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Summary

This report analyses the major events and developments in international direct taxation. It revolves around four questions. The first question deals with the emergence of the ideational context in international tax policy. Although this is not the only ‘policy idea’ available, there is no doubt that since the mid-1990s harmful tax competition has provided a focal point for tax coordination at the international level. It has also created the pre-conditions for integrating tax issues with other important issues, such as the fight against money laundering. Hence the question arises why have recent international tax initiatives revolved around the notion of harmful tax competition? We answer this question by looking at the major player in international tax coordination, that is, the OECD.

Secondly, we examine the scope of international tax governance. Over the last ten years the OECD has moved towards multilateral, outward reaching and harder modes of governance. We look at the specific modes the OECD has chosen and deal with questions of timing (that is, when) and explanation (that is, why).

Thirdly, we address the question why governance in international taxation has become less technocratic and more political by examining the changing constellation of actors and their preferences.

Finally, we assess what has been achieved in three broad categories, that is, learning, processes, and outcomes.

A full comparative analysis between the OECD and the EU actions in international taxation will be presented in the final report for this project. This report, together with D4, presents the empirical evidence that will be used for the systematic comparison in the final report.

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I. Introduction

In this report we explore the scope of governance in international direct taxation. Four questions have motivated our inquiry in this domain. First, harmful tax competition is not the only policy problem in this area, yet there is no doubt that it has provided a focal point for the initiatives of major organisations involved in the creation of international tax governance – first of all the OECD, but also the EU, the United Nations, and the G7-G8-G20 at critical junctures in the 1990s and post 9-11. The question arises why has harmful tax competition become an idea whose time has come?

Secondly, we were intrigued by the changing scope of tax coordination. Looking at the major player, that is, the OECD, there have been shifting choices about who should contribute to the edifice of coordination, with what modes of governance, and for what final goals in terms of level-playing field. This question about the scope of governance relates this report to some of the major issues underlying the whole NEWGOV project.

Thirdly, modes of governance have also changed in a less technical sense. We refer to the increasing politicisation of the discussion on international tax organisations and tax coordination. What are the causes of politicisation? Does it produce less legitimacy for organisations such as the OECD? Or is politicisation a vehicle for policy learning, and if so how?

The fourth question is about what has been achieved. We cannot handle this question without specifying different types of achievement. Accordingly, we measure achievements in three broad categories, that is, the creation of specific processes for mutual cooperation, exchange of information, and tax cooperation, policy learning at the level of the major players (that is, the OECD, the member states, and offshore jurisdictions), and finally outcomes (for example, whether a level-playing field has been created and is having an impact on the level and type of tax competition).

At the outset, however, it is useful to situate our analysis of international tax coordination in the broader framework of the NEWGOV project. NEWGOV is eminently concerned with the emergence, efficiency, and legitimacy of new modes of governance. Although this is not the exclusive research aim, NEWGOV puts particular emphasis on new modes of governance that enable society to participate in the policy process. Self-regulation – to mention another example - is also a central feature of NEWGOV. Here the main question is about the structural, discursive, and efficiency properties of self-governing networks of private actors and the interplay between soft and hard regulation in enforcement pyramids. The informal characteristics of governance are analysed in NEWGOV both in terms of their outcome and in relation to their participatory quality.

At first glance, this discussion of ‘new’ and ‘old’ modes of governance does not seem a good starting point for international direct taxation. The latter is not an area where one would expect informal governance in the sense of society-centred self-governing networks dominated by private actors. Taxation is a fundamental function of government. In a sense, it defines the state - to such an extent that the proliferation of international tax policy issues has been considered an indicator of fragmentation of the state (Radaelli 1997: chapter 1). In the context of this paper, therefore, we define formal governance in international taxation as binding measures operating in the shadow of sanctions, with a high degree of rigidity (typically, they are applied to all members of a political organisation without opt-out options). By contrast, informal governance is non-binding, operates in the shadow of political determination to act (as opposed to sanctions), and it is often based on ‘a la carte’ options.

But in all cases (formal as well as informal governance) the key actors are Finance Ministers and revenue authorities meeting in organisations like the OECD. There is no important aspect of tax policy that is entirely delegated to the self-regulation of social actors. Moreover, the notion of international tax governance does not imply high degrees of institutionalisation of governance. The ‘international tax order’ is a metaphor. There is nothing similar to a World Trade Organization for taxation and the tax competence of the OECD is not uncontested. Thus, we should perhaps say ‘embryonic tax governance’: there is more chaos than order in this notion.¹ Accordingly, we would expect policy tools with features of informal governance to be the default mode in international tax policy.

This does not mean that governments are always the winners in tax governance. We argue that they will always participate, but winners and losers can change. Indeed, one theme in the long-term history of international direct taxation is that it started with business as the main beneficiary of informal governance, whereas recent patterns seem to benefit revenue authorities and government institutions in general more than business interests. The main winning preferences underlying the political economy of international tax policy have changed over time.

This paper covers the long-term development of informal governance in international direct taxation. We argue that informal governance is ‘old’ governance as far as direct taxation is concerned. This is yet another reason to reject the old versus new governance approach to the design of a governance continuum. Evidence for this claim comes from the emergence of an epistemic community within the League of Nations before World War II and the soft mechanisms used to diffuse principles of income taxation in the first part of the last century. Principles, rules, and instruments were then somewhat institutionalised by the OECD in the context of the model treaty convention and transfer pricing guidelines between the 1960s and the 1980s. The OECD approach – based on informal governance features – was quite successful both in terms of diffusion and in terms of acceptance among stakeholders.

In recent years, the OECD has somewhat ‘hardened’ its approach to modes of governance in three directions. First, the OECD has stepped up gear from bilateral solutions proposed by the Paris-based organisation for adoption by member states (note that even the single articles of the tax treaty convention can be adopted with flexibility and the insertion of special clauses by governments) to multilateral initiatives in which the OECD provides a clear centre of political gravity. Second, the OECD has sought to produce policy change in offshore jurisdictions, thus effectively proposing a more formal definition of the OECD worldview of a ‘fair tax world’. Third, at least in some critical junctures, the OECD has made use of the shadow of sanctions to put pressure on recalcitrant jurisdictions. The implication is that bold statements about a generalised trend towards informality in governance are not corroborated by empirical evidence.

We further argue that the content of international taxation and the competence of organisations like the OECD has become the object of more political discussions about the role of international organisations, their legitimacy, and who should provide the international tax order.

Governance beyond the nation state is a topic predestined to raise concerns about concepts like accountability, legitimacy, and participatory quality (Risse 2004). Without a world state in the international system there’s no monopoly force able to ensure these concepts – the international systems is ‘governance without government’ (Czempiel and Rosenau 1992).

¹ So much so that the idea of a dedicated International Tax Organization has been discussed on several occasions. See Tanzi (1999) and Horner (2001).

The deepening of informal governance structures and relations provides both opportunities and problems. On the one hand it should be easier to get more actors from different levels on board to participate in information exchange, discussion, development of solutions for problems or ideas for improvement and to pursue common goals. On the other hand there is a danger that the lack of hierarchy and commanding control leads to unbalanced participation structures, be it out of opportunistic interests of strong actors or simply because relevant groups of actors were forgotten and therefore not involved in the process. That would create lower acceptance among stakeholders as well as problems of efficiency (Christiansen, Follesdal and Piattoni 2003: 10).

Empirically, over the long-term (say, from the 1930s to the present days), the contestation of international tax policy has increased. There are several reasons for that, most importantly the scope of governance and the range of actors involved therein. The wider the scope and the range of actors targeted by governance mode on the informal side of the spectrum, the larger the contestation of OECD (and EU) initiatives. This may lead to the paradoxical (but false, as will be shown later) conclusion that legitimacy, that is, the perception of legitimacy dominant among international tax policy stakeholders, has been higher under conditions of close, technocratic governance networks – a point hard to reconcile with democratic theory. In this report, we discuss the paradox and conclude that the real issue is about ‘legitimacy for whom?’ We then re-interpret what at first glance looks like a decrease in acceptance (of international tax coordination) as an increase in the political salience of international tax policy. In doing so, we describe another important shift – one from a technocratic logic of international tax policy to a more political logic. This shift towards politicisation has transformed opaque policy domains into arenas where public opinion, diffuse interests, parliamentary oversight, and political parties make tax problems more visible and the logic at work more political. It has also activated learning dynamics, which will be discussed in the remainder of this report.

The report is structured as follows: We first present the history of international direct taxation and the developments on the OECD level (Section 2). We then analyse the case of international direct taxation in the context of the interplay of formal and informal governance and the consequences for acceptance among stakeholders (Section 3). In Section 4 we try to explain shifting modes of governance by addressing the questions of politicisation and moving towards more ambitious governance. The last Section concludes with a short assessment of the achievements made by the OECD and some practical and theoretical recommendations.

II. Crafting International Tax Governance – The OECD

At the outset, the most relevant problem of international direct taxation was the jurisdictional conflict about the taxation of diplomats. But soon the explosion of world trade in the first part of the 20th century brought corporations into the scene. The League of Nations 1928 report on international taxation was a landmark in three respects (Picciotto 1992). First, it defined a set of principles for international taxation. The principles were not invented by the League of Nations, but the latter provided a forum for discussion and systematisation of important definitions of tax policy problems, concepts, and solutions. Second, the process of institutionalisation of principles was supported by the emergence of international consensus among tax experts (Picciotto 1992) – arguably an embryonic epistemic community. Third, the League of Nations report established a soft and very informal method to deal with international tax governance – one based on the gradual diffusion of principles and policy solutions via consensus. Put differently, the role of international governance was to provide a catalogue of problems, a menu of solutions, and a forum for discussion. The diffusion of specific definitions of prob-

lems, solutions, and instruments was left to the propensity of individual governments to buy in into the framework.

After World War II, the major agent of diffusion of mainly informal governance in international taxation was the Organization for Economic Cooperation and Development (OECD)², with primary emphasis on developed countries, although the United Nations has also been active for the rest of the world. Broadly speaking, today the international tax system still follows the path-breaking suggestions of the League of Nations and the ‘codification’ efforts made by the OECD between the 1960s and the 1980s. The main components of this system are the following ones:

- a) *The classification of types of income.* As the League of Nations suggested in 1928, and the OECD followed this suggestion in its model tax convention (OECD 1992), taxing rights are allocated between the residence country and the source country (i.e. the country where income originates) depending on the type of income. For example, the residence country is given the right to tax royalties and capital gains, but the source country can tax profits generated by permanent establishments of a multinational corporation operating within the state. The rule is that if the source country has the right to tax a certain item of income, the residence country will give a credit for the tax paid abroad, or alternatively will exempt that item for taxation, thus eliminating international double taxation. As averred, the main pressure point on the classification of income comes from financial sophistication: new financial instruments and innovative corporate finance strategies have blurred the distinction between debt and equity, income and capital, interest and other forms of return on money.
- b) *The residence principle.* This principle stipulates that a state will tax the income of its citizens comprehensively: both the income earned in the residence country and the income earned abroad must be taxed. The importance of this principle relates to progressive income taxation (one of the bulwarks of the welfare state and re-distributive policies): should foreign income escape taxation, governments would not be able to pursue redistribution and their objectives of fairness and equity. The main pressure point on the residence principle stems from the asymmetrical internationalisation of portfolios and corporate strategies, on the one hand, and public administration, on the other. For a taxpayer there is a panoply of financial instruments and an impressive array of methods for channelling savings abroad through different forms of financial intermediaries acting as ‘tax shields’. Conversely, the internationalisation of tax administration has not progressed much (Picciotto, 1992; Tanzi, 1995). Without a substantive flow of information, significant disclosure, and ultimately cooperation among revenue authorities of different countries, the taxation of foreign income is an unattainable goal.
- c) *The treaty network.* A network of bilateral tax treaties governs the taxation of foreign income. Tax treaties follow the OECD model tax convention, which states, in its preamble, the two important objectives of tax treaty policy: ‘the avoidance of double taxation and the prevention of fiscal evasion’. Two points must be observed. The first point is that bilateral tax treaties face the extremely difficult task of achieving two objectives (i.e., avoidance of double taxation and suppression of evasion) with only one policy instrument,

² Member Countries of the OECD (by March 2006) are Australia, Austria, Belgium, Canada, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, the Slovak Republic, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. The European Commission also takes part in the work of the OECD.

i.e. the treaty. Secondly, historically the emphasis has been on avoiding double taxation, not on tax evasion and tax avoidance. When the League of Nations drafted its suggestions for treaty policy, international double taxation (i.e. the taxation of the same income by two jurisdictions) was the predominant preoccupation of international tax policy-makers. Today, due to the progress in terms of capital movement liberalisation, financial sophistication, and aggressive tax policies pursued by tax havens, the salience of tax avoidance, often in combination with regulatory competition coming from offshore centres, has increased dramatically. Add to this that the institutionalisation of the model treaty has not been complete. Whilst countries agree to art.1 of the OECD model convention (1992) which stipulates that tax treaties cover residents of both countries, the US has always held the view that treaties are only for the benefit of non-resident aliens³. Consequently, the US entered a reservation on art.1 of the model convention. The implication is that the US holds the right to tax its residents as if the treaty did not exist.

- d) *Arm's length rules for transfer pricing.* As far as multinational corporations are concerned, the potential for tax avoidance has increased with the manipulation of transfer prices, i.e. the price that a subsidiary, for example, charges to the headquarters for specific components of a product. The essence of the method is clear and can be articulated as follows: for tax purposes, related enterprises within a multinational company are treated as if they were separate businesses. Consequently, trans-national companies must account for transactions (of goods and services) between their subsidiaries at transfer prices which would be ideally the same that would be charged to unrelated companies. The aim of the arm's-length method is to allocate taxable income within different jurisdictions, thus avoiding both international double taxation and, most importantly, tax-induced income shifting within multinationals. The pressure points on this rule boil down to the fact that the arm's-length method is extremely difficult to employ when sophisticated transactions occur or in highly integrated businesses: sometimes it is impossible to find cross-border transactions within a multinational that are similar to transactions between unrelated companies because the product that has been exchanged is unique. If there is not a market for a particular product, it is impossible to establish the market value of a transaction. Moreover, the proliferation of transactions involving 'intangibles', R&D, central services and unique products makes the arm's-length method less realistic. Finally, by postulating that enterprises within a trans-national group are separate entities, the method goes against the rationale of a trans-national company. Indeed, a trans-national company is established for the very purpose of dealing with a unitary business.⁴

The OECD is – apart from the EU – the most significant organisation in the area of international tax policy. OECD Secretary-General Donald Johnston states in the 2005 report of the Centre for Tax Policy and Administration: "Taxation policy is a priority for OECD member countries and the OECD plays an important role in this field. Sound taxation policy is necessary in a well functioning market economy, and brings benefits to many aspects of our everyday lives." One of its characteristics is that it mainly develops and promotes international norms rather than binding agreements. It works largely by defining standards of appropriate behaviour for states which seek to identify themselves as modern, liberal, market-friendly, and efficient (March and Olsen 1998: 961), and uses peer review mechanisms to socialise member states into accepting OECD-recommended practices (Webb 2004: 792). This doesn't

³ As noted by Sandler (1994:107) this position explains the US objections to tax sparing provisions in treaties with developing countries.

⁴ For a detailed explanation of these components see Picciotto (1992)

necessarily mean that OECD standards and agreements are weak. Usually states comply with the norms and standards of the OECD (Webb 2001).

Another characteristic of the OECD is the existence of a permanent secretariat that tries to mobilise peer pressure and finding consensus among member states. It consists of a mix of economists, scientists, lawyers and other professionals in Paris servicing the Committees, including the Committee of Fiscal Affairs (CFA). The CFA was established in 1971 to provide a forum for policy makers to discuss international and domestic tax matters. The Committee seeks to eliminate tax measures which distort trade and investment flows, to prevent double taxation, to counteract tax evasion and to promote best practices in tax policy and administration. Chairman Bill McCloskey made it a priority during his chairmanship of the CFA to “strengthen its role in international tax rules, to ensure that there are mechanisms in place to minimise and resolve tax disputes and to intensify our dialogue with non-OECD economies” (OECD 2005: 5). Financial Support is provided by the Centre for Tax Policy and Administration (CTPA). The Centre, directed by Jeffrey Owens, is the focal point for the organisation’s work on taxation – it services the CFA and examines all aspects of taxation apart from macro-fiscal policy which is dealt with by the Economic Policy Committee.

The CFA’s work programme is carried out by a number of subsidiary bodies, consisting mainly of participants from OECD countries. Table 1 gives an overview of OECD groups concerned with tax issues. Liberal economic theory is the dominant framework for all OECD initiatives; so much so that Smythe (1998: 243) called it “a missionary for values of liberalization”.

Table 1 – OECD groups dealing with taxation issues

Working groups	
Working Party 1	Tax Treaties, Tax Conventions and related issues
Working Party 2	Tax policy analysis and statistical work
Working Party 3	Company taxes (wound up after completion of task)
Working Party 4	Taxation of international bond issues (wound up after completion of task)
Working Party 5	Negotiation of securities (wound up after completion of task)
Working Party 6	Taxation of multinational enterprises
Working Party 7	Taxation of energy (wound up after completion of task)
Working party 8	Investigates how member government can cooperate to minimise the extend of tax evasion and avoidance
Working Party 9	Consumption taxes
Fora	
Forum on Harmful Tax Practices	Created in 1998 to take forward the OECD's work on harmful tax practices
Forum on Tax Administration	Created in 2002 to improve taxpayer service and compliance
Recent ad-hoc groups	
Meetings with financial market specialists	Tax treatment of new kinds of financial transactions
Joint group of fiscal and environmental experts	Eco-taxes
Groups with a consulting function	
Business and Industry Advisory Committee (BIAC)	Frequent advise to the CFA
Trade Union Advisory Committee (TUAC)	Frequent advise to the CFA

For a long time, this approach was effective and considered legitimate by governments and the business community. In the 1990s, however, it became clear that the micro-foundations of the approach (principles, instruments, and problems) were no longer up to the job. This triggered a re-orientation of the OECD activity. The approach based on bilateral action informed by OECD guidelines and model conventions was not rejected. Rather, it was supplemented by a shift of gear, from bilateralism to multilateralism, with political implications for non-OECD jurisdictions. Over the last five years the CTPA has widened its dialogue with non-OECD countries: Argentina, Russia and South Africa are now observers in the Committee and there's a regular dialogue with over 70 non-OECD economies. It also sponsors the International Tax Dialogue (ITD), which is a joint initiative with the International Monetary Fund

(IMF), the World Bank, and the United Nations (UN)⁵ to provide a forum for the improvement of international coordination in taxation. The CFA also cooperates with the World Trade Organization (WTO), the Financial Action Task Force, and regional tax organisations (e.g. CIAT⁶, CREDAF, IOTA⁷). Table 2 shows the OECD approach until the mid-90s in contrast to the OECD approach today.

Table 2 - Tax Governance: The OECD approach until mid-1990s and today

	Until mid-90s	today
System of Interaction		
Problem Definition	Elimination of double taxation Allocation of taxing rights among jurisdictions	Harmful tax competition
Instruments	Informal governance tools (Model treaties, guidelines)	More formal tools (peer review, name and shame, defensive measures, timetable for compliance)
Institutions	Working Parties	Working Parties, Global Tax Forum
Actors	Revenue authorities, business community	Revenue authorities, offshore jurisdictions
Outcomes of Tax Governance		
Impact on third countries	None	Yes
Winners	Business community	Revenue Authorities
Level of Politicisation	Low	High

⁵ The United Nations further operate the Ad Hoc Group of Experts on Tax Treaties between Developed and Developing Countries. This group was established in 1968 pursuant to an ECOSOC resolution after considerable efforts made by the League of Nations, the Organization for European Economic Cooperation (later on OECD) and the United Nations. In 1980 this group finalized the UN Model Double Taxation Convention whose aim was to promote the conclusion of treaties between developed and developing countries, acceptable to both parties. In April 1980 the ECOSOC renamed the Group Ad Hoc Group of Experts on International Cooperation in Tax Matters. Members are 25 tax administrators from 10 developed and 15 developing countries. Task of the group is to explore in consultation with interested international agencies ways and means of facilitating the conclusion of tax treaties between developed and developing countries and bearing on international cooperation in tax matters. The group examines among other things transfer pricing, mutual assistance in collection of debts, treaty shopping and treaty abuses, interaction of tax, trade and investment, and capital flight. The group became a standing committee in November 2004 and had its first meeting in December 2005 in Geneva.

⁶ Centro Interamericano de Administraciones Tributarias

⁷ Intra-European Organisation of tax Administrations

III. Widening the Scope of Governance: More Actors and Ambitions, less Acceptance?

In the second half of the 1990s, the OECD launched more ambitious and multilateral plans aimed at cracking down harmful tax practices in member states and in non-OECD jurisdictions.

The landmark report on harmful tax competition (OECD 1998) was a sea-change in terms of problem definition, instruments, and scope of tax governance. For the first time the major problem of international tax coordination was defined in terms of damaging or harmful tax competition. At that point, neither the existence nor the practices of ‘tax havens’ and offshore financial centres were new. But the 1980s and early 1990s had seen an increasing fear among governments of losing revenue and having capital escaping to low tax jurisdictions. The success of Ireland’s 12.5% corporate tax rate, flat tax systems in Estonia, Slovakia and Russia and tax advantageous regimes in Luxembourg, Belgium and the Netherlands caused some of the bigger EU states, such as Germany and France, to push harmful tax competition parallel to the EU on the OECD agenda⁸. At the G7 summit in Lyon in June 1996 the heads of government declared: “Finally, globalization is creating new challenges in the field of tax policy. Tax schemes aimed at attracting financial and other geographically mobile activities can create harmful tax competition between states, carrying risks of distorting trade and investment and could lead to the erosion of national tax bases. We strongly urge the OECD to vigorously pursue its work in this field, aimed at establishing a multilateral approach under which countries could operate individually and collectively to limit the extent of these practices. We will follow closely the progress on work by the OECD, which is due to produce a report by 1998. We will also follow closely the OECD’s continuation of its important work on transfer pricing, where we warmly endorse the significant progress that the OECD has already achieved.”⁹. Thus the OECD created a task force in 1997 to look into the newly defined problem. The result was the 1998 report, adopted by the CFA in January and by the ministers on 28 April 1998. This report was an exercise in political creativity rather than a case of usage of ideas developed by economists. Economists are familiar with tax competition, and have discussed the conditions under which coordination improves collective welfare. But the identification of ‘harmful’ tax competition goes beyond the prescriptions of economics¹⁰. Instead, in the 1998

⁸ All 15 old and 4 of the new EU Member States are also members of the OECD. The EU state aid rules also apply to the European Economic Area (Iceland and Norway are also EU members). Therefore the developments on the EU level are particularly important for the OECD campaign. With the Verona Paper in April 1996 the EU started as well to engage in the debate about harmful tax competition. The code of conduct on business taxation also established criteria for determining whether a tax regime falls within its scope or not. These criteria are very similar to the OECD’s 1998 report. A number of regimes listed by the code of conduct Group do not appear on the OECD list: The OECD list does not contain holding company regimes, nor does it include measures for substantial activities. Apart from that almost all EU measures listed by the OECD are also on the code of conduct list. Differences between the EU tax package and the OECD initiative resulted mainly out of the exemptions made for three EU member countries (Belgium, Austria and Luxembourg) under the EU savings directive. They are allowed to introduce a withholding tax instead of joining the exchange of information system. This led to considerable critique from media, experts, and the OECD (see D4).

For a detailed analysis of EU tax policy development see D4. For detailed comparisons see Osterweil 1999 and Pinto 2003.

⁹ Economic Communiqué: Making a success of globalization for the benefit of all, Lyon G7 summit, 28 June 1996, paragraph 16

¹⁰ For a review of international tax competition see Wilson and Wildasin (2003) and Zodrow (2003).

report the OECD achieved consensus on a set of specific criteria to be used to test for the presence or absence of tax competition.

The Paris-based organisation defined classical tax havens (see Box 1), preferential regimes (see Box 2), and normal tax regimes (regimes that collect significant revenues from individual and corporate income taxes, but at relatively low effective rates), and mentions damaging tax competition, and other concepts. Tax policy coordination was thus provided with new concepts and new vocabulary.

Box 1: OECD Tax Haven Criteria

Four key factors are used to determine whether a jurisdiction is a tax haven. The first is that the jurisdiction **imposes no or only nominal taxes**. The no or nominal tax criterion is not sufficient, by itself, to result in characterisation as a tax haven. The OECD recognises that every jurisdiction has a right to determine whether to impose direct taxes and, if so, to determine the appropriate tax rate. An analysis of the other key factors is needed for a jurisdiction to be considered a tax haven. The three other factors to be considered are:

- Whether there is a **lack of transparency**
- Whether there are **laws or administrative practices that prevent the effective exchange of information** for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation.
- Whether there is an **absence of a requirement that the activity be substantial**

Transparency ensures that there is an open and consistent application of tax laws among similarly situated taxpayers and that information needed by tax authorities to determine a taxpayer's correct tax liability is available (e.g., accounting records and underlying documentation).

With regard to exchange of information in tax matters, the OECD encourages countries to adopt information exchange on an "upon request" basis. Exchange of information upon request describes a situation where a competent authority of one country asks the competent authority of another country for specific information in connection with a specific tax inquiry, generally under the authority of a bilateral exchange arrangement between the two countries. An essential element of exchange of information is the implementation of appropriate safeguards to ensure adequate protection of taxpayers' rights and the confidentiality of their tax affairs.

The no substantial activities criterion was included in the 1998 Report as a criterion for identifying tax havens because the lack of such activities suggests that a jurisdiction may be attempting to attract investment and transactions that are purely tax driven. In 2001, the OECD's Committee on Fiscal Affairs agreed that this criterion would not be used to determine whether a tax haven was co-operative or uncooperative.

Source: www.oecd.org

Box 2: OECD Preferential Regime Criteria

Four main factors are used to determine if a preferential tax regime is harmful:

- The regime imposes low or no taxes on the relevant income (from geographically mobile financial and other service activities). Although a low or zero effective tax rate is the necessary starting point of an examination of a preferential regime, it alone is never sufficient to find harmfulness. The OECD recognises each country's right to determine its own tax rate.
- The regime lacks transparency;
- There is no effective exchange of information with respect to the regime;
- The regime is ring-fenced from the domestic economy.

Transparency ensures that there is an open and consistent application of tax laws among similarly situated taxpayers and that information needed by tax authorities to determine a taxpayer's correct tax liability is available (e.g., accounting records and underlying documentation).

With regard to exchange of information in tax matters, the OECD encourages countries to adopt information exchange on an "upon request" basis. Exchange of information upon request describes a situation where a competent authority of one country asks the competent authority of another country for specific information in relation to a specific inquiry, generally under the authority of a bilateral exchange arrangement between the two countries. An essential element of exchange of information is the implementation of appropriate safeguards to ensure adequate protection of taxpayers' rights and the confidentiality of their tax affairs.

A regime is ring-fenced if a country insulates its core tax base from the effects of providing the preference. For example, if a country offering a preferential tax regime denies that regime to resident taxpayers or domestic activities, it means that it is not willing to bear the cost in lost revenues with respect to its own tax system.

There are also a number of other factors to be considered in evaluating whether a preferential tax regime might be harmful, including the extent of compliance with the OECD Transfer Pricing Guidelines. Any evaluation requires an overall assessment of each of the above factors and once a regime has been identified as potentially harmful the economic effects would, where necessary, have to be examined.

Source: www.oecd.org

The report issued a number of multilaterally orientated recommendations and some guidelines "for dealing with harmful preferential tax regimes in member states". The recommendations included among others greater access to banking information for tax authorities, greater use of exchange of information, the establishment of a Forum on Harmful Tax Practices to implement the guidelines and recommendations, the creation of a list of tax havens and the engagement in dialogue with non-members. The guidelines for member states consisted mainly of proposals for peer review, stand-still and roll-back of preferential tax regimes in member states.

The scope of tax governance was changed. The campaign against harmful tax competition enabled the OECD to engage with multilateral coordination. But it was the first time that multilateralism became so prominent. The scope of governance went further than the OECD itself, by affecting non-OECD members.

A substantial blow to the impact of the 1998 report came from the abstention of Switzerland and Luxembourg. Both countries accepted that tax competition can be harmful but refused to agree with the report on the grounds of regarding it partial, unbalanced and aiming at the

abolishment of bank secrecy rather than cracking down on harmful tax competition. Switzerland even considered to veto the report but eventually decided to abstain so as not to prevent other members from adopting it.

The 1998 report demanded the creation of two lists: a list of the potentially harmful measures in the OECD member states themselves and a list of tax havens. Both lists were presented in the 2000 Progress Report ‘Towards Global Tax Co-Operation’. The Forum on Harmful Tax Practices identified 47 preferential tax regimes in member states as potentially harmful. These regimes should be eliminated by April 2003. The second list was a list of 35 non-member tax havens¹¹.

At this stage tax governance was hardened in that jurisdictions unwilling to sign the Memorandum of Understanding¹² were threatened with possible defensive measures. Surprisingly for the OECD a considerable number of offshore jurisdictions showed interest in cooperation and more dialogue with the OECD in order to have objective criteria and a fair process. This was unexpected for the OECD but the organisation quickly changed its strategy. In its effort to collect a high number of signatures to its Memorandum of Understanding, the new motto became: “We want a list without any names on it”¹³.

An important step was taken by the so-called ‘new global tax forum’ created at a meeting hosted by Barbados in early January 2001, which led to the separation between cooperative and un-cooperative regimes. Only jurisdictions placed on the uncooperative list would be subject to defensive measures after 31 July 2001. These defensive measures included among others not to enter into any comprehensive income tax conventions with uncooperative tax havens (UTHs), to consider terminating existing ones, to impose charges on transactions involving UTHs, to ensure that domestic defensive measures are also applicable to transactions with UTHs, to impose withholding tax on some payments to residents of UTHs, etc. On the other side there were offers for cooperative regimes to assist in restructuring their economies and strengthening their tax administrations.

However, the 2001 progress report stated two major changes to the project on harmful tax practices. The first one was the strengthened dialogue with non-OECD-members and the increasing importance of the tax partnership programme that explicitly promoted cooperation with non-members. The second major change was the amount of contestation the OECD had to face.

The debate especially in the US and the tax havens soon became political. When the Bush administration changed the US Treasury Secretary and Paul O’Neill took over from Larry Summers, the American support for the OECD campaign declined. In May 2001 O’Neill

¹¹ These were Andorra, Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Bahrain, Barbados, Belize, the British Virgin Islands, the Cook Islands, Dominica, Gibraltar, Grenada, Guernsey (including Alderney and Sark), the Isle of man, Jersey, Liberia, Liechtenstein, the Maldives, the Marshall Islands, Monaco, Montserrat, Nauru, the Netherlands Antilles, Niue, Panama, Samoa, the Seychelles, St. Lucia, St. Christopher and Nevis, St. Vincent and the Grenadines, Tonga, Turks and Caicos, The US Virgin Islands, and Vanuatu. Examined and omitted from the list were Brunei, Costa Rica, Dubai, Jamaica, Macao and Tuvalu. A further six jurisdictions avoided being listed by committing to the principles of the 1998 report and to eliminate their preferential tax regimes by the end of 2005. These were Bermuda, the Cayman Islands, Cyprus, Malta, Mauritius, and San Marino.

¹² To sign the memorandum of understanding meant to commit to the above mentioned principles of the 1998 report.

¹³ Expert interview with high-level OECD officials on 19 April 2005

wrote an op-ed in the *Washington Times*¹⁴ questioning the punitive intent of the OECD and the idea of ‘stifling competition which forces governments, like businesses, to create efficiencies’. The op-ed was accompanied by a private letter to the OECD. This was the first time that the OECD project was discussed outside the technical framework of working groups of revenue authorities and specialists conferences. The tone of the article was aggressive and explicitly political. The reaction of offshore jurisdictions was also vocal and political. Most of the technical points made by the OECD report about the difference between desirable and harmful competition were ignored. So was the fact that the OECD report did not argue for any initiative on tax rate coordination. The public attack on the OECD revolved around the notion that the OECD was against low tax rates and that the organisation had no legitimacy to act as the ‘tax policy of the world’.

Offshore jurisdictions and some parts of business soon found their advocates in the media and Congress. A right-wing lobbying organisation, The Center for Freedom and Prosperity (CFP), was established with anonymous funding. Its members visited offshore jurisdictions and started lobbying against the OECD in Washington¹⁵.

Some US American politicians criticised the OECD to focus on the wrong problem and to use instruments which may violate WTO obligations. In September 2000, the House majority leader Richard Armev wrote a letter to then US Treasury Secretary, Lawrence Summers, in which the OECD was portrayed as a ‘tax cartel’. On 3 January 2001, US representative Sam Johnson, a Republican from Texas, wrote to the OECD Secretary General making the point that the OECD is focusing on the wrong problem and is using instruments which may violate WTO obligations (the reference is to sanctions that OECD members should use against uncooperative jurisdictions after July 2001). In March 2001, Armev wrote a second letter, this time posted to the then US Treasury Secretary, Paul O’Neill, describing the OECD project as ‘a global tax cartel for the benefit of a small handful of high-tax nations’. He argued that the OECD initiative is ‘fatally flawed and contrary to America’s interests’¹⁶.

A trio of US legislators, among them the chair of the Foreign Affairs Committee at the US Senate (Jesse Helms), criticised openly the OECD in their separate letters to the US Treasury¹⁷. US Senator Don Nickles, a Republican assistant majority leader of the Senate, used his influential position to argue in yet another letter to O’Neill that the ‘financial protectionism of OECD nations’ is ‘contrary to America’s economic interests’ because tax competition ‘keeps politicians in check and enhances economic growth’¹⁸. And a Democrat from the Virgin Islands (and Congressional black caucus member), Delegate Donna M. Christensen, stepped up pressure on O’Neill with her 12 March 2001 letter in which she argues that the ‘OECD should not have the right to rewrite the rules of international commerce on taxation simply because they are upset that investors and entrepreneurs are seeking higher after-tax returns’¹⁹.

¹⁴ Pail O’Neill, *Confronting OECD’s notions on taxation*, *Washington Times*, May 10, 2001.

¹⁵ R. Goulder, ‘New coalition strikes back at OECD tax haven campaign’ *Tax Notes International*, 11 December 2000: 2650-2654.

¹⁶ C. Scott, ‘House Majority leader, Congressional black caucus member join growing list of US lawmakers opposed to OECD tax haven campaign’ *Tax Notes International*, 26 March 2001: 1479-1480.

¹⁷ R. Goulder, ‘Trio of US legislators question OECD tax haven initiative’, *Tax Notes International*, 19 March 2001: 1339-1340.

¹⁸ R. Goulder, ‘US Senator questions OECD policy on tax competition’ *Tax Notes International*, 26 February 2001: 944-945.

¹⁹ C. Scott, ‘House Majority leader, Congressional black caucus member join growing list of US lawmakers opposed to OECD tax haven campaign’ *Tax Notes International*, 26 March 2001: 1479-1480.

Others like tax attorney Marshall Langer criticised the OECD countries as a whole but especially the United States for having forced some of the tax havens to adopt tax practices that the OECD was now calling into question²⁰. None of this produced the withdrawal of US support to the OECD campaign, but it made it more qualified.

The OECD reacted by promoting more dialogue with offshore jurisdictions and by insisting on exchange of information as the final objective of the campaign, capitalising on the issue linkage between tax transparency, money laundering, bank secrecy, and security which has characterised the post 9-11 environment. However, they compromised on the following points: a) the deadline for making a commitment to cooperate was put back from 31 July 2001 to 28 February 2002, b) coordinated defensive measures would not apply to UTHs any earlier than to OECD member countries, and c) the ‘no substantial activity’ criterion no longer determined whether a jurisdiction is considered to be a UTH. Now the OECD considers jurisdictions to be cooperative if they commit to the international standards of transparency and effective exchange of information upon request.

When the 2004 Progress report was released on 4 February 2004 there were only 5 uncooperative tax havens left on the list. Box 3 gives an overview on the originally listed tax havens and the date of signing the Memorandum of Understanding.

²⁰ S. Kirkell, ‘OECD: 2002 Year in Review’, *Tax Notes International*, 30 December 2002: 1316-1318.

Box 3: Tax Havens committing to the OECD principles

Original list of tax havens	Date of commitment
Bermuda	Prior to 2000 progress report
Cayman Islands	Prior to 2000 progress report
Cyprus	Prior to 2000 progress report
Malta	Prior to 2000 progress report
Mauritius	Prior to 2000 progress report
San Marino	Prior to 2000 progress report
Aruba	Prior to 2000 progress report
Bahrain	Prior to 2000 progress report
Isle of Man	Prior to 2000 progress report
Netherland Antilles	Prior to 2000 progress report
Seychelles	Prior to 2000 progress report
2000 Progress report - released on 26 June 2000	
Antigua and Barbuda	20 February 2001
Guernsey	27 February 2001
Jersey	27 February 2001
Grenada	27 February 2001
St. Vincent and the Grenadines	27 February 2001
Deadline to commit: 28 February 2002	
Dominica	5 March 2001
St. Christopher and Nevis	5 March 2001
St. Lucia	5 March 2001
Montserrat	7 March 2001
Anguilla	8 March 2001
Turks and Caicos	8 March 2001
US Virgin Islands	11 March 2001
Gibraltar	14 March 2001
Bahamas	18 March 2001
Belize	20 March 2001
Cook Islands	27 March 2001
British Virgin Islands	3 April 2001
Samoa	18 April 2001
Publication of the revised list on 18 April 2002	
Vanuatu	20 May 2001
Nauru	12 December 2001
2004 Progress Report – released on 4 February 2004	
Andorra	Accepts invitation to participate in the Global Forum on transparency and exchange of information on 9 February 2005, but no commitment to the OECD principles on harmful tax practices yet
Liechtenstein	No commitment
Liberia	No commitment
Monaco	No commitment
Marshall Islands	No commitment

The 2004 progress report still provoked hostile reactions from organisations like the CFP:

‘The OECD made two commitments to low-tax jurisdictions. First, it promised that it would achieve a "level playing field." This promise has been broken. Second, it committed to the even-handed application of sanctions against nations and territories with free market tax policy. This "uniform consequences" promise also has been broken. Low tax jurisdictions should be outraged by the OECD's deceitful actions’²¹.

Already in October 2003, Antigua and Barbuda had announced that it was withdrawing its commitment and Prime Minister Lester Bird called on other Caribbean nations to follow his lead at a meeting of the Caribbean Financial Action Task Force in Trinidad²². The main point of the complaint was the lack of a level-playing field: OECD member countries were not held to the same standards as non-member tax havens. From the 47 potentially harmful measures identified by the 2000 Progress Report just 18 regimes were abolished or in the process of being abolished by the time of the 2004 Progress report. 14 regimes had been amended to remove any potentially harmful features, and 13 were found not to be harmful. Two regimes (Switzerland’s administrative company regime and Luxembourg’s 1929 Holding company regime) are still discussed.

However, the dialogue with offshore jurisdictions is a reality, under the aegis of the OECD Global Tax Forum. The Global Forum on Taxation was developed as one of eight Global Forums by the OECD’s Committee for Co-operation with Non-members (CCN) in 2000. It is one of the two main pillars of the work with non-members the other being country and regional programmes. The Global Forum on Taxation builds on the Expertise of the CFA, the interaction of non-OECD economies and members and tries to incorporate some of the criticism the OECD had to face. At the Global Forum in Berlin in June 2004 the OECD introduced the definition of a global level playing field (see Box 4).

²¹ D. Mitchell, ‘The OECD’s Dishonest Campaign Against Tax Competition: A Regress Report’, www.freedomandprosperity.org

²² Scott, C. 2003, Two Tax Havens Suspend Commitment Letters to OECD, Tax Notes International, 20 October, p.203

Box 4: The definition of a Global Level Playing Field**A) Concept**

The level playing field is fundamentally about fairness to which all parties in the Global Forum are committed.

In the context of exchange of information achieving a level playing field means the convergence of existing practices to the same high standards for effective exchange of information on both criminal and civil taxation matters within an acceptable timeline for implementation with the aim of achieving equity and fair competition.

B) Features

Will provide for i) inclusive process, ii) mutual benefits through bilateral implementation, iii) a consistent and rigorous approach to any failure to implement, iv) review and verification mechanisms, v) the standard and the timeline.

C) Role

The level playing field serves as a goal.

Achieving a level playing field in respect of exchange of information requires that all jurisdictions, OECD and non-OECD members, should act in a manner consistent with the concept in their bilateral relationships and more broadly.

Source: OECD, 2004, A Process for Achieving a Global Level Playing Field, Global Forum on Taxation, Berlin, 3-4 June, p. 2ff

The last meeting took place in November 2005 in Melbourne where government officials from 55 OECD and non-OECD countries met for discussions on what is needed for a ‘global playing field’ in the areas of transparency and effective exchange of information in tax matters. The concluding remarks state:

“The underlying objective of the global level playing field is to facilitate the creation of an environment in which all significant financial centres meet the high standards of transparency and effective exchange of information on both criminal and civil taxation matters. This is vital to ensuring that countries can obtain from other countries the information necessary to enforce their own tax laws, to ensuring that financial centres that meet such standards are not unduly disadvantaged by doing so, and to ensuring that financial centres that meet such high standards are and remain fully integrated into the international financial system and the global community. Any significant financial centre that decides not to adopt high standards of transparency and effective exchange of information must not be permitted to profit from that decision.

Individual, bilateral, and collective actions in combination are necessary for the achievement of the common objective of the global level playing field: an international financial system characterised by fair competition, and which is free of the distortions created through lack of transparency and lack of effective exchange of information.”²³

²³ OECD, Progress Towards a Level Playing Field: Outcomes of the OECD Global Forum on Taxation, Melbourne, 15-16 November 2005

The degree of politicisation has increased for yet another reason, that is, the activity of NGOs on taxation. Charities such as War on Want²⁴ have campaigned on tax issues like the Tobin tax since 1998. The Tobin Tax Network²⁵ was set up in 2000, after ECOFIN voted against a European Tobin Tax. In 2000 the charity Oxfam published a report on tax havens, capital flights, and poverty (Oxfam 2000). The anti-globalisation organisation Attac²⁶ and the Tax Justice Network are fighting against tax havens. The advent of NGOs has raised new moral issues in the discussion of tax avoidance. Newspapers have been sent ‘tax stories’ about scandals, poverty and capital flight, major abuse of transfer pricing legislation, figures on the amount of tax revenue ‘lost’ in tax havens. Although Tax Justice Network is a small organisation, its media campaigns have been carefully planned, with figures on tax avoidance released on Easter Sunday, when Bishops in the UK speak about global fairness.

The United Nations has revived its ad-hoc group of experts on international taxation and tax matters, now called the Committee of Experts on International Cooperation in Tax Matters, and NGOs have been invited to attend²⁷.

To conclude, the OECD campaign shows some important changes in patterns of tax governance. First, there is a shift towards harder forms of governance. The new campaign has moved along the continuum towards harder forms: it contains defensive measures, it is explicitly multi-lateral, and covers jurisdictions outside the OECD. The diffusion process is not based on the adoption of instruments that suit a government’s preference, nor is it based on the intrinsic efficiency of the model. Instead, it is based on a mechanism of sanctions and a certain degree of coercion. Although the recent changes also show the importance of learning processes, there is no doubt that the mode of governance contains more formal features than in the past. The social legitimacy of OECD policy and, occasionally, of the OECD itself, has been contested by some actors and the discussion has become more political.

IV. Explaining Shifting Modes

The claims presented in the previous Sections have to be explained. Specifically, two questions arise from our discussion of shifting modes of governance:

1. Why does the OECD move towards more ambitious modes of governance?
2. Why does governance switch from technocratic to political?

We answer the questions in reverse order. The politicisation of international tax policy is explained by the emergence of a new focal point. Following Blyth (2002), Steinmo (2003), and drawing on our previous work on the role of knowledge in politics (Radaelli 1995), we acknowledge that ideas about taxation and interests (of revenue authorities and the business community) are interrelated²⁸. Within this approach to ideational politics, Steinmo (2003) has discussed the evolution of ideas about taxation in the 20th century. His account of changing paradigms in tax policy terminates with the advent and institutionalisation of the paradigm according to which tax policy should promote the efficient allocation of resources (as opposed

²⁴ For more information about War on Want see www.waronwant.org

²⁵ For a position paper by the Tobin Tax Network on the International Financial Facility see <http://www.globalpolicy.org/soecon/develop/oda/2003/09iff.htm>

²⁶ For more information about Attac see www.attac.org

²⁷ B. Zagaris, The United Nation’s role in international tax cooperation, *Tax Notes International*, April 25, 2005.

²⁸ For an analysis of the problems that this interrelation creates see Hay (2004).

to a paradigm oriented towards equity and ‘ability to pay’). This ideational turn was consistent with the interests of an increasingly mobile capital and the economics of open markets.

However, Steinmo’s account can be usefully completed with the changing economic ideas in the last decade of the 20th century. This is the period in which tax policy-makers became aware of some un-desirable consequences of unbridled competition in tax matters, especially in terms of the deterioration of tax systems and revenue losses. In a (evolutionary) sense, tax policy-makers were discovering the limits and international efficiencies (in open economies and at the global level) of what looked sensible at the purely domestic level: to tweak tax systems in order to attract capital from abroad without losing the domestic revenue base.

These material preoccupations were reflected in the emerging narrative of harmful tax competition – ‘the’ emerging narrative of international tax policy in the 1990s. As shown in another article (Radaelli 1999), this narrative is more than the reflection of the interest of revenue authorities. It is also the product of ideational entrepreneurs like the European Commission (and in the OECD the Committee for Fiscal Affairs). Faced with the substantial neglect of proposals for tax policy coordination, these entrepreneurs successfully promoted a more political discussion of international taxation by shedding light on the harmful consequences (not only for the revenue coffers, but for the welfare state and employment as well) of some wicked types of tax competition.

Rapidly, harmful tax competition became a dominant discourse in international tax policy circles. As mentioned, this discourse is more political than the discourse on tax efficiency. It brings in considerations of fairness in the tax world, moral considerations about tax justice and un-justice, norms of behaviour according to which the actions of offshore jurisdictions should be assessed, North-South imbalances and distortions induced by tax-generated capital flights from Africa and Latin America. This more political discourse has gone further than re-kindling cooperation among revenue authorities at the OECD and in the EU. It has also wetted the political appetite of tax NGOs like Tax Justice Network, that see this as an opportunity to transform international taxation into the new environmental politics (in terms of political mobilisation of citizens)²⁹. Further, harmful tax competition has brought into the debate the thorny political question of the relationship between offshore jurisdictions and the OECD members, and, within the business community, the issue of the legitimate uses of tax havens for socially responsible corporations. The whole notion of the public interest in international taxation is gradually emerging in tax policy discussions, with potentially huge implications about the range of actors involved and the issues to be addressed. To conclude on this point, our answer to the second question is that the emergence and institutionalisation (in the EU and the OECD) of the narrative of harmful tax competition (in turn linked to interest politics) has widened the range of actors and policy issues, and has made technocratic approaches obsolete, at least for the time being.

Let us go back to the first question. How can one explain the OECD’s selection of governance modes? Three mutually reinforcing factors were at work. First, the narrative of harmful tax competition was grounded in real preoccupations of the revenue authorities, increasingly frustrated by the difficulty to tax their own residents via traditional instruments. It should be considered that the Committee for Fiscal Affairs of the OECD is eminently a committee of revenue authorities. Second, and in connection with the previous point, due to technological innovation and financial sophistication, the marginal returns of uni-lateral (i.e., controlled foreign company legislation) and bi-lateral solutions to tax avoidance and tax evasion decreased

²⁹ Houlder, V. The tax avoidance story as a morality tale, *Financial Times*, 22 November 2004.

quickly between 1980 and the 1990s – a point illustrated by Hugh Ault (2002). The OECD multi-lateral action should not be seen as an alternative to uni-lateral and bi-lateral initiatives, but as a much needed complement to increasingly limited instruments (OECD 1998: 42). In consequence, the choice of the OECD was one of widening the menu of instruments available rather than drastic re-direction. Third, in the late 1980s and the 1990s tax policy problems showed their connection with another bundle of policy problems, emanating from money laundering, security, political corruption, and lack of transparency in international economic transactions. The bundling of taxation with other and more political salient problems made the harder and more ambitious approach suggested by the OECD possible.

V. Conclusions

In this final Section, we go back to the initial questions and provide our answers. The first point was to trace the emergence of harmful tax competition as ideational focal point in international taxation. We answer this question by relating the ideational components of international taxation (and specifically the emergence of policy narratives about harmful tax competition) to the material preoccupations of revenue authorities. We have also noted that the focal point provided by harmful tax competition has its own impact. For a start, it has generated a more political discourse. In turn, this shift in discourse has made political leaders more alert to the problems arising out of unbridled tax competition – with of course a big difference in terms of propensity to cooperate between winners and losers from tax competition. But it has also put taxation on the radar of NGOs like the Tax Justice Network. The latter sees this as an opportunity to transform international taxation into a vehicle for social mobilisation and a new debate on international justice and fairness. Further, harmful tax competition has made explicit the hard questions surrounding the relationship between offshore jurisdictions and the OECD members. Looking inside the business community, the issue of the uses of offshore finance has implications for the socially responsible corporations. An embryonic notion of the public interest in international taxation is gradually emerging. To conclude on this first point, we have shown the many ways in which ideas matter and produce policy development. This is our contribution to an otherwise sterile debate about whether ideas matter or not in politics. We think it is more important to show empirically the ways in which ideas impact on policy.

Our second and third questions were about the scope of governance both in a technical sense (formal versus informal governance) and in the more general sense of the overall orientation of the discussion – more technical or more political.

We have argued that informal governance is ‘old’ governance as far as direct taxation is concerned. Informal modes were already used by the League of Nations and then institutionalised by the OECD with the model treaty convention and guidelines for transfer pricing between the 1960s and the 1980s. OECD-promoted governance is less informal and more ambitious than in the past. The impact of tax policy formulated within the OECD has reached out to third countries and tax havens. The business community has less impact than in the past on policy formulation. Non-governmental groups are, broadly speaking, still outside the radar, but occasionally they make their presence more visible. Opaque organisations such as the Centre for Freedom and Prosperity have made the attack on the OECD political and visible to policy-makers in the US Congress. Political movements such as War on Want, Attac or Oxfam have limited influence on the development of international direct taxation. However, the foundation of the Tax Justice Network in 2001, its increasing media presence (especially in the UK and Switzerland), and its efforts to influence national and international agenda-setting can be seen as an indicator that the debate has not only become politicised but also entered the territory of ethical issues.

So, is international tax governance more contested now than 80 years ago? Legitimacy and contestation – we have argued – lead to a wild goose chase. The question is not that international tax governance has less legitimacy than in the past. The real question has something to do with the scope of governance and the range of actors involved therein. The wider the scope and the range of actors targeted by informal governance, the higher the potential for more political discussions – and political discussion is often conflictual. Conflict, in turn, may lead some actors to argue that the other is not legitimate enough to impose its preferences on policy.

We have then looked into the issue of ‘legitimacy for whom’ to dissipate ambiguities about this term. The old world of international taxation was dealing with low political salience issues. It was limited in scope. The OECD operated like a forum for the elaboration of instruments to be voluntarily adopted by the members. International tax governance was eminently bilateral. International tax policy was not contested because that world was somewhat insulated from wider political debates and the scope of governance limited. There was high acceptance within networks of specialists and revenue officers.

By contrast, the new world is one where tax debates are more political than in the past. The scope of governance has widened, with the OECD (but also the United Nations and the G7-G8 Ministers) engaged in multilateral policy. For the OECD, the structural properties of tax coordination – notably, the fact that coordination is fragile if achieved only by a limited number of countries – have pushed towards an ambitious attempt to promote the level-playing field outside its jurisdiction. The emphasis on harmful tax competition has made tax issues more prominent in the political agenda, but has also raised the political awareness of a multitude of actors. Corporations want to know more about discussions on tax regimes where there is a lot of corporate money invested. National parliaments do not provide any major input in the discussion about the roll-back of tax regimes. NGOs and radical political organisations from the left and the right try to influence the agenda – so far maybe with limited success, but they have access to the media and may soon get on the radar.

Overall, the process is not one of lower degrees of legitimacy over the long run, but one of politicisation of the debate. Politics has brought more fundamental discussions about the competences of actors into the previously insulated world on international taxation. Hot discussions about “legitimacy” – we submit – are an indicator of the maturation of the debate.

Clearly, there have been some achievements – our last question. There has been a process of learning. The OECD has learned that blacklisting and sanctions are less important than establishing a process by which offshore jurisdictions take commitments to transparency and discuss the scope for exchange of information upon request. The number of uncooperative tax havens went down from 33 to 5. Additionally, tax havens have learned the advantages of transparent tax competition. There is still the exception of major financial centres like Singapore, which are still outside the framework of the Global Tax Forum,³⁰ preventing the establishment of a true global level playing field and raising the anger of those who have committed themselves to the principles of the OECD. But in turn this will create additional pressure to join the vast majority of the jurisdictions that have agreed to the level-playing field.

Arguably, and at a more general level, a more political discussion of international taxation is the best way to forge the notion of public interest in this policy area – a notion that so far has

³⁰ China Hong Kong and China Macao have recently decided to join in.

been hinted only in textbooks of public economics but has not been taken seriously by tax policy-makers.³¹

Another dimension on which achievement should be measured is process. Several processes of dialogue, coordination, and exchange of information have been created since the mid-1990s. The OECD has been the most active player in this area, with initiatives such as the memorandum of understanding and the Global Tax Forum. Future work should look at how other organisations (such as the UN, IMF, the World Bank, and the WTO) are creating clubs for coordination and whether the overall web of clubs and initiatives is efficient.

Finally, it is too early to talk about outcomes in terms of the overall degree of tax competition. Indeed, the whole issue here is not to increase or decrease the level of tax competition. The goal is about limiting some forms of undesirable tax competition. The level-playing field advocated by the OECD is not about setting floors to tax rates or harmonising tax policy. The final outcome should not be measured on the degree of tax competition. There may be more or less tax competition as a result of the OECD campaign. Indeed, there is evidence of more tax competition. But the quality of tax competition is changing, from opaque, non-transparent, often unlawful tax competition to a more transparent process in which governments legitimately select their tax policies in order to achieve economic and social goals. The challenge for the future is whether commitment to the memorandum of understanding and to the principles of transparency will also produce concrete action.

³¹ We wish to mention that we ran an international workshop with tax policy-makers and stakeholders on the topic of the public interest in international taxation at the University of Exeter in February 2006. See http://www.eu-newgov.org/datalists/deliverables_detail.asp?Project_ID=22

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