"An Unacceptable Surrender of Fiscal Sovereignty": the neoliberal turn to international tax arbitration

Appendix 1: the development of the international tax regime from the 1920s to 1960s

State and Capital collaborate to create a new regime

The moment when tax affairs were most open to institutional innovations was the 1920s. The second half of the 19th century had seen the diffusion of corporate income taxes throughout the Western world, often – as in the United Kingdom and Austria – initially as a temporary measure (Seligman 1914). By the turn of the 20th century, these states had begun to consolidate corporate income taxes, and were joined by late starters, notably the United States in 1894 and France in 1909. States raised rates further during World War I. At this point, international taxation of multinational corporations was not a major concern, since most international investment flows were in the form of loans to governments and most of what we would today think of as multinationals were in fact separate companies acting as cartels (Picciotto 1992). Nonetheless, limited cross-border investment resumed after the war, and businesses began to complain about the problem of what they rhetorically framed as "double taxation."

The problem as they saw it was this. If a multinational company owed U.S. tax on its worldwide income (including that generated in France) and owed French tax on that same French-derived income, then it could be said to be double taxed. To complicate matters, businesses also labeled as "double taxation" the co-existence of the corporate tax and a tax on dividend payments to individuals – conflated in countries like France by additional tax withholdings for dividends paid to foreigners, or so-called "triple taxation."

There is no necessary reason business' framing should have prevailed. Indeed, governments still do not accept that there is a normative wrong in taxing both corporations and dividends (Bank 2010). What businesses saw as international double taxation could have instead been described as a tax on capital mobility and a way to root capital nationally. In the words of Senator Charles Curtis (R-Mo.), U.S. tax policy *should* penalize American firms that invest abroad: "Our people get the worst of it, and they ought to, if they go to another country to invest. Let them invest in their own country" (Penrose, 1921, 64). Or as Rep. John Nance Garner (D-Texas) – who would become Franklin Roosevelt's first vice-president – put it in 1930, lessening double taxation "is going to lose money and give an opportunity and a haven for large taxpayers to escape paying taxes" (Hawley 1930, 47).

Nevertheless, prevail business did – using a number of techniques. First, lawmakers were subjected to threats of a capital strike. Testifying before Congress in 1918, Phanor Eder of the Mercantile Bank urged lawmakers to exempt overseas income from any taxation, and sharply reduce the corporate income tax at home. If they did not, "the first effect will be that these corporations will be compelled to give up their American charters and will be compelled to seek incorporation in foreign jurisdictions, naturally in the place where they are doing business, and in that way this Government is going to lose that revenue from those corporations." (Kitchin 1918, 649). An International Chambers of Commerce (ICC) resolution in 1920, one of a series addressed to the League of Nations, called for "prompt agreement between the Governments of the Allied countries in order to prevent individuals or companies from being compelled to pay a tax on the same income in more than one country" (Graetz and O'Hear 1997, 1066).

Second, business penetrated government. Conservative parties dominated the U.S., U.K., and French legislatures for most of the 1920s. Robber Baron Andrew Mellon was the U.S. Treasury Secretary, and called double taxation "evil," "unscientific and unsound" (Hawley 1930, 18). The economist Thomas Adams dominated the US's international tax policymaking during the decade, first as the Treasury's principal tax advisor, and then as its lead representative in international negotiations (Adams 1929; Graetz and O'Hear 1997). He also sat on the ICC's committee on Double Taxation and chaired a US Chamber of Commerce subcommittee on the topic. On the global scale, the League responded in 1921 by creating a committee of fiscal experts, consolidated in 1929 into a Fiscal Commission. Although the US was not a member of the League, Adams and other US representatives were deeply involved throughout the era, both via the ICC and the League.

This co-mingling of private and public interests had serious consequences. The draft model texts adopted 'transfer pricing' to allocate the multinational corporate tax base. This required the conceptual fragmentation of multinational firms into separate entities, each of which would be taxed independently on its profits as if it were not part of a multinational group. This would give businesses substantial discretion in reporting income gains in favorable jurisdictions. It was favored by the representatives of capital exporting countries such as the United Kingdom and United States, in spite of the widespread use of more holistic approaches in continental Europe (Picciotto 1992, 27–35). The decision was heavily influenced by Adams' successor on the US delegation, Mitchell Carroll, also a member of the ICC's US committee. Carroll used a Rockefeller Foundation grant to write a report for the League, concluding that the main alternative to separate accounting – unitary taxation, a method of accounting would have sharply limited business discretion, instead linking profits to the location of business – was economically and political marginal (Carroll 1935). To resolve any disputes, the model conventions included an arbitration provision. The combined effect of these pro-capital design choices was to sideline methods whereby generally poorer and administratively weaker capital importing countries might have a shot at taxing inbound capital.

Yet business did not get everything it wanted. The regime left national governments' veto powers intact. The Commission opted for a bilateral treaty regime, which should be negotiated using model agreements first agreed by the body in 1928. It made this recommendation in spite of a recognition that multilateral agreement would be a more effective solution to the problem at hand, but concluded that "the fiscal systems of the various countries are so fundamentally different that it seems at present practically impossible to draft a collective convention, unless it were worded in such general terms as to be of no practical value" (League of Nations 1927, 8). The first double taxation treaty the U.S. would sign, in the final days of the Hoover administration, was bilateral with France – and no provision for arbitration (or any other cooperative mechanism) was included. Indeed, in spite of a recognition at this early stage that arbitration provisions might be needed, they would not become a part of bilateral tax treaties for many decades.

Phase 2: Collaboration gives way to antagonism

As the Great Depression worsened, cross-border capital and trade flows shrank. World War II battered capital stocks and saw government's share of national income rise to new heights. Over this period, governments shed their alignment with business and began to operate autonomously (Piketty 2014). In 1936, President Roosevelt captured the zeitgeist when he said capital "had begun to consider the Government of the United States as a mere appendage to their own affairs. We know now that Government by organized money is just as dangerous as Government by organized mob… They are unanimous in their hate for me--and I welcome their hatred."

This shift towards greater state power was reflected in changes to the double taxation regime. Roosevelt signed treaties with Canada and the United Kingdom that added inter-governmental exchange of tax information about private taxpayers from each country. Tax officials would later explain the thinking with the proposal: "If we are going to exchange information and our people are over there and they are your taxpayers, we should give you information on them, and if your people are in England, you should give us information on them. We should not draw lines of nationality" (Vandenberg 1947, 978). In 1939, Roosevelt pushed through a treaty with Sweden that added a commitment of each government to aid in collecting the taxes of the other. A year later, the administration extended these onto Hoover's earlier French treaty – saying the existing convention had a "method of eliminating double taxation [that] afforded the taxpayer the opportunity of being relieved entirely of taxation" (Harrison 1940, 13). These pro-state additions were so uncontroversial that the Senate did not even hold hearings, and – after the war was over and the Vichy government removed – the Senate gave approval without a single member objecting.

Belatedly, as war patriotism ebbed, business reacted. In 1946, the Truman administration extended the French treaty's cooperation mechanism to enable French authorities to collect taxes due to the US by US citizens and businesses operating in France. The case they made for mutual assistance emphasized the need for discipline of business:

> It is very rare that [countries] have ever exercised [the cooperation requests]. They compromise with the taxpayer and settle things out without ever having to call on each other country for enforcement. I might say that we have had our treaty in force with Sweden for about 6 years and we have had only one case… without such provision with another country we are constantly confronted with situations where the taxpayers owe us money. Their assets are abroad and they ignore us more or less …with the spread of these conventions and the announcement that we are going to have a negotiation with another country they do come in and begin to talk to us even before the treaty goes through. In that respect they are quite valuable from the United States point of view on collections (Quoting from a 1946 hearing) (Vandenberg 1947, 23-24).

Businesses mightily protested. Carroll – now with the National Foreign Trade Council (NFTC), another lobby group for multinationals – testified, "we feel it violates our Constitution and the rights of American citizens and companies… we want to make this absolutely plain. We must conscientiously and consistently oppose the enforcement provisions in this treaty or in any other treaty that might be adopted which do not exclude from its operation American citizens and corporations" (Vandenberg 1947, 34-38).

These cries fell on deaf ears. Sen. Alexander Smith – a New Jersey Republican – responded, "I see something in the government's point… I do not know why you should give a special status to Americans trying to evade taxes as against anybody else." "That is what it really amounts to. It absolutely amounts to that," responded an administration official (Ibid, 41). While the administration asked tax negotiators to compromise with the NFTC, the resulting renegotiation kept states' procedural prerogatives largely intact. The result passed by acclamation.

This relative non-accommodation of capital was mirrored internationally. As the League prepared to hand its functions over to the new United Nations in 1946, the fiscal committee (with Carroll still serving on it after all these years and after he had left government employ) wrote that "it might be desirable to examine again whether tax treaties should not be so formulated as to permit the application of the most-favoured-nation clause" – a legal mechanism to effectively multi-lateralize bilateral pacts. However, the practical implications of such musings were nil. The same document noted that the new international model treaties contained procedures for taxpayers to complain to national authorities about double taxation, but noted "that the procedure contemplated is not a judicial procedure, but a direct consultation between the tax administrations involved" (Fiscal Committee 1946, 32).

References

Adams, Thomas S. 1929. "International and Interstate Aspects of Double Taxation." Proceedings of the Annual Conference on Taxation under the Auspices of the National Tax Association 22: 192–99.

Bank, Steven A. 2010. From Sword to Shield: The Transformation of the Corporate Income Tax, 1861 to Present. Oxford University Press.

Carroll, Mitchell Benedict. 1935. Taxation of Foreign and National Enterprises. Geneva: League of Nations.

Fiscal Committee. 1946. London and Mexico Model Tax Conventions: Commentary and Text. Geneva: League of Nations.

Graetz, Michael J, and Michael M O'Hear. 1997. "The 'Original Intent' of U.S. International Taxation." Duke Law Journal 46(5): 1020–1109.

Harrison, Pat. 1940. France - Double Taxation. Washington, DC: U.S. Senate Committee on Foreign Relations. Executive Report.

Hawley, Willis C. 1930. (U.S. House of Representatives) H. R. 10165: A Bill to Reduce International Double Taxation. Washington, DC: Government Printing Office.

Kitchin, Claude. 1918. (U.S. House of Representatives) Revenue Act of 1918, Part 1: Income, Excess Profits, and Estate Taxes. Washington, DC.

League of Nations. 1927. Report of the Committee of Technical Experts on Double Taxation and Tax Evasion. Geneva: League of Nations.

Penrose, Boies. 1921. (U.S. Senate) Internal Revenue: H.R. 8245, Part I.

Picciotto, Sol. 1992. International Business Taxation : A Study in the Internationalization of Business Regulation. London: Weidenfeld & Nicolson.

Piketty, Thomas. 2014. Capital in the Twenty-First Century. Cambridge Massachusetts: Harvard University Press.

Seligman, Edwin RA. 1914. The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad. New York: Macmillan.

Vandenberg, Arthur. 1947. (U.S. Senate) Executive A: Convention with France on Double Taxation. Washington, DC: Government Printing Office.

Appendix 2: list of interviews (numbered) and informal conversations

	2015, Oxford	*Lawyer (US)* *Lawyer (UK)*
1	2015, Skype	International organisation secretariat staff member
2	2015, Washington DC	Lawyer (US) Lawyer (US)
3	2015, Washington DC	Treasury official (US)
4	2015, Skype	Former international organisation advisor
5	2016, London	Accountant (UK)
6	2016, London	Lawyer (UK)
7	2017, Geneva	Lawyer (US)
8	2017, Geneva	Treasury official (Canada)
	2017, London	*International organisation secretariat staff member*
9	2018, New York	Lawyer (Netherlands)