Brooklyn Journal of International Law

Volume 26 | Issue 4 Article 25

5-1-2001

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THE IMPORTANCE OF INTERNATIONAL COOPERATION IN FORGING TAX POLICY

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My thesis is simple and ties together various parts of the Symposium discussions. Without intensified international cooperation, there won't be an income tax on capital income for very long. Which is to say there won't be an income tax for very long, but a consumption tax in some form, or worse, some package of transaction taxes. Obviously, there are some people here—X number of people at least—who would welcome the consumption tax result. But if you start from the premise that we should try at least to preserve the income tax, and that we need multilateral efforts to do so, the question then becomes how to achieve this result. That brings me to Professor Thuronyi's paper.

The paper makes a welcome contribution to the growing literature on what forms international cooperation in the direct tax area might take. I think that I agree with all the various parts of the paper, but I have some reservations about the way they are put together and some of the conclusions that are reached. Most basically, I think an international organization which focuses mostly on a multilateral treaty puts the wrong priority as to where efforts on international cooperation should be focused. To revert to the somewhat dangerous metaphor we were using yesterday, we principally should be concerned with termite extermination, not with making sure some of the rooms in the house are tidied up.

But even on a narrower point, I am not convinced about the advantages of a multilateral treaty to replace the existing network of bilateral treaties. First of all, to a large extent, we

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already have a multilateral treaty in the Organization of Economic Cooperation and Development ("OECD") Model; which is the basis for almost all current treaties, involving both developed and developing countries. I am pleased to note that Professor Thuronyi cites with approval the American Law Institute Study which states, "[t]he OECD Model has almost acquired the status of an international agreement."[1] A number of people who worked on that project are here, and I am sure they share my satisfaction that the Study is still having an influence.

The basic question is: What would be gained by making the treaty more explicitly multilateral? When I look at the multilateral tax treaty I am most familiar with—the Nordic Treaty—the text is either substantially identical to the OECD Model or else has a series of references to the special problems of fitting together the legal systems of the five countries represented: What is a *utdelning* under Danish law? What is the status of a Swedish *enkel bolag*? It is of course useful to have all this in one place, but I wonder what a treaty would be like if it wasn't dealing with five countries but fifteen or fifty or one hundred fifty. More fundamentally, I see the treaties as primarily a bilateral means to work out the way in which the specifics of the tax systems of the two countries fit together, within the general framework of the allocation of taxing rights and obligations set out in the OECD Model.

Now, of course, there are problems with consistent interpretation and making sure that the same terms are interpreted in the same way by courts in the various countries. An important source for uniform inter-operation here is the OECD Commentaries. One notices these days much greater acceptance of the Commentaries in the courts as a legitimate and, in some cases, binding source of interpretative material. Moreover, there are other means to insure uniform interpretation. For example, the Memorandum of Understanding to the U.S.-Austrian treaty provides, "[i]t is understood that provisions of the treaty drafted according to the corresponding provisions of the Organization of Economic Cooperation and Development (OECD) shall generally have the same meanings as expressed

1. Victor Thuronyi, *International Tax Cooperation and a Multilateral Treaty*, 26 BROOK. J. INT'L L. 1641 (2001).

in the OECD Commentary thereon . . . ."[2] The Commentary—as it may be revised from time to time—constitutes a means of interpretation in the sense of the Vienna Convention on the Law of Treaties of May 23, 1969.

In addition, the Model itself, as adopted by the Council in the form of a Recommendation, and thus constituting a high level political commitment, takes the position that subsequent Commentary is to be applied to existing treaties, and this practice has been followed in the recent Partnership report. So, uniform interpretation is a problem, but not necessarily an insurmountable one. Professor Thuronyi goes on to mention other problems—like the fascinating issue of triangular situations and the like—the kind of needlepoint work that tax lawyers the world around love, but I wonder if these issues, viewed from a larger perspective, warrant the cannon of an international organization focused on treaties.

Professor Thuronyi mentions one point, however, which I think provides the appropriate transition to what I think the focus should be. He discusses the problem of a country which wishes to tax inbound portfolio investment but is reluctant to do so because taxing non-residents may drive the capital to other jurisdictions. This, of course, is a classic problem of tax competition, but not one about which a multilateral treaty, along the lines of any of the existing treaties, really can do anything. If the treaty allows a positive rate of tax on interest, that does not mean that all countries will in fact impose the tax, as witnessed, for example, by the U.S. portfolio interest exemption. The treaty can limit taxing rights, but it can't force the country to impose a tax and that is the issue which tax competition raises.

However, one can take Professor Thuronyi's proposal as broader than I have been reading it and view the focus not on "treaty," but on "multilateral," in the sense of the need for some international institutional structure in which multilateral co-operation can take place. This structure could be used to reach some general understanding as to how tax systems should interact, what are appropriate and inappropriate measures for countries to introduce, how they should take into

2. Taxation Convention with Austria, July 20, 1996, U.S.-Austria, Memorandum of Understanding, *at* http://ftp.fedworld.gov/pub/irs-treaty/austria.pdf.

account the effects which their domestic law changes would have on other countries, and similar matters.

But I wouldn't put that structure in the form of a treaty with legally binding international commitments. Rather, the focus should be on a body in which countries can have some degree of assurance that, where they are accepting certain restrictions on their tax sovereignty, other countries will be taking the same steps. This is the classic prisoner's dilemma, or assurance game situation. But to think that we can get to, or need, the binding commitments which a treaty would entail, at least at this stage of the development of international cooperation, seems to me potentially to harm the whole exercise. Reliance on soft law, monitoring, and the recognition of mutual advantage are what should be stressed; not the existence of formal treaty obligations.

Let us look at what international cooperation, without binding commitments, has been able to accomplish to date:

- The Model Convention itself;
- The Transfer Pricing Guidelines;
- The 1998 Report on Harmful Tax Competition;
- The Financial Action Task Force Money Laundering Report; and,
- The Bank Secrecy Report.

All of these efforts are OECD sponsored initiatives. But they go beyond the OECD member countries and show the more flexible ways to structure developing international institutional organizations. For example, the Financial Action Task Force started out as an OECD body but then was "spun off" as an independent group with non-OECD members. There are other kinds of structures which could be considered to broaden the participation in these types of cooperative exercises.

Now in urging these kinds of cooperative efforts which will help preserve the income tax, I well may be siding with Ptolemy and simply tossing another epicycle into a fatally flawed system with the income tax at its center. Perhaps what we need is a paradigm shift; in which case our consumption tax Copernicuses may have it right. But in my view, the jury is clearly still out on that issue. Much thought has to be given to the steps which could be taken to preserve the income tax and the institutional framework in which those steps could be taken. I am not clear as to what the end of the process will be, but

the results which we have been able to accomplish to date are encouraging.