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A multilateral tax treaty: designing an instrument to modernise international tax law

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6 A design strategy for a multilateral agreement for international taxation

6.1 Introduction

So far, we have learned that in their cooperative efforts, states should aim at being 'procedurally fair' (Chapter 4). This requires that deliberations on international tax law are continuous, transparent and inclusive, which, in turn, allows the law-making process to include all relevant moral, social and political perspectives, leading to law that is 'neutral' and hence 'fair'. And indeed, provided that steps are taken one at a time and with care, the amount of participating states may be incrementally increased (see section 5.4.7.1). Moreover, although opening the doors to the negotiations can cause the public to 'measure' bargaining success by setting off negotiation outcomes against publicly known baselines, there is a strong suggestion that transparency enhances cooperation, and transparency may be achieved in varying ways and to varying degrees (see section 5.4.7.2).

We have also learned that there are limits to the substantive rules that can be agreed upon in a multilateral negotiation (Chapter 5). Multilateral agreement is discouraged by the presence of obvious distributive issues. A multilateral agreement for international taxation should therefore leave a good deal of room for accommodating divergent state interests, e.g., by reservations and 'rules of the road'. Disagreement should, so to speak, not be emphasised by precise rules from which parties cannot deviate. But this means that some rules, such as those that make use of formulary apportionment mechanisms, may be politically unfeasible. Therefore, when state action in the tax field continues to be constrained by egocentric rationality and the need to protect the national economic interests, the development of distributive norms of international taxation, whatever their contents may be, is likely to be slow and indeterminate.

In the light of these outcomes, the aim of this chapter is to argue that achieving procedural fairness in international taxation is not only 'the right thing to do', but also indispensable for enabling the international tax regime to continuously adapt and evolve. This resonates well with the normative view set forth in Chapter 4 on 'fair' international tax rules. But it also matches Chapter 5's suggestion that cooperation in the international tax field requires transformative flexibility mechanisms. In the face of uncertainty, states may employ such mechanisms to ensure that the arrangement itself can be changed once further information becomes available. States can, over time, learn more

about the effects and impacts of certain courses of action or inaction and act accordingly. Moreover, a flexibility design would provide states with the ability to tackle issues as they come up. It is, in this light, for instance, not unthinkable that emerging ideas on 'fair share' propel states into further cooperation on international tax matters in the future (i.e., BEPS 2.0, 3.0, 4.0, etc.), much like it did for the 2013 BEPS Project.[1]

So, the most promising strategy for designing a multilateral agreement for international taxation is one in which the multilateral agreement functions as a robust 'managerial' framework that facilitates interaction, enabling the system to progressively transform and develop *over time*.[2] This involves considering the two functions of the multilateral agreement for international taxation set forth in Chapter 3. As follows from Chapter 3, the potential of a multilateral agreement is to facilitate international tax cooperation by: (1) providing a structural solution to swiftly amend bilateral tax relationships, and (2) providing a structural level playing field, so that states can coordinate on addressing collective action problems.

1. *A level playing field.* The multilateral agreement for international taxation requires a level playing field in which states can coordinate on tax policy options necessary to address the collective action problems, such as rule deficiencies associated with tax competition and tax arbitrage. In such terms, states, when entering into the agreement, perceive *ex ante* a management risk *ex post.* How can the multilateral agreement's designers ensure that substantive treaty commitments, over time, evolve and are maintained collectively?
2. *A quicker tax treaty amendment process.* The multilateral agreement for international taxation must be able to enhance the implementation or renegotiation of new norms in bilateral tax treaties. How can this be achieved, given the restraints on cooperation posed by egocentric, rational states acting to protect their self-interests?

Section 6.2 paves the way for the 'managerial' design strategy to international tax cooperation. Section 6.3 then builds up the 'managerial' design strategy using three elements borrowed from neoliberal institutional theory supple-

1 Indeed, ideas on fairness can have a strong influence on cooperative outcomes, see the discussion in section 5.2. See also Keohane, who notes that 'perceptions of self-interest depend both on actors' expectations of the likely consequences that will follow from particular actions and on their fundamental values'. R.O. Keohane (1984), p. 63.

2 See for this approach generally: J. Brunnée and S.J. Toope, *Environmental Security and Freshwater Resources: Ecosystem Regime Building*, 91 American Journal of International Law 26 (1997) and M.P. Cottrell and D.M. Trubek, *Law as Problem Solving: Standards, Networks, Experimentation, and Deliberation in Global Space*, 21 Transnational Law and Contemporary Problems 359 (2012).

mented with constructivist viewpoints.[3] These are: (1) continuous interaction (2) building on shared understandings and (3) the role of legal norms. The combination of these three elements can cause international tax cooperation to deepen over time. By facilitating states to gather expertise and knowledge, by building trust and confidence amongst parties, by providing a forum for continuous interaction, and by streamlining the tax treaty amendment process, states can strengthen initially weak commitments by means of further (bilateral or multilateral) interaction. Section 6.4 illustrates the managerial design strategy by referring to the regime on the very complex, uncertain and as such comparable issue of global warming. Although this regime is not considered very effective, the fact is that an agreement is in place and that progress, albeit slowly, is made.[4] Conclusions are drawn in section 6.5.

6.2 A forum for discussions

6.2.1 The level playing field

Multilateral agreements are often non-committal when it comes to setting binding rules. Such agreements are best regarded as forums for further bargaining on issues collectively accepted as relevant,[5] rather than as systems that punish violations and mandate rules.[6] Indeed, Goldsmith and Posner have argued that:

> 'most multilateral treaties that are not purely hortatory are based on some form of embedded bilateral cooperation. What little genuine multilateral cooperation

3 As argued in section 5.2, the constructivist perspective is seen as complementary to the neoliberal institutional one.

4 The main instrument in this regard is the *United Nations Framework Convention on Climate Change* (adopted 9 May 1992), 1771 UNTS 107. The instrument does not contain binding restrictions on greenhouse gas emissions but rather sets commitments for further cooperation. See e.g. M. Bothe, *The United Nations Framework Convention on Climate Change: An Unprecedented Multilevel Regulatory Challenge*, 63 Zeitschrift für ausländisches öffentliches Recht und Völkerrecht 239 (2003); J.K. Sebenius, *Designing Negotiations Toward a New Regime: The Case of Global Warming*, 15 International Security 110 (1991).

5 J.D. Fearon, *Bargaining, Enforcement, and International Cooperation*, 52 International Organization 269 (1998).

6 Some authors restrict the use of the term 'enforcement' only to situations of treaty breach or non-observance. See C.J. Tams, *Enforcement*, in: Making Treaties Work: Human Rights, Environment and Arms Control (G. Ulfstein ed., Cambridge University Press 2007) p. 393. I, however, use the term in a broader sense, and relate it to the upward delegation of adjudicative as well as (quasi)-legislative authority, by means of which, generally speaking, behaviour can be sanctioned and obligations mandated. See: B. Koremenos (2016); A. Aust, *Modern Treaty Law and Practice* (Cambridge University Press 3d ed. 2013) p. 51.

> we might see is thin, in the sense that it does not require nations to depart much, if at all, from what they would have done in the absence of the treaty'.[7]

While this is a distinctly general kind of observation, the point is that by using multilateralism, states are often unable to achieve more than they would have under bilateral deals or even unilaterally.[8] Under the current system, the OECD produces soft law, which provides a state – member or not – with relative flexibility in reciprocally deciding on its commitments. A state is, at least in theory, relatively free to use or ignore OECD soft law when concluding a tax convention.[9] OECD soft law has, so to speak, influenced tax treaty negotiations 'from the bottom up'. There is little reason to regard a multilateral agreement for international taxation, that would lead states to collectively agree to binding rules, as a more deeply institutionalised system than the one currently in place.

In this light, the delegation of authority to i.e., a legislative or adjudicative body, that can mandate state compliance with certain requirements (e.g., by means of binding resolutions or adjudicative decisions) or impose financial sanctions, is unlikely. The tax sovereignty costs of an upward shift of authority that such centralised institutional mechanisms would require are likely to be too high. They are in any case higher than in other, less politicalized areas of international law, such as in the law on food standards or transportation, where delegation and institutionalisation are common. Taxation is, after all, tightly connected to the operation of the state and lies at the core of all state functions.[10] An indication of these costs is that government authority over direct taxation has not been delegated upward within the highly integrated EU.[11] 'Tax sovereignty' is, in other words, not merely a rhetorical resource to be bargained away for influence over tax policies of others, but, as Ring notes:

> '(1) a loss of tax sovereignty can undermine both the significant functional roles played by a nation-state (revenue and fiscal policy) and important normative governance values (democratic accountability and legitimacy); (2) sovereignty

7 J.L. Goldsmith and E.A. Posner, *International Agreements: A Rational Choice Approach*, 44 Virginia Journal of International Law 113 (2003) at 138. See also J.L. Goldsmith and E.A. Posner (2005).

8 See also: G.W. Downs, D.M. Rocke and P.N. Barsoom, *Is the Good News About Compliance Good News About Cooperation?*, 50 International Organization 379 (1996).

9 This point is, in essence, also made in Ch. 3.

10 L. Murphy and T. Nagel, *The Myth of Ownership: Taxes and Justice* (OUP 2002) in their work on the 'fairness' of taxes are convinced that there are no property rights antecedent to tax structure. At p. 9: 'It is illegitimate to appeal to a baseline of property rights in, say pretax income, for the purpose of evaluating tax policies, when all such figures are the product of a system of which taxes are an inextricable part'.

11 The classic doctrine is established in ECJ, *Finanzamt Köln-Altstadt v. Schumacker,* 14 February 1995, C-279/93, par. 21: 'Although, as Community law stands at present, direct taxation does not as such fall within the purview of the Community, the powers retained by the Member States must nevertheless be exercised consistently with Community law'.

> rhetoric, though capable of being misused and of obscuring critical issues, nonetheless provides a valuable signalling benefit'.[12]

Considering the highly politicised and 'core' role of taxation in state matters, the sovereignty costs of an upward shift of authority in the field of direct taxation may even be similar to those of upward power shifts in the area of national security, which encompasses issues related to the survival of the nation state. Unsurprisingly, delegation in the securities field is moderate or has severely lagged behind other institutional developments.[13] Equally, the use of enforcement mechanisms to ensure the observance and developments of specific rules of international tax law might be very problematic.[14]

In addition to the argument that enforcement mechanisms may be unlikely, enforcement rules are generally *unnecessary* in international tax, that is, as long as international tax remains ultimately based on bilateral arrangements. The current system of international tax law is self-enforcing; 'policing' capacities are not required. As Ring notes, avoiding double taxation is a transparent, reciprocal, iterated game. As a consequence, defections are not in a country's medium to long-term interest. If country A defects, this will immediately become clear for B, as B's residents, now facing double taxation, will start to complain about their tax treatment. This will trigger two responses. First, residents of B will hesitate to invest in A because country A cannot be relied on to provide relief on the basis of the tax convention. Secondly, B may seek to terminate the tax treaty, or engage in similar defections.[15] Neither option is desirable for A. In international tax, the best enforcement is self-enforcement.

In sum, a multilateral deal for international tax law can best be seen as a system that marginally influences bilateral negotiations 'from the top down',

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12 D.M. Ring, *What's at Stake in the Sovereignty Debate: International Tax and the Nation-State*, 49 Virginia Journal of International Law 155 (2008) p. 225.

13 K.W. Abbott and D. Snidal (2000) p. 440-441 distinguish by issue type in this respect. On the one end of their spectrum are issues of national security, in which sovereignty costs are high. Unsurprisingly, delegation is moderate in this field or has severely lagged behind other institutional developments. On the other end of their spectrum are 'technical matters' in which the incidence of legalized agreements and delegation is correspondingly high. Tax policy, they note, is sensitive and 'displays little overall institutionalization'. See also: C.A. Bradley and J.G. Kelley, *The Concept of International Delegation*, 71 Law and Contemporary Problems 1 (2008) p. 30, who say that 'the costs of delegation are higher for subjects that have traditionally been regulated by the state, such as criminal law and punishment, family relationships, and religious freedom'.

14 This discussion of the issue of delegation is somewhat stylized. The costs of delegation also intensify with the independence of the international body and the legal effects (binding, non-binding) of the delegation, and may further depend on the type of delegation (adjudicative, regulatory, legislative, etc.). See C.A. Bradley and J.G. Kelley (2008). Moreover, as also noted in section 5.4.6 and 7.10.3, the need for delegation may be inversely related to the degree of precision in an agreement. See also B. Koremenos, *When, What, and Why do States Choose to Delegate?*, 71 Law and Contemporary Problems 151 (2008).

15 D.M. Ring (2007) p. 133.

in which the relevant setting is one where states collectively negotiate on the basis of persuasion rather than enforcement and coercion. Starting off with general and unthreatening commitments, states may increase commitment and deepen cooperation, with the aim of converging on ideals over time.

6.2.2 A quicker tax treaty amendment process

But there is another logic to using multilateralism as a forum for discussions. A multilateral treaty, when seen as a forum for discussions, has an implicit two-step rationality. In the first step, it has the benefit of solving a simple coordination problem: where and when will states meet, and what are the common value-maximising terms? It allows governments to take advantage of economies of scale, e.g., by making all participants, at the same time, fly to New York. In the second step, states negotiate, in pairs if necessary, on the common-value maximising terms or principles hence identified.[16] In the second step, in other words, states may then engage in deeper forms of co-operation in line with common terms identified in step one.

To explore the relevance of this observation, it is wise to further investigate the different types of multilateralism. The backdrop of Chapter 5's analysis was the realisation of multilateral binding norms: *substantive* multilateralism. It goes without saying that if a multilateral norm *is* arrived at by participating states, this norm may influence the terms of their bilateral tax *in one go.* In this view, a multilateral agreement may be used to 'more expeditiously' amend bilateral tax treaties, provided that the time taken to agree upon the norm does not exceed 18 years (see Chapter 2). Certainly, to surpass those 18 years, the negotiation must be quite complex, and the question for the most part depends on the 'deepness' of the multilateral norm to be negotiated (i.e., obvious distributive problems may perhaps never be solved multilaterally).[17]

There is, however, another important aspect of multilateralism. Multilateralism may also be *formal*, when regimes are multilateral in name but ultimately bilateral in nature.[18] For instance, as Pauwelyn writes, as the WTO treaty is

16 J.L. Goldsmith and E.A. Posner (2005) p. 87; and R.O. Keohane (1984) p. 89-92.

17 There is little research on the duration of international negotiations. But the literature (unsurprisingly) suggests that the aim to negotiate more substantial or deeper norms leads to lengthier negotiations. E.g. J.D. Fearon (1998) and D.H. Bearce, C.D. Eldredge and B.J. Jolliff, *Do Finite Duration Provisions Reduce International Bargaining Delay?*, 69 International Organization 219 (2015) argue that a longer 'shadow of the future' (which reflects the future gains to be expected from cooperation) gives an incentive to states to bargain harder, delaying negotiations.

18 J.G. Ruggie, *Multilateralism: The Anatomy of an Institution*, 46 International Organization 561 (1992) argues what is distinctive about 'multilateralism' is that it not merely coordinates multilateral relations but also establishes multilateral principles. 'Let us examine next an institutional arrangement that is generally acknowledged to embody multilateralist principles: a collective security system. None has ever existed in pure form, but in principle

about market access for goods or services from one state to another, WTO obligations are essentially bundles of bilateral relationships. 'Nor does the fact that an obligation is equally binding on all parties to a treaty make that obligation a collective obligation; it may consist of bundles of (the same) bilateral relationships', Pauwelyn points out. A breach of WTO law can affect the rights of *only one* WTO Member.[19] Indeed, as Guzman writes, the WTO system works because states can selectively suspend their own compliance with portions of the agreement when another state violates WTO law.[20] Likewise, the Vienna Convention on Diplomatic Relations is a multilateral treaty that imposes rights and obligations of states in relation to diplomats sent from *one* country to *another* country.[21]

The difference between multilateralism and bilateralism therefore need not necessarily be strict: formal multilateralism may be employed in step one so as to achieve bilateral negotiations in step two, at least in situations where arriving at substantive multilateralism proves impossible (see Chapter 5). Multilateralism in this 'formal' sense has the mundane benefit of reducing the transaction costs traditionally associated with bilateral treaty negotiations. The math is simple: it is cheaper to get together to negotiate bilateral agreements at one central place and time than to bilaterally negotiate at different places and times (i.e., the benefits of economies of scale); at the same time, the regime does not prevent states to continue bilateral negotiations outside the formal rounds. Further benefits can be achieved if states bargain in negotiating groups consisting of states with similar interests, rather than in pairs. Recognising this, the OECD organised a 'speed dating' session in relation to the BEPS Convention.[22] And indeed, a multilateral instrument:

> 'may overcome the hurdle of cumbersome bilateral negotiations and produce important efficiency gains (…)'.[23]

Moreover, transaction costs of negotiations in the second step can be further reduced by communal knowledge building, guiding principles and established

the scheme is quite simple. It rests on the premise that peace is indivisible'. Also: R.O. Keohane, Reciprocity in International Relations, 40 International Organization 1 (1986), who distinguishes between 'specific' and 'diffuse' reciprocity.

19 J. Pauwelyn, *A Typology Of Multilateral Treaty Obligations: Are WTO Obligations Bilateral or Collective in Nature?*, 14 European Journal of International Law 907 (2003) p. 929-930.

20 A.T. Guzman (2008) p. 66.

21 *Vienna Convention on Diplomatic Relations* (18 April 1961), 500 UNTS 95. See also J. Pauwelyn (2003b) p. 911.

22 See K.A. Bell, *Multilateral Treaty Not Simple, But Clear: OECD's Saint-Amans,* Bloomberg BNA News, 30 November 2016, https://www.bna.com/multilateral-treaty-not-n73014447884/.

23 OECD, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties* (2014) p, 15.

procedure.[24] Establishing guiding principles at the outset 'makes it unnecessary to renegotiate them each time a specific question arises'.[25] In addition, an independent secretariat and procedural structure may provide a degree of neutrality in managing interstate disputes and conflicts,[26] connect different rounds of bargaining, set the rules for negotiations and agreement, help states to draft negotiating texts,[27] and provide 'political leaders' who rely on negotiating skills to foster integrative bargaining.[28] Additionally, a multilateral forum that encourages the exchange and generation of information among its members reduces transaction costs.[29] Hence, a robust multilateral framework may ensure that the marginal costs of dealing with each additional issue under the regime (even if these issues are ultimately fleshed out on a bilateral basis) may be lower than it would be without the regime (i.e., increasing returns to scale).[30]

In sum, it cannot be said for certain that this simple reduction of transaction costs may lead to a more expeditious bilateral tax treaty amendment process than that considered in Chapter 2. But even if it is assumed that states bilaterally negotiate in step 2 (i.e., that for some issues, 'substantive multilateralism' proves hardly possible), making it cheaper for governments to negotiate their bilateral agreements (i.e., by bringing representatives together at the same time and in the same place and by institutionalising negotiations), may prove sufficient to quicken the implementation of new norms in the bilateral tax treaty system. Doing nothing will in any case not quicken the implementation of new norms in bilateral tax treaties. In the words of the OECD:

> 'only a multilateral instrument can overcome the practical difficulties associated with trying to rapidly modify the 3000+ bilateral treaty network'.[31]

24 N.M. Simonelli, *Bargaining over International Multilateral Agreements: The Duration of Negotiations*, 37 International Interactions: Empirical and Theoretical Research in International Relations 147 (2011) shows that the involvement of international organisations in the negotiation of non-security related agreements reduces the length of the negotiations. The duration of multilateral negotiations is shorter when an international organisation makes a first proposal for non-security agreement negotiations, e.g. related to the environment or commodities.

25 R.O. Keohane (1984) p. 90.

26 K.W. Abbott and D. Snidal, *Why States Act through Formal International Organizations*, 42 The Journal of Conflict Resolution 3 (1998).

27 J.D. Fearon (1998).

28 O.R. Young, *Politcal Leadership and Regime Formation: On the Development of Institutions in International Society*, 45 International Organization 281 (1991) p. 293-294.

29 J.D. Morrow, *Modeling the Forms of International Cooperation: Distribution Versus Information*, 48 International Organization 387 (1994).

30 R.O. Keohane (1984) p. 90.

31 OECD, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties* (2014) p. 15-16.

6.2.3 Introducing the managerial approach to international taxation

Based on these findings, perhaps the wisest thing to do is to 'manage' the development of matters that could be dealt with by multilateral agreement. Instead of enforcing and mandating further and deeper forms of cooperation, for which an upward shift of authority to administrative or judicial bodies would be required, it may be better to start off with achieving consensus on typical 'rules of the road' in a forum for discussions. Moreover, reducing the transaction costs traditionally associated with bilateral tax treaty negotiations may facilitate such negotiations.[32]

A multilateral agreement, built on this managerial approach to international cooperation, enables a regime to 'take on a momentum of its own, by providing a forum for discussions, serving as a focal point for international public opinion, and building trust among participants'.[33] Indeed, a robust multilateral institutional framework has the benefit of persisting over time, so that it can set gears in motion under which states' interests can slowly converge on certain ideals. Moreover, 'managing' the cooperation process may lead states to reconstruct, explore and redefine their self-interests, or 'learn'. This may, as is argued in the next section, allow the international tax system to progress towards substantive solutions for international tax's collective action problems, even if the scope and contents of such solutions is likely to be disputed or unclear in practice.[34]

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32 Hence the managerial approach to international cooperation: it is based on 'the finding that state compliance with international agreements is generally quite good and that enforcement has played little or no role in achieving and maintaining that record'. G.W. Downs, D.M. Rocke and P.N. Barsoom (1996) p. 380.

33 D. Bodansky, WHO Technical Briefing Series: The Framework Convention/Protocol Approach (1999) WHO/NCD/TFI/99.1.

34 An argument to a similar effect is given by Schön in his seminal three-part articles on 'international tax coordination for a second-best world': W. Schön (2009); W. Schön, *International Tax Coordination for a Second-Best World (Part II)*, 2 World Tax Journal 65 (2010); W. Schön (2010b). He concludes that, given the point of departure that dramatic changes are unlikely, it is best to aim at creating rules that support 'continuity' among business options: basic choices made by (the owners of) a firm should not be distorted by sudden changes to tax treatment. From this view, far-reaching rules (e.g. formulary apportionment) should not be advocated.

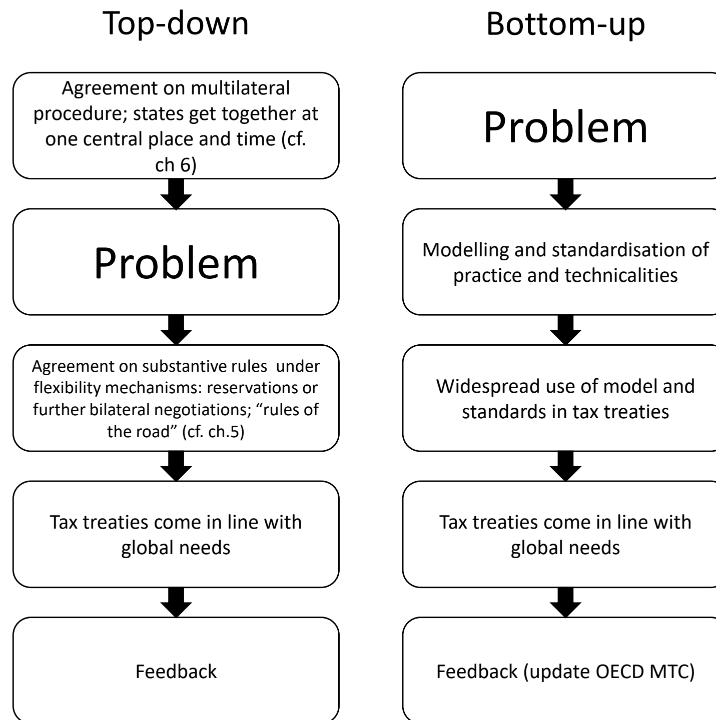

Figure 3: regulatory influence on bilateral tax treaties

6.3 THE DESIGN STRATEGY: 'MANAGING' INTERNATIONAL TAX MATTERS OVER TIME

6.3.1 Introduction

Based on the findings above, a multilateral treaty for international taxation should, at a minimum, have two features. First of all, it should make use of persuasive rather than coercive mechanisms to ensure that states tackle current and future collective action problems collectively. Secondly, it should reduce transaction costs traditionally associated with the negotiation of bilateral tax treaties.

A design strategy that resonates well with these outcomes is the managerial view to treaty design. The managerial view is generally characterized by three underlying elements, which follow from neoliberal literature, supplemented by constructivist arguments. Remember that constructivism can help further understand how rational, egocentric states' understandings of the world come

into existence and change (see Chapter 5.2). Introducing constructivist arguments in neoliberal theory may hence explain how states 'learn', that is, how regimes evolve over time, what compels actors to converge on certain ideals, and why some issues and solutions end up on the bargaining table and others do not.[35] Indeed, supplementing the neoliberal theory on international relations with constructivism leads, in the words of Ring, to 'a modified interest-based model where the institutional bargaining pursued by the states is significantly impacted by information or knowledge'.[36]

The three elements that underlie the managerial view, are: continuous interaction (section 6.3.2), the building on shared understandings, i.e., by norm entrepreneurs and epistemic communities (section 6.3.3), and the use of legal norms (section 6.3.4). Individually, these elements do not enhance cooperation. Rather, their *combination* leads to a model of cooperation in which international obligations are created, evolve, and are maintained over time (section 6.3.5).

6.3.2 Continuous interaction

Section 6.2.2 showed that multilateral negotiation, by solving a coordination problem ('the first step' of multilateral cooperation), reduces the transaction costs of further (bilateral) interactions, as it takes benefit of economies of scale ('formal multilateralism'). This may allow states, in 'the second step' of multilateral cooperation, to more quickly negotiate bilateral treaties and therefore form deeper commitments over time.

Indeed, an important lesson of neoliberal theory is that cooperation amongst self-interested actors may emerge and then evolve on the deeper, second level of cooperation through initial weak forms of cooperation in step one, even when an enforcement system is not feasible. Provided that the cooperation game is iterated indefinitely, players can be expected to base their strategy

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35 In constructivist literature, 'learning' is generally caused by the role of normative values and ideas, such as e.g. 'fairness'. The force of 'doing what is right' or 'doing what is fair' that compels states to enter into certain cooperative structures is captured by 'the logic of appropriateness'. March and Olsen describe the 'logic of appropriateness' to involve cognitive and ethical dimensions, targets, and aspirations. As an ethical matter, they say, appropriate action is action that is virtuous. J.G. March and J.P. Olsen (1998) p. 951-952. See also more fundamentally: F.V. Kratochwil, *Rules, Norms, and Decisions: On the Conditions of Practical and Legal Reasoning in International Relations and Domestic Affairs* (Cambridge University Press 1989). And for discussions: e.g.: T. Risse, *Let's Argue!: Communicative Action in World Politics*, 54 International Organization 1 (2000); H. Müller, *Arguing, Bargaining and All That: Communicative Action, Rationalist Theory and the Logic of Appropriateness in International Relations*, 10 European Journal of International Relations 395 (2004).

36 D.M. Ring (2007) p. 114.

on conditional, reciprocal cooperation called 'tit-for-tat'.[37] Under such form of interaction, one player repeats the previous action of the other player in a subsequent move. For instance, if player A cooperates in round one, player B cooperates in round two; if player A reneges in round one, player B reneges in round two. Knowing that actions are repeated by other players in subsequent moves, players may value future payoffs more than short-term gains. In the terms of international relations literature: when there is a large 'shadow of the future', cooperation will thrive.[38] The more important the outcomes of future plays are, the more sensible it is for actors to forego short-term payoffs.[39] A regime may therefore be used to repeatedly bring participants together, so as to install infinite reciprocal iterations of the Prisoners' Dilemma game. This offsets the immediate costs of cooperation with long-term benefits.

For international lawyers, reciprocal interaction is a commonly used explanation for obligations in international law. Former President of the international Court of Justice (ICJ) Rosalyn Higgins, for instance, has argued that obligation in international law is essentially based on reciprocity, in which states trade self-interests:

> 'If consensus, often tacit and sometimes unenthusiastic, is the basis of international law, then that consensus comes about because states perceive a reciprocal advantage in cautioning self-restraint. It rarely is in the national interest to violate international law, even though there might be short-term advantages in doing so. For law as a process of decision-making this is enough'.[40]

And in the view of Luis Henkin, almost all states observe international law almost all the time because of reciprocity: states observe those obligations they do not care about to maintain others they value, he says. To keep the system intact, a state observes law when it 'hurts' others, so that others will observe laws to that state's benefit.[41]

If regimes set standards of behaviour around which expectations of actors converge, then, by reducing the transaction costs of each iteration, repeated and reciprocal interaction is a necessary condition for the evolution of cooperation over time.[42] In fact, a minimum of two iterations is required for any form

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37 In this strategy, players cooperate on the first move, and in subsequent moves repeat what the other player did in the previous one. J.L. Goldsmith and E.A. Posner (2005) p. 87. See also R.O. Keohane (1986) p. 9.

38 This has been tested by R. Axelrod, *The Evolution of Cooperation* (Basic Books Inc. 1984).

39 R.O. Keohane (1986) p. 9.

40 R. Higgins, *Problems and Process: International Law and How We Use It* (OUP 1994) p. 16.

41 L. Henkin, *How Nations Behave: Law and Foreign Policy* (Columbia University Press 2nd ed. 1979) p. 51-52.

42 R. Axelrod (1984); building on this J. Brunnée and S.J. Toope (1997) p. 32-37 and B. Frischmann, *A Dynamic Institutional Theory of International Law*, 51 Buffalo Law Review 679 (2004). See also R. Keohane, *The Demand for International Regimes*, 36 International Organization 325 (1982) at p. 334: 'international regimes help to make governments' expectations con-

of cooperation to deepen: this logic already follows from agreeing to general value-maximising norms in the first step and engaging in deeper cooperation on these terms in a second step. For instance, the iteration perspective may explain why obligations under the law of treaties set out in the Vienna Convention on the Law of Treaties (VCLT)[43] deepen with each additional legal act. As to the conclusion of treaties, the VCLT expressly sets forth two iterations upon which obligations of states increase, namely during subsequent acts of signature and ratification. At each of these iterations 'a nation may formally cooperate with, or defect from, the efforts at cooperative action prescribed by the rules of the treaty at issue'.[44] Initially, a party can cooperate without undertaking any obligations. Upon signature, a party must refrain from taking action that goes against the object and purpose of the signed treaty. And upon entry into force, a party must comply with all the obligations imposed by the treaty. The deepness of obligations progressively increases with each iteration. The VCLT hence 'reflects a deep and pervasive concern with the promotion of iteration'.[45]

Of course, reciprocal iterations do not necessarily have to occur between pairs. Reciprocity may also take place if multilateral groups can be broken down into smaller clusters.[46] This means, in the words of Blum, that a multilateral negotiation is 'often essentially a series of bilateral negotiations evolving toward coalitions and broader consensus'.[47] For example, states may agree to restrict the concept of treaty residence by means of a general anti avoidance rule (GAAR) to prevent unilateral action. Some players may, however, choose to defect under such a rule to attract short-term gains, such as an inflow of FDI. But knowing that other actors, under the reciprocal and conditional form of interaction of 'tit-for-tat', may then choose to defect as well, e.g., by putting unilateral anti-abuse measures in place, the value of future interaction compels these players to cooperate. For both clusters of actors, neither a chaos of overlapping unilateral anti-abuse rules nor the complete redundancy of income tax systems due to increased tax competition is, in the long run, a more welcome alternative to multilateral cooperation. Hence, repeated reciprocity 'is an appropriate principle of behaviour when norms of obligations are weak – the usual case in world politics – but when the occurrence of mutually beneficial cooperation seems possible'.[48]

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sistent with one another. Regimes are developed in part because actors in world politics believe that with such arrangements they will be able to make mutually beneficial agreements that would otherwise be difficult or impossible to attain'.

43 *The Vienna Convention on the Law of Treaties* (adopted 23 May 1969), 1155 UNTS 331.

44 J.K. Setear, *An Iterative Perspective on Treaties: A Synthesis of International Relations Theory and International Law*, 37 Harvard International Law Journal 139 (1996) p. 191.

45 Id. at p. 190.

46 R.O. Keohane (1986)

47 G. Blum (2008) p. 351.

48 R.O. Keohane (1986) p. 24.

In international tax law, like in other economic relationships, infinite reciprocal interaction is possible, as interstate relationships are lasting and interdependent: states in principle do not seek to eliminate each other by means of military retaliation (as is the case in security affairs).[49] An international regime can therefore facilitate iterated interaction by taking care of communication, so that actors 'can learn about each other's intentions and actions, agree on standards of behaviour, and learn about the relationship between their actions and outcomes'.[50] In sum, provided that states have an interest in the common, and that there is a 'shadow of the future', procedural arrangements that ensure that states keep playing the reciprocal cooperative game indefinitely can lead to more successful and deeper forms of cooperation over time.

6.3.3 Building on shared understandings

6.3.3.1 Introduction

Literature shows that states generally come to redefine an agreement by building on concepts that are already recognized by a wider public. On the basis of such recognized norms, states 'learn', that is, develop interests and consequently develop new legal norms while old ones evolve. This argument is reflected in two main accounts on norm dynamics: on the role of norm entrepreneurs in developing norms (section 6.3.3.2) and on the role of epistemic communities (section 6.3.3.3). The central conviction is that, as Ernst Haas phrases it, 'change in human aspirations and human institutions over long periods is caused mostly by the way knowledge about nature and about society is married to political interests and objectives'.[51]

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49 R. Axelrod and R.O. Keohane, *Achieving Cooperation under Anarchy: Strategies and Institutions*, 38 World Politics 226 (1985) p. 232.

50 L.L. Martin (1999) p. 55.

51 E.B. Haas, *When Knowledge is Power: Three Models of Change in International Organizations* (University of California Press 1990) p. 11. Haas argues that there are three models of organisational change: 'incremental growth', 'turbulent non-growth', and 'managed interdependence'. The latter (which he refers to as 'learning') is the ideal-type of change: 'learning should be seen as the actors' way of saying that life under conditions of turbulent nongrowth is not satisfactory, that something ought to be done to overcome turbulence. Learning could also represent a decision that incremental growth is simply not good enough because it is too slow and results in problem definitions that are excessively decomposable. (…) [M]y argument that institutions can be arenas for innovation in addition to being constraints on change clearly depends on the presumed capability of actors to use institutions to cope with problems never before experienced'. Id. at p. 127.

6.3.3.2 Norm entrepreneurs

In an article about how norms come into existence, Finnemore and Sikkink point at the role of norm entrepreneurs. Norm entrepreneurs actively build norms, as 'norms do not appear out of thin air'.[52] Norm entrepreneurs have strong notions about what is appropriate and desirable behaviour in their community.

The process of norm building, so Finnemore and Sikkink argue, can be understood to occur in three stages. The first stage is 'norm emergence', the second stage involves broad state acceptance which they call a 'norm cascade', in which some states persuade others to join, and the third stage involves norm internalisation where norms are 'taken for granted'. The first two stages are divided by a tipping point, at which 'a critical mass of relevant state actors adopt the norm'.[53] To reach the tipping point, it matters which states are 'in', as well as the amount of states that are persuaded. Once enough states are on board, i.e., when the crucial tipping point for a 'norm cascade' is reached, a different dynamic begins in which other countries adopt norms, even without being pressurised.[54]

In the most important first stage, norms are built by two main drivers: norm entrepreneurs and institutional platforms. But the norms that norm entrepreneurs create and name usually resonate within broader public understandings.[55] Actors are more likely to accept norms if these norms are similar to already accepted ideas. As Payne for instance says:

> 'actor A communicates to actors B, C and D that new normative concern Z should be embraced because Z is similar to already agreed norms X and Y'.[56]

As regards the BEPS Project, for instance, the norms the OECD created resonated within wider public understandings, as most if not all of the outcomes of the BEPS Project proposed are based on existing notions familiar to those working in international taxation. For example, the idea of LOB rules, tweaking the

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52 M. Finnemore and K. Sikkink, *International Norm Dynamics and Political Change*, 52 International Organization 887 (1998) p. 986. Also: E.A. Nadelmann, *Global Prohibition Regimes: The Evolution of Norms in International Society*, 44 International Organization 479 (1990) refers at p. 482 to 'transnational moral entrepreneurs', which are groups that 'mobilize popular opinion and political support both within their host country and abroad; they stimulate and assist in the creation of like-minded organisations in other countries; and they play a significant role in elevating their objective beyond its identification with the national interests of their government'. Also: C.R. Sunstein, *Social Norms and Social Roles*, 96 Columbia Law Review 903 (1996).

53 M. Finnemore and K. Sikkink (1998) p. 895.

54 Id. at p. 902.

55 Id. at p. 896-897.

56 R.A. Payne, *Persuasion, Frames and Norm Construction*, 7 European Journal of International Relations 37 (2001) at p. 43.

permanent establishment concept, and alterations to the operation of the arm's length standard all functioned within frames already recognized by the wider public. In the same vein, the final BEPS reports do not contain any concepts that are completely new.

6.3.3.3 Epistemic communities

Another account of the creation of shared understandings is one that centralizes so-called 'epistemic communities', and emphasises learning. First defined by Peter Haas, epistemic communities are networks of knowledge-based experts that work together on scientific, technical or economic matters. They often consist of experts with an authority claim within their domain of expertise, and for that reason enjoy social authority.[57] They help states identify their self-interests, frame issues for collective debate, and set policies and points for negotiation.[58] Lawmakers can collectively learn from epistemic communities, as they are persuaded by the virtue of new ideas,[59] which in turn leads to new shared understandings, by implication redefine interests, and therefore ultimately lead to new rules. In this regard, Haas says, 'we identify and interpret problems within existing frameworks and according to past protocols and then try to manage the problems according to the operating procedures that we have applied in the analogous cases'.[60] Epistemic communities, in other words, can help to create understandings that have some affiliation with previously existing ideas.[61]

From this perspective, for instance, Ring explains how the OECD has helped to form international tax policy. The influence and expertise of the OECD has changed the behaviour of actors. Tax rules are difficult. Because of their highly technical nature, 'the stories of international tax organisations and tax organisations and tax policy are likely intertwined with the story of knowledge and expertise'.[62] She therefore notes that the experts of the OECD, somewhat like an epistemic community, have helped states to understand the world as well as form their interests through, e.g., the OECD MTC. Policymakers turn to experts to help them formulate policy, frame issues for debate and identify points for negotiation. This, she says, created a dynamic that:

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57 P.M. Haas, *Epistemic Communities*, in: The Oxford Handbook of International Environmental Law (D. Bodansky, J. Brunnée and E. Hey eds., OUP 2012) p. 793.
58 P.M. Haas, *Introduction: Epistemic Communities and International Policy Coordination*, 46 International Organization 1 (1992) p. 2.
59 P.M. Haas (2012) p. 797.
60 P.M. Haas (1992) p. 28.
61 Id. at p. 28-29.
62 D.M. Ring, *Who is Making International Tax Policy? International Organizations as Power Players in a High Stakes World*, 33 Fordham International Law Journal 649 (2010) p. 682.

> 'provided a setting in which many of the detailed issues of international taxation could be explored and elaborated by and among those with extensive knowledge. In addition, the momentum within these organizations to identify, enumerate, and solve the problems of double taxation propelled countries toward model treaties. The resulting model treaties themselves had an independent life of their own'.[63]

Hence, the two above accounts, i.e., the first one on norm entrepreneurs and the other on epistemic communities, suggest that norm innovation takes place on the basis of beliefs that already exist. Epistemic communities help states, in a process of social learning, to identify their self-interests on the basis of new shared understandings. Norm entrepreneurs, likewise, name and create norms that resonate within broader public understandings.

6.3.3.4 Transparency and inclusivity

'Learning' by means of norm entrepreneurs and epistemic communities stresses the importance of transparency and inclusive deliberation.[64] What is needed, as pointed out above, is a mechanism in which knowledge can be gathered, in which problems can be solved, and in which states' interests can change. Hence, in the managerial design strategy, the idea of 'deliberation' (arguments and persuasion) plays a central role.

A more diverse and inclusive set of actors 'fosters exchange of policy knowledge and experience, promotes common understandings and purpose through continued interaction, contestation, and justification of action, and thus more likely leads to changes in legal norms'.[65] Or as Downs, Danish and Barsoom say:

> 'If collective deliberation and intraregime information can reliably transform state preferences so that even relatively regressive states find themselves increasingly committed to ever deeper levels of international cooperation, it makes good sense to be as inclusive as possible. membership restrictions would only lessen the aggregate amount of cooperation in the system with noconcomitant advantage'.[66]

63 D.M. Ring (2007) p. 145.

64 See for an explanation, from a rational perspective, of the importance of communication to solve dilemmas of the type that characterizes negotiations in international tax law, i.e., 'games of common aversion': J.D. Morrow (1994).

65 M.P. Cottrell and D.M. Trubek (2012) p. 371.

66 G.W. Downs, K.W. Danish and P.N. Barsoom, *The Transformational Model of International Regime Design: Triumph of Hope or Experience?*, 38 Columbia Journal of Transnational Law 465 (2000) p. 507.

Indeed, the argument for inclusiveness in the literature that deals with persuasion, rather than coercion, is that broad-based membership exerts a stronger and more authoritative 'community pressure' on reluctant states.[67]

Likewise, transparency, which has been discussed more extensively from the neoliberal institutionalist viewpoint in section 5.4.7, facilitates the exchange of information and hence enables states and non-state actors alike to take an active role in ongoing discussions, even if they have no formal status. Transparency may lubricate discussion, compromise and persuasion,[68] provided that the public does not 'measure' the success of its representatives against publicly known baselines. If understandings are to be shared, so that knowledge can be built, and if actors are to be persuaded rather than coerced into certain behaviour, transparency is indispensable. In the words of Ernst Haas, who writes about change in international organisations:

> 'increasing the transparency of decision processes is a necessary, though far from sufficient, step in encouraging a transideological dialogue. Regimes and their organizations become less threatening to the outsiders when their inner workings are better understood. Once understood and subjected to knowledgeable critique, the routines can then be revised to the satisfaction of the outsiders while accomplishing what the staff and the dominant coalition wish to do. Transparency does not guarantee successful and consensual redefinition of problems. But without it, no consensual redefinition seems possible'.[69]

Important in this regard, and so far understated and only briefly discussed in sections 4.2.3 ('iterative, inclusive and transparent deliberation on tax rules')[70] and 5.4.7.2 ('transparency'),[71] is the role of non-state actors such as NGOs. The international theatre cannot be imagined without them, and NGOs have, as a matter of fact, grown in importance.[72] The point is that the involve-

67 R. Goodman and D. Jinks, *How to Influence States: Socialization and International Human Rights Law*, 54 Duke Law Journal 621 (2004) describe this process as 'acculturation'. See p. 667-673. See also: T. Risse (2000) (open debate and constructive dialogue may construct common lifeworlds).

68 A.E. Boyle and K. Mccall Smith (2013) ('deliberation and transparency go together in most law-making processes').

69 E.B. Haas (1990) p. 219.

70 The point here is that the inclusion of non-state actors such as NGOs enhances the 'fairness' of international tax law.

71 The point here is that NGO inclusion should be seen in the light of the limitations posed by opening the doors to negotiations.

72 R. Thakur and T.G. Weiss, *Framing Global Governance, Five Gaps*, in: Thinking about Global Governance: Why People and Ideas Matter (T.G. Weiss ed., Routledge 2009) p. 147 ('The growing influence and power of civil society actors means that they have effectively entered the realm of policy-making'). As regards tax, see A. Christians, *Tax Activists and the Global Movement for Development through Transparency*, in: Tax Law and Development (M. Stewart and Y. Brauner eds., Edward Elgar Publishing 2012), available at SSRN: http://ssrn.com/abstract=1929055.

ment of NGOs may foster knowledge building. For instance, Koh emphasises their importance to the development of norms in the contemporary transnational stage:

> 'as governmental and nongovernmental transnational actors repeatedly interact within the transnational legal process, they generate and interpret international norms and then seek to internalize those norms domestically. To the extent that those norms are successfully internalized, they become future determinants of why nations obey'.[73]

And indeed, the cooperative role of NGOs in propelling forward the international decision-making process is supported by the idea that NGOs can mobilize public opinion and defend viewpoints that are off-limits for governments.[74]

6.3.4 Legal norms

According to the intuition of any lawyer, legal norms matter. The rules set out in the Vienna Convention on the Law of Treaties for instance hold that the existence of a legal obligation means this obligation is to be carried out in good faith: *pacta sunt servanda*.[75] The sense of duty, or of obligation, that originates from legal norms almost speaks for itself. Yet, there are many authors who seek to explain why legal norms exert an influence on state behaviour. Let's look at some of them.

For Goldsmith and Posner, legal obligations are nothing but an extension of a state's self-interests. From this viewpoint, compliance with a legal norm can be explained by two reasons: retaliation and reputation. The element of retaliation that they describe is closely related to the importance of reciprocity, discussed in sections 6.2.2 and 6.3.2. Action leads to reaction: faced with uncertainty as regards the future reciprocal reactions of others, states choose to forego short term gains for long-term cooperation. Reputation, on the other hand, refers to a state's beliefs about the likelihood that another state will comply with the treaty. When a state violates a treaty, that violation can be

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73 H.H. Koh, *Why Do Nations Obey International Law?*, 106 Yale Law Journal 2599 (1997) p. 2651. Also: H.H. Koh, *Transnational Legal Process*, 75 Nebraska Law Review 181 (1996).

74 See e.g. D.C. Esty, *Non-governmental Organizations at the World Trade Organization: Cooperation, Competition, or Exclusion*, 1 Journal of International Economic Law 123 (1998) at p. 129: 'Non-governmental organizations can serve as service providers (either acting independently or as government subcontractors); mobilizers of public opinion, defenders of viewpoints that governments do not represent or under-represent; watchdogs or private enforcement agents; policy analysists and expert advisors to governments; and bridges between state and non-state actors connecting local and global politics'. Also: S. Charnovitz (2006); A.E. Boyle and C.M. Chinkin, *The Making of International Law* (OUP 2007) Ch. 2.

75 VCLT art. 26.

generalised to the state's reputational status under all treaties subject to international law, as well as to the quality of that state's institutions,[76] making violation costly.

But why would states use *legal* norms? After all, states can also decide to use soft law. Goldsmith and Posner give three arguments. First of all, legal norms require legislative consent, a process that conveys important information about a state's preferences for a norm. A parliamentary process reveals information to other treaty partners about the policy preferences of the state's legislature, and therefore of the state's public. It thus conveys information about the reliability of a state's commitment.[77] Secondly, legal norms take advantage of 'default rules' that apply to them. By entering into a legal norm, a state invokes the law of treaties, such as set out in the VCLT, on its interpretation, modification and application, etc. An incentive for states to enter into legal agreement, therefore, is to 'inform each other that the default rules set forth by the law of treaties will apply if a dispute arises'.[78] Lastly, the legal norm serves to signal the seriousness of a state's level of commitment. A legal obligation is, in other words, 'stronger' than a nonlegal obligation.[79]

Unlike Goldsmith and Posner, who focus on rationality to explain state compliance, there are others who relate rule-following not to reputation and reciprocity, but to their duty-imposing character. This constructivist viewpoint tries to explain the role of legal norms beyond the fear of states for penalties or repercussions. Here, the role of traditions or rituals is emphasised, as is the relevance of identity, by means of which the individual identifies him or herself with the collective, as well as that of deliberation, that is seen as the basis for deciding moral questions.[80] As Chayes and Chayes note, what generally follows from the academic discussions in this regard is that actors follow norms because of the belief 'that social life would be impossible without some kind of obligation to follow prescriptions'.[81] States who fail to comply, or for instance 'stretch' a legal interpretation – it is often possible to distinguish good legal argument from bad – have to justify or explain their deviant behaviour.[82] And as Braithwaite and Drahos show in their vast empirical study on international business regulation, for compliance, 'dialogue that redefines

76 J.L. Goldsmith and E.A. Posner (2005) p.101. See also: K.W. Abbott and D. Snidal (2000) p. 427 and A.T. Guzman, *A Compliance-Based Theory of International Law*, 90 California Law Review 1823 (2002).
77 J.L. Goldsmith and E.A. Posner (2005) p. 91-95.
78 Id. at p. 95-98.
79 Id. at p. 98-99.
80 F.V. Kratochwil (1989) p. 123-129. The author refers to Durkheim and Habermas for this.
81 A. Chayes and A.H. Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (Harvard University Press 1995) p. 116-117.
82 Id. at p. 118-123.

interests, delivers the discipline of complex interdependency and persuades to normative commitments is enough'.[83]

The point of both explanations is that legal norms matter in international cooperation, whether on the basis of fears for reputation and retaliation, or due to their duty-imposing character.

But what does this say about the *development* of legal rules? The point is made by Garrett and Weingast, in an influential article on the matter. Publicized legal norms can act as 'focal points' around which future negotiations can gravitate.[84] In their capacity to distinguish 'appropriate' behaviour from 'inappropriate' behaviour, legal norms serve as points of coordination, because they are the result of bargaining and argumentative processes that do not need to be repeated.[85] 'By embodying, selecting, and publicizing particular paths on which all actors are able to coordinate, institutions may (…) help construct a shared belief system that defines for the community what actions constitute cooperation and defection'.[86] Simply said, in a world where many solutions and alternatives exist for certain policy directions, legal norms can be used to give direction to further debate and negotiation, by distinguishing good from bad arguments, and by differentiating appropriate from inappropriate behaviour.

Garret and Weingast refer to the emergence of the EU internal market. The ECJ's landmark *Cassis de Dijon* decision provided the first stepping stone in this regard by acknowledging the principle of mutual recognition: it 'acted as a focal point around which EC members could coordinate their bargaining'.[87] With mutual recognition established by the *Cassis de Dijon* decision acting as a focal point, the EU developed not in the direction of a heavily regulated internal market layered 'on top of' existing national regimes, but towards a successful 'constitutional' system with only limited sanctioning powers.[88] Under this system, the benefits from cooperation were captured

83 J. Braithwaite and P. Drahos, *Global Business Regulation* (Cambridge University Press 2000) p. 553-559.

84 The logic of a focal point speaks of itself, and is eloquently set out by Schelling. When a man loses his wife in the department store without any prior understanding of where to meet if the couple gets separated, the chances are good that they will think of some obvious place. Even if they both dislike walking, and an obvious meeting point would be a larger distance for the one than for the other, (signalling an obvious conflicts of interest), 'the need for agreement overrules the potential disagreement, and each must concert with the other or lose altogether'. T.C. Schelling, *The Strategy of Conflict* (Harvard University Press New ed. 1980), Ch. 3.

85 The same argument, i.e., the coordinative function of law, is inherent to the work of G. Brennan and J.M. Buchanan (1985), Ch. 2 section VII, and is moreover made by made by J. Habermas (1996) in Ch. 3 of *Between Facts and Norms*, where he sets out that modern law solves a coordination problem between facticity and validity; between natural law and popular sovereignty.

86 G. Garrett and B. Weingast (1993) p. 176.

87 Id. at p. 189.

88 Id. at p. 196-197.

by the general idea of mutual recognition. This principle was then 'fairly' translated by the ECJ into acceptable and unacceptable standards of behaviour under the circumstances provided by specific cases.

But legal norms need not be precise to guide the development of rules. We have seen that precise rules can be counterproductive *ex ante*, as states might find that precise rules emphasise disagreement (see on this Chapter 5). Moreover, as Abbott and Snidal note, imprecise norms have benefits *ex post* too, as they may offer strategies for individual and collective learning. Such obligations 'offer flexibility and protection for states to work out problems over time through negotiation shaped by normative guidelines, rather than constrained by precise rules'.[89] And under such normative guidelines, new rules may be formulated once more information has become available,[90] such as the specific circumstances of a case decided on by the ECJ. Imprecise norms, in other words, can provide a normative template against which endless discussion of the scope of the norm and the appropriateness of behaviour can take place. The central constructivist argument here is that imprecise norms may come to be associated with the identity of the group. As it is status within the group that the actor seeks (i.e., isolation from the group would mean e.g., the loss of the opportunity for economic growth and political influence), imprecise rules may establish broad consensus which has institutionalizing effects, and mobilise social pressure on states to adopt social norms. For instance, the adoption of a broad 'general anti-avoidance' norm might strengthen the rhetoric that aggressive tax planning is bad.[91] Over time, the strength of the norm and the stigma associated with its violation can create social pressure on actors to adopt anti-tax arbitrage policies.[92]

89 K.W. Abbott and D. Snidal (2000) p. 443.

90 Id. at p. 441-444.

91 As to BEPS, I. Grinberg (2016) at p. 1178 writes that non-legal norms can have a similar same function: 'debates about international standards can act as a kind of focal point. Indeed, law firms and accounting firms around the world now routinely catalogue the various national proposals that are vaguely related to outcomes of the BEPS project, even as they depart from the details thereof. When a multilateral project is sufficiently politically salient, even an inconclusive part of the project may matter because it can act as a locus for subsequent domestic policy debates'.

92 E.g. R.B. Mitchell, *Flexibility, Compliance and Norm Development in the Climate Regime*, in: Implementing the Climate Regime: International Compliance (O.S. Stokke, J. Hovi and G. Ulfstein eds., Earthscan Press 2005) p. 79-80, in respect of the climate change regime: 'Perhaps the largest influence of the regime lies in its effect on how behaviours that contribute to climate change are framed (…) Although [the purpose of the Kyoto targets] is to create legal categories of compliant and non-compliant behaviours, their more important effect may be as foundations for social categories of identity. [The Kyoto targets] become the basis for a broader social definition (…)'. Also: R. Goodman and D. Jinks (2004) p. 680-685 and R.B. Mitchell, *Inernational Control of Nuclear Proliferation: Beyond Carrots and Sticks*, 5 The Nonproliferation Review 40 (1997) p. 46. The counterargument is that explicit and precise international commitments create unequivocal social sanctions and mitigate holding-out behaviour (i.e., prevent actors from waiting and seeing who moves first). E.g. C.R. Kelly,

6.3.5 Transforming international tax law over time

The combination of the three elements, i.e., continuous interaction, legal norms and enabling actors to build on shared understandings, results in a theory about how international obligation is constituted, developed, and maintained collectively over time.

One of the most important recent contributions to managerial theory has been that of Brunnée and Toope.[93] Brunnée and Toope provide a pragmatic view of how international obligation is created and maintained over time in their 'interactional' account of international law. They argue that international obligation is built and maintained by lining up prospective legal norms with their underlying shared understandings by means of an ongoing 'practice of legality'.

In particular, the authors focus on the work of Fuller to make their argument. Fuller has set out several 'desiderata' that are seen as the essential characteristics that embody the 'inner morality of law'.[94] They are: generality, promulgation, non-retroactivity, clarity, non-contradiction, not asking the impossible, constancy, and congruence between rules and official action.[95] Given that repeated interaction takes place on the basis of shared understandings, the point of Brunnée and Toope is that the adherence to these 'criteria of legality' creates a 'practice of legality'. This 'practice of legality' is crucial to international law's ability to promote adherence, to inspire the 'fidelity' of actors. It allows actors to 'pursue their purposes and organize their interactions through law'.[96] After all, states are both lawmakers as well as the subjects of international law; international law does not depend on hierarchy between lawgivers and subjects. Hence, their claim: international law 'can exist only when actors collaborate to build shared understandings and uphold a practice of legality'.[97] For them, consequently, international law is 'hard work'.[98]

Enmeshment as a Theory of Compliance, 37 New York University Journal of International Law and Politics 303 (2005) ('Nations will self-enforce regime rules when: (i) those rule are precise, obligatory, can be objectively interpreted, and (ii) compliance is in their interest and within their capabilities'). Also: A. Chayes and A.H. Chayes (1995) p. 10-13.

93 J. Brunnée and S.J. Toope, *Legitimacy and Legality in International Law: An Interactional Account* (Cambridge University Press 2010).

94 L.L. Fuller, *The Morality of Law* (Yale University Press 1964).

95 J. Brunnée and S.J. Toope (2010) p. 7.

96 Id. at p. 7.

97 Id. at p. 7.

98 Id. at p. 5-9.

Implicit in the interactional account of international law is also a claim of legitimacy.[99] If law is made on the basis of the three criteria of the interactional framework, it can be said to be legitimate. Reciprocal interaction and building on shared understandings require broad participation by intergovernmental organisations, civil society organisations, and other collective entities. This builds sustained relationships (which the authors name a 'deep sense of reciprocity'), which are created and maintained collectively.[100] Likewise, inclusive and transparent deliberations foster shared understandings, for instance through epistemic communities or by the work of norm entrepreneurs. International organisations, enterprises and NGOs are all important in the creation of such understandings.[101] In their discussions on the climate change regime, the authors for instance hold that the community of practice, created by the participation of many NGOs and business organisations, as either formal participants or as observants, is crucial for the working of the regime.[102] Hence, inherent to the theory is a strong claim that inclusive deliberations and transparency are important elements of successful international treaty regimes.

So, the managerial account of Brunnée and Toope integrates the three elements of the managerial approach. It shows that in the process of treaty negotiation, existing understandings (c.f. section 6.3.3: 'building on shared understandings') may be pushed or advanced modestly to allow for normative change, as long as this meets Fuller's 'criteria of legality' (c.f. section 6.3.4: 'legal norms') and becomes the object of a continuous practice (c.f. section 6.3.2:

99 In this respect, the theory resembles that of T.M. Franck, *The Power of Legitimacy Among Nations* (OUP 1990) who argues that the legitimacy of international law is the factor that 'pulls' states into compliance. The qualities of law that make law 'legitimate' are: determinacy (i.e., clearness), symbolic validation, coherence (i.e., consistency of the rule itself and of its relation with other rules) and adherence (i.e., to a normative hierarchy). As Franck explains: 'each rule has an inherent pull power that is independent of the circumstances in which it is exerted, and that varies from rule to rule. This pull power is its index of legitimacy'. T.M. Franck, *Legitimacy in the International System*, 82 The American Journal of International Law 705 (1988). Nevertheless, Franck's theory has been criticized for being circular. As Keohane notes: 'Legitimacy is difficult to measure independent from the compliance that it is supposed to explain. For instance, Franck describes a rule's compliance 'pull power' as 'its index of legitimacy.' Yet legitimacy is said to explain 'compliance pull', making the argument circular'. R.O. Keohane (2002), p. 121; also A.T. Guzman (2002) p. 1834-1835. Be that as it may, K. Raustiala and A. Slaughter, *International Law, International Relations and Compliance*, in: The Handbook of International Relations (T.R. Carlnaes, T. Risse and B. Simmons eds., Sage Publications 2002) note that Franck's argument 'is quite consistent with many constructivist assumptions and insights. The theory of state behavior embedded in legitimacy theory is non-instrumental: rather than game theory or bureaucratic politics, Franck invokes theories of legal process and obligation'.

100 J. Brunnée and S.J. Toope (2010) p. 40.

101 Id. at p.45

102 Id. at p. 142-146.

'continuous interaction').[103] The three elements of the previous sections are, in other words, crucial for generation of effective legal obligation in the international setting.[104] For instance, the authors apply these criteria to explain the formation and development of obligation under the climate change regime. All three elements are there, as we will see in section 6.4: the climate change regime allows actors to build on shared understandings, has created a practice of interaction, and its procedural (and some of its substantive) elements meet Fuller's 'criteria of legality'.[105]

Another managerial account on international cooperation is that of the Chayeses, which also (but more implicitly) integrates the above three elements. Their argument is quite similar to that of Brunnée and Toope: states comply with (and hence develop)[106] international law because of 'continuous processes of argument and persuasion, 'justificatory discourse' that ultimately 'jawbones' states into compliance'.[107] International law is important in upholding such discourse.[108] And hence, the three elements of sections 6.3.2-6.3.4 are present.

But what really drives compliance in the view of the Chayeses is what they call 'the new sovereignty', which expresses the increasing interdependence of states in the international system. In this increasingly interdependent world, states have no choice but to cooperate to protect their interests. Indeed:

> 'sovereignty no longer consists in the freedom of states to act independently, in their perceived self-interests, but in membership in reasonably good standing in the regimes that make up the substance of international life. To be a player, a state must submit to the pressures that international regulations impose. Its behaviour in any single episode is likely to affect future relationships not only within the particular regime involved but in many others as well, and perhaps its position within the international system as a whole'.[109]

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103 J. Brunnée and S.J. Toope, *Interactional International Law: An Introduction*, 3 International Theory 307 (2011).

104 Id. at p. 308.

105 J. Brunnée and S.J. Toope (2010) p. 127-132.

106 The Chayes' work is primarily focused on compliance with international law, and not (also) on how international law is created and developed. Their theory simply departs from the presumption that international law exists (simply put: states consent to international law if it is in their self-interest to do so). Nevertheless, arguments about why states comply with international law are closely related to international law's development over time. After all: law that is not complied with is either ineffective or a dead letter, and hence becomes subject to scrutiny. In that case, it makes sense that a law is altered, scrapped or changed. As a consequence, the compliance perspective of the Chayes does not to touch on fundamentally different issues.

107 J. Brunnée and S.J. Toope, *Persuasion and Enforcement: Explaining Compliance with International Law*, 13 Finnish Yearbook of International Law 273 (2002) p. 281.

108 A. Chayes and A.H. Chayes (1995) p. 115-124.

109 Id. at p. 26-27.

In their book, the Chayeses first argue that coercive strategies are unsuitable to make states comply with international law. In sum, they argue that 'sanctioning authority is rarely granted by treaty, rarely used when granted, and likely to be ineffective when used'.[110] Instead, they argue, states comply on the basis of other reasons. Indeed, the Chayeses identify three elements under which there is an assumption that states have a propensity to comply. These are: efficiency, interests, and norms.[111]

As regards the first element, the Chayeses argue that governmental resources for policy analysis and decision-making are costly and in short supply. In simple terms: following an established treaty rule saves costs, as this makes a recalculation of each and every single decision unnecessary. As the Chayeses point out: 'compliance is the normal organisational presumption'.[112] Following norms is, in other words, efficient. Secondly, the Chayeses argue that it is a fair assumption that the parties' interests were served by entering into the treaty in the first place. And, they note, even if a state is unable to achieve all of its policy objectives,

> 'if the agreement is well designed – sensible, comprehensible, and with a practical eye to the probable patterns of conduct and interaction – compliance problems and enforcement issues are likely to be manageable. If issues of noncompliance and enforcement are endemic, the real problem is likely to be that the negotiating process did not succeed in incorporating a broad enough range of the parties' interests, rather than wilful disobedience'.[113]

Thirdly, the Chayeses argue that the existence of legal obligation translates into a presumption of compliance, in the absence of strong countervailing circumstances. The argument that law creates a duty of compliance is so familiar to many (i.e., 'pacta sunt servanda') that it is 'almost superfluous to adduce evidence or authority for a proposition that is so deeply ingrained in common understanding and so often reflected in the speech of national leaders'.[114]

Based on these assumptions, the Chayeses argue that the principal sort of noncompliance is not wilful disobedience, but the lack of clarity or priority that states might have as regards the operation of an agreement. In the simplest

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110 Id. at p. 32-33.

111 One of the elements that the Chayeses name that may induce non-compliance, however, is ambiguity. Yet, they say, detail also comes with difficulties and 'it may be wiser to indicate a general direction, to try to inform a process, rather than seeking to foresee in detail the circumstances in which the words will be brought to bear. If there is a degree of trust in those who are to apply the rules, a broader standard may be more effective in realizing the general policy behind the law than a series of detailed regulations'. Id. at p. 10-11.

112 Id. at p. 4.

113 Id. at p. 7.

114 Id. at p. 8.

form, this means that repeated interaction (i.e., participating in the regime, attending meetings, responding to requests and meeting deadlines), may set gears in motion that propel states to comply. This effect can be reinforced by for instance increased transparency, informal dispute settlement mechanisms, capacity building (the authors refer to the strengthening of technical and administrative means of participating states to comply with the treaty's rules) and the use of persuasion.[115] This, in sum, leads to a strategy that induces states to comply because:

> 'modern states are bound in a tightly woven fabric of international agreements, organizations, and institutions that shape their relations with each other and penetrated deeply into their internal economics and politics. The integrity and reliability of this system are of overriding importance for most states, most of the time. These considerations in turn reflect profound changes in the international system within which states must act and decide'.[116]

To this they add that:

> 'Our experience as well as our research indicates that (…) the fundamental instrument for maintaining compliance with treaties at an acceptable level is an iterative process of discourse among the parties, the treaty organization, and the wider public. We propose that this process is usually viewed as management rather than enforcement. As in other managerial situations, the dominance atmosphere is one of actors engage in a cooperative venture, in which performance that seems for some reason unsatisfactory represents a problem to be solved by mutual consultation and analysis, rather than an offense to be punished. States are under the practical necessity to give reasons and justifications for suspect conduct. These are reviewed and critiqued not only informal dispute settlement processes but also in a variety of other venues, public and private, formal and informal, where they are addressed and evaluated'.[117]

So, in sum, the managerial design strategy to the multilateral agreement for international taxation integrates the three characteristics set forth above: continuous interaction (section 6.3.2), building on shared understandings (section 6.3.3) and legal norms (section 6.3.4). It is not characterized by enforcement mechanisms, but rather employs systems such as the continuous interaction between parties and other interested actors, legal norms as constructed focal points, and transparency and inclusivity to enhance learning. When combined with the need to use interpretative flexibility devices to achieve cooperative outcomes, as set forth in Chapter 5, this results in a regime in which parties are able to dynamically adjust commitment levels and alter their

115 Id. at p. 22-28.
116 Id. at p. 26.
117 Id. at p. 25-26.

mutual expectations and actions over time.[118] In such a setting, for instance, parties' commitments can be discussed, increased or if necessary readjusted so that the likelihood of future compliance and continuing participation is maintained.

This managerial strategy to treaty design leads to the type of multilateral treaty that will be illustrated in the next section.

6.4 An illustration: the climate change regime

6.4.1 Introduction

The regime on climate change illustrates the above observations. The most important instrument of this regime is the 1992 UN Framework Convention on Climate Change (UNFCCC).[119] Its aim is to curb the emission of greenhouse gases, which are by now considered as 'extremely likely to have been the dominant cause of global warming'.[120] The UNFCCC was drafted to prevent that these gases 'caused further warming and long-lasting changes in all components of the climate system, increasing the likelihood of severe, pervasive and irreversible impacts for people and ecosystems'.[121] To do so, the UNFCCC

118 There are more theories to, basically, the same effect as the two theories discussed here (i.e., they are characterised by the same three elements). E.g. H.H. Koh (1997) argues that compliance should not only be sought at the international level but also at the domestic level. Hence his 'transnational legal process' explanation for compliance: states obey international law, he argues, because they 'internalize' international norms. This process can be viewed as having three phases: 'One or more transnational actors provokes an *interaction* (or series of interactions) with another, which forces an *interpretation* or enunciation of the global norm applicable to the situation. By so doing, the moving party seeks not simply to coerce the other party, but to *internalize* the new interpretation of the international norm into the other party's internal normative system. The aim is to 'bind' that other party to obey the interpretation as part of its internal value set. Such a transnational legal process is normative, dynamic, and constitutive. The transaction generates a legal rule which will guide future transnational interactions between the parties; future transactions will further internalize those norms; and eventually, repeated participation in the process will help to reconstitute the interests and even the identities of the participants in the process', at p. 2646.

119 United Nations Framework Convention on Climate Change; *Kyoto Protocol to the United Nations Framework Convention on Climate Change* (adopted 11 December 1997), 2303 UNTS 162. A lot has been written on the problem of climate change. A good starting point is J.S. Dryzek, R.B. Norgaard and D. Schlosberg eds., *The Oxford Handbook of Climate Change and Society* (OUP 2011).

120 IPCC, *Climate Change 2014 Synthesis Report: Summary for Policymakers*, available through: https://www.ipcc.ch/pdf/assessment-report/ar5/syr/AR5_SYR_FINAL_SPM.pdf, p. 4.

121 Id. p. 8. The widespread success of earlier environmental framework accords (in particular the *Vienna Convention for the Protection of the Ozone Layer* (adopted 22 March 1985), 1513 UNTS 324 and its *Montreal Protocol on Substances that Deplete the Ozone Layer* (adopted 16 September 1987), 1522 UNTS 3) led the international community to build a climate change

itself does not contain concrete reduction targets of greenhouse gases, but rather provides a forum in which, in the light of established aims, principles, institutions and procedures, negotiations can take place.[122]

6.4.2 The problem structure of addressing climate change is comparable to that of addressing BEPS

What makes the UNFCCC very interesting for comparative purposes here is that the underlying problem structure of addressing climate change can be compared, at least to a certain degree, to the problem structure underlying the curbing of BEPS.[123] Both problem structures are collective action problems and require a global, multilateral solution. But more fundamentally, both issues are characterised by distributive conflict and uncertainties about the effect of alternative policy options.

First, like in tackling BEPS, different policy options as regards climate change have immense distributive consequences, as greenhouse gas production 'goes to the heart of energy, transport, agricultural, and industrial policy in all developed states and increasingly in developing ones too'.[124] Indeed, tackling climate change is characterized by the sharing of a 'carbon pie' amongst nations, which makes up the remaining greenhouse gases that humanity can

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convention on the basis of the framework convention-protocol design. See T. Bernauer, *Climate Change Politics*, 16 The Annual Review of Political Science 421 (2013) p. 423.

122 G. Blum (2008) p. 345.

123 In selecting a regime for this section's comparative purposes, I have primarily looked for a regime with a comparable problem structure to tackling BEPS, and in which political processes and outcomes are transparent and distinct. For instance, I dismissed a comparison with the trade regime and investment law regime for the following reasons.
The regime on trade is similar to the regime on the avoidance of double taxation (the aim of both regimes is to reduce trade barriers). Unsurprisingly, bargaining within the trade regime is ultimately bilateral, and the WTO is most of all a negotiating forum. See e.g. J.L. Goldsmith and E.A. Posner (2005) Ch. 5. However, in comparison to tackling BEPS, trade liberalization rules have more the aspects of a private good issue than a public good issue (i.e., countries can be excluded from the liberalization of trade, and this does not necessarily affect the effectiveness of the institution's rules between its members). See Wto, *World Trade Report 2007: Six Decades of Multilateral Trade Cooperation: What Have We Learnt?*, WTO Publications, p. 126-127.
Investment law's problem structure is different too: in contradiction to combating BEPS, the free-rider problem is not as dominant. Although host countries use investment treaties to compete to attract investors, it is not clear whether all participating countries face a collective action problem in this regard. A collective action problem may be identified within groups of (developed) countries (i.e., competition pressurises states into signing a BIT, yet each individual state is better off not signing a BIT). But this problem may also be solved by regional agreements. See Z. Elkins, A.T. Guzman and B. Simmons (2006).

124 P.W. Birnie, A.E. Boyle and C. Redgwell, *International Law and the Environment* (OUP 2009) p. 356.

safely exhaust without causing severe damage to the environment.[125] One facet of this distribution conflict is that the North and the South have fundamentally different interests in solving the issue. Restrictions on emissions can severely harm the development of developing states' economies, something Western countries were not faced with at the time their economies were developing.[126] Another facet of distributive conflict is the split between major energy producers and others. States without domestic fossil fuel reserves are more likely to accept having to reduce emissions than states whose economies heavily depend on energy exports. It is therefore no wonder that the negotiations on climate change have been named 'the greatest challenge the UN has ever faced'.[127]

Secondly, like in tackling BEPS, uncertainties exist regarding different policy options of reducing greenhouse gas emissions, in both economic as well as scientific terms. Indeed, uncertainties have persisted in relation to almost every aspect of the climate change problem.[128] As Thompson points out, three kinds of uncertainty have hampered cooperation in the area of climate change. First, 'there is uncertainty about the severity of the global warming problem'.[129] Predictions and models of e.g., temperature change and sea-level rise are incomplete; atmospheric processes are very complex. Secondly, 'there is uncertainty regarding the regional and local impacts of climate change', because of an incomplete grasp of the regional details. Part of this problem is the difficulty of predicting how well firms and people will adapt to change as well as to what extent technological innovations will ease adaptation.[130] Thirdly, 'there is uncertainty regarding the costs and benefits of different policy options' in tackling climate change. An important factor in this respect is that it is very hard to predict the future effect of policy options, both internationally as well as domestically. Simply said: policy makers do not have the capabilities to make accurate predictions so as to make a cost-benefit analysis of different policy options possible.[131] Now, a quick recall of the uncertainties related to addressing BEPS (see section 5.4.1), shows the relevance of comparing the issue of BEPS with the climate change problem. In both areas, uncertainties are related to (1) the severity of the problem; (2) the regional/national impact

125 A. Thompson, *Management under Anarchy: The International Politics of Climate Change*, 78 Climatic Change 7 (2006) p. 10-11.

126 Hence, the relative importance of historical emissions has played an important role in the North-South discussion. Moreover, as developing states have a more limited access to technology, they expect the wealthier states to take on a higher burden of emission reduction. See e.g. M. Paterson and M. Grubb, *The International Politics of Climate Change*, 68 International Affairs 293 (1992) p. 295-297.

127 P.W. Birnie, A.E. Boyle and C. Redgwell (2009) p. 378.

128 D. Bodansky, *The Emerging Climate Change Regime*, 20 Annual Review of Energy and the Environment 425 (1995) p.426.

129 A. Thompson (2010) p. 277-278.

130 Id. at p. 278-279.

131 Id. at p. 279.

of the problem and (3) the national economic (cost-benefit) implications of different policy responses related to addressing the problem.

The distributive aspects of the climate change negotiation, in combination with the role played by uncertainty, have particularly surfaced during the negotiations on the Kyoto protocol, that bindingly establishes the baselines for and allocation of emission reduction targets of 'the carbon pie'.[132] In particular, establishing the size and shares of the 'carbon pie' proved very difficult. The choice of, and the proportioning between, the criteria used to assign emissions quotas, such as per capita, GNP, land area, etc., have created 'obvious winners and losers' in this distributive conflict, making agreement hard if not impossible to achieve.[133] Particularly striking for purposes of the comparison is Kyoto's introduction of the emissions trade mechanism, an innovative 'rule of the road' that allowed states to reach agreement on emission reduction targets. As the future demand for permits was – given the uncertainties related to the climate change problem – uncertain at the time of their allocation,[134] the rule operates 'fairly' in the sense spoken of in Chapter 5. Indeed, states can buy or sell permits as circumstances change, insuring them against uncertainty.[135]

So, in some respects, curbing climate change can be compared to addressing BEPS. Both areas are characterized by stark distributive conflict (that is, 'sharing a pie') and high levels of uncertainty about both the impact of the problem as well as about the implications of alternative policy options.

6.4.3 Managing the climate change problem by multilateral agreement

The climate change regime has been criticized for lacking effectiveness. Indeed, it can be questioned how effective the climate change regime is in reducing CO_2 emissions. Even after the big negotiation achievement of Paris 2015 there is still a lack of agreement on 'real' reduction targets.[136] Moreover, critics

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132 Kyoto Protocol to the United Nations Framework Convention on Climate Change, art. 3. See also: S. Schiele, *Evolution of International Environmental Regimes* (Cambridge University Press 2014) p. 67.

133 A. Thompson (2006) p. 10.

134 Id. at p. 10. The time frame is a decade: the Kyoto protocol has sought to set targets for 2008-2012 in 1997. See also; D.G. Victor, *International Agreements and the Struggle to Tame Carbon*, in: Global Climate Change: The Science, Economics and Politics (J.M. Griffin ed., Edward Elgar 2003) p. 215-216.

135 A. Thompson (2010).

136 See e.g. P. Friedlingstein and others, *Persistent Growth of CO_2 Emissions and Implications for Reaching Climate Targets*, 7 Nature Geoscience 709 (2014). For an overview and discussion of literature in which the effectiveness of environmental regimes is measured see: O.R. Young, *Effectiveness of International Environmental Regimes: Existing Knowledge, Cutting-Edge Themes, and Research Strategies*, 108 Proceedings of the National Academy of Sciencs of the USA 19853 (2011).

say the regime has had little impact on the reduction of global warming.[137]

Yet, the fact is that some form of agreement on curbing climate change is in place. As Bodansky for instance notes, 'like politics generally, building a climate change regime is the art of the possible'.[138] The climate change regime has set forces in motion by means of which the climate change problem is managed, and under which, albeit slowly, states converge on common ideals over time. From this viewpoint, some authors have questioned whether critics who aim to expose the lack of effectiveness of the international climate change regime have not overstated the expectations of what treaties really can do. Is it, they suggest, not better to measure the regime's effectiveness by looking at 'its robustness to evolve, better reflect domestic norms, and strengthen itself towards achieving its objectives'?[139]

The 'management' of the climate change problem takes place within the framework of the UNFCCC, which is characterized by the three 'managerial' elements spoken of above: it installs continuous interaction, it is characterized by the use of primarily procedural and some substantive legal norms, and it builds on explicit and implicit shared understandings. Moreover, the regime makes use of flexibility mechanisms to accommodate the high levels of distributive conflict and uncertainty spoken of above.

Because its initial commitments were relatively weak, the UNFCCC enjoys near universal membership. Almost all states were willing from the outset to accept a framework convention.[140] What the UNFCCC's design as a framework convention most importantly has achieved, is that it has created a setting in which states repeatedly interact by coming together at the same place and at the same time, under accepted legal procedures. Indeed: it has international summits held every year.[141] Moreover, the regime establishes legal procedural requirements, for instance on information exchange and reporting, treaty bodies, and decision-making and amendment rules. For example, the regime's yearly meetings are governed by the regime's supreme body, called Conference of the Parties (COP), which has the authority to review the implementation

137 From 1970 to 2010 the total emissions of anthropogenic greenhouse gasses have only continued to increase, leading to potential detrimental consequences to the environment such as warming oceans and melting glaciers. IPCC, *Climate Change 2014 Synthesis Report: Summary for Policymakers*, available through: https://www.ipcc.ch/pdf/assessment-report/ar5/syr/AR5_SYR_FINAL_SPM.pdf, p. 3-6. Because it has not met its objectives, it can be argued that the regime must be considered as ineffective. See e.g. L.E. Susskind, *Environmental Diplomacy: Negotiating More Effective Global Agreements* (OUP 1994) p. 30-42.

138 D. Bodansky (1995) p. 432.

139 E.g. W.B. Chambers, *Towards an Improved Understanding of Legal Effectiveness of International Environmental Treaties*, 16 Georgetown International Environmental Law Review 501 (2003) p. 526. Also: T. Gehring, *International Environmental Regimes: Dynamic Sectoral Legal Systems*, 1 Yearbook of International Environmental Law 35 (1990); S. Schiele (2014), Ch. 2.

140 See the website of the UN Framework Convention on Climate Change: http://unfccc.int/essential_background/convention/items/2627.php. D. Bodansky (1995) p. 430.

141 M. Bothe (2003) p. 245-249. The 2015 was the 21st yearly session of the COP to the UNFCCC.

of the Convention, examine the obligations of the parties in light of the objective of the Convention, and develop amendments and protocols.[142] Moreover, there are reporting standards that require states to submit national reports and inventories, e.g., on anthropogenic emissions and on the national policies and measures to implement the Convention.[143] Such requirements put pressure on states, as states know their behaviour will be exposed to an international review, and builds trust among them, as free-riders can be singled out.[144] Hence, a main aim of the Convention's procedural functions is to provide a permanent forum for discussion and negotiation and to create a sense of community.

The climate change regime builds on implicit and explicit shared understandings. First of all, the need for a global climate change regime is widely accepted,[145] not only by states but also by an army of NGOs and nongovernmental observers. Moreover, the framework convention sets out the regime's general principles and institutions, which may be seen as the explicitly shared understandings upon which the regime rests. The framework convention's general objective is to achieve 'stabilization of greenhouse gas concentrations in the atmosphere at a level that would prevent serious anthropogenic interference with the climate system'.[146] But some other principles also inform the negotiations, such as the 'common but differentiated responsibility' principle, which comes down to the initial compromise that the North should take the lead in combating climate change and its adverse effects,[147] and the 'precautionary principle', which holds that parties should not use the lack of full scientific certainty as a reason for postponing action.[148]

Finally, the climate change regime makes use of flexibility mechanisms. First of all, the Kyoto protocol introduced the emissions trade mechanism: a clear 'rule of the road' for the climate change problem (see above). But the climate change regime also makes use of a transformative flexibility mechanism: the framework convention/protocol design. The framework convention/protocol design has enabled treaty negotiators to insulate the regime's core commitments from the risk of negotiation breakdown under successive negotiation rounds. Indeed, the quantified reduction targets and emission trading mechanism of the Kyoto protocol were only committed to by the so-called

142 United Nations Framework Convention on Climate Change art. 7.
143 Id. at art. 4. The Kyoto Protocol to the UNFCCC contains information standards too: see e.g. art. 7.
144 D. Bodansky, *The United Nations Framework Convention on Climate Change: A Commentary*, 18 Yale Journal of International Law 451 (1993) p. 444-445.
145 J. Brunnée and S.J. Toope (2010) p. 142.
146 United Nations Framework Convention on Climate Change art. 2.
147 Id. at art. 3(1).
148 Id. at art. 3(3).

Annex I parties, which are mostly developed countries, whilst the general obligations of the convention[149] continued to apply to all states.

Ultimately, the point of these elements is to slowly advance and develop cooperation on the climate change problem.[150] As regards the regime's substantive legal rules, this has indeed been a matter of process and gradual development. For instance, after the framework convention's establishment in 1992, the Kyoto protocol was added in 1997, and refinements to the protocol and its procedures have been made since.[151] The flexibility of the market allocation mechanism has provided states with a way to work towards meeting the regime's core aims. It provides, hence, the perfect example of how innovation can lead to states to agree, over time, to a multilateral rule in an area characterized by stark distributive concerns. And more recently, the robustness of the regime has again paid off: the 2015 round was particularly successful, 'charting a fundamental new course in the two-decade-old global climate effort', in which states have agreed to limit global temperature increase below 2°C and to report regularly on emissions and implementation efforts.[152] The hopes are high that the dynamic and sustainable approach to combating climate change will lead to deeper agreement and to the convergence of states' interests in the future.

6.5 Conclusions

Negotiations in the field of international taxation need to accommodate divergent state interests, and are likely to be and continue to be confined by egocentric and self-interested states. But state interests may change and evolve over time. After all, international cooperation is not static. Indeed, the coming into existence of the BEPS Project is a clear example of how cooperation in the

149 These are set out in art. 4(1) of the convention.

150 See e.g. T. Gehring (1990); T. Gehring, *Treaty-Making and Treaty Evolution*, in: The Oxford Handbook of International Environmental Law (D. Bodansky, J. Brunnée and E. Hey eds., OUP 2008).

151 In 1995, a start was made to achieve stricter emission stabilisation obligations by the negotiations on the UNFCCC's Kyoto Protocol. In the Kyoto protocol, the Annex I parties, which mostly are developed countries, committed to quantified reduction targets. To achieve cost-effective results, the Protocol allows the trading of emission permits. However, Parties were not directly able to agree on the implementation and further development of the Kyoto Protocol. See S. Schiele (2014) p. 68. This, in turn, required more detailed rules on the calculation of assigned amounts and on the functioning of the flexibility mechanism, of which the finalisation took place in 2001 (the 'Marrakech Accords'). M. Bothe (2003) p. 241. Further agreements were reached in 2009 in Copenhagen (which contains the aspiration to reduce emissions so that global warming does not exceed two degrees Celsius).

152 Center for Climate and Energy Solutions, *Outcomes of the U.N. Climate Change Conference in Paris: 21st Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP 21)*, December 2015, http://www.c2es.org/docUploads/cop-21-paris-summary-12-2015-final.pdf.

area of international tax is a dynamic rather than a static undertaking, which may be driven by normative forces (e.g., 'fair share').

A multilateral agreement for international taxation that seeks to facilitate progressive, collective international tax law-making is characterized by two features. First of all, it must ensure that states engage in solving collective action problems. The point is that the international tax regime should be able to continuously respond to the needs of society. In this regard, treaty designers perceive *ex ante* a management risk *ex post*. The key lies in mechanisms of persuasion, rather than of coercion. The argument against coercive mechanisms is, generally speaking, that the delegation of authority to legislative and adjudicative and institutional bodies is not feasible, and perhaps not even necessary, for the area of international taxation (section 6.2.1). Secondly, a multilateral treaty may streamline the renegotiation or amendment of bilateral tax treaties. Obviously, would states come to agree to a substantive multilateral norm ('substantive multilateralism'), e.g., a 'rule of the road', bilateral tax treaties could be amended *in one go.* This would quicken the tax treaty amendment process, provided that the negotiation of the norm would not take longer than 18 years (see Chapter 3). But even if a 'substantive' multilateral obligation proves unfeasible to negotiate (see Chapter 5), a multilateral agreement may be beneficial as it provides a setting that encourages bilateral interaction. Indeed, a 'formal' multilateral agreement may reduce the transaction costs traditionally associated with bilateral tax treaty negotiations. The argument follows from the two-step logic of a multilateral negotiation: transaction costs of bilateral tax treaty negotiations can be reduced by bringing states together at one central place and time. Moreover, transaction costs can be further reduced by institutionalising bargaining (i.e., by centralising knowledge building and the exchange of information), and by the identification of common value-maximizing terms in 'step one', so that states can converge on these terms when entering into deeper forms of cooperation in 'step two' (section 6.2.2).

These two features point at the use of the 'managerial' design strategy for a multilateral agreement for international taxation. The point of the managerial view is that it smoothens collective interplay and facilitates states to progressively deepen their commitments by installing continuous interaction, by enabling them to build on shared understandings (for which transparency and inclusivity are indispensable), and by using legal norms such as 'rules of the road' to act as focal points for further discussions. The point of the combination of the three elements of the 'managerial' strategy is to facilitate 'learning'. Flexibility mechanisms (see Chapter 4) can be used to dynamically adjust and readjust commitment levels, so that mutual expectations and actions can be altered as the cooperative effort goes along. After all, from the previous chapter follows that such mechanisms are needed to accommodate diverging state interests.

A managerial treaty improves the exercise of regulatory influence by means of the OECD MTC and Commentaries (i.e., see Chapter 3), for two important reasons. First of all, it makes international tax law-making fairer (i.e., more inclusive and transparent) and therefore also more likely to develop and respond to deal with the collective action problems that international tax law faces or may come to face. Secondly, the managerial treaty design allows parties to 'streamline' the tax treaty amendment process. A substantive multilateral deal would of course allow parties to amend their bilateral tax relationships *in one go*. But even if this proves unfeasible, it provides a setting in which transaction costs of bilateral interaction are reduced, as it brings parties together at one time and place and under established principles and procedure.

As in many other areas of international cooperation, such as in the area of climate change, progress towards certain solutions for collective action problems may be slow or indecisive. Rome was not built in a day. But a structural, dynamic legal solution to cooperation in the international tax area may provide a solid basis for fruitful cooperation in the future. 'Fair procedure' is at the heart of this approach. Inclusive, continuous and transparent deliberation provides a setting in which knowledge may be build, interests may shift, and hence norms may change. A multilateral agreement for international taxation should provide, in other words, the correct process and infrastructure for international tax law to advance towards substantive solutions over time.