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"Human Rights at the Borders of Tax Sovereignty"

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Vanderbilt Hall-208
Time: 4:00-5:50p.m.
Week #4

SCHEDULE FOR SPRING 2017 COLLOQUIUM NYU TAX POLICY
(All sessions meet from 4:10-6:00 pm in Vanderbilt 208, NYU Law School)

1. Monday, January 23 – Lily Batchelder, NYU Law School. "Accounting for Behavioral Biases in Business Tax Reform: The Case of Expensing."

2. Monday, January 30 – Mark Gergen, Berkeley Law School. "How to Tax Global Capital."

3. Monday, February 6 – Alan Auerbach, Berkeley Economics Department. "U.S. Inequality, Fiscal Progressivity, and Work Disincentives: An Intra-generational Accounting."

4. **Monday, February 13 – Allison Christians, McGill Law School. "Human Rights at the Borders of Tax Sovereignty"**

5. Tuesday, February 21 – Jason Oh, UCLA Law School. "Are the Rich Responsible for Progressive Marginal Rates?"

6. Monday, February 27 – Stephen Shay, Harvard Law School. "'A Better Way' Tax Reform: Theory and Practice."

7. Monday, March 6 – Scott Dyreng, Duke Business School. "Trade-offs in the Repatriation of Foreign Earnings."

8. Monday, March 20 – Daniel Hemel, University of Chicago Law School. "Federalism as a Safeguard of Progressive Taxation."

9. Monday, March 27 – Leonard Burman, Urban Institute. "Is U.S. Corporate Income Double-Taxed?"

10. Monday, April 3 – Kathleen Delaney Thomas, University of North Carolina Law School. "Taxing the Gig Economy."

11. Monday, April 10 – Julie Cullen, UC San Diego Department of Economics. "Political Alignment and Tax Evasion."

12. Monday, April 17 – Miranda Perry Fleischer, University of San Diego Law School. "The Libertarian Case for a Universal Basic Income."

13. Monday, April 24 – Joel Slemrod, University of Michigan Business School. "Taxing Hidden Wealth: The Consequences of U.S. Enforcement Initiatives on Evasive Foreign Accounts."

14. Monday, May 1 – Richard Vann, University of Sydney Law School. "International tax post-BEPS: Is the corporate tax really all that bad?"

Human Rights at the Borders of Tax Sovereignty

Allison Christians*

Tax scholarship typically presumes the state's power to tax and therefore rarely concerns itself with analyzing which relationships between a government and a potential taxpayer normatively justify taxation, and which do not. This paper presents the case for undertaking such an analysis as a matter of the state's obligation to observe and protect fundamental human rights. It begins by examining existing frameworks for understanding how a taxpayer population is and ought to be defined. It then analyzes potential harms created by an improperly expansive taxpayer category, and those created by excluding from consideration those beyond the polity even if directly impacted by the tax regime. It concludes that a modified membership principle is a more acceptable framework for normative analysis of the jurisdiction to tax, even while acknowledging the overwhelming weight of existing perceptions about the bounds of the polity and the state-citizen relationship as significant barriers to acceptance.

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I. INTRODUCTION

Which states can rightfully claim tax on the income or transactions of a multinational business, a pooled investment vehicle, or a dual national? Conceptions about what gives any one person the right to demand resources from any other filter their way through the institutions of governance into tax regulation, where the presence and absence of principles are exposed in implementation. Assumed normative foundations supporting the jurisdiction to tax, on the part of the state, and the obligation to pay tax, on the part of the taxpayer, are often acknowledged and challenged only when the claims of one state over someone or something collide with those of another. But such collisions merely reflect one aspect of the deeper struggle for principle that characterizes the construction of the tax state.

Despite the clear need for normative analysis of the jurisdiction to tax, scholars often simply presume the state's power and right to tax and therefore rarely concern themselves with analyzing which relationships between a government and a potential taxpayer normatively justify taxation, and which do not. Eliding this difficult question leads to unexamined claims about the state's obligation to act on behalf of "its" people, and the taxpayers' obligation to pay a fair share of tax to "their" state. These unexamined claims can lead states to place unjustified obligations on individuals, or conversely to ignore those who are deemed beyond the polity yet are affected by its policy choices. Those experiencing such outcomes are marginalized by the nature of the harm itself, and may find few or no means to assert their right to be excluded or included, as the case may be. It falls to scholarly inquiry to highlight what is otherwise unnoticed or, when acknowledged, viewed as peripheral.

This paper accordingly analyzes theoretical assumptions and practical observations about the jurisdiction to tax, and demonstrates that a legitimate claim is necessarily conditioned on respecting the fundamental rights of those claimed but also, and more controversially, those not claimed. It begins by examining three rationales for the jurisdiction to tax—namely, sovereignty, nexus, and membership—and exploring the normative foundations of each. It then tests these foundations by applying them to two contemporary jurisdictional claims that have been criticized as improperly over- or under-inclusive. The paper concludes that membership, specifically tied to tax-relevant factors, is a more satisfactory framework for normative analysis of the jurisdiction to tax than either sovereignty or nexus, but acknowledges the overwhelming weight of existing perceptions about the bounds of the state as significant barriers to acceptance.

II. WHAT EXPLAINS THE JURISDICTION TO TAX?

To probe a state's decision that it has the jurisdiction to impose a tax on someone is to identify the dominance of a state's "rights" (really, the appropriate use of sovereign power) over or against the rights of an individual, since the act of taxation is the act of preserving some resources for the use of a polity instead of that individual. The scope of and potential boundaries on the jurisdiction to tax are typically explained in the tax literature by one of two main rationales, namely sovereign entitlement and nexus. But the normative content of each of these rationales is unsound, confusing power, which is the state's ability to enforce its will, and right, which is a normatively justifiable exercise of that power. A third rationale, found in political theory, is referred to as the membership principle, and explains the relationship between individual and state in terms of demonstrated voluntary belonging to a shared community. Each of these rationales is examined in turn.

A. SOVEREIGNTY

The power to tax is often cast as a defining feature of sovereignty, such that any state could theoretically impose a tax on any person or thing, with the only constraints being practical.[1] A related view holds that states, as creatures of international law, are constrained by nothing but the equally valid jurisdictional claims of their fellow states.[2]

[1] *See, e.g.*, *Austro-German Customs Union Case*, Advisory Op. (1931), P.C.I.J. Ser. A/B, No. 41 ("The Independence of Austria…is nothing else but the existence of Austria…as a separate state and not subject to the authority of any other state or group of states."); *B.C. Electric Railway Co. v. R.* [1946] A.C. 527 (holding that since the powers of Canada's Parliament were "as plenary and as ample within the [constitutional] limits prescribed…as the Imperial Parliament in the plenitude of its power possessed or could bestow," the federal government was empowered to "rais[e] money by any mode or system of taxation, even though such laws have an extra-territorial operation."); BRIAN J. ARNOLD, TAX DISCRIMINATION AGAINST ALIENS, NON-RESIDENTS, AND FOREIGN ACTIVITIES: CANADA, AUSTRALIA, NEW ZEALAND, THE UNITED KINGDOM, AND THE UNITED STATES 7 (1991) ("A country's legal authority to levy tax is effectively limited only by practical considerations of enforcement and collection. Rules of public international law or domestic constitutional law restrict a country's jurisdiction to tax only in narrow, relatively insignificant ways."); SOL PICCIOTTO, INTERNATIONAL BUSINESS TAXATION 307 (1992) ("From the point of view of formal sovereignty, there is no restriction on a state's right to tax, and it may be exercised without regard to its effects on other states."); Stanley S. Surrey, *Current Issues in the Taxation of Foreign* Corporate *Investment*, 56 COLUM. L. REV. 815, 817 (1956) (stating that "the assertion of jurisdiction is essentially a matter of national policy and national attitudes" not restricted by law); Martin Norr, *Jurisdiction to Tax and International Income*, 17 TAX L. REV. 431 (1962) (stating that "[n]o rules of international law exist to limit the extent of any country's tax jurisdiction" and that "a country is free to adopt whatever rules of tax jurisdiction it chooses"); Harold Wurzel, *Foreign Investment and Extraterritorial Taxation*, 38 COLUM. L. REV. 809, 812, 814 (1938) (stating that "taxing power stems from sovereignty and sovereignty is omnipotence" and denying the existence of "anything in the written or unwritten law of nations" to limit the jurisdiction to tax, based on the lack of any such articulation by international tax law scholars and policymakers to that date).

[2] See, e.g., *The Schooner Exchange v. McFadden*, 11 U.S. (7 Cranch) 116 (1812) (associating sovereign immunity with the territorial right of each sovereign against encroachment by the others); United States v. Harden (1963) 44 W.W.R. 630, 634 ("an assertion of sovereign authority by one State within the territory of another…is (treaty or convention apart) contrary to all concepts of independent sovereigns"). Contemporary scholarship notes that "the 'sovereignty' of states has … become understood to be reflected in and constrained by rules of jurisdiction which define the limits of the powers of coexisting 'sovereigns', in particular, the scope of regulatory authority of states in international law." Alex Mills, *Rethinking Jurisdiction in International Law*, 84 BRIT. Y.B. INT'L L. 187, 194 (2014). This view is associated with contemporary understanding regarding the relationship between states operating in a fundamentally cooperative international society. *See, e.g.*, Cees Peters, ON THE LEGITIMACY OF INTERNATIONAL TAX LAW 35 (2013). It is a view that has been adopted, if implicitly, by the OECD. See OECD, REPORT ON HARMFUL TAX PRACTICES 15 (1998) ("Countries should remain free to design their own tax systems as long as they abide by internationally accepted standards in doing so"); Edwin van der Bruggen, *State Responsibility under Customary International Law in Matters of Taxation and Tax Competition* 29 INTERTAX 115, 116 (2000) (exploring the OECD's efforts to frame the rights of

The implication of both of these positions is that the state is entitled to absolute authority to rule over a people and a territory.[3] In this narrative, the taxpayer is a mere object of regulation, possibly to be fought over where two sovereigns collide, but ultimately uninvolved in the act of claiming and regulating. Tax scholarship implicitly accepts this narrative when it uncritically assumes the *a priori* nature of a state's right to tax.[4]

1. The Powerful and Needy State

When scholars explicitly acknowledge the assumption that power equals right, a defense typically proceeds on grounds that sovereign status is self-evidently, intrinsically, and of necessity associated with the power to tax.[5] Many equate power with entitlement by referring to Hobbes's argument that "[t]hese are the rights which make the essence of sovereignty . . . the power of raising money."[6] Others equate

jurisdictions to use tax rules that inflict harm on others). Accordingly, the classic-positivist view of statehood, which ascribes no limits to the tax jurisdiction other than that set by the state itself, is rejected to the extent it implies any duty on the part of other countries in respect of their own taxpayers. It should be noted, however, that equality of sovereignty implies that states are equally entitled to deference from others, but not that they have equal power or resources to defend their entitlement.

[3] Mills, *supra* at 196. The other main jurisdictional basis is territoriality, which is said to "reflect the intimate connection between territorial control and statehood in international law." *Id.*

[4] Few governments would leave their authority to theory, since there are always those who will go to great lengths to challenge the imposition of any tax. As a result, most countries explicitly claim their right to tax under formative documents such as constitutions. For example, Canada's Constitution duly authorizes the federal government to impose taxes of any kind, while it authorizes the provinces and territories to impose direct taxation. CANADA CONSTITUTION ACT, 1867-1982 s. 91 ("T]he exclusive Legislative Authority of the Parliament of Canada extends to all Matters coming within the Classes of Subjects next hereinafter enumerated; that is to say, ...3. The raising of Money by any Mode or System of Taxation,"); s. 53, 54, and 125 ("In each Province the Legislature may exclusively make Laws in relation to Matters coming within the Classes of Subjects next hereinafter enumerated; that is to say,...2. Direct Taxation within the Province in order to the raising of a Revenue for Provincial Purposes....9. Shop, Saloon, Tavern, Auctioneer, and other Licences in order to the raising of a Revenue for Provincial, Local, or Municipal Purposes. "). Similarly, the U.S. Constitution explicitly provides that "The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States." U.S. CONST., Art. I, Sec. 2. However, the Constitution also originally stated that "Representatives and direct Taxes shall be apportioned among the several States," according to a formula that infamously discounted Native Americans and slaves. U.S. CONST. Art. I. Sec. 8. Mainly owing to some contestation over the meaning of direct taxes, the Sixteenth Amendment was passed by Congress in 1909 and ratified in 1913, so as to ensure that a federal income tax could be levied without apportionment. U.S. CONST. Amend. XVI ("The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.). Together, Article I and the Sixteenth Amendment unequivocally enable U.S. lawmakers to impose taxation, yet both are silent on the limits to that power.

[5] *See, e.g.*, Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 54 TAX L. REV. 261, 227 (2001) ("No function is more at the core of government than its system of taxation.")

[6] THOMAS HOBBES, LEVIATHAN OR THE MATTER, FORME AND POWER OF A COMMON WEALTH ECCLESIASTICAL AND CIVIL (1651). A century earlier, Jean Bodin more explicitly claimed that "[t]he right of levying taxes and imposing dues, or of exempting persons from the payment of such, is also part of the power of making law and granting privileges." JEAN BODIN, SIX BOOKS ON THE COMMONWEALTH

necessity with entitlement, citing the state's need for revenues in order to exist as a moral justification for taxation.[7] Both intuitions lack normative support.

In maintaining that taxation is essential to sovereignty, Hobbes was defending an argument that the sovereign, ideally a monarch, possesses the divinely bestowed and inviolable right to command his subjects, including an absolute power to raise money from them.[8] Hobbes' appeal to sovereignty defends the idea that even a self-appointed and unaccountable ruling class, so long as it maintains order, has an inherent right to extract rent from everyone else, including by force or threat of force. This is far from a compelling justification of the jurisdiction to tax.[9] The absolutist view is not only incompatible with virtually any conception of justice; it is also not an accurate description of how states have actually carried out their power.[10] Instead, the sovereign state's decision to rely on taxation as the primary means of raising money should be viewed as an admission that its own power is self-evidently and intrinsically limited by the countervailing force of individual rights.

This is explained by the simple observation that a state that does not concern itself with individual rights, ruling instead by brute force, would not need to tax but could raise money by commandeering whatever resources were necessary to its own

47 (M.J. Tooley trans., Blackwell 1955) (1576). *See, e.g.*, Deborah Bräutigam, *Building Leviathan: Revenue, State Capacity, and Governance*, 33 IDS BULL. 10, 10 (2002) (quoting Hobbes); Peggy B. Musgrave, *Sovereignty, Entitlement, and Cooperation in International Taxation*, 26 BROOK. J. INT'L L. 1335, 1336 (2001) ("international law" recognizes "national entitlements to tax").

[7] *See, e.g.*, Jonathan R. Macey, *Government as Investor: Tax Policy and the State*, in ELLEN FRANKEL PAUL, ET AL, EDS., TAXATION, ECONOMIC PROSPERITY, AND DISTRIBUTIVE JUSTICE 255, 266 (2006) ("One moral justification for giving government the power to tax is that such power is justified simply because the state needs revenue and the state is legitimate. ...Alternatively, one can claim that the state lacks the power to impose tax under some natural rights theory. But as long as the state has the power to collect taxes in practice, this argument is purely theoretical and academic.").

[8] Hobbes supra; see also Bodin, supra (arguing, contra Aristotle's view of the superiority of mixed forms of government, that to sustain order, government must rest the absolute power to make, interpret, and enforce laws in one person or institution, because competing rulemakers would inevitably disagree and resort to force, and ultimately civil war, to resolve their differences.). For a review of Hobbes' and Bodin's shared views of the need for absolute supremacy in a single sovereign, see PRESTON KING, THE IDEOLOGY OF ORDER: A COMPARATIVE ANALYSIS OF JEAN BODIN AND THOMAS HOBBES 58-60 (1974).

[9] See Macey, *supra* at 266 ("[G]overnments compete for the right to control various land masses. States that lack the power to tax inevitably will fail in Darwinian competition for power and authority with rival states. For this reason alone, taxation will survive as a feature of civil life. This is troubling to those interested in controlling the power of government, not only for the obvious reasons that taxation creates distortions in the real economy and provides the state with sufficient resources to create a leviathan that can destroy fundamental rights and quash dissent, but also for other reasons."). Certainly, a Hobbesian view was insufficient to convince the American colonists that the English King was their permanent sovereign to whom both allegiance and tax was owed. See, e.g., JOHN PHILLIP REID, CONSTITUTIONAL HISTORY OF THE AMERICAN REVOLUTION (1986-1993).

[10] *See, e.g.*, Hanna Pitkin, *Obligation and Consent II*, 60 AM. POL. SCI. R. 39, 39 (1966) ("legitimate authority is precisely that which ought to be obeyed, to which one ought to consent, which deserves obedience and consent, to which rational men considering all relevant facts and issues would consent, to which consent can be justified. Anything or anyone else who tries to command us is then merely coercing, and is not entitled to our obedience.").

functioning.[11] Yet few states act in this manner, and it is clear that to do so would be to act without justification. A main reason is that virtually all societies recognize that individuals are entitled to certain basic rights, which would prohibit as unjust the use of force to seize resources at random.

These rights are of course embodied in a certain core set of principles laid out in the Universal Declaration of Human Rights (UNDHR) and multiple other international agreements that embody the UNDHR principles, to which most states adhere.[12] Signatories to these conventions explicitly commit themselves to regulate, including with respect to tax, in a manner that accepts as foundational the fundamental rights of the individual.[13]

The UNDHR clearly lays out as fundamental every individual's rights to liberty and property as well as freedom from unwarranted interference or intrusion by the state, which prohibits forced taking without recompense.[14] These rights are commonly articulated in various forms, with various adaptations and interpretations, in national constitutions and laws. Canada's Charter of Rights, for example, states *inter alia* that everyone has the right not to be deprived of life, liberty or security "except in accordance with the principles of fundamental justice" and to be secure against unreasonable search and seizure.[15] Similarly, the U.S. Constitution declares that no

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[11] This idea was explored in the so-called "Carter Commission Report," an independent study by accountants and tax law practitioners commissioned by the Canadian Conservative government in 1962 to examine the existing tax system and make recommendations to ensure a steady flow of revenue. In laying out the parameters of this task, the Prime Minister asked the commission to consider reforms necessary "to achieve greater clarity, simplicity, and effectiveness in the tax laws," but the group found that it could not answer this pragmatic question without first coming to terms with the normative foundations of the nation state's exercise of taxation. Order in Council, PC 1962-1334, reprinted in Canada, Royal Commission on Taxation, Report (Ottawa: Queen's Printer, 1966) (Chair: Kenneth LeM Carter), vol. 1 at v [*Carter Commission*].

[12] *See e.g.* Michael Boylan, A THEORY OF NATURAL HUMAN RIGHTS (2015). The UNDHR established the main principles underlying several international conventions and treaties, including the 1948 International Covenant on Civil and Political Rights, Dec. 16, 1966, 999 U.N.T.S. 171 [ICCPR], the 1966 International Covenant on Economic, Social, and Cultural Rights, Dec. 16, 1966, 999 U.N.T.S. 3 [ICESER], the 1979 Convention on the Elimination of Discrimination Against Women [CEDAW], the Convention on the Elimination of All Forms of Racial Discrimination [ICERD], and the 1981 Declaration on the Elimination of All Forms of Intolerance and of Discrimination Based on Religion or Belief, G.A. Res. 55, U.N. GAOR, 36th Sess., Supp. No. 51, U.N. Doc A/36/684 (1981), at http://www.un.org/documents/ga/res/36/a36r055.htm.

[13] Human rights are defined by many as rights that all human beings share simply by virtue of their common humanity. See, e.g., Boylan *supra;* Jack Donnelly, International Human Rights 18 (1998); Alan Gewirth, Human Rights: Essays on Justification and Applications 1 (1982); H.L.A. Hart, *Are There Any Natural Rights?*, 64 Phil. Rev. 175 (1955); A. John Simmons, *Human Rights and World Citizenship, in* Justification and Legitimacy: Essays on Rights and Obligations 185 (2001).

[14] UNDHR Art. 3, 12, 17 (Stating in Art. 3 that "Everyone has the right to life, liberty and security of person"; in Art. 12 that "No one shall be subjected to arbitrary interference with his privacy, family, home or correspondence, nor to attacks upon his honour and reputation. Everyone has the right to the protection of the law against such interference or attacks" And in Art. 17 that "No one shall be arbitrarily deprived of his property.").

[15] CANADA CONSTITUTION ACT, 1867-1982, Art. 7 ("Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of

person shall be deprived of life, liberty, or property without due process of law, and that private property shall not be taken without just compensation.[16]

In extracting resources from individuals, ultimately under threat of force, even if for common projects, the state might seem poised to routinely contravene even the most basic terms of these universally accepted rights.[17] Some scholars, especially prompted by the influential work of Robert Nozick, consider the act of taxation as a clear infringement of such rights and therefore liken the act of taxation to theft.[18] But most, including Nozick himself, have acknowledged the equally valid counter proposition that individuals cannot ensure that any of their rights are protected unless they voluntarily relinquish some resources to the state to act on their behalf.[19] This is a Hobbesian argument that, but for the state, individuals would be able to exercise none of their individual rights to property (or liberty, or security, etc). However, these accounts condition the state's right to raise money on its doing so by means and methods that protect the rights of those who initially agreed to its authority precisely because they sought to forestall the constant state of war that is life without the state, in Hobbesian terms.[20]

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fundamental justice") and 8 ("Everyone has the right to be secure against unreasonable search or seizure").

[16] U.S. Constitution Amend. V ("No person ... shall be ... deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation") and Amend. XIV ("No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws"). Subnationally, legal texts echo the same sentiments. For example, Quebec's Civil Code opens with a declaration that "Every person is the holder of personality rights, such as the right to life, the right to the inviolability and integrity of his person, and the right to the respect of his name, reputation and privacy." Civil Code of Quebec, Art. 3. Similarly, U.S. states that impose income taxes have consistently enacted similar safeguards for individual rights. See, e.g., David E. Joyce, *Raiding the Confessional: The Use of Income Tax Returns in Nontax Criminal Investigations*, 48 Fordham L. Rev. 1251 (1979) (reviewing reforms to protect taxpayer rights that were adopted in several states after the Nixon scandal).

[17] Locke, *supra* ("if any one shall claim a power to lay and levy taxes on the people, by his own authority, and without such consent of the people, he thereby invades the fundamental law of property, and subverts the end of government: for what property have I in that, which another may by right take, when he pleases, to himself?")

[18] ROBERT NOZICK, ANARCHY, STATE AND UTOPIA (1974); *see also* RICHARD EPSTEIN, TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN (1985); LOREN LOMASKY, PERSONS, RIGHTS AND THE MORAL COMMUNITY (1987).

[19] Nozick, *supra* (laying out the conditions for society-forming agreements to compel the payment of taxes based on mutual benefit. Nozick asks if the state did not exist, "[w]ould one be needed and would it have to be invented? He launches from this question into a theory that justifies the existence of the (minimal) state to order human society by positing that even if it didn't exist, the state would naturally arise.). The central argument of perhaps the most widely-recognized book on taxation and philosophy argues that the state has a justifiable claim of right to tax because it contributes to economic outcomes by providing the laws, institutions, and mechanisms necessary to enable market transactions. LIAM B. MURPHY AND THOMAS NAGEL, THE MYTH OF OWNERSHIP: TAXES AND JUSTICE (2002).

[20] *See, e.g.*, Murphy and Nagel *supra*; see also Macey *supra* at 259 ("Embracing in a disciplined fashion Thomas Hobbes's assumptions about the proclivities of man and the nature of the state requires one to recognize that government is the ultimate "necessary evil.").

From this perspective, while the state's existence is necessary to protect humans against their own state of being under conditions of lawlessness, having undertaken to exist for that function requires the state to sustain itself financially in a manner that does not simply recreate state of nature conditions with itself as the main threat to order and peace. Commandeering resources is out of the question in that case; instead, taxation arises as a potentially justifiable method for raising money.

This addresses only the threshold question of right with respect to the state's jurisdiction to tax, however. The form and methods by which the state carries out its taxing authority remains subject to moral inquiry, such that justice and fairness are indisputably vital to tax policy analysis.[21] Moreover, not everything a state does to fund a government is immediately recognizable as taxation in the sense of compulsory payments according to a set of established rules. For example, a state might raise funds by licensing or selling state-controlled resources, by directly owning the means of production, by interjecting itself as a sole buyer of domestic goods or services, by printing money, or by borrowing funds. Each of these activities is like taxation in the sense that each places resources under the direct control of the government and beyond the reach of individuals. Each might thus be viewed as economic equivalents to taxation, indirect forms of taxation, or taxation by another name, and therefore equally subject to moral inquiry.

Casting the state as essential facilitator of basic human entitlements invokes social contract theory as a justification for the authority of the sovereign, and is therefore potentially more satisfying than blanket deference to the state as an absolute authority owing to either its power or its need.[22] However, even social contract theory glosses over some major difficulties by assuming that a clear relationship always exists between a given state and a given individual. The assumption works well enough in many cases (and works best in circumstances of non-mobility of capital, goods, and labour), but it fails if it does not include, as a threshold matter, some principled explanation for the initial association between a specific sovereign and a specific individual.[23]

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[21] See, e.g., Michael J. Graetz, *Taxing International Income – Inadequate Principles, Outdated Concepts, and Unsatisfactory Policy*, 54 TAX LAW REV. 261, 307 (2001) ("deciding to tax income reflects a decision to place issues of fairness at the heart of tax policy debates").

[22] *See, e.g.*, Jean-Jacques Rousseau, *Of the Social Contract*, *in* The Social Contract & Other Later Political Writings 39,50 (Victor Gourevitch ed., Cambridge Univ. Press 1997) (1791) (arguing that people need social order to preserve their innate freedom through cooperation, and stating the theory of social contract as the idea that "[e]ach of us puts his person and all his full power in common under the supreme direction of the general will; and in a body we receive each member as an indivisible part of the whole."); John Locke, Second Treatise on Government (1690), at Sec. 140 ("It is true, governments cannot be supported without great charge, and it is fit every one who enjoys his share of the protection, should pay out of his estate his proportion for the maintenance of it. But still it must be with his own consent, i.e. the consent of the majority, giving it either by themselves, or their representatives chosen by them: for if any one shall claim a power to lay and levy taxes on the people, by his own authority, and without such consent of the people, he thereby invades the fundamental law of property, and subverts the end of government: for what property have I in that, which another may by right take, when he pleases, to himself?").

[23] As explored in Part III, *infra*.

Without this explanation, social contract theory cannot support sovereign entitlement as a justification for taxation for any case other than the individual who intentionally, voluntarily, and with resources to choose differently, never ventures beyond a single state for any purpose, personal or economic.[24] This is because social contract theory fails to provide a principled basis for limiting a community by territory or population and thereby excluding anyone from consideration.[25] The work of John Rawls, which is almost instinctively cited in normative tax scholarship, illuminates the theoretical problem.

2. The Just State

In his seminal work *A Theory of Justice*, Rawls developed what are now fundamental principles of a just society, including the protection of fundamental liberties and acceptance of social and economic inequality only on conditions of equality of opportunity and of maintaining or bettering the lot of the least-advantaged.[26] But in later work that attempted to apply his reasoning to a world in which there is more than a single society, Rawls inexplicably abandoned the individual, instead envisioning states, as embodiments of their populations, becoming parties to a second-level social contract.[27] He therefore argued that rational states should seek an international system that favors political independence and non-interference amongst themselves as states, while ensuring a truncated list of essential individual rights for their associated populations.[28]

This account is inconsistent with the core foundation of Rawls' theory of justice, as well as inapposite to how states have behaved toward each other. The main inconsistency is that a second-stage social contract among sovereigns is missing the core element that makes the theory of justice plausible. Rawls argued that the coherence

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[24] It would likely also have to be the case that the state in question never abused that individual or any of the others it included in the hypothetical social contract.

[25] I explore this idea more thoroughly in Allison Christians, *Sovereignty, Taxation and Social Contract*, 81 MINN. J. INT'L. L. 99 (2009).

[26] JOHN RAWLS, A THEORY OF JUSTICE (1971) [hereinafter Theory of Justice] at 92. To briefly summarize, Rawls posited that people in a hypothetical pre-political "original position" would form a just social contract among themselves if they were ignorant about what their ultimate position would be in that society.

[27] John Rawls, THE LAW OF PEOPLES: WITH "THE IDEA OF PUBLIC REASON REVISITED" 62–64 (1999) [hereinafter Law of Peoples]. Rawls explicitly rejects the use of the term "nation" or "state," placing political authority in "peoples," which he attempts to define as groups of persons aligned by "common sympathies," and a "willingness to live together under the same set of democratic principles." However, as Nussbaum and others have shown, the departure is "confused and confusing," as well as possibly indistinguishable from current conceptions of statehood in any event. NUSSBAUM at 246.

[28] Law of Peoples at 106. (Rawls' short list of duties includes a just war theory and a theory that people will want states to honor a bare minimum of human rights and help people living under conditions that preclude the existence of a just (national) social regime (what he calls "burdened societies.") The list is shorter than the list of basic liberties he outlines in *A Theory of Justice*. A THEORY OF JUSTICE at 61. Analogizing to the original contract, the "veil of ignorance" would prevents representatives from knowing the size, wealth, etc. of their states, so they "will develop a system that ensures their political independence, civil liberties, and self-respect as a people." Mike Wiser, Book Review, 14 HARV. HUM. RTS. J. 299, 299 (2001).

of the social contract theory rests on the idea that persons in the original position are subject to the "circumstances of justice" as outlined by Hume and Rousseau: in general, everyone has a need to form a social contract because resources are relatively scarce, everyone has something with which to bargain, and no one has too much.[29] Rawls observed that since all people who start out in circumstances of justice would universally support the ideals he laid out for a just society, all societies should therefore universally seek to embody them. Accordingly, Rawls concluded that societies that do not pursue equal basic liberties for all, that tolerate inequality of opportunity, or that pursue social or economic gain at the expense of the least-advantaged among them, are illiberal, and therefore, unjust.[30]

In dictating that everyone will and moreover should want to contract with each other on equal terms because no one is better off in a Hobbesian state of nature, the circumstances of justice conceptually respects the autonomy of the individual even when the social contract, out of practical necessity, depends on implied rather than actual agreement.[31] However, the assumption falters when the state is delegated to act on behalf of one group of people, with respect to other groups of people, because states are not, and cannot be imagined to have ever been, in circumstances of justice with respect to each other. Instead, wealthy states are clearly better off dominating poorer or weaker states and summarily excluding the populations of such states from their own domestic legal orders, instead of bargaining with such states for a just international order in which every person would have an equal demand for basic entitlements.[32]

The preference to dominate in a state of nature rather than contract to pursue the equality of all plays out openly in international tax relations, where the world's wealthiest states have routinely and consistently used their outsize economic power to make decisions that benefit themselves, and only in recent years, after intense public pressure, expressed any need to include other states in their deliberations.[33] In fact, the

[29] *Id.* at 137; *see also* DAVID HUME, A TREATISE OF HUMAN NATURE (Selby-Bigge ed., Oxford Univ. Press 2d. 1978) (1739).

[30] Rawls *supra* at 453-62.

[31] MARTHA C. NUSSBAUM, FRONTIERS OF JUSTICE: DISABILITY, NATIONALITY, SPECIES MEMBERSHIP (2006)

[32] Nussbaum, *supra*. An argument to the contrary would posit that many states do find it mutually beneficial to contract with each other on tax, as evidenced in the continuous efforts to coordinate tax jurisdictions and enhance cooperation via the OECD. However, since social contract theory is only coherent if every member of the implied contract would benefit from entering into the contract as compared to the situation in the state of nature, the fact that some states have in fact agreed to contract on mutually beneficial terms in taxation is insufficient to imply that all would do so, and can be assumed to have done so, when there are also states that have clearly and actively resisted joining any such effort. See, e.g., Vaughn E. James, *Twenty-First Century Pirates of the Caribbean: How the Organization for Economic Cooperation and Development Robbed Fourteen CARICOM Countries of Their Tax and Economic Policy Sovereignty*, 34 U. MIAMI INTER-AM. L. REV. 1 (2002).

[33] *See* Christians, *supra* note 25; Hugh Ault, *Some Reflections on the OECD and the Sources of International Tax Principles*, 70 TAX NOTES INT'L 1195-1201 (2013); PETER CARROLL & AYNSLEY KELLOW, THE OECD: A STUDY OF ORGANISATIONAL ADAPTATION (2011); Richard Eccleston, *The OECD and Global Economic Governance*, 65 AUSTL. J. INT' L AFF. 243, 243-46 (2011); Lyne Latulippe, *The Expansion of the Bilateral Tax Treaty Network in the 1990s: The OECD's Role in International Tax Coordination*, 27 AUST. TAX FORUM 851-883 (2012); Jeffrey Owens and Sebastien Beer, THE STRUCTURES AND MANDATES OF EIGHT INTERNATIONAL AND REGIONAL ORGANIZATIONS

international tax order, characterized as it has been for a century by unilateral power exercised key players, bilateral negotiations among selected parties, rare and hard-fought regional cooperation, and, until recently, unequivocal resistance to multilateralism and a single world tax order, are perhaps the best example for why social contract theory cannot possibly explain relations among states. Instead, states have jealously guarded their autonomy on taxation, supported by scholarship that rejects cosmopolitan theories of justice and instead accepts the privileging of "national" interests, even if doing so harms those outside, as a rational and just prerogative of the state.

Social contract theory is therefore insufficient to rescue sovereignty from its inherently unjust nature. Instead, to assert that sovereignty implies the power to tax as an act of the collective will of "the people" is to do little more than demonstrate precisely why the state cannot be free to exercise such a power without restraint. The opposite conclusion must be reached: the state must offer some prior normative justification for claiming those it seeks to regulate through taxation, and then, having asserted the right to tax, must carry out that power in a manner consistent with individual rights. This is why the first threshold question for any tax system is defining who may be taxed in a way that accords with generally accepted individual rights, and why failing in this task has caused major harms to individuals as well as systemic problems for the overall international tax order.[34]

Determining who belongs and who does not belong in a taxpayer population is a deeply political act with major implications for the rights of individuals vis à vis the state. Often triggered by tax, struggles and even wars for independence have been fought over the act of defining a polity.[35] To be just in this pursuit requires the government to rightfully earn the individual's acquiescence to its regulatory authority. Declarations about the intrinsic power of sovereign states, and about the obvious need for sovereigns to raise revenue in order to be a sovereign at all, are simply insufficient to overcome the countervailing force of individual rights. Appeals to social contract theory, in which sovereignty as a respected status offers the promise of a mutually beneficial relationship to a people, point in a more principled direction, but still more is needed to ensure that the individual is an agent and not an object in dealings with the state. In tax scholarship, this further justification of the state's power to tax is most commonly achieved by reference to nexus.

B. Nexus

In the early days of income taxation, the League of Nations took note of increasing conflicts involving the jurisdiction to tax, and famously asked four economists to lay out a framework for dividing the tax base in a principled way, or, at

THAT WORK IN TAX (2014); PETER DIETSCH, CATCHING CAPITAL: THE ETHICS OF TAX COMPETITION (2015).

[34] See *infra* discussion at Part III.A.

[35] *See, e.g.*, Kenneth LeM. Carter, *Canadian Tax Reform and Henry Simons*, 11 J. L. & ECON. 231, 241 (1968) ("Over the years there has been scarcely any relationship between government and people which has been more sensitive than taxation and, indeed, which has caused more civil blood-shed.").

least, in a way that would lead the key global powers of the day to agree was to their mutual benefit.[36] In a move that would resonate through the century that followed, the four economists sought to articulate a principled approach to the jurisdiction to tax as a function of what they termed "economic allegiance."[37] Defining an objectively identifiable nexus between the individual and the tax state was a deliberate move away from the political relationship between states and individuals described in social contract theory, which the economists recognized did not and could not sufficiently explain the jurisdiction to tax.[38] While economic allegiance had conceptual merit, the economists chose two types of nexus—residence and source—that states ultimately implemented in ways that arguably defeated the original principle.

The economists' decision to define nexus as economic allegiance arose from their sense that the tax base, as a product of economic activity, ought to be understood not on the basis of a taxpayer's political or personal connections to a state (which, especially in conditions of mobility across borders, could be difficult or impossible to discern), but by economic interaction with and within the state. As the economists put it, "In the modern age of the international migration of persons as well as of capital, political allegiance no longer forms an adequate test of individual fiscal obligation. It is fast breaking down in practice, and it is clearly insufficient in theory."[39] Since income taxation in particular concerned itself with measuring the economic resources available to a person, the economists posited that the state's claim must relate in some fashion to having provided or protected some of those resources.[40]

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[36] For a discussion of the events that led to the appointment of these economists, see Allison Christians, *Networks, Norms and National Tax Policy,* 9 WASH. U. GLOB. STUD. L. REV 1 (2010); Nancy Kaufman, Nancy H. Kaufman, *Fairness and the Taxation of International Income*, 29 LAW & POL'Y INT'L BUS. 167-168 (1998).

[37] Gijsbert W. J. Bruins, Luigi Einaudi, Edwin R. A. Seligman, and Sir Josiah Stamp, REPORT ON DOUBLE TAXATION, April 5, 1923 [hereinafter, 1923 Report]. See Reuven Avi-Yonah, *The Structure of International Taxation: A Proposal for Simplification*, 74 TEX. L. REV. 1301, 1306 (1996) (explaining that this work formed the foundations for contemporary international tax consensus); Steven Dean, *The Incomplete Market for Global Tax Information,* 49 BOST. COLL. L.R. 605, 644-49 (2008), 639 ("It would be difficult to overstate the significance of the work of the committees and experts ... that formed the basis for ... today's very successful international tax regime."); Christians *supra* note 36 (outlining the policy trajectory for global tax consensus from the 1920s to the present); Sjoerd Douma, *The Three Ds of Direct Tax Jurisdiction: Disparity, Discrimination and Double Taxation*, 11 EUROP. TAX. 522, 523 (Nov. 2006) ("the fundamental jurisdictional connection is the territorial basis that refers to jurisdiction over persons, matters and things within the geographical boundaries of a state. In relation to fiscal jurisdiction, this is illustrated by the taxation of income with its source, or a person residing, within the territory. The other jurisdictional connection is personal, based on the nationality or domicile of a person as the connecting factor."), citing RAMON J. JEFFERY, THE IMPACT OF STATE SOVEREIGNTY ON GLOBAL TRADE AND INTERNATIONAL TAXATION 44 (1999).

[38] 1923 Report at 18 ("The older theory of taxation was the exchange theory, which was related directly to the philosophical basis of society in the "social contract," according to which the reason and measure of taxation are in accordance with the principles of an exchange as between the government and the individual.").

[39] 1923 Report at 19.

[40] This idea was also explored in the Carter Commission Report, *supra*; *see also* Carter, *supra* note 35 at 241. The notion that an obligation to pay tax is triggered by having received a benefit of some kind resembles the membership principle described in the next section. The extent to which nexus and

In making the case for basing tax jurisdictional claims on economic instead of political allegiance, the economists argued that an economic interaction with a jurisdiction could be determined by considering four factors. These were the physical location of an object to be taxed, especially an asset that produces income ("*situs*"); the enforceability of rights, for example with respect to an income-producing asset ("enforceability"); the jurisdiction of normal residence by the subject of the tax ("residence"); and, the "origin" of the income to be taxed ("source").[41] The group ultimately condensed the four factors to two main categories of tax jurisdiction analysis that characterize international tax discourse today, namely, source and residence. The two other elements—*situs* and enforceability—were subsumed in this exercise as generally less relevant or dispositive, or susceptible to facile manipulation (for example, storing a stock certificate in a lock box would eviscerate any formalistic *situs* rule).[42]

Over the years, however, it has been difficult to reconcile the normative promises of nexus by residence and source with the theories and practices adopted by states. In the case of residence, states have made awkward compromises that have not been and probably cannot be explained by any theory of justice. This is mainly because in practice residence has been defined in formalistic terms to serve goals of expediency rather than theoretical coherence, and because states simply abandon any pretense at determining nexus whenever they cannot agree amongst themselves on common principles.[43]

The breakdown of the normative foundations for residence-based nexus begins when states rely on social and political factors as proxies for economic nexus. The abandonment of principle to absolutism is complete when they rely on state-assigned and often virtually immutable personal characteristics (such as nationality assigned at birth) to assert nexus. While the United States is unique in routinely basing its jurisdiction to tax on such factors, tax treaty tie-breaker rules that assign nexus on a cascading set of factors demonstrate that the willingness to abandon nexus and return to the comfort of absolute sovereignty is universal.[44]

This is because, when none of the factors that would involve choices and actions taken voluntarily and purposefully by individuals settle in favour of assigning a jurisdictional claim to one state instead of the other, states uniformly resort to

membership should be viewed as alternative accounts of the same underlying principle is accordingly explored *infra* Part II.C.

[41] *Id.* at 22-26.

[42] *Id.*

[43] This is especially the case with respect to entities. See, e.g., Michael J. McIntyre, *Determining the Residence of Members of a Corporate Group*, 51 CAN. TAX J. 1567, 1571 (2003) ("as currently constituted, [corporate residency tests] are elective to a substantial degree"); Daniel Shaviro, *The Rising Tax- Electivity of U.S. Corporate Residence*, 64 TAX L. REV. 377, 381-85 (2011) (same); Omri Marian, *Jurisdiction to Tax Corporations*, 54 B.C. L. REV. 1613, 1614 (2013) (same, and arguing that there is no normative basis for the jurisdiction to tax the corporation based on residence so a functionalist approach is warranted instead). To further complicate matters, states take varying approaches to assigning residence for entities, with some identifying as resident any company organized within its territory and others identifying residence as the location of the company's "mind and management," which could mean where managers are located or where management decisions take place.

[44] *See, e.g.*, OECD Model and Commentary.

nationality, which is typically assigned by the state, and finally to diplomatic agreement between themselves.[45] While some personal factors, such as time spent in a place and location of family and home, might be acceptable as evidence that a person has voluntarily engaged with a state, created nexus and thereby consented to the jurisdiction to tax, the same cannot be said of either legal status (especially if summarily conferred upon a person as a birthright) or diplomacy.[46] Both deny any role for voluntary action by the individual, so establishing jurisdiction on these grounds should be read not as based in nexus at all, but instead as a return to Hobbesian sovereign authority.[47]

Using a person's economic activity in the state has provided a similarly thin normative justification for the imposition of taxation. First, this link to the state, referred to as territorial or geographic source, is also a concept constructed by the state with few normatively justified parameters.[48] Second, in virtually every case of an asserted source-based jurisdiction, an opposite and equally powerful claim can be made on the basis of residence.[49] Again, pragmatic compromise is the primary explanation for the actual practice of states in exercising source as a jurisdictional basis for imposing taxation, or ceding such right to the country of residence.[50] When it falls to the state to

[45] Tie-breaker rules for companies are even more formalistic, assigning residence to the state of formation or incorporation, resorting to diplomacy, and, if diplomacy fail, accepting the overlapping and simultaneously claims of two or more states without any redress for the beleaguered taxpayer.

[46] Likewise, if states themselves decide reject all the tie-breaking options that they agreed to in their treaties, there appears to be no normative reason to fall back on an assumption that each therefore has a rightful claims over the taxpayer. In the case of individuals, the eventual resort to citizenship following the failure of other jurisdictional alternatives presents an additional problem for thinking about the jurisdiction to tax, as discussed more fully infra at Part III.A.

[47] See, e.g., A. JOHN SIMMONS, JUSTIFICATION AND LEGITIMACY: ESSAYS ON RIGHTS AND OBLIGATIONS 65 (2001) ("We are for the most part born into political societies and rise into our places as citizens of them without ever freely choosing to participate or to become members.").

[48] *See, e.g.*, Lawrence Lokken, *What is This Thing Called Source*, 37 INT'L TAX J. 25 (2011); Hugh Ault and Brian Arnold, COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS, 5th Ed. 495-499 (2010) ("countries...assert the right to tax income that, broadly speaking, can be said to 'arise' in the country.... This approach is based in part on practical and administrative considerations. ... [T]he details tend to be relatively undeveloped.").

[49] Indeed, many source concepts explicitly rely on residence as the determining factor. *See, e.g.*, Graetz *supra* note 21 at 317 ("many of the basic source rules themselves turn on the legal nature of a transaction rather than its economic substance. Examples include distinctions between sales and licenses and between rents on a financial lease and interest. In addition, a number of source rules turn simply on the residence of the payor, and ... corporate residence today is itself a problematic category.")

[50] States simply draft doctrinal rules that designate streams of income as either domestic or foreign (or mixed) in nature according to internal decisions about what the state can access as an administrative matter, and then work out pragmatic compromises with other states on an ad hoc, selective, and probably biased basis. *See, e.g.*, Charles I. Kingson, *Taxing the Future*, 51 TAX L. REV. 641, 648 (1996) ("increasingly, when we can't analyze what something is, we replace analysis by a rule and a name"); Shay, Fleming & Peroni *supra* at 154 (given the problems of geographic sourcing attempts, "the content of any particular source rule should relate to the rule's purpose and not to debates over geographical origin"). Even with respect to services, long considered relatively straightforward as a matter of determining geographic source by reference either to the location of the service provider or the location of the services rendered, the principles are far from clear. *See, e.g.*, Michael Kirsch, *The Role of Physical Presence in the Taxation of Cross-Border Personal Services*, 51 BOS. COLL. L. REV. 993 (2010) (discussing the challenges to conventional thinking about source rules posed by such innovative practices

explain why it uses its source jurisdiction to chase some resources and not others, there is simply no normative justification to offer in response.

Even so, source plays a key role in shaping our understanding of the jurisdiction of the tax state. Once source-based jurisdiction is accepted as an appropriate base for taxation, it becomes clear that anyone, anywhere, who can be claimed to have interacted economically with or within the state, even indirectly (even by something as remote as using its currency in an international transaction) could theoretically be gathered up in the taxpayer category.[51] This allows a state to claim any person that passes virtually any threshold it puts forth, no matter how arbitrary.[52]

The residence principle thus establishes little more than that a state could tax anyone it cares to identify as subject to its law, while the source principle establishes the same entitlement with respect to anyone or anything that could be said to have generated income within the territory. Despite being theoretically attractive on the surface, nexus on the basis of both residence and source ultimately relies on the logic of absolute sovereign authority. As a result, we may be forced to dismiss the principle as a plausible normative explanation for the jurisdiction to tax.

Even so, the idea of using residence and source to connect a person to a jurisdiction continues to drive virtually all contemporary tax policy discourse. One reason may be that the scholar's search for meaning and rationale is inexhaustible even if experience continuously demonstrates that no satisfactory theory will likely be found. The other, potentially more optimistic reason may be that, in committing to the idea that jurisdiction fundamentally requires purposeful and voluntary engagement by the taxpayer with the state, nexus is, despite its many flaws, the best normative framework

as remote surgery, which allows a doctor in one country to perform procedures on a patient located in another country via computer.)

[51] Some theorize that source can be understood as an expression of benefits theory but the argument has been rejected as a normative principle. *See, e.g.*, Steven A. Dean, *More Cooperation, Less Uniformity: Tax Deharmonization and the Future of the International Tax Regime*, 84 TUL. L. REV. 125, 144 (2009) (source-based taxation draws "on the Lockean notion that governments earn the right to collect tax revenues by providing the services that make the creation of the underlying income possible"); 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, 307 (2001) (source-based taxation "is often rationalized as a benefits-based charge imposed by the source country"); Edward A. Zelinsky, *Citizenship and Worldwide Taxation: Citizenship as an Administrable Proxy for Domicile*, 96 IOWA L. REV. 1289, 1293-1294 (2011) (reviewing these and similar claims that "source-based taxation reflects the claim of the nation in which income arises or assets are held that such nation provides the benefits" but ultimately rejecting the thesis."). The normative analysis would change if source-as-benefit was instead seen as a threshold only (and not a means for measuring an amount owed commensurate with that received). This idea is discussed in the context of the membership principle in the next section.

[52] In a world that is characterized by global economic integration, it could be quite difficult for a person to absolutely ensure that she is never caught in any particular state's asserted source jurisdiction—the simple act of buying something could in theory subject a person to that definition. But the absurdity is further demonstrated on the other extreme when income can disappear altogether, such as under rules for categorizing entities that seem to have nothing to do with source. For example, since a foreign entity that is deemed not to exist for US tax purposes cannot be allocated an income stream, the US may completely ignore transfers to or from such an entity even if such transfers occur as a legal matter, and even if they in fact affect the income ultimately earned by U.S. entities further up in an ownership chain.

currently available.[53] Methodically studying the flaws for the purpose of searching for meaningful ways to adjust the framework seems more acceptable than simply ceding that the state is an absolute authority after all. Like the concept of sovereignty, the concept of nexus will, of necessity, remain a guiding framework until a more acceptable alternative can be developed. A third idea, generally found not in the tax literature but in political philosophy, may provide some different tools for developing this more normatively satisfying approach.

C. MEMBERSHIP

A third normative explanation for the jurisdiction to tax is the membership principle. In simplified terms, this principle attempts to explain a link between person and polity by reference, at least in some accounts, to voluntary choice on the part of the individual.[54] The membership principle is a component of the concept of political obligation, which attempts to explain why one can be expected to obey laws laid down by a sovereign.[55] The membership principle is invoked rarely in tax scholarship, but was offered as a key normative framework in recent work by economic philosopher Peter Dietsch.[56]

Dietsch defines the membership principle as one's intrinsic obligation to obey the tax laws in every state of which one is a member, with membership arising when one benefits from the public services or state-provided infrastructure.[57] Dietsch offers this principle explicitly as a normative explanation for the jurisdiction to tax, linking it conceptually to the universally accepted residence and source principles.[58] So linked, this risks disqualifying the membership principle as a satisfactory explanation of the tax jurisdiction for the reasons noted above, but further examination reveals its potential to fill normative gaps left by both the sovereign entitlement and nexus theories. This is because, while sovereignty and nexus implicitly depend on either the inherent authority

[53] This is so even though the economists' idea that the jurisdiction to tax could be accurately allocated on the basis of scientific and technical factors turns out to have been implausible from the start. *See, e.g.*, Philipp Genschel, *Globalization and the Transformation of the Tax State*, 13 EUR. REV. 53, 60 (2005) (The traditional idea that "all taxable events have a clearly identifiable place in space" within one jurisdiction or another "has always been a fiction.")

[54] *Contra, see, e.g.*, RONALD DWORKIN, LAW'S EMPIRE 206 (1986); JOHN HORTON, POLITICAL OBLIGATION 146, 150 (1992).

[55] Political obligation is itself the subject of multiple and conflicting accounts, but generally connotes a communal responsibility that is either assigned by local social practices "to membership in some biological or social group," such as a family or neighborhood (in the anti-voluntarist view) or that arise from the individual's voluntary choice to subject herself "to the political authority of others or to participate in the ongoing cooperative schemes of political life" (the voluntarist view, as in social contract theory). A. JOHN SIMMONS, JUSTIFICATION AND LEGITIMACY: ESSAYS ON RIGHTS AND OBLIGATIONS 65-73 (2001). *See also* MAGDA EGOUMENIDES, PHILOSOPHICAL ANARCHISM AND POLITICAL OBLIGATION (2014); Michael Hardimon, *Role Obligations*, 91 J. PHIL. 333, 342-344, 353 (1994); CAROLE PATEMAN, THE PROBLEM OF POLITICAL OBLIGATIO: A CRITICAL ANALYSIS OF LIBERAL THEORY 27 (1985); Margaret MacDonald, *The Language of Political Theory*, in ANTONY FLEW, ED., LOGIC AND LANGUAGE 184 (1963); THOMAS MCPHERSON, POLITICAL OBLIGATION 64 (1967); Pitkin *supra* at 39.

[56] PETER DIETSCH, CATCHING CAPITAL: THE ETHICS OF TAX COMPETITION (2015).

[57] Dietsch at 80-83.

[58] Id.

of the state or implied consent or both, the use of benefit from specified items as a threshold in the membership principle (at least as Dietsch explains it) suggests the addition of two principles that have not been explored in tax policy discourse.

These two principles may be stated in simple terms as: (1) a state cannot justifiably tax unless it can point to certain tax-specific evidence of an individual's voluntary consent to the jurisdiction, and (2) a state cannot interpose (or allow itself to be used) to defeat the claims of another state with respect to those likewise observed to have voluntarily consented to that other state's jurisdiction. These are not claims about what states can accomplish as a practical matter. Rather, they are claims about what states have a right to expect from each other in the international tax order, and what individuals have a right to expect from all states in which they are members.

Tying the jurisdictional claim to benefit specifically from public services and infrastructure is a central plank in this account of the membership principle. The reason to make this link appears again to be grounded in respect for fundamental individual rights. In Humean terms, the circumstances of justice seem to exist: if an individual is observed using a publicly-funded road, school or hospital, it seems fair to conclude that in the abstract she must have had a need to form a social contract because her resources were too scarce to privately supply herself with these goods, and that she voluntarily bargained with others in the same circumstances to mutual benefit. The membership principle would therefore conclude that using publicly funded services and infrastructure is tacit evidence of an individual's unforced expression of belonging, and therefore acceptance of obligation to others.[59]

A few areas of ambiguity require resolution in order to assess the potential normative strength of the membership principle as applied to the jurisdiction to tax. The first involves whether the public services and infrastructure that benefited the putative taxpayer must have been funded by taxation and not taking.[60] If this is necessary, there may be overwhelming difficulties in implementation because much infrastructure, and many national borders, will be traceable to past instances of forced taking and exploitation that were unjust then and are no more just now.[61] It seems necessary to explain how the legacies of war, exclusion, and slavery that touch so many states would not invalidate virtually any normative claim regarding political obligation.

[59] See, e.g., Margaret Gilbert, *A Theory of Political Obligation: Membership, Commitment, and the Bonds of Society* 138-139 (2006) (explaining her idea of membership and obligation as the formation of joint commitments are formed, which "involves a kind of expressive behaviour on the part of the would-be parties. In each case, each one's expressive behaviour is an expression of readiness for joint commitment: each understands what a joint commitment is, and expresses all that is needed on his or her part to bring such a commitment into being, namely, readiness to be jointly committed." For Gibson, the relevant expressive behaviour must also be common knowledge among the parties, meaning that "if some fact is common knowledge between A and B (or among members of population P, described by reference to some common attribute), that fact is entirely out in the open between (or among) them, and, at some level, all are aware that this is so.").

[60] As discussed above at Part II.A.

[61] The legacies of war and slavery that touch virtually every state would thus seem to invalidate virtually any normative claim regarding political obligation.

A second is that the definition of public services and infrastructure is open to interpretation.[62] Presumably they would include actual use of tangible things such as roads, schools, hospitals, sanitation and so on. But what about intangible goods, such as the rule of law, or a reliable global reserve currency? If the rule of law that protects contract and intellectual property rights, backed by institutions of review and redress are not public services, what excludes them? If these things are not excluded, then it is difficult to exclude laws promoting legal or financial service industries specifically to assist taxpayers in avoiding taxation by other states. Yet if these are included in public services and infrastructure, the membership principle could be, like nexus, no barrier to the claim of multiple sovereign states on virtually any ground. The usefulness of the principle would seem to disappear in this case.

Finally, the scope of requisite benefit is undefined. Membership is explicitly used only to establish, as a threshold, a necessary prior link to the legitimate claim of jurisdiction; after establishing that a person has enjoyed a benefit, the membership principle makes no further claim about how the jurisdiction to tax may be implemented in order to be just.[63] Dietsch's account omits any discussion of given amount or value of benefit to be received before membership is triggered, such that presumably any conceivable use might be considered a benefit.[64] Benefit might be defined very broadly as to mean virtually any contact with an item that even tangentially involves a state, such as using its currency as investment or medium of exchange, or buying goods that were developed from scientific research it funded. If so, the membership principle would do nothing to prevent a single, economically important state from claiming the world.[65] This would make membership a no more normatively acceptable concept than sovereignty. The parallels to nexus seem plain, raising again the risk of returning to sovereign absolutism in the implementation.

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[62] At least, Dietsch does not explicitly limit them.

[63] Dietsch at 80; see also Simmons at 73. The membership principle is therefore not simply another name for the benefit theory of taxation, which has been universally rejected as a normative claim. Benefits theory posits that people should contribute to government according to the benefits they receive from it. This is a compelling idea, grounded in the notion that societies form for the purpose of engaging in shared projects, and a government's main role, perhaps especially in a democratic state, should be that of aggregator of preferences. Scholars often attribute some version of benefit theory to John Locke, who claimed that "it is fit everyone who enjoys his share of the protection [of life, liberty, and property] should pay out of his estate his proportion for the maintenance of it." JOHN LOCKE, CONCERNING CIVIL GOVERNMENT, SECOND ESSAY (1690), Ch. IX, sec. 140. However, scholars universally reject benefits theory as justifiable tax policy given its many shortcomings, including the impossibility of accurately measuring the value of non-cash transfers to individuals (especially when they are intangible or difficult to disaggregate, such as clean air or a corruption-free legislature); and the difficulty of collecting payment or excluding benefits from those without the means to pay (namely, the poor, the young, and the old). In the context of the membership principle, benefit is instead a broad threshold concept which, when triggered by the actions of the taxpayer, gives the state legitimate jurisdictional claims.

[64] Dietsch *supra* ch. 1.

[65] It would not suffice to counter that the level of taxation ultimately imposed would have to accord with the level of benefit that triggered the membership, since that would imply a normatively unsupported defense of benefits-based taxation.

If these ambiguities can be resolved, membership might prove a stronger normative claim than nexus, however.[66] That is because, unlike sovereignty and nexus, the need for an expression of the individual's consent to the jurisdiction could impose an objective and observable element of constraint on a claim of jurisdiction. Requiring a benefit from public services or infrastructure as a prerequisite to membership could prevent some forms of manipulation that plague the nexus theory and force states out of an otherwise rightful claim to tax, or, conversely, entice them to resort to non-normative grounds (especially diplomacy) to produce a preferred outcome. For example, if certain types of favourable regulatory regimes provided by states are not considered public services or infrastructure, the taxpayer that uses such a regime to strategically place herself (or itself) outside of the jurisdiction of another state (in membership terms, denying or disguising its obvious consent to be a member of that state) may fail to accomplish that task. Taxpayers taking advantage of certain forms of competitive tax regimes might be denied the association to jurisdictions providing these services in a way that accords with basic principles of justice, thus enjoining a refusal of obligation to another state.[67]

Accordingly, while in present discourse the application of the membership principle to the tax jurisdiction leaves many key questions unanswered, it is worthwhile testing the theory to see if it sufficiently distinguishes itself from nexus and sovereignty as a normative matter. To do so, the next section posits two contemporary international tax controversies that have raised normative challenges with respect to the jurisdiction to tax which to date have not been satisfactorily solved, and applies each of the foregoing jurisdictional rationales in a search for a coherent analytical framework.

III. Testing the Normative Framework

To test the normative framework of the membership principle in contrast to the existing conventional explanations of sovereignty and nexus, this section applies each of the three rationales to two contemporary international tax controversies that implicate the jurisdiction to tax. The first is the jurisdictional claim of the United States over its nonresident citizens (citizenship-based taxation), which, boosted by recent regulatory efforts, has created a major source of policy discord. The second is the assertion that some states' tax regimes and practices interfere with or deprive a jurisdiction sought by

[66] However, a few additional caveats would seem to be in order in analyzing the efficacy of the membership principle. According to Dietsch, the principle applies to both natural persons and legal entities. At first glance, equal treatment of the individual and the entity is justified where each is explicitly recognized as a right holder under domestic legal documents (as is the case in most jurisdictions, for example with respect to procedural rights of notice and appeal in tax matters). However, the individual and the entity are really distinct taxpayers: the former are indelibly bound by their physicality, while the opposite is true for legal entities. The implications for jurisdiction are significant in that physicality is also the feature most associated with the claim of authority over a given territory. Moreover, a legal entity itself experiences no benefit from public services or infrastructure. Instead, its owners, officers, employees, and customers are the ones who benefit from the existence of the entity and the public services and infrastructure (including legal structure) that allow them to interact with and through legal entities.

[67] This is explored more thoroughly in Part III.B., *infra*.

others, for example by facilitating aggressive tax-avoidance schemes or by compelling weaker states to abandon their right to tax. Each is examined in turn.

A. CITIZENSHIP-BASED TAXATION

Consistent with the nexus principles laid out above, virtually every national income tax system in the world is premised on the jurisdictional concepts of residence and source.[68] The exception to the rule has always been the United States, which, in addition to residence and source in line with international practice, has also claimed its intention to tax individuals on the basis of their citizenship alone, and to do so in the same manner as its residents.[69] For almost one hundred years, this claim was more or less unenforceable as to the nonresident population of U.S. citizens, and by all accounts it was in fact unenforced except as to individuals who voluntarily complied either on their own behalf or, in the case of U.S.-based companies, with respect to their employees.[70] The failure to enforce may be explained by the inherent lack of sufficient unilateral control over nonresidents who lack economic ties or activities in the territory,[71] but the United States nevertheless persistently staked a claim over this globally dispersed population, including in every tax treaty it signs.[72]

[68] *See, e.g.*, Ault & Arnold *supra*.

[69] I.R.C. § 7701 (a)(30)(A) (citizens); (b)(1)(A) (greencard holders). (b)(3) (residents); (b)(1)(B), 871, 872, 897 (non-residents on U.S.-source income). The practice dates back to the income tax adopted to finance the Civil War, as described in Ruth Mason, *Citizenship Taxation*, 89 S. CAL. L.R. 169, 187-96 (2016); *see also* Surrey *supra* at 815 ("From the very start of the modem income tax the United States has asserted jurisdiction to tax on the basis of two factors-citizenship and source of income."). The dictatorship of Eritrea is viewed as another outlier for its attempts to tax its nonresident citizens permanently at a flat rate of 2% of worldwide income, for which it has been denounced by the United States, Canada, and the United Nations. S.C. Res. 2023, ¶ 11, U.N. Doc. S/RES/2023 (Dec. 5, 2011) http://www.securitycouncilreport.org/atf/cf/% 7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/Somalia%20S%20RE S%202023.pdf ("Eritrea shall cease using extortion, threats of violence, fraud and other illicit means to collect taxes outside of Eritrea from its nationals or other individuals of Eritrean descent.").

[70] *See, e.g.*, Mason, *supra* note 69, at 219; J. Richard (Dick) Harvey, Jr., *Offshore Accounts: Insider's Summary of FATCA and Its Potential Future*, 57 VILL. L. REV. 471 (2012) (stating that prior to FATCA, U.S. persons "were on the honor system" in terms of reporting non-U.S. financial accounts, and that "it would appear many U.S. taxpayers with offshore accounts have not been very honest."). This is also the case for financial reporting obligations, which are not tax obligations but are administered by the IRS with similar (but not identical) scope as the tax jurisdiction. *See, e.g.*, Steven Toscher & Michel R. Stein, *FBAR Enforcement-Five Years Later*, 10 J. TAX PRAC. & PROC. 37, 37-38 (2008); Eschrat Rahimi-Laridjani, *FBAR-Where We Are and How We Got There*, 8 J. TAX'N FIN. PRODUCTS 29, 25-26 (2009).

[71] Some opportunities may arise for the United States to enforce its tax jurisdiction on certain nonresidents with non-U.S. source income. For example, the IRS appears to have broad powers to seize the bank deposits of certain nonresident U.S. Persons through the global banking system, even if such individuals never directly interact with the U.S. economy. The IRS may generally seize financial assets held by U.S. banks, subject to a 21-day notice period. I.R.C. §§ 6331, 6332, 7401; 26 C.F.R. §§ 301.6332-3, 301.7401-1. The commissioner may seize assets "without delay" if he fears the taxpayer plans to move assets to avoid seizure. I.R.C. § 6861; *see also* United States v. Stonehill, 702 F.2d 1288, 1292 (9th Cir. 1983). The IRS takes the position that a levy on one branch of a bank is effective against funds held in all branches of the bank if the bank's internal account system allows one branch to freeze accounts across all branches. *See, e.g.*, Bank Leumi Trust Co. v. Klein, No. 92-CV-2016, 1993 WL 403967, at *12 (S.D.N.Y. Oct. 7, 1993). This would suggest that a deposit in a foreign branch could be

This status quo quickly changed when, in 2010, the United States adopted legislation that would make it very costly for any financial institution, anywhere in the world, to host accounts for clients that might be identifiable as U.S. citizens.[73] This legislation, the Foreign Account Tax Compliance Act, or FATCA, reversed the virtual non-enforceability of citizenship-based taxation by applying economic sanctions to compel the assistance of foreign institutions, and ultimately foreign governments, in the task of identifying and controlling the worldwide population of U.S. citizens not living in the United States.[74] While possibly unintentional on the part of its drafters,[75] it now appears clear that FATCA's main impact has been to forcefully compel thousands and perhaps even millions of previously unaware citizens living permanently in other countries into compliance with the laws of a state to which they formerly recognized no obligation.[76]

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seized indirectly by imposing the levy on a U.S. branch of the same bank, provided the internal controls allow cross-branch freezing of accounts. However, this position is controversial and may not be supported in international law. For a discussion, see Steven R. Mather & Paul H. Weisman, TAX MANAGEMENT PORTFOLIO, FEDERAL TAX COLLECTION PROCEDURE: LIENS, LEVIES, SUITS AND THIRD PARTY LIABILITY, NO. 637-2D (Bloomberg BNA 2016), at IV(C)(3)(c)(1).

[72] *See, e.g.*, U.S. Model Double Tax Convention art. 1, Para 4. (stating that "this Convention shall not affect the taxation by a Contracting State of its residents ... and its citizens."); Convention between the United States of America and Canada with Respect to Taxes on Income and on Capital, U.S.-Can., arts. XXIV, XXVIA, Sept. 26, 1980, T.I.A.S. No. 11087 [hereinafter, Canada-U.S. Double Tax Convention] (same). While the U.S. retains the right to tax its citizens in accordance with domestic law, the Convention respects the primary right of the source state to tax and provides that the U.S. will relieve double taxation, including in the case of citizens.

[73] Hiring Incentives to Restore Employment Act (HIRE), Pub. L. No. 111–147, §§ 501–31, 124 Stat. 71 (2010) (codified in scattered sections of the Internal Revenue Code). For purposes of brevity, the term citizen herein is deemed to include greencard holder where relevant. While the definitional rules that subject citizens to the U.S. tax system apply equally to greencard holders, the FATCA regulations do not effectively capture these taxpayers, as explained in Allison Christians, *A Global Perspective on Citizenship-Based Taxation* (forthcoming) MJIL (2017). The permanent taxation of nonresident greencard holders like citizens and residents raises its own related if distinct normative questions. *See, e.g.*, Tessa Davis, *The Tax-Immigration Nexus*, working papepr (2015) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2657250.

[74] For a detailed explanation of the regime, its consequences for financial intermediaries, and how foreign governments became involved in enforcement within their own territories, see Christians, *supra* note 73; Mason *supra* note 69; DAVID KERZNER AND DAVID CHODIKOFF, INTERNATIONAL TAX EVASION IN THE GLOBAL INFORMATION AGE 84-85; 313-350 (2015).

[75] For instance, a lengthy article discussing the rationale for FATCA, authored by by a self-identified insider, begins with the proposition that "U.S. taxpayers have been hiding income overseas for years" without defining the term "U.S. taxpayer" (which is not a defined term) and without ever mentioning citizenship-based taxation. J. Richard (Dick) Harvey, Jr., *Offshore Accounts: Insider's Summary of FATCA and Its Potential Future*, 57 VILL. L. REV. 471, 473 (2012). The article suggests that the direct focus of FATCA was on the use by high net worth U.S.-resident individuals of anonymous or unidentified accounts in specified countries, especially Switzerland and Lichtenstein, with the express goal of hiding their identities from the tax authorities. Harvey at 476-79.

[76] *See, e.g.*, David Jolly & Brian Knowlton, Law to Find Tax Evaders Denounced, New York Times (26 December 2011) B1, online: http://nyti.ms/1I7SMjg (expected $8 billion over ten years to be raised by FATCA disproportional to the expected implementation costs for foreign institutions, and citing Professor H. David Rosenbloom, that "the FATCA story is really kind of insane" and that "Congress came in with a sledgehammer.").

This is occurring because U.S. taxation follows U.S. citizenship, and U.S. citizenship is a matter of birthright rather than choice.[77] Having been assigned citizenship at birth, an adult is trapped into costly regulatory compliance under threat of major financial penalties, including in order to leave.[78] Complicating matters, it was at one time possible for a person to relinquish her citizenship automatically upon naturalization in another country.[79] However, the U.S. Supreme Court rejected this position in 1980 and, unbeknownst to many, reinstated citizenship once thought lost.[80] Most of the beneficiaries of this decision were officially notified of neither the decision

[77] *See U.S. v. Wong Kim Ark*, 169 U.S. 649, 688, 703, 709 (1898). While birthplace within the territory is automatic, the rules for citizenship have changed over time for those born abroad of a U.S. parent. *See* Rogers v. Bellei, 401 U.S. 815 , 831(1971) (stating that in the case of individuals born abroad, Congress "may prescribe a period of residence in the United States as a condition *precedent*" to a grant of citizenship); Immigration and citizenship law in the United States flows from the constitutionally articulated power of the federal government to "establish a uniform Rule of Naturalization." U.S. CONST. art. I, § 8, cl. 4; *see also* 8 U.S.C. § 1251 (detailing federal rules and standards regarding deportable aliens). These rules have been periodically reformed and revised according to political and social circumstances. The Patriot Act of 2001 is the most recent comprehensive legislative reform. Pub. L. No. 107-56, 115 Stat. 272 (2001). Moreover, the law is subject to agency and judicial interpretation and application. The Department of Homeland Security, established in 2002, oversees all matters involving immigration and naturalization and is the parent agency of the United States Citizenship and Immigration Services (U.S.C.I.S.) the agency directly responsible for administering the Immigration and Nationality Act. U.S.C.I.S. issues memoranda, administrative decisions, and generalized guidance. In addition, President Obama recently sought to alter legislated outcomes by recourse to his plenary executive power but his efforts are currently subject to judicial review. *See, e.g.*, *Obama's Immigration Executive Actions on Hold Until Legal Challenge Resolved*, PBS NEWSHOUR (May 28, 2015, 6:30 PM), http://www.pbs.org/newshour/bb/obamas-immigration-executive-actions-hold-legal-challenge-resolved; U.S. CITIZENSHIP & IMMIGRATION SERVS., EXECUTIVE ACTIONS ON IMMIGRATION (2015), http://www.uscis.gov/immigrationaction.

[78] An adult of sound mind may expatriate from their citizenship if they pay a fee of $2,350 and are deemed by the United States to do so knowingly and wilfully upon presenting their case to the relevant authority. *See generally*, 8 U.S.C. §§ 1481(a)(5)–(6), 1488 (laying out procedures required to renounce and stating that relinquishing acts include becoming naturalized in a foreign state after age 18, making an oath of allegiance to a foreign state after age 18, serving in the armed forces of a foreign state under certain circumstances, or committing an act of treason); *Perkins v. Elg*, 307 U.S. 325, 334 (1939) ("Expatriation is the voluntary renunciation or abandonment of nationality and allegiance."); U.S. DEP'T OF STATE, FOREIGN AFFAIRS MANUAL, CT:CON-553, LOSS AND RESTORATION OF U.S. CITIZENSHIP (2014). However, expatriation has no impact for tax purposes until prior compliance with the tax laws is demonstrated. Even where compliance is demonstrated, additional costs may be imposed on high-net worth individuals, who face a significant exit tax upon expatriation. *See* I.R.C. §§ 877(a)(2)(c); 877A(g)(4); Form 8854, Initial and Annual Expatriation Statement; Matthew Morris, *FATCA and the Road to Expatriation*, 149 TAX NOTES 691 (Nov. 2, 2015) (explaining that under § 877(a)(2)(c), an individual will not consider to have expatriated until Form 8854 is filed, which requires certification under penalty of perjury of compliance with U.S. income tax and information return responsibilities for the preceding five tax years). *See also* Expatriation Act of 1907, 34 Stat. 1228, 1229 (1907). (Exceptions apply to the children of diplomatic officers and others in addition the rules for U.S. territories and possessions are myriad and complex.). *See* 8 U.S.C § 1401); *see also generally* 7 U.S. DEP'T OF STATE, FOREIGN AFFAIRS MANUAL § 1120 (2013), https://fam.state.gov/fam/07fam/07fam1120.html

[79] *See Savorgnan v. United States et al.*, 338 U.S. 491, 505-06 (1950) (holding that the plaintiff had lost her American citizenship by applying for and obtaining Italian citizenship followed by residence abroad).

[80] *Vance v. Terrazas*, 444 U.S. 252, 253 (1980) (holding that the government must prove intent to surrender United States citizenship and not just the voluntary commission of an expatriating act).

nor the tax consequences to them thereof.[81] One pernicious outcome of this rule is that individuals who lack the capacity to renounce are permanently trapped in their citizenship and therefore in their tax obligations.[82]

How should citizenship-based taxation be assessed from a normative perspective? Applying the three rationales above suggests that citizenship-based taxation violates both the nexus and the membership principles. Only sovereign absolutism (which as discussed above, is not a normatively acceptable basis for taxation) provides any justification for the jurisdictional claim over a citizen whose only tie to the government is a legal status that cannot be abandoned without that government's permission. Citizenship-based taxation further exposes the normative failing of sovereign entitlement by demonstrating that there is no principled response to such a jurisdictional claims by those drawn into compliance; the same is true for those drawn into enforcement against their own citizens and residents under pressure from FATCA. Each of these arguments is addressed in turn.

1. Nexus

While nexus is not a wholly satisfactory account of the jurisdiction to tax, as discussed above, it is the natural starting point in a normative analysis owing to its central role in tax policy discourse. In this case, even though flawed, the superior claims of residence and source demonstrate the weakness of the citizenship-based taxation claim by comparison.[83]

In taxing its residents, as generally defined by a physical presence test, on all income, from whatever source derived, and foreign persons on their U.S.-source

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[81] Today, the individual must generally display intent in order to lose citizenship status. *Afroyim v. Rusk*, 387 U.S. 253, 255, 259, 264 (1967); *Terrazas*, 444 U.S. at 253. However, see 8 U.S.C § 1481(b) for rebuttable presumptions. *See also* 7 U.S. DEP'T OF STATE, FOREIGN AFFAIRS MANUAL § 1200 app. B (2012).

[82] A person that seeks to relinquish citizenship must proclaim her specific intent to engage in the expatriating act; such an act therefore cannot be undertaken by another, such as a parent or guardian. See 8 U.S.C. § 1481(a) (individuals will lose their U.S. citizenship only by "voluntarily performing any of the following acts with the intention of relinquishing United States nationality"); DAVID WEISSBRODT AND LAURA DANIELSON, IMMIGRATION LAW AND PROCEDURE IN A NUTSHELL, Ch. 12-1 (2011) (outlining the evolution of U.S. rules limiting the ability to expatriate); SIGAL R BEN-PORATH; ROGERS M. SMITH, VARIETIES OF SOVEREIGNTY AND CITIZENSHIP, 107-108 (2013) (explaining the evolution of U.S. jurisprudence and legislation surrounding the requirement of intent for the relinquishment of citizenship). For a first-person account of this issue, see Amber Hildebrandt, *U.S. FATCA tax law catches unsuspecting Canadians in its crosshairs*, CBC NEWS, Jan. 13, 2014, http://www.cbc.ca/news/canada/u-s-fatca-tax-law-catches-unsuspecting-canadians-in-its-crosshairs-1.2493864 (describing the difficult choices facing the Canadian citizen parents of a 40-year old developmentally disabled son, born in the United States, who cannot renounce his citizenship; the financial accounts built up to provide for his ongoing care are subject to reporting and taxation in the United States despite being exempt from taxation in Canada and directly contributed to by the Canadian government as part of a registered disability savings plan).

[83] Mills, for example, argues that "individual autonomy is increasingly recognized as playing an important role in questions of jurisdiction," and that rather than nationality alone being sufficient to claim a person as subject to the state, "the practice of states instead supports the idea that a jurisdiction may be based on a flexible combination of both territorial and personal connecting factors." *See* Mills, *supra* at 207.

income, the United States follows the practice of virtually all countries that use income taxation as a source of revenue, and for good reason.[84] Individuals who are resident in a jurisdiction, and those that hold property situated in the United States, are accessible to tax law enforcement efforts by the taxing state. This is because the state virtually always controls either the person receiving the income or the person paying the income, or both—nexus theory is at least coherent in this respect.[85] As discussed above, the power to enforce is not ultimately a sufficient normative explanation, but the issue of control is important to the analysis of why the use of a regime like FATCA is pernicious even to the theory of nexus.

In the case of people who do not reside in the territory but who earn income from U.S. sources, the United States can similarly compel obedience to its tax laws by virtue of its control over either the payors of the income or the property generating the income.[86] With respect to the former, withholding ensures that the coercive power of the state is evenly applied to all the subjects of the tax. With respect to the latter, the power of the state to seize property ensures uniform application.[87] The enforceability of source-based taxation explains why it enjoys the same universal acceptance as residence-based taxation.[88]

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[84] For discussion and comparative analysis of national practices, see generally AULT & ARNOLD *supra* note18; Avi-Yonah *supra* note 18; Ernst & Young, 2016-17 WORLDWIDE PERSONAL TAX AND IMMIGRATION GUIDE (Sep. 2016), http://www.ey.com/Publication/vwLUAssets/Worldwide_Personal_Tax_and_Immigration_Guide_2016-17/$FILE/Worldwide%20Personal%20Tax%20and%20Immigration%20Guide%202016-17.pdf.

[85] This is not to suggest that enforcement is easy or straightforward; the volume of legislation and jurisprudence associated with the administration of the law demonstrate that it is neither. Rather the claim here is simply that the sovereign state's coercive power over a territory is understood to enable its ability to enforce tax laws on those present within the territory, regardless of how they come to be there. This accords with general principles of international jurisdiction. *See, e.g.*, Alfred M. Boll, MULTIPLE NATIONALITY AND INTERNATIONAL LAW 291 (2007) ("The vast majority of individuals' obligations to states do not correspond to, or follow, nationality, but accrue to all persons. This reflects the primacy of the territorial jurisdiction and power of the state.").

[86] Thus, for nonresidents' income from items such as stocks, bonds, licenses, and the like, the U.S. (like most countries), imposes obligations to report and withhold taxation at source. I.R.C. §1441. However, where the source of the income is fixed in place, for example in the case of real property, the United States generally allows nonresident taxpayers to self-report. This makes sense because nonpayment can be cured by asset seizure.

[87] For a classic explanation, see Edward S. Stimson, *Jurisdiction to Tax Income*, 22 CORNELL L. REV. 487, 488 (1937) (examining jurisprudence regarding the taxing rights of the several United States in respect of each other and concluding that "[t]he state having power over the property which is the source of the income or over the payor of the income can, by seizure of the property or corporeal suasion of the payor, withhold a portion of the income; and the state having power over the person receiving the income can force him to pay").

[88] Avi-Yonah, *supra* at 8-12; Mason, *supra* note 29, at 178-79; Allison Christians, *Drawing the Boundaries of Tax Justice*, *in* THE QUEST FOR TAX REFORM CONTINUES: THE ROYAL COMMISSION ON TAXATION FIFTY YEARS LATER 63-65 (Kim Brooks ed., 2013); Ault & Arnold, *supra* at 431-32. Countries typically reduce or eliminate source-based tax on certain passive income items in the case of a treaty. In such cases, the country of residence is typically expected to tax such items, and may be aided by the source country by the exchange of tax information. *See, e.g.*, OECD Model Income Tax Convention (2014), at http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf, arts. 10-13, 26 (providing maximum rates for withholding at source for specified passive income items and mechanisms for information exchange, respectively).

Where reporting and withholding is not mandated by law, and property is not easily seized, however, the power of the state to compel compliance dissolves. In such cases, the state loses its power to tax consistently. For this reason, the power of the state to compel compliance with respect to U.S. citizens is inherently inconsistent once nexus of residence or source is eliminated. Where these categories overlap with the conditions relevant to taxation on the basis of residence or source, the claim can be enforced with the same justification as that which supports the taxation of other nexus-based taxpayers. But this is eliminated where the conditions necessary to taxation in the other two categories are absent.

As a result, the United States can, consistent with its claim over all other nexus-based taxpayers, unilaterally assert its claim over citizens only if the citizen is also connected by nexus of residence or source.[89] The same cannot be said of non-U.S. source income earned by nonresident citizens. As to this income, unilateral enforcement of U.S. taxation is virtually impossible. Enlisting the aid of other countries at their own expense becomes the only viable option to achieve the will of the sovereign state.[90] It is for this reason that the vast majority of the world eschews the taxation of nonresidents on their foreign income, even if they are citizens or nationals.[91]

Citizenship-based taxation is thus not only different than residence and source based taxation, but it explicitly interferes with jurisdictions that base their taxing power on nexus.[92] Accordingly, the principles that support nexus-based taxation would rule out citizenship-based taxation as an acceptable alternative, in line with the four economists' initial rejection of political allegiance as an appropriate basis for tax.

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[89] The distinction between worldwide taxation (which refers to the practice of taxing all income from whatever source derived) and residence-based taxation (which refers to taxing a category of persons based on where they live) has caused some confusion in public discourse over the taxation of citizens. For example, the New York Times erroneously reported in early 2015 that China is embracing U.S.-style citizenship-based taxation, by enforcing "a little-known and widely ignored regulation: Citizens and companies must pay domestic taxes on their entire worldwide incomes, not just on what they earn in China." Keith Bradsher, *China Wants Taxes Paid by Citizens Living Afar*, N.Y. TIMES (Jan. 7, 2015), http://mobile.nytimes.com/2015/01/08/business/international/china-starts-enforcing-tax-law-for-citizens-working-abroad.html. This conflated worldwide taxation of residents, which many countries exercise, with worldwide taxation of non-residents based solely on their legal status as citizens, which virtually no country, including China, exercises.

[90] *See generally*, Susan C. Morse, *Ask for Help, Uncle Sam: The Future of Global Tax Reporting*, 57 VILL. L. REV. 529 (2012).

[91] Some countries, including Finland, Hungary, Spain, and Turkey, have "clinging" residency rules that in general terms treat non-resident citizens or nationals as tax resident for a specified time period, sometimes with exceptions for treaty countries or a showing of real ties to another jurisdiction. *See* OECD, RULES GOVERNING TAX RESIDENCE (last updated Sept. 23, 2016), http://www.oecd.org/tax/automatic-exchange/crs-implementation-and-assistance/tax-residency/.

[92] *See, e.g.*, Boll, *supra* note 85 at 290-93 (2007) (outlining the "presumption that jurisdiction is first and foremost territorial" and explaining that, given the fact that multiple nationality is increasingly common around the world, if nationality were the primary basis for the exercise of jurisdiction over persons, significant and irresolvable international law problems would result; instead, nationality relies on a connection with territoriality as the basis for jurisdiction.)

2. Membership

Failing to satisfy the nexus principle, citizenship-based taxation must evidently also violate the membership principle, with its even more stringent requirement of evidence of actual consent to the jurisdiction by using public services and infrastructure. While some U.S. courts and some U.S. scholars have argued that the status of U.S. citizen is intrinsically beneficial, that position has been thoroughly debunked in more recent scholarship.[93] The burdens citizenship-based taxation places on those unable to abandon their citizenship reinforces this observation. Moreover, citizenship-based taxation explicitly interferes with the political choices of other states as to individuals who would clearly be identified as their own members owing to their use of public services and infrastructure. An example from another chapter in U.S. tax law vividly demonstrates the compelling nature of the membership principle, made even more vivid by the fact that in this case, the targeted taxpayers were not citizens but people who seemed to have voluntarily sought membership in the U.S tax jurisdiction.

In the mid 1980s, the state of California faced a concerted global backlash against a tax practice viewed as impermissibly extraterritorial in scope[94] as well as inconsistent with international tax norms.[95] The rule at issue was California's "worldwide unitary method," which required certain businesses in California to measure their corporate income for tax purposes according to a formula that required tax-relevant information to be collected from global affiliates and disclosed to California's tax authority.[96]

Like citizenship-based taxation, California's regime required taxpayers to annually submit disclosures of their income and assets on a global basis.[97] Unlike citizenship-based taxation, the state regime then applied a formula to tax only the

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[93] In favor of a benefit theory of citizenship status, see Cook v. Tait, 265 US 47 (1924); Kirsch; Zelinsky. Contra, see Mason, *supra*; Christians, *supra* note 25; Reuven S. Avi-Yonah, *The Case Against Taxing Citizens*, 58 TAX NOTES INT'L 389 (2010).

[94] Statement of Allen Wallis, reprinted in FINAL REPORT OF THE WORLDWIDE UNITARY TAXATION WORKING GROUP 1063, August 31, 1984, reprinted in 24 Tax Notes 1043 (Sept. 10, 1984) [hereinafter, Unitary Tax Group Report] (stating that "the unitary tax method leads inevitably to extraterritorial and double taxation" and "allows a state to reach beyond its borders and tax higher profits earned elsewhere."). Wallis further expounded his view that "the unitary tax method is contrary to international practice" by making the case that arms' length transfer pricing should be viewed as an international standard owing to widespread practice and "years of effort" by all the OECD member nations." *Id.*

[95] The U.S. Treasury convened a task force to "examine the taxation problem in its broadest aspects, as regards multinational corporations, whether foreign or domestic . . . and the implications . . . on our international relationships . . . as well as on states' revenues and states' rights". Unitary Tax Group Report 1043, 1047.

[96] The regime is a key component of combined reporting and formulary apportionment, which is a method of allocating income across the members of a group of controlled or affiliated companies. Combined reporting and formulary apportionment, while in common usage across the several states, is an alternative to the arm's length method, which is favored for federal corporate income tax purposes by the United States as well most of its major trading partners. For an overview of the regime and a contemporary argument in favor of continuing jurisdictional limits on tax information reporting, see Todd Roberts and Joel Walters, *In Defense of Water's-Edge Reporting*, TAX NOTES INT'L. 885 (Sept. 5, 2016).

[97] *See* California Franchise Tax Board, California's Corporation Taxes- Frequently Asked Questions 2, https://www.ftb.ca.gov/forms/misc/1083.pdf (Explaining that California's unitary method formula "takes into account ... worldwide property, payroll, and sales factors.").

California-source portion of such income.[98] Yet nations around the world aligned together in vehement opposition to California's regime as it applied to their own resident companies, ultimately convincing California to restrict its jurisdiction.

The arguments for and against California's regime as applied to nonresident taxpayers parallel many of those raised in defense of and against citizenship-based taxation. For example, California advanced the argument that, as a matter of sovereignty, it should be entitled to design its own tax policy free from interference by other jurisdictions.[99] Proponents of the system expressed their belief that an alternative tax design would lead to tax avoidance (the alternative being the arms' length standard employed by the United States and most of its trading partners).[100] Finally, they defended the heightened compliance burdens faced disproportionately by non-US based taxpayers on grounds that it is more difficult to get accurate information from these taxpayers, owing to their remoteness, i.e., lack of nexus, to the jurisdiction.[101] All of these arguments ultimately proved insufficient to support California's regime in the face of widespread opposition from the international community, yet very similar arguments are advanced in support of citizenship-based taxation today.[102]

Conversely, constituents who sought reform of California's regime expressed concerns regarding the likelihood of over- and under-taxation, the vast complexity and even "bewildering" nature of the rules as they applied to non-U.S. based taxpayers, the likelihood for interference with international trade and investment flows, and the disproportionate compliance costs for, and other impacts on, non-U.S. based taxpayers as compared to those based in the United States.[103] All of these arguments apply equally to the application of citizenship-based taxation to nonresidents. Indeed, the arguments are strongest in the case of those who, for reasons beyond their control, are included in a tax system they consider foreign, in contrast to the multinationals whose exposure to the California tax system came about because they voluntarily sought to access the market.

The positions taken in respect of California's tax system are particularly instructive in thinking about what norms ought to be seen as proper limits on the state's jurisdiction to tax.[104] The parallels with citizenship-based taxation affirm some of the grounds for other states to resist citizenship-based taxation in the same way they resisted California's regime. Important differences between the affected constituencies

[98] *Id.* (explaining that the business income of a unitary business is "divided and assigned to California by means of an apportionment formula").
[99] Unitary Tax Group Report at 1046 ("the states believe that they should be free from federal interference in establishing their fiscal systems.").
[100] Unitary Tax Group Report at 1046.
[101] *Id.*
[102] *See e.g.*, Mason, *supra* note 6669(reviewing the arguments in favor of citizenship-based tax).
[103] Unitary Tax Group Report at 1046-48 (describing foreign-based multinationals objections to the compliance burdens of California's system, including especially the "need to translate their entire foreign operations into U.S. currency and to conform them to U.S. accounting rules."). This burden in particular is replicated for nonresident citizens as to their entire financial lives, a hardship that is compounded by their fewer resources and access to competent professionals at affordable cost compared to multinationals that expressly sought to do business in California.
[104] As discussed below, rather than press the issue in litigation, California undertook to voluntarily resolve the issues through legislative reform.

may explain some of the reasons why such resistance has not yet materialized, may be unlikely to materialize, and yet is fully warranted on the basis of the membership principle.

In the case of California's worldwide unitary tax, multiple heads of state from key trading partners voiced uniformly strong objections to the unitary tax regime, pointing out the perceived interference with their own jurisdictions and threatening retaliation in the form of sanctions.[105] Similarly, global business interests railed in unison against California's system, calling for federal intervention to "provide adequately for the international pressures" should the state fail to remedy the situation.[106] A working group was formed to study the broad domestic and international impacts of California's regime on U.S. international relations as well as states' revenues and rights.[107] The working group convened multiple meetings and included multiple stakeholders, who deliberated at length over the competing interests at stake.[108]

There has been no similar international outcry by foreign officials, no concerted determination to retaliate on behalf of their own resident taxpayers, in the case of U.S. citizenship-based taxation. No working group has been convened to study the issues attending to how FATCA enforces citizenship-based taxation of nonresidents, and no international public meetings have been held among officials and those impacted by the laws to discuss and deliberate the international implications, revenues, and competing rights involved.

The reason for the disparate reaction of the international community in these two cases appears obviously related to the resources of the respective affected constituencies. Major multinational firms were the aggrieved parties in the case of the California worldwide unitary system. They understandably acted in their own interests, and they sought the assistance of governments to further their cause.[109] In contrast, citizenship-based taxation impacts individuals of varying means, with less ability to marshal the forces of their governments to rally on their behalf in the face of overwhelming pressure to comply.[110] Their own marginalization from the United States, their very lack of membership, effectively prevents them from being heard on an issue that affects them.

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[105] See Unitary Tax Group Report at 1063 (noting "sharp criticism from all of our major trading partners," with the Secretary of State stating that "few issues have provoked so broad and intense a reaction from foreign nations. The United States Government has received diplomatic notes from 14 member countries of the [OECD] ... as well as communications from the OECD itself, all protesting against the application of the unitary tax method to their companies.").

[106] STATEMENT BY THE BUSINESS REPRESENTATIVES ON THE WORLDWIDE UNITARY TAXATION WORKING GROUP, May 1, 1984, reprinted in 24 Tax Notes 1043, 1065 (Sept. 10, 1984).

[107] Unitary Tax Group Report at 1047.

[108] Unitary Tax Group Report at 1047, 1051.

[109] For example, those seeking reform of California's system called for "special emphasis" regarding the economic effects attendant to furthering a system that is universally reviled by foreign investors. *See, e.g.*, Unitary Tax Group Report at 1063.

[110] Foreign governments face pressure not only from the United States, but also from their own financial institutions, which sought to alleviate legal uncertainties and economic pressures on themselves by working to ensure uniform application of the U.S. regime under the supervision and sanction of their governments. For a discussion, see Christians, *supra* at 32-35.

Ultimately, under pressure from within the state, by other states, by business groups, and by the federal government,[111] California amended its laws in response to complaints from the international community that its claimed jurisdiction was extraterritorial in scope, incompatible with global legal standards, and normatively unacceptable.[112] Accordingly, potential legal violations were not ultimately addressed by any courts. Similar issues arising today in the case of global enforcement of citizenship-based taxation on non-U.S. residents are, in contrast, largely being neglected by the international community and left to the courts to adjudicate. While no one has advanced a philosophical argument that the resistance of the international community to California's expansive regulatory regime was normatively just, this episode in U.S. international tax relations provides some evidence that the membership principle is at least latent in the intuitions of tax policymakers about just limits on the jurisdiction to tax.

3. Sovereign Entitlement

Finally, having failed to satisfy both nexus and membership principles, only the absolute authority of the sovereign could provide any explanation for a jurisdictional claim on the basis of citizenship alone. Consistent with the uncritical deference to sovereign status that characterizes much scholarly work in this area, the right to tax on the basis of citizenship is often described as arising from the international recognition of the state's prescriptive or legislative jurisdiction based on nationality, which is said to reflect "ideas of individual subjectivity to sovereign power."[113] According to this view, state regulatory power derives from the relationship between the individual as a subject and a sovereign, and therefore travels with the individual wherever she may go.[114] This view, sometimes called the "active personality principle," seeks to explain why a state may regulate the conduct of its nationals regardless of their territorial location, for example as in the case of the U.S. Foreign Corrupt Practices Act.[115] However, international law scholars note that the power to regulate nationals extra-territorially is typically reserved for serious crimes.[116]

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[111] Much of the concern within the United States focused on whether California's regime interfered with US foreign commerce and foreign policy interests. Unitary Tax Group Report at 1047 (quoting Treasury Secretary Regan that "the effects of the use of the worldwide unitary method may interfere with the foreign commerce of the United States, so this becomes a matter of vital federal interest.").

[112] California's officials and members of the business community preferred a negotiated outcome obtained by consensus to a hierarchically imposed solution. Unitary Tax Group Report at 1047 (stating that "[t]he decision on federal legislation reflected a shared view by both the state and business members of the Working Group that a cooperative voluntary approach based on consensus offered the best choice of obtaining a solution to the difficult problems before the Group."); Statement of James R. Thompson, reprinted in Unitary Tax Group Report at 1066 ("This is a responsible effort to make sure that state tax policies will be conducive to harmonious international economic relations.").

[113] Mills, *supra* at 196.

[114] *See, e.g.*, *id.* at 198.

[115] *See, e.g.*, Adefolake Adeyeye, *Foreign Bribery Gaps and Sealants: International Standards and Domestic Implementation*, 15 BUS. L. INT'L. 169, 178 (2014).

[116] *See, e.g.*, Mills, *supra* at 198. While Mills acknowledges citizenship-based taxation as an exception to this rule, he offers no theoretical, normative, or legal justification therefor. *Id.* at 198.

Beyond the regulation of serious crimes, nationality-based obligations are in conflict not only with more contemporary views that volition of the individual is necessary to create a link to a state, but also with other explicitly undertaken duties of states, such as to guard against discrimination on the basis of nationality.[117] Sovereign entitlement is especially difficult to reconcile with a state's asserted "right" to tax beyond the internationally agreed standard. That rights imply correlative duties is indisputable, but the question is which duties are implied by which rights.[118] In the context of citizenship-based taxation, the United States is making a claim that it has a right to legislate within its competence free from interference from other states. This in turn implicitly claims that other states, in acknowledging that right (by treaty or otherwise), agree not to interfere with attempts by the United States to enforce its own jurisdiction.

However that agreement in no way explains why or to what extent other states are obliged to actively assist the United States in enforcing its will where it is unable to do so alone, such as within the territory of another.[119] Even if citizenship-based taxation is viewed to be within the scope of U.S. sovereign authority, the claim does not by itself outline the duties of other states to yield, thus "subject[ing] their nationals willingly to other states' jurisdiction."[120] This question of a state's duty to respond to the asserted tax rights of another does not fit neatly within the existing scholarship on the limits of the

[117] *See, e.g.*, Mills, *supra* at 206 (citing the law of the European Union and the European Convention on Human Rights as well as investment treaties as possible sources of conflict).

[118] *See, e.g.*, Anthony A. D'Amato, THE CONCEPT OF CUSTOM IN INTERNATIONAL LAW 69 (1971). at 69 (stating that "a claim of 'right' can only make sense if the claimant is asserting implicitly that others have a 'duty' to allow or accede to this claim.").

[119] The opposite conclusion is the foundation for the so-called revenue rule, under which the United States, along with many other countries, generally refuses to enforce the tax laws of other states on grounds that to do so would be to take on the role of tax authority against its own people on behalf of a foreign sovereign. *See, e.g.*, *Holman v. Johnson*, (1775) 1 Cowp 341 ("no country ever takes notice of the revenue laws of another"); *Moore v. Mitchell*, 30 F2d 600, 604 ("To pass upon the provisions for the public order of another state is, or at any rate should be, beyond the powers of a court"); *United States v. Harden* (1963) 44 W.W.R. 630, 634 ("enforcement of a claim for taxes is but an extension of the sovereign power that imposed the taxes"). The revenue rule is consistent with conventional principles surrounding conflict of laws, which permit states to regulate their people, even extra-territorially, but cannot oblige others to enforce. Ernest G Lorenzen, *Huber's De Conflictu Legum*, 13 ILL. L. REV. 375, 403 ("The idea of territoriality was expressed, for example, in the first two 'maxims' of the Dutch eighteenth century private international law scholar Ulrich Huber: (1) The laws of each state have force within the limits of that government and bind all subject to it, but not beyond. (2) All persons within the limits of a government, whether they live there permanently or temporarily, are deemed to be subjects thereof."); JOSEPH STORY, COMMENTARY ON THE CONFLICT OF LAWS (1834), s.20; 21 ("no state or nation can, by its laws, directly affect, or bind property out of its own territory, or persons not resident therein ... To this general rule there appears the exception that a nation has a right to bind its own citizens or subjects by its own laws in every place; but this exception is not to be adopted without some qualification).

[120] Boll, *supra* at 303; Story *supra* note 119 ("No nation will suffer the laws of another to interfere with her own to the injury of her own citizens; and whether they do or not depends on the condition of the country in which the law is sought to be enforced, the particular state of her legislation, her policy and the character of her institutions. In the conflict of laws, it must often be a matter of doubt which should prevail; and, whenever a doubt does exist, the court which decides will prefer the law of its own country to that of the stranger.").

jurisdiction to tax. That scholarship has mainly focused on identifying and explaining the boundaries of the sovereign power, rather than identifying and explaining the scope of potential duties among sovereigns to each other when it comes to taxation.

Even if the United States has a right to tax individuals based on their nationality or citizenship, then, it does not automatically follow that other states are obligated to locate individuals who may be U.S. citizens for the sole purpose of making the United States aware of their existence so that it can begin taxing them.[121] In fact, by most accounts, the opposite must be true: the equal sovereignty of other states over their own peoples and territory would seem to stand in direct confrontation of that view. The inability to resolve this conflict with any normative principle seems to reinforce the general failure of sovereignty as an acceptable theory of the jurisdiction to tax.

B. Facilitation of Tax Avoidance

Going in the opposite direction of citizenship taxation, some states have been critiqued (and in some cases investigated) for using their tax system to interfere with or deprive a rightful tax jurisdiction sought by others. Prevalent among these claims are that states are facilitating aggressive tax-avoidance schemes, such as diverting profits with lax transfer pricing rules and taxpayer-friendly financial structures and transactions,[122] that richer states' tax policies are harming poorer states,[123] and, within the European Union, that some states are, in a practice referred to as fiscal state aid, using their tax system or administration to deliberately to divert business and investment away from the others.[124] The OECD's project on base erosion and profit

[121] For a discussion, see Christians *supra* note **Error! Bookmark not defined.** at 105-06.

[122] Most of these claims are from nongovernmental organizations that seek to connect taxation to the fulfillment of human rights goals, but some are from government officials. *See, e.g.*, Claire Godfrey, *Tax rules facilitate avoidance, with developing countries the biggest losers*, THE GUARDIAN, 2 May 214, at https://www.theguardian.com/sustainable-business/tax-avoidance-multinationals-developing-countries-oxfam-report; *Report of the High Level Panel on Illicit Financial Flows From Africa* (2015), www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf; Global Financial Integrity/UNDP, ILLICIT FINANCIAL FLOWS FROM THE LEAST DEVELOPED COUNTRIES: 1990-2008 (2011), www.gfintegrity.org/report/report-least-developed-countries/; Joseph Spanjers and Håkon Frede Foss, *Illicit Financial Flows and Development Indices: 2008–2012* (2015), www.gfintegrity.org/wp-content/uploads/2015/05/Illicit-Financial-Flows-and-Development-Indices-2008-2012.pdf; UNHRC, 'Final draft of the guiding principles on extreme poverty and human rights, submitted by the Special Rapporteur on extreme poverty and human rights' (2012), *http://www.ohchr.org/EN/Issues/Poverty/Pages/DGPIntroduction.aspx*; Action Aid, *Sweet Nothings* (February 2013), www.actionaid.org/publications/sweet-nothings; Matthew Hill, *Zambia Says Tax Avoidance Led By Miners Costs $2 Billion a Year*, Bloomberg Business News, 25 November 2012: www.bloomberg.com/news/articles/2012-11-25/zambia-says-tax-avoidance-led-by-miners-costs-2-billion-a-year; UNECA, *The State of Governance in Africa: The Dimension of Illicit Financial Flows as a Governance Challenge, Third Meeting of the Committee on Governance and Popular Participation*, 20-21 Feb. 2013 (E/ECA/CGPP/3/2), http://repository.uneca.org/handle/10855/22142.

[123] See, e.g., Niko Lusiani, *Monitoring Tax Spillovers In The Financing For Development Accord*, 9 April 2015, at http://www.cesr.org/article.php?id=1718; OECD, Policy coherence for inclusive and sustainable development, https://www.oecd.org/dac/POST-2015%20PCD.pdf.

[124] Treaty on the Functioning of the European Union (TFEU) Art 107(1); DG Competition – Internal Working Paper – Background to the High Level Forum on State Aid of 3 June 2016, ; see also Allison

shifting (BEPS) is parallel evidence of growing concern about the obligations states may have to other in regards to tax. The emerging phenomenon of "spillover analyses," under which states examine certain of their own practices with respect to smaller or weaker states, similarly displays new-found concern for the extra-territorial impacts of a state's competitive tax policies.[125]

Based on what normative theory would states need to concern themselves with how their domestic policies impact the domestic policies of other states? The idea seems patently at odds with the accepted tax jurisdiction frameworks of sovereignty, since the sovereign state is entitled to act without constraint, as well as nexus, since each state's entitlement to tax on the mutually accepted factors of residence and source would seem to forestall any forced deprivation of its claim by the others. Indeed, the nexus framework in particular appears to have nothing to say about whether states are obliged to assist each other or refrain from harming each other. Leaving sovereignty to the task results, as explained below, in a very unsatisfactory justification for compelling tax cooperation among states. However, in this case the membership principle has more to add to the analysis, affirming its potential normative strength in comparison.

1. Sovereignty

Sovereign entitlement holds that no state need concern itself in the tax affairs of others, but, as the further examination of the theory above shows, the principle is unjustified in theory as well as unworkable in fact. Even so, sovereignty has been explicitly advanced, albeit paradoxically, as an explanation for curbing sovereignty in some circumstances.

The positioning of sovereignty for this purpose first arose almost two decades ago, when the OECD explored the idea that "countries may be forced by spillover

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Christians, *Friends With Tax Benefits: Apple's Cautionary Tale*, 78 TAX NOTES INT'L 1031 (June 15, 2015) (explaining the origin of the EU's investigation into illegal state practices by Ireland in respect of Apple);

[125] For example, the UK Parliament recently considered and rejected a bill that would have required the government to assess and report on the impact of British tax treaties with developing countries. Double Taxation Treaties (Developing Countries) Bill (HC Bill 16), 28 Nov 2016, at http://services.parliament.uk/bills/2016-17/doubletaxationtreatiesdevelopingcountries.html (covering, inter alia, the U.K.'s duty "to have regard to reducing poverty overseas in entering negotiations [and] to assess and report on reducing poverty before a treaty is signed"). This follows the release of co-called "spillover analysis" studies undertaken by the Netherlands and Ireland to investigate the effects of their tax systems on the economies of developing countries. Francis Weyzig, Evaluation issues in financing for development; Analysing Effects of Dutch Corporate Tax Policy on Developing Countries, November 2013; IBFD Spillover Analysis Possible Effects of the Irish Tax System on Developing Economies, July 2015, at http://www.budget.gov.ie/Budgets/2016/Documents/IBFD_Irish_Spillover_Analysis_Report_pub.pdf. A joint report to the G20 undertaken by the IMF, WB, OECD and UN encouraged G-20 countries to undertake spillover analyses "of any proposed changes to their tax systems that may have a significant impact on the fiscal circumstances of developing countries...in moving, for instance, from residence to territorial systems." SUPPORTING THE DEVELOPMENT OF MORE EFFECTIVE TAX SYSTEMS: A REPORT TO THE G-20 DEVELOPMENT WORKING GROUP BY THE IMF, OECD, UN AND WORLD BANK (2011) http://www.oecd.org/ctp/48993634.pdf [hereinafter Effective Tax Systems Report]

effects to modify their tax bases, even though a more desirable result could have been achieved through intensifying international co-operation."[126] "Spillover effect" is an economics term that generally connotes the impact of one state's policy actions on the economic outcomes of other states.[127] In invoking the idea of spillover, the OECD's expressed fear in 1998 was that one sovereign state could design tax policies that would undermine the policymaking autonomy of another, thus violating the latter's sovereignty. In the view of many at the time, the undermining countries were nonOECD members, mainly small, island jurisdictions, whose participation in global financial and commercial flows could be boiled down to that of parasites, termites, and renegades, working away at the fabric of the international tax order.[128] The OECD sought to "shut down" these uncooperative jurisdictions, but softened its stance after losing key support for the initiative from the United States.[129]

The OECD accordingly argued that sovereign states might be obligated to refrain from a number of actions that might impede or adversely impact the tax efforts or economic outcomes of others.[130] By 2006, the OECD had concluded that, as a matter of tax sovereignty, "tax competition between countries [must be] based upon transparent and internationally accepted standards, including standards of international cooperation in tax matters necessary to counter the increased cross-border opportunities to unlawfully avoid or evade national taxes enacted by democratically elected legislatures."[131] An influential paper published the same year by IMF economist Peter Mullins brought spillover analysis to the forefront of policy debate, by examining the predicted impact of a U.S. move to territorial taxation on the rest of the world (looking

[126] OECD, HARMFUL TAX COMPETITION (1998), https://www.oecd.org/tax/transparency/44430243.pdf

[127] However, it is also used more casually by non-economists to connote the general impact of one state's policy choices on that of others.

[128] Vito Tanzi, *Globalization and the Work of Fiscal Termites*, IMF Finance and Development Vol 28:1 (March 2001); Joel Slemrod and John D. Wilson, *Tax Competition with Parasitic Tax Havens*, 93 J. PUB. ECON. 1261 (2009); Lorraine Eden & Robert Kudrle, *Tax Havens: Renegade States In The International Tax Regime?* 27 L. & POL'Y 100 (2005).

[129] *See* Andrew Morriss and Lotta Moberg, *Cartelizing Taxes: Understanding the OECD's Campaign against "Harmful Tax Competition"*, 4 COLUM. J. TAX. L. 1, 48 (2011) (describing the events surrounding the withdrawal of the United States from the Harmful Tax Project following the election of George W. Bush to the presidency); Press Release No. PO-366, U.S. Dep't of the Treasury, Treasury Secretary O'Neill Statement on OECD Tax Havens (May 10, 2001), https://www.treasury.gov/press-center/press-releases/Pages/po366.aspx (explaining the U.S. Treasury's decision to "re-evaluate the United States' participation in the Organization for Economic Cooperation and Development's working group that targets 'harmful tax practices'").

[130] All of these claims are explored in Christians, *supra* note 25 (discussing OECD claims that states should refrain from, *inter alia*, impeding a country's autonomy in the design of its tax system; adversely impacting the tax base in another country; creating externalities that allow the state to bear little of the cost of its own preferential tax regimes; allowing people to benefit from public goods without contributing to them; frustrating other country's audit procedures; distorting trade and investment with deliberately non-neutral tax regimes; causing a shift of targeted activities to economies outside the OECD area by employing an "unwarranted competitive advantage"; or limiting the effectiveness of the OECD's cooperative exercise (using "practices [that] are anti-competitive and can undercut the gains that tax competition generates").

[131] OECD, REPORT ON HARMFUL TAX PRACTICES (2006).

at FDI outflows, intensity of tax competition, and tax revenues in host countries).[132] Mullins' paper sketched out some of the possible spillovers and concluded that the move to territoriality should be rejected because it would have significant and negative effect on poor countries that were in competition for capital investment from the United States.[133]

Calls for spillover analysis have continued since then, with recent papers defining spillover to include both base spillover effects (an action by one country that affects another without the second doing anything in response) and strategic spillover effects (an action by one country that creates an incentive for a second country to change its own policy).[134] The intensity of this work may be seen as culminating in the BEPS project, in which the OECD has reasserted and refined its approach to defining obligations among states.[135] In fact, it is doing so more clearly and forcefully than ever, by advancing the mechanism of peer review on four "minimum standards" that were agreed to in BEPS, together with additional agreed monitoring areas.[136] Peer review is in effect a means of policing spillover effects, simultaneously "measuring and monitoring"

[132] Peter Mullins, *Moving to Territoriality? Implications for the United States and the Rest of the World*, IMF Working Paper 06/161 (June 2006), at http://www.imf.org/external/pubs/ft/wp/2006/wp06161.pdf

[133] Id ("Past experience suggests that further reductions in tax rates owing to tax competition is likely to affect developing countries more than developed countries, with the main impact being a reduction in much-needed tax revenues. It is the impact on tax revenues that is likely to be the biggest concern for the rest of the world, especially for developing countries."). The possible spillovers included that a change in the tax base or rate in a capital exporting country like the US, for example, might (or might not--most claims are contested): reduce overall foreign direct investment; retain overall foreign direct investment level but change location to lower tax countries; increase efforts by conduit countries to attract foreign direct investment flows; increase pressure on host countries to lower source taxes; force host countries to search for alternative sources of revenue; force host countries to increase administrative costs to counter tax avoidance schemes; or reduce overall revenue in host countries.

[134] IMF, Issues in International Taxation and the Role of the IMF (2013), http://www.imf.org/external/np/pp/eng/2013/062813.pdf

[135] See OECD, Action Plan on Base Erosion and Profit Shifting 25 (2013) [hereinafter OECD 2013 BEPS Report], https://www.oecd.org/ctp/BEPSActionPlan.pdf ("[I]nterested G20 countries that are not members of the OECD will be invited to be part of the project as Associates, i.e. on an equal footing with OECD members (including at the level of the subsidiary bodies involved in the work on BEPS), and will be expected to associate themselves with the outcome of the BEPS project. Other non-members could be invited to participate as Invitees on an ad hoc basis."); *All Interested Countries and Jurisdictions to Be Invited to Join Global Efforts Led by the OECD and G20 to Close International Tax Loopholes*, OECD.ORG (Feb. 23 2016), http://www.oecd.org/newsroom/all-interested-countries-and-jurisdictions-to-be-invited-to-join-global-efforts-led-by-the-oecd-and-g20-to-close-international-tax-loopholes.htm. Work on BEPS officially began in June 2012 with an announcement by the G20 in support of the initiative. G20, 1, 9. By February of 2013, the OECD released its initial report, identifying the fifteen action item areas and setting a "rapid" timeline of as little as twelve months for delivery of action items. OECD 2013 BEPS REPORT at 24 (stating tautologically that "[t]he pace of the project must be rapid so that concrete actions can be delivered quickly," and laying out the expectation that "the Action Plan will largely be completed in a two-year period, recognising that some actions will be addressed faster as work has already been advanced, while others might require longer-term work").

[136] For a discussion, see Allison Christians, *BEPS and the New International Tax Order*, 2016 B.Y.U. L. Rev (forthcoming) (outlining the minimum standards and explain the role and process of peer review).

while also preventing some of the evils described in the Harmful Tax Practices Report and in the more recent IMF reports.[137]

These events may be characterized as an effort of some states to protect their own sovereign prerogatives by forcing others to comply with a set of standards that the former states designed, implemented, and monitored.[138] In its 1998 report, in the series of successive reports it produced on Harmful Tax Practices through 2006, and in BEPS, the OECD offers no normative explanation for determining which states are entitled to curb the sovereignty of others. The earlier reports implied that since the sovereignty of some OECD member states appeared to be at risk from the actions of some non-member states, the former had entitlements that the latter were duty-bound to respect.[139] But BEPS now justifies the OECD's development of international standards to be universally implemented on grounds that states that all states are at risk of having their sovereignty undermined by all others.[140]

The OECD's decision to appoint itself to measure and monitor instances of harms to sovereignty without ever examining the underlying normative claim of sovereignty is, to say the least, unfortunate. The practical impact may be to imperil the legitimacy of the entire exercise, even if its aims were noble.[141] Grounded on sovereignty, however, the use of peer pressure to work states into an order they did not all ask for or help design cannot be equally acceptable to all affected parties.[142] One possible lesson for the

[137] See, e.g., *The OECD' s Peer Review Process: A Tool for Co-Operation and Change*, OECD.ORG, https://www.oecd.org/site/peerreview/. For a discussion of the origins, evolving goals, and uses of peer review at the OECD, see CARROLL & KELLOW, *supra* 31–34.

[138] *BEPS-Frequently Asked Questions*. ("[The BEPS outputs] are soft law legal instruments. They are not legally binding but there is an expectation that they will be implemented accordingly by countries that are part of the consensus. The past track record in the tax area is rather positive. . . . [A]ll OECD and G20 countries have committed to consistent implementation in the areas of preventing treaty shopping, Country-by-Country Reporting, fighting harmful tax practices and improving dispute resolution.").

[139] I explored the failure of principled explanation of this logic in Christians, *supra* note 25.

[140] OECD 2013 BEPS Report.

[141] Pierre-Hugues Verdier, *Transnational Regulatory Networks and Their Limits*, 34 YALE J. INT' L L. 113, 163 (2009) (demonstrating that transnational regulatory networks built upon mainly soft law coordination mechanisms are "ill-equipped to effectively address enforcement problems," as illustrated in the case of the Basel Committee on Banking Supervision, whose 1988 Basel I Accord "gradually unraveled as national regulators adopted self-serving exceptions and interpretations because the Committee had little effective leverage to enforce its rules," and in the case of the International Organization of Securities Commissions, whose bilateral securities regulation agreements "painstakingly avoid commitments that would bind . . . powers to act against important domestic interests in specific cases"); ROBERT O. KEOHANE, AFTER HEGEMONY: COOPERATION AND DISCORD IN THE WORLD POLITICAL ECONOMY 51–52 (1984) ("[I]ntergovernmental cooperation takes place when the policies actually followed by one government are regarded by its partners as facilitating realization of their own objectives, as the result of a process of policy coordination."); JOHN BRAITHWAITE & PETER DRAHOS, GLOBAL BUSINESS REGULATION 553 (2000) ("Self-regulated cooperation without enforcement by a leviathan is possible . . . when there is a commitment 'to follow the rules so long as (1) most similarly situated individuals adopt the same commitment and (2) the long-term expected net benefits to be achieved by this strategy are greater than the long-term expected net benefits for individuals following short-term dominant strategies.'").

[142] See, e.g., Nozick, *supra* Ch. 8 ("people have a right to a say in the decisions that importantly affect their lives"). Nozick probes this statement in a footnote, asking, "[w]hy not those that unimportantly

OECD will be that sovereignty is not enough to achieve the amount of global cooperation on tax that its member states apparently desire. However, if states were willing to abandon their insistence on sovereignty as the motivator for reform, the membership principle might help steer the world's tax policymakers in a better direction in the future.

2. Membership

A different and more satisfying normative framework may soon become an urgent necessity for international tax relations because the underlying normative void left by sovereignty (as well as nexus) continuously threaten any effort to join the world in accepting tax policies that look like they protect the tax systems in some countries at the expense of others. This is because, as the BEPS project illuminates, curbing tax competition is not (and will never be) a win-win scenario for all jurisdictions.[143] All countries potentially stand to lose from tax competition, to be sure. But it is equally true that all countries potentially stand to lose from curbing tax competition, as well. It just depends on how that term is defined, and, as defined, how it is to be regulated.

As the OECD moves into the implementation phase of its carefully crafted definition of the types of tax competition to be curbed, it seems clear that the impacts of the new international tax order will not be felt equally by all states. Spillover analysis conceptually has the potential to be a means of monitoring self-dealing in this regard. On the other hand, there is a danger that spillover analysis may be used strategically, to simply reinforce a given framework as a baseline and absolve governments of any culpability for the adverse effects of the international tax regime visited upon those outside its traditional power structure. Basing the need for care about the effects of one state's actions on the economic outcomes on another on sovereignty alone will allow state to simply abandon the effort when it no longer seems important to them (such as, for example, when the public and therefore the politicians lose interest in the project).

In contrast, the membership principle holds that a state is entitled to tax those who are members, by virtue of the explicit consent evidenced by those members in availing themselves of public services and infrastructure. Applied to the types of rules and practices the OECD describes as interfering with sovereignty, the membership principle would instead cast the harm as one of facilitating a betrayal of a society in which a

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affect their lives as well, with some scheme of weighted voting used (with the number of votes not necessarily being proportional to the degree of effect)?" *Id.*

[143] *See, e.g.*, Adam Rosenzweig, *Why Are There Tax Havens?* 52 Wm. & M. L. Rev 923 (2010); Steven Dean, *The Incomplete Global Market for Tax Information*, 49 BCL Rev. 605 (2008); Christians, *supra* note 136. The biggest winners are likely to be the architects of BEPS, who define tax competition, sort it into acceptable and non-acceptable categories, and design the regulations to eliminate the latter. Adherents, who contribute modestly or not at all to the design and build, may equally benefit from the collective action that ensues. But there are many jurisdictions are not described in either of the foregoing categories. *See, e.g.*, Ronen Palan, *Tax Havens and the Commercialization of State Sovereignty*, 56 INT'L ORG. 151 (2002); Dharmapala Hines, *Which Countries Become Tax Havens?* 31 J. PUB. ECON. 1058 (2009).

person has willingly, voluntarily, and explicitly signaled membership.[144] The membership principle is more satisfying than sovereignty in this case not because it changes the harm but because it changes the idea of who is harmed. For sovereignty theorists, it was the state. For membership theorists, it is the members of a society who have explicitly contracted with each other and have expressed their consent to be governed.[145]

Appealing to membership instead of sovereignty suggests that in agreeing to things like BEPS minimum standards and peer monitoring, states are not using their sovereign power to coerce each other (as attempted in the Harmful Tax Practices Project and achieved in FATCA), but because each has a duty to prevent its own members from betraying each other, and none has the right to help members of other societies betray those societies. Facilitating tax avoidance thus looks like helping people free ride when the evidence of their use of public services and infrastructure already explicitly admitted their intent to be members of other societies. By changing the rationale from protecting sovereignty to protecting the consequences of freely made individual choices, the membership principle might be more compelling than the sovereignty rationale.

Again, neither rationale answers the pragmatic question of what states are capable of as a matter of power in the global economy or the society of states. None of the three rationales is equipped to answer those questions, but membership at least posits a plausible normative framework that could guide states in their efforts to convince each other to cooperate on international tax.

IV. CONCLUSION

An expansive state might (by design or inadvertently) include those that should be excluded from its jurisdiction, or it might enable individuals to escape the rightful jurisdictional claims of other states in which they are members. Conversely, a state might exclude from decision-making those that are directly affected by the polity's decisions. Any of these outcomes challenge the notion about the fundamental rights individuals hold and the duty of the state to respect and uphold those rights even as it sustains itself through taxation. In the context of ever-intensifying integration of markets and populations across global societies, the likelihood of both over- and under-inclusivity is continuously expanding, making justifiable claims about the jurisdiction to tax are an increasingly vital element of any coherent normative analysis of a tax system.

While sovereignty itself is very often referred to as the justification for the state's jurisdiction to tax, the claim is far from normatively acceptable. Nexus via

[144] Simmons *supra*; Gibson *supra* at 152 ("Given that a sense of betrayal is appropriate in the context of a joint commitment, such a commitment clearly gives the parties a special standing in relation to one another's actions. There are certain actions that one party can only perform at the cost of betraying the other party.").

[145] Gibson *supra* at 287-288 ("There is a recognized class of genuine obligations that have a special feature—directedness—that I interpreted in terms of *owing*, following H. L. A. Hart and others. If I have a directed obligation towards you I owe you an action. In other terms, I am obligated *to* you to perform that action.")

residence and source, equally a permanent feature of the tax policy landscape, is more justifiable than sovereignty but is nevertheless characterized in both theory and practice by serious normative weakness. Nevertheless, tax policy scholarship continues to adhere to long-held perceptions about the intrinsic nature of sovereignty as power, of the sovereign state as a rightfully needy creature entitled to raise money to finance its own vital functions, and of the comfortable certainty of the residence and source principles, even if all are normatively flawed. As a few contemporary examples of jurisdictional dilemmas demonstrate, the membership principle potentially adds some useful language to the debate about what states and people owe each other, and what they can rightfully expect from each other, in the transnational tax law order. It remains to be seen whether the principle can help overcome the persistent associations of taxation with ideas about benefits, contract theory, pragmatism, and even patriotism and develop a different, more normatively justifiable definition of he tax jurisdiction.