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Daniel W. Blum

Normativity in International Tax Law

A Legal Theoretical Inquiry into Contemporary International Tax Discourse

25

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Tax Law and Policy Series

Normativity in International Tax Law

Why this book?

The set of rules applicable to cross-border situations found in both tax treaties and domestic tax law has, in recent years – and in an unprecedented manner – been the object of political, academic and legislative scrutiny. At the core of this global tax policy debate lies the ubiquitous claim that the current allocation of taxing rights between jurisdictions is "outdated", "inappropriate" and "conceptually flawed". Originally designed to be applied to a "brick and mortar" economy, digitalization – the dominant narrative – has rendered the system's reliance on physical criteria for allocating taxing rights meaningless. In response, the ongoing debate has produced a variety of reform proposals intended to overcome the shortcomings of the status quo.

Although the real-life changes accorded with digitalization are undisputed, the question remains as to why such change requires reforming the rules of international tax law. Looking at why reform is seen as inevitable, the book identifies three lines of argumentation on which essentially all reform proposals are based. Accordingly, substantial change is found to be a demand of fairness and economic efficiency. Moreover, the discourse is characterized by the recurring assumption that taxation requires justification.

Why, however, these claims carry any normative weight, i.e. why international tax law should be fair and efficient and why taxation requires justification, remains unanswered. Instead, their normative value and, hence, potential legal relevance is assumed, leading to the core hypothesis of this book, according to which the international tax discourse is characterized by a lack of consensus and transparency concerning the understanding of normativity employed in formulating arguments therein. By revisiting the key claims made in the debate from a legal theory perspective, the book situates them within the legal theoretical spectrum ranging from Kelsian/Hartian positivism to Dworkinian interpretivism and analyses the explanatory value of legal theory in establishing their legal validity.

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Visitors' address:
Rietlandpark 301
1019 DW Amsterdam
The Netherlands

Postal address:
P.O. Box 20237
1000 HE Amsterdam
The Netherlands

Telephone: 31-20-554 0100
Email: info@ibfd.org
www.ibfd.org

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Preface

This book is based on my habilitation thesis, which was submitted to the Vienna University of Economics and Business in March 2021, and is the result of a post-doctoral research project conducted between 2016 and 2020 at the Institute for Austrian and International Tax Law at WU Vienna. I would like to express my sincere gratitude to the FWF Wissenschaftsfonds (FWF Einzelprojekt P 28786) and the Heinrich Graf Hardegg'sche Stiftung for supporting the project and providing the necessary funding for its completion. Moreover, I would like to wholeheartedly thank the professors of the Institute, Prof. Michael Lang, Prof. Claus Staringer, Prof. Alexander Rust, Prof. Josef Schuch, Prof. Georg Kofler and Prof. Karoline Spies, for their great support and encouragement, without which this project would not have been possible. They have created a unique academic institution that provides the necessary institutional and personal support to promote and foster the success of projects such as this. The very first step in this project, however, was in 2015, when Prof. Walter Hellerstein, University of Athens, GA, and Prof. Yariv Brauner, University of Florida Gainesville, FL, were so kind as to host me during a research stay at each of their universities. I am very grateful to both of them for their generous support. In addition, I would like to thank Prof. Fadi Shaheen, Rutgers University, NJ, for fruitful discussions and personal encouragement throughout the process, as well as for inviting me to present interim findings at the Rutgers Law Policy Colloquium in September 2019. I also owe sincere thanks to the Global Hauser Law Program at NYU School of Law, which generously supported my studies at NYU during the completion of an LL.M. in International Tax at NYU in 2017 as a Global Hauser Scholar. Moreover, I would like to thank DDr Patrick Weninger, Deloitte Vienna, for being so understanding and giving me the necessary time to finalize the project while working in private practice. Finally, I would like to thank Kristof Misic, BSc, for his valuable support in editing the footnotes of this manuscript.

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during pandemic-induced lockdowns, necessitating my wife to take care of our son in order to allow me to pursue my academic work. Special thanks also go to my dear friend, Dr Peter N. Csoklich, who provided the most valuable moral support in times of great doubt.

Vienna, October 2022

Chapter 1

Normativity in International Tax Law: Setting the Scene

1.1. The importance of legal theory in the field of international tax law

1.1.1. Starting point, or the question "why"

The set of rules applicable to cross-border situations found both in treaty and domestic tax law has, in recent years – in an unprecedented manner – been the object of political, academic and legislative scrutiny.[1] At the core of this global tax policy debate lies the ubiquitous claim that the current allocation of taxing rights between jurisdictions is "outdated", "inappropriate" or "conceptually flawed". Originally designed to be applied to a "brick-and-mortar" economy, digitalization – so the dominant narrative goes – has rendered the system's reliance on physical criteria for allocating taxing rights meaningless.[2] In response, a variety of reform proposals have been formulated, although at first without any of them being able to find the necessary approval in the respective rule-making fora (i.e. the OECD, United Nations and European Union). As of October 2021, when this book was finalized, political consensus to implement a two-pillar solution seemed to have finally been reached among the OECD and the Inclusive Framework member countries.[3] Nevertheless, the debate leading up to that moment, as this book argues, serves as a call to academia to closely examine the legal theoretical underpinnings and/or pitfalls of the discourse. One might ask what role legal theory plays in the ongoing debate and in international tax in general. In this book, the author will argue that the answer is simple. Legal theory and the explanations it offers concerning a norm's source of normativity are key to understanding the structure and operation of contemporary

1. *See* sec. 2.2. for a detailed account and analysis.
2. *See*, in detail, sec. 2.3.2.4. and the sources cited therein.
3. Please note that this manuscript was finalized in October 2021 and, hence, only takes into consideration developments until October 2021. This includes the declaration of 132 jurisdictions to join the OECD's endeavour to introduce a two-pillar solution to address the tax challenges arising from the digitalization of the economy (*see* https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-july-2021.htm (accessed 30 June 2022)) and the OECD's statement regarding the two-pillar solution from 8 October 2021 (*see* https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.pdf (accessed 30 June 2022)).

international tax discourse and the substantive disagreement over key issues arising therein.

"While international law is developing at a pace without precedent … , there is some danger that the technique of its growth may be impaired by not giving a certain weight to theoretical considerations."[4] Although meant as an observation concerning the field of international law in general, this claim is of equal relevance for international tax law. While – as the debate on how to reform the allocation of taxing rights in an increasingly digitalized economy shows – key concepts of international tax law, e.g. the permanent establishment threshold for source taxation, are called into question and alternatives are being discussed at length, the underlying legal theoretical questions accompanying the debate are being bypassed, a shortcoming of the debate that, as this book argues, comes at a considerable cost.

An example from the ongoing international tax policy debate might help clarify this point: essentially all proposals for extending taxation in the market state put considerable effort into arguing why source taxation is justified.[5] In assuming that taxation actually requires justification, the proposals' advocates inadvertently prompt a much more fundamental question: does justification – or the lack thereof – change a tax rule's legally normative nature? Going one step further, one is inclined to ask: what is the source of normativity of international tax law in general? At this point, the debate inevitably ventures into the territory of legal theory and the various explanations it offers as to what makes law actually law. Depending on the understanding of law employed – legal positivism, realism or naturalism – the answers to the posited questions will vary substantially. The ubiquitous recourse to the need to justify taxation, for example, surprisingly suggests that the mainstream understanding of international tax law is rather naturalistic.[6]

In fact, contemporary international tax discourse offers ample examples of concrete normative claims being made without revealing the source of their normativity, i.e. why they should be seen as legally relevant to begin with: taxation in the market state is justified by that state providing a market and, thus, contributing to the income generation process. The allocation of taxing rights among states should lead to "fair" results, and the allocation of

4. J.G. Starke, *Monism and Dualism in the Theory of International Law*, in *Normativity and Norms: Critical Perspectives on Kelsian Themes* p. 537 (S. Paulson & B. Litschewski Paulson eds., Oxford University Press 2007).
5. *See* sec. 2.3.3.2.
6. *See* sec. 4.2.3.2.2.

taxing rights should not distort the behaviour of market participants, i.e. it should be efficient and, thus, maximize welfare.[7] Analysing the proposals for reform and the academic discussion surrounding them reveals that all proposals can be categorized according to the implicit meta-level assumptions that they are based upon, encompassing the justification of taxation, the necessity of reform and the principles that reform proposals should realize (e.g. value creation). However, already asking one seemingly simple question potentially causes the arguments raised to fall apart. Why does taxation require justification? Why should the allocation of taxing rights be fair? Why should tax law yield economically efficient results? As this book claims, this shortcoming has – both at the substantive and the methodological level – far-reaching implications. By revisiting these claims from a legal theory perspective, the book hopes to offer valuable and novel insights into a variety of heatedly discussed issues.

1.1.2. The substantive aspect, the methodological aspect and the link between them

1.1.2.1. International tax law between positivism, realism and naturalism

Legal theory ideally offers an explanation as to why a certain statement of "ought" carries legal weight, i.e. why it is a valid legal norm that requires compliance. Three dominant theories exist that offer alternative answers to that question: legal positivism, legal realism and naturalism.[8] The key difference – in a nutshell and very simplified – is best explained by reference to the "is" versus "ought" dichotomy and the following three takes on it: (i) a legal "ought" can never follow from an "is" (Kelsian positivism);[9] (ii) the "is" – at least if qualified by a certain conviction of obligation – creates the "ought" (Hartian positivism and legal realism);[10] and (iii) "ought" informs the "is" (naturalism/interpretivism). Under the first two propositions, the question of whether or not the thus ascertained norm comports with fundamental requirements of morality or ethics is, prima facie, irrelevant. On the opposite side of the spectrum, one can find naturalistic theories of law,

7. *See*, e.g. S. Moyal, *Back to Basics: Rethinking Normative Principles in International Tax*, 73 The Tax Lawyer 1, p. 1 (2019), available at https://ssrn.com/abstract=3386678 (accessed 30 June 2022): "There are three normative International Tax principles that determine how a taxpayer should be taxed: Benefits, Single Tax, and Neutrality."
8. *See*, in detail, sec. 3.2.3.2.
9. *See* sec. 3.2.3.2.2.2.
10. *See* secs. 3.2.3.2.2.3. and 3.2.3.2.3.

which ultimately base the binding nature of any norm on political morality. Law is, thus, not limited to norms created by reference to yet another authorizing/ascertaining norm, but also, in the words of Dworkin, encompasses "principles" that reach beyond the formal sources of law.[11] "Ought" in a legal sense thus flows directly from a moral proposition of "ought".

Barely explicit is on which understanding of law the manifold normative claims encountered in the digital economy debate and international tax in general are based. Instead, it has to be inferred from its content and use. Considerable confusion seems to exist when authors simultaneously cite positivists and naturalists when establishing the normative nature of the "principles of international tax law" that they assess, although the conceptions of law that each theory represents could not be more different.[12] The substantive implications of the lack of transparency and consensus concerning the underlying legal-theoretical understanding of international tax law, which characterizes the debate, become clear when Schön – one of the few outspoken sceptics of the ongoing reform endeavour – describes the arguments brought forward as proof of the necessity of change as "not linked to hard-wired legal considerations", but of a mere political nature.[13]

This argument perfectly shows the problem arising from the clash of implicitly endorsed conflicting conceptions of law. A positivist will rebut the claim that the allocation of taxing rights has to be reformed because the current rules lead to unfair results as simply legally irrelevant. From this perspective, distributive fairness is a mere policy argument, but not a demand of the formal sources of international law based on (at least some form of expression of) consent on the side of the states involved. However, once legal normativity – under a naturalistic understanding of law – depends on the rules' substantive content, the dynamics of the argument change. The conformity with demands of morality turns into a legal question, since the "ought" informs the "is". The delimitation between *de lege lata* and *de lege ferenda* thus becomes blurred, giving normative desirability precedence over concreteness. The discourse, as Koskenniemi has described so masterfully in the context of international law, thus oscillates between ascending and descending patterns of argumentation, without hope for reconciliation.[14]

11. *See* sec. 3.2.3.2.4.3.
12. S. Moyal, *Rethinking Normative Principles in International Tax*, p. 29.
13. W. Schön, *Ten Questions about Why and How to Tax The Digital Economy*, 72 Bull. Intl. Taxn. 4/5, p. 280 (2018), Journal Articles & Opinion Pieces IBFD.
14. M. Koskenniemi, *From Apology to Utopia: The Structure of International Legal Argument* p. 59 et seq. (Cambridge University Press 2005).

Once one becomes aware of the implications that legal theory has for international tax law, long-lasting disputes in academia appear in a new light. At least in the following two instances, legal theory, i.e. the understanding of law and the source of its normativity, is decisive for a better understanding (or dismissal) of the arguments made within the debate:

– Principles of international tax law: Recourse to alleged principles of international tax is an omnipresent phenomenon in international tax scholarship.[15] The prominent role that the so-called "value creation principle" plays – or at least used to play up until the emergence of the two-pillar solution – within the proposals advanced in the digital economy debate advocating for extended taxation at source illustrates this point perfectly. Whether or not an identified principle carries legal normative weight depends entirely on the understanding of law endorsed. A principle can either be inducible from existing formal sources of law by means of abstraction (positivism), establish a normative demand of morality (naturalism) or simply be an empirically observable common feature of various bodies of rules governing the taxation of cross-border situations (realism). As legal theoretician Raz has put it: "Some apparent statements of principle are merely abbreviated references to a number of laws, not statements of the content of one complete legal principle."[16]

– State sovereignty and the existence of an international tax regime: The role of fiscal sovereignty and its limitations is inherently connected to the understanding of international law employed. The OECD and its recurrent claim according to which "[t]ax policy is at the core of countries' sovereignty, and each country has the right to design its tax system in the way it considers most appropriate",[17] while advocating far-reaching rule coordination and harmonization, serves as a perfect example in that context. Advocates of coordination regularly stress the therewith-accorded enhancement of "fairness" and "efficiency" of the international tax system, while opponents point at the restriction that such endeavours establish on the individual states' fiscal sovereignty. Both positions reflect a conflicting understanding of the source of

15. *See* sec. 4.1.1. and the sources cited therein.
16. *See* J. Raz, *Legal Principles and the Limits of Law*, 81 Yale Law Journal 5, p. 829 (1972).
17. OECD, *Action Plan on Base Erosion and Profit Shifting* p. 13 (OECD 2013), Primary Sources IBFD; and OECD, *Harmful Tax Competition: A Emerging Global Issue* para. 26 (OECD 1998): "Countries should remain free to design their own tax systems as long as they abide by internationally accepted standards in doing so."

normativity of international law. While under a traditional positivist understanding of international law, state consent and, thus, sovereignty forms the bedrock of international law's normative power, naturalism stresses the moral foundation of legal obligations, not only in relationships among individuals, but also among states.[18] Similarly, the debate on whether a hard-wired international tax regime exists is a reflection of the respective proponents' underlying understanding of law.[19] After all, such a regime is meant to constrain the policy choices of states and, thus, their fiscal sovereignty. Under which conditions the existence of such a system of norms creating a full-fledged international tax regime can be identified depends entirely on the theory of law embraced.

1.1.2.2. Legal theory, legal doctrine and the role of law in tax policy

Beyond its readily understandable substantive aspect, a legal theoretical perspective on international tax law also comprises a methodological dimension, insofar as legal theory defines the subject matter of the doctrinal

18. *See*, on the notion of fiscal sovereignty and jurisdiction to tax, F.A. Mann, *The Doctrine of International Jurisdiction revisited after Twenty Years*, in *Further Studies in International Law* p. 19 et seq. (F.A. Mann ed., Clarendon Press 1990); J. Crawford, *Brownlie's Principles of Public International Law* p. 445 et seq. (8th ed., Oxford University Press 2012); C. Ryngaert, *Jurisdiction in International Law* p. 2 et seq. (2nd ed., Oxford University Press 2014); M. de Heijer & R. Lawson, *Extraterritorial Human Rights and the Concept of "Jurisdiction*", in *Global Justice, State Duties* p. 155 et seq. (M. Langford et al. eds., Cambridge University Press 2013); T. Endicott, *The Logic of Freedom and Power*, in *The Philosophy of International Law* p. 245 et seq. (S. Besson & J. Tasioulas eds., Oxford University Press 2010); R. Jennings, *Sovereignty and International Law*, in *State*, *Sovereignty, and International Governance* (G. Kreijnen ed., Oxford University Press 2002); D. Ring, *What's at Stake in the Sovereignty Debate?: International Tax and the Nation-State*, 49 Virginia Journal of International Law 1, p. 155 et seq. (2008); and C.E. McLure, *Globalization, Tax Rules and National Sovereignty*, 55 Bull. Intl. Taxn. 8, p. 328 et seq. (2001), Journal Articles & Opinion Pieces IBFD.

19. R.S. Avi-Yonah, *International Tax as International Law: An Analysis of the International Tax Regime* p. 4 et seq. (Cambridge University Press 2007); Y. Brauner, *An International Tax Regime in Crystallization – Realities, Experiences and Opportunities*, NYU Law School, Public Law Research Paper No. 43 (2002); H.D. Rosenbloom, *International Tax Arbitrage and the International Tax System, David R. Tillinghast Lecture on International Taxation*, 53 Tax Law. Rev. 2, p. 137 et seq. (2000); E. Baistrocchi, *The International Tax Regime and the BRIC World: Elements of a Theory*, 33 Oxford Journal of Legal Studies 4, p. 4 et seq. (2013); A. Christians, *BEPS and the New International Tax Order*, Bringham Young University Law Rev. 6, p. 1611 (2016); J.M. Rigoni, *The International Tax Regime in the Twenty-First Century: The Emergence of a Third State*, 45 Intertax 3, p. 205 et seq. (2017); and, most recently, W. Schön, *Is There Finally an International Tax System?*, 13 World Tax J. 3, p. 375 et seq. (2021), Journal Articles & Opinion Pieces IBFD. For a legal-theoretical analysis, *see*, in more detail, sec. 4.2.3.4.

discourse by identifying law as law and demarcating it from non-legal norms. Kelsen, for example, claims that his presupposed "basic norm", being the ultimate source of law's validity, is implicitly applied by everyone making a statement about what the law entails.[20] Only once this first step – the identification of law as law – has been taken can an argument about what the law entails be formulated according to the methods of interpretation accepted within the respective judicial forum. This constitutes and enables the scientific process of jurisprudence in the form of legal reasoning, which, in turn, consists of the parallel application of logic, analysis, argumentation and hermeneutics. [21]

The understanding of law applied thus not only defines how a legal argument is being constructed, but also the role that tax lawyers play in the policy discourse. If one maintains a strict separation of "is" and "ought", as under a Kelsian positivist understanding of law, the contribution of tax lawyers to the tax policy discourse would be minimal at best. They would be bystanders restricted to pointing out potential limitations set by existing superior law and maybe advising on the best means to implement the law's envisaged new content. The actual discourse, however, seems to take a different position in this respect when – at least from a strict positivist standpoint – integrating non-legal arguments into the debate's key narratives while applying well-known argumentative patterns of legal methodology. As this book will show, there is ample evidence in contemporary international tax discourse of attempts to employ methods known from doctrine, i.e. interpretation, for proposing new rules when arguing beyond the scope of currently applicable and formally ascertainable norms – a phenomenon that resembles the analogy that Weinberger drew between *de lege ferenda* arguments and a teleological analysis of law and that ultimately underlines this book's hypothesis on the vast – but mostly unexplored – relevance of legal theory for explaining the ongoing international tax law debate.[22]

1.2. Existing scholarship and identified research gap

Scholarship has repeatedly turned to political philosophy in assessing the existing domestic and treaty-based rules governing the allocation of taxing rights, focusing primarily on the justification of taxation from a

20. H. Kelsen, *Pure Theory of Law* p. 46 et seq. (University of California Press 1989).
21. *See* J. Stelmach & B. Brozek, *Methods of Legal Reasoning* p. 17 et seq. (Springer 2006).
22. O. Weinberger, *Zur Theorie der Gesetzgebung,* in *Rechtsphilosophie und Gesetzgebung* p. 185 (H. Mokre & O. Weinberger eds., Springer 1976).

contractarian perspective and questions of distributive justice at the interstate level.[23] Moreover, Peters' thesis on the legitimacy of international tax concentrates on the relationship between law and society and offers highly interesting insights by applying Habermasian sociology to the field of international tax law.[24] Anglo-American scholars have repeatedly stressed the importance of gaining a better understanding of the actual norm-setting processes taking place in international tax and the institutions involved therewith from a sociological perspective.[25] In light of the disruptive effects that digitalization has on the ways in which businesses operate and the therewith-accorded discussion on how to adapt the rules of international tax law, various scholars have subjected the existing rules to a "normative analysis".[26] The normative nature of the benchmarks employed in the analyses, however, are either taken for granted or described as extra-legal, e.g.

23. *See*, e.g. N. Kaufman, *Fairness and the Taxation of International Income*, 29 Law & Poly. Intl. Bus. 2, p. 145 (1998); P. Hongler, *Justice in International Tax Law: A Normative Review of the International Tax Regime* p. 369 et seq. (IBFD 2019), Books IBFD; M. Valta, *Das Internationale Steuerrecht zwischen Effizienz, Gerechtigkeit und Entwicklungshilfe* p. 22 et seq. (Mohr Siebeck 2014); I. Benshalom, *The New Poor at Our Gates: Global Justice Implications for International Trade and Tax Law*, 85 NYU L. Rev 1, p. 1 (2010); I. Benshalom, *Rethinking International Distributive Justice: Fairness as Insurance*, 31 Boston University International Law Journal 2, p. 267 et seq. (2013); T. Dagan, *International Tax and Global Justice*, 18 Theoretical Inquiries in Law 1, p. 1 et seq. (2017), available at http://dx.doi.org/10.2139/ssrn.2762110 (accessed 30 June 2022); T. Dagan, *Pay as You Wish: Globalization, Forum Shopping, and Distributive Justice* (20 June 2014), available at https://ssrn.com/abstract=2457212 (accessed 30 June 2022); A. Christians, *Sovereignty, Taxation and Social Contract*, 18 Minnesota Journal of International Law 1, p. 99 et seq. (2009); A. Christians, *Human Rights at the Borders of Tax Sovereignty*, p. 16 et seq. (27 Feb. 2017), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2924925 (accessed 30 June 2022); M. Ranzoni, *Global Tax Governance: The Bullets Internationalists Must Bite – and Those They Must Not*, 1 Moral Phil. & Pol., p. 37 et seq. (2014); P. Dietsch & T. Rixen, *Tax Competition and Global Background Justice*, 22 J. Pol. Phil., p. 150 et seq. (2014); P. Dietsch, *Catching Capital, The Ethics of Tax Competition* p. 77 et seq. (Oxford University Press 2015); K. Brooks, *Inter-Nation Equity: The Development of an Important but Underappreciated International Tax Value*, in *Tax Reform in the 21st Century* p. 471 et seq. (R. Krever & J.G. Head eds., Wolters Kluwer 2008); A. Cappelen, *National and International Distributive Justice in Bilateral Tax Treaties*, 56 FinanzArchiv 3/4, p. 424 et seq. (1999); and J. Stark, *Verteilungsgerechtigkeit als Prinzip des internationalen Steuerrechts*, 1 Steuer und Wirtschaft 1, p. 71 et seq. (2019).

24. C. Peeters, *On the Legitimacy of International Tax Law* (IBFD 2014), Books IBFD.

25. A. Christians et al., *Taxation as a Global Socio-Legal Phenomenon*, 14 ILSA Journal of Intl. and Comp. Law 2, p. 3030 et seq. (2010); R. Azam, *Ruling the World: Generating International Tax Norms in the Era of Globalization and BEPS*, 50 Suffolk University Law Rev. 4, p. 4 et seq. (2017); and A. Christians, *Hard Law and Soft Law in International Taxation*, 25 Wisconsin International Law Journal 2 (2007).

26. *See*, e.g. P. Hongler, *Justice*; S. Moyal, *Rethinking Normative Principles in International Tax*; and S. Gadzo, *Nexus Requirements for Taxation of Non-Residents' Business Income: A Normative Evaluation in the Context of the Global Economy* (IBFD 2018), Books IBFD. With respect to the benefit principle, *see* E. Escribano Lopez, *Jurisdiction to Tax*

relevant only as a question of political and/or moral philosophy. Magalhaes recently offered a highly interesting assessment of the existing international tax system from the standpoint of critical legal studies – a modern iteration of legal realism – making him one of the very few authors to reveal the legal theory position assumed as the scholarship's starting point.[27]

So far, however, no comprehensive analysis of the international tax discourse exists that (i) assesses the understanding of law that the participants in the debate implicitly endorse; and (ii) assesses the explanatory value of the prevailing legal theories in offering alternative argumentative routes in establishing the recurrent claims as legally relevant. This book hence hopes to fill this research gap and contribute to the field of international tax law by offering insights into its legal theoretical underpinnings.

1.3. Applied methodology and limitations of the inquiry

This book adopts a legal theory perspective in order to assess the arguments made in the ongoing discourse on how to allocate taxing rights in a digitalized economy. It thus analyses the explanatory value of the prevailing legal theories in establishing the legal validity of the dominant normative claims underlying the debate, i.e. that taxation requires justification and should be fair and neutral. In doing so, the book proceeds in two steps, each entailing different methodological approaches. First, it describes the reform proposals and groups them according to the meta-level assumptions that they are based on. The first step thus applies standard legal doctrine, i.e. statutory interpretation. In a subsequent step, after having outlined the key theories explaining the normativity of law and its sources, the book situates the identified and categorized claims in legal theory, i.e. within the spectrum ranging from Kelsian positivism to Dworkinian interpretivism. Leaving doctrine behind, it thus tries to reconcile the actual arguments encountered with its potential theoretical underpinnings. In exploring the legal theories' value in supporting the concrete claims made within the discourse, the book returns to the realm of doctrine, since only an interpretation of the existing sources of law reveals whether positivism supports the respective argument.

Corporate Income Pursuant to the Presumptive Benefit Principle: A Critical Analysis of Structural Paradigms Underlying Corporate Income Taxation and Proposals for Reform (Kluwer Law 2019).

27. T.C. Magalhaes, *What Is Really Wrong with Global Tax Governance and How to Properly Fix It*, 10 World Tax J. 4, p. 499 et seq. (2018), Journal Articles & Opinion Pieces IBFD.

Two clarifications are necessary at this point. First, although dealing with questions of legal theory and, arguably, legal philosophy,[28] it is important to stress that this book was written by a lawyer who does not claim to be a trained philosopher. All he can offer is an overview and a deepened understanding of legal theory, or, as the German philosopher Heidegger has put it: "The knowledge about philosophical schools of thought does not equate being a philosopher."[29] The book does not aim to establish a comprehensive theory of international tax law, but intends to show the influence that legal theory implicitly has on how the actual international tax discourse is taking place and to test the explanatory force of different legal theoretical conceptions of law in enhancing the persuasiveness of the field as such. The starting point and permanent point of reference hence are the proposals and arguments made in the tax policy discourse.

Second, the book does not apply an interdisciplinary approach. Hence, the author does not test the substantive merit of the arguments encountered in the digital economy debate, e.g. that the current allocation of taxing rights is unfair or economically inefficient, against benchmarks derived from philosophy or public finance itself. Instead, the book explores whether and, if so, under which conception of law these claims become legally relevant, i.e. are being incorporated into the legal analysis due to the normative weight attributed to them by the respective understanding of law.

1.4. Objective, hypotheses and structure

1.4.1. Objective

Fully explaining the objective of this book calls for a brief look back at its genesis. Initially, this postdoctoral research project pursued a more technical goal, as highlighted by the title under which it received funding by the Austrian Research Fund (FWF) in 2016, "The Taxation of Non-Residents: Concepts and Limitations". At the beginning, the aim was to develop a clearer picture of the legal limitations that a state's jurisdiction to tax faces under international and EU law. Over time, however, the author realized that this endeavour could only yield persuasive results if limited to a predefined understanding of law and its normativity, i.e. if he adopted a positivist understanding of law. Whether or not a state's jurisdiction to

28. For the difficulties of demarcating theory from philosophy and its relevance for this book, *see* sec. 3.1.2.
29. M. Heidegger, *Einführung* in die Metaphysik p. 9 (Max Niemeyer 1953).

tax is limited under public international law is ultimately a question of the understanding of law endorsed.[30] Hence, any finding would either be the result of a mere intra-mural doctrinal discussion embracing a specific concept of international law or vulnerable to criticism by those endorsing a different understanding. Any result reached within the theoretical conception of legal positivism, e.g. that no international law limitation to asserting a right to tax exists, can be rightfully attacked by opponents as either ignoring justice and legitimacy aspects (naturalists) or as a mere tool of powerful actors to uphold a favourable status quo (critical legal studies).[31] International tax scholarship, the author realized, was, thus, highly path-dependent. Moreover, the reality of the discourse led in international tax suggests that – rather counterintuitively – naturalistic arguments, i.e. arguments that only acquire meaning when embracing a non-positivist understanding of law, were commonplace. Against this background, the author adjusted the focus of the research project to concentrate on the role that legal theory plays in international tax discourse.

In doing so, this book hopes to contribute to the academic field of international tax law and tax policy by pursuing the following objectives:

– to critically assess and categorize the proposals made and the arguments raised in their favour within the ongoing debate on how to allocate taxing rights among states in a digitalized economy;
– to identify the assumptions on which the proposals rest and the understanding of law they implicitly endorse;
– to assess the explanatory force of the prevailing legal theories in establishing the legal relevance of the discourse's key claims according to which (i) taxation requires justification; (ii) the allocation of taxing rights should be "fair" or "just", both viewed from the perspective of the individual taxpayer and within the trilateral state-state-taxpayer relationship; and (iii) international tax law should be efficient, i.e. lead to welfare maximization; and
– to raise awareness of the relevance that legal theory has in formulating claims in the international tax law debate and their substantive and/or methodological persuasiveness.

30. *See* sec. 4.2.3.4.5.1.
31. *See*, e.g. T.C. Magalhaes, *What Is Really Wrong with Global Tax Governance and How to Properly Fix It*, p. 499 et seq.

1.4.2. Key hypotheses

Given the objectives described above, this book poses the following two main hypotheses:

– Hypothesis (1): The discussion on how to address the tax challenges raised by digitalization is characterized by a lack of consensus and transparency concerning the understanding of law employed in making the arguments. Instead, all proposals rest on a set of meta-level assumptions concerning the need to justify taxation (sovereign entitlement and benefit/economic allegiance doctrine), the necessity of reform and the principles that the reformed allocation of taxing rights should be based upon (fairness and efficiency).

– Hypothesis (2): The digital economy debate offers a perfect case study, showing that – rather counterintuitively – rule-setters like the OECD, as well as international tax scholars, implicitly embrace a naturalistic understanding of law. Positivism offers very little support in establishing the legal relevance of the repeated claims. The discourse is, thus, characterized by irreconcilable descending naturalist and ascending positivist patterns of argumentation. Even within the supra-national, hierarchically superior legal framework of EU primary law, a constructivist interpretation of the law's formal sources provides the best explanation for the legal relevance of the claims made within the debate.

1.4.3. Structure

The book consists of four main parts:

(1) Chapter 2: The Debate on How to Reform the International Tax System in Light of Digitalization

In this chapter, the book offers an overview of the key proposals advanced within the ongoing debate on how to reform the allocation of taxing rights in an increasingly digitalized economy by the relevant rule-making fora (OECD, United Nations and European Union), as well as academia.[32] The chapter categorizes the proposals according to their aim (extending source-based taxation, extending residence-based

32. Please note that developments within in the debate have been taken into account if they occurred prior to October 2021.

taxation and abandoning the residence/source dichotomy) and the technical means to implement them (consensus-based treaty solution versus (quasi) unilateral implementation in domestic law, even if mandated by an EU Directive). In a second step, the chapter identifies three key groups of assumptions that the debate relies upon, concerning the necessity of reform, the justification of taxation and the principles that a reformed allocation of taxing rights should be built upon. In doing so, it not only highlights the assumptions' implications, but also engages in a discussion of the assumptions' substantive merit and conceptual persuasiveness.

(2) Chapter 3: Normativity and Legal Validity in International Taxation

Against the background of the analysis offered in chapter 2, chapter 3 deals with the relevance of legal theory for international tax and tax policy, both from a substantive and a methodological perspective. It explains why legal theory matters and how theory, doctrine and policy interact. Most importantly, however, it offers an overview of the three prevalent legal theories, i.e. positivism, realism and naturalism, and their key claims with respect to both domestic and international law; after all, this book defines international tax law as encompassing both the domestic and international law sources applicable to the taxation of income stemming from cross-border activities.

(3) Chapter 4: Normativity and Its Source in International Tax Law: International Tax Discourse between Positivism, Realism and Naturalism

Chapter 4 constitutes the book's core element and ties the loose ends between the analysis of the debate made in chapter 2 and the legal theories described in chapter 3. Before venturing into a legal theoretical analysis of the contemporary international tax discourse, it first critically assesses the role and use of principles from a theoretical perspective, defines the subject matter of international tax law and discusses the interaction between its sources (i.e. domestic and international law). Moreover, by reference to Koskenniemi's account of international law between apology and utopia, it describes the explanatory paths that each theory embraces in abstract. After clarifying these preliminary questions, the chapter focuses on its key objective to situate the arguments raised in the debate within legal theory and assesses the legal theories' explanatory value in establishing the claims' legal relevance. It thus revisits the digital economy debate and the assumptions that it rests

The Home of International Taxation

Contact

IBFD Head Office
Tel.: +31-20-554 0100 (GMT+2)
Email: info@ibfd.org

Visitors' Address:
Rietlandpark 301
1019 DW, Amsterdam
The Netherlands

Postal Address:
P.O. Box 20237
1000 HE Amsterdam
The Netherlands