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When International Tax Agreements Fail at Home: A U.S. Example

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WHEN INTERNATIONAL TAX AGREEMENTS FAIL AT HOME: A U.S. EXAMPLE

*Diane Ring**

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INTRODUCTION

Over the past two and a half years, the international tax community has focused on the Base Erosion and Profit Shifting Project (BEPS project) undertaken by the Organisation for Economic Co-operation and Development (OECD) at the behest of the G20. The mission of the project, as its title suggests, is to address the substantive and procedural tax rules that have enabled taxpayers, particularly large multinational businesses, to pursue transactions and strategies that have effectively eroded tax bases and shifted profits to low- or no-tax jurisdictions. In October 2015 the OECD delivered its BEPS package of sixteen reports and related recommendations to the G20 for approval. According to the OECD, the subsequent analysis and agreement involved the direct participation of more than sixty countries.¹ An additional fifty-nine countries indirectly participated through regional dialogues.² Furthermore, numerous international organizations are credited with participating in discussions and contributing to the resulting product.³ According to the OECD, the next step is to design and implement an “inclusive framework for monitoring BEPS and [for] supporting implementation of the measures, with all interested countries and jurisdictions invited to participate on an equal footing.”⁴ In early 2016 the OECD announced the framework that will allow the

1. ORG. FOR ECON. CO-OPERATION AND DEV. [OECD], EXPLANATORY STATEMENT: 2015 FINAL REPORTS 4 (2015), <http://www.oecd.org/ctp/beps-explanatory-statement-2015.pdf>.

2. In two rounds of meetings in 2015 and early 2016, fifty-nine countries participated in Regional Network meetings, offering input for the BEPS project. *Id.* at 4–5.

3. Participating organizations included the African Tax Administration Forum, Centre de recontre des administrations fiscales, Centro Interamericano de Administraciones Tributarias, International Monetary Fund (IMF), World Bank, and the United Nations. *Id.*

4. *OECD Presents Outputs of OECD/G20 BEPS Project for Discussion at G20 Finance Ministers Meeting*, OECD.ORG (Oct. 5, 2015), <http://www.oecd.org/ctp/oecd-presents-outputs-of-oecd-g20-beps-project-for-discussion-at-g20-finance-ministers-meeting.htm>.

equal participation of all countries in the BEPS implementation process.⁵

Over the past three years, significant energy and resources have been channeled toward achieving international consensus on the nature of major international tax problems and on reform responses. Examples of international tax cooperation certainly predate the BEPS project, as do scholarly examinations of such cooperation.⁶ But, the scale and scope of international engagement in the BEPS project presents a unique opportunity to evaluate international cooperation.⁷ Nonetheless, the BEPS project's

5. See *Implementing the BEPS Package: Building an Inclusive Framework*, OECD.ORG (Feb. 2016), <https://www.oecd.org/tax/flyer-implementing-the-beps-package-building-an-inclusive-framework.pdf>; see also *All Interested Countries and Jurisdictions to be Invited to Join Global Efforts Led by the OECD and G20 to Close International Tax Loopholes*, OECD.ORG (Feb. 2, 2016), <http://www.oecd.org/ctp/all-interested-countries-and-jurisdictions-to-be-invited-to-join-global-efforts-led-by-the-oecd-and-g20-to-close-international-tax-loopholes.htm>; Kevin Bell, *OECD Invites All Countries to Implement BEPS Measures*, Int'l Tax News (BNA) (Feb. 23, 2016), <http://www.bna.com/oecd-invites-countries-m57982067630/>.

6. Tsilly Dagan, *The Tax Treaties Myth*, 32 N.Y.U. J. INT'L L. & POL. 939, 1 (2000); Tsilly Dagan, *Dilemmas of Tax Policy in a Globalized World*, SOCIAL SCIENCE RESEARCH NETWORK (Nov. 11, 2001), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1957945; Antonio Hugo Figueroa, *Tratados tributarios para evitar la doble imposición internacional o para transferir recursos de países en desarrollo a países desarrollados* [*Tax Treaties to Avoid Double International Taxation or Transfer of Resources from Developing to Developed Countries*], VOCES EN EL FENIX, May 2012, at 128.

7. See, e.g., Yariv Brauner, *What the BEPS?*, 16 FLA. TAX REV. 55, 74–75 (2014) (describing character and source rules as a “major bone of controversy between developing countries and the OECD”); Arthur J. Cockfield, *BEPS and Global Digital Taxation*, 75 TAX NOTES INT'L 933, 933–40 (2014); Reuven S. Aviyonah & Haiyan Xu, *Evaluating BEPS* (Univ. of Mich. Law Sch., Pub. Law & Legal Research Paper Series, Paper No. 493, 2016), <http://ssrn.com/abstract=2716125>; Adam H. Rosenzweig, *Building a Framework for a Post-BEPS World*, 74 TAX NOTES INT'L 1, 1–7 (2014); Jung-hong Kim, *A New Age of Multilateralism in International Taxation?*, 21 SEOUL TAX L. REV. 227 (2015), <http://ssrn.com/abstract=2733964>; Dirk Maarten Broekhuijsen & Henk Vording, *The Multilateral Tax Instrument: How to Avoid a Stalemate on Distributional Issues?*, 2016 BRITISH TAX REV. 39, <http://ssrn.com/abstract=2745229>; Baitshepi Tebogo, *The Transfer Pricing Problem: When Multinational Corporations Shift Profits Across International Borders*, SOCIAL SCIENCE RESEARCH NETWORK 1 (July 30, 2011), <http://ssrn.com/abstract=1899014>; Tsilly Dagan, *Community Obligations in International Taxation*, SOCIAL SCIENCE RESEARCH NETWORK (Feb. 23, 2016), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2736923; Yariv Brauner, *Treaties in the Aftermath of BEPS*, 41

stated mission will not be achieved exclusively through the international agreement evidenced in the final reports and recommendations released in 2015. Effective implementation of the BEPS package approved by the G20 in 2015 requires domestic action of various types—the domestic side of international agreement.⁸

Execution of the BEPS recommendations relies on those measures being implemented “through domestic law changes, including [but not limited to] strengthened rules on Controlled

BROOK. J. INT'L L. 973 (2016); Itai Grinberg, *Breaking BEPS: The New International Tax Diplomacy* (Georgetown Univ. Law Center, 2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2652894; Hugh J. Ault, *Some Reflections on the OECD and the Sources of International Tax Principles*, 70 TAX NOTES INT'L (2013); Hugh J. Ault, Wolfgang Schoen, & Stephen E. Shay, *Base Erosion and Profit Shifting: A Roadmap for Reform*, 68 BULL. INT'L TAX'N 275 (2014), <http://ssrn.com/abstract=2459646>; Michael Lang & Jeffrey Owens, *The Role of Tax Treaties in Facilitating Development and Protecting the Tax Base* (WU Int'l Taxation Research Paper Series, No. 2014-03, 2014), <http://ssrn.com/abstract=2398438>; Orly Mazur, *Transfer Pricing Challenges in the Cloud*, 57 B.C. L. REV. 643 (recommending that, given the features of a new business environment driven by Cloud computing and virtual information storage, an international tax reform solution that adopts formulary apportionment or the profit-split methodology on a coordinated global basis would better address BEPS and minimize the undesirable policy results of our current transfer pricing rules); Andres Baez & Yariv Brauner, *Withholding Taxes in the Service of BEPS Action 1: Address the Tax Challenges of the Digital Economy* (WU Int'l Taxation Research Paper Series, Paper No. 2015-14, 2015), <http://ssrn.com/abstract=2591830>. Economic analysis offers insights into particular base erosion problems and the potential for action. See, e.g., Kimberly A. Clausing, *The Effect of Profit Shifting on the Corporate Tax Base in the United States and Beyond* (June 17, 2016) (unpublished paper), <http://ssrn.com/abstract=2685442> (estimating the effect of profit shifting on corporate tax base erosion for the United States and the sensitivity of foreign incomes to tax burdens for major foreign direct investment destinations, and considering extension of this analysis to other countries).

8. H. David Rosenbloom & Joseph P. Brothers, *Reflections on the Intersection of U.S. Tax Treaty Policy, U.S. Tax Reform, and BEPS*, 78 TAX NOTES INT'L 759–69 (2015) (“The stated goal of BEPS is a coordinated effort to reduce corporate tax avoidance. The real-world effect, however, is more likely to be seen in the efforts of individual countries to impose a greater tax burden on inbound investment. Coordination of the BEPS actions seems unlikely in a world with hugely disparate views of the function of an income tax. The more foreseeable result is a cacophony of new rules, predicated on BEPS and tempered only by the views of individual countries regarding adverse impacts on the inflow of capital.”).

Foreign Corporations, a common approach to limiting base erosion through interest deductibility and new rules to prevent hybrid mismatch arrangements from making profits disappear for tax purposes through the use of complex financial instruments.”⁹ In addition to such purely domestic law steps, the BEPS project requires rapid incorporation of BEPS concepts into the vast number of bilateral tax treaties. Traditionally, the treaty process entails bilateral renegotiation and domestic ratification on a treaty-by-treaty basis. To bypass this cumbersome process, the OECD introduced a multilateral instrument (available for countries’ signatures in 2016) that is designed to facilitate the incorporation of BEPS treaty-related measures into existing bilateral treaties.¹⁰ Thus, while the BEPS final package represents a level of global engagement and agreement,¹¹ crucial steps must be taken at the domestic level to ensure any real effectiveness for the BEPS project.

This article makes three points regarding the pivotal domestic side of international tax agreements—including the BEPS project. First, domestic-level compliance cannot be presumed simply from the existence of some degree of international agreement. Even if states reach an understanding regarding some facet of an international tax problem, an “agreement” by states is not the end game. Instead, the true goal is full implementation

9. *OECD Presents Outputs of OECD/G20 BEPS Project for Discussion at G20 Finance Ministers Meeting*, *supra* note 4.

10. *Id.*

11. For purposes of this article, it is acknowledged that the BEPS project has achieved notable global participation and agreement. That said, there are significant critiques of the OECD and the work of the BEPS project. Some contend that the project is not aggressive enough in combatting avoidance and profit shifting and that the resulting measures are too diluted to be significant. *See, e.g.*, Eva Eberhartinger & Matthias Petutschnig, *Practicing Experts’ Views on BEPS: A Critical Analysis* (WU Int’l Taxation Research Paper Series, Paper No. 2015-27, 2015), <http://ssrn.com/abstract=2683552>; Dhammika Dharmapala, *What Do We Know About Base Erosion and Profit Shifting? A Review of the Empirical Literature* (Univ. of Chi. Coase-Sandor Inst. For Law & Econ., Research Paper No. 702, 2014), <http://ssrn.com/abstract=2373549> (arguing through different empirical approaches for identifying income shifting that the estimated magnitude of BEPS is typically much smaller than that found in earlier studies). Others have questioned developed countries’ use of power to shape the terms of the international tax system. *See, e.g.*, Allison Christians, *Hard Law, Soft Law, and International Taxation*, 25 WIS. INT’L L.J. 325 (2007); Allison Christians, *Sovereignty, Taxation, and Social Contract*, 18 MINN. J. OF INT’L L. 99 (2009).

of any and all steps necessary to bring that agreement into full effect. The question, then, is why is international agreement not necessarily sufficient?

The answer is the power and role of the domestic side of the nation-state. Although states must act and negotiate as monoliths in their state-to-state interactions,¹² there remains the ever-present constraint of democracy at home and the possibility that a deal struck on the global stage will be undone in the domestic sphere. This dynamic between international relations and domestic "politics" is neither new nor limited to taxation. The ongoing U.S. failure in tax treaty ratification, however, provides a fascinating case study of one significant domestic derailment of international agreement. Given the heightened expectations regarding cooperation among nations in the BEPS project,¹³ adequate attention should be directed to the domestic side of cooperation.

12. For example, as the OECD continues to pursue the BEPS project, both in its initial formulations and in future applications, the United States must present a single U.S. position on the questions. But, to the extent progress on the BEPS issues is premised on a measure of agreement among the participating states and anticipates corresponding cooperation, the real success of international agreement remains contingent on domestic support. Of course, the complexities are even richer than simply the addition of domestic compliance to the international cooperation story. At the earlier state-to-state level of negotiation, even though countries formally adopt positions as a single actor, the reality of competing views domestically remains likely. The existence of competing positions percolating within the jurisdiction can be evidenced by the array of non-state actors seeking to influence the discussion (including, for example, trade and industry organizations, multinationals, and nongovernmental agencies).

13. See OECD, *supra* note 1 (highlighting goals of the BEPS project to include the "urgent need to restore the trust of ordinary people in the fairness of their tax systems, to level the playing field among businesses, and to provide governments with more efficient tools to ensure the effectiveness of their sovereign tax policies."). But, the BEPS project is also seen as a way to preempt a multitude of potentially conflicting domestic steps. *Id.* ("It was also imperative to move quickly to try to limit the risks of countries taking uncoordinated unilateral measures which might weaken key international tax principles which form a stable framework for cross-border investments."). Moreover, the project's structure and goals, by their very design, require widespread cooperation. *Id.* ("The G20 and the OECD have recognised that BEPS by its very nature requires coordinated responses, which is why countries have invested the resources to participate in the development of shared solutions."). The G20 has supported the group effort of the OECD in the base erosion work. See, e.g., Group of Twenty [G-20], *Los Cabos Summit Leaders' Declaration* ¶ 48 (June

Second, the reasons why international agreements may be stymied on the domestic front vary greatly, but can include: (1) a conflict in goals between the branch of government responsible for negotiating with other states and the branch(es) involved in the process of domestic implementation; (2) a state's decision to only nominally accept an emerging global rule or practice; (3) a change in political parties between the international negotiation phase and the completion of the required domestic steps; (4) the use of procedural techniques by a political minority to forestall domestic implementation; and (5) the inability of international agreements crafted by technical experts to gain broader political traction and support in the domestic arena. Study of international tax relations (i.e., the intersection between international relations theory and practice and international tax) may provide a better understanding of the origins and nature of any gap between a nation's international position on a tax issue and the domestic view of that same problem.

Third, the BEPS project—which contains multiple issues, types of commitments, and players—presents numerous dimensions on which strategic conduct can be pursued. The two-level game theory model of international relations, which formalizes the observation that a state must secure international agreement with global actors (level one of the game) and must secure domestic agreement to the international commitment (level two of the game), becomes quite intricate when played with so many moving pieces. One possibility is that states have become sophisticated players of this two-level game in the BEPS project. For example, perhaps states have been willing to make general,

18–19 2012), https://g20.org.tr/wp-content/uploads/2014/12/G20_Leaders_Declaration_Final_Los_Cabos_0.pdf (expressing the “need to prevent base erosion and profit shifting” and voicing support for the work being done in that area by the OECD). The U.S. Treasury Secretary reiterated the emphasis on coordinated rather than unilateral action. Press Release, Statement by Treasury Secretary Jacob J. Lew at the G-20/OECD BEPS Press Conference (Oct. 9, 2015), <https://www.treasury.gov/press-center/press-releases/Pages/jl0204.aspx> (noting the acceptance of deliverables from the BEPS project and underscoring the “wide agreement that these recommendations should be successful when implemented in cooperation, and that countries should avoid unilateral action inconsistent with the process.”). For more on the U.S. perspective, see STAFF OF THE J. COMM. ON TAXATION, 114TH CONG., JCX-139-15, BACKGROUND, SUMMARY, AND IMPLICATIONS OF THE OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT (Comm. Print 2015).

global commitments on the expectation that not all commitments with all actors will be executed with equal robustness at the domestic level.

Fortunately, to date, international tax policy analysis provides a good foundation for exploring, assessing, and evaluating the effects of the domestic politics of a democracy on developments in tax policy. In recent years, the tax literature has begun the task of evaluating international tax policy formation through the insights, questions, and analytical frameworks offered by the broader international relations literature.¹⁴ International tax topics explored through this lens include: the development of global fiscal transparency norms;¹⁵ the contest between automatic information reporting and anonymous withholding;¹⁶ cooperative non-treaty mechanisms to resolve collective action problems in international tax;¹⁷ sovereignty in international tax

14. See, e.g., Diane Ring, *International Tax Relations: Theory and Implications*, 60 TAX L. REV. 83 (2007); Paul R. McDaniel, *The David R. Tillinghast Lecture Trade Agreements and Income Taxation: Interactions, Conflicts, and Resolutions*, 57 TAX L. REV. 275 (2004); Eduardo A. Baistrocchi, *The International Tax Regime and the BRIC World: Elements for a Theory*, 33 OXFORD J. LEGAL STUD. 733 (2013); Joshua Aizenman & Yothin Jinjarak, *The Collection Efficiency of the Value Added Tax: Theory and International Evidence* (Nat'l Bureau of Econ. Research, Working Paper No. 11539, 2005), <http://ssrn.com/abstract=779949>; Michael J. Graetz, *Can a 20th Century Business Income Tax Regime Serve a 21st Century Economy?* 30 AUSTL. TAX F. 551 (2015).

15. See, e.g., Lisa Philipps & Miranda Stewart, *Fiscal Transparency: Global Norms, Domestic Laws, and the Politics of Budgets*, 34 BROOK. J. INT'L L. 797 (2009); ALASDAIR S. ROBERTS, GLOB. INITIATIVE FOR FISCAL TRANSPARENCY, PROMOTING FISCAL OPENNESS (2015), <http://ssrn.com/abstract=2608967>; Lisa Philipps, *The Globalization of Tax Expenditure Reporting: Transplanting Transparency in India and the Global South* (Osgoode Hall Law Sch. Comparative Research in Law & Political Econ. Research Paper Series, Research Paper No. 43/2012, 2012), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2156484&download=yes.

16. See, e.g., Itai Grinberg, *The Battle Over Taxing Offshore Accounts*, 60 UCLA L. REV. 304 (2012).

17. See, e.g., Adam H. Rosenzweig, *Thinking Outside the (Tax) Treaty*, 2012 WIS. L. REV. 717 (2012); Laura Friedlander & Scott Wilkie, *Policy Forum: The History of Tax Treaty Provisions—And Why it is Important to Know About it*, 54 CANADIAN TAX J. 907 (2006) (detailing the vast amount of inaccessible precedent and history regarding the intent and application of tax treaties and the subsequent difficulty in relying upon tax treaties for modern tax policy).

policy;¹⁸ identity and impact of key actors in creating international tax policy;¹⁹ and “sharing” among nations.²⁰

The task of this article is to explore how domestic politics can impact the heart of the international tax system—the agreements among nation-states on important issues of tax policy design and practice. This inquiry is not a normative question of if and when international tax cooperation is appropriate or desirable. Rather, it is a positive question of how agreements transition from the global arena to the domestic sphere successfully or unsuccessfully.

Emphasizing the reality of domestic derailments of international tax agreements, Part I introduces the prominent and recent U.S. domestic failure to secure ratification of U.S. tax treaties. The story is outlined in some detail to provide a rich sense of the complicated political forces at play on the domestic side when bilateral tax treaties are signed. Although the precise sequence of events, motivations, and constraints are context specific, the message regarding the potential for a gap between a nation’s asserted position on the international stage and its capacity to execute at home resonates more broadly. The BEPS project, which contains a variety of international agreements and commitments, provides ample opportunity for domestic-international gaps and discords to emerge.

Part II provides a preliminary review of the international relations literature regarding international cooperation, which provides valuable insights for building a model of domestic politics in international tax. Although the international relations literature has directed some attention to taxation in recent years, there remains significant work to be done in translating core theoretical ideas from the general literature (and from the case studies in defense, human rights, and trade) to the tax context.

18. See, e.g., Diane M. Ring, *Democracy, Sovereignty & Tax Competition: The Role of Tax Sovereignty in Shaping Tax Cooperation*, 9 FLA. TAX REV. 555 (2009).

19. See, e.g., Diane M. Ring, *Who is Making International Tax Policy?: International Organizations as Power Players in a High Stakes World*, 33 FORDHAM INT’L L.J. 649 (2010).

20. See, e.g., Allison Christians, *How Nations Share*, 87 IND. L.J. 1407 (2012); Allison Christians, *Global Trends and Constraints on Tax Policy in the Least Developed Countries*, 42 U.B.C. L. REV. 239 (2010).

Part III looks to some of the theoretical work reviewed in Part II to offer preliminary thoughts on a framework for understanding the intersection of international tax and domestic politics. In light of the increasing role that global cooperation and coordination play in the development of successful international tax policy and practice, the article concludes by considering the next research steps that could illuminate the domestic side of international agreements.

I. CASE STUDY OF DOMESTIC CHALLENGES TO INTERNATIONAL TAX COOPERATION

This Part introduces a U.S. case study in order to launch a conversation about, and an examination of, the domestic side of international taxation. To gain a solid understanding of the full forces at work, it will be important to develop a body of international tax case studies across different jurisdictions. In that undertaking, it will be critical to envision the relationship between the domestic and the global spheres as interactive and dynamic. The two spheres are not entirely separate, nor is their relationship linear, one-directional, or episodic. In fact, one could observe that there could be no “national position” to bring to the international negotiating table without first having developed some sense of an issue domestically. Despite the iterative dimension of the interaction between these spheres, it is useful to examine an important and definitive way in which they can collide—when an international agreement “returns” home and is challenged, blocked, or rejected. Thus, this case study identifies an international agreement—here tax treaties—that faced resistance domestically. This article draws attention to a significant U.S. example in order to provide a starting point to assess the level of detail and the array of relevant actors engaged in such stories.

A. U.S. Tax Treaties and Domestic Ratification

The U.S. treaty formation and ratification process provides one illustration of the dynamic between the domestic political sphere and international tax relations. U.S. treaties are negotiated and signed by the executive branch of the government. The signed treaty is then submitted to the Senate for “advice and

consent.”²¹ After the Senate approves the treaty (through a two-thirds majority of Senators present), the president exchanges signed ratification instruments with the treaty partner, thereby bringing the treaty into force. The U.S. House of Representatives (the “House”) plays no role in the process, despite the fact that under the U.S. Constitution the House is the designated body for originating “all bills for raising Revenue.”²² U.S. tax treaties do not have to be incorporated into domestic law²³ to have the force of law. Instead, tax treaty provisions in the United States are generally considered to be “self-executing,” meaning no further legislation is required to implement the treaty terms. IRC § 894(a),²⁴ which states that the tax code shall be applied “with due regard to any treaty obligation of the United States,” can be interpreted as granting legislative effect to tax treaties.²⁵

21. U.S. CONST. art. II, § 2, cl. 2; *see also Advice & Consent*, U.S. SENATE, http://www.senate.gov/general/Features/Treaties_display.htm (last visited May 31, 2016).

22. U.S. CONST. art. I, § 7, cl. 1. Tax treaties, however, do not increase the burden on taxpayers relative to U.S. domestic tax law, and taxpayers can elect to decline the benefits of tax treaties. Taxpayers, though, are limited in their ability to apply provisions of a relevant treaty selectively.

23. “Dualist” is the term often used to describe countries where treaties do not automatically operate in domestic law and “monist” for countries where they do automatically operate.

24. 26 U.S.C.A. § 894 (West 2016). I.R.C. § 894 itself is domestic law passed according to Constitutional provisions regarding the role of the House of Representatives in passing tax legislation.

25. Unlike the legal relationship between treaties and domestic statutes in many countries, U.S. domestic legislation can override treaties. Article VI, clause 2 of the U.S. Constitution provides that “[l]aws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the Supreme Law of the Land.” According to the U.S. Supreme Court, this language means that statutes and treaties are of equal standing. *Reid v. Covert*, 354 U.S. 1 (1957). In the event of a conflict between a domestic statute and a treaty, the Supreme Court has held that the later-in-time rule prevails (i.e., whichever treaty or statute is adopted or enacted later will prevail). *See Whitney v. Robertson*, 124 U.S. 190, 194 (1888) (“By the Constitution a treaty is placed on the same footing, and made of like obligation, with an act of legislation. Both are declared by that instrument to be the supreme law of the land, and no superior efficacy is given to either over the other. . . . If the two are inconsistent, the one last in date will control the other . . .”). Courts, however, will seek to harmonize the language of potentially conflicting treaties and statutes where possible, and will try to reserve the finding of a conflict (and thus the need to resort to the later-in-time rule) to those cases in which Congress has indicated a knowing intent to create conflict and override a treaty with a later statute.

As is often the case in U.S. government, the Constitution does not tell the whole story. Once a treaty is submitted to the Senate for its consent, then, per Senate rules,²⁶ “it shall be read a first time; and no motion in respect to it shall be in order, except to refer it to a committee [Foreign Affairs Committee], to print it in confidence for the use of the Senate, or to remove the injunction of secrecy.” After the Foreign Affairs Committee considers the treaty and any potential amendments to it,²⁷ it may then vote to report the treaty to the floor of the Senate. The treaty may then lie over another day before being read again and opened up to discussion and amendment, unless the Senate unanimously consents to immediate discussion.²⁸

The resolution for a treaty vote follows the general rules for Senate consideration of a bill, meaning that it is open for unlimited debate and amendment. Amendments need not be germane, and by continuing debate or suggesting new amendments, one senator may postpone a ratification vote indefinitely.²⁹ Thus, as a basic matter, a single senator can block a treaty from reaching the Senate floor and facing a vote on advice and consent to ratification. Much Senate business is conducted by unanimous vote,

Anthony C. Infanti, *United States, in TAX TREATIES AND DOMESTIC LAW* 370–372 (Guglielmo Maisto ed., 2006). Historically, domestic tax law in the United States expressed an approach that generally sought to preserve treaties, but revisions to I.R.C. § 894(a) and § 7852(d)(1) now reiterate the later-in-time view (but with a continued commitment not to seek out conflict where it can be avoided). *Id.* The United States has enacted a number of tax treaty overrides in the past decades, including the Foreign Investment in Real Property Tax Act (I.R.C. § 897 and § 1445) and the Branch Level Interest Tax (I.R.C. § 884).

26. S. Res. 285, 113th Cong. art. XXX (revised on Jan. 24, 2013), <https://www.gpo.gov/fdsys/pkg/CDOC-113sdoc18/pdf/CDOC-113sdoc18.pdf>.

27. A reported treaty will often carry several amendments as a matter of course that limit the interpretation of the treaty. One such amendment, the Byrd-Biden condition, mandates that the treaty only be interpreted in accordance with the understandings and representations made between the president and the Senate, and a second prohibits the treaty from being enforced in a manner that would contravene the U.S. Constitution. S. COMM. ON FOREIGN RELATIONS, 106TH CONG., TREATIES AND OTHER INTERNATIONAL AGREEMENTS: THE ROLE OF THE UNITED STATES SENATE 128–31 (Comm. Print 2001). Once the treaty is reported, it is rewritten as a resolution for ratification and, upon motion to enter into executive session, becomes the business on the floor. *Id.* at 137.

28. S. Res. 285.

29. *Id.* at 140.

and when tax treaties are approved by the Senate Foreign Relations Committee, the Committee Chair requests unanimous consent of the Senate that the full Senate move to a vote on the agreement. Failure to achieve that consent on a move to a vote would set in motion potentially significant delays in Senate consideration of the treaty.

B. U.S. Tax Treaty Failure

In 2011 the basic Senate treaty process became the stage on which a tax-treaty battle erupted. The story began, however, in September 2009 when the United States and Switzerland negotiated a protocol to their existing 1996 tax treaty. The protocol sought to amend the treaty to provide for more robust exchange of tax information between the two countries. The negotiation itself resulted from the banking scandals of 2007 and 2008. Pursuant to the ratification process, the president of the United States submitted the Swiss treaty protocol (which had been ratified by the Swiss Parliament in June 2010) to the Senate in January 2011.³⁰ The Senate Foreign Relations Committee then approved the protocol³¹ and it was reported to the full Senate on July 26, 2011.³²

As the Swiss protocol was moving through the ratification process, Senator Rand Paul (R-KY) was elected in fall 2010 (with the support of a group referred to as the “Tea Party”³³) and took his seat in the Senate in January 2011. In late 2011 Senator Paul exercised a privilege to postpone the vote on the Swiss treaty protocol. Senator Paul couched his objection to the treaty protocol in constitutional terms. Specifically, he contended that a citizen’s right to privacy in his or her banking data under the Fourth Amendment would be violated by the provisions. Additionally, he asserted that disclosure of U.S. taxpayers’ financial

30. Protocol Amending Tax Convention with Swiss Confederation, Switz.-U.S., Jan. 26, 2011, S. TREATY DOC. No. 112-1 (2011), <http://www.foreign.senate.gov/imo/media/doc/treaty112-1.pdf>.

31. In June 2011 the Treasury Department strongly recommended that the Senate pass the protocol in hearings before the Senate Foreign Affairs Committee. *Treaties: Hearing Before the S. Comm. on Foreign Relations*, 112th Cong. (2011) (statement of Manal Corwin, Treasury Deputy Assistant Secretary).

32. Jason R. Connery et al., *Current Status of U.S. Tax Treaties and International Agreements*, 42 TAX MGMT. INT’L J. 638, 641 (2013).

33. *See infra* note 121.

data to Switzerland over taxpayer objections violated the due process rights of the affected taxpayer.³⁴ Such Senate opposition is uncharacteristic of tax treaty ratification, which usually occurs without incident.³⁵

Senator Paul's opposition to the tax treaty was coupled with his opposition to a domestic legislative regime, the Foreign Account Tax Compliance Act³⁶ (FATCA), which was enacted in 2010. He also considered this regime an unconstitutional breach of privacy.³⁷ The FATCA regime sought to elicit the cooperation of foreign banks in aiding U.S. efforts to identify unreported offshore financial assets and accounts of U.S. taxpayers. Motivating foreign bank cooperation was FATCA's imposition of new withholding taxes on noncompliant foreign financial entities.

Ultimately, due to Senator Paul's opposition, the resolution regarding the Swiss treaty protocol was not brought before the Senate meeting in executive session and was returned to the Senate Foreign Relations Committee at the end of the 112th Congress in January 2013.³⁸ Senator Paul blocked subsequent

34. David Voreacos & Richard Rubin, *Rand Paul Seeks to Block Tax Treaty Change on Swiss Accounts*, BLOOMBERG NEWS (Apr. 29, 2012), <http://www.bloomberg.com/news/articles/2012-04-29/rand-paul-seeks-to-block-tax-treaty-change-on-swiss-accounts>.

35. The tax and business communities understand that tax treaties and tax information exchange agreements are beneficial in promoting international information flows. They even recognize that information exchange can sometimes be considered in the best interests of businesses seeking to avoid negative international attention resulting from litigation, such as the case against Union Bank of Switzerland. See Patrick Driessen, *Is There a Tax Treaty Insularity Complex?*, 135 TAX NOTES 745 (2012).

36. In an effort to "encourage" third parties (particularly financial entities) to share information with the United States, Congress passed domestic legislation that imposes a withholding tax on investments held by foreign financial institutions (a specially defined term) unless they have previously complied with the new statutory requirements to provide specified financial, account, and asset information about third parties.

37. Rand Paul, *Limiting Foreign Access to Your Bank Accounts*, INV.'S BUS. DAILY (May 17, 2013), <http://www.investors.com/politics/perspective/limit-for-foreign-access-to-your-bank-accounts/>.

38. See, e.g., Kristen A. Parillo, *U.S. Senate Committee Works to Resolve Treaty Impasse with Rand Paul*, WORLDWIDE TAX DAILY (July 10, 2015), <http://www.taxnotes.com/worldwide-tax-daily/treaties/us-senate-committee-works-resolve-treaty-impasse-rand-paul/2015/07/10/14908816>; Marie Sapirie, *The Case for Optimism About Mandatory Arbitration*, WORLDWIDE TAX DAILY (July 14, 2015), <http://www.taxnotes.com/worldwide-tax-daily/treaties/news-analysis-case-optimism-about-mandatory-arbitration/2015/07/14/14912041>;

tax treaties and protocols with similar exchange of information provisions (such as those with Luxembourg, Hungary, and Chile) from a Senate vote.³⁹ Business groups within and outside the United States sought to prompt Senate action on these treaties, but Senator Paul refused to negotiate with the treaty's proponents, stating that only fundamental alterations to the information-sharing provisions in the treaty would cause him to withdraw his objection.⁴⁰

In the event that one senator seeks to keep debate on a treaty open and thereby delay a vote, there is a counterresponse available to other senators: "cloture." This process may be invoked to end debate on an advice and consent matter and bring it to a vote. Under Senate Rule XXII, a vote of sixty senators can force debate to end, despite filibuster efforts by other senators.⁴¹ The motion to invoke cloture requires the bill called into question to be treated as the sole business on the floor, subject to an additional thirty hours of further debate.⁴² Although no senator may speak for more than one hour, and any further proposed amendments must be germane, the Senate may not conduct any other business during that time.⁴³ If, on the other hand, cloture is not invoked and the resolution of ratification is not approved before the end of the Congressional session, then the treaty or protocol is returned to Senate Foreign Relations Committee (i.e., the Swiss protocol in January 2013), and the process must begin again as if no proceedings had taken place.⁴⁴ The time commitment required for cloture means that if a senator makes a convincing threat that he or she will object to a request for unanimous consent to bring a treaty to full Senate vote, then the Senate may be unlikely to press for discussion and vote.

Protocol Amending Tax Convention with Swiss Confederation, CONGRESS.GOV, <https://www.congress.gov/treaty-document/112th-congress/00001> (last visited July 31, 2016).

39. Voreacos & Rubin, *supra* note 34.

40. Patrick Temple-West, *Senator Paul Stirs Business Ire Over Blocking of Tax Treaties*, CHI. TRIB. (Apr. 28, 2013), http://articles.chicagotribune.com/2013-04-28/business/chi-rand-paul-tax-treaties-20130428_1_treaties-senator-rand-paul-fatca.

41. S. Res. 285, 113th Cong. art. XXII (revised on Jan. 24, 2013), <https://www.gpo.gov/fdsys/pkg/CDOC-113sdoc18/pdf/CDOC-113sdoc18.pdf>.

42. *Id.*

43. *Id.*

44. *Id.* art. XXX.

Further insight into the implications of the Senate procedural rules is gleaned as a result of another failed effort to secure ratification of pending tax treaties in spring 2014. On April 1, 2014, the Senate Foreign Relations Committee approved five tax treaties or protocols.⁴⁵ Later, on May 7, 2014, Senator Paul sent a letter to the Senate Majority Leader Harry Reid expressing his disapproval of the exchange-of-information provisions in the treaties. He argued that the new terms might facilitate implementation of the FATCA rules.⁴⁶ Senator Paul further stated: "I will object to any unanimous consent request, motion, or waiver of any rule in relation to these treaties or any related measure."⁴⁷ Despite this renewed commitment by Senator Paul (and perhaps frustrated by the multiyear delay in tax treaty approvals), on May 22, 2014, Senate Foreign Relations Committee Chairman Robert Menendez decided to ask for unanimous consent that the full Senate move to a vote on the Swiss treaty protocol. Senator Paul, as promised, objected to the action.⁴⁸ It was subsequently reported that during a June 19, 2014 hearing on tax treaties, Chairman Menendez reflected on the practical impact of Senator Paul's refusal to allow by unanimous consent a treaty vote:

The problem is that we have to bring up each treaty individually on the floor with full time for debate when these treaties used to go by unanimous consent It's going to be very difficult to get time on the Senate floor to go through an elaborate process of a debate.⁴⁹

That is, for the Senate to counter Senator Paul's veto with cloture, the Senate had to be willing to commit significant time and resources.⁵⁰ Given the limits on Senate time and the competing business on its calendar, cloture was unlikely:

45. See S. REP. NO. 114-78, at 7 (2015).

46. Letter from Rand Paul, U.S. Senator, to Harry Reid, Senate Majority Leader (May 7, 2014), reprinted in *Tax Treaties Violate Taxpayer Privacy*, WORLDWIDE TAX DAILY (May 9, 2014), <http://www.taxnotes.com/worldwide-tax-daily/legislative-tax-issues/tax-treaties-violate-taxpayer-privacy-us-senator-says/2014/05/09/218986>.

47. *Id.*

48. Alison Bennett, *Paul Blocks Effort by Foreign Relations Chief to Move Ratification of U.S.-Swiss Treaty*, DAILY TAX REP., May 27, 2014, at G-2.

49. See, e.g., Drew Singer, *Sen. Menendez Predicts Slow Progress on Tax Treaties*, LAW360 (June 20, 2014), <http://www.law360.com/articles/549776/sen-menendez-predicts-slow-progress-on-tax-treaties>.

50. Given the rules, Senator Paul could force the Senate to consider each treaty or protocol separately, leading to nearly a month of floor time before all

Considering the time frame left before the Senate having to deal with appropriation process to make sure the fiscal year is fully appropriated for, issues of current events that happen across the globe that sometimes rivet our attention—like Iraq, where many of our members are on the floor talking about what the U.S. should do—and nominations for both judges and ambassadorships, it is going to be very difficult to get time on the Senate floor to go through the elaborate process of a debate.⁵¹

Thus, although a single senator's power to block legislation may seem adequately counterbalanced by the option of cloture, the practical realities of pursuing cloture limit its effectiveness. Tax treaties, which apply only to cross-border taxpayers, were unlikely to have been a priority issue for most U.S. voters.⁵² When the treaties were sent back to the Senate Foreign Relations Committee, other more controversial matters and treaties occupied the forefront of foreign policy discussions, most notably the U.N. Arms Trade Treaty and the conflict in Syria.⁵³

Despite the absence of support for cloture, key government bodies attempted to persuade Senator Paul to drop his opposition. The U.S. State Department strongly criticized Senator Paul's refusal to negotiate on the treaty. With the United States being a major proponent of expanded information exchange and the government negotiating agreements with several governments, both under the umbrella of FATCA and as stand-alone treaties, the inability of the United States to meet its own commitments due to the treaties' stalling in the Senate weakened its bargaining position.⁵⁴ While ratification has been pending, the Internal Revenue Service (IRS) has continued to use existing tax treaties to support requests for taxpayer information from the

treaties currently stalled could be passed. See S. COMM. ON FOREIGN RELATIONS, 106TH CONG., TREATIES AND OTHER INTERNATIONAL AGREEMENTS: THE ROLE OF THE UNITED STATES SENATE 142–43 (Comm. Print 2001).

51. See, e.g., Singer, *supra* note 49.

52. See Driessen, *supra* note 35.

53. Paul Eckert et al., *John Kerry to Sign U.N. Arms Treaty: Diplomats*, HUFFINGTON POST (Sept. 24, 2013), http://www.huffingtonpost.com/2013/09/24/john-kerry-un-arms-treaty_n_3983318.html.

54. See Voreacos & Rubin, *supra* note 34.

Swiss government. But, approval of the expanded tax treaty protocol would improve the ability of the IRS to request information.⁵⁵

Beyond the government, business groups also lobbied Senator Paul in an attempt to get him to drop his hold on the vote. Lobbying groups for U.S. businesses (including the U.S. Chamber of Commerce and the National Foreign Trade Council)⁵⁶ stressed the historic role of tax treaties, noting that treaties promote international investment by allowing companies to operate overseas free from fear of double taxation and by facilitating smooth dispute resolution between taxpayers and various tax jurisdictions. Moreover, although the Swiss protocol and other stalled tax treaties included information exchange provisions, their ratification was supported by the business community. Exchange-of-information provisions are valuable to businesses that are seeking an alternative to the burdensome FATCA withholding tax regime. Under FATCA, withholding can be avoided if foreign governments and financial institutions allow exchange of information (but that possibility can depend on the treaty in place).⁵⁷

Foreign businesses also expressed support for the tax treaties by lobbying together under the Organization for International Investment.⁵⁸ Foreign businesses generally support tax treaties

55. See Kristen A. Parillo & Marie Sapirie, *IRS Submits Treaty Request to Switzerland on Credit Suisse Data*, 136 TAX NOTES 770 (2012), http://www.capdale.com/files/7393_ARTICLE%20IRS%20Submits%20Treaty%20Request%20to%20Switzerland%20on%20Credit%20Suisse%20Data.pdf.

56. See, e.g., Letter from Information Technology Industry Council, National Association of Manufacturers, National Foreign Trade Council, Organization for International Investment, Software Finance & Tax Executives Council, TechAmerica, Trans-Atlantic Business Council, U.S. Chamber of Commerce, United States Council for International Business, to Bob Corker, U.S. Senator (July 11, 2013) [hereinafter Letter to Senator Corker], <http://www.ofii.org/sites/default/files/Tax%20Treaty%20Coalition%20Letter%20July%202013.pdf> (regarding the Senate Foreign Relations Committee and the need to approve the pending tax protocols and treaties).

57. See *Automatic Response: The Way to Make Exchange of Tax Information Work*, ECONOMIST (Feb. 16, 2013), <http://www.economist.com/news/special-report/21571561-way-make-exchange-tax-information-work-automatic-response>.

58. See Temple-West, *supra* note 40.

in order to avoid excessive taxation and discriminatory treatment by foreign governments,⁵⁹ but foreign companies and financial institutions are also aware of mounting U.S. pressure to release financial information to tax authorities. For example, in late 2011 (the same year Senator Paul first blocked the treaties) ten Swiss banks acceded to U.S. pressure to provide client financial information in order to avoid the publicity associated with prosecution in U.S. courts.⁶⁰ It is likely that businesses are eager to see ratification of the treaty in order to facilitate solutions that bypass public investigations, to update rules and procedures, and to coordinate emerging tax-reporting obligations.

The appeals by business groups to Senator Paul and libertarian organizations, such as the Cato Institute, have failed to gain traction. Senator Paul's opposition focuses on the information-sharing provisions of the treaties, which he claims violate individuals' privacy rights in their banking records. He contends that his position defends individual rights from infringement by big government and big business, a stance lauded by the Cato Institute. The business community has been unable to convince Senator Paul that the benefits of the tax treaty outweigh his expressed concerns for individual rights.⁶¹ Offering additional grounds for objecting to the treaties, the Cato Institute has questioned the confidentiality of information obtained by tax authorities, suggesting it may be leaked or misappropriated by foreign regimes.⁶² Ironically, the traditionally noncontroversial nature of double taxation treaties may now be impeding ratification. Senator Paul's move has not drawn widespread general media attention because tax treaties have not been a matter of much debate and have generally been approved without objection after referral to the Senate for a vote.⁶³ The average individual taxpayer is unlikely to be impacted by either ratification or nonratification of the Swiss treaty protocol (at least in the short term).

59. See Org. for Int'l Inv., *The Purpose and Scope of U.S. Tax Treaties*, OFII.ORG, http://www.ofii.org/sites/default/files/docs/Background_on_Tax_Treaties.pdf (last visited July 31, 2016).

60. Randall Jackson, *Swiss Banks Turn Over Encrypted Data to U.S. Officials*, WORLDWIDE TAX DAILY (Feb. 1, 2012), <http://www.taxnotes.com/worldwide-tax-daily/2012-02-01>.

61. See Temple-West, *supra* note 40.

62. Richard W. Rahn, *Rise of the Global Tax Collectors*, CATO INST. (July 9, 2012), <http://www.cato.org/publications/commentary/rise-global-tax-collectors>.

63. See Driessen, *supra* note 35.

Thus, private individuals have not been active in convincing Senator Paul to change his position.

Paradoxically, the Cato Institute has framed its opposition to tax treaty information exchange as part of its pro-business stance, despite support for tax treaties from prominent business groups. Cato Institute fellows argue that international efforts to “plug holes” in the tax base, such as information sharing and formulary apportionment, allow countries to manipulate their tax codes to maximize the income taxable under their respective regimes.⁶⁴ If higher-tax countries are able to reach assets in lower-tax jurisdictions (by virtue of more effective information sharing), lower-tax jurisdictions will lose their incentive to keep rates low, and the resulting rise in rates will subsequently impede foreign investment by multinationals.⁶⁵

In early summer 2015 Senate Foreign Relations Committee Chairman Bob Corker conferred with Senator Paul in an attempt to move several pending tax treaties toward ratification.⁶⁶ In commenting to reporters, Corker acknowledged that the committee appreciated the importance of resolving the issue, but that he “couldn’t give an exact deadline” on the discussion.⁶⁷ Observers remained skeptical that the issue would be resolved expeditiously.⁶⁸

Days after Corker’s statement, Senator Paul showed that he would not back down. In July 2015⁶⁹ he filed a lawsuit challenging the constitutionality of FATCA.⁷⁰ Senator Paul and six other

64. See, e.g., Daniel J. Mitchell, *OECD Scheme to Boost Taxes on Business Sector Will Hurt Global Economy and Enable Bigger Government*, CATO INST. (June 9, 2015), <http://www.cato.org/blog/oeed-scheme-boost-taxes-business-sector-will-hurt-global-economy-enable-bigger-government>.

65. Daniel Mitchell, *OECD Launches New Effort to Undermine Tax Competition*, CATO INST. TAX & BUDGET BULL. (Mar. 2013), http://www.cato.org/sites/cato.org/files/pubs/pdf/tbb_68.pdf.

66. Parillo, *supra* note 38. On July 9, 2015, Corker indicated that in the six weeks of prior discussion between Senator Paul and the committee staff the two sides did not address any potential solutions discussed by the parties.

67. *Id.*

68. See Kristen A. Parillo, *U.S. and Vietnam Sign Tax Treaty*, 79 TAX NOTES INT’L 110 (2015).

69. *Crawford v. U.S. Dep’t of Treasury*, 2015 WL 5697552, at *1 (S.D. Ohio Sept. 29, 2015).

70. See William R. Davis & Andrew Velarde, *Sen. Paul Files Lawsuit Challenging FATCA*, 79 TAX NOTES INT’L 110 (2015); *Senator Rand Paul to Sue IRS, U.S. Treasury*, WASH. TIMES (June 24, 2015), <http://www.washington-times.com/news/2015/jun/24/sen-rand-paul-sue-irs-us-treasury/>.

plaintiffs argued that “FATCA eschews the privacy rights enshrined in the Bill of Rights in favor of efficiency and compliance by requiring institutions to report citizens’ account information to the IRS even when the IRS has no reason to suspect that a particular taxpayer is violating the tax laws.”⁷¹ The petition sought to strike several key provisions of FATCA, contending they infringe upon the Fourth, Fifth, and Eighth Amendments to the U.S. Constitution.⁷² Additionally, the plaintiffs filed for a preliminary injunction to bar enforcement of FATCA and foreign bank reporting.⁷³

On September 29, 2015, the U.S. District Court for the Southern District of Ohio denied the request for a preliminary injunction, finding that the parties lacked standing and, thus, likely would be unsuccessful on the merits.⁷⁴ The District Court also reasoned that the U.S. Constitution does not recognize a right to privacy in bank records.⁷⁵ The court further commented that the public had an interest in continued enforcement of the disclosure provisions at issue due to the importance of encouraging tax compliance and combatting tax evasion.⁷⁶

From the time Senator Paul entered the Senate and objected to the Swiss protocol (and all subsequent tax treaties and protocols that contained exchange-of-information language) through November 2015, a total of nine U.S. tax treaties and protocols were blocked from moving through the Senate (ranging from the 2009 proposed protocol to the Luxembourg-U.S. treaty to the 2015 proposed Vietnam-U.S. treaty).⁷⁷

71. See, e.g., Davis & Velarde, *supra* note 70; see also Sapirie, *supra* note 39 (quoting former U.S. Treasury International Tax Counsel, H. David Rosenbloom).

72. *Id.*

73. *Crawford*, 2015 WL 5697552.

74. *Id.*

75. *Id.*

76. *Id.*

77. The pending treaties include: (1) a proposed protocol to the 1996 Luxembourg-U.S. treaty, signed in 2009; (2) a proposed protocol to the 1996 Switzerland-U.S. treaty, signed in 2009; (3) a proposed new Hungary-U.S. treaty, signed in 2010; (4) a proposed new Chile-U.S. treaty, signed in 2010; (5) a proposed protocol to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, signed in 2010; (6) a proposed protocol to the 1990 Spain-U.S. treaty, signed in 2013; (7) a proposed new Poland-U.S. treaty, signed in 2013; (8) a proposed protocol to the 2003 Japan-U.S. treaty, signed in 2013; and, (9) a proposed Vietnam-U.S. treaty, signed in 2015. See Parillo, *supra* note 38.

Signs of a possible breakthrough came in November 2015 when the Senate Foreign Relations Committee gave its approval of eight pending treaties and protocols (Chile, Hungary, Japan, Luxembourg, Poland, Spain, Switzerland, and the Multilateral Convention on Mutual Administrative Assistance in Tax Matters).⁷⁸ Prior to the vote on October 29, 2015, the U.S. Deputy Assistant Secretary (International Tax Affairs) Robert Stack spoke at a hearing held by the Senate Foreign Relations Committee.⁷⁹ Stack argued that the tax treaties needed to be approved in order to protect U.S. multinationals from double taxation, to respond to tax evasion and maintain U.S. credibility, and to establish the United States as a leader in international taxation.⁸⁰ Although these observations were not new (and businesses had been lobbying Senator Paul to retract his objections),⁸¹ commentators considered Stack's remarks at this hearing a precursor that set the stage for the Senate Foreign Relations Committee's decision to approve the treaties and move them on to the Senate for advice and consent.⁸² Observers, however, still questioned whether Senator Paul, who had not announced a change in his position, would seek to filibuster the agreements if and when they were brought to the full Senate for a vote.⁸³ As of the date of this publication, there has been no further movement on the tax treaties. In April 2016, however, the

78. See, e.g., Patricia Zengerle, *Senate Panel Approves Eight International Tax Treaties*, REUTERS (Nov. 10, 2015), <http://www.reuters.com/article/us-usa-tax-treaties-idUSKCNOSZ1YD20151110>.

79. *Treaties: Hearing Before the S. Comm. On Foreign Relations*, 114th Cong. (2015) (opening statement of Robert B. Stack, Treasury Deputy Assistant Secretary (International Tax Affairs)), http://www.foreign.senate.gov/imo/media/doc/102915_Stack_Testimony.pdf.

80. *Id.*

81. See Temple-West, *supra* note 40; *The Ratification of Income Tax Treaties and Protocols: Hearing Before the S. Comm. On Foreign Relations*, 113th Cong., (2014) (statement of Catherine Schultz, Vice President for Tax Policy, National Foreign Trade Council), http://www.foreign.senate.gov/imo/media/doc/Schultz_Testimony.pdf.

82. See generally Ryan Finley, *Pending Tax Treaties Clear U.S. Senate Foreign Relations Committee*, TAX NOTES TODAY (Nov. 11, 2015), <http://www.taxnotes.com/tax-notes-today/treaties/pending-tax-treaties-clear-senate-foreign-relations-committee/2015/11/11/17748591>.

83. Ryan Finley & William Hoke, *Tax Treaty Instruments Awaiting U.S. Senate Vote Face Uncertain Future*, TAX NOTES TODAY (Nov. 12, 2015), <http://www.taxnotes.com/tax-notes-today/treaties/pending-tax-treaties-clear-senate-foreign-relations-committee/2015/11/11/17748591>.

U.S. District Court for the Southern District of Ohio dismissed Senator Paul's case challenging FATCA and related information-sharing measures for lack of jurisdiction.⁸⁴

II. DOMESTIC POLITICS IN INTERNATIONAL RELATIONS—A THEORETICAL PERSPECTIVE

Although the U.S. experience with a single senator's efforts to stop tax treaties may be interesting, it becomes useful when set against the larger backdrop of international relations theory. The story provides a valuable way to distill more general questions, concerns, and observations from this specific example. Ultimately, a more in-depth examination of international relations theory will be needed to generate a comprehensive picture of when and why international tax agreements fail or succeed at home. But, for purposes of this article, gaining a preliminary understanding of key features of international relations theory is appropriate.

A. *International Relations Theory—an Overview*

A predominant focus of the rich international relations literature is explaining and predicting why, when, and how nations cooperate. Before examining the theoretical place of domestic politics in international relations and the analysis of cooperation, it is essential to have an overview of international relations theory and its work on cooperation. Historically, two major theoretical traditions have shaped the analysis of international cooperative behavior: neorealism and neoliberalism.⁸⁵ Typically, neorealism has emphasized four key elements:

- (1) the state as the central (and rational) actor in the international arena;
- (2) the state's desire to achieve relative gains over other states (thus the attention to the balance of power);
- (3) the

84. *Crawford v. U.S. Dep't of Treasury*, 2016 WL 1642968, at *1 (S.D. Ohio Apr. 25, 2016).

85. See, e.g., JAMES E. DOUGHERTY & ROBERT L. PFALTZGRAFF, JR., *CONTENTING THEORIES OF INTERNATIONAL RELATIONS: A COMPREHENSIVE SURVEY* 68–69 (5th ed. 2001); Ring, *supra* note 14, at 91–110; Shah M. Tarzi, *The Role of Principles, Norms, and Regimes in World Affairs*, 15 *INT'L J. ON WORLD PEACE*, no. 4, 1998, at 5 (“Neorealism and neoliberalism, the two leading contending interpretations in international politics, incorporate broad conceptions of international order and the organization of the international system.”).

importance of survival of the state in what is an anarchical international society; and (4) the importance of structure in terms of the relationship among units of the international system (that is, the power dynamics).⁸⁶

In short, neorealists see “power” (i.e., securing, maintaining, or lacking power) as the motivation for the decisions, conduct, and relations witnessed in the global environment.⁸⁷

86. Ring, *supra* note 14, at 91; *see also* ARTHUR STEIN, WHY NATIONS COOPERATE 4–7 (1990) (defining realism); Andrew T. Guzman, *International Law: A Compliance Based Theory* 18 (Univ. of Cal. Berkeley, Pub. Law and Legal Theory Research Paper Series, Paper No. 47, 2001), <http://ssrn.com/abstract=260257> (characterizing neorealism as “an outgrowth of classical realism, [which] treats states as unitary actors and the relevant unit in international relations . . . [where] the interests of states are believed to be power and security, and power is considered to be the primary influence on international behavior.”). Neorealism has been described as a theory that draws strong parallels to rational choice theory in microeconomics:

Just as in microeconomic theory, the rational-choice assumption of profit maximization makes it unnecessary to know or even to speculate about the management of a specific firm in the neorealist view, explaining international outcomes does not require any functional differentiation among states or any insight into their particular characteristics. Nor is there any need, from the neorealist perspective, to factor non-state, trans-state, or sub-state actors into a causal account of international outcomes, which is a refinement of some classical realists’ openness to incorporating domestic politics or influential leaders into causal stories. Finally, a neorealist believes it is unnecessary to consider that a state might seek something other than interest defined in terms of power, just as microeconomists do not account for the possibility that a firm might seek to maximize something other than profit, for instance, the happiness of its constituent employees.

Thomas H. Lee, *International Relations Theories and International Law* 4 (Fordham Univ. Sch. of Law Legal Studies Research Paper Series, Paper No. 2606223, 2015), <http://ssrn.com/abstract=2606223>.

87. *See, e.g.*, STEIN, *supra* note 86, at 4–7 (addressing the importance of the balance of power and power dynamics between and among states); Ring, *supra* note 14, at 93 (comparing neorealism and neoliberalism); Walter Carlsnaes, *Foreign Policy*, in HANDBOOK OF INTERNATIONAL RELATIONS 307 (Walter Carlsnaes, Thomas Risse, & Beth A. Simmons eds., 2d ed. 2013); Lee, *supra* note 86, at 4 (contending that “on the neorealist view of world politics, international outcomes are wholly explained by differences in the power possessed by the interacting state units.”); JOYCE P. KAUFMAN, INTRODUCTION TO INTERNATIONAL

Neoliberalism similarly presumes that the state is the primary actor in international relationships but considers the “state’s pursuit of national self-interest in a market-oriented model as a dominant factor in shaping international relations and in determining how successful international institutions can be in directing and modifying international behaviors.”⁸⁸ While it does not reject a role for power, neoliberalism finds more explanatory value in viewing state action as predicated on the pursuit of national self-interest in a world in which information and monitoring costs can block the pursuit of mutually beneficial goals. This neoliberal picture essentially characterizes international agreements as the response to, or intervention in, cases of “market failure.”⁸⁹ Under this vision of international relations, achievement of absolute gains (for example, where both states are better off) is a more important goal, and the achievement of relative gains is a less important one.

In summary, these two dominant theoretical strands offer divergent stories on international cooperation—neorealism contends that states pursue relative advantage (i.e., a good outcome is one that secures relative gains measured in comparison to the other states involved), whereas neoliberalism anticipates that

RELATIONS: THEORY AND PRACTICE 45 (2013) (noting that “the structure of the international system and the distribution of power within it become determining factors in the ways in which states behave.”).

88. Ring, *supra* note 14, at 91; *see also* KAUFMAN, *supra* note 87 (stating that neoliberalism “plac[es] greater emphasis on the role that nonstate actors play in understanding international relations” although neoliberalism “start[s] with the assumption of the state as a unitary actor that will act in its own best interest.”). Another refinement of the power argument in neorealism is found in the vision that neoliberalism appreciates that “soft power is an increasingly important source of power” and that “different actors,” not just “different countries,” are important in the international relations. *See* Mia Mahmudur Rahim, *Who’s Who: Transnational Corporations and Nation States Interface Over the Theoretical Shift into Their Relationship*, 4 *AFR. J. POL. SCI. & INT’L REL.* 195, 196 (2010).

89. *See, e.g.*, STEIN, *supra* note 86, at 7–8 (stating that neoliberalism typically views regimes, i.e., cooperation, as the response of states in their effort to overcome interstate “market failure”); *see also* Ring, *supra* note 14, at 91–93; Michael Tomz, *International Finance*, in *HANDBOOK OF INTERNATIONAL RELATIONS* 698–700 (Walter Carlsnaes, Thomas Risse, & Beth A. Simmons eds., 2d ed. 2013) (reviewing the impact of the market failure-based paradigm in international relations theory); KAUFMAN, *supra* note 87, at 51 (observing that “even in an international system without a single central authority, states will work together cooperatively because it is in their best interests to do so.”).

states seek absolute gains (arrangements that make both states better off).⁹⁰ Eventually, these two dominant perspectives were augmented by two developments in international relations theory: pluralism and cognitivism.

Advocates of pluralism encouraged both neorealists and neoliberalists to pay more attention to the role of nonstate actors in the path and shape of international relations. The pluralist approach does not reject the importance of the state. Rather, pluralism views the virtually exclusive focus on the nation-state as shielding from view other major forces on international relations: individual actors, bureaucracies, nongovernmental agencies, businesses, etc.⁹¹

The other notable development, cognitivism,⁹² emerged from the postmodern international relations literature and the broader work of constructivism.⁹³ Cognitivism serves more as a critique of existing theories than an independent paradigm for international relations. The major complaint of cognitivists is that other theories fail to question the “origins” of states’ identities, goals, and knowledge. Given the centrality of such knowledge in shaping the course of international relations, attention should be directed to how knowledge is developed, controlled, and transmitted.⁹⁴ More precisely, cognitivism is a challenge to the implicit rationale underlying the other theories by

90. See, e.g., Ring, *supra* note 14, at 91.

91. See, e.g., DOUGHERTY & PFALTZGRAFF, *supra* note 85, at 28–34; Peter Willets, *Transnational Actors and International Organizations in Global Politics*, in THE GLOBALIZATION OF WORLD POLITICS: AN INTRODUCTION OF INTERNATIONAL RELATIONS 326–45 (John Baylis, Steve Smith, & Patricia Owens eds., 5th ed. 2011); see also Paul Schiff Berman, *Global Legal Pluralism*, 80 S. CAL. L. REV. 1155, 1159 (2007) (criticizing international law scholars for “emphasizing formal state-to-state relations” and for paying little attention to pluralist literature).

92. Ultimately, cognitivism can be seen as a dimension of the broad postmodern concept of constructivism, where cognitivism is the branch looking at knowledge formation and the development and movement of ideas. See, e.g., DOUGHERTY & PFALTZGRAFF, *supra* note 85, at 166–68.

93. See, e.g., *id.* at 38–40.

94. See, e.g., ANDREAS HASENCLEVER, PETER MAYER, & VOLKER RITBERGER, THEORIES OF INTERNATIONAL REGIMES 136 (1997). See generally RICHARD ECCLESTON, THE DYNAMICS OF GLOBAL GOVERNANCE: THE FINANCIAL CRISIS, THE OECD, AND THE POLITICS OF INTERNATIONAL TAX COOPERATION 45–50 (2012). See also Stephan Haggard & Beth A. Simmons, *Theories of International Regimes*, 41 INT’L ORG. 491, 499 (1987) (offering a comparison between functional theories, which “see regimes as more or less efficient responses to fixed needs”

underscoring the “pervasive ambiguity of reality and consequently emphasiz[ing] factors such as perception, knowledge, and ideology”⁹⁵ in shaping the choices made by states.

Despite the effort in this article to concisely capture the core dimensions of international relations theory, it cannot be emphasized strongly enough that the literature is infinitely more complicated, overlapping, and detailed than what has been described. For example, at certain points in time, and in some contexts, dividing lines blur, and the works of neorealism and neoliberalism become nearly indistinguishable. Further complicating any neat theoretical story are the myriad variations on all of the above theoretical camps and categories, as well as other strands not addressed here. The size of the literature (and literally the books) seeking to encapsulate international relations theory signals the unwieldy nature of any such endeavor. These caveats, however, are not meant to dissuade the reader from the task at hand. The goal is not to tame international relations theory. Rather, the aim is to ascertain the essential parameters of international relations analysis and then determine how to incorporate the “complication” of domestic politics into the picture.

Before proceeding to a consideration of domestic politics, one final facet of international relations theory must be introduced: regime theory. Regime theory is generally viewed as the dimension of international relations theory most specifically focused on the creation, maintenance, and demise of “regimes”⁹⁶—i.e.,

and cognitive theories, which “see them as conditioned by ideology and consensual knowledge and evolving as actors learn.”)

95. Peter Mayer et al., *Regime Theory: State of the Art and Perspectives*, in *REGIME THEORY AND INTERNATIONAL RELATIONS* 409 (Volker Rittberger ed., 1993). For a basic overview of cognitivism, see Ring, *supra* note 14, at 110–12.

96. A commonly used definition of regimes has been offered by Stephen Krasner, who has described regimes as

implicit or explicit principles, norms, rules, and decision-making procedures around which actors’ expectations converge in a given area of international relations. Principles are beliefs of fact, causation, and rectitude. Norms are standards of behavior defined in terms of rights and obligations. Rules are specific prescriptions or proscriptions for action. Decision-making procedures are prevailing practices for making and implementing collective choice.

Stephen Krasner, *Structural Causes and Regime Consequences: Regimes as Intervening Variables*, 36 *INT’L ORG* 185, 186 (1982). For examples of reliance on

the cooperative dimension of international relations. Despite the moniker, regime theory is not a “single theory.” Rather, regime theory operates with the expectation that there are multiple explanatory variables in regime formation. Thus, it draws upon the major strands (neorealism and neoliberalism) along with the refinements and perspectives encouraged by pluralism and constructivism (including cognitivism).⁹⁷

Models of regime formation grounded in neorealism would view regimes and the specific shapes they take as a function of the power-based positions of the parties. Given the centrality of power to this view, the game theory models typically employed by neorealists would differ from those utilized by neoliberals—even where the cooperation in question could potentially also be viewed as a response to market failure (the hallmark explanation of regime formation according to neoliberalism). Thus, for example, “whether one views international tax conflicts as the result of market failure (for example, uncertainty, information needs, and transaction costs) or not, may have a direct bearing on the applicability of neorealist vs. neoliberal regime

the Krasner definition, see Virginia Haufler, *Crossing the Boundary Between Public and Private: International Regimes and Non-State Actors*, in REGIME THEORY AND INTERNATIONAL RELATIONS 96–97 (Volker Rittberger ed., 1993); Robert O. Keohane, *The Analysis of International Regimes: Towards a European-America Research Programme*, in REGIME THEORY AND INTERNATIONAL RELATIONS, 23, 26–27 (Volker Rittberger ed., 1993); TERENCE C. HALLIDAY & GREGORY SHAFFER, TRANSNATIONAL LEGAL ORDERS 16 (2015) (noting Krasner’s “consensus definition of ‘regimes’”); see also HASENCLEVER, MAYER, & RITTBERGER, *supra* note 94, at 8–9. Refinements of Krasner’s definition include some attention to the effectiveness of the regime and compliance, even where such compliance is inconvenient for a state. See Keohane, *supra* note 96, at 27–28, 33.

97. See, e.g., Mayer et al., *supra* note 95, at 413 (stating that scholars envision regime theory grounded in multiple variables whose relevance and reliability as predictive tools will depend on the context of cooperation); ECCLESTON, *supra* note 94, at 40–50 (reviewing the contributions of neorealism, neoliberalism, cognitivism, and the role of non-state actors such as the OECD and the IMF). Peter Hass identified four regime-based patterns: (1) neorealist “follow-the-leader,” (2) institutionalism/neoliberalism with bargaining, (3) “follow-the-leader with the influence of epistemic (i.e., knowledge) communities, and (4) bargaining with the influence of epistemic communities. Peter M. Haas, *Epistemic Communities and the Dynamics of International Co-operation*, in REGIME THEORY AND INTERNATIONAL RELATIONS 180–90 (Volker Rittberger ed., 1993).

theories.”⁹⁸ It seems quite plausible that certain issues in international tax may be more aptly characterized as being driven by power (meriting neorealist-based regime analyses and its corresponding game theory models), whereas other issues would be described better as reflecting market failure (and warranting a neoliberalist regime theory approach and the game theory models most reflective of market failure dynamics).

B. *Two-Level Game Theory with Domestic Politics*

The above section offers a high-level overview of the dominant elements of international relations theory and, in particular, its focus on cooperation. Scholars, commentators, and observers, however, have recognized that any effort to fully understand international relations must incorporate the pressures, steps, and influences from the domestic sphere. For example, cognitivists have critiqued neorealism and neoliberalism for their lack of attention to the power and potential role of the domestic arena.

A more comprehensive effort to integrate a state’s domestic processes into the study of international relations, however, came in a 1998 article,⁹⁹ which framed the dynamic as a two-level game. This approach, advocated by Robert Putnam, emerged as an influential way to model the dynamics between domestic politics and international relations. The core insight of the game is that a state engaged in international negotiations is not only engaged in a game on the global level (which is comparable to the game theory models noted above and employed by neorealists and neoliberals seeking to explain cooperation or the lack thereof). A state engaged in international negotiations is simultaneously playing a game at the domestic level. One scholar, Joel Trachtman, offers a vivid picture of the tension created by being a player in both games:

Putnam’s two-level game theory suggest[s] that the role of the national government in international relations is to mediate between two separate “games,” the international game and the

98. Ring, *supra* note 14, at 113.

99. Robert D. Putnam, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, 42 INT’L ORG. 427 (1988); see also Ahmer Tarar, *Constituencies and Preferences in International Bargaining*, 49 J. OF CONFLICT RESOL. 383 (2005) (noting the “seminal” status of Putnam’s article); Kenneth Schultz, *Domestic Politics and International Relations*, in HANDBOOK OF INTERNATIONAL RELATIONS 480–81 (Walter Carlsnaes, Thomas Risse, & Beth A. Simmons eds., 2d ed. 2013).

domestic game: “The unusual complexity of this two-level game is that moves that are rational for a player at one board (such as raising energy prices, conceding territory, or limiting auto imports) may be impolitic for that same player at the other board.”¹⁰⁰

The key is to arrive at a deal that is successful on both levels, especially if domestic ratification or implementation of some type is required in addition to the formal international agreement.¹⁰¹ Variations on this two-game model consider, for example, how different ratification requirements,¹⁰² veto power,¹⁰³ or underlying government forms affect the game.¹⁰⁴

The two-level game perspective can help preview the problem of cooperation versus commitment. “Successful” international relationships seek cooperation between international actors (typically states) symbolized by an “agreement.” But cooperation at the outset has limited value unless accompanied by a credible commitment to comply with the agreement, as reflected in the

100. Joel P. Trachtman, *International Law and Domestic Political Coalitions: The Grand Theory of Compliance with International Law*, 11 CHI. J. INT'L L. 127, 153 (2011).

101. The quest for domestic legitimacy has been characterized as not merely a “political fact,” but also “a reason within a normative order.” Richard Bellamy & Albert Weale, *Political Legitimacy and European Monetary Union: Contracts, Constitutionalism and the Normative Logic of Two-Level Games*, 22 J. EUR. PUB. POL'Y 257, 264 (2015).

102. See Tarar, *supra* note 99, at 292–93; Helen V. Milner & B. Peter Rosendorff, *A Model of the Two-Level Game*, in INTERESTS, INSTITUTIONS, AND INFORMATION: DOMESTIC POLITICS AND INTERNATIONAL RELATIONS 67 (1997).

103. See, e.g., Edward D. Mansfield et al., *Free to Trade: Democracies, Autocracies, and International Trade*, 94 AM. POL. SCI. REV. 305, 308–10 (2000); Christian Adam et al., *It's Not Always About Winning: Domestic Politics and Legal Success in EU Annulment Litigation*, 53 J. COMMON MKT. STUD. 185, 191 (2015) (noting that “where legal disputes affect domestic reform issues in which national governments that are seeking reform encounter strong opposition from effective veto players, negative rulings challenging the legality of existing domestic arrangements can be used as a normative lever in domestic bargaining processes.”). Veto power can be understood to encompass far more than literal veto power within the political structure of a jurisdiction. See, e.g., Jobst Heitzig & Ottmar Edenhofer, *Cap, Insure & Compensate: Domestic Policies and the Ratification of International Environmental Agreements* 3 (Apr. 26, 2015) (unpublished manuscript), <http://ssrn.com/abstract=2256875> (noting the power of various kinds of veto players such as the fossil fuel energy industry).

104. See, e.g., Mansfield et al., *supra* note 103, at 308–10; Robert Pahre, *Endogenous Domestic Institutions in Two-Level Games and Parliamentary Oversight of the European Union*, 41 J. OF CONFLICT RESOL. 147 (1997).

parties' behavior over time.¹⁰⁵ Domestic politics is relevant both in determining the creation and content of an agreement *and* in shaping the degree of state compliance in practice. The precise effect of domestic politics may vary. For example, success at the outset (creation of the agreement) may enhance the likelihood of compliance in the long-term through the mechanism of domestic politics.¹⁰⁶ But, in other cases, subsequent pressures from domestic politics can constrain compliance and, thus, commitment.¹⁰⁷

III. INTERNATIONAL RELATIONS THEORY AND THE DOMESTIC SIDE OF INTERNATIONAL COOPERATION: SOME INITIAL OBSERVATIONS

Building on the existing theoretical framework for international relations outlined in Part II, this Part explores the ways in which such theory can provide a more sophisticated understanding of international tax cooperation. The case study of U.S. tax treaty negotiation offers an opportunity to test the explanatory powers of the various dimensions of international relations theory, in particular the two-level game theory view that recognizes the importance of the domestic level in international cooperation.

A. *International Relations and Domestic Action*

As we begin to unravel the events and forces at work in the U.S. tax treaty ratification story, the theoretical frames detailed above provide valuable insight. For example, in applying neorealist theory to the domestic realm, power remains at the fore-

105. See, e.g., Bellamy & Weale, *supra* note 101, at 263 (contending that states must satisfy two conditions related to their games: "First an international agreement requires 'fair dealing' among states . . . [s]econd, states must ensure the general acceptability of the agreement to their respective peoples and be able to justify their international commitments.").

106. See, e.g., BETH A. SIMMONS, *MOBILIZING FOR HUMAN RIGHTS: INTERNATIONAL LAW IN DOMESTIC POLITICS* (2009) (making this observation based on an example from the human rights context); HELEN V. MILNER, *RESISTING PROTECTIONISM: GLOBAL INDUSTRIES AND THE POLITICS OF INTERNATIONAL RELATIONS* (1988) (offering an example from the trade context). See generally Schultz, *supra* note 99.

107. See, e.g., B. Peter Rosendorff & Helen V. Milner, *The Optimal Design of International Trade Institutions: Uncertainty and Escape*, 55 INT'L ORG. 829, 832-35 (2001).

front of consideration, and the state is the centerpiece of the action. Thus, a key question in thinking about the transition from negotiating a U.S. tax treaty to final implementation is the power of the state not just vis-à-vis other states (as discussed in the general consideration of international relations and regime theory) but vis-à-vis the public and “organized” interest groups.¹⁰⁸ A “strong” state is one that is able to effectively pursue “national policy” (including securing resources and exercising global power on behalf of the nation) unconstrained by domestic politics. Inherent in some of these formulations is the sense that domestic forces are an intrusion with the potential to derail otherwise desirable state power and policy.¹⁰⁹ The power model seems to require less contemplation of state interests and state goals (and perhaps places less value on domestic forces) because the end game is acquiring power and preserving sovereignty and autonomy.

The neoliberal tradition—which envisions the global arena as one in which states pursue cooperative behavior to manage informational uncertainties due to market failure—pays more attention to *which* interests the state ultimately pursues. In that regard, domestic forces become a more central part of the account rather than a distraction from the state’s business at hand. All the players (i.e., political leaders, agencies, and interest groups) are expected to have “interests,” and the question becomes how the multitude of interests coalesce into a national position pursued by the state at the global level.

In the case of U.S. tax treaties, which of these two dominant visions of international relations theory might be more persuasive in grounding our understanding of the dynamics? A power-based story, which focuses on the relative positioning of countries, may offer insight into the support for Senator Paul’s obstruction of the treaty process in the Senate. In contrast, the support of U.S. tax treaties from the business community suggests that they perceive the situation as one in which international agreement provides an efficient solution to certain tax coordination issues—a view more consistent with neoliberalism. For example, a letter from multiple business and trade groups urging approval of the blocked treaties argued: “Tax treaties

108. See, e.g., Schultz, *supra* note 99; Michael Mastanduno et al., *Toward a Realist Theory of State Action*, 33 INT’L STUD. Q. 457 (1989); see also *infra* text accompanying notes 117–118.

109. Schultz, *supra* note 99 (observing this feature in the realist tradition).

help the U.S. economy by allowing U.S. companies to more efficiently conduct their businesses abroad and by making the U.S. more hospitable to foreign investment, which creates and sustains millions of American jobs.”¹¹⁰ The difficulty in isolating a dominant vision of international relations in this context may reflect the fact that the debate over the treaties taking place at the domestic level involves a disagreement over what values should drive U.S. tax policy-making power or efficiency.

Moreover, the constructivist branch of postmodern international relations theory from which cognitivism emerged¹¹¹ not only rejects the idea that the goals of the state are clear (arguably a view supported by neorealists) but also challenges the neoliberalist suggestion that domestic politics is merely the venue in which the state’s positions are formed in the face of competing interests (such as those espoused by Senator Paul and by the opposing business and trade groups) and interest groups. Rather, the constructivists believe that more can, and does, take place in the domestic sphere—national identity can be shaped and reshaped here.¹¹² Such identity or vision developed and shared at the domestic level can then have a lasting impact on

110. See Letter to Senator Corker, *supra* note 56.

111. See *supra* text accompanying note 92.

112. See, e.g., Schultz, *supra* note 99. Scholars seeking to place constructivism in a broader context offer an overview explanation:

Constructivist scholars reject the dominant assumption of contemporary I[n]ternational R[elations] theory that the interests of states and other actors are formed prior to social interaction. Instead, constructivists claim that identity formation is relational and occurs before, or at least concurrently with, interest formation. Interests are therefore defined both in material and non-material terms. While acknowledging the importance of power and material interests, constructivists focus attention upon the role that culture, ideas, institutions, discourse, and social norms play in shaping identity and influencing behaviour. For this reason, constructivist thought is especially compelling when seeking to explain the constitution of actors, institutions and social structures, and their change over considerable periods of time. (Citations omitted)

Jutta Brunnée & Stephen J. Toope, *Constructivism and International Law*, in *INTERDISCIPLINARY PERSPECTIVES ON INTERNATIONAL LAW AND INTERNATIONAL RELATIONS* 119 (Jeffrey L. Dunoff & Mark A. Pollack eds., 2013).

state decisions internationally. In the context of the recent U.S. treaty negotiations, an in-depth study would consider the origins of the political rift that resulted in the government negotiating agreements that generated some objection at home. An initial reaction may emphasize the one-off nature of the objections (a single senator), the confluence of a single objecting senator and the intricacies of Senate rules of operation, or the growing domestic political tension about international cooperation. But too much attention to any single explanatory factor may belie the complicated formation of U.S. tax policy. For example, given the frequent characterization of modern U.S. national politics as being driven by big business and big donors, why has Senator Paul been unmoved for many years by the entreaties of the business community that has sought ratification of U.S. treaties? Was the time-consuming cloture technique (for challenging Senator Paul) the only realistic option for other senators who supported the negotiated treaties?

Although the two dominant theoretical threads (neorealism, neoliberalism) and the two refinements (pluralism and cognitivism) differ when applied to domestic politics, there is, nonetheless, a shared conceptual acknowledgement that at some point a state presents itself on the global stage as capable of making agreements. The precise mechanism varies from state to state but always involves the emergence of one individual, or a group of individuals, with the political authority to make decisions on the behalf of the state. It is for this reason that we can speak of domestic politics and international relations as two distinct but highly intertwined spaces.¹¹³ As others have noted, the two spheres interact through the mechanism of “influencing” these key decision makers. The potential for influence is premised on the assumption that these decision makers wish to retain power and status and that their ability to do so depends in part on the acquiescence of others. But, in the process of unraveling the story behind how the decision makers respond to competing goals, claims, and values, the theories diverge, with some emphasizing a “competitive” marketplace of views on international policies in which the most influential domestic groups prevail.¹¹⁴ Others portray decision makers as players who internalize

113. See generally Schultz, *supra* note 99, at 480–81.

114. *Id.* at 480–502.

emerging norms and identities or alternatively as actors who stake out their own paths first and are only disciplined later.¹¹⁵

B. Game Theory and Integration of the International and Domestic Spheres

The primary tools and concepts of international relations study, including neorealism, neoliberalism, and constructivism, were developed in the context of state-to-state relations. When the analysis sought to incorporate the domestic level into the state-to-state frame, the theory needed more—the two-level game model. The model does not replace the ideas of neorealism, neoliberalism, or constructivism. Rather, it shapes the context in which those explanatory frames are explored.

1. Institutional and Structural Features

A dominant starting point for inquiry into the two-level game view of domestic politics and international relations is the institutional structure delineating the actions and powers of the domestic players. The ability of the domestic actors to block completion of an international agreement clearly signals the existence of the two-level game. Perhaps the most significant aspect of the treaty two-level game is the institutional structure prescribing the relationship between the executive and legislative branches.

As a formal matter, the executive (the Treasury Department performs this function for tax) negotiates at the global level in anticipation of satisfying the Senate in the second game (through “advice and consent”). Historically, this resulting two-level game, played sequentially, has progressed predictably.¹¹⁶

115. *Id.*

116. The two levels may typically be sequential as a formal matter, with states negotiating their agreement, which then would be ratified through internal domestic processes. Given established treaty practice (including the U.S. Model Tax treaty and the OECD Model Tax treaty), little risk generally would be anticipated at the second (i.e., domestic) level. It should be noted, though, that in 1995 Senators Bob Dole and Jesse Helms blocked ratification of tax treaties until President Clinton compromised on another unrelated bill. This situation, which differed from the current U.S. treaty blockage in that there was no underlying objection to the tax treaties themselves, emerged after the Senate failed to vote on the State Department Reorganization and Authorization Act. As retaliation, Senate Majority Leader Dole coordinated with Senator Helms, the Chair of the Senate Foreign Relations Committee, to block all tax treaties until the White House acquiesced. A month later, Senator Helms

With the baseline of the U.S. Model Tax treaty and the similar OECD Model treaty, the United States regularly negotiates treaties with other countries with the expectation that the resulting agreement will be ratified domestically in the United States. Thus, tax agreements have been sufficiently consistent and stable to create a presumption that tax treaties and protocols will face no actual challenge in the second level of the game, despite the Senate's formal power.

The U.S. case study of tax treaty blockages involving Senator Paul, the Swiss protocol, and a stalled ratification process turns not just on the institutional structure of the executive and legislation branches delineated in the U.S. Constitution but also on the rules and procedures adopted by the Senate. In the floor vote on the Swiss protocol, Senator Paul had a single vote. But under the current Senate rules he can block a bill unless, and until, others in the Senate invoke cloture. Once Senator Paul blocked the bill, why did others not pursue cloture? Committee Chairman Menendez's June 2014 statement clearly confirms that the combination of insufficient Senate resources to counter Senator Paul and the existence of other items on the Senate's calendar led him to believe that cloture was unrealistic. The Senate would have needed to view the standoff as sufficiently serious to put aside other business and pursue the cloture process, not just on the Swiss protocol but on the other tax treaties and protocols as well.

released seven tax treaties as a show of "good faith," though he continued to delay meetings of the Senate Foreign Relations Committee, effectively holding up all foreign policy legislation requiring Senate approval. *See* John Godfrey, *Dole, Helms Hold U.S. Tax Treaties Hostage*, 11 TAX NOTES INT'L 420 (1995). Perhaps reflecting both the general ease with which tax treaties passed Congress and the lack of any noted objection to the terms of the tax treaties, the business community missed the initial signs of trouble in this 1995 tax treaty hold up:

As of August 4 [three days after the cloture vote failed] most members of the Senate Finance Committee, many industry representatives, and ranking White House and Treasury officials said they had no knowledge of the impasse. A Foreign Relations Committee aide had no explanation, but an industry lobbyist said most affected by the treaties have simply assumed they will pass and have therefore not paid much attention.

Id.

Whether a failure to progress on treaty ratifications generates the level of political interest sufficient to motivate other senators to table pressing matters and pursue cloture depends in part on the structure of the U.S. government as a presidential democracy. In a presidential democracy such as the United States, the popular election of the president occurs independently of the election of members of Congress. Members of Congress are elected individually, and their party affiliations and political perspectives can differ from that of the president, especially in the case of members of Congress who are elected in the middle of a presidential term. As a result, legislators may not be inclined to vote in a manner consistent with the goals of the current executive.¹¹⁷ The gap between the executive branch (in this case the Treasury and the president) and members of the Senate can be difficult to curb in the presidential system. When combined with the procedural power of individual senators, the result is a stalled protocol.¹¹⁸ Despite the importance of tax information sharing and the public discussion of individual tax evaders and multinationals engaged in tax avoidance, the Senate calendar has been occupied by other pressing debates.

The problem can be more generally stated as a challenge faced by democracies with potentially strong veto players. In a paper by Betz and Hanif considering the two-level game and India's domestic and foreign energy policy, the authors observed that the core of the two-level game imposes on governments the need to "reconcile" the competing domestic and international forces in an effort to establish and implement policy.¹¹⁹ But this task is complicated in a democracy:

117. See, e.g., Schultz, *supra* note 99, at 492 ("Presidential democracies are more likely than parliamentary democracies to produce legislatures in which the median voter has different preferences from the executive.").

118. In the context of the 1995 treaty blockage, the impasse was clearly understood as a direct battle between the policy goals of the executive branch and the goals of some senators in the opposing political party. See, e.g., Godfrey, *supra* note 116 ("Senate Finance Trade Subcommittee Chair Charles E. Grassley, R- Iowa, said he knew of Helms's decision and fully supported it. The president has decided to block Republican efforts to reorganize the State Department, so he can pay the consequences.").

119. Joachim Betz & Melanie Hanif, *The Formation of Preferences in Two-level Games: An Analysis of India's Domestic and Foreign Energy Policy* 6 (Ger. Inst. of Glob. and Area Studies, Working Paper No. 142, 2010), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1670627.

Domestic power polarity, that is, the government's domination of society vis a vis societal groups and forces, is obviously less favorable for the government in democracies and federal systems, particularly when the interplay of governmental and electoral systems tends to produce fragmented parliaments and executives.¹²⁰

A significant gap does not always exist between the executive branch and the legislature, but when it does, the reality of two levels of the international tax relations "game" becomes profoundly apparent.

2. Changing Political Forces

A related and important part of the U.S. treaty story involved a changing political landscape, which can occur faster on an individual state level than on the presidential/executive branch level. In 2009 and 2010 the Tea Party rose to relative prominence in the United States.¹²¹ Perhaps best characterized as a decentralized movement coalescing around a mix of socially conservative and "small government" views (reduction of the national debt, decreased national spending, and reduction in taxes), the Tea Party supported Rand Paul when he won his Senate seat in 2010. During his time in the Senate, Senator Paul has continued to espouse what he has described as "libertarian" views.¹²² To date, however, Senator Paul's statements, actions, and ideologies have created domestic discord. The combination of Senator Paul's decision to block the treaty protocol and the gap that exists between his political views (including what could be described as his principles regarding the relationship between the government and taxpayers) and those of the executive branch (and much of the Senate) have all contributed to the dis-

120. *Id.*

121. See, e.g., *Tea Party: Evolution of a Revolt*, WASH. POST, <http://www.washingtonpost.com/wp-srv/metro/teaparty> (last visited Aug. 2, 2016); *Timeline: The Tea Party's Path to Power*, CNN POLITICS, <http://www.cnn.com/2010/POLITICS/10/25/tea.party.timeline/index.html> (last visited Aug. 2, 2016); *About Us*, TEAPARTY.ORG, <http://www.teaparty.org/about-us/> (last visited Aug. 2, 2016).

122. See, e.g., *Dr. Rand Paul, the Son of Texas Republican Rep. Ron Paul, Told CNN Monday that He is Seriously Considering a Run for the Senate*, CNN POLITICAL TICKER (May 4, 2009), <http://political-ticker.blogs.cnn.com/2009/05/04/im-very-serious-about-running-ron-pauls-son-says/>.

cord. This discord has produced tangible consequences: with respect to the Swiss protocol, the United States reached an agreement on tax policy goals and specific information exchange language with Switzerland, but has failed to achieve the necessary acceptance at home.

Although Senator Paul's immediate constituency in Kentucky may support his more libertarian Tea Party position on information exchange (to the extent they have considered it), he has faced growing pressure, even from the business community, to change his stance. For example, major U.S. business lobbies, such as the Chamber of Commerce and the National Foreign Trade Council, have reiterated their support for treaty ratification as being crucial to smooth business relations.¹²³ If and when the combination of business pressure and/or the pursuance of cloture becomes sufficiently powerful to pressure Senator Paul to change his stance, this domestic barrier to international agreement could be resolved.

There may be a perception that, although tax treaty matters are important, they are not as crucial as a peace treaty, nor as high profile as some other matters (i.e., certain trade agreements or immigration reform). The United States' inability to ratify the protocols and treaties, however, has generated its own source of momentum for change. As Senator Paul continues to block treaties, the number of treaties stuck in the pipeline has grown. The failure to vote and approve the treaties thus has impacted countries, businesses, and other parties as well.

For that reason, perhaps some viewed the November 2015 movement on tax treaties as promising.¹²⁴ But the treaties have not been brought to the Senate for vote as of the date of this publication. The political influence of the libertarian base does not seem to be rapidly growing such that the executive branch would be likely to shift its position on exchange of information in the near future, nor is Senator Paul losing his voter support. The key to bridging the gap will be interest groups working against the landscape of the Senate rules. What may have been merely a "delay" at the end of 2011 looks considerably more like

123. See, e.g., Letter from Troy K. Lewis, Chair, Tax Exec. Comm., to Bob Corker, Chairman, U.S. Senate Comm. on Foreign Relations, & Robert Menendez, Ranking Member, U.S. Senate Comm. on Foreign Relations (Feb. 3, 2015), <http://www.aicpa.org/advocacy/cpaadvocate/2015/pages/senate-tax-treaty-letter.aspx>.

124. See *supra* notes 78–83.

a serious block to ratification in 2016. Even among interest groups that have always supported ratification, time delay may intensify and solidify their interest in breaking the jam. Finally, it is worth noting that, even if the treaties move successfully through the Senate process in 2016, the block would have lasted approximately five years and would represent a serious example of international agreements “failing at home.”

3. Iterative Dynamic Between Domestic Politics and International Cooperation

Not only does the Senate Foreign Relations Committee stand-off impact those seeking relief under the blocked treaties, the failure to achieve agreement at the domestic level of the game could also impact subsequent U.S. efforts at tax treaty negotiations. Negotiating states have two dominant concerns: cooperation (can we reach a deal) and commitment (will the other party cheat, back out, or fail to respect the deal). The block on U.S. tax treaties renders the first concern paramount—at least where there has been no ratification and entry into force of a U.S. tax treaty over a period of years. Of course, nations may proceed to negotiate with the United States with expectations that the blockage in the Senate will be resolved in the near future and any resulting agreement will be in line for ratification. But, as time progresses without resolution, other states are faced with a choice—should resources be devoted to negotiating a deal with the United States if it is unlikely to be ratified? Finally, there is a risk that diminished credibility, due to the United States’ incapacity to execute *and then* ratify a tax deal, will impair the power and influence that the United States can bring to these deals and will constrain its ability to “encourage” countries to engage in negotiation and information exchange.¹²⁵

125. The United States’ new unilateral domestic legislation requiring information disclosure to the U.S. tax authorities by third parties (the FATCA regime) may have mitigated the negative effects of failed tax treaty ratification. Other countries now have an independent reason to negotiate with the United States regarding information exchange practices. FATCA, however, is not entirely divorced from the treaty process. For example, the Swiss still need the protocol to the Switzerland-U.S. treaty to be ratified in order to fully effectuate their FATCA agreement with the United States. See Temple-West, *supra* note 40; Sandy Fitzgerald, *Rand Paul Not Backing Down on Tax Treaty Fight*, NEWSMAX (May 5, 2013, 4:13 PM), <http://www.newsmax.com/Newsfront/rand-paul-tax-treaty/2013/05/05/id/502854/>.

C. Summary Observations

Although the story of recent treaty blockage in the United States is specific to one country and one domestic failure, it, nonetheless, illuminates a number of valuable takeaways: (1) identifying risk junctures in the domestic side of international agreement requires examination of domestic procedural rules and realistic practices and not just the constitutional or formal roles of the actors; (2) domestic barriers can arise even when the majority of domestic participants support the international agreement; (3) business lobbies can be more limited in their success than might be anticipated in the absence of strong counter lobbies; and (4) domestic stalemate does not necessarily deter subsequent negotiating efforts by other countries, at least to the degree that might be expected.

One question that arises in contemplating the case study is whether countries can find work-arounds when a barrier becomes entrenched. The answer seems to be yes, in some cases.¹²⁶ With regard to bilateral tax treaties and their protocols, a direct work-around has not been possible—these tax treaties have such an established role in the international tax framework that there seemingly has been no movement since 2011 to broadly replace the agreements with something not susceptible to hold up in the Senate.

In a related area, however, the Treasury introduced a new form of international tax agreement that it has executed with

126. An unintentional example of self-help or work-arounds could be the treaty-based portions of the BEPS project. In a recent BEPS article, which contends that the BEPS project has adopted the practices and structure of international finance law for developing and reaching global agreement, Itai Grinberg makes a separate argument regarding when and which BEPS commitments will be successful. He argues that the success of BEPS will vary depending on whether a particular issue is one that concerns bilateral treaties or instead concerns another area of international tax law. Specifically, Grinberg observes that the BEPS commitments that are implemented through the OECD Model treaty effectively will be reflected in most existing bilateral tax treaties *without* further action by the states (due to the relationship among the Model Treaty, bilateral treaties, and judicial interpretation). Thus, the game becomes a one-level game, and once the first game is completed (i.e., the international agreement, here represented by the BEPS Reports and related material), there is no second game that must be played to effectuate compliance. Grinberg, *supra* note 7, at 35–47.

many treaty parties. These new agreements, called Intergovernmental Agreements (“IGAs”),¹²⁷ have been viewed by some commentators as an end run-around the tax treaty process. These agreements were negotiated with treaty parties in an effort to create a smoother mechanism by which foreign financial institutions could satisfy the expectations of the new FATCA regime¹²⁸ (the same regime that Senator Paul sued to bar enforcement). The United States took the position (though some commentators disagreed) that the treaty approval process was inapplicable to IGAs because they were executive agreements.¹²⁹

In terms of international relations analysis, IGAs can be viewed as evidence of the interactive nature of the two-level game. In cases where agreement at the international level *could* be reached but the agreement would encounter significant domestic barriers, the state level negotiators might revisit the arrangement and explore structures and options more likely to survive the second level of the game.

Finally, consideration of the U.S. treaty case against the backdrop of expanding international agreements from BEPS raises an additional complexity. What strategies and nuances do the multilateral aspects of BEPS bring to a two-level game analysis? Of course, the two levels (domestic and international) have certainly included multiple players at the international level when the game has taken place in nontax fields. For example, in trade negotiations, multilateral international agreements are common, thus, the first level game would include multiple jurisdictions. Historically, however, tax treaties have been bilateral

127. See, e.g., *Additional FATCA Documents*, TREASURY.GOV, <https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA-Archive.aspx> (last visited Aug. 2, 2016); *FATCA Information for Governments*, IRS.GOV, <https://www.irs.gov/Businesses/Corporations/FATCA-Governments> (last visited Aug. 2, 2016).

128. See, e.g., Press Release, Statement of Mutual Cooperation and Understanding Between the U.S. Department of the Treasury and the Authorities of Japan to Improve International Tax Compliance and to Facilitate Implementation of FATCA (June 11, 2013), <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Statement-Japan-6-11-2013.pdf> (“FATCA has raised a number of issues, including that Japanese financial institutions may not be able to comply with certain aspects of FATCA due to domestic legal impediments; [w]hereas, intergovernmental cooperation to facilitate FATCA implementation would address these issues and reduce burdens for Japanese financial institutions.”).

129. See, e.g., Allison Christians, *Interpretation or Override? Introducing the Hybrid Tax Agreement*, 80 TAX NOTES INT'L 51 (2015).

(and the agreements that have stalled in the U.S. Senate are bilateral). But, the BEPS project incorporates a range of agreement structures, including multilateral commitment to the BEPS final reports, possible commitment to a multilateral treaty, and implications for bilateral treaties. Analysis of the underlying negotiation dynamics raises the prospect that jurisdictions might make a broad multilateral, international commitment at the first level but at the second (domestic) level of the game implement this global agreement very differently on a country-by-country basis.¹³⁰

CONCLUSION

One might imagine that at the close of this analysis we could reasonably conclude that domestic politics is a bit of a “problem,” a hindrance to achieving the business of promoting and pursuing the state’s interest (arguably neorealism’s unstated view). Certainly, the BEPS project, with its completion of the final reports in 2015, could characterize a state’s inability to follow through with commitments in the BEPS final package as a “problem” created by domestic politics. Following that line of reasoning, perhaps the problem is democracy itself. But that conclusion moves too fast.

Facilitating global cooperation is not the sole national goal of a democracy. Other “goods” result from the democratic process. Moreover, the neoliberal view that “unencumbered” state executives do not inherently pursue “ideal” national policy undermines any quick labeling of the democratic process as a hindrance. Perhaps a better national position can emerge from a public debate among interest groups with competing substantive positions. Finally, although democracies (especially ones unable to control the domestic game) can have difficulty signaling their ability to successfully negotiate an agreement, nondemocracies may have a challenge of their own in credibly committing to a stable outcome over time. Thus, an appreciation for the power of domestic politics to shape international tax agreements is not a call for significant constraints on democracy. But it does demand that we understand when, how, and why domestic politics “intrude” on international agreements. Additionally, it requires that we consider how specific features of a domestic system contribute to the democratic process and to related goals that we

130. See Grinberg, *supra* note 7.

identify. A more sophisticated appreciation of all of these relationships can help anticipate likely outcomes of an agreement, determine when and whether early intervention on the domestic front is appropriate, and assess whether any elements of the domestic institutional infrastructure should be reevaluated in light of their impact on the business of the legislature and the executive branch in the pursuit of international cooperation.