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Tax Competition and the Ethics of Burden Sharing

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ARTICLE

TAX COMPETITION AND THE ETHICS OF BURDEN SHARING

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Abstract

Tax scholars have long suggested that tax competition should be mitigated because it reduces the collective revenues of countries, impairs their ability to redistribute wealth, and produces more regressive tax systems. Likewise, international organizations such as the Organization for Economic Co-operation and Development ("OECD") and the European Union increasingly move towards designing a global framework aimed at reducing tax avoidance and mitigating tax competition.

However, there is no comprehensive discussion on the costs that would arise from institutional reform designed to tackle tax competition. To the extent that any change in the international tax order will benefit some countries but also harm others, an ethical analysis of tax competition should include an examination of how to distribute the losses resulting from overall institutional reform. As international policy decisions tend to reproduce the present imbalance of the global power, the lack of an explicit discussion on how to share the costs arising from an institutional change might result in countries with less negotiating power bearing most of these costs.

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This Article introduces the costs side of curbing tax competition and offers four normative principles that can help illuminate how the burdens of reforming the current international tax regime should be shared among countries.

I. INTRODUCTION

Right and responsibility are commonly conceived of as two sides of the same moral coin. However, determining the existence of a right might not easily lead to who bears the responsibility to ensure it. It has long been argued that tax competition should be mitigated, as it results in more regressive national tax systems and impairs countries' capacity to redistribute wealth.[1] Scholars observe that tax competition undermines the autonomy of countries[2] and curtails national identity and democratic participation.[3] These consequences seem to suggest that countries which suffer the most have the right against the negative impacts of tax competition. A question should immediately follow: who ought to bear the responsibility of fulfilling these rights? Although an intuitive answer might point to the countries that presently engage in tax competition, a deeper examination of the institutional history of the existing international tax regime and a broader look at the background conditions of the global economy might suggest otherwise.

Any solution for curbing tax competition entails important consequences to all countries involved and generates winners and losers. Even if mitigating tax competition were to lead to collective benefits for most states, it would still create costs for others in the short run.[4] A normative analysis of tax competition should not be limited to the ethics of tax competition in itself. It also needs to include a broader ethical examination of how the losses resulting from institutional reform should be distributed among countries. This Article analyzes this question by borrowing from a similar discussion in the context of climate change. Since a reduction in carbon emissions involves opportunity costs relating to economic development and growth, the prospects of a global solution to tackle anthropogenic climate change have generated a number of philosophical questions about how the burden of a solution should be shared among nations.[5]

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1. Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1578–79 (2000).

2. PETER DIETSCH, CATCHING CAPITAL: THE ETHICS OF TAX COMPETITION 46–54 (2015).

3. Tsilly Dagan, *The Tragic Choices of Tax Policy in a Globalized Economy*, *in* TAX, LAW AND DEVELOPMENT 57, 63 (Yariv Brauner & Miranda Stewart eds., 2013).

4. *See* Allison Christians, *Spillovers and Tax Sovereignty*, 85 TAX NOTES INT'L 831, 833 (2017) (arguing that although all countries may stand to lose from tax competition, all countries may equally stand to lose from curbing tax competition, depending on how tax competition is defined and how it is to be regulated); Ilan Benshalom, *The New Poor at Our Gates: Global Justice Implications for International Trade and Tax Law*, 85 N.Y.U. L. REV. 1, 79 (2010) (noting that unlike the developed countries, which stand only to gain from effective tax coordination, developing countries may fear to enter such a cooperative scheme because the short-term costs may outweigh the long-term (speculative) benefits").

5. For a comprehensive collection of essays on the topic, see CLIMATE ETHICS: ESSENTIAL READINGS (Stephen Gardiner et al. eds., 2010).

Tax competition and climate change are similar in that they are both problems of collective action.[6] In collective action problems, all parties would benefit from a solution, but the associated costs make it implausible that anyone would undertake it individually.[7] The rational choice is to solve the problem cooperatively and share the costs.[8] Studies in climate change have extensively discussed the costs resulting from a collective solution, as well as criteria for an equitable distribution of these costs in a way that reflects the needs of developing countries in terms of poverty reduction and growth.[9] In contrast, debates on tax competition rarely acknowledge explicitly that a collective solution for tax competition will create costs for some countries while favoring others.[10] A look at the debates surrounding the efforts to mitigate climate change helps illustrate the different ethical perspectives on the burden sharing of curbing tax competition and

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6. *See* THOMAS RIXEN, THE POLITICAL ECONOMY OF INTERNATIONAL TAX GOVERNANCE 43–46 (2008) (analyzing tax competition as a collective action problem from a game-theoretical perspective). *See also* Elinor Ostrom, *Polycentric Systems for Coping with Collective Action and Global Environmental Change*, 20 GLOBAL ENVTL. CHANGE 550 (2010) (addressing climate change as a problem of global collective action and arguing that a combination of collective action theory and behavioral theory suggests approaches that might achieve a more effective solution).

7. RUSSELL HARDIN, COLLECTIVE ACTION 8 (1982).

8. Robert E. Goodin, *The Collective Action Problem*, *in* FAIR RESOURCE ALLOCATION AND RATIONING AT THE BEDSIDE 224, 224 (Marion Danis et al. eds., 2014).

9. Nicholas Stern, *What is the Economics of Climate Change?*, 7 WORLD ECON. 1, 6 (2006).

10. There are, however, notable exceptions. Peter Dietsch discusses a number of ethical questions arising from the implementation of a solution for tax competition. DIETSCH, *supra* note 2, at 188–218. Laurens Van Apeldoorn suggests that a solution for tax competition that disregards the different fiscal constraints faced by low-income and high-income countries will result in unequal (and unjust) levels of fiscal self-determination. *See* Laurens Van Apeldoorn, *BEPS, Tax Sovereignty and Global Justice*, CRITICAL REV. INT'L SOC. & POL. PHIL. 478, 487 (2016). Allison Christians emphasizes that curbing tax competition is not a win-win scenario for all jurisdictions and argue for the need of a fair normative framework. Christians, *supra* note 4. Martin Hearson argues that reforming international tax rules in a way that realizes equity among countries requires not only tackling tax competition, but also looking at the distributional impacts of those rules. Martin Hearson, *The Challenges for Developing Countries in International Tax Justice*, J. DEV. STUD.1932, 1936 (2018). Tsilly Dagan argues that the shift from competition to negotiated coordination produces unjust inequalities that derive from asymmetries in the relative bargaining power of the negotiating states and suggests that restricting tax competition might produce severe distributive effects on poor countries. TSILLY DAGAN, INTERNATIONAL TAX POLICY: BETWEEN COMPETITION AND COOPERATION 142–84 (2017).

Interestingly, discussions on climate change seem to suffer from the opposite deficiency. It has been argued that there is too little focus on the economic advantages of tackling climate change. Paul G. Harris, *Collective Action on Climate Change: The Logic of Regime Failure*, 47 NAT'L RESOURCES J. 195, 223 (2007).

offers possible alternatives for a fair distribution of costs resulting from institutional reform.

Part II provides an overview of how the changes in the global economy resulting from globalization have intensified policy competition between governments. It then introduces the problem of international tax competition and describes some of its potential negative consequences. Part III points to particular implications for developing countries and discusses some of the challenges and constraints they face in the global economy. Part IV examines normative questions involving what I call the rights side of curbing tax competition and introduces some theoretical developments in the literature aimed at justifying the need to tackle tax competition. Part V analyzes the costs side of the problem and argues that a just solution for tax competition requires an equal concern with fairness in the upshot of institutional reform. It then describes how a similar problem has been discussed in the context of climate change and outlines four normative principles that could independently or jointly guide the burden sharing of curbing tax competition: the responsible party pays principle, the retrospective beneficiary pays principle, the prospective beneficiary pays principle, and the ability to pay principle. The Article concludes by suggesting that the complexity of tax competition might require a combination of principles rather than the sole application of one of them and offers recommendations for further research.

II. GLOBALIZATION, THE COMPETITION STATE, AND INTERNATIONAL TAXATION

A. From the Welfare State to the Competition State: Globalization and Tax Competition

In recent decades, reduced costs of transportation and communication, combined with reduced policy barriers to trade and investment, have heavily facilitated cross-border investment.[11] Economic decisions are less and less constrained by national boundaries, as multinational corporations can easily shift capital and profits to any country where they operate.[12] As a political phenomenon,

11. Jeffrey Frankel, *Globalization of the Economy*, *in* GOVERNANCE IN A GLOBALIZING WORLD 45, 45–46 (Joseph S. Nye Jr. & John D. Donahue eds., 2000).

12. DANI RODRIK, THE GLOBALIZATION PARADOX 76–77 (2011).

globalization translates as a shift in the playing field of politics from isolated units (the state) to a multilayered, complex arena.[13] Governments are pressed to adapt to an intricate economic and political environment of international institutions, multinational corporations, and cross-border flows of all kinds.[14] To cope more effectively with the complex changes in institutional, cultural, and market structures, governments have reinvented themselves as quasi-market actors.[15] Since states cannot allow mobile capital to be driven away by the inadequate design of their institutions, government policies have shifted focus towards how domestic institutions influence the cross-border transfer of economic activities.[16]

Globalization puts countries under pressure to improve their attractiveness, since more competitive countries attract the influx of mobile factors—labor and capital—and leave other economies in a relatively inferior position, similar to competition between private firms.[17] However, the political economy literature suggests that, contrary to market competition, competition between governments is likely to fail in two respects. First, because governments mostly undertake economic activities that cannot be handled satisfactorily by markets, competition between states is likely to replicate the market failures that justified government intervention in the first place.[18] Second, government competition imposes an important shift in the focus of governmental politics away from the general maximization of welfare within a nation—particularly redistributive transfer payments and social service provision—towards the promotion of enterprise and profitability.[19] This shift tends to lead to what is known as a "race to

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13. *See* Philip G. Cerny, *Paradoxes of the Competition State: The Dynamics of Political Globalization*, 32 GOV'T OPPOSITION 251 (1997). *See also* DAVID HELD, DEMOCRACY AND THE GLOBAL ORDER: FROM THE MODERN STATE TO COSMOPOLITAN GOVERNANCE 92 (1995) ("[T]he meaning of national decision-making institutions today has to be explored in the context of a complex international society, and a huge range of actual and nascent regional and global organizations which transcend and mediate national boundaries.").

14. KATE NASH, CONTEMPORARY POLITICAL SOCIOLOGY: GLOBALIZATION, POLITICS, AND POWER 44 (2d ed. 2010).

15. Cerny, *supra* note 13, at 251.

16. HANS-WERNER SINN, THE NEW SYSTEMS COMPETITION 4 (2003).

17. Viktor Vanberg & Wolfgang Kerber, *Institutional Competition among Jurisdictions: An Evolutionary Approach*, 5 CONST. POL. ECON. 193, 204 (1994).

18. Hans-Werner Sinn, *The Selection Principle and Market Failure in Systems Competition*, 66 J. PUB. ECON. 247, 248 (1997).

19. Cerny, *supra* note 13, at 260.

the bottom," that is, a downward convergence of policies and practices that preclude adequate protection of the social and economic well-being of citizens, especially the poor.[20]

This phenomenon is typically seen in international taxation.[21] The increasing ease and volume of cross-border activity have shaped the international tax scene, as multinationals can choose among countries in which to locate investments and shop among potential host countries for the most attractive investment "package," which includes the tax regime as one important element.[22] Governments, in turn, aim their policies at attracting "both portfolio and direct investment by lowering their tax rates on income earned by foreigners."[23] On the one hand, nations have their tax revenues reduced by aggressive maneuvering of taxpayers and, on the other, each nation seeks to benefit by embracing behaviour, against other nations, intended to capture as much global capital as possible.[24]

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20. NITA RUDRA, GLOBALIZATION AND THE RACE TO THE BOTTOM IN DEVELOPING COUNTRIES: WHO REALLY GETS HURT? 3 (2008). Even some types of competition, such as strategic infrastructural investment, that might be considered beneficial because they tend to lead countries to a "race to the top" might be problematic in some cases for wasting more resources in local expenditures than would be reasonable or necessary. *See* DIETSCH, *supra* note 2, at 96–97, 101–02*; see also* Leon Taylor, *Infrastructural Competition among Jurisdictions*, 49 J. PUB. ECON. 241 (1992) (observing that if competition is long and involves many contestants, it can produce net social loss, especially in the case of identical jurisdictions that compete by building infrastructure with no alternative value).

21. Other forms of government competition include more relaxed rules for incorporation, banking regulations, environmental laws, and employment laws.

22. Michael C. Durst, *Poverty, Tax Competition, and Base Erosion*, 89 TAX NOTES INT'L 1189, 1194 (2018). *See* Philipp Genschel & Peter Schwarz, *Tax Competition: A Literature Review*, 9 SOCIO-ECON. REV. 339, 340–41 (2011) (explaining that, "for a long time, taxes were simply too low and cross-national tax differentials too small to trigger significant cross-border movements of taxpayers and bases," which changed in the twentieth century with the increase of tax burdens and the erosion of mobility barriers).

23. *See* Avi-Yonah, *supra* note 1, at 1575–76. *See also* Dagan, *supra* note 3, at 58 ("Competition provides taxpayers with an alternative: to shift either their capital, their residency, or even their citizenship, to another country. In the extreme case, tax competition changes taxation from the mandatory regime it used to be, to a regime that is basically elective, or more precisely, elective for some.")

24. Allison Christians, *Putting the Reign Back in Sovereign*, 40 PEPP. L. REV. 1373, 1375 (2013). *See* Tsilly Dagan, *International Tax and Global Justice*, 18 THEORETICAL INQUIRIES L. 1, 13–15 (2017) ("Competition increasingly is turning states into market players that offer their goods and services to potential 'customers.' In this market for sovereignty goods, states compete for capital and residents, while (at least some) individuals 'shop around' for sovereign-provided privileges, public goods, and social and cultural goods. . . . [T]he tax policymaking process has gradually transformed under competition, and states increasingly operate as recruiters of mobile

Tax policy decision-making and the relationship between state and its subjects are then reversed. Rather than making compulsory demands from its residents to promote collective goals, as traditional tax policy would, governments increasingly act as "recruiters" of residents and investments from the global arena.[25] Some see tax competition as a desirable process which creates locational efficiency[26] and produces gains for developing countries.[27] However, many tax scholars suggest that, by turning countries into competitive players, it undermines the focus on setting tax regimes optimally to promote normative goals.[28]

B. Negative Consequences of Tax Competition

The effects of tax competition are not zero-sum. They reduce the collective revenue of countries as taxable income is moved from high-tax to low- or no-tax jurisdictions, decreasing total tax payments.[29] As taxes represent the principal means for governments to allocate resources, the decrease in tax revenues directly affects the ability of states to provide citizens with services and benefits.[30] Tax scholars

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investments and residents from other states, while at the same time striving to retain their own residents and investments.").

25. Dagan, *supra* note 3, at 58.

26. Julie Roin, *Competition and Evasion: Another Perspective on International Tax Competition*, (2001) 89 GEO. L.J. 543, 570 (arguing that the harms of tax competition commonly associated with the disruption of the redistributive process have been exaggerated in several respects).

27. Michael Littlewood, *Tax Competition: Harmful to Whom?*, 26 MICH. J. INT'L L. 411, 445–48 ("[T]he shifted investment, although producing less tax revenue than in its original country, might nonetheless produce private benefits for its new host country—in forms such as wages, training, and technology transfer. . . . [T]here is no obvious reason to suppose that any undermining of tax equity in developed countries represents a loss greater than the gain made by developing countries.").

28. *See, e.g.,* Avi-Yonah, *supra* note 1; Dagan, *supra* note 3, at 63; DIETSCH, *supra* note 2.

29. INT'L MONETARY FUND, SPILLOVERS IN INTERNATIONAL CORPORATE TAXATION 14 (2014). In terms of macroeconomic policy, one country's domestic tax decisions may affect other countries' policies in different ways: by affecting growth and macroeconomic stability, due to the impacts of shift of real (foreign direct investments) and financial flows (corporate financing arrangements); by constraining the corporate tax base, as the reflection of changes in multinationals' investments decisions; by creating pressure to reduce tax rates, in response to lower tax rates abroad; and by modifying world prices, as tax policies affect investment and saving behavior, changing interest rates and wages around the globe. *Id.* at 12–13.

30. The tax literature has noted that the negative effects of tax competition on different countries vary significantly depending on country size, level of development, and level of

observe that countries have responded in two ways to tax competition. First, by shifting the tax burden from more mobile economic factors (such as business profits and capital income) to less mobile ones (mainly, wages and consumption),[31] and second, when the increase of taxation of labor has become politically and economically problematic, by reducing the social safety net.[32]

This means that tax competition can negatively affect tax equity in three different dimensions.[33] First, as the ability for relocating income facilitated by tax competition is mostly enjoyed by the rich, tax competition might hinder *vertical equity*, which requires that individuals with unequal incomes should be taxed differently, according to their abilities to pay.[34] As higher-income taxpayers contribute less to the tax burden than those with lower income, the burden tends to shift to the poor.[35] Moreover, since the tax and transfer system is traditionally conceived as the most powerful policy instrument for income redistribution,[36] tax competition can also impose adverse effects on vertical equity taken as a broader notion of distributing goods among residents according to their needs and capabilities, as it might reduce countries' tax revenues to concerning levels. Second, as the tax burden shifts from capital to labor, taxpayers with the same level of income, one from capital and the other from

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domestic institutional constraints. *See* Genschel & Schwarz, *supra* note 22, at 341–42; DIETSCH, *supra* note 2, at 55–61.

31. Alex Easson, *Fiscal Degradation and the Inter-Nation Allocation of Tax Jurisdiction*, 3 EC TAX REV. 112, 112 (1996); Diane Ring, *Democracy, Sovereignty and Tax Competition: The Role of Tax Sovereignty in Shaping Tax Cooperation*, 9 FLA. TAX REV. 555, 576 (2009); Allison Christians, *How Nations Share*, 87 INDIANA L.J. 1407, 1408 (2012); Thomas Rixen, *Tax Competition and Inequality: The Case for Global Tax Governance*, 17 GLOB. GOV. 447, 452 (2011). For a more detailed explanation, suggesting three distinct categories of taxpayers (the relatively "easy-to-tax," the relatively "hard-to-tax," and the virtually "impossible-to-tax"), see Allison Christians, *Drawing the Boundaries of Tax Justice*, *in* THE QUEST FOR TAX REFORM CONTINUES: THE ROYAL COMMISSION ON TAXATION FIFTY YEARS LATER 53, 72–76 (Kim Brooks ed., 2013).

32. Avi-Yonah, *supra* note 1, at 1576.

33. Laura Seelkopf & Hanna Lierse, *Taxation and Inequality: How Tax Competition Has Changed the Redistributive Capacity of Nation-States in the OECD*, *in* WELFARE STATE TRANSFORMATIONS AND INEQUALITY IN OECD COUNTRIES 89, 92–93 (Melike Wulfgramm, Tonia Bieber & Stephan Leibfried eds., 2016).

34. Anthony C. Infanti, *Tax Equity*, 55 BUFF. L. REV. 1191, 1200 (2008).

35. Seelkopf & Lierse, *supra* note 33.

36. RICHARD A. MUSGRAVE, THE THEORY OF PUBLIC FINANCE: A STUDY IN PUBLIC ECONOMY 18 (1959).

labor, are taxed differently.[37] This affects *horizontal equity*, according to which the same income should be taxed at the same rate, independently of its source.[38] Third, as countries have different sets of advantages and disadvantages in competing for capital and income, tax competition changes the income distribution not only within but also between countries involved. Because tax competition affects countries differently, it might worsen international inequality, precluding *inter-nation equity*—i.e., equity between countries.[39]

It has also been argued that tax competition undermines the autonomy of countries regarding the size of the public budget and the desired level of redistribution.[40] A country's taxing choices (what, who, and how much to tax) is classically based on political factors such as fairness and distribution of political power. Tax policy choices, however, depend not only on what the country wants to tax but also on what it *can* tax.[41] As tax competition pushes countries to lower their tax rates, it limits their fiscal policy choices and might curtail national identity and democratic self-determination.[42]

The risk of a "race to the bottom" in the tax competition scenario is evident. As investors can freely choose where to invest in the world, they choose the country with the most favorable tax regime. Governments, in turn, have the incentive to attract foreign capital by undercutting each other's tax rates. This race leads to mobile incomes being taxed less or not at all[43] and, some argue, results in the under-provision of public goods.[44] In terms of justice, tax competition tends

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37. Seelkopf & Lierse, *supra* note 33.

38. Infanti, *supra* note 34.

39. For an overview of the definition and importance of the concept of inter-nation equity, see Nancy H. Kaufman, *Fairness and the Taxation of International Income*, 29 L. & POL'Y INT'L BUS. 145 (1998); Jinyan Li, *Improving Inter-Nation Equity Through Territorial Taxation and Tax Sparing*, *in* GLOBALIZATION AND ITS TAX DISCONTENTS: TAX POLICY AND INTERNATIONAL INVESTMENTS 117 (Arthur J. Cockfield ed., 2010).

40. DIETSCH, *supra* note 2, at 46–54. *But see* David C. Elkins, *The Merits of Tax Competition in a Globalized Economy*, 91 INDIANA L.J. 905 (2016); Mitchell B. Weiss, *International Tax Competition: An Efficient or Inefficient Phenomenon?*, 16 AKRON TAX J. 99 (2001); Roin, *supra* note 26; Littlewood, *supra* note 27.

41. Richard M. Bird & Eric M. Zolt, *Tax Policy in Emerging Countries*, 26 ENV'T & PLANNING C: GOV'T & POL'Y 73, 75 (2008).

42. Dagan, *supra* note 3, at 63.

43. Seelkopf & Lierse, *supra* note 33, at 95.

44. *See* George R. Zodrow & Peter Mieszkowski, *Pigou, Tiebout, Property Taxation, and the Underprovision of Local Public Goods*, 19 J. URB. ECON. 356 (1986). For an overview of

to undermine the ability of states to maintain the necessary conditions for promoting justice and for providing their constituents with the assurances required for social cooperation.[45]

III. IMPLICATIONS AND CHALLENGES FOR DEVELOPING COUNTRIES

Compared to the developed world, developing countries face more significant tax policy constraints in an increasingly globalized world. Due to weak revenue administrative capacity, they have great difficulty in collecting enough tax revenues to support the desired level of expenditures.[46] Moreover, the average cost of collecting taxes in the developing world is substantially higher than in developed countries.[47] In this respect, commentators suggest that three potential constraints hinder the ability of developing countries to improve their tax administrations: the availability of funds, the domestic political will, and the speed with which capability can be built.[48] Developing countries with weak administrations also face major challenges from international outflows of capital and profits, as in many cases they are simply "unaware of the revenue they are losing."[49]

Inefficient tax administrations create additional difficulties for developing economies. First, the inability to effectively collect income tax hinders the tax and transfer system that support lower-income populations.[50] Second, taxpayer compliance costs (i.e., costs incurred by taxpayers to comply with tax regulations) in developing countries is often high compared to the developed world. Research suggests the average compliance costs in developing countries are four to five times higher than in developed countries,[51] discouraging investment and

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the baseline model of tax competition and some variations, see also Genschel & Schwarz, *supra* note 22.

45. Dagan *supra* note 24, at 4.

46. *See* Bird & Zolt, *supra* note 41, at 76 (explaining that, in principle, revenues should grow at the same rate as desired expenditures, but that emerging and developing countries hardly achieve this target, which leads to frequent tax reforms aimed primarily at closing short-term revenue gaps).

47. *Id*.

48. *See*, *e.g.*, Michael Carnahan, *Taxation Challenges in Developing Countries*, 2 ASIA PACIFIC POL'Y STUD. 169, 180 (2015).

49. *Id*. at 179.

50. Bird & Zolt, *supra* note 41, at 80 n.12.

51. *See* Roy W. Bahl & Richard M. Bird, *Tax Policy in Developing Countries: Looking Back—and Forward*, 61 NAT'L TAX J. 279, 291 (2008). *See also* INT'L MONETARY FUND,

impeding productivity and competitiveness.[52] Third, tax revenues in developing countries are quite low compared to the developed world. While the average tax revenue to GDP ratio in developed countries is approximately 35%, tax revenue in developing countries is approximately 15% of GDP, and in the poorest of these countries it is about 12%.[53]

An important factor affecting developing countries' tax systems is the substantial size of the informal economy. The literature suggests that the tax regime in developing economies can be split in two systems: one has relatively high tax-compliance rates and comprises medium and large corporations, which are subject to strict reporting requirements and keep relatively accurate records; the other is comprised of many small enterprises operating in great part in the informal sector, with low compliance rates.[54] Efforts to bring this sector into compliance are difficult and expensive.[55] Besides, a large informal sector makes it almost impossible to tax income consistently, which is problematic from an equity point of view. Furthermore, the elasticity of taxable income relative to the level of taxes is high, which means that when the government of a country with a large informal sector tries to raise taxes, the taxable income reported drops substantially.[56]

Another important challenge for developing countries is that the present international tax regime was designed in a way that favors richer nations. Today, most of bilateral tax treaties follow the OECD Model Tax Convention, which allocates more taxing rights in favour

REVENUE MOBILIZATION IN DEVELOPING COUNTRIES 21 (2011) (suggesting more modestly that while a typical firm spend 210 hours preparing and paying taxes in high-income countries, the time spent by firms in developing countries exceeds 300 hours).

52. Empirical research on tax compliance cost also shows significant regressivity in tax compliance costs in the developing world. Jacqueline Coolidge, *Findings of Tax Compliance Cost Surveys in Developing Countries*, 10 EJOURNAL TAX RES. 250, 256 (2012).

53. CLEMENS FUEST & NADINE RIEDEL, TAX EVASION, TAX AVOIDANCE AND TAX EXPENDITURES IN DEVELOPING COUNTRIES: A REVIEW OF THE LITERATURE 1 (2009), http://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Docs/Publications/Reports/TaxEvasionReportDFIDFINAL1906.pdf (last visited Sept. 26, 2018).

54. Bird & Zolt, *supra* note 41, at 80.

55. *Id*.

56. Timothy Besley & Torsten Persson, *Why Do Developing Countries Tax So Little?*, 28 J. ECON. PERSP. 99, 110 (2014). *See also* Ernesto Crivelli, Ruud De Mooij & Michael Keen, *Base Erosion, Profit Shifting and Developing Countries* 23 (Int'l Monetary Fund, Working Paper No. 15/118, 2015).

of capital-exporting countries (mostly, developed countries), at the expense of capital-importing countries (mostly, developing countries).[57]

Tax policy choices in many developing countries have also been limited by their reliance on foreign trade and investment and by the constraints imposed by outsiders, such as international lenders and major trading partners.[58] One important example is tax conditionalities required by international financial institutions to provide needed financial and technical support. Commentators argue that tax conditionalities imposed by the International Monetary Fund ("IMF") ignore domestic equity concerns by focusing solely on economic efficiency and administrative efficacy, and that the secretive and expert-driven process of tax conditionality is conducted by the IMF staff directly with a government or technical "elite," whose goals and values may differ from those of the country's population.[59]

Aside from these general tax policy constraints to developing countries, tax competition poses additional challenges to the world's poorest countries for three main reasons.[60] First, economists have long observed the dependence of developing economies on corporate income tax revenues as a share of all revenues. While in developed countries personal income tax revenues are often three to four times the corporate income tax revenues, in developing countries personal

57. Hearson, *supra* note 10, at 1936; KEVIN HOLMES, INTERNATIONAL TAX POLICY AND DOUBLE TAX TREATIES: AN INTRODUCTION TO PRINCIPLES AND APPLICATION 62–63 (2d ed. 2014). For a broader critical analysis of the contemporary structures of global tax governance, see Tarcisio Diniz Magalhães, *What Is Really Wrong with Global Tax Governance and How to Properly Fix It*, 10 WORLD TAX J. (forthcoming 2018).

58. *See* Allison Christians, *Global Trends and Constraints on Tax Policy in the Least Developed Countries*, 42 U.B.C. L. REV. 239, 274 (2010) ("Decisions made by and for the developed world about how to foster and encourage globalization through international tax policy limit the range of tax policy strategies available to the world's least developed countries.")

59. *See* Miranda Stewart & Sunita Jogarajan, *The International Monetary Fund and Tax Reform*, 2 BRIT. TAX REV. 146, 162-63 (2004). *See also* Christians, *supra* note 58, at 263 (observing that institutional assistance is available only to support tax policy strategies that are favored by the international community of finance experts); Richard M. Bird, *Foreign Advice and Tax Policy in Developing Countries* 15 (Int'l Ctr. for Public Policy, Working Paper No. 13-07, 2013), https://scholarworks.gsu.edu/cgi/viewcontent.cgi?article=1037&context=icepp [https://perma.cc/MHC8-A2WW] (last visited Sept. 26, 2018) (suggesting that, at least to some extent, such tax policies were accepted because they coincided with elite interests).

60. INT'L MONETARY FUND, *supra* note 29, at 7.

income tax revenues are often lower than corporate income revenues.[61] Revenues from personal income tax in developing countries amount to only one to two percent of gross domestic product ("GDP"), compared with nine to eleven percent in developed countries.[62] As tax competition is primarily driven by corporate tax cuts, fiscal performance in developing countries is significantly more vulnerable to pressures from tax competition.[63] Studies suggest that developing countries might lose from tax competition three times as much as they receive in development aid.[64]

Second, developing countries are also more vulnerable to tax competition because of tax-sensitivity of firms. Some studies indicate that multinationals' investment and profit levels in developing countries are more sensitive to taxation than in the developed world, making them more vulnerable to increasing capital mobility.[65] Indeed, while the global decrease of corporate tax rates has not significantly affected corporate tax revenues in developed countries(both as a share of GDP and as a share of total tax revenues), it has considerably reduced corporate tax revenues in some of the poorest and most vulnerable of the developing countries.[66] Third, in the tax competition scenario, some types of tax incentives are likely to be more successful than others in attracting investments and generating benefits for the host country.[67] Since designing effective tax incentives is already a challenge for well-resourced tax administrations in developed countries, the likelihood for serious revenue leakages and negative consequences in developing countries is much greater.[68]

61. Richard M. Bird & Eric M. Zolt, *Redistribution via Taxation: The Limited Role of the Personal Income Tax in Developing Countries* 52 UCLA L. REV. 1627, 1656 (2005).

62. Carnahan, *supra* note 48, at 176.

63. Reuven Avi-Yonah, *Globalization and Tax Competition: Implications for Developing Countries*, 44 L. QUADRANGLE NOTES 60, 63 (2001).

64. *See* DIETSCH, *supra* note 2, at 192.

65. FUEST & RIEDEL, *supra* note 53, at 40, 43.

66. Michael Keen & Alejandro Simone, *Is Tax Competition Harming Developing Countries More Than Developed?*, 34 TAX NOTES INT'L 1317 (2004).

67. Carnahan, *supra* note 48, at 177.

68. *Id*.

IV. THE RIGHTS SIDE OF CURBING TAX COMPETITION: FAIRNESS IN FISCAL SELF-DETERMINATION

As mentioned in Section II.B, tax competition tends to result in more regressive national tax systems, decreased capacity for redistribution of wealth, and reduced ability of the world's poorest countries to pursue sustainable development. This has led tax scholars to question whether limits should be imposed on the sovereignty of countries in designing domestic policies that, although beneficial for their constituents, may impose harms and constraints on other countries.[69] As tax competition undermines the autonomy of countries in determining their fiscal policies (i.e., in establishing their desired level of taxation and redistribution), it has been noted that governments must give up some of their *de jure* sovereignty (the legal right to design their tax systems) through cooperation if they want to retain *de facto* sovereignty (i.e., their ability to achieve policy goals).[70]

Contemporary conceptions of sovereignty suggest that it comprises two related ideas, one of autonomy and another of duty.[71] The right of a state to make autonomous choices (its *sovereign*

69. *See generally* Allison Christians, *Sovereignty, Taxation and Social Contract*, 18 MINN. J. INT'L L. 99 (2009); Ring, *supra* note 31; Peter Dietsch, *Rethinking Sovereignty in International Fiscal Policy*, 37 REV. INT'L STUD. 2107, 2117 (2011).

70. *See* Rixen, *supra* note 31, at 448. *See also* Easson, *supra* note 31, at 112 (explaining that the apparent defense of national fiscal sovereignty has brought about a real loss of sovereignty by virtue of tax erosion and that states cannot protect their tax bases without cooperation); Diane M. Ring, *What's at Stake in the Sovereignty Debate?: International Tax and the Nation-State*, 49 VA. J. INT'L L. 155, 233 (2008) (suggesting that cooperation itself may be the key to preserving sovereignty); Daniel Shaviro, *Why Worldwide Welfare as a Normative Standard in U.S. Tax Policy*, 60 TAX L. REV. 155, 178 (2007) (arguing that cooperation with other countries rather than following beggar-your-neighbor strategies should make all countries better off if adherence to the agreed norms is sufficiently reciprocal); Li, *supra* note 39, at 129 (suggesting that in the age of globalization many international problems can only be addressed effectively by international cooperation). From a broader perspective, not limited to taxation, *see, e.g.*, Miriam Ronzoni, *Two Conceptions of State Sovereignty and Their Implications for Global Institutional Design*, 15 CRIT. REV. INT'L SOC. & POL. PHIL. 573 (2012) (arguing that, in certain circumstances, only the establishment of supranational institutions with some sovereign powers can allow states to exercise sovereignty in a meaningful way and suggesting that tax competition is one of these circumstances); ROBERT O. KEOHANE, POWER AND GOVERNANCE IN A PARTIALLY GLOBALIZED WORLD 204 (2002) ("If world government is unfeasible and laissez-faire a recipe for a backlash, we need to search for an intermediate solution: a set of practices for governance that improve coordination and create safety valves for political and social pressures, consistent with the maintenance of nation-states as the fundamental form of political organization.")

71. *See* Christians, *supra* note 69.

autonomy), as happens with any other kind of right, is constrained by the rights of others to make their own autonomous choices. The right to sovereignty of a state conceptually implies the notion of a duty to respect the similar right of other states (*sovereign duty*).[72] Contemporary conceptions of sovereignty seem to suggest a shift from a notion of absolute autonomy towards an idea of restraint.[73] Sovereignty is redefined as responsibility, both in the state's internal functions (responsibility towards citizens) and in international relations (responsibility towards fellow nations).[74]

This new conception of sovereignty implies ethical constraints to the autonomy of states in designing their domestic tax policies. Recent developments in the political philosophy literature on tax competition suggest that strategic fiscal policy decisions that produce negative impacts on the fiscal autonomy of other states are ethically unacceptable.[75] This means that although countries are ethically allowed to compete, competitive policies that produce a collectively suboptimal outcome should be condemned from an ethical perspective.[76] Moreover, it has been noted that the fact that tax competition has a deeper impact upon developing economies brings

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72. *See Id.* at 101 (suggesting the term "sovereign duty" to express the duty of a state to respect the sovereign right of other states to tax).

73. *See generally* Eyal Benvenisti, *Sovereigns as Trustees of Humanity: On the Accountability of States to Foreign Stakeholders*, 107 AM. J. INT'L L. 295 (2013). From the perspective of tax sovereignty, see Christians, supra note 69, at 99 ("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.")

74. Dietsch, *supra* note 69, at 2112–14.

75. DIETSCH, *supra* note 2, at 80. In his book, Dietsch develops a comprehensive normative framework for tax competition. He proposes two principles of global tax justice: the membership principle and the fiscal policy constraint. According to the membership principle, individuals and corporations are liable to pay tax in the state of which they are a member, i.e., one cannot enjoy public services of one country and "choose" to pay taxes to another. According to the fiscal policy constraint principle, a fiscal policy undertaken by a state is unjust if it is *both* strategically motivated (to attracting foreign corporations) *and* has a negative impact on the aggregate fiscal self-determination of other states. *See id.* In contrast, Laurens Van Apeldoorn criticizes Dietsch's conception of fiscal self-determination and argues that an adequate concept should consider the existing policy constraints of low-income countries rather than assume that, eliminated tax competition, the levels of fiscal self-determination of high- and low-income countries would be the same (what he terms the "equality interpretation") or at least satisfy a minimum baseline (what he calls the "baseline interpretation"). *See* Van Apeldoorn, *supra* note 10, at 484-89.

76. DIETSCH, *supra* note 2, at 97–102.

about additional normative concerns.[77] In this respect, a human rights analysis might suggest that tax competition should be mitigated as it tends to undermine the opportunities of the disadvantaged around the world.[78]

Commentators have proposed different solutions for curbing tax competition.[79] The OECD has been leading efforts to achieve international cooperation to address tax competition.[80] In 1998, the OECD issued a report entitled *Harmful Tax Competition: An Emerging Global Issue*,[81] which established criteria for what the OECD regards as harmful tax competition and recommended counteractive measures.[82] In 2013, the OECD initiated a more comprehensive project aimed at tackling different forms of tax avoidance, now commonly known as the Base Erosion and Profit Shifting ("BEPS") project.[83] This ongoing initiative proposes different measures to address tax base erosion by adopting a collaborative-based rather than a competition-based paradigm.[84] One of its sections (Action 5) is specifically aimed at tackling tax competition.[85] As a continuation of OECD's 1998 initiative, it condemns countries' tax regimes that are "designed in a way that allows taxpayers to derive benefits from the regime while

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77. Miriam Ronzoni, *Global Tax Governance: The Bullets Internationalists Must Bite – And Those They Must Not*, 1 J. MORAL PHIL. & POL. 37, 43 (2014).

78. Allison Christians, *Fair Taxation as a Basic Human Right*, 9 INT'L REV. CONST. 211, 228 (2009).

79. An analysis of these proposals would be beyond the scope of this Article. For an overview of the most prominent proposals, see Sol Picciotto, *Unitary Alternatives and Formulary Appointment, in* TAXING MULTINATIONAL ENTERPRISES AS UNITARY FIRMS 27 (Sol Picciotto ed., 2017).

80. *See* Allison Christians, *Taxation in a Time of Crisis: Policy Leadership from the OECD to the G20*, 5 NW. J.L. & SOC. POL'Y 19, 20 (2010) (pointing out that the OECD has long enjoyed a position of central importance in formulating and disseminating international tax policy norms).

81. OECD, HARMFUL TAX COMPETITION: AN EMERGING GLOBAL ISSUE (1998). For a comprehensive and critical analysis of the OECD's harmful tax practices initiative, see Christians, *supra* note 69.

82. In the same year, the European Union ("EU") published a code of conduct for business taxation, which, similar to the OECD's report, aimed at curbing what it considered harmful tax competition. For more details on the EU's code of conduct and on the OECD's report, see Michael Keen, *Preferential Regimes Can Make Tax Competition Less Harmful*, 54 NAT'L TAX J. 757 (2001).

83. OECD, ADDRESSING BASE EROSION AND PROFIT SHIFTING (2013).

84. Yariv Brauner, *What the BEPS?*, 16 FLA. TAX REV. 55, 58 (2014).

85. *See* OECD, ACTION PLAN ON BASE EROSION AND PROFIT SHIFTING 18 (2013).

engaging in operations that are purely tax-driven and involve no substantial activities."[86]

V. THE COSTS SIDE OF CURBING TAX COMPETITION: FAIRNESS IN SHARING THE BURDEN

A. The Costs of Curbing Tax Competition

The literature on the ethics of tax competition often focuses on what I am labeling "the rights side" of the problem, that is, on the ethical reasons for curbing tax competition. However, there is little discussion on what I term "the costs side" of addressing tax competition, i.e., on how to share the burden of mitigating tax competition.[87] Any potential solution for tax competition entails important consequences to all countries involved, from states that strategically engage in competitive behavior to others that participate only defensively, from the poorest to the richest nations in the globe. Any global institutional change aimed at tackling tax competition will result in winners and losers. Restricting tax competition will affect multinationals' decisions about where to locate their economic activities. Investment location decisions will be determined by other competitive factors, such as natural resources, infrastructure, and regulatory framework.[88]

As problematic as it may be for countries to pursue strategic policies that negatively affect other nations, one may argue that simply

86. OECD, COUNTERING HARMFUL TAX PRACTICES MORE EFFECTIVELY, TAKING INTO ACCOUNT TRANSPARENCY AND SUBSTANCE, ACTION 5: 2015 FINAL REPORT 23 (2015). *See* Allison Christians, *BEPS and the New International Tax Order*, 6 BYU L. REV. 1603, 1631 (2016) (pointing out the shift in the OECD's approach from the 1998 initiative to the BEPS project and explaining that the latter focuses on identifying unacceptable country tax practices rather than singling out countries themselves, after criticism over the previous initiative, which appeared to focus on small, non-OECD countries while overlooking the contributions of its own members to the overall phenomenon of harmful tax competition).

87. *But see* DIETSCH, *supra* note 2. In a chapter entitled "Life with (or after) tax competition," Dietsch discusses some ethical questions that arise from the implementation of institutional reform that address tax competition, regarding them as matters of transitonal justice. *See also* DAGAN, *supra* note 10, at 120–212 (pointing to the inefficiencies and potentially regressive effects among and within states arising from multilateral tax cooperation).

88. In this respect, it may be argued that even if curbing tax competition could result in greater tax revenues for all economies, some countries might be better off with the domestic benefits of attracting foreign investments through lower tax rates, as they may have more pressing needs than maintaining a social welfare net. DAGAN, *supra* note 10, at 133.

putting an end to tax competition would be to correct one injustice—tax competition—with another—creating global institutions that are likely to be biased in favor of the most powerful and rich countries.[89] Indeed, some of the low-tax countries—which would arguably be the biggest losers of institutional reform—are small economies that heavily rely on the current international regime.[90] An example is the small island economies that, characterized by profound economic disadvantages, have specialized in hosting offshore finance centres.[91] The literature points out that international organizations have often encouraged these small, resource-poor countries to embrace tax-haven strategies as a means for accelerating development,[92] ignoring the "crowding out" effect of the booming sector that would lead to a situation of overdependence.[93] Institutional reform would cause a relevant impact on these countries, on their financial sectors but also on other sectors of their economy—tourism, agriculture, manufacturing—which were crowded out by the financial industry.[94]

Whether or not it is true that mitigating tax competition might be collectively better for all states in the long run,[95] it is undeniable that it will create costs for some countries while favoring others.[96] Discussing

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89. *See* DIETSCH, *supra* note 2, at 202. *See also* DAGAN, *supra* note 10, at 142–212; Littlewood, *supra* note 27, at 414 n.3 ("The extent to which the tax avoidance industry benefits the residents of havens generally (as distinct from merely benefiting those who work in that industry) is debatable, but it seems reasonable to assume that there is generally some benefit.").

90. Gillian Brock, *Taxation and Global Justice: Closing the Gap between Theory and Practice*, 39 J. SOC. PHIL. 161, 168 (2008).

91. Mark P. Hampton & John Christensen, *Offshore Pariahs? Small Island Economies, Tax Havens, and the Re-Configuration of Global Finance*, 30 WORLD DEV. 1657, 1657 (2002).

92. Philipp Genschel & Laura Seelkopf, *Winners and Losers of Tax Competition*, *in* GLOBAL TAX GOVERNANCE: WHAT IS WRONG WITH IT AND HOW TO FIX IT 55, 69 (Peter Dietsch & Thomas Rixen eds., 2016).

93. Hampton & Christensen, *supra* note 91, at 1664 ("The assertion ran that wealthy tourists would visit the islands, enjoy the lifestyle, and subsequently establish residence and invest. At the same time bankers and tax accountants would be attracted by the climate and lifestyle and would bring with them their knowledge and experience, adding to the virtuous circle. How could such a favorable situation for a small economy go wrong?")

94. DIETSCH, *supra* note 2, at 211.

95. While some commentators argue that global tax competition produces unfairness by reducing global tax revenues, others contend that it is rather a desirable process that creates locational efficiency. *See generally* Elkins, *supra* note 40; Weiss, *supra* note 40. *See also* Roin, *supra* note 26. Moreover, some suggest that tax competition might be beneficial as they produce gains for developing economies. Littlewood, *supra* note 27.

96*.* *See* Christians, *supra* note 4, at 833 (arguing that although all countries may stand to lose from tax competition, all countries may equally stand to lose from curbing tax competition, depending on how "tax competition" is defined and how it is to be regulated).

international policies to tackle tax competition should not be limited to the ethics of tax competition in itself but should include a broader ethical examination of how the losses resulting from institutional reform should be distributed among countries. Since every change in international policy will positively affect some actors and negatively impact on others, one question needs to be asked: how should the burden of an institutional change be shared? Before addressing this issue, I suggest that observing how a similar problem is treated in another context might illuminate our discussion on tax competition. This will be done in Subsection V.B.

B. The Principle of Common but Differentiated Responsibility

The problem just described resembles the discussion on climate change. That anthropogenic climate change should be mitigated is almost undisputed in the scientific literature.[97] The United Nations Convention on Climate Change,[98] drafted in 1992 at the UN Conference on Development and Environment, was signed by 197 parties to date[99] and demonstrates that there is a global consensus on the issue. Similarly, the 2015 Paris Agreement affirms the commitment to a two degrees limit target.[100] However, despite acknowledging that emissions reductions are necessary, states recognized that such a solution would result in opportunity costs relating to economic development and growth.[101] In the discussions on how to address climate change, states realized that, for reasons of justice and political feasibility, they would need to think of how to distribute the global responsibility to cap total global greenhouse gas emissions among countries.[102]

At the 2015 Paris Climate Conference, China and India argued for differentiated responsibilities among richer and poorer countries

97. *See* John Cook et al., *Quantifying the Consensus on Anthropogenic Global Warming in the Scientific Literature*, 8 ENVTL. RES. LETTERS 1 (2013).

98. U.N. Framework Convention on Climate Change, May 9, 1992, 1771 U.N.T.S 107.

99. U.N. CLIMATE CHANGE, *Status of Ratification of the Convention*, https://unfccc.int/process/the-convention/what-is-the-convention/status-of-ratification-of-the-convention [https://perma.cc/5NXS-9TDB] (last visited Sept. 26, 2018).

100. *See* The Paris Agreement, Apr. 22, 2016, T.I.A.S. No. 16-1104 [hereinafter *Paris Agreement*].

101. KOK-CHOR TAN, WHAT IS THIS THING CALLED GLOBAL JUSTICE? 120 (2017).

102. Darrel Moellendorf, *Treaty Norms and Climate Change Mitigation*, 23 ETHICS & INT'L AFF. 247, 251 (2009).

considering their different capabilities.[103] Acknowledging this demand, the Paris Agreement provided that a solution for climate change should "recogniz[e] the specific needs and special circumstances of developing country Parties"[104] and that it should be implemented "to reflect equity and the principle of common but differentiated responsibilities and respective capabilities, in the light of different national circumstances."[105] The agreed principle is now broadly known as the Common but Differentiated Responsibility ("CBDR") principle and stands in contrast to the idea that the burden of climate justice should be shared equally by all societies regardless of background conditions.[106]

Political philosophers and commentators have suggested that richer nations should bear more costs than developing countries in addressing climate change based on different moral grounds. For simplicity, I will limit the arguments to the two most common grounds: 1) historical responsibility for benefits and damages brought forth by past emissions; 2) ability to pay.[107]

The argument based on historical responsibility comprises two similar but distinct versions.[108] One is the polluter pays principle, which ascribes responsibility to the historical polluter.[109] It builds on the intuitive notion that one should take responsibility for their actions. The polluter pays principle is defended by commentators both on fault and no-fault grounds (strict liability).[110] The second version is called

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103. *Key Points of the Paris Climate Pact*, N.Y. TIMES (Dec. 12, 2015), https://www.nytimes.com/interactive/projects/cp/climate/2015-paris-climate-talks.

104. Paris Agreement, *supra* note 100, at 1.

105. *Id*. at 3.

106. TAN, *supra* note 101, at 121.

107. *See* Derek Bell, *Global Climate Justice, Historic Emissions, and Excusable Ignorance*, 94 MONIST 391, 391 (2011) (pointing out that the expression *Common but Differentiated Responsibilities and Respective Capabilities* itself suggests a "hybrid" principle, according to which all states bear a common responsibility for protecting climate-related rights and that how much each state should pay depends on *both* their historical emissions ("differentiated responsibilities") and their ability to pay ("respective capabilities")).

108. A more detailed classification can be found in Lukas H. Meyer & Dominic Roser, *Climate Justice and Historical Emissions*, 13 CRITICAL REV. INT'L SOC. POLIT. PHIL. 229 (2010), where the authors subdivide what I here present as the polluter pays principle in two: the emitter pays principle (based on individual responsibility) and the community pays principle (based on collective responsibility). I here conflate both categories for simplification.

109. TAN, *supra* note 101, at 124.

110. For a detailed analysis, see DARREL MOELLENDORF, THE MORAL CHALLENGE OF DANGEROUS CLIMATE CHANGE 165–69 (2014).

the beneficiary pays principle and identifies the beneficiary of emissions as responsible.[111] It is based on the idea that if the current inhabitants of industrialized countries have benefited from emissions so that their standard of living today is higher than it would otherwise have been, they must pay a cost for that.[112]

Arguments built on historical responsibility, especially in the case of the polluter pays principle, require justifying why the wrongs committed by individuals in the past should fall on persons in the present.[113] One possible solution to the problem of intergenerational justice is to adopt a collectivist approach to moral responsibility.[114] Such a solution, however, requires answering some deeper questions about justice and moral agency.[115] The beneficiary pays principle faces similar problems. It requires answering whether present actors should pay if it was only their ancestors who benefited the most.[116] It also involves the issue of identification and measurement. Who are the beneficiaries?[117] How should one measure the benefits?[118]

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111. TAN, *supra* note 101, at 127–28.

112. Simon Caney, *Cosmopolitan Justice, Responsibility, and Global Climate Change*, 18 LEIDEN J. INT'L L. 747, 757 (2005).

113. *See* MOELLENDORF, *supra* note 110, at 173–74.

114. *See* Caney, *supra* note 112, at 774.

115. TAN, *supra* note 101, at 126 ("The collectivist turn is a promising solution to the problem of reparations for past international injustice. But its full defense will require some deeper understanding of what makes for a collective *moral agent* and how a collective responsibility can be distributed among individuals of the collective. What are some of the necessary conditions for collective moral agency? Must the collective show some structured deliberative capacity? Must it be a collective whose individuals share national ties or other bonds of solidarity? Or must the individuals of the collective be enjoined via certain common interests? And if there is indeed a collective responsibility, what is the right way of parceling this responsibility out among individuals?").

116. *See generally* Simon Caney, *Climate Change and the Duties of the Advantaged*, 13 CRITICAL REV. INT'L SOC. POL. PHIL. 203 (2010).

117. *See*, *e.g.*, Henry Shue, *Global Environment and International Inequality*, 75 INT'L AFF. 531, 534-35 (1999) (pointing out that "[q]uite a bit of breath and ink has been spent in arguments over how much [less developed countries] have benefited from the technologies and other advances made by the [developed countries], compared to the benefits enjoyed by the [developed countries] themselves.").

118. *See* TAN, *supra* note 101, at 128 ("For instance, is a country benefitting from such activities if it gains economically but loses out in terms of breathable air and clean environment for its citizens? Moreover, how direct must the benefits from emission production be in order to count as a relevant benefit? . . . And finally, what difference does it make, if any, if the benefits acquired were not sought out or voluntarily accepted, but simply thrust upon an agent? If the present generation benefits from the actions of their predecessors without asking for them – indeed they can't avoid the benefits – can it be fairly held to account?").

The other moral ground for differentiated responsibilities is the ability to pay principle, which focuses on the different capabilities of countries to address climate change.[119] It may be argued that the ability to pay principle is so fundamental that it is difficult to justify it by deriving it from considerations that are more fundamental still.[120] One possible moral justification can be found in John Rawls's difference principle, one of the most important principles of justice in modern political philosophy.[121] The difference principle states that the advantages of the better situated are just only if they are part of an institutional setting that improves the expectations of the least advantaged members of society so that existing inequalities must contribute effectively to the benefit of the least advantaged.[122]

The ability to pay principle applied to the problem of climate change requires that transition costs be incorporated into reform design. It suggests that, although necessary to mitigate climate change, this transition should not slow human development and the eradication of poverty in the least developed countries.[123] This principle does face important challenges. The idea that principles of distributive justice— which traditionally apply to relations between individuals within one jurisdiction— should apply at the international level has been strongly argued by cosmopolitans[124] but has faced equally vigorous opposition from anti-globalists.[125]

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119. *See* Caney, *supra* note 116.

120. Shue, *supra* note 117, at 537.

121. *See* JOHN RAWLS, A THEORY OF JUSTICE 65–70 (Harvard Univ. Press rev. ed. 1999) (1971); *see also* JOHN RAWLS, JUSTICE AS FAIRNESS: A RESTATEMENT 61–66 (Erin Kelly ed., 2001).

122. *See supra* note 121.

123. MOELLENDORF, *supra* note 110, at 175.

124. For early developments of cosmopolitanism, see CHARLES BEITZ, POLITICAL THEORY AND INTERNATIONAL RELATIONS (1999); *see generally* THOMAS POGGE, WORLD POVERTY AND HUMAN RIGHTS: COSMOPOLITAN RESPONSIBILITIES AND REFORMS (2nd ed. 2008).

125. *See*, *e.g.*, Thomas Nagel, *The Problem of Global Justice*, 33 PHIL. & PUB. AFF. 113 (2005); Michael Blake, *Distributive Justice, State Coercion, and Autonomy*, 30 PHIL. & PUB. AFF. 257 (2002); Samuel Freeman, *Distributive Justice and The Law of Peoples*, *in* RAWLS'S LAW OF PEOPLES: A REALISTIC UTOPIA? 243 (Rex Martin & David A. Reidy eds., 2006); Andrea Sangiovanni, *Global Justice, Reciprocity, and the State*, 35 PHIL. & PUB. AFF. 3 (2007)).

For an overview of the various positions on this debate, including others not mentioned here, such as the equal per capital emissions approach and the idea of subsistence versus luxury emissions, see TAN, *supra* note 101, at 120–33; *see also* Philippe Cullet, *Common But Differentiated Responsibilities*, *in* RESEARCH HANDBOOK ON INTERNATIONAL ENVIRONMENTAL LAW 161, 178 (Malgosia Fitzmaurice et al. eds., 2010) (pointing out that even

C. How to Share the Burden of Curbing Tax Competition

Returning to the problem of tax competition, we can see that curbing tax competition involves a similar issue of burden sharing. An ethical analysis of tax competition includes asking who should bear the costs of addressing tax competition and how responsibilities should be assigned among countries. In other words, what normative principles should apply to the burden sharing of mitigating tax competition? Studies in tax competition have often failed to address this issue. Much thought has been directed at pointing the negative effects of tax competition and finding an *effective* solution to tackle tax competition, but the matter of *fairness* in how the costs of a solution are distributed internationally has been largely overlooked.[126] Although a comprehensive response to tax competition might be beneficial to most countries—and even if we were to assume that this would bring more fairness to the international tax regime—, a just solution requires an equal concern with fairness in the upshot of institutional reform.[127]

I do not attempt to settle the question here. I rather argue that this is a much-needed discussion, especially considering the increasing efforts of international organizations to achieve cooperation in building a more comprehensive and inclusive framework for international

the binding nature of the principle of CBDR remains disputed, as developed countries are wary of the implications and long-term consequences of recognizing differential treatment as a compulsory principle of international law).

126. For important exceptions, see *supra* note 10 and accompanying text; *see also* Avi-Yonah, *supra* note 1, at 1650 (suggesting that between two alternative solutions for tax competition, a solution that favors poorer countries should be preferred as a matter of inter-nation equity).

127. In this respect, fairness might also help achieve cooperation. Research suggests that even when self-interest favors cooperation, countries might fail to contribute if they feel the distribution of costs is unfair. Scott Barrett, *Making International Cooperation Pay: Financing as a Strategic Incentive*, *in* THE NEW PUBLIC FINANCE: RESPONDING TO GLOBAL CHALLENGES 357, 366 (Inge Kaul & Pedro Conceição eds., 2006). This means that a fair distribution of the burden can also be seen as an important strategy to establish incentive structures that motivate agreement. *See* Benshalom, *supra* note 4, at 79–80 (arguing that if a state has confidence that a long-term agreement is fair, it might be willing to cooperate whether or not its economic position relative to the position of other countries improves); *see generally* Charles Bram Cadsby & Elizabeth Maynes, *Voluntary Provision of Threshold Public Goods with Continuous Contributions: Experimental Evidence*, 71 J. PUB. ECON. 53 (1999) (suggesting that compensation encourages compliance and reduces risks of free-riding behavior).

taxation.[128] Building on the insights of philosophers and legal and political scholars developed in the context of climate change, I outline below four principles that could independently or jointly guide the burden sharing of curbing tax competition: the responsible party pays principle, the retrospective beneficiary pays principle, the prospective beneficiary pays principle, and the ability to pay principle.

1. Responsible Party Pays Principle

One might argue that the costs of curbing tax competition should be shared among the countries that gave cause to it in the first place—let us call this idea the "responsible party pays principle."[129] It builds on the idea of reparative justice and asks for accountability and responsibility-taking from those who are responsible for harm.[130] At first glance, this may seem to suggest that the existing low-tax countries are responsible for the current international tax scene, and as such, they should bear the costs of curbing tax competition. The institutional history of the existing international tax regime, however, might suggest otherwise.

The present international tax regime was forged when, in the 1920s, the League of Nations commissioned a group of experts to evaluate how to avoid the problem of double taxation in cross-border

128. An important example is the OECD's Inclusive Framework on BEPS, an initiative launched by the OECD in January 2016 to include the participation "on an equal footing" of non-G20 countries, particularly developing economies, in the implementation of the BEPS project. *Background Brief: Inclusive Framework on BEPS*, OECD (Jan. 2017) https://www.oecd.org/ctp/background-brief-inclusive-framework-for-beps-implementation.pdf [https://perma.cc/4XRN-B3DD] (last visited Sept. 26, 2018). Another example is the Platform for Collaboration on Tax, a joint effort launched in April 2016 by the IMF, the OECD, the UN, and the World Bank to increase cooperation between these organizations on designing and implementing international tax standards, providing capacity-building support to developing countries, and ensuring a greater participation of developing countries in international tax policy discussions and institutions. *The Platform for Collaboration on Tax: Concept Note*, WORLD BANK (Apr. 19, 2016), http://documents.worldbank.org/curated/en/801891468196141038/pdf/104902-SECOND-REVISION-concept-note-platform-for-collaboration-on-tax.pdf [https://perma.cc/SL36-GM4F] (last visited Sept. 26, 2018).

129. This principle resembles the polluter pays principle discussed in the climate change debate. Here I adapt the term to the problem of tax competition.

130. Margaret Urban Walker, *Restorative Justice and Reparations*, 37 J. SOC. PHIL. 377 (2006).

transactions.[131] The principles then articulated have since been the pillars of international taxation.[132] The decision made then resulted in the existing international tax regime, a web of inconsistent rules exploited by multinationals to avoid taxes.[133] It has been argued that although policymakers at the time did foresee that this tax regime would allow taxpayers to more easily engage in tax avoidance and evasion, they were more concerned that an alternative solution would harm efforts to liberalize trade and investment, the primary objective at the time.[134]

This discussion illustrates the most important problem with the responsible party pays principle. It requires identifying who is responsible and determining how to measure their degree of responsibility.[135] In this respect, other actors might as well be held accountable for the current state of international tax competition. Commentators note that low-income economies have oftentimes been encouraged by rich countries and by international organizations such as the IMF or the World Bank to pursue policies that include low taxation of capital.[136] Moreover, a broader perspective of the

131. Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 26 BROOK. J. INT'L L. 1357, 1358 (2001).

132. Gabriel Zucman, *Taxing Across Borders: Tracking Personal Wealth and Corporate Profits*, 28 J. ECON. PERSP. 121, 123 (2014).

133. *Id.* at 124.

134. *See, e.g.*, Thomas Rixen, *From Double Tax Avoidance to Tax Competition: Explaining the Institutional Trajectory of International Tax Governance*, 18 REV. INT'L POL. ECON. 197, 212 (2011).

135. It is interesting to note that in the case of climate change historical polluters often put forward the argument that they were excusably ignorant of the consequences of their actions. Bell, *supra* note 107. This argument cannot be as easily advanced in the case of tax competition, as delegates in the League of Nations were already informed in the 1920s that the international tax regime then decided would generate international tax arbitrage, but they preferred to avoid any potential obstacle to international circulation of capital, seen at the time as "one of the conditions of public prosperity and world economic reconstruction." Rixen, *supra* note 134, at 212. As Rixen points out, however, what policymakers could not foresee was that the magnitude of cross-border activity and the significance of intangible assets would one day overburden the capacities of tax administrations around the globe. *Id.* at 212.

136. DIETSCH, *supra* note 2, at 205; Genschel & Seelkopf, *supra* note 92, at 69 (pointing out that international organizations such as the United Nations Conference on Trade and Development ("UNCTAD") often encourage small, resource-poor countries to embrace tax-haven strategies as a means for accelerating development). It is also important to note that the current tax regimes of many tax havens hardly result from an expression of their will as they are often "holdovers from the colonial era." 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, 936 (2007).

international tax regime might suggest that policy choices made by developed countries in the last few decades have intensified tax competition. The adoption of specific domestic policies of developed countries creates international conditions that favor tax competition over cooperation, which constrains policy alternatives of less developed countries, as multinationals put pressure on them to reduce their taxes.[137] Indeed, some argue that given the need for tax revenues, developing countries would generally prefer not to engage in tax competition, but they are compelled to grant tax incentives in response to the existing competition.[138]

The responsible party pays principle also raises an important philosophical problem. A principle based on historical responsibility that implies reparations for past wrongs requires justifying why wrongs committed in the past should be borne by individuals in the present. One needs to justify how perpetrators who are no longer alive can be held accountable and how the responsibility can be transferred to present individuals simply because of national or generational association.[139] These issues pose important challenges for a principle based on historical responsibility.[140]

2. Retrospective Beneficiary Pays Principle

An alternative but related principle might be drawn in the form of the beneficiary pays principle. There could be two different versions of

137. *See* Christians, *supra* note 58, at 265–66 (mentioning as an example the United States' "deferral" tax regime, which increases the sensitivity of taxpayers to foreign tax rates). The recent U.S. tax reform has substituted the system of worldwide taxation with deferral by a system more akin to territorial taxation. Commentators suggest that the new legislation will exert even more pressure for tax competition. David Kamin et al., *The Games They Will Play: Tax Games, Roadblocks, and Glitches Under the 2017 Tax Legislation*, 103 MINN. L. REV. (forthcoming 2018).

138. *See, e.g.*, Avi-Yonah, *supra* note 63, at 63.

139. For a strong case that it should, see DAVID MILLER, NATIONAL RESPONSIBILITY AND GLOBAL JUSTICE 135–61 (2007).

140. A somewhat "negative" approach to this idea of responsibility was proposed by Steven Dean. Steven A. Dean, *Neither Rules nor Standards*, 87 NOTRE DAME L. REV. 537, 576–82 (2013). Focusing on global tax revenue allocation among countries, Dean suggests what he calls the "Benefits and Burdens Principle," according to which global tax revenues should be shared according "not only to the proportion of the world's sales that occur in a particular jurisdiction but also to a measure of the enforcement assistance it provides to other states." *Id.* at 578. I consider his benefits and burdens principle a negative approach to the responsible party pays principle in the sense that the more a jurisdiction offers in enforcement assistance to reduce tax evasion the less responsible it should be held for the current state of tax competition.

this principle, depending on how we look at the issue. A first version—let us call it the "retrospective beneficiary pays principle"—looks at the gains and losses generated by tax competition and suggests that the past and present beneficiaries of tax competition should bear the costs resulting from curbing it. The larger the benefits one gained from international tax competition, the larger one's share of the costs of mitigating the problem.

This version resembles the beneficiary pays principle discussed in the climate change debate. It builds on the idea that where a country "has been made better off by a policy that has contributed to the imposition of adverse effects on third parties, then that country has an obligation not to pursue that policy itself and an obligation to address the harmful effects suffered by the third parties."[141] Although similar to the responsible party pays principle, it focuses on the beneficiaries rather than on causation. One could argue that this principle creates positive incentives for wider institutional reform due to its rhetorical value for a shaming strategy against the current beneficiaries of tax competition, which would otherwise be unlikely to cooperate.[142] However, although public shaming by international organizations can be effective in bringing about compliance,[143] we should not ignore that a shaming strategy might result in unprincipled coercion by the most powerful states if there are no clear agreed-upon criteria for defining relevant concepts such as "tax havens" and "unjust tax competition."[144] A recent example is the EU's release of a blacklist of "non-cooperative tax jurisdictions."[145] It has sparked criticism for lack of both

141. Caney, *supra* note 112, at 756.

142. *See*, *e.g.*, DIETSCH, *supra* note 2, at 192–93 (arguing that net winners of tax competition have a duty to compensate net losers and suggesting that the main reason to argue for these compensatory duties is not actually to see them paid, but rather to deploy them as rhetorical device in the fight against unjust tax competition). It is important to note that Peter Dietsch's proposal of compensatory duties does not build on the idea of benefits, but rather focuses on the losses generated by tax competition to what he calls the "right holder states." He also does not suggest compensation based on the costs of *curbing* tax competition but rather aims at offsetting the losses caused so far by tax competition itself. *Id.* DIETSCH, *supra* note 2, at 188–218.

143. J.C. Sharman, *The Bark Is the Bite: International Organizations and Blacklisting*, 16 REV. INT'L POL. ECON. 573 (2009).

144. *See* Christians, *supra* note 69 (analyzing the OECD's 1998 Project on Harmful Tax Practices and arguing that the guiding principles for intervention in domestic tax policy decisions should be explicitly stated and subjected to rigorous analysis and inclusive debate).

145. The original list and subsequent adjustments are available at *Common EU list of third country jurisdictions for tax purposes*, EUROPEAN COMMISSION,

transparency and objective criteria as it omits EU members and countries commonly regarded as tax havens.[146]

The retrospective beneficiary pays principle faces some relevant challenges. The first question is whether the principle should be limited to current beneficiaries (and current gains from tax competition) or whether it should include historical beneficiaries (and past gains as well). Second, it might be difficult to determine who the beneficiaries are and how to measure the benefits, as such an analysis requires a counterfactual exercise, i.e., it depends on hypothesizing what the world economy would be like had tax competition (which would also need a definition) not taken place.[147] Third, the definition of "benefit" is problematic. Should it consider the gains and losses of tax revenues? Should it include the economic growth resulting from foreign capital attraction? Fourth, if we consider the institutional history of the present international tax scene, as well as the role of rich countries and international organizations in constraining (or influencing) the choices of poorer countries regarding their domestic fiscal policies, it seems ethically troublesome to suggest that the latter alone should bear the costs resulting from the mitigation of tax competition.

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https://ec.europa.eu/taxation_customs/tax-common-eu-list_en [https://perma.cc/2FYC-RY67] (last visited Sept. 26, 2018).

146. *See EU Blacklist Names 17 Tax Havens and Puts Caymans and Jersey on Notice*, THE GUARDIAN, Dec. 5, 2017, https://www.theguardian.com/business/2017/dec/05/eu-blacklist-names-17-tax-havens-and-puts-caymans-and-jersey-on-notice [https://perma.cc/3ZZL-ACKY]; Francesco Guarascio, *EU Adopts Tax Haven Blacklist, British Territories Spared*, REUTERS, Dec. 5, 2017, https://www.reuters.com/article/us-eu-ecofin-tax/eu-adopts-tax-haven-blacklist-british-territories-spared-idUSKBN1DZ172. *See* also Christians, *supra* note 69, at 101 (observing that the naming and shaming in the OECD's work on harmful tax competition is problematic and represents the determination of taxing rights of sovereign nations by a "relatively small and elite group of individuals"). For general criticism of the practice of blacklisting, particularly by supranational institutions, see Lucas de Lima Carvalho, *The Ills of Blacklisting for International Taxation*, KLUWER INTERNATIONAL TAX BLOG (Sep. 20, 2018), http://kluwertaxblog.com/2018/09/20/ills-blacklisting-international-taxation [https://perma.cc/7LH7-75ZT] (last visited Sept. 26, 2018).

147. *But see* DIETSCH, *supra* note 2, at 196–201 (suggesting criteria for estimating losses originated from each of the three kinds of tax competition: portfolio capital, paper profit, and foreign direct investments).

One may suggest that an estimation in this case might not be needed, since the implementation of any given solution for tax competition itself would automatically burden the present beneficiaries of tax competition. However, although it is true that the effects of implementation would fall on present beneficiaries, the distribution of the burden would not necessarily be proportionate to how much each country gains or has gained from tax competition, as different alternative solutions for tax competition would produce different economic results.

3. Prospective Beneficiary Pays Principle

A second version of the beneficiary pays principle would aim at the *prospective beneficiaries* of the mitigation of tax competition. According to this idea, winners from institutional reform should compensate losers for their resulting losses. Compared to the first version of the beneficiary pays principle, this version suggests an almost contrary view. Whereas the retrospective beneficiary pays principle tends to favor countries that currently lose from tax competition, the prospective version of the principle would favor countries that presently benefit from it. The "prospective beneficiary pays principle" takes tax competition as the status quo and proposes to compensate the prospective losers of institutional reform. It builds on the somewhat intuitive notion that who benefits more from a given policy should also contribute a larger share in bearing its costs. From an ethical perspective, it may be argued that the international community has a moral obligation to smooth the transition for net losers.[148]

An important advantage of this principle seems to be political acceptability. Negotiations for major institutional reform often involve estimations of costs by prospective losers, which will hardly cooperate unless some form of compensation for their losses is ensured.[149] To the extent that a comprehensive solution for tax competition requires cooperation from prospective losers (mainly, low-tax countries), compensation based on the prospective beneficiary pays principle might be needed to achieve agreement.[150] Moreover, from a practical perspective, a compromise based on prospective benefits seems more feasible than a solution based on the other principles mentioned so far

148. DIETSCH, *supra* note 2, at 213.

149. *See* Genschel & Schwarz, *supra* note 22, at 355 ("The spread of multilateral cooperation is held back by small, low-tax countries either refusing to participate or premising their participation on costly side-payments and/or substantive concessions undermining the effectiveness of the cooperation.").

150. *See* DIETSCH, *supra* note 2, at 212 (arguing that a targeted compensation of citizens of transitioning tax havens would weaken the feasibility constraints facing the unwinding of tax havens and increase the chances of their cooperation in the transition); *see also* Rixen, *supra* note 134, at 201–02 (analyzing tax competition from a game-theoretical perspective and observing that present losers from tax competition would either have to provide side payments to current winners or somehow use their power to force them into compliance). *But see* Dean, *supra* note 136 (criticizing the common assumption that international tax policy is determined by "enlightened philosopher kings devoted to pursuing the national public interest" and that cooperation would only occur where participating nations were to benefit economically from it).

(the responsible party pays principle and the retrospective beneficiary pays principle). It is arguably harder to set agreement about who gave cause to or has benefited from tax competition than about the prospective gains and losses from reform.

A prospective beneficiary analysis depends on the agreed solution for tax competition. The distribution of gains and losses from institutional reform will vary significantly according to how tax competition is defined and how it will be regulated.[151] Indeed, any potential solution for tax competition would not "reinstate" the global economy to what it "should" be in the absence of tax competition. Institutional reform will rather create a new tax order that will change, not eliminate, the global competition arena. This means that prospective benefits can only be estimated after a specific solution for tax competition is determined. Commentators warn about the risk that an institutional solution for curbing tax competition may favor richer countries.[152] If this were the case, a prospective beneficiary pays principle should at least alleviate the effects of an unjust institutional solution.

4. Ability to Pay Principle

The three principles discussed so far consider justice from the somewhat narrow perspectives of who gave cause to tax competition (responsible party pays principle), who benefited from it (retrospective beneficiary pays principle), or who would benefit were it to be mitigated (prospective beneficiary pays principle). A recurring weakness of these principles is that they are indifferent to the existing background inequality and varying abilities of countries to bear the burden of institutional reform. Indeed, one might say that the world is not only unequal, but it is unequal in a particular way: most of the inequality is due to inequality among countries, rather than within countries.[153] A broader observation of the global economy might

151. Christians, *supra* note 4, at 833.

152. *See*, *e.g.*, DAGAN, *supra* note 10, at 140; Hearson, *supra* note 10; Christians, *supra* note 80.

153. BRANKO MILANOVIC, GLOBAL INEQUALITY: A NEW APPROACH FOR THE AGE OF GLOBALIZATION 132 (2016). Milanovic points out that inequality among nations is high enough that being born in a rich country matters much more than being born in a rich family and suggests the terms "citizenship premium" for those who are born in a rich country and "citizenship penalty" for those born in poor ones. *Id*. at 128, 131.

suggest a more comprehensive conception of international justice which considers that some countries have more economic needs than others. It suggests it might be unfair—and even infeasible—to distribute the burden among countries in any way that disregards distinct capabilities to bear them.

The "ability to pay principle" is widely recognized in the tax literature as a measure to determine how to share the burden of taxation among citizens fairly.[154] It builds on the idea that a just tax scheme should distinguish among taxpayers according to their relative income, taking more from those who have more, so as to ensure that each taxpayer bears the same loss of overall welfare.[155] It is relevant to note that the ability to pay principle is discussed in tax scholarship only as a matter of *inter-individual equity* within a nation, i.e., it is a theory that compares inequalities among residents of a given country.[156] Here we consider it as a matter of *inter-nation equity*, applying it as a measure of fairness between countries. Interestingly, the term "ability to pay principle" has been largely used in the philosophical debates on climate change as referring to inter-nation equity rather than to inter-individual equity.[157]

The ability to pay principle applied in the international context suggests that a fair institutional reform that involves distinct gains and losses for different countries should not aggravate the situation of the worse off. This is particularly important as empirical research suggests that structural inequalities among countries play a relevant causal role in the production and perpetuation of poverty around the world.[158]

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154. *See* M. Slade Kendrick, *The Ability-to-Pay Theory of Taxation*, 29 AM. ECON. REV. 92, 92 (1939).

155. For a philosophical discussion on the justification of the ability to pay principle in the context of domestic tax policy, see LIAM MURPHY & THOMAS NAGEL, THE MYTH OF OWNERSHIP: TAXES AND JUSTICE 20–30 (2002).

156. Even when discussing international taxation, commentators limit the scope of the ability to pay to equity among individuals within a country rather than among countries. *See*, *e.g.*, J. Clifton Fleming Jr., Robert J. Peroni & Stephen E. Shay, *Fairness in International Taxation: The Ability-to-Pay Case for Taxing Worldwide Income*, 5 FLA. TAX REV. 299 (2001) (analyzing how different US policies of taxing residents on their worldwide incomes adhere to the ability to pay principle, so understood as fairness among American residents).

157. *See*, *e.g.*, Caney, *supra* note 116; Shue, *supra* note 117, at 542–43; MOELLENDORF, *supra* note 110, at 173–80; Bell, *supra* note 107.

158. *See* Niheer Dasandi, *International Inequality and World Poverty: A Quantitative Structural Analysis*, 19 NEW POL. ECON. 201 (2014) (suggesting the need for policymakers to consider the negative effects of international policies and actions on poverty, rather than focusing exclusively on reforms to be undertaken within developing countries).

As every state in the world is simultaneously a participant in and a potential victim of the global game of tax competition,[159] winners and losers of tax competition do not compose homogeneous groups. They have different structures and varying levels of development, as would the potential winners and losers of overall institutional reform.[160] Curbing tax competition will not eliminate competition between countries but will rather shift the game to one that relies on other sets of advantages in the search for international competitiveness. How different nations will be adversely affected by such a change will depend on which solution is chosen to address tax competition. The different principles for burden sharing mentioned above (the responsible party pays, the retrospective beneficiary pays, and the prospective beneficiary pays) do not directly consider the different capabilities of countries to meet these costs.[161]

The ability to pay principle requires that a distribution of a burden reduce the advantage of those at the top and prevent existing inequalities from becoming worse through the infliction of an unfair additional disadvantage upon those at the bottom.[162] To ignore these inequalities at a time when some countries are still struggling to overcome extreme poverty is to disregard their right to economic development.[163] As some countries suffer from greater structural disadvantages than others, international justice requires that the main institutions of the global economic order be designed to be fair to poor and developing countries.[164]

An important question for applying this principle is how to measure the development level of affected countries. Should it be limited to economic inequality? Should it consider a broader notion of development? The concept of development itself has evolved rapidly in the development literature,[165] and each different conception of the term

159. Christians, *supra* note 24, at 1375.

160. For an analysis of the determinants of who wins and who loses from tax competition, see Genschel & Seelkopf, *supra* note 92, at 69.

161. For an analysis of the structure of the international tax regime as a game between parties with asymmetric capabilities, see DAGAN, *supra* note 10, at 142–84.

162. Shue, *supra* note 117, at 540.

163. TAN, *supra* note 101, at 123.

164. MARTHA C. NUSSBAUM, FRONTIERS OF JUSTICE: DISABILITY, NATIONALITY, SPECIES MEMBERSHIP 319 (2006).

165. IAN GOLDIN, THE PURSUIT OF DEVELOPMENT: ECONOMIC GROWTH, SOCIAL CHANGE, AND IDEAS 3 (2016).

would suggest a different classification system.[166] Possible measures include per capita income, purchasing power parities, the Human Development Index ("HDI"), the Sustainable Development Goals index, the Index of Sustainable Economic Welfare, the Happy Planet Index, and the World Happiness Report.[167] International organizations have been using different indicators for this purpose. The World Bank uses the gross national income per capita ("GNI/n") as the basis for determining preferential assistance because it considers it to be "the best single indicator of economic capacity and progress."[168] The UN Development Programme uses the HDI as ultimate criteria for assessing the development of a country.[169] The International Monetary Fund employs a framework based on per capita income, market access, and short-term vulnerability, to determine eligibility for concessional financing.[170] The OECD proposes a broader measurement of well-being with its Better Life Index, which includes eleven indicators: community, education, environment, civic engagement, health, housing, income, jobs, life satisfaction, safety and work-life balance.[171]

VI. CONCLUSION

The goal of this Article is not to provide definitive answers. More fundamentally, I argue that a solution for curbing tax competition, as is the case with any institutional reform, brings about costs that should not be excluded from an ethical analysis of tax competition. A normative analysis requires thinking about the moral justifications for mitigating it, but it should equally include an analytical examination of the ethical implications of an institutional solution for tax competition. I have suggested four normative principles that could independently or jointly apply to the burden sharing of curbing tax competition. Two of these principles—the responsible party pays and the retrospective beneficiary pays—look at the past and suggest that countries that gave

166. Lynge Nielsen, *Classifications of Countries Based on Their Level of Development: How It Is Done and How It Could Be Done* 4 (Int'l Monetary Fund, Working Paper, 2011), https://www.imf.org/external/pubs/ft/wp/2011/wp1131.pdf [https://perma.cc/6NHH-K5EP] (last visited Sept. 26, 2018).

167. Goldin, *supra* note 165, at 4–17.

168. Nielsen, *supra* note 166, at 10–11.

169. UNITED NATIONS DEVELOPMENT PROGRAMME, HUMAN DEVELOPMENT REPORT 2016: HUMAN DEVELOPMENT FOR EVERYONE (2016).

170. INT'L MONETARY FUND, ELIGIBILITY TO USE THE FUND'S FACILITIES FOR CONCESSIONAL FINANCING 1 (2017).

171. OECD, HOW'S LIFE? 2017: MEASURING WELL-BEING (2017).

cause to the problem or have benefited from it should bear the costs of overall institutional reform. The other two principles—the prospective beneficiary pays and the ability to pay—consider the prospective effects of institutional reform in the global economy and the inequities that may arise from it.

Although not definitively advocating which of (or how) these principles should apply to the burden sharing of curbing tax competition, as well as not excluding other possible principles not discussed here, I believe that the complexity of tax competition and the heterogeneity of the actors involved might require a combination of principles.[172] Any solution needs to consider the existing background injustices of the international tax system and should thus include the ability to pay principle as one of its elements.[173] A fair framework for tax competition should allow the pursuit of sustainable development in the least developed and developing countries rather than create even more constraints to these economies. On the other hand, a concern with fairness but also with political feasibility might suggest some form of compensation for prospective net losers, as it would otherwise be difficult—and unjust, as we have seen in Subsections V.B and V.C.3—to achieve consensus. Therefore, a tentative proposal might be a combination of the prospective beneficiary pays and the ability to pay principles.

As suggested throughout Section V.C, several questions remain to be answered, such as how to identify and measure past responsibility and how to determine beneficiaries and measure their respective benefits. More importantly, arguing for a fair distribution of the burden requires answering the broader question of why principles of distributive justice should apply to the relations between countries.[174] Although a practical conception of inter-nation equity has long been

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172. Similarly, Simon Caney proposes a mixed normative principle for the burden sharing of climate change, arguing that, although convenient, a simple formula would fail to address the complexity of the problem. Caney, *supra* note 157, at 222.

173. *See* Van Apeldoorn, *supra* note 10, at 491 (arguing that background justice in the international context requires the creation of redistributive institutions and suggesting that tax revenues from the taxation of multinationals' income should be shared among states in proportion to their GDP or per capita income so as to increase the fiscal self-determination of the poorest countries).

174. On the problem of fairness in the international tax context, see I.J.J. Burgers & I.J. Mosquera Valderrama, *Fairness: A Dire International Tax Standard with No Meaning?*, 45 INTERTAX 767 (2017) (arguing that fairness in taxation is a disputed and blurred concept and calling for the need of more research on global perceptions of fairness).

suggested in the tax literature,[175] no comprehensive theory has been proposed to date to analyze why and how a concept of inter-nation equity should guide the normative framework of international taxation.[176] A broad normative theory of inter-nation equity is needed to help illuminate how the international tax regime should relate to development, poverty, and global justice.[177]

Further research is also needed on how the costs of mitigating tax competition should be technically shared. I believe this would greatly depend on what solution is to be applied to tax tackle tax competition. A distribution of the costs might include, for example, financial compensation[178] or unequal restrictions on tax competition (i.e., limiting tax competition according to the chosen criteria, e.g., allowing low-income countries to engage in some forms of tax competition under more moderate restrictions compared to high-income countries).[179]

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175. Richard A. Musgrave & Peggy B. Musgrave, *Inter-Nation Equity*, *in* MODERN FISCAL ISSUES: ESSAYS IN HONOUR OF CARL S. SHOUP 63 (Richard M. Bird & John G. Head eds., 1972).

176. *See* Li, *supra* note 39, at 121–22 (pointing out that the Musgraves did not provide any theoretical foundation for inter-nation equity and arguing that the concept should be taken seriously in international tax reforms as it provides an "important, and perhaps superior, policy framework than the principle of neutralities to guide future reforms").

177. *See* Benshalom, *supra* note 4 (arguing that the long-term economic relationships established between countries give rise to distributive obligations toward foreigners and, thus, proposing a theoretical solution that avoids the common philosophical debate between cosmopolitans and statists on global distributive justice). For a similar argument in a more general context not focused on international taxation, *see also* David Miller, *National Responsibility and Global Justice*, 11 CRITICAL REV. INT'L SOC. & POL. PHIL. 383, 395–96 (2008) (arguing that interaction between countries through trade and investment flows, as well as cooperation to provide collective goods, raise specific questions of justice and suggesting what he calls the "principle of equal net benefit," according to which "when people belonging to separate political communities interact and co-operate to their mutual advantage [. . .], the costs and benefits of co-operation should be fairly allocated, so that each party receives approximately the same net gain").

178. An interesting proposal based on financial compensation is advanced by Dean, *supra* note 136, at 965. Dean proposes that "tax flight jurisdictions" (countries which commonly suffer from tax evasion and avoidance) negotiate "tax flight treaties" with tax haven jurisdictions, in which the latter agree to exchange information while the former commit to financial compensation by financing the information infrastructure and sharing a portion of the additional tax revenues generated by the tax haven's cooperation. Dean's proposal, however, is not based on normative grounds. He rather suggests it "stand[s] a greater chance [than some alternative proposals] of persuading tax havens to help reduce tax flight."

179. *See* DIETSCH, *supra* note 2, at 202 (suggesting that in the current state of global background injustice, a solution for tax competition could be more permissive with respect to developing countries by tolerating their resorting to tax-competition practices).

Another possibility would be to incorporate the burden sharing element as a factor in what is known as "formulary apportionment." As multinationals today can easily shift income and profits from one country (high-tax jurisdiction) to another (low-tax jurisdiction), advocates for formulary apportionment propose that the collective income of members of a multinational corporate group be apportioned among countries according to pre-established formulas, rather than considering each of these members as a separate entity as it is today.[180] Since the rights of countries to tax are determined by where the income is allocated, formulary apportionment would significantly change the current distribution of taxing rights among countries.[181] Proposals for formulary apportionment mostly suggest a formula based on a combination of economic factors, such as the location of sales, payroll expenses, and physical assets.[182] Different proposals suggest varying weights to each of these economic factors.[183] An analysis of the fairness of each proposal inevitably requires identifying which countries would benefit more depending on which of these factors is favored in the formula.[184]

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180. *See* INT'L MONETARY FUND, *supra* note 29, at 39 ("The primary appeal of FA [formulary apportionment] is in dispensing with the need to value intra-group transactions, so eliminating direct opportunities to shift profits through transfer pricing and other devices. And by then allocating the base using proxies to substantial activities, it holds the prospect of aligning tax payments more closely with economic fundamentals.")

181. *See* James R. Hines Jr., *Income Misattribution Under Formula Apportionment*, 54 EUR. ECON. REV. 108 (2010) (showing that formulas included in proposals for formulary apportionment are not strongly correlated with determinants of business incomes); *see also* INT'L MONETARY FUND, *supra* note 29, at 39 (suggesting that the primary appeal of formulary apportionment is in dispensing with the need to value intra-group transactions, which would eliminate direct opportunities to shift profits through the current tax regime).

182. Ilan Benshalom, *How to Redistribute: A Critical Examination of Mechanisms to Promote Global Wealth Redistribution*, 64 U. TORONTO L. J. 317, 354 (2014).

183. Heinz-Klaus Kroppen, Roman Dawid & Richard Schmidtke, *Profit Split, the Future of Transfer Pricing? Arm's Length Principle and Formulary Apportionment Revisited from a Theoretical and a Practical Perspective*, *in* FUNDAMENTALS OF INTERNATIONAL TRANSFER PRICING IN LAW AND ECONOMICS 267, 273 (Kai A. Konrad & Wolfgang Schön Yariv eds., 2012).

184. For example, a policy paper issued by the International Monetary Fund estimates how the different weights in sales, assets, and employment used in the formula would favor different groups of countries (advanced, developing, and "conduit" countries). The paper concludes that advanced economies generally gain tax base whichever factor is used and emerging and developing economies would gain base only if heavy weight is placed on employment. INT'L MONETARY FUND, *supra* note 29, at 39–40.

Explicitly incorporating in the formula one or a combination of the normative principles discussed in this Article is more likely to achieve fairness in the prospective changes of the international tax order. A consideration for the ethics of burden sharing might suggest that an apportionment formula should incorporate—among the economic factors commonly proposed—additional factors that consider the prospective beneficiary pays and the ability to pay principles.[185] In this case, it would not be unreasonable to initially apportion more tax base to both prospective losers and poorer countries and gradually reduce the share of prospective losers.[186] More importantly, a formula that, for example, directly incorporated some economic or human development indicator would arguably be more suitable to accomplish inter-nation equity, as it would allow a discussion of fairness in the formula to be more transparent[187] and less reliant on estimations that might suffer from data limitations.[188]

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185. Although not focused on the issue of burden sharing discussed in this Article, Ilan Benshalom argues that the reallocation of taxing rights is more efficient in promoting international wealth redistribution than alternative policies. Benshalom, *supra* note 182.

186. As for the ability to pay, the formula should self-adapt. As the development level of countries evolve, the changes should reflect in the chosen indicator (e.g., GNI/n or HDI).

187. A formula based on purely economic factors (such as sales, employment, or assets) would likely generate *apparently* technical disagreements on the economic suitability of each of these factors, when the *real* interests behind these discussions would be which countries would eventually gain from one or another allocation factor. For example, it has been observed that capital-importing countries might argue for factors based on destination sales while capital-exporting states might argue for apportionment focused primarily on residence. *See* Arthur J. Cockfield, *Formulary Taxation Versus the Arm's-Length Principle: The Battle Among Doubting Thomases, Purists, and Pragmatists*, 52 CAN. TAX J. 114, 120 (2004).

188. *See, e.g.*, INT'L MONETARY FUND, *supra* note 29, at 40 (stating that data limitations prevent calculations of how formulas based on the different economic factors (sales, employment, and assets) would impact on developing countries). *See also* Picciotto, *supra* note 79, at 37 (emphasizing the lack of data, especially relating to developing countries, for this type of quantification).

As commentators have pointed out, a formulary apportionment mechanism could be used either in a *unitary tax regime*, where multinationals would disregard intragroup transactions by consolidating all their earnings, which would require a major overhaul of the current international tax system, or in a *separate-accounting regime*, which is the system adopted in the current treaty-based international tax regime, and which seems more feasible in the present scenario. Reuven S. Avi-Yonah & Ilan Benshalom, *Formulary Apportionment: Myths and Prospects* (Univ. of Mich. Law Sch., Pub. L. & Legal Theory Working Paper Grp., Paper No. 221, 2010), https://ssrn.com/abstract=1693105 [https://perma.cc/TV9U-GJKN] (last visited Sept. 26, 2018). The idea advanced in this Article of including a burden sharing factor in the formula would arguably be applicable in both cases.

Interestingly, although there is a rich literature on the philosophical and practical problems of a fair distribution of the burden of mitigating climate change, the discussion of burden sharing in the tax competition literature is nearly non-existent.[189] In this respect, it should be noted that the different normative principles involved in the climate change debate present significant intersections. Those responsible for causing the problem (the polluters, which are the duty bearers according to the polluter pays principle) are oftentimes the ones which have most benefited from it (the beneficiaries, which are the duty bearers according to the beneficiary pays principle) and are mostly richer industrialized countries (the most able to pay, which are the duty bearers according to the ability to pay principle). In contrast, the intersection of duty bearers in the case of tax competition is significantly narrower. The current beneficiaries of tax competition can hardly be regarded as the most economically capable to bear the costs of institutional reform. Likewise, the causes of the present state of international tax competition cannot be easily assigned to its current beneficiaries. This suggests that, philosophical concerns aside, the implications of how the burden of curbing tax competition is shared should take even more practical relevance.

As international organizations increasingly move towards designing a global framework aimed at reducing tax avoidance and mitigating tax competition, the game of tax competition gradually changes, shifting the distribution of gains and losses among countries. The absence of a serious discussion on how to share the costs of curbing tax competition brings about the risk of a distribution based on power rather than on principle. As commentators have observed, institutional policy decisions tend to reproduce the present imbalance of the global power[190] and a reform of the international tax order is likely to reinforce the existing monopoly of a small number of rich countries over the international tax policy.[191] The lack of an explicit discussion on how to

189 *See supra* notes 10, 97-125 and accompanying text.

190. *See* BRANKO MILANOVIC, WORLDS APART: MEASURING INTERNATIONAL AND GLOBAL INEQUALITY 149 (2005) (arguing that global power is currently held by a relatively small number of very rich people within very rich countries).

191. Christians, *supra* note 86; *see* Dagan, *supra* note 10, at 142–84 (arguing that the shift from competition to negotiated coordination produces unjust inequalities that derive from asymmetries in the relative bargaining power of the negotiating states and suggests that restricting tax competition might produce severe distributive effects on poor countries); *see* Hearson, *supra* note 10, at 5 (pointing out that the track record of global tax governance so far

share the opportunity costs arising from the implementation of global tax reform might result in countries with less negotiating power bearing most of these costs.

suggests that institutional international decisions would likely favor more powerful states); *see also* Martin Hearson, *When Do Developing Countries Negotiate Away Their Corporate Tax Base?*, 30 J. INT'L DEV. 233 (2018) (undertaking a more nuanced analysis of the determinants of tax treaty negotiation outcomes, such as government's revenue base, its reliance on corporate tax, investment asymmetries, and knowledge and negotiation experience).

It is worth noting that since there is no generally accepted baseline of acceptable tax competition against which to define harmful tax competition, different countries have been defining tax competition based on what shifts the rules in their own favor. Lilian V. Faulhaber, *The Trouble with Tax Competition: From Practice to Theory*, 71 TAX L. REV. 311 (2018).