alter the structure of taxation (by shifting part of the tax burden from mobile to relatively immobile factors and from income to consumption) and may hamper the application of progressive tax rates and the achievement of redistributive goals.").

which may include economic sanctions, is almost never justified because it interferes with the right people have to form associations among themselves by forming a political society embodied in the state.[182] The problem is not easily solved, but what Nussbaum's approach offers is another set of factors which will need to be added to the existing analysis of tax practices. The rights-based approach, and its implicit adoption by the OECD, demonstrates that any evaluation of tax policy based on the distribution of rights and responsibilities within a closed system, however defined, is incomplete without factoring in the role of the state as both a member of international society itself, and as a repository of rights and obligations of and by its people.

C. A RIGHTS-BASED ANALYSIS OF THE OECD'S ENVISIONED SOCIAL CONTRACT

The OECD's work in articulating a conception of sovereign duty, although implicit, provides a basis for comparison with more general theories about what duty means and how it might come to be assigned to a particular institution such as the state. The OECD's approach to assessing tax systems suggests that the experts working through this institution see the need to look beyond national boundaries to gauge the international impact of domestic policy choices. These tax experts and policymakers, at least, seem to believe that the state as an institution has both a right and a duty to pursue something they call fairness in tax competition. This thin concept is slowly gaining content through implementation. For example, in formulating a conception of what fairness means for tax policy, these experts suggest that all states, to be validated as members in good standing of the global community, must share tax information with each other and not help to hide assets and income from each other's revenue authorities.[183]

The OECD proposes no international contract to embody or enforce these principles—no multilateral agreement indicating terms and conditions has been drafted for signature.[184] The principles are articulated, revised, and disseminated through OECD guidance. Perhaps this is an example of soft law,

182. NUSSBAUM, *supra* note 5, at 259–60.

183. 2004 REPORT, *supra* note 49; 2006 REPORT, *supra* note 49.

184. The signing of bilateral or multilateral information sharing agreements is one indication of a state's acceptance of the OECD's principles; a state's unilateral tax reform which eliminates competitive tax policies such as ring-fencing regimes might be another indicator.

through which the OECD is attempting, via theoretical, political and economic means, to influence states to adopt laws in accordance to its proffered best practices.[185] But what principles allow the OECD to compel states which do not stand to benefit from inclusion in this society, ordered by leaders not of their own choosing, to adopt rules that are not necessarily in their own best interests?

Nussbaum's insight is that we may identify a contract for mutual advantage only where there is, in fact, mutual advantage to be gained—in this case by cooperating rather than competing.[186] The advantage of being members in good stead may suffice to explain those states that choose to cooperate, but the naming and shaming of those that have refrained from adopting the OECD's recommendations, presumably because they do not expect to be advantaged by entering the contract, is problematic. For these states, the OECD's persistence might look like unprincipled coercion.

The OECD's work seems to fundamentally embody a contest of principles, in which cooperation and competition are in constant tension, and in which some actors promote one principle over the other while others attempt to promote both at the same time, and in which positions may change with political winds.[187] But if there is one unifying principle underlying the tension between tax cooperation and tax competition, it seems to be the growing acceptance that among the features of sovereignty is membership in a global community, that community means interconnectedness, and that isolated action in tax system design is neither possible nor desirable.

Perhaps the starting point for developing some content for the OECD's theory of sovereign duty that is emerging from this broad principle lies in re-assessing the concept of equity. This longstanding policy tool has mainly been used to describe and evaluate how national policies impact people within a given system.[188] In the traditional sense, equity has been assessed by comparing "similarly situated" persons within a national system (sometimes referred to as horizontal equity, or, to emphasize its

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185. *See* Christians, *supra* note 42.

186. NUSSBAUM, *supra* note 5.

187. *See* BRAITHWAITE & DRAHOS, *supra* note 171, at 18, 507–31 (showing that actors support some principles and oppose others, "using principles to do so").

188. For example, all of the potential taxpayers collected in one state, or all of the potential taxpayers encompassed in the overlapping tax jurisdictions of two or more states that cooperate by formal agreement (treaty).

domestic context, intra-nation horizontal equity) or comparing relative burdens among differently-situated persons (intra-nation vertical equity based on ideas about relative ability to pay).[189] Internationally, the concept has been used to describe and evaluate the proper allocation of revenues among equally legitimate claims from different jurisdictions (referred to as inter-nation equity).[190] But the concept does not easily describe or evaluate the means by which persons are determined to be within a given system, and therefore subject to comparison, and which are not.

For example, if intra-nation equity means that everyone within a state is entitled not to be inequitably burdened by taxes, how do we decide what an equitable burden is? In the traditional sense, one might take all of the potential "comparable" taxpayers—people who earn the same amount of income, for example, and then attempt to design tax policy so that the tax outcome is similar.[191] Determining comparables is a matter of deciding whose individual tax burdens will be analyzed. In a closed-system analysis, they are only those people who are identifiably part of the tax base, according to the state's internal means of detection and classification. In a globalized world, however, the ability of individuals to escape detection and classification might remove comparables from the picture, thus preventing an accurate intra-nation equity analysis as well as obscuring the impact one nation's tax system may have on another.[192]

Following Nussbaum, if every person is in fact entitled to be spared an inequitable tax burden, then every person must have a duty to every other person to be honest and pay a "fair share" of taxation. Since that concept is thin and, even if definable, difficult (perhaps impossible) to implement, we may come back to the state as a logical institution in which to rest the power to determine what constitutes fairness and then to figure out how to compel everyone—associated with whatever particular

189. *See, e.g.*, Bankman and Griffith, *supra* note 113.

190. Musgrave & Musgrave, *supra* note 22.

191. For example, this kind of equity argument has been used to support the taxation of capital, to prevent the undue burdening of labor income.

192. For example, foreign and domestic corporations are taxed differently under the U.S. Internal Revenue Code, so that domestic corporations are arguably not comparable to foreign ones. Since for tax purposes the United States determines whether a corporation is domestic or foreign by reference to its place of incorporation, a corporation can change its universe of comparables by re-incorporating offshore. *See* I.R.C. § 7701 (2008).

state—to comply with that determination.

Once this responsibility is lodged in the state, a global economic order forces states to take into account every person in the world, whether individual or corporate, in order to identify and assess comparables for the purpose of determining what is equitable—if not, the range of comparables may be inaccurately assembled so fairness and efficiency cannot be coherently assessed. But this task is insurmountable: no state has the political means to create and assess a database of every person in the world, and while some states may have the financial and technical ability to identify every potential taxpayer and their available assets from which to pay taxation, it seems unlikely that resources would be deployed for this purpose. Still, the OECD's approach to harmful tax practices moves in this direction.

The OECD's approach suggests that, because of the technological advances of the latest wave of globalization, it is no longer coherent for states to adhere to tax policy assessment tools that rely for their implementation on the concept of the state as a closed system. Our current perceptions about efficiency, equity, and simplicity are inadequate to the task of assessment when applied on this basis. The OECD's work demonstrates that we cannot rationally talk about fairness, or what equity means, by looking only at persons within a given territory or subject to a given sovereign authority—we can only hope to determine whether a given system approaches equity by examining how a given rule impacts every person, both within and without the system.

What we may take as a starting point from the OECD's work to establish principles for inter-state dealing is a basic skeleton of sovereign duty that requires states to consider the impact of national tax policy decisions on the revenue policies of other states. Suggesting that sovereign duty requires states to refrain from enacting or maintaining legislation that undermines the revenue efforts of other states adds some content to this skeleton, but more detail is needed—we must apply this basic framework to existing tax policies in order to evaluate both the theory and the policy. Attempting to implement the theory will expose its strengths and weaknesses, further informing the development of tax policy principles.

A comprehensive evaluation of existing, influential tax

regimes,[193] perhaps the most logical next step, is a task that bears exploring. But at this stage it seems important to recognize that ideas are currently being formulated in the international arena regarding what states owe one another as members of a global community, and the implications of these ideas may reach far more broadly than their architects necessarily envisioned. In identifying sovereign duty in a specific context, the OECD is explaining the existence of, or perhaps even creating, a global tax community. Its current protocol for sovereign duty may have implications for the OECD countries themselves that have not been considered—we need to examine these ideas for their broad implications for the design of tax systems around the world.

V. CONCLUSION

National tax systems are undeniably the product of domestic political battles and policy tradeoffs, but global economic interdependence necessarily leads us to reexamine our traditional conceptions about the nature of the state. Rights and responsibilities are being determined and established within the global community through dialogue and debate. Whether intentionally or not, a group of people within the OECD is advancing the dialogue and the debate by implicitly proposing a theory of sovereignty that does not support absolute autonomy in taxation.

Recognizing that one state's tax policy choices may impede another's, the OECD's harmful tax competition work focuses on the tradeoffs governments make between retaining political, social and economic autonomy and fostering economic interrelationships; between competing with other states and cooperating with them.[194] Cooperation, according to the OECD, does not erode but fundamentally "support[s] the effective fiscal

193. Such as the controlled foreign corporation or foreign tax credit regimes employed in the United States.

194. The 1998 Report lays out a story of increasing tax competition among countries as competition for geographically mobile capital intensifies, and argues that countries would be better off if they cooperated. 1998 REPORT, *supra* note 39, 13–18. The competition/cooperation paradigm is mirrored in other international regulatory areas, such as bankruptcy law. *See, e.g.*, Bruce G. Carruthers and Terence C. Halliday, *Law, Economy, and Globalization: Max Weber and How International Financial Institutions Understand Law*, *in* ON CAPITALISM 128 (Victor Nee and Richard Swedberg, eds., 2007).

sovereignty of countries over the design of their tax systems."[195] The question of obligation arises starkly: in competing, how much must any country cooperate with any other, even when competition might be more advantageous?

The OECD's work on harmful tax competition suggests that all states might be thought to owe each other some due in tax system design, irrespective of the relative advantages or disadvantages that deference to a particular norm or principle might present for any one state.[196] This theory is consistent with (and perhaps evidence of) a belief that some sort of social contract among states exists, and that the contract is not a mere theoretical apparition but carries real requirements: states may actually expect other states to act in some affirmative ways as a result of their status as fellow sovereign members of international society.[197] Moreover, the contract appears to involve a basic list of economic rights and obligations owing to all persons, regardless of their affiliation with any one particular country, region or locale.[198] The role of the state in

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195. 2000 REPORT, *supra* note 49, at 5. For a complementary view, see Daniel Shaviro, *Why Worldwide Welfare as a Normative Standard in U.S. Tax Policy?*, 60 TAX L. REV. 155 (2007) (suggesting that cooperation in tax matters may serve long-term national interests even when defecting serves short-term ones).

196. As such, a purely "egoistic" or self-interested social contract theory, such as that advanced by David Gauthier, may inadequately explain the behaviors of the parties. DAVID GAUTHIER, MORALS BY AGREEMENT (1986) (using game theory to show that the sole purpose of social cooperation is to secure mutual advantage).

197. This is not to suggest that states will comport with the expectations. Compliance is unpredictable to the extent "states are independent entities with diverse interests and have no guarantees that other states will act benignly toward them or even keep their commitments." Robert O. Keohane, *Hobbes' Dilemma and Institutional Change in World Politics: Sovereignty in International Society*, *in* WHOSE WORLD ORDER? UNEVEN GLOBALIZATION AND THE END OF THE COLD WAR 165, 166 (Hans-Henrik Holm and Georg Sørensen, eds., 1995) (citing Kenneth Waltz for the proposition that "world politics is a self-help system"). However, a lack of certainty in compliance does not negate the existence of the principle, as discussed *infra*, Part III.

198. The OECD does not explicitly articulate a list of basic entitlements, but the contours may be extracted from OECD reports which implicitly advance the idea that people have a right to organize their states around socio-economic goals such as redistribution and the pursuit of economic growth and prosperity. *See* 1998 REPORT, *supra* note 39, at 9, 14 (calling on all states to reduce "the distortionary influence of taxation on the location of mobile financial and service activities, thereby promoting fair competition for real economic activities" to counter globalization's distortionary effects, which "can erode national tax bases of other countries, . . . alter the structure of taxation (by shifting part of the tax burden from mobile to relatively immobile factors and from income to consumption) and . . . hamper the application of progressive tax rates and the achievement of redistributive goals."); 2006 REPORT, *supra* note 49, at 3 (OECD seeks to "create an environment in which all countries,

this contract is thus as delegate for the universal advancement of these rights and obligations.

Exploring the realm of sovereign duty is a theoretical exercise, but it has important implications for national tax system design.[199] If no duty among states exists—if there is no social contract—it seems that states are, at least in the realm of taxation, in a Hobbesian-style state of nature with respect to all other states, engaged in perpetual conflict, capable of cooperation for mutual advantage where it exists, but not required to cooperate and therefore subject to perpetual uncertainty regarding how other states may act and what possible reactions may be pursued without resorting to violence.[200] Under this view, each state may freely resort to whatever fiscal strategies it deems appropriate, without any regard to external impact, and subject only to self-restraint according to its own interests, but also subject to deference and assistance from other states only where it can be successfully negotiated.[201] Without a social contract, tax policy may (perhaps may only) be legitimately shaped by public choice considerations

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large and small, OCED and non-OECD, those with an income tax system and those without, can compete freely and fairly, thereby allowing economic growth and increased prosperity to be shared by all.").

199. For example, the OECD states that one of the reasons they explain what constitutes harmful (as opposed to fair) tax competition is to arm lawmakers with some defensive policy arguments to effectively resist members of the business community who pressure them to adopt harmful tax practices. *See* 1998 REPORT, *supra* note 39, at 17. The extent to which the OECD can attain the protection and order they seek in matters of taxation ultimately depends upon these developing ideas about sovereignty.

200. *See* HOBBES, *supra* note 5. Hobbes argued that people may have had some moral claims in the state of nature owing to their humanity (i.e., deriving from principles of natural law), but these claims would go unmet because morality would not be sufficient to create stability without political society. Since Hobbes' conception of sovereignty involved the collection of all the natural rights held by individuals into the institution of the state, he saw little chance for morality to create stability among sovereigns. A more optimistic view of the strength of moral obligations in the state of nature would paint a less bleak picture, but few grounds for such optimism are presented in political philosophy. *See, e.g.*, Keohane, *supra* note 197.

201. For example, the Treasury Department claims that when "international trade and investment flows were much less important than they are today to the U.S. economy and to U.S. companies . . . the United States was free to make decisions about its tax system based primarily on domestic considerations," and that U.S. adherence to international standards arises mainly from a sense that "[g]lobalization has made it imprudent for the United States, or any other country, to enact tax rules that do not take into account what other countries are doing." *See* HP-1060, Statement For the Record of the Senate Committee on Finance Hearing on International Tax Reform (June 26, 2008), *available at* http://www.treas.gov/press/releases/hp1060.htm.

in a global strategic game based on power rather than principle.[202]

But the OECD's work on harmful tax competition suggests that while power matters, principles might matter too. Evolving ideas about what sovereignty requires in the context of an international contract seem to be at work in the efforts of this institution. And although it is not explicitly articulated, much of the scholarly response to the OECD's work demonstrates that the question of sovereign duty is paramount in understanding not only this particular project, but the broader issue of cooperation and coordination of taxation in an economically integrated world.[203] This growing body of scholarship suggests a movement toward seeing domestic taxation as inherently and indelibly a global governance issue, which must be guided by some universal principles about what people owe and are owed as citizens of the world as well as members of particular states.

At a minimum, the OECD project demonstrates that the international aspects of a tax policy choice cannot be isolated from the domestic. We may not yet (or ever) be in a position to discuss whether countries have a duty to redistribute income or otherwise seek global distributive justice through globally-oriented tax policy choices. But this does not mean that

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202. To the extent that the state of nature is amoral (e.g., no social contract exists), national officials may justifiably act with regard only to national or sub-national interests, and individuals may justifiably act with regard only to their own interests. *See, e.g.*, Graetz, *supra* note 8, at 280–281 (Arguing that the proper lens for evaluating U.S. tax policy is the welfare of and distribution effects among U.S. persons, because "[p]aying attention to the distribution of the burdens and benefits of taxation among U.S. families and to the revenue consequences of the tax law is a fundamental obligation of both legislators and the executive branch in our democracy."); Tsilly Dagan, *National Interests in the International Tax Game*, 18 VA. TAX REV. 363 (1998) (stating that since global coordination and cooperation are virtually impossible to attain, nations should maximize their own long-term welfare); Julie Roin, *Taxation without Coordination*, 31 J. LEGAL STUD. S61 (2002) (arguing that potentially beneficial harmonization efforts are currently co-opted by interest groups, especially national legislators and powerful taxpayers, seeking to protect current social and economic positions).

203. Critics typically frame the OECD's work as a violation of the sovereign right of non-intervention, while proponents view the OECD's work as critically important to the future of the welfare state, or even the state itself as a going concern. *Compare, e.g.*, Papali'i T. Scanlan, *Globalisation and Tax-Related Issues: What Are the Concerns?*, *in* INTERNATIONAL TAX COMPETITION: GLOBALIZATION AND FISCAL SOVEREIGNTY 43 (Rajiv Biswas, ed., 2002), (arguing that the OECD's work overlooks or at least discounts the sovereignty of nations), *with* Avi-Yonah, *supra* note 175 (arguing that a race to the bottom will destroy the welfare state without global intervention), *and* Nov, *supra* note 175 (arguing that a race to the bottom cannot be prevented without a multilateral treaty).

countries must or even may retreat to domestic debate in assessing their choices. The flow of tax policy is now across a multifaceted, shifting and evolving transnational grid of power and principle. Understanding this grid, and the central role that institutional actors like the OECD play in defining its existence is integral to understanding the shape of tax law in the United States and elsewhere.

I have argued in this article that the OECD's approach to harmful tax competition may be interpreted as an implicit claim that states are the primary repositories of a responsibility to work toward creating a global economic order in which everyone has both economic opportunity and fiscal responsibility. Even so, it is clear that adherence to an exogenous code of conduct will not be equally advantageous for all people and all states. Guiding principles are needed to connect ideas about sovereignty to what people owe and are owed as taxpayers in an increasingly open global economic system. The OECD's theories about these principles deserve to be explicitly stated and subjected to rigorous analysis. Defining what sovereignty requires for tax system design necessitates an inclusive dialogue.

Finally, some clear principles must be advanced, and subjected to debate, regarding what steps states may take in order to compel compliance with agreed-upon norms, however determined. Whether states may invoke sovereignty to justify economic, political or social sanction in response to perceived breach of a code of conduct is a discussion that should be independent of the debate over the scope and meaning of sovereign duty itself. As Nussbaum has argued, "no existing state is fully just," so the grounds must be clear and important for members of one state to criticize and find violations of an international social contract by those of another.[204]

To identify grounds upon which one state can or should intervene in the tax policy decisions of another is essentially to identify and define a code of conduct for tax system design in an international social contract.[205] Since the contract is unwritten, its implications necessarily involve a contest of principles that should be subject to open debate.[206] Like the contract itself, a

204. NUSSBAUM, *supra* note 5, at 260 (All states "contain violations of important moral principles.").

205. *Id.* ("It is surely not respectful of another nation when state actors or concerned citizens criticize only other nations and fail to criticize their own.").

206. *See* BRAITHWAITE & DRAHOS, *supra* note 171, at 18, 507–31.

discussion of the grounds for its implementation has long revolved around largely unstated and under-analyzed assumptions about what sovereignty means or requires. It is critical to reexamine the basic assumptions underlying how we evaluate these questions. Reassessment should open up a discussion about how ideas about sovereignty, taxation and social contract emerge, are shaped and ultimately impact people around the world.