

# Interrogating the Relationship Between “Legally Defensible” Tax Planning and Social Justice

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# Tax Planning < -- > Social Justice

I was asked to explore the above link, for a conference organized by the NYU Center for Human Rights & Social Justice.

If tax cheating by the super-rich & major corporations were a major cause of rising high-end inequality ...

... then the link between tax ethics & distributive justice would be straightforward.

But most of these groups' tax planning – reflecting their interests & incentives – is, at a minimum, “legally defensible.”

Doesn't eliminate the link – but certainly complicates it.

# The Romney defense

“I paid every penny I owed – but not a cent more.”

Agreed, no ethical duty to overpay (if accept self-interest as a permissible guide in ordinary daily life).

On the other hand, that sounds way more passive & automatic than high-end tax planning actually is.

Note (a) legal uncertainty, (b) audit lottery, (c) fault standard (“reasonable basis”) for most penalties, (d) “unintended” results, (e) lobbying activity (playing both offense & defense).

# Opinion “quality” (one version)\*

<b>Will</b>	At least 90% probability of success if challenged by IRS
<b>Should</b>	At least 70% probability of success if challenged by IRS
<b>More likely than not</b>	Greater than 50% probability of success if challenged by IRS
<b>Substantial authority</b>	At least 40% probability of success; weight of authorities in support is “substantial” relative to that of authorities opposing the position
<b>Realistic possibility of success</b>	At least 1 in 3 probability of success if challenged by IRS
<b>Reasonable basis</b>	Significantly higher than not frivolous, but lower than 1/3
<b>Not frivolous</b>	Not patently improper; some merit to position
<b>Frivolous</b>	Patently improper

## On the one hand, on the other hand

Change the incentives & rules if one wants to change outcomes?

After all, one expects, e.g., Apple & Tim Cook to seek to pay less taxes rather than more. (And note general fiduciary duties to shareholders.)

But exploiting legal uncertainty amid the audit lottery & devising “unintended” tax benefits both raise ethical issues.

Plus, social norms play a role in what TPs & their advisors do.

# Ethics for myself vs. ethics for you

Suppose I hold myself to a higher ethical standard than I demand of others.

I would not be proud of myself (although I'd be well-compensated) if I had devised Apple's "Double Dutch Irish Sandwich" &/or negotiated its deals with Irish & Luxembourg tax officials.

But (a) someone will, and (b) I have no qualms about maintaining friendships with people who do these things.

Also, (c) given that I'm doing what I want, & generally am not treated too badly, my "ethics" are quite convenient for me!

# Why not write a “2-handed lawyer” paper?

On the one hand, blah blah; but on the other hand, blah blah.

But I thought this would be boring, so tried something a bit different.

To wit, a dialogue – not Socratic, but between 2 evenly matched friends who have taken different career turns & who argue intelligently (I think) & in good faith.

Don't assume the law prof is me! – I hear both voices.

## The players and the ground rules

“Megan,” a tax professor who “favors increasing high-end effective rates,” but is now “keenly aware ... of the associated efficiency costs & practical difficulties” that can turn well-intended rules into fiascos.

“Russell,” an economist & her former Treasury colleague, now doing tax planning & lobbying in DC for an accounting firm, has seen first-hand how convoluted pro-gov’t rules just create tedious mazes through which he must (& can) guide his clients.

Their rule: 2 propositions each, fair-minded & candid debate.

My rule: No speeches longer than a short paragraph w/o interjection.



# Proposition #1

MEGAN: “Large-scale tax avoidance by wealthy individuals and large companies that is legally defensible can nonetheless harm social justice and public morale.”

This might be true but banal, a la “Sometimes the normal pursuit of self-interest has bad social effects.”

But Russell demands empirical evidence re. corporate tax incidence and the claimed ill effects on public morale.

Megan notes links between corporate tax avoidance & taxing owner-employees (e.g., Steve Jobs), & issues around high-end inequality between individuals.

## Proposition #2

RUSSELL: “Taxpayers have a right to pay as little tax as they legally can. If you don’t like the results, change the rules!”

Megan brings up legal uncertainty & the audit lottery, proposes no-fault penalties (e.g., based in principle on audit lottery odds).

Russell: Right or wrong, that means you agree with me – you’re saying we need to change the rules so people will act differently.

Megan: But in the absence of adequate penalties ...

## Proposition #3

MEGAN: “Tax advisors’ professional and personal ethical obligations require them to do more than just minimize expected tax liability.”

Russell notes fiduciary obligations to clients.

And, even outside his comfort zone, “if people have incentives to do things, they will do them. It’s like an ecological niche for nasty things like mosquitoes.”

Both: there are ethical responsibilities towards the system – but where to draw the line, & how sustainable it is without reputational or other prudential pressures, is unclear.

## Proposition #4

RUSSELL: “It’s a tactical error for human rights advocates to focus on ‘corporate social responsibility’ & tax professionals’ ethics rather than on the existing rules & resulting incentives.”

E.g., good luck if you think American consumers are going to boycott Apple over the Double Irish Dutch sandwich!

Megan: But one may need silly moralism to sell good policy politically (e.g., if you dislike inversions, may need politicians to rant about “Benedict Arnold” companies & CEOs).

Russell doesn’t like this – so for a change he’s the intellectual purist of the two.

## Closing thoughts

Movie rights available; casting suggestions appreciated; lessons inconclusive.

Broader academic ruminations: Note relationship to compliance literature (Allingham-Sandmo vs. TP “morale”).

Avoidance  $\neq$  evasion, & the players are different, but similar in departing from pure “rational” calculation (defined in terms of \$\$ & risk aversion)?

Easier to affect than general TP morale?

But views/tastes will differ re. approaching this moralistically, linking up tax planning aggressiveness w/ “rights” rhetoric.