Singapore Journal of Legal Studies
[2024] 126–148

THE FUTURE OF TAX JURISDICTION

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Tax jurisdiction is a legal concept, but it is fundamentally dependent on state capacity, technology and politics. The jurisdictional boundaries of the tax state are in turn crucial in delimiting its taxing power. This article considers how tax jurisdictional concepts, in particular residence, source and the location of consumption, are changing as the capability of states to tax labour, capital and consumption changes in a global digital economy. These changes are occurring through contestation in the "borderlands" of the tax state, between multiple states and non-state actors. Governments can enhance tax capability by cooperating with each other and with global intermediaries and by adopting new technologies, but also take contradictory steps to abrogate tax jurisdiction. The article illustrates the discussion with examples of tax jurisdiction for individuals as residents, workers, investors or consumers; and for corporations, including recent global developments aimed at taxation of multinational enterprises.

I. Introduction

Tax jurisdiction is a legal concept, but it is fundamentally dependent on state capability, technology and politics. The taxing power of a government that relies on taxes – which we can call a "tax state"[1] – depends on the capabilities of the state to enforce taxation, not just on the terms of tax law. States are actively engaged in asserting new jurisdictional boundaries from both a legal and enforcement perspective, and state capability to tax is changing rapidly in a context of technological and political change. The establishment of tax jurisdiction takes place through three modes of tax law-making: the unilateral enactment of laws by states; bilateral tax treaties; and multilateral treaties, forums, and norms. Tax jurisdiction intersects

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1 Miranda Stewart, *Tax and Government in the 21st Century* (Cambridge: Cambridge University Press, 2022) [Stewart]. While all nation states levy taxation, a subset of states are substantially and successfully financed by taxes; these comprise mostly (though not only) middle and upper income countries, including most member states of the OECD. The concept of the "tax state" is usually attributed to Joseph A Schumpeter, "The Crisis of the Tax State" (Wolfgang F Stolper & Richard A Musgrave (translators)) (1917; 1954) 4 *International Economic Papers* 5 at 7; Rudolf Goldscheid, *State Socialism or State Capitalism*: *A Fiscal Sociological Contribution to the Solution of the Problem of Public Debt* (Vienna: Anzengruber Verlag, 1917) according to Richard A Musgrave, "Schumpeter's Crisis of the Tax State: An Essay in Fiscal Sociology" (1992) 2 Journal of Evolutionary Economics 89 at 90.

with other elements of state action in international economic law, including international trade or investment laws and treaties.

This article considers the evolution of the tax jurisdiction of states, which is usually premised on the "residence" of taxpayers and the "source" of income, which may be defined as the location of production or consumption. Part II introduces the tax state and its jurisdiction. It argues that the negotiation of tax jurisdiction is a layered and dynamic process in the "borderlands" of states.[2] The article draws on the concept of the "borderlands" developed by Saskia Sassen, which enables us to consider the border itself as an object of analysis, rather than a line dividing mutually exclusive territories of domestic and international.

Part III explores the shifting borders of tax jurisdiction over people, on the basis of residence, or the derivation of labour and capital income. It then turns to discuss the rise of consumers as a tax base. Part IV addresses tax jurisdiction over corporations, including recent global developments in multilateral rules for taxation of multinational enterprises ("MNEs"). In particular, the multilateral dimension of international corporate tax is undergoing significant development as we observe the trajectory of the "Two-Pillar Consensus" of the OECD Inclusive Framework, which both embeds, and calls into question, the reality of multilateralism in international taxation. Part V presents some concluding thoughts.

II. The Tax State and its Jurisdiction

A. *The Tax State*

The Treaty of Westphalia generated "a political imaginary that mapped the world as a system of mutually recognising, sovereign territorial states".[3] Taxation is a sovereign function of the state, and the "tax state" evolved as the capability to tax developed.[4] Indeed, the capability to tax underpinned the "assemblage" of "territory, authority, and rights" in the "new organising logic represented by the territorially constituted sovereign state".[5] The borders of the tax state established the bounded constitution of centralised power to tax and to govern.

One historical observer of this trend was the political economist Adam Smith, well known as the "father" of free market economics, and less well known as an advocate of taxes to finance government.[6] In *The Wealth of Nations* first published in

[2] Saskia Sassen, *Territory, Authority, Rights: From Medieval to Global Assemblages* (New Jersey: Princeton University Press, 2008) [Sassen].

[3] Nancy Fraser, "Reframing Justice in a Globalizing World" (2005) 36 New Left Review 69 at 70, footnote 2 [Fraser], discussing the analysis of Richard Falk, "Revisiting Westphalia, Discovering Post-Westphalia" (2002) 6 Journal of Ethics 311. The Treaty of Westphalia divided up the territory of Europe into states in 1648. Whether or not the Treaty really changed the distribution of power at the time, it contributed to a long-lasting idea of nation states.

[4] Wolfgang Schön, "National Sovereignty and Taxation" in Thomas Cottier & Krista N Schefer eds, *Elgar Encyclopedia of International Economic Law* (Cheltenham: Edward Elgar, 2017) 507–510.

[5] Sassen, *supra* note 2 at 35.

[6] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London: Methuan & Co Ltd, 1776) <https://www.econlib.org/library/Smith/smWN.html>, Book V, Chapter II, Part I, Article II, "Tax on Profit, or Upon the Revenue Arising from Stock" [Smith].

1776, Smith assimilated taxation and nationhood. He argued that the establishment of an efficient, fair and effective tax system was necessary to make Britain a "great nation" in an international order of other nations. The successful assertion of tax jurisdiction was essential to the success of many nation states as they evolved over the next 200 years.[7]

During the 20th century, successful tax states usually operated in a "Keynesian-Westphalian" mode as a tax and welfare state, reliant on a market economy in which both economic activity and claims for redistribution were nationally bounded.[8] The tax state succeeded as a form of governance where it enabled states to harness the returns from capitalism for the financing of public goods and redistribution. Today, the tax state is based on a two-fold justification: its capability to deliver public goods and services to its people (benefit) and its capability to carry out redistribution (ability to pay) through a welfare or social state. These two justifications underpin and provide legitimacy for the tax state's monopoly on coercive taxing power subject to the rule of law.

The tax state prospered in many OECD countries in the 20th century, on the basis of taxation of labour income and consumption by workers, as well as taxes on land, corporations and capital. However, it faced a challenge in the 1970s and 1980s, when the collapse of capital controls which had maintained the economic borders of nation states led to a new era of economic globalisation. This had a dramatic effect on tax capability. Tax policy had "traditionally been thought of as an entirely domestic matter" but "in an increasingly global world economy, nations can no longer afford to design their tax system without accounting for the effects on international trade and investment".[9] The digital revolution that started in the 1990s and continues today exacerbated the effects of economic globalisation and introduced new challenges, as was observed by the OECD in its Base Erosion and Profit Shifting ("BEPS") project that commenced in 2012.[10] Economic globalisation and digitalisation appears to have halted the upward trend in the size of the tax state, which has nonetheless maintained a relatively steady overall level of tax to GDP in most member states.[11]

B. *The International Tax System*

In public international law, the sovereign state is reconciled with the international context by a fundamental principle that recognises the right of all states to exist on equal terms. States have "the right to exercise jurisdiction and the duty to recognise

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7 Sassen, *supra* note 2 at 10.

8 Fraser, *supra* note 3 at 70.

9 Joel Slemrod, "Tax Principles in an International Economy" in Michael J Boskin & Charles E McLure Jr eds, *World Tax Reform: Case Studies of Developed and Developing Countries* (San Francisco: ICS Press, 1990) 11 at 12.

10 OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 – 2015 (Final Report)* (15 October 2015) https://www.oecd.org/tax/beps/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report-9789264241046-en.htm [OECD, *Action 1 Report on the Digital Economy*].

11 OECD, *Revenue Statistics*, <https://stats.oecd.org>.

the same right of other States".[12] Tax jurisdiction is similarly established by sovereign acts consistent with international law, and sovereignty implies that each state must be permitted to decide their own tax policy and to tax their own people, and assets or businesses in their jurisdiction.

The traditional jurisdictional rules of *residence* of the taxpayer permitting taxation of worldwide income (with an obligation to relieve double tax), and taxation on the basis of *source* of income, established the framework for an international tax system or set of norms.[13] These tax rules have legal roots in the international law concepts of jurisdiction *in personam* of a sovereign over individuals or entities, and jurisdiction *in rem* over economic activity, land or other assets within the territory.[14] The source jurisdiction was elaborated by Edwin Seligman as "economic allegiance", which requires us to consider "where is wealth acquired, where does it exist, where do the property rights become enforceable, and where is the wealth disposed of".[15] As governments began to increase their levels of taxation in an era of growing cross-border trade and investment a century ago, the assertion of jurisdiction to tax the worldwide income of residents led to the problem of double taxation across jurisdictions. The bargain to relieve double taxation was implemented by allocating to the residence state the primary right to tax worldwide income and the primary responsibility to relieve taxation where another state taxes income from economic activities sourced in their jurisdiction.

It has never been the case that sovereigns could successfully tax all their subjects as legally defined. In the 18th century, Smith accepted that the sovereign had jurisdiction to tax the rents from land in its territory and considered that taxes on goods, such as excises, could be levied in the place where goods were consumed, while customs tariffs could be levied at the borders of nations. It was more difficult, Smith argued, for states to tax capital other than land; we return to this challenge below.

It is interesting to ask, as Wei Cui does, whether the concepts of "residence" and "source" are "empty rules", or concepts that are merely operationalised by states to assert taxing jurisdiction as an exercise of political power.[16] I argue that these concepts are best understood as rules of convenience that are to be given meaning through linking legal jurisdiction to "enforcement jurisdiction".[17] We can analogise to the basis of jurisdiction in other areas of law; for example, territory is often a

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[12] Frederick A Mann, "The Doctrine of International Jurisdiction Revisited after 20 Years" in *Collected Courses of the Hague Academy of International Law*, vol 186 (The Hague: The Hague Academy of International Law, 1984) 14 at 20.

[13] It has been proposed that this rises to the level of international law – whether customary or by treaty – by Reuven Avi-Yonah, *International Tax as International Law* (Cambridge: Cambridge University Press, 2009).

[14] Yoram Margalioth, "Taxation, International" in *Max Planck Encyclopedias of International Law* (Oxford: Oxford University Press, 2011).

[15] Edwin RA Seligman, *Double Taxation and International Fiscal Cooperation* (NY: Macmillan, 1928) at 112–113.

[16] Wei Cui, "Minimalism about Residence and Source" (2017) 38 Mich J Intl L 245.

[17] Walter Hellerstein, "Jurisdiction to Tax in the Digital Economy: Permanent and Other Establishments" (2014) 68(6/7) Bulletin of International Taxation 1; Stephen E Shay, Robert J Peroni & J Clifton Fleming, Jr, "The David R. Tillinghast Lecture: 'What's Source Got to Do With It?' Source Rules and U.S. International Taxation" (2003) 56 Tax L Rev 81.

basis for jurisdiction, but it is not an absolute rule. Philip Jessup concluded that "territoriality of jurisdiction" is a rule of convenience, "not a requirement of justice or even a necessary postulate of the sovereignty of the State".[18] The rationale of convenience can be used to justify the selection of tax jurisdictional rules that may be asserted by states and that should be respected by other states. To align legal jurisdiction reasonably closely to enforcement jurisdiction, simplicity and "rough justice" approaches are usually to be favoured.[19]

Combining Jessup's concept of jurisdictional *convenience*, Seligman's notion of *economic allegiance*, and the fundamental concept of residence, we can identify the following requirements for tax jurisdiction:

(a) the duty of the taxpayer to the state, largely derived from benefits obtained from the state, including the ability to create wealth, property rights associated with it and the ability to dispose of wealth;
(b) the taxpayer's right to just taxation and the obligation of the state to deliver just taxation to the taxpayer;
(c) the ability of the state to administer and of the taxpayer to comply with the tax; and
(d) the duty of states to each other in permitting the legitimate exercise of tax jurisdiction involving the above elements.

The issue of double taxation was only a problem for individuals or enterprises engaged in activities in more than one state that actually sought to levy taxation. Yet in the real world, there are many states, historically and today, that levy no, or very little, taxation either domestically, or on cross-border transactions. These jurisdictions include so-called "tax havens", but also include many states that provide low taxes on particular kinds of income, such as labour income or capital gain; and states that deliver tax incentives that reduce taxes for foreign direct investment. Some states rely on other sources of revenue, such as ownership of resources, while other states prioritise attracting investment over tax revenues, or operate as hubs for global capital flows. Some small states, such as Singapore, have established a strong fiscal bargain through which citizens contribute to funds that cover health, housing and retirement, while maintaining relatively low taxes for internationally mobile trade, labour, and capital.[20]

The attractiveness to taxpayers of locating economic gains outside the borders of tax states, which could be achieved by locating them in low-tax jurisdictions, grew as taxes increased during the 20th century. States lacked capability to enforce taxes on individuals who were able to shift their income or assets, or corporations operating across the globe. However, states seem to have tacitly accepted this limitation of their taxing jurisdiction, or even supported the use of havens by failing to fully

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[18] Philip Jessup, *Transnational Law* (New Haven: Yale University Press, 1956) at 41, 44.

[19] David Rosenbloom, "Where's the Pony? Reflections on the making of international tax policy" (2009) 57(3) Can Tax J 489 at 496–497.

[20] The Singapore Central Provident Fund is a key pillar of Singapore's social security system for home ownership, retirement, and insurance and savings for health care. Working age participants contribute 37% of monthly wages to the fund: <https://www.cpf.gov.sg/member/cpf-overview>.

exercise their taxing capabilities. For example, high-tax states frequently, and sometimes openly, supported tax havens despite their undermining of some elements of state tax capacity.[21]

The ability of taxpayers to circumvent the borders of high-tax states expanded in the late 20th century. Income or consumption could escape the tax system; for example, banking innovations made holding income in a legal entity or account offshore accessible to many investors, or shopping could increasingly occur "offshore". Challenges include identifying and locating the taxpayer, their place of work, business or consumption, the nexus of profits to a jurisdiction, valuing intangibles and pricing transactions, tracing cryptocurrency, and investigation and collection of tax across borders. In particular, the MNE, which was first substantially established in the 1960s, was able to reduce taxes by carrying on business in low-tax jurisdictions, and by locating profit in tax havens through the interposition of intermediaries in the corporate group.

High-tax states may have seen value in having convenient low-taxed offshore locations to ease the flow of international financial capital and investment in the era of capital controls and to retain cooperation of high income or wealthy elites. In the corporate sphere, governments supported the use of low-tax jurisdictions by MNEs in their active global expansion, seeing this as aligned with national political power.

C. *Analytical Borderlands of the Tax State*

The international tax system assumes a "billiard ball" model of a many-country world in which all states are equal. Yet, states are clearly not equal in taxation (or in geopolitical power, resources, income, or wealth). This approach fails to account for the variation among states; even "tax states" are highly varied with tax levels varying from 20 per cent to 45 per cent of GDP, and there are many "non-tax" or "low-tax" states. The billiard ball model of states conceives of the border as a line separating mutually exclusive zones – one nation state from another; the state from the taxpayer; or the national from the global. It fails to account for the way in which states (and the people within them) are becoming increasingly interdependent, in terms of harms such as climate change or financial crisis, or in benefits of economic growth or technological innovation.

Instead, I argue that we need to analyse the construction, shape and movement of the border itself, drawing on the approach of Saskia Sassen who investigated the "analytical borderlands" of states in her work on global financial capitalism.[22] This approach treats the border as its own entity with a territorial and legal space that is neither purely national nor purely global. The approach of analysing the "borderlands" of tax states suggests that the border is not a hard line, but is porous,

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21 See, *eg*, Vanessa Ogle, "Archipelago Capitalism: Tax Havens, Offshore Money, and the State, 1950s–1970s" (2017) 122(5) American Historical Review 1431.

22 Sassen, *supra* note 2.

or fuzzy. However, the borderlands of tax states are not a commons, a pre-existing tax base available to all, or a neutral zone. Instead, the borderlands are "frontier zones where operations of power and domination, resistance and unsettlement, get enacted".[23] In the borderlands, we find the enactment of the global inside the national:

> The strategic spaces where many global processes are embedded are often national; the mechanisms through which new legal forms, necessary for globalization, are implemented are often part of state institutions. … embedded in various national territories.[24]

This process "denationalises" the enactment of international tax rules, changing the dimensions of the state itself. The "denationalisation" process has some similarities with the transformation of tax sovereignty that is suggested by Tsilly Dagan to occur through a competitive game between states. Dagan observes that:

> [A]lthough sovereign states still insist on preserving their formal exclusive authority in tax matters, the truth of the matter is that under conditions of competition, it is all too often the invisible hand of the international market of states, rather than the individual sovereign state, that shapes tax policies.[25]

One difference between the approaches of Sassen and Dagan is the diversity of actors who are recognised as engaging in international tax law-making, which engages states and private parties. The process of establishing tax jurisdiction in the borderlands of tax states engages complex power relations between a variety of different kinds of actors: public and private; governments and businesses; consumers and workers; and other non-government actors, including the tax profession or advisors and civil society.

In these negotiations, taxing power may expand or contract. A feature of the contested negotiations of territory and power in the tax borderlands is that many states – whether developing or developed – are seeking to *increase* tax revenues. The tipping point to an assertion of expanded tax jurisdiction may have been a response to domestic politics and fiscal pressure, for example after the global financial crisis of 2008 and more recently the COVID-19 pandemic of 2019. Tax capability is dynamic and can be expanded through leveraging technological or bureaucratic innovation, co-opting intermediary or private business capabilities. For example, during the mid-20th century, pay-as-you-go withholding dramatically enhanced the capability to tax wages by harnessing corporations as employers to collect and remit the tax. In the international context, states have in the last decade begun to

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23 Sassen*, supra* note 2 at 230.

24 Sassen, *supra* note 2 at 3.

25 Tsilly Dagan, "Tax Justice in the Era of Mobility and Fragmentation", *Revue européenne du droit, Paris: Groupe d'études géopolitiques* (31 July 2022) <https://geopolitique.eu/en/articles/tax-justice-in-the-era-of-mobility-and-fragmentation/>.

leverage the administrative and data capabilities of economic intermediaries such as corporations and banks to expand their international tax jurisdiction.

States can also extend their tax jurisdiction by co-operating with each other. Cooperation does not undermine tax sovereignty. The reverse is true: international tax cooperation is an expression of national sovereignty. Increased international cooperation is evident in changes to tax law and in tax administration through a range of "hard" and "soft" law approaches including multilateral agreements, memos of understanding, and increasingly integrated data and administration. Yet, we see continued tax competition between tax states about capital investment and skilled labour.

Finally, the (re)negotiation of tax jurisdiction is leading to changes in the tax base itself. The economic concept of "income", or net rather than gross basis taxation, was developed by Henry Simons and others on the fundamental assumption of a single government levying taxation.[26] To assert tax jurisdiction, states are increasingly shifting from a net to a gross income or turnover approach (a digital services tax, or withholding tax, for example); from a base of income to consumption; and across entity boundaries, by extending the measure of profit or income beyond the legal entity of the corporation or the territory of the state itself. Parts III and IV explore some of these developments.

III. Tax Jurisdiction over People

A. *Expanding, or Shrinking, Residence Jurisdiction*

The jurisdiction of states over the worldwide income of residents matches our expectations that "what makes a given collection of individuals into fellow subjects … is their shared residence on the territory of a modern state and/or their membership in the political community that corresponds to such a state".[27] The state of residence "stands in a position to see the entirety of the taxpayer's income and therefore is best situated to avoid international double taxation".[28] The Draft Model Tax Convention Commentary of 1927 by the Experts for the League of Nations said, "the tendency of modern fiscal law is to consider that all persons domiciled in a State should be liable to the same taxation therein whatever their nationality may be".[29]

Tax law definitions of individual residence combine criteria about home and belonging: physical presence, place of birth, personal, family, social and economic connections, intention, and legal connection to the state. The tax law must take account of mobility of people, and establishes rules or tie-breakers in domestic law or treaties to address individuals with multiple connections to different states. If these do not resolve the matter, a test of citizenship or nationality is relied on by many countries in the last resort.

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26 Henry Simons, *Personal Income Taxation* (Chicago: University of Chicago Press, 1938).

27 Fraser, *supra* note 3 at 80.

28 H David Rosenbloom, "What's trade got to do with it" (1994) 49 Tax L Rev 593 at 596.

29 1927 Model Tax Convention; see Sunita Jogarajan, *Double Taxation and the League of Nations* (Cambridge: Cambridge University Press, 2018) at 287.

We have seen in recent years the extension of the "residence" jurisdiction over individuals. Some states have expanded "residence" in response to mobility of individuals, for example by making it more difficult for residents to exit the jurisdiction avoiding tax on their worldwide income. The UK has expanded the definition of "residence",[30] and the long-standing status of "non-domiciled" resident has also been wound back.[31]

Australia has proposed modernising the tax law definition of individual residence to make it more "sticky".[32] One reason is the ability of skilled professionals to earn income in low-tax jurisdictions (such as geologists working in the Middle East), such that if the individual was not a "resident" of Australia, income tax may not be paid anywhere. This extension of "residence" draws the jurisdictional line in the tax "borderlands" in a different way with respect to another tax state (which would tax the labour income) compared to a low-tax state. If foreign tax was paid, Australia would provide a credit against the Australian tax owed. The differential tax treatment is not a result of direct engagement between the foreign (low-tax) state and the relatively high-tax state of Australia. Rather, this proposal engages Australia in a fiscal negotiation with its resident high skilled (and highly paid) workers, who may choose to exit the jurisdiction in response to tax rates.

On the other hand, the expansion of "residence" by a state does not always carry with it higher taxes. Some states have taken the alternative route of broadening "residence" while narrowing the tax obligations that go with it, to attract wealthy or high-skilled individuals to become residents in a deal sweetened with lower taxes.[33] Presumably, government think such individuals will contribute to the domestic economy in other ways. Governments implementing "residence for sale" programs abrogate the "worldwide" residence tax jurisdiction, while facilitating mobile individuals to avoid the tax jurisdiction of other states. This could be considered to run counter to the duty of states not to interfere with the ability of other states to assert jurisdiction. It could lead to direct state-to-state responses, such as the termination of bilateral tax treaties or political pressure domestically.[34] Domestic politics may also affect such concessions. Portugal has recently announced that it will abolish its low-tax "non-habitual resident" regime in response to domestic concerns about housing.[35]

Some of these issues could be addressed by the use of citizenship as the tax nexus. The US has always been an outlier in asserting jurisdiction to tax its citizens (numbering in the millions) who do not reside in the US. While the citizenship tax

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30 Her Majesty's Revenue and Customs (HMRC), *Guidance* Note *RDR3: Statutory Residence Test* <https://www.gov.uk/government/publications/rdr3-statutory-residence-test-srt>.

31 HMRC, *Tax on foreign income – 'Non-domiciled' residents* <https://www.gov.uk/tax-foreign-income/non-domiciled-residents>.

32 The Board of Taxation, *Reforming Individual Tax Residency Rules – A Model for Modernisation* (March 2019); Australian Treasury, *Modernising the individual tax residency rules* (Consultation Paper, 21 July 2023 – 22 September 2023) <https://treasury.gov.au/consultation/c2023-205344>.

33 Allison Christians, "Buying In: Residence and Citizenship by Investment" (2017) 62 Saint Louis ULJ 51.

34 For example, Sweden with Portugal and Greece; see Stewart, *supra* note 1 at ch 10.

35 Barney Jopson & Sergio Anibal, "Portugal to scrap 'fiscal injustice' of tax breaks for foreign residents", *Financial Times* (3 October 2023).

base of the US could be seen as an assertion of extraterritorial tax jurisdiction by a powerful state, it is not engaged in a contest with other states, so much as with its own citizens. Historically, the jurisdictional reach of US taxation based on citizenship may often have been unenforced and unenforceable. This changed when the US extended its power to identify and assess offshore financial income through the *Foreign Account Tax Compliance Act 2010*. Foreign-based US citizens are highly troubled by this, but they have not yet managed to persuade the US Congress to change the law. The choice to renounce citizenship is open to US citizens, but conditions are strict especially for individuals with assets, who must pay an exit tax on asset gains over a threshold.[36] One well-known example is Eduardo Saverin, a multi-billionaire who was a founder of Facebook, and who renounced his US citizenship (and residence) for Singapore in 2009 to take advantage of Singapore's territorial tax jurisdiction which makes it an attractive location for residence by some people with high global wealth or income.[37]

B. *Jurisdiction over Labour and Capital Income*

The boundaries of jurisdiction to tax work, or services, are contested in the tax borderlands. While governments work hard to maintain and protect the labour income tax base, they may also deliver lower tax rates to attract desirable people to the jurisdiction. The high-income working elite comprising skilled professionals and scientists are likely to be attractive workers; earning high wages, they are exposed and may be sensitive to high marginal tax rates. There is evidence that "superstar" inventors are responsive to taxes, but responsiveness depends partly on whether they are in their home jurisdiction or not.[38] For example, a top tax rate reduction was found to increase migration by "superstar" inventors into a country by as much as 26 per cent.

This leads to the argument that governments should reduce top tax rates or flatten the progressivity of the tax rate structure to attract, or retain, elite workers. Various countries have applied tax discounts for skilled immigrants, including Belgium, Denmark, Finland, Italy, the Netherlands and Sweden.[39] But governments face a dilemma: either devise special packages – leading to potential criticism – or cut top rates, which may undermine progressivity and revenue more generally.

Another fundamental issue is legal characterisation of the contract for services performed. The key administrative constraint for taxation of labour income is whether the tax may be collected through wage withholding from the employer or recipient of services (this is a core tax base of most tax states). Alternatively, is

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36 Internal Revenue Service, *Expatriation Tax* <https://www.irs.gov/individuals/international-taxpayers/expatriation-tax>.

37 "Eduardo Saverin", *Wikipedia* <https://en.wikipedia.org/wiki/Eduardo_Saverin>.

38 Ufuk Akcigit, Salomé Baslandze & Stefanie Stantcheva, "Taxation and the International Mobility of Inventors" (2016) 106(10) American Economic Review 2930.

39 Alejandro Esteller-More, Armedeo Piolatto & Matthew D Rablen, "Taxing High-Income Earners: Tax Avoidance and Mobility" in Nigar Hashimzade & Yuliya Epifantseva eds, *The Routledge Companion to Tax Avoidance Research* (New York: Routledge, 2018) at 304.

the taxpayer an independent contractor with personal responsibility to file a return and pay income tax? Governments expend significant effort in maintaining, and improving, withholding and "real time" data and tax collection systems to ensure the appropriate tax is collected from workers.

While the legal distinction between an employee and independent contractor has a long history, the ability of taxpayers to select and self-define the relationship has become easier, especially in the "gig" economy where service workers become small businesses. These key elements of the tax system are "privatised" as taxpayers select their own terms and structure, reducing the scope of wage withholding systems (and other aspects of labour regulation and social provision, such as workers' compensation or occupational health and safety rules).

This issue is even more complex across borders. The "source" jurisdiction is usually defined to be the place where the work is performed, with most laws or tax treaties requiring a minimum period of physical presence or a fixed place of business. The legal structure and terms of the contract for service are amenable to tax planning, which is even more of a challenge in today's era of increasing remote or digital work. Bilateral treaty rules for taxing independent professional services tend to favour the residence state; for developing countries, the provision of professional and technical services is of such importance that the United Nations inserted a new Article 12A (technical services) to permit a withholding tax to be applied to fees for such services, even if there is no fixed base in the jurisdiction.[40] This leverages a flat withholding rate on the gross fee to ensure source taxation. To address the new modes and flexibility of working, states must engage directly with the separate legal entities or platform intermediaries through which contractual services are provided, harnessing new forms of technology and international cooperation to change the fiscal bargain.

The mobility of capital has long posed a challenge to the capability of states to enforce taxation. Adam Smith was conscious of capital mobility of capital, or "stock". He observed that:

> [L]and is a subject which cannot be removed; whereas stock easily may. The proprietor of land is necessarily a citizen of the particular country in which his estate lies. The proprietor of stock is properly a citizen of the world, and is not necessarily attached to any particular country. He would be apt to abandon the country in which he was exposed to a vexatious inquisition, in order to be assessed to a burdensome tax.[41]

In this circumstance, it was inevitable, in Smith's view, that governments seeking to tax capital investment must "content themselves with some very loose, and, therefore, more or less arbitrary, estimation. The extreme inequality and uncertainty of a

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[40] United Nations, *Model Double Taxation Convention Between Developed and Developing Countries 2021*, <https://desapublications.un.org/file/914/download>, Article 12A.

[41] Smith, *supra* note 6, Book V, Chapter II, Part I, Article II, "Tax on Profit, or Upon the Revenue Arising from Stock".

tax assessed in this manner can be compensated only by its extreme moderation."[42] That is, taxes on mobile capital must be low.

Early in the 20th century, many states had higher tax rates on "unearned" (capital) income than "earned" (labour) income. Tax jurisdiction over capital income was traditionally allocated to the country of residence. The source country retains limited rights to tax dividends, interest and royalties by applying a withholding tax on the gross payment. Since the 1980s, we have seen a decline in tax rates on capital, including the corporate tax rate (we return to this below) and withholding tax rates, in response to capital mobility.

Today, the exit from a jurisdiction of a resident who owns capital may be less common than the exit or accumulation of capital outside the jurisdiction, controlled by residents in the jurisdiction.[43] The exit of the resident who owns capital may be partly addressed by exit taxes. Usually, states can locate the individual; they will be a resident somewhere (but noting the challenges of "residence" taxation discussed above). However, states have more trouble finding and taxing "offshore" capital or income.

The taxation of personally controlled capital income or gains of a resident, held offshore directly or through corporations or trusts, requires legal rules to assert jurisdiction over income that arises outside the investor's residence jurisdiction.[44] States must breach the corporate veil and attribute income to the individual resident controller through controlled foreign corporation ("CFC") rules and foreign fund rules. Alternatively, they must apply anti-avoidance or sham rules to overturn the offshore use of such entities. Until early this century, these approaches were considered to potentially breach bilateral tax treaties or operate in an extraterritorial manner. Today, the OECD has accepted this extension of taxing jurisdiction of the residence state beyond its borders into other states. In general, the rules bite only where the offshore income has not been taxed, or is low-taxed; otherwise, the residence state will usually provide a tax credit.

Successful assertion of tax jurisdiction over worldwide capital income requires states to cooperate with other states so that governments can access information, investigate, and assess and collect the tax. The era of tax secrecy may be over in respect of some forms of offshore income such as interest on foreign bank accounts. However, the substantial data sharing and cooperation required to achieve residence taxation of capital income remains a work in progress. Essentially, states have negotiated different levels of cooperation, in law and in practice, generating uneven enforcement and gaps. Enforcement of taxes including tracing the ultimate beneficial ownership of such entities, addressing offshore tax fraud and evasion and collecting the tax remains a significant challenge, and states often appear slow, and reluctant, to assert their jurisdiction by fully cooperating with other states.

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42 *Ibid*.

43 As discussed by Reuven Avi-Yonah, "And Yet It Moves: A Tax Paradigm for the 21st Century" (2013) University of Michigan Law School Law and Economics Research Paper Series, Paper 12-008.

44 See the detailed discussion in Stewart, *supra* note 1 at ch 10.

C. *The Rise of the Consumer*

An important development in the last two decades has been the rise of the consumer in so-called "market" jurisdictions as a base for taxation, not only for domestic consumption, but also in relation to international or offshore digital purchases of goods and services. The issue arises both in terms of the application of Value Added Tax ("VAT") or Goods and Services Tax ("GST") on domestic consumption, in the structure and enactment of unilateral Digital Services Taxes ("DSTs") around the world, and in proposed reform of taxation of MNEs.

The VAT multi-stage tax on "supplies" of goods or services, is today enacted in about 170 countries around the world. The spread of the VAT was at least in part driven by developed countries to align country tax systems with the World Trade Organisation principles of free trade. This was achieved by the *destination* principle which allocates tax jurisdiction to the place of residence of the end-consumer, and relieves exports from taxation. The destination principle was adopted uniformly in the European Union ("EU") VAT, and generally around the world.[45]

Until the 1990s, international sales of goods and services directly from offshore businesses to consumers ("B-to-C") were limited in scale. Cross-border shopping occurred where shoppers could physically cross the border, such as tourist shopping, or in border towns; while mail-order catalogue shopping rarely operated across national borders. Most imported goods were supplied to domestic businesses ("B-to-B") which then on-sold to resident consumers. VAT laws taxed the importation by applying a "reverse charge" mechanism that puts the obligation to remit the tax on the importing business in the jurisdiction, instead of the offshore supplier. Direct cross-border purchases by consumers were usually ignored, although export tax credits were sometimes provided for tourists.

The advent of e-commerce expanded international consumer transactions. The "disjuncture between the geographical foundations of modern taxing systems, on the one hand, and the nonterritorial character of e-commerce on the other, is at the heart of the challenge that e-commerce poses to taxation".[46] This massively expanded global consumer market in turn led to the growth of digital companies. The OECD observed that the digital economy is not at the margins of some real or physical economy, but, rather, all the economy is becoming digitised.[47] There was increased governmental concern about a loss of revenue and an unfair playing field for domestic businesses. After a slow start, governments scrambled

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[45] There is significant diversity among "real" VATs around the world, which are rather different from the benchmark "ideal" VAT/GST, including in implementation of the destination principle: see Kathryn James, *The Rise of the Value-Added Tax* (Cambridge: Cambridge University Press, 2015); Kathryn James & Thomas Ecker, "Relevance of the OECD International VAT/GST guidelines for non-OECD countries" (2017) 32 Australian Tax Forum 317 at 335.

[46] Roland Paris, "The Globalization of Taxation? Electronic Commerce and the Transformation of the State" (2003) 47(2) International Studies Quarterly 153 at 162; see also Richard L Doernberg *et al*, *Electronic Commerce and Multijurisdictional Taxation* (Netherlands: Kluwer Law International, 2001) at 2; and Arthur Cockfield *et al*, *Taxing global digital commerce* (Netherlands: Kluwer Law International, 2013).

[47] OECD, *Action 1 Report on the Digital Economy*, *supra* note 10.

to extend their VAT jurisdiction to international digital supplies of goods and services. This included goods acquired through online global sales platforms such as eBay, Amazon or Alibaba, digital services and content delivery in music, film, books and news by Netflix, Disney and Apple, and the invention of entirely new forms of digital use and value creation, such as on Facebook and Twitter. For governments to expand jurisdiction in this way required them to access the digital intermediaries and build on the technology that enabled the online sales of goods and services.

The expansion of the international consumption base has also led some states to cooperate with other states. While there is a lot of variation between VATs in EU member states, EC Directive 2006/112/EC establishes fundamental parameters for the VAT base and rate in each country.[48] The EU Directive on e-commerce was issued in 2002[49] and led to early commitments to comply by digital firms such as Amazon. In 2015, the Global Forum on VAT brought together more than 100 countries to propose the taxation of offshore supplies in B-to-C transactions through a system for withholding and remittance of VAT by the offshore platform or seller.[50]

The residence of the consumer for delivery or payment (*eg*, a credit card) would provide the administrative and legal proxy for the seller to identify which jurisdiction had the right to tax collected on the sale.[51] Australia and Singapore have both extended the GST to offshore digital goods and services supplied to domestic consumers. This approach is gradually being adopted in a number of countries around the world, harnessing the intermediary seller or platform to calculate, collect and remit the tax on the price charged to the ultimate consumer. The new systems depend on quasi-voluntary compliance of the large digital corporations; their successful application required harnessing large corporate platforms and data systems in a new fiscal bargain that establishes a new jurisdiction for taxing some kinds of cross-border consumption. We see in the VAT the most advanced form of cross-country cooperation in the establishment of the EU "One-Stop-Shop" system for collection and remittance of VAT from one member state to others across the EU, a system that is gradually expanding in number of businesses and volume of consumption covered, both within the EU and for imports into the EU.[52]

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48 EC, *Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax*, [2006] OJ L 347/1.

49 EC, *Council Directive 2002/38/EC of 7 May 2002 amending and amending temporarily Directive 77/388/EEC as regards the value added tax arrangements applicable to radio and television broadcasting services and certain electronically supplied services*, [2002] OJ L 128/41.

50 OECD, *Recommendation of the Council on the Application of Value Added Tax/Goods and Services Tax to the International Trade in Services and Intangibles*, Doc No OECD/LEGAL/0430 (2016) <https://legalinstruments.oecd.org/en/instruments/OECD-LEGAL-0430>.

51 OECD, *International VAT/GST Guidelines* (Paris: OECD Publishing, 2017) at 66: Guidelines 3.5, 3.6.

52 EC, *One Stop Shop* <https://vat-one-stop-shop.ec.europa.eu/index_en>.

IV. Tax Jurisdiction over Corporations

A. *The Fictional Residence of Corporations*

Around the world, governments have effectively harmonised the legal form of the corporation so that this legal fiction is today universally recognised by states, a move that has been crucial for global capitalism.[53] Corporate taxation is also nearly universal, but the legal fiction of the corporation creates a puzzle for corporate tax. If we tax corporations, the burden is always shifted to real people: the owners of the company or of capital (who may be domestic or foreign); workers; or consumers.

A standardised concept of corporate residence, like the concept of the corporation itself, has also become "one of the cornerstones of corporate income taxation, both in domestic and international law".[54] At first glance, jurisdiction to tax a resident corporation seems to be the same as for a resident individual: worldwide jurisdiction. But the reality is that most corporate income is taxed on a "territorial" basis – where the business activity is done and the business income is earned. The territorial system (taxing at the location of the business) was applied early in the 20th century in many countries, in line with a realist approach to enforcement of tax jurisdiction.

During the 20th century, in part because governments sought increased revenue, many corporate tax systems shifted to a "classical" mode in which both the company and shareholders were taxed. The jurisdictional base was expanded, in some countries at least, to worldwide income of corporations, with a credit for foreign taxes. This was possible in an era of capital controls, with some leakage via tax havens. The territorial (exemption) approach reappeared during the 1980s, as governments sought to encourage increased inbound and outbound investment. Most countries today apply a hybrid approach that exempts foreign active business income but applies tax to foreign passive income, for example by CFC rules.

The "residence" of a corporation layers a fiction of geographical location on top of the fiction of personhood. Corporate tax residence is usually based on the place of incorporation, or the place of central or effective management or control; because a corporation "in a natural sense does not reside anywhere, some artificial test must be applied".[55] As John Prebble observed:

> Humans must have spent at least *some* time in the jurisdictions where they were born, but (to the extent that companies are capable of having a substantive connection with any geographical place) companies may have no substantive

[53] Katharina Pistor, *The Code of Capital: How the Law Creates Wealth and Inequality* (Princeton: Princeton University Press, 2019) explores the broader effects of global standardisation of the legal form of the corporation and of financial transactions such as debt and equity investment.

[54] Edoardo Traversa ed, *Corporate Tax Residence and Mobility* (EATLP International Tax Series No. 16) (Netherlands: IBFD, 2017) at 1 [Traversa].

[55] *De Beers Consolidated Mines Ltd v Howe (Surveyor of Taxes)* [1906] AC 455 at 458 (HL). This case is the origin of the "central management and control" test; see John A Jones & Johann Hattingh, "De Beers Consolidated Mines Ltd v Howe (1906): Corporate Residence: An Early Attempt at European Harmonisation" in Dominic de Cogan & John Snape eds, *Landmark Cases in Revenue Law* (Oxford: Hart Publishing, 2019) 67.

> connection at all with the place of their incorporation. The result is that the place-of-incorporation test of corporate residence for some companies reaches a result that is purely formal and devoid of any substance. … The solution is only a little happier when courts or legislatures try to compose substantive corporate residence rules.[56]

Where the corporation carries on business, then its residence in the jurisdiction can operate as a good tax handle for the government. However, corporate residence can just as easily facilitate the avoidance of tax jurisdiction. Much tax planning, until the COVID-19 pandemic, involved appointing directors of corporations who are residents in specific (usually low-tax) jurisdictions, or flying directors into jurisdictions to hold board meetings to ensure corporate tax residence. The challenges of locating the corporate residence have increased in an era of digital corporate management. In this new era, even the supposedly practical test of central or effective management and control may become increasingly difficult to apply.

The concept of corporate residence is paradoxically "both reinforced and eroded by the evolution of the global economy".[57] The development of the corporation into the flexible, mobile, and globally proliferating form of the MNE established across geographical territories poses a significant challenge to the tax state. The MNE is ideally suited to facilitate the distribution of the ownership of assets and the construction of transactions across high-tax and low-tax territories around the world. As a consequence, the rule of corporate "residence" no longer serves its jurisdictional purpose.

B. *Source: Where Corporations Do Business*

The pragmatic response of states to taxing corporations doing business without a corporate presence was the concept of "permanent establishment" ("PE"). Traditionally, a PE is a fixed place of business; an office, a mine, a factory, a construction site. This concept looks through the corporate entity form to the underlying activity. The net profit attributable to the PE is taxable in the source jurisdiction.

The PE concept was intended to achieve, and was successful at achieving, a *convenient* taxation base that is reasonably certain and capable of being enforced by the jurisdiction where the business is carried on, and that applies to net gain. The residence state of the entity would be required to relieve double taxation by applying an exemption or credit for foreign tax. The PE concept also limits source taxation by providing a threshold that must be met before tax can be levied. In general, states successfully harmonised the PE concept; however, in the details, a jurisdictional battle was waged, and led to the positioning of the tax border differently through bilateral tax treaties with different states. The delimitation of the PE threshold has

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[56] John Prebble, "Ectopia, Tax Law and International Taxation" (1997) 5 Brit Tax Rev 383 at 389–390 [emphasis in original].

[57] Traversa, *supra* note 54, at ch 1 near footnote 59; Wolfgang Schön, "International Tax Coordination for a Second-Best World (Part I)" (2009) 1(1) World Tax Journal 67 at 69–70.

long been a subject of negotiation in the borderlands of the tax state, engaging capital exporting and capital importing states, rich and poor states, and MNEs.

The concept of PE faced significant challenges in the global digital economy. A key purpose of the OECD BEPS project was to address challenges to source taxation of business profit including the PE nexus. The practical advantages in identifying a PE were also diminished as value is increasingly found in intangible assets such as intellectual property, securities, trademarks or brands, and returns can be generated from a jurisdiction without a physical presence. The legal source of income from intangibles may be based on factors such as the location of the payer; the place of the contract, funds payment, or other legal transactions; or some indirect identification of the underlying economic activity that produced the income.[58] All of these elements may be uncertain, arbitrary or easily manipulated.

Finally, the allocation of profit to the PE became a matter for negotiation, and its flexibility and complexity led to transfer pricing becoming among the most disputed of tax jurisdictional issues. The digital economy increased the difficulty of identifying comparable prices, valuing transactions and assets, and locating the DEMPE factors of development, enhancement, maintenance, protection and exploitation of intangible assets. The move in the digital economy away from mass industrial capitalism (dominant in the 20th century) towards tailored services for which each consumer pays a unique price undermines comparability, while modular production, value chains and centralised IP make the production of such bespoke goods and services ever more efficient. Internally, each MNE operates uniquely. Prices may be fully integrated within the MNE, or market prices for services and products are determined uniquely, in which case, comparability also loses its usefulness.

The extent to which MNEs may have become completely uncoupled from the states in which they are resident, or headquartered, is unclear. The economist Mihir Desai has suggested that "the archetypal multinational firm with a particular national identity and a corporate headquarters fixed in one country is becoming obsolete as firms continue to maximise the opportunities created by global markets".[59] By tailoring tax systems and enclosing the territories of low-tax havens inside the boundaries of the corporate group, MNEs take on some of the characteristics of states. They extract value from labour and investment outside the jurisdiction of states into a different juridical and territorial space that enables the accumulation of economic rents. Arnold Harberger argued that the economic rent of MNEs itself operates like a tax on value that should go to consumers in the market, or to governments. He concluded that there is no easy way to tax such monopoly profits, but that the corporate income tax is the best way.[60]

It appears that to tax such corporate profits, governments need either to devise a new way of establishing a nexus for profit to their jurisdiction, or to extend their cooperation with other states, increasing interdependence so as to re-establish their national tax jurisdiction on a stable footing. We can see this being attempted by

58 John Prebble, "Why is Tax Law Incomprehensible?" (1994) 4 Brit Tax Rev 380 at 384.

59 Mihir Desai, "The Decentering of the Global Firm" (2009) 32(9) The World Economy 1271 at 1271.

60 Arnold Harberger, "The Incidence of the Corporation Income Tax Revisited" (2008) 61(2) Nat'l Tax J 303.

states both unilaterally and multilaterally: the former, in DSTs and the latter, in the Two-Pillar multilateral consensus.

C. *Digital Services Taxes*

The growth in importance of the consumer has led to the unilateral development by a significant minority of countries around the world of new taxes on "digital" sales, transactions and activities. DSTs tend to be levied at a low flat rate (*eg*, 2 or 3 per cent) on gross revenues in connection with defined digital services for consumers or users in the jurisdiction. DSTs are a kind of excise on specific forms of revenue from advertising, or sales on digital platforms, and not on profits or income.[61]

Usually, DSTs apply to large MNEs, for example with revenues exceeding the €750 million threshold for "country by country" ("CbC") reporting in the previous year. Covered digital services include online marketplaces enabling sales of goods and services, including online advertising and social media digital interface services or internet search engines. The nexus is based on the presence of the user in the jurisdiction, usually by accessing an IP address used by the service recipient. The DST is to some extent a backstop to the corporate tax which is unable to collect tax on profits made from users in the jurisdiction.

Governments began to take unilateral action to levy DSTs on MNEs which accrued revenue from consumers in their jurisdiction because an agreement had not been reached in the OECD about how to address the taxation of MNEs in the global digital economy. India was a first mover with its digital equalisation levy enacted in 2016. Soon after, France enacted a DST, followed by the UK. The spread of DSTs has been criticised as likely to lead to chaotic and complex double taxation on gross revenues around the world. A potential trade dispute ensued, as the US government argued that DSTs are unfairly targeted at US-based digital MNEs. Under President Trump, the US Trade Representative initiated a trade investigation into DSTs enacted by France, and later by Austria, India, Italy, Spain, Turkey and the UK, on the basis that these were discriminatory trade measures burdening US digital companies and are inconsistent with principles of international taxation.[62]

The DST takes us far from a corporate income tax on net profit. In a sense, we are back to the future – in Adam Smith's time, governments levied an excise on salt. Today, the tax is levied on digital "clicks". Despite this, the DST has also been praised as a suitable levy to capture tax on the high profits derived by large digital MNEs delivering to mass consumer markets, without a physical presence in the jurisdiction.[63] While DSTs have generated some tax revenue, they also play a larger

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61 Christopher Noonan & Victoria Plekhanova, "Digital Services Tax: Lessons from the Section 301 Investigation" (2021) 1 Brit Tax Rev 83.

62 Office of the US Trade Representative, "USTR announces next steps of Section 301 Digital Services Taxes Investigations" <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2021/march/ustr-announces-next-steps-section-301-digital-services-taxes-investigations> (26 March 2021).

63 See, *eg*, Wei Cui, "The Digital Services Tax: A Conceptual Defense" (2019) 73(1) Tax Law Rev 69; Daniel Shaviro, "Mobile Intellectual Property and the Shift in International Tax Policy from Determining the Source of Income to Taxing Location-Specific Rents: Part One" [2020] Sing JLS 681; Daniel

role in the geopolitical negotiations over reforming the corporate tax, most importantly between the US and other countries, in the Two-Pillar Consensus. In 2018, the European Commission proposed a common DST for Europe.[64] It has postponed this until the Inclusive Framework negotiations are settled. More recently, Canada and other jurisdictions have indicated they will implement a DST if the Two-Pillar Consensus is not achieved.[65] Thus, DSTs also form part of a complex bargaining process involving states, MNEs and multilateral forums such as the OECD and EU.

D. *The Two-Pillar Consensus*

Unilateral DSTs address one aspect of taxation for the global digital economy. However, national policymakers can only address the challenges of MNEs by establishing coherent rules that draw aside the corporate veil and directly focus on the location and appropriate tax rate for corporate profits.[66] The Two-Pillar Consensus of the Inclusive Framework comprising 140 countries, established by the OECD, aims to establish an overall approach to taxing the MNE's corporate profits, and their allocation to a specific jurisdiction by an agreed nexus rule, or to agree that countries levy a "minimum" tax on such profits. Whatever approach is taken, the corporation and especially its "head" or ultimate parent entity, remains a valuable entity for tax data and collection. The "residence" jurisdiction of the head entity may become increasingly important in collecting such information and sharing it with other governments. This then requires us to consider what are the duties of that location in collecting and sharing the data, and possibly taxes, with other jurisdictions.

We can see these developments in the multilateral negotiations for the Two-Pillar Consensus (including 136 out of 140 countries) in October 2021.[67] Pillar One examines the entire group accounting profit and allocates a proportion of it to the state of the end-consumer; the market state where consumers are located in respect of the largest MNEs. Pillar Two aims to establish a new global minimum tax for MNEs no matter where they operate in the world.[68] The Consensus was achieved after the US expressed a strong commitment, as the White House stated: "The United States is now seeking a global agreement on a strong minimum tax through multilateral

Shaviro, "Mobile Intellectual Property and the Shift in International Tax Policy from Determining the Source of Income to Taxing Location-Specific Rents: Part Two" [2021] Sing JLS 128.

64 EC, "Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services", COM(2018) 148 final.

65 Government of Canada Department of Finance, "Digital Services Tax Act" <https://www.canada.ca/en/department-finance/news/2021/12/digital-services-tax-act.html> (14 February 2022).

66 Scott Wilkie, "New Rules of Engagement? Corporate Personality and the Allocation of 'International Income' and Taxing Rights" in Brian Arnold ed, *Tax Treaties after the BEPS Project: A Tribute to Jaques Sasseville* (Toronto: Canadian Tax Foundation, 2018) 349.

67 OECD, "Tax and digital: OECD G20 Inclusive Framework on BEPS invites public input on the Pillar One and Pillar Two Blueprints" <https://web-archive.oecd.org/2021-02-05/566289-oecd-g20-inclusive-framework-on-beps-invites-public-input-on-the-reports-on-pillar-one-and-pillar-two-blueprints.htm> (12 October 2020).

68 OECD, "Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy" (8 October 2021).

negotiations."[69] It was endorsed by the G20 Finance Ministers who claimed, "we have achieved a historic agreement on a more stable and fairer international tax architecture".[70]

Pillar One aims to ensure a fairer distribution of taxing rights to market countries for the largest MNEs, including digital companies, regardless of whether firms have a physical presence. It applies to allocate some MNEs with global turnover exceeding €20 billion, reducing to €10 billion after 2030, and with profit before tax/revenue above ten per cent. It is estimated that this will cover only about the top 100 global MNEs. Apple, Microsoft, Amazon, Alphabet (Google) and Facebook are in the top ten by market capitalisation, but other top 100 global companies are in traditional sectors including retail, cars, finance, pharmaceuticals, foods and oil or mineral resources.[71] For these companies, 25% of MNE profit above ten per cent will be allocated to be taxed in market jurisdictions where there is a minimum €1 million in revenue derived (but for jurisdictions with small GDP, this is lowered to €250,000).

Pillar Two, or the Global Anti-Base Erosion Rule ("GloBE") is not a global corporate minimum tax. Instead, it is a set of tax rules to be enacted by participating countries in their domestic law, consistently with an international framework of model rules and guidance. It applies to MNEs with revenues over a threshold of €750 million at a rate of 15%. The 15% effective tax rate will be determined on a CbC basis, requiring the minimum to apply in each jurisdiction. If the effective tax rate in a jurisdiction is lower, then the country where the parent company or another entity is located can levy a top-up tax. However, a new norm has been introduced in the negotiating process, as the ability of a government to enact a Qualifying Domestic Minimum Top-up Tax ("QDMTT") in order to itself capture revenue from the minimum 15% tax has made the GloBE feasible and likely politically acceptable across a wide range of countries. Participating countries are required to carry out law reforms in time for an effective start date, in general, in 2024.

In respect of Pillar One, the multilateral tax treaty for the allocation of Amount A is now available for signature.[72] However, despite the drafting of a treaty and the many countries formally involved in the process, this apparent multilateralism is, in the end, controlled by one jurisdiction: the United States. For entry into force, the treaty requires ratification by at least 30 jurisdictions including the headquarters of at least 60% of MNEs expected to be within scope – which demands signature by the US. Even if this is achieved and the multilateral regime were to commence, the convention will automatically terminate if the US were to withdraw from the agreement.[73]

It seems very unlikely that the US will join a multilateral treaty to tax MNEs, so Pillar One will not proceed in its proposed form. In respect of Pillar Two, it is

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[69] The White House, "FACT SHEET: The American Jobs Plan" <www.whitehouse.gov/briefing-room/statements-releases/2021/03/31/fact-sheet-the-american-jobs-plan/> (31 March 2021).

[70] G20, Communique, <http://www.g20.utoronto.ca/2021/210710-finance.html>.

[71] PwC, "Global Ranking of the Top 100 Public Companies by Market Capitalisation" <https://www.pwc.com/gx/en/services/audit-assurance/publications/global-top-100-companies.html>.

[72] OECD, "International tax reform: Multilateral Convention to Implement Amount A of Pillar One" <https://www.oecd.org/tax/beps/multilateral-convention-to-implement-amount-a-of-pillar-one.htm>.

[73] *The Multilateral Convention to Implement Amount A of Pillar One*, Article 51, Annex I.

not yet clear whether the US domestic corporate minimum tax, or its tax on Global Intangible Low Taxed Income ("GILTI"), can be made consistent with the OECD-designed GloBE. Nonetheless, the US continues to take steps in support of the Consensus, most recently recognising that Qualifying Domestic Minimum Taxes established under Pillar Two will be eligible for a US foreign tax credit.[74]

Despite the weaknesses in the multilateral framework for both Pillar One and Pillar Two, this process has introduced several important features that are likely to have a significant impact on the future shape of international tax. These include a "global MNE" approach to determine the MNE's globally determined taxable profits, using consolidated accounting profits. This has the potential advantage of reintroducing a single useful "tax handle" into the state's tax armoury, at the level of the MNE. The place of residence, or incorporation, of the parent company of the MNE will be the place of administration but Pillar One would allocate some taxing rights to to market jurisdictions. While not yet legally effective (except in unilateral DSTs), the market jurisdiction, being the location of the end-consumer, now has a legitimate and recognised entitlement to tax jurisdiction.

Pillar Two potentially can succeed in establishing a "floor" for tax competition. It is well advanced in its adoption in some jurisdictions, having been adopted in the EU by a directive mandated for all member states, and by commitments in various other countries around the world, although Canada and Australia are still at the stage of draft legislation; the United Kingdom, Japan and South Korea have enacted the rule. There are still many important jurisdictions which have not progressed Pillar Two, including the US, China and India, but there is momentum attached to the Pillar Two process. Assuming this process of multilateral rule making continues to be implemented by domestic law reform in, one would expect, somewhat diverse ways, we can observe the development of a new way of defining jurisdiction. The process for ensuring compatibility (by peer review), and ongoing maintenance and interpretation of this regime, has yet to be worked out, but we can say at least that it is an entirely novel approach to defining jurisdictional borders that crosses state borders, and draws on new sources (such as financial accounting), as well as relying fundamentally on interstate cooperation, to build elements of a new international tax system for MNEs.

V. Conclusion

This article considered tax jurisdiction in a global digital era and in a new multilateral reality of international tax. The examples discussed in this article show that governments expand or retract tax jurisdiction over income, entities and activities both inside and outside their territory. This occurs in response to a dynamic set of international interactions and interdependencies.

It was argued that the "billiard ball" model of tax states struggles to explain the shifting boundaries of tax jurisdiction and the contradictory approaches of tax competition and cooperation by states. It does not provide us with the right information

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[74] Internal Revenue Service, Notice 2023-20, *Guidance Regarding the Foreign Tax Credit and Dual Consolidated Losses in Relation to the GloBE Model Rules.*

to make a judgment as to whether the tax imposed on economic return in the global digital economy is too little or too much, let alone which country is entitled to tax it. Nor does it equip us to answer the question of whether states must recognise the right of other states not to exercise tax jurisdiction, or what states should do when people, businesses and assets become intertwined across states, deriving gains linked to two or more states, or seemingly to none of them.

Applying an alternative approach to investigate the "analytical borderlands" of the tax state, the examples presented show that the shifting borders of the "tax state" overlap with but are not coextensive with the geographical territory of states. The "borderlands" of the tax state are a place of contestation between governments and non-governmental actors to establish tax jurisdiction and capture economic return. The debate about international corporate tax is largely framed as being about where to tax, and indeed this is the narrative of the OECD. However, the more fundamental issue at stake is whether taxation is levied at all: it is about ensuring a reasonable level of taxation to finance governments. States are demonstrating a new assertiveness aiming to expand tax jurisdiction, and appear to understand that cooperation between states will enhance their tax capability and can support expanded tax jurisdiction. However, there are many contradictions as states feel the pressure of global capitalism and change their tax laws competitively to attract capital and people, and as taxation continues (as it always has been) to be intertwined with geopolitics. Tax jurisdiction is established through myriad interactions in the shifting borderlands of states.

The process of enhancing tax capability by interstate cooperation, harnessing global intermediaries and new technologies in taxation, requires new international tax laws. These changes will enhance states' jurisdiction to tax, while at the same time "denationalising" tax law-making and tax administration. However, it is not clear how far the multilateral developments in the Two-Pillar solution will enhance tax capacity or revenues, or how far they will re-establish private gains from labour and capital, both for individuals and MNEs.

While we wait to see what states will do in response to the Two-Pillar consensus, the United Nations has for the first time passed a resolution suggesting the possibility of a UN-based global multilateral tax convention, framework or negotiation process.[75] The resolution was led by the Africa Group (especially Nigeria) and was opposed by the United States and other OECD member states.[76] For its part, Nigeria has refused to participate in the Inclusive Framework Consensus and proposed a range of unilateral legislative solutions to the challenge of taxing gains in the global digital economy. These developments indicate a fundamental divide, and lack of legitimacy, of current multilateral processes.

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75 UN GA Economic and Financial Committee (Second Committee), *Promotion of inclusive and effective international tax cooperation at the United Nations*, 77th Sess, Agenda Item 16, UN Doc A/C.2/77/L/11/Rev.1, 16 November 2022 at [2].

76 UN GA Economic and Financial Committee (Second Committee), *United States: amendment to draft resolution A/C.2/77/L.11/Rev.1*, 77th Sess, Agenda Item 16, UN Doc A/C.2/77/CRP.2, (22 November 2022): "Delete from operative paragraph 2: 'including the possibility of developing an international tax cooperation framework or instrument that is developed and agreed upon through a United Nations intergovernmental process'".

There has been less attention paid to international tax jurisdiction over people – their residence, labour and capital income. Yet this is likely more important for governments than corporate taxation: the personal tax base, encompassed by personal income taxation and consumption taxes, delivers the lion's share of revenues for most countries. Tax jurisdiction in law and reality ultimately reflects labour and capital relations, power and inequalities, as well as relations of the state with other states. We might wonder at the domestic politics of taxation, and the international tax relations between states and taxpayers, which lead many governments to prefer to negotiate over relatively minor tax revenues from MNEs, while failing to close international tax loopholes for individuals, or to ensure tax reform to achieve adequate and fairly collected revenues at home. The new, explicitly multilateral processes in international corporate tax bring the politics of taxation to the surface, revealing what have historically been implicit exercises of political power that underpin the rules for tax jurisdiction. There has not yet been such an explicit contest over the levying of taxation on people in the global digital economy.