INTERNATIONAL TAXATION: THE INTERNATIONAL LAW PERSPECTIVE

ABSTRACT

This essay analyses International Tax Law from the perspective of an international lawyer. It examines early 20th century arbitral awards to reveal that the early jurisprudence on states' jurisdiction to tax did not develop in a systematic manner. Thereafter it traces the development of International Tax Law beginning with the efforts of the League and the subsequent role played by the Organisation for Economic Co-operation and Development. The importance of each of the two institutions is elaborated. While the League played a vital role in the founding phase of the ITL, the Organisation for Economic Co-operation and Development currently enjoys a pre-eminent status in setting the agenda of international tax policy. The role of the Organisation for Economic Co-operation and Development in addressing the current challenges in ITL – the issue of tax competition and a multilateral tax agreement is then examined before concluding.

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I. INTRODUCTION

International tax law (ITL) ordinarily only attracts the attention of tax lawyers. Scholarship on ITL generally studies it not as a discipline of international law but as a sub-discipline of tax law with international aspects.[1] The tax implications of transnational economic transactions and the inability of the current tax treaty structure to prevent tax evasion is a dominant concern in international tax scholarship.[2] The viewpoint of an international lawyer is amiss. In this essay, I show how international law can provide useful insights on ITL.

This essay examines the different aspects of ITL and is divided as follows: Section II discusses arbitral awards and cases dating back to the early 20th century with a view to examine the concept of jurisdiction to tax in international law. It is argued that jurisdiction can offer an alternate perspective to the sovereignty paradigm that currently dominates ITL scholarship. Section III examines the development of ITL – the initial efforts of the League of Nations (the League) and the role of the Organisation for Economic Co-operation and Development (the OECD) as the primary international organisation in ITL. Section IV looks at the current challenges in ITL – the issue of tax competition, the possibility of states signing a multilateral tax treaty and OECD's ongoing efforts to develop a multilateral tax treaty. Section V concludes.

II. JURISDICTION TO TAX

Early jurisprudence on the jurisdiction of a state to tax did not develop in a systemic manner but offers an interesting perspective on tax. In *Brewer, Moller & Co* case, the claimants paid taxes on their warehouses. The taxes were assessed against them by the municipality of San Cristóbal in the Republic of Venezuela. Subsequently, the claimants sought to recover the amount paid as taxes by

[1] See generally Diane M. Ring, 'The Promise of International Tax Scholarship and its Implications for Research Design, Theory and Methodology' (2010) 55 Saint Louis Univ L J 307.
[2] See, for instance, Peter Harris, David Oliver, *International Commercial Tax* (Cambridge University Press 2010).

challenging the actions of the municipal council – they argued that the taxes were irregular and illegal. The umpire held that there is no ground to sustain the claim and upheld the absolute right of a state to impose tax and further observed that it is very doubtful that the Republic of Venezuela could under any circumstances be held liable for the amount of irregular or illegal taxes collected by one of its municipal districts.[3] In *George Cook v United Mexican States*, the claimant's building was exempt from real estate tax under a statute that provided tax exemption for twenty years. However, before the passage of twenty years, the local municipality collected tax on claimant's building. The claimant paid the tax under protest and later challenged the authority of the state to revoke the tax exemption. The umpire rejected the claim and held that: 'In all cases relative to tax exemption it is necessary to bear in mind the generally accepted standards of construction. The right of the State to levy taxes constitutes an inherent part of its sovereignty; it is a function necessary to its very existence and it has often been alleged, not only in Mexico, but in the United States and other countries that legislatures, whether of states or of the Federation cannot legally create exemptions which restrict the free exercise of the sovereign power of the State in this regard.'[4]

In both the above discussed cases, the right of a state to levy tax was not only interpreted as integral to its sovereignty but it was also interpreted to be unfettered - without any exceptions.[5] This categorical position is incorrect and outdated. Imposing taxes is an important part of sovereign function but the state cannot wilfully act in breach of its own laws or its obligations under an international treaty without facing legal action. In a domestic court, the irregular or illegal tax will ordinarily be refunded. Recent jurisprudence and developments in international law do not support the decisions in *Brewer, Moller & Co* and the

[3] *Brewer, Moller and Co. Case*, (1903) X Reports of Int'l Arbitral Awards 423 (the umpire, however, did acknowledge that if the claimants were able to show that they were unlawfully classified because of their (German) nationality, the claim could be considered to have some merit).
[4] *George Cook v United Mexican States*, (1927) IV Reports of Int'l Arbitral Awards 217.
[5] Also see *Kügele v Polish State* (1932) 6 ILR 69 (the reported facts state that the claimant, a trader, owned a brewery in Upper Polish Silesia. As a result of a series of licence fees successively imposed by the authorities, the claimant's business ceased to be profitable and the claimant was eventually obliged to close it. The tribunal held that the trader did not lose his right to engage in a trade simply because tax (licence fee) increases led him to close his business. The conclusion in the award is questionable for if a right cannot be realised, it is effectively extinguished).

George Cook cases. For instance, if a promised tax exemption by a state is revoked, the state could either be held liable for breach of a contract or for violation of its obligations under an investment treaty.[6] In fact, the above mentioned awards are not only inconsistent with the recent developments in jurisprudence but they are also not supported by some of the other early 20th century rulings.

In the *Japanese House Tax* the dispute revolved around the settlements for foreign residents built in the Japanese ports.[7] Foreign nationals had limited property rights in Japan and they held land under a lease in perpetuity signed with the government of Japan. A dispute arose about the scope of tax exemption extended to foreign nationals. Japan argued that it had the right to tax the buildings built on the land since the tax exemption extended only to the land. France, Germany and Britain on the other hand defended the absolute character of the tax exemptions. Japan's argument was premised on the fact that fiscal immunity to foreigners was a sovereign act of limited applicability and granting complete tax immunity would be akin to restricting it from performing a vital sovereign act.[8] The Permanent Court of Arbitration (PCA) rejected Japan's argument and held that the treaties not only protected the land but also building of any description constructed on the land from any taxes, charges or contributions.[9] This restrictive notion of jurisdiction to tax even though articulated in the context of specific treaties reflects a more nuanced view of the sovereign right to impose taxes. It is arguable whether Japan intended the tax exemption to extend to both - the buildings and

[6] The liability of the state would depend on factors such as the nature and duration of promised tax exemptions, the manner and circumstances of revocation of tax exemption. See, for instance, *Total S.A. v Argentine Republic* ICSID Case No. ARB/04/1 (Decision on Liability, 27 December 2010) (where Total argued that because Argentina retroactively withdrew the promised exemption from custom duties, it was liable for breach of its substantive obligations such as fair and equitable treatment under the investment treaty).
[7] *France, Germany and Great Britain v Japan* (PCA, Award of the Tribunal, 22 May 1905).
[8] The argument was, in part, based on the provisions of the Anglo-Japanese treaty. Article 18 of the Anglo-Japanese Treaty 1894 provided that: 'The several foreign settlements in Japan shall be incorporated with the respected Japanese Commune, and shall thenceforth form part of the general municipal system of Japan.'
[9] See Arnulf Becker Lorca, *Mestizo International Law A Global Intellectual History 1842-1933* (Cambridge University Press 2015) 171; Contemporary courts have also interpreted terms such as 'land' and 'lease' in tax disputes with a certain degree of elasticity. See *Maierhofer v Finanzamt Augsburg-Land* (Case C-315/10) [2003] ECR I-563 (the court held that even if the structure can be demolished any time within ten days, it still constitutes an immovable property for tax purposes. There was no need for the structure to be inseverably fixed to or in the ground.); *Cottage Holiday Associates Ltd v Customs and Excise Comrs* (Case C-269/00) [1983] QB 735 (where the court held that use of holiday cottage for one week a year over an 80 year period was a legal lease.). Both cases were decided under the UK Value Added Tax Act, 1994.

the land. However, the court in rejecting Japan's argument did endorse a qualified sovereign right to tax; the ability of a state to impose a tax liability can be lawfully restricted once it voluntarily agrees to narrow its jurisdiction to tax.

A state has complete authority to impose taxes in the territory under its control but once it waives its right to tax a certain category of economic activity or a certain class of persons - it cannot revoke it without a valid reason or without paying compensation to the affected persons.[10] Consequently, a permanent loss of territory would entail a permanent loss of right to tax but, if a state loses and then regains control over a territory, its authority to impose taxes for the intervening period becomes questionable. In the *Guastini* case, the umpire held that the legitimate government when back in power cannot enforce a second payment of taxes once paid to revolutionary authorities.[11] From May 1898 to May 1900, the Venezuelan government had lost control over large portions of its territory to the Matos revolutionaries. During these two years, the residents and businessmen in the territories controlled by revolutionaries, paid taxes to them. The Venezuelan government on regaining the territory sought to levy taxes on the people - even for the time period it did not have control over the territory. The retrospective imposition of taxes by the Venezuelan government was challenged. The umpire observed that when the revolutionaries were in control of the territory, they were, for that time period the de facto government.[12] The umpire concluded that if the person running his business in that territory paid his taxes to the revolutionaries he cannot be forced to pay the taxes again once the government regains control of the territory.

The above mentioned awards suggest that in early 20th century, tribunals and courts failed to articulate the limitations on the state's jurisdiction to tax in a systematic or a cohesive manner. The inconsistency in the above mentioned decisions and arbitral awards is not surprising. The issues that the courts and tribunals were required to adjudicate on were still pre-dominantly domestic in nature and the claims were based on different legal instruments.[13] Moreover, the

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[10] See *John B. Okie (U.S.A.) v United Mexican States* (1926) IV Reports of Int'l Arbitral Awards 54, at 55-57.
[11] *Guastini Case (Italy v Venezuela)* (1903) X Reports of Int'l Arbitral Awards 561.
[12] *Ibid*.
[13] It is also possible to suggest that the different outcomes are a result of the disputes being adjudicated under different legal instruments and thus there may actually be no inconsistency. However, the observations of the

awards did not involve contemporary international problems of sharing of tax revenues between two or more states or two states simultaneously exercising tax jurisdiction over the same economic transaction. While there was never an occasion to apply international law directly, at no point do any of the tribunals or umpires refer to customary norms, state practice or general principles of law to decide the disputes. For instance, in the *Japanese House Tax* case where there was an occasion to refer to international norms – the arbitral tribunal did not mention them.

Nonetheless, the above mentioned awards and decisions, reveal the lack of certainty in ITL and also the inadequacy of general international law in taxation matters.[14] It is in part due to the limitations of international law, that the varied opinions on the extent of state jurisdiction have not yet been settled conclusively. There is no unanimity on how to address simultaneous state claims of jurisdiction to tax, especially outside the tax treaty network. In so far as disputes are within the scope of tax treaties, a fragile consensus exists that the state's power to tax is not unqualified in nature but there is no agreement beyond this general proposition. Also, there is lack of meaningful co-operation among the states in ITL. A number of contemporary scholars tend to view this aspect of ITL as the 'sovereignty problem.' Sovereignty is either dismissed as irrelevant in a globalised world or its importance in taxation matters is emphasised. The former view suggests that in an inter-connected world the importance and role of states is diminishing and thus sovereignty is irrelevant in international law including taxation.[15] The latter view suggests that sovereignty is not only important but also the biggest hurdle in resolving international tax issues.[16] The debate on the exact

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tribunal in *Brewer, Moller & Co*. and *George Cook* are categorically in favour of an absolute sovereign right to tax unlike in the *Japanese House Tax* case and the *Guastini* case which recognised a more limited right to tax. In my view, it is doubtful if the inconsistency arises merely because different legal instruments were involved. The tribunals endorsed different views on the limitations of a state's right to tax.

[14] See generally Asif H. Qureshi (ed.), *Public International Law of Taxation: Text, Cases Materials* (Kluwer Law International 1994).

[15] See generally Philip Genschel, 'Globalization and the Transformation of the Tax State' (2005) 13 European Rev 53; Also see Insop Pak, 'International Finance and State Sovereignty: Global Governance in the International Tax Regime' (2010) 10 Annual Survey of Int'l & Comp L 165.

[16] See, for instance, Ronen Palan, 'Tax Havens and the Commercialisation of State Sovereignty' (2002) 56 Int'l Org 151.

role of sovereignty in ITL is ongoing and unsettled;[17] but it should not prevent us from examining the role of state jurisdiction to tax. The sovereignty-centric approach should, in my view, be supplemented with a focus on scope of state jurisdiction to tax.

III. DEVELOPMENT OF ITL

A. The League as a Trailblazer

In 1919, the newly founded International Chamber of Commerce (ICC) began efforts for international co-operation to reduce double taxation.[18] In 1920, the Brussels International Financial Conference also passed a resolution suggesting that the League undertake a study on the issues of capital flight, tax evasion and double taxation.[19] In 1921, the League commissioned an expert report from its Financial Committee. The Committee further entrusted the task of preparing a theoretical report on double taxation to four economists.[20] In 1922, the Financial Committee delegated the task of studying double taxation to a group of tax administrators and requested a report from a practical and an administrative viewpoint.[21] The four economists prepared and submitted a report in 1923.[22] The tax administrators submitted their report in 1925.[23] The 1923 report adopted the criteria of economic allegiance which it contended was based on taxpayer's ability

[17] See Diane M. Ring, 'What's at Stake in the Sovereignty Debate?: International Tax and the Nation-State' (2008) 49 Virginia J Int'l L 155.

[18] In 1920, the Organisation Meeting of the ICC in Paris considered international double taxation to be one of the most important items on its agenda. See Michael J. Graetz, Michael M. O'Hear, 'The "Original Intent" of US International Taxation' (1997) 51 Duke L J 1021 (stating that the role and contribution of the ICC in ITL is often ignored); Also see Stefano Simontacchi, *Taxation of Capital Gains under the OECD Model Convention* (Kluwer Law International 2007) 1-10.

[19] See Louis W. Pauly, 'International Financial Institutions and National Economic Governance: Aspects of the New Adjustment Agenda in Historical Perspective' in Marc Flandreau, Carl-Ludwig Holtfrerich, et al. (eds.), *International Financial History in the Twentieth Century System and Anarchy* (Cambridge University Press 2003) 239.

[20] The four economists were called 'Academic Experts.' Their names were: Gijsbert Bruins, Luigi Einaudi, Edwin Seligman and Josiah Stamp.

[21] The tax administrators were from seven different European states: Belgium, Czechoslovakia, France, Great Britain, Italy, Netherlands and Switzerland.

[22] League of Nations, *Report on Double Taxation submitted to the Financial Committee by Professors Bivens, Einavai, Seligman and Sir Josiah Stamp*, Doc. E.F.S.73.F.19 (1923) (hereinafter 1923 report).

[23] League of Nations, *Report and Resolutions submitted by the Technical Experts to the Financial Committee of the League of Nations*, Doc. F. 212 (1925) (hereinafter 1925 report).

to pay.[24] The report's recommendations favoured the capital exporting or the resident states.[25] The 1925 report, which in part relied on the 1923 report, recommended that due to imbalance in the capital movements between the states the jurisdiction to tax should be shared between the source and the resident states. The 1925 report refrained from offering a single solution to double taxation and stated that in the case of impersonal taxes/scheduler taxes[26] the idea of origin is important while in the case of personal taxes (tax on income or capital) the idea of domicile is of importance.[27]

After the recommendations contained in the 1925 report were accepted by the League, the Fiscal Committee then requested the tax administrators/technical experts to prepare preliminary Model Conventions on the basis of the 1925 report. The technical experts issued a report in 1927 which inter alia contained four Model Conventions along with commentaries: Bilateral Convention for the Prevention of Double Taxation in the Special Matter of Direct Taxes dealing with Income and Property Taxes, Bilateral Convention for the Prevention of Double Taxation in the Special Matter of Succession Duties, Bilateral Convention on Administrative Assistance in Matters of Taxation and a Bilateral Convention on Judicial Assistance in the Collection of Taxes.[28] The 1927 report also mentioned that bilateral tax treaties were preferable to a multilateral treaty for: 'the fiscal systems of the various countries are so fundamentally different that it seems at present practically impossible to draft a collective convention, unless it were worded in such general terms as to be of no practical value.'[29]

In 1928, the League called for a General Meeting of government experts to discuss the 1927 report. The General Meeting recommended certain changes and prepared three versions of the first 1927 Model Convention. The three Model Conventions

[24] See 1923 report, *supra* note 22; Also see Peter Harris, David Oliver, *supra* note 2, at 43-86 (discussing that the principle of economic allegiance principle is not related to the ability of a taxpayer to pay but the territory from which benefits are derived); K Vogel, 'Worldwide vs. Source Taxation of Income: A Review and Re-evaluation of Arguments (Part I)' (1988) 16 Intertax 216.
[25] 1923 report, *supra* note 22, at 22.
[26] The scheduler taxes were common in Europe during the early 1900s. Under the scheduler system, tax was imposed on different kinds of income classified under the 'schedule' of the relevant tax law.
[27] 1925 report, *supra* note 23, at 8.
[28] League of Nations, *Report submitted by the Committee of Technical Experts on Double Taxation and Tax Evasion* Doc. C. 216.M.85.1927.II (1927)(hereinafter 1927 report).
[29] *Ibid*, at 26.

prepared in 1928 were – 'Bilateral Conventions for the Prevention of Double Taxation in the Special Matter of Direct Taxes', No. 1*a*, 1*b* and 1*c*.[30] The General Meeting of 1928, in a sense, marked the end of the most influential period of the efforts made by the League. The Model Conventions that were prepared and the reports that were submitted during the period of 1923-1928 laid a very strong foundation of the ITL regime. They continue to influence the texts of the modern day tax treaties. However, the efforts of the League continued thereafter.

The League played a leading role in laying the foundations of modern ITL. The approach of the League has influenced the content and nature of ITL in multiple ways, I shall emphasise two that are relevant to the aim and scope of this thesis – the emphasis on bilateral instruments and the use of Model Conventions. The League recognised the impracticability of formalising a multilateral tax agreement and did not spend too much time or effort in persuading states to adopt a multilateral instrument. The League understood the importance of bilateral approaches in international tax and laid the foundation for 'hegemony of bilateral instruments' in ITL.[31] The reports submitted to the League stated that the dissimilarities in the tax laws of different states were a reason for the impracticality of a multilateral tax treaty.[32] But, the League also realised the importance and advantages of bilateral relations in ITL. It noted that the constant extension of the network of tax treaties was due to their 'cumulative effect.'[33] Each time a new clause was incorporated in the Model Convention it was included in the subsequent treaties and states which had entered into treaties earlier sought to amend their treaties.[34] Bilateral relations between states helped in constant evolution of ITL in its early stages. The frequent amendment of treaties would have been difficult if a multilateral approach was adopted because of the need to convince a larger number of states. Undue emphasis on multilateral

[30] League of Nations, *Report presented by the General Meeting of Government Experts on Double Taxation and Tax Evasion* C.562.M.178.1928.II (1928) (the League mentioned that the first Model Convention proposed in 1927 applied to states which levied impersonal tax and a general personal tax. The two additional versions prepared in 1928 were intended to apply to states which did not distinguish between personal and impersonal taxes).
[31] Maria Amparo Grau Ruiz, *Mutual Assistance for the Recovery of the Claims* (Kluwer Law International 2002) 104-115 (describing the presence of huge number of bilateral tax treaties as 'the traditional hegemony of bilateral instruments').
[32] See, for instance, 1927 report, *supra* note 28.
[33] *Ibid*.
[34] *Ibid*.

approach in the founding phase of ITL would have impeded its progress and development. The League wisely emphasised on bilateral relations.

The approach adopted by the League was to a large extent successful in addressing the issue of international double taxation. However, the stability and success of the initial efforts in ITL contains the 'seeds of its own undermining.'[35] Thomas Rixen argues that the narrow focus on preventing double taxation led to the problem of international tax evasion and tax competition that acquired prominence in late 1990s.[36] He further suggests that while the League did foresee the problem of tax avoidance and evasion, it did not give it a priority at the time of establishment of ITL.[37] Thus, in a way the founding phase of the ITL regime contributed to surfacing of the problem of tax evasion and tax competition addressed by the OECD from 1996 onwards.[38]

Rixen's observations are important to understand the difficulty of changing international tax rules. The efforts of the League certainly laid the foundation of ITL and provided a certain measure of continuity and predictability to the ITL regime; it helped to partially overcome the earlier patchwork of arbitral awards and uncertain rules. The compromise between the source and the residence principle in the Model Conventions has, by and large, survived for more than eight decades. But, it is also possible to mistakenly believe that the stability is due to adequate rules. Thomas Rixen suggests that path dependency and inability of states to bring a meaningful change could in fact be the reasons for the continuity and stability of ITL and the continued inability of ITL to successfully address tax competition.

B. The OECD – Primary Standard-Setter since 1963

[35] Thomas Rixen, 'From Double Tax Avoidance to Tax Competition: Explaining the Institutional Trajectory of International Tax Governance' (2010) 18 Rev Int'l Pol Eco 197, at 197.
[36] See Thomas Rixen, Philipp Genschel, 'Settling and Unsettling the Transnational Legal Order of International Taxation' in Gregory Shaffer, Terence C. Halliday (eds.), *Transnational Legal Orders* (Cambridge University Press 2015) 154.
[37] Thomas Rixen, *supra* note 35, at 205.
[38] For a detailed discussion on tax competition see Section IV.A below.

The Organisation for European Economic Cooperation (OEEC) was created by 18 members in 1948 under the Marshall Plan.[39] In 1956, it organized its own Fiscal Committee to address double taxation.[40] The OEEC was recreated as the OECD in 1961 with the addition of United States and Canada as members.[41] Even under OEEC's new avatar as the OECD, the work on international taxation continued and its first major success in ITL was in 1963 - the publication of the non-binding OECD Model Convention (OECD Model).[42]

The OECD Model is a modern day successor of the 1927 Model Conventions drafted by the League. The structure of the Model Convention and its contents - the compromise between the residence and source principle – were borrowed from the earlier work of the League. The OECD Model, however, retained the London Model Convention's bias of greater share of revenue for the residence states.[43] In 1977, relying on the tax treaties concluded during the intervening period and after receiving feedback from the states, the OECD published an updated final version of the Model Convention.[44] The OECD Model Convention has been relied on by the states to conclude bilateral tax treaties and has proved to very influential.

One of the reasons for the continued and almost unchallenged influence of the OECD Model is due to lack of any viable alternatives. There were unsuccessful efforts at the regional levels to publish alternative Model Conventions.[45] The Latin American Free Trade Association (LAFTA) in 1976 adopted criteria for avoidance of

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[39] For details on OECD's early history see Robert Wolfe, 'From Reconstructing Europe to Constructing Globalization: The OECD in Historical Perspective' in Rianne Mahon, Stephen McBride (eds.), *The OECD and Transnational Governance* (UBC Press 2008) 77.

[40] Some authors have suggested that the OEEC constituted the Fiscal Committee at the insistence of the ICC since the UN was unable to offer effective leadership in international tax policy after dissolution of the League; *Ibid*.

[41] The goals of the OECD were also reformulated and were no longer confined to the Marshall Plan. See Art 1, OECD Convention (inter alia providing that the aims of the OECD is to contribute to expansion of world trade, sound economic expansion in member and non-member states).

[42] See generally Jeffrey Owens, 'The Main Differences between the OECD and the United Nations' Model Conventions' in Richard Vann (ed.), *OECD Proceedings. Tax Treaties. Linkages between OECD Member Countries and Dynamic Non-Member Economies* (OECD 1996).

[43] *Ibid*.

[44] The OECD Model Convention has since been regularly updated – the first update was in 1994 and the latest in 2010.

[45] UN, Department of Economic & Social Affairs, *United Nations Model Double Taxation Convention between the Developed and Developing Countries* (2001) ST/ESA/PAD/SER.E/21 xix (hereinafter UN Model Convention).

double taxation between LAFTA member states and states outside the region.[46] The alternate Model proposed by LAFTA did not gain traction because the OECD member states refused to sign treaties based on the LAFTA Model.[47] Currently, there are only two other Models that exist apart from the OECD Model – the UN Model and the US Model. The UN Model, first published in 1980, is essentially designed to be used for negotiating and entering into tax treaties with developing states. The fundamental principles contained in the UN Model are similar to the OECD Model. The vital difference is the greater share of taxes for the source state in the UN Model. In this respect, the UN Model is based on the Mexico Model Convention.[48] The drafting of the US Model was inspired more by the desire of US to aggressively protect its fiscal powers.[49] The fact that US adopts a unique worldwide taxation system which imposes taxes on citizens irrespective of their place of residence probably also contributed to its efforts to develop a separate model for itself.[50] Instead of providing an alternate to the OECD Model, the UN Model and the US Model in fact underline the influence of the OECD Model.[51]

In addition to the wide influence of the OECD Model Convention, OECD's manner of working has also contributed to its success in shaping ITL. The OECD either adopts recommendations or binding decisions. Recommendations are non-binding agreements that generally represent policy advice and member states generally use recommendations as a means to influence domestic policy and/or as a precursor to a decision. Member states arrive at decisions with consensus.[52] The decisions are binding on the member states though there are no known cases of

[46] The Commission of the Cartagena Agreement also adopted a Model Convention to prevent double taxation within the Andean group. *Ibid*, at xx.
[47] See Thomas Rixen, Philipp Genschel, *supra* note 36.
[48] *Supra* note 42.
[49] See generally Reuven S. Avi-Yonah, 'Who Invented the Single Tax Principle?: An Essay on the History of U.S. Treaty Policy' (2014) 59 NYL School L Rev 309; Also see P.D. Reese, 'United States Tax Policy Towards Developing Countries' (1987) 35 UCLA L Rev 369.
[50] Surrey S. Stanley, 'United Nations Group of Experts and the Guidelines for Tax Treaties between Developing Countries' (1978) 19 Harvard Int'l L J 1.
[51] See Michael Kobetsky, *International Taxation of Permanent Establishments Principles and Policy* (Cambridge University Press 2011) 152-178.
[52] Art 6, OECD Convention (requires consensus for adoption of Recommendations and Decisions, though members may abstain and thereby enter the equivalent of a reservation); For a criticism of OECD's consensus approach see Hugh Ault, 'Reflections on the Role of the OECD in Developing International Tax Norms' (2009) 34 Brook J Int'l L 757, at 763 ('… if a country A says the world is flat and country B says the world is round, after a long discussion, the OECD issues a report that says the world is an attractive shape and declares a consensus has been reached...').

the OECD imposing sanctions for noncompliance. One of the means through which the OECD has been able to achieve consensus among its member states is through peer review.[53] Peer review is extensively used at the OECD for it 'has been facilitated by the homogeneous membership and the high degree of trust shared among the member countries.'[54] The membership of the OECD makes it a unique international organisation. It is more diverse than other regional groupings like the North American Free Trade Association (NAFTA) but less diverse than the UN.[55]

It is a reflection of OECD's uniqueness that that the standards articulated by the OECD are neither utopian in nature nor a mere re-statement of the existing national practices of its various members.[56] The standards set by the OECD are generally incorporated and adhered to by the member states. JC Sharman observes that the 'very process of having its principles adopted as 'the international standard' by other international institutions simultaneously strengthens and disguises the OECD's policy influence'.[57] There are various reasons for the success of the OECD in ITL – first, the OECD effectively became the successor organisation to the League. It benefitted from the earlier pioneering work done by various experts and administrators and consolidated their efforts. The most visible source of benefit is the OECD Model Tax Convention. Second, in 1955 when the OECD (then OEEC) began working on ITL, a significant number of tax treaties had already been signed by the states. Thus, the principles proposed in the Model Conventions of the League had begun to be accepted by the states. The OECD benefitted from the emerging state practice that had accepted the residence-source compromise formula contained in the tax treaties. Thus, in its initial efforts in ITL, the OECD could rely on the treaties in force and the increasing acceptance of the source-residence compromise and did not have to propose any radical new rules; unlike the League, it did not have to start from scratch.

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[53] Peer reviews are also adopted by other international organisations such as the Financial Action Task Force. See http://www.fatf-gafi.org/publications/mutualevaluations/?hf=10&b=0&s=desc%28fatf_releasedate%29

[54] Pagini Fabrizio, 'Peer Review: A Tool for Co-operation and Change' (2002) 1 Directorate of Legal Affairs OECD. SG/LEG, available at www.oecd.org

[55] See Rianne Mahon, Stephen McBride, *supra* note 39.

[56] See Anne-Marie Slaughter, 'The Real New World Order' (1997) 76 Foreign Aff. 183, at 196 (arguing that the next generation of international institutions are likely to look like Basel Committee and the OECD as they provide a forum for transnational problem-solving and harmonisation of national laws); Anne-Marie Slaughter, *A New World Order* (Princeton University Press 2004).

[57] See Rianne Mahon, Stephen McBride, 'Standardizing and Disseminating Knowledge: The Role of the OECD in Global Governance' (2009) 1 Eur Pol Sci Rev 83.

IV. CURRENT CHALLENGES OF ITL

A. Unregulated Tax Competition

In May 1996, an OECD Ministerial Communiqué stated the need to develop measures to counter the effects of harmful tax competition on investment and financial decisions.[58] Later in September 1996, Heads of States of the G-7 'strongly urge[d]' the OECD to vigorously pursue its work in the field of harmful tax competition.[59] In October 1996, the European Union (EU) issued a report on the development of tax systems in Europe.[60] The report endorsed the need to eliminate harmful tax competition and supported the need to work with the OECD.[61] Due to the above mentioned developments, the OECD began its harmful tax competition project.

In 1998, the OECD published a report that developed criteria to identify harmful tax competition and preferential regimes.[62] It was followed by subsequent related reports.[63] Even though OECD's reports were not binding on the non-member states, the OECD curiously adopted an unusually aggressive approach in its harmful tax competition project. In the 2000 report, the OECD listed a set of defensive measures that the member states may take against jurisdictions that do not co-operate to eliminate their harmful tax practices.[64] The targeted jurisdictions, identified as 'harmful', questioned the legitimacy of OECD's initiative and termed

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[58] Council of the OECD, Ministerial Communiqué (1996) OECD Observer I, at III; Also see Reuven S. Avi-Yonah, 'Globalization, Tax Competition and the Fiscal Crisis of the Welfare State' (2000) 113 Harv L Rev 1573, at 1603 (stating that Japan and France were primary movers for this initiative).
[59] Statement of G7 Finance Ministers and Central Bank Governors, at http://www.g8.utoronto.ca/finance/fm970920.htm
[60] Commission of the European Communities, *Taxation in the European Union Report on the Development of Tax Systems* (1996), COM (96) 546 Final.
[61] *Ibid*, at para 3.15.
[62] OECD, *Harmful Tax Competition: An Emerging Global Issue* (1998) (hereinafter 1998 Tax Competition Report).
[63] 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); OECD, *The OECD's Project on Harmful Tax Practices: the 2001 Progress Report* (2001) (hereinafter 2001 report); OECD, *The OECD's Project on Harmful Tax Practices: The 2004 Progress Report* (2004); OECD, *The OECD's Project on Harmful Tax Practices: 2006 Update on Progress in Member Countries* (2006); Also see www.oecd.org (the website contains other related press briefings, notes and presentations).
[64] See 2000 Report, *supra* note 63, at 24.

them as undue interference with their national tax sovereignty.[65] Later in 2000, a newly established organisation – the Centre for Freedom and Prosperity (CFP) - began lobbying the US Congress against participation in the OECD project.[66]

Partly as a result of extensive lobbying by the CFP, in May 2001, U.S. Secretary of the Treasury Paul O'Neill stated that: 'The United States does not support efforts to dictate to any country what its own tax rates or tax systems should be, and will not participate in any initiative to harmonize world tax systems. The United States simply has no interest in stifling the competition that forces governments – like businesses—to create efficiencies.'[67] The statement is widely believed to have contributed to undercutting OECD's efforts and marked an effective end to the OECD project.[68] Thereafter, the OECD narrowed the focus of its efforts and concentrated on increasing transparency in jurisdictions and began stressing on better exchange of tax-related information between states to curb international tax evasion.[69]

Given the original aims and the actual achievement – the OECD harmful tax competition project is widely (and correctly) believed to be a failure. The project nonetheless, due to its timing and the approach of the OECD was an important development in ITL. I argue that OECD's harmful tax competition project significantly shifted the nature and trajectory of ITL. Additionally, I also suggest that the harmful tax competition project has altered OECD's approach and its position in international tax policy.

To begin with, due to harmful tax competition, the focus in ITL since 1998 has been decisively re-directed from prevention of international double taxation to prevention of tax evasion. In the 1927 report, the League had emphasised on the importance of the principle - that incomes should be taxed once.[70] But prevention of tax evasion became ancillary to the goal of preventing double taxation.

[65] See 2001 Report, *supra* note 63.
[66] See Robert Goulder, 'New Coalition Strikes Back at OECD Tax Havens Campaign' (2000) 21 Tax Notes Int'l 2650; For more details see http://freedomandprosperity.org/
[67] A copy of the Treasury press release is available at http://www.treasury.gov/press/releases/po366.htm
[68] The inability of the OECD to convince some of its own member states to cease harmful tax practices in their jurisdictions was also a major contributing factor. See Thomas F. Field, 'Tax Competition in Europe and America' (2003) 29 Tax Notes Int'l 1235.
[69] See 2001 Report, *supra* note 63.
[70] 1927 report, *supra* note 28, at 23.

Provisions relating to exchange of tax information were included in the tax treaties, but tax evasion was effectively relegated to the domestic sphere – the fight against it was perceived to be the individual responsibility of national tax authorities. Also, the League and the states could not contemplate the importance that intangibles such as intellectual property would acquire in international taxation.[71] The shift of the focus towards preventing international tax evasion was evident when in 2002 the OECD released a Model Tax Convention on Tax Information Exchange. Since 2002, various states have entered into standalone bilateral tax information exchange agreements based on the aforementioned Model. The OECD has also launched a Base Erosion and Profit Shifting (BEPS) project with a view to address international tax evasion comprehensively. The BEPS project was launched in 2013 and the OECD has since released comprehensive reports detailing the changes required to curb international tax evasion.[72] Thus, while the period from 1923-1998 witnessed primacy being given to curb international double taxation, the period from 1998 onwards can be characterised where international tax evasion is the dominant concern in ITL.

B. Multilateral Tax Agreement – A Work in Progress

To overcome the difficulty of achieving multilateral consensus on international tax, some scholars have even suggested to look beyond the usual treaty mechanisms.[73] Additionally, it has been suggested that states need to begin with multilateral agreements that focus on specific substantive areas that demand multilateral solutions.[74] The latter approach is evident in the recent initiative of the OECD – Developing a Multilateral Instrument to modify Bilateral Tax Treaties.[75] A multilateral tax instrument is being developed as part of the BEPS project and OECD's aim is to implement treaty measures to eliminate BEPS.

[71] Intangibles like patents, trademarks constitute an important part of international tax evasion due to the ease with which they are re-located in different jurisdictions.
[72] The reports are available at: http://www.oecd.org/ctp/beps-about.htm
[73] Adam H. Rosenzweig, 'Thinking Outside the Tax Treaty' (2012) Wisc. L Rev 717; Allison Christians, 'Getting to Yes? Thoughts on a BATNA for International Tax' (2013) Wisc. L Rev Online 7.
[74] See Diane M. Ring, 'Prospects for a Multilateral Tax Treaty' (2001) 26 Brooklyn J Int'l L 1699; John Azzi, 'Tackling Tax Treaty Tensions: Time to Think about an International Tax Court' (1998) 52 Bull'n Int'l Fiscal Doc 344, at 349.
[75] OECD, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties* (2014) (a report endorsed by the G-20, which concluded that a multilateral instrument is desirable and feasible).

The BEPS project is the second time the OECD is extensively campaigning for a binding multilateral instrument after the MAI. The aim, the OECD claims, is to prevent the current tax treaty network from facilitating BEPS.[76] It is a novel approach as the aim is to facilitate a targeted multilateral tax instrument. Such an approach helps to circumvent the hurdles in negotiating an 'all encompassing' multilateral treaty.[77] The OECD has been careful to suggest that the proposed instrument will not be binding on any state and it needs to be accepted voluntarily by the states. Further, the OECD has claimed that the multilateral treaty will 'complement and co-exist with bilateral tax treaties.'[78] The OECD in its attempt to form a multilateral tax treaty is underappreciating the nature of *quid pro quo* provisions contained in various bilateral tax treaties.[79] While the OECD has emphasised that it seeks to harmonise only 'BEPS-related' provisions in bilateral tax treaties – it remains to be seen how the OECD will segregate the BEPS related provisions of tax treaties from the non-BEPS related provisions. The OECD has presently not identified the criteria to differentiate BEPS-related provisions from other provisions. However, if a multilateral instrument with a narrow scope is signed by several states, it will be a positive step in the development of ITL and may provide the template for future multilateral agreements in ITL.

V. CONCLUSION

ITL has a long and interesting history, more than two thousand tax treaties, an increasing number of tax information exchange agreements, soft law in the form of Model Conventions and yet it has, by and large, escaped the attention of international lawyers. This essay has attempted to provide the international law perspective on taxation. To begin with, there was a lacuna in international law with respect to state jurisdiction to tax. When the problem of international double taxation came to the forefront in the early 20th century, some aspects of the

[76] *Ibid*, at 16.
[77] See OECD, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 – Final Report* (2015).
[78] *Ibid*, at 24.
[79] One state can sign tax treaties with two different states with both containing different definitions of Permanent Establishment and different share of revenues for the source state and the residence state. Thus, provisions of tax treaties vary depending on the treaty partner.

lacuna were addressed. The League beginning from 1921 had to extrapolate certain principles from domestic tax laws and invite inputs from various states to formulate rules to prevent international double taxation. The tax treaties signed by states thereafter have to a large extent managed to combat international double taxation. However, bilateral tax treaties have been unable to address challenge of international tax evasion. The strong bilateral roots of ITL combined with the perceived proximity of taxation with sovereignty has prevented a truly multi-lateral solution from emerging. The OECD, the most prominent standard setter in ITL is, however, currently engaged in developing a multilateral tax instrument in order to prevent BEPS. Proposing a narrow and focused multilateral tax treaty may be a step forward in increasing co-operation of states in international tax.

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UNDERTAKING:

I confirm that this essay is my original work and has not been submitted for any other competition or publication.

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