Criteria of International Tax Policy

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I. INTRODUCTION

A generation ago, Professor (now Circuit Judge) Joseph Sneed identified seven pervasive purposes of the income tax useful in evaluating proposals to change income tax provisions.[1] This paper asks

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1. Joseph T. Sneed, *The Criteria of Federal Income Tax Policy*, 17 STAN. L. REV. 567 (1965), *expanded in* JOSEPH T. SNEED, THE CONFIGURATIONS OF GROSS INCOME (1967) [hereinafter CONFIGURATIONS].

whether those criteria also apply to the international aspects of the United States income tax, and whether other criteria might also apply. Sneed's criteria are:

> 1. Adequacy. To what extent does the provision raise adequate income?
> 2. Practicality. How easily is the provision administered by both the government and taxpayers? This criterion calls for provisions with bright lines that respect normal business and accounting practices, and that are easy and inexpensive to enforce.
> 3. Equality. To what extent does the provision impose equal taxes on those with equal incomes?
> 4. Stability. To what extent does the provision contribute to economic stability?
> 5. Reduced economic inequality. To what extent does the provision reduce economic inequality by disproportionately increasing tax as wealth increases?
> 6. Free market compatibility. To what extent does the provision distort what would happen in the market in its absence?
> 7. Political order. To what extent does the provision complement or contradict the Constitution or nontax statutory provisions or implement the aspirations of a dominant political group?[2]

International income tax provisions can be divided into five groups. There are provisions defining the territory, such as those specifying the geographic source of income,[3] or the definition of a resident.[4] Group two provisions are designed for uniquely international events, such as currency translation[5] (and there may be arguments about whether groups one and two constitute but a single class). A third group of provisions are ordinary, domestic tax provisions that happen to find their greatest field of application in the international sphere. An example is allocation of income.[6] The largest number of international tax provisions are overlays. There is a perfectly good domestic provision that has problems in the international area, so a new provision is enacted that relates to those international problems. An example is the area of tax-free incorporations, which under previous law permitted some gains to

2. The close reader has noted that the statement of each criterion has assumed that no provision will perfectly implement that criterion, nor will any completely destroy it. In each case, one is comparing the proposed provision to the current one, and it is a matter of direction (e.g., does this provision increase or reduce economic stability?) and degree (by how much?).
3. I.R.C. §§ 861–865 (2004).
4. *Id.* § 7701(b)(1)(A).
5. *Id.* §§ 964(b), 988.
6. *Id.* § 482.

escape tax when the property was transferred to a foreign corporation.[7] Finally, there are a series of provisions that use the tax laws to implement nontax policies, such as international antiboycott legislation.[8] Tax criteria do not often influence the enactment of provisions in this fifth group, but they may be crucial in determining their nature.

Professor Sneed's criteria are meant to be used on individual provisions, rather than on an entire subsystem, and are meant to be analyzed in much more detail than is done below. However, it is instructive to take an impressionistic look at the extent to which his criteria seem appropriate to international provisions.

II. THE SNEED CRITERIA AND INTERNATIONAL TAX

A. Adequacy

Adequacy on its face seems to assume that there is a set amount of income required by the federal government.[9] For our purposes, it is easier to ask whether the provision tends to increase or decrease federal revenues.

Some international tax provisions decrease revenues. One thinks of the foreign earned income and housing exclusion, whereby the first $80,000 of earned income of a U.S. citizen with a bona fide foreign residence is excluded from gross income[10] or the exclusion of certain U.S. bank interest from the taxable income of nonresident aliens.[11]

Tax treaties occupy a strange position. The United States has signed

7. *Compare id.* § 351 (nonrecognition of gain or loss on transfer of property to a corporation if exchanged for a controlling share of its stock) *with* § 367 (taxation of some gain on transfer of property by a U.S. corporation to an 80% controlled foreign corporation).

8. *Id.* § 999 (requiring reports of solicitations to participate in an international boycott); *id.* § 908 (reducing the foreign tax credit of persons who cooperate with international boycotts); *id.* § 952(a)(4) (characterizing payments of illegal bribes or kickbacks as Subpart F income).

9. A cynic would suggest that regardless of which party rules, there is no limit on the spending desires of the federal government. But when Democrats are in charge, spending is restrained by the state's ability to collect taxes, while Republican spending is restrained by the government's ability to borrow.

10. I.R.C. § 911.

11. *Id.* § 871(h). One might argue that this is not truly a loss of revenue because if this bank interest were taxed by the United States, the gross amounts on deposit in U.S. banks would be severely reduced with the result that the banks would have less taxable income and would pay much less tax. A careful empirical study might establish the truth of this proposition, but I find it dubious.

more than forty tax treaties. Most of them are with our major trading partners. They reduce or eliminate tax at source on investment income, grant the first right to tax to the source state on business income and personal service income but only if that income is earned through a permanent establishment or a fixed base, and require the home state to relieve double taxation by granting either a credit or a deduction for taxes paid in the source state. The practical effect (much simplified) is that the ability to tax interest and royalties is reserved to the home state; tax on dividends is split roughly evenly between the source and the home state; and business income is taxed almost entirely by the source state. Through the late 1980s, the United States was a net capital exporting state; since about 1990, it has been a net capital importer, though it remains a net exporter for foreign direct investment (mostly stocks and bonds of controlled foreign corporations). The capital export is about three fourths of the capital import.[12] So the net tax effect will depend on the kinds of income earned by those capital exports.

When the basic provisions of tax treaties became fixed, the United States was a net capital exporter in all categories. So its revenue benefited from the way tax treaties exempted interest and royalties from tax in the source country, and from tax treaties' limit on source country taxation to half the tax on dividends. Provisions granting the source country's unlimited right to tax income from real estate simply confirmed the reality that the source country had the power to do so because it had control of the realty, the income-generating entity. The provisions on taxing business income and personal services income carve a slice from the source country's otherwise limitless tax jurisdiction: source country tax will be imposed only when the activities in the source country reach a certain degree of intensity that is called either a permanent establishment or a fixed base. The practical obligation imposed on the home state by tax treaties was to mitigate double taxation by providing either a credit for source country tax or a deduction for source country income. Most capital exporting states were already doing this as a matter of domestic law, so although the promise was very valuable to capital-importing states (because without it the capital flow would be significantly reduced), these provisions had no net cost to the capital-exporting states because they were already providing it. Thus, when the income tax treaties' provisions became fixed for the United States, the provisions were revenue-enhancing.

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12. Elena L. Nguyen, *The International Investment Position of the United States at Yearend 2001*, 82 SURV. CURRENT BUS. 10 (2002); Russell Scholl, *The International Investment Position of the United States: Developments in 1971*, 52 SURV. CURRENT BUS. 18 (1972).

Tax treaty status today depends on the precise figures, but it is fair to say that portfolio investment (where the United States is more frequently the source state today) favors the home state, and foreign direct investment (where the United States is more frequently the home state) appears to favor the source state, but in fact favors the home state. Consequently, as the United States shifts its position from home to source state, treaty provisions that were once revenue-enhancing become revenue-draining.

Most international tax provisions tend to increase federal revenues. The basic problem of international tax is that a plethora of national jurisdictions impose widely varying taxes on different tax bases and at different rates. Given complete freedom, a rational taxpayer selects the tax system that produces the lowest effective tax, whether by reducing the tax base, reducing the rate, or evasion. Most international tax provisions are designed to cabin that freedom. For instance, a taxpayer can establish a wholly-owned corporation and transfer assets to it without paying tax on the gain that has accrued on those assets.[13] If these assets were located outside the United States or were intangible assets, they could be sold by a foreign taxpayer without realizing gain. A special international tax provision requires that the incorporator pay tax on some of these assets at the time of incorporation, thereby increasing federal revenues.[14] Likewise a taxpayer's attempt to allocate income to a low-tax jurisdiction or to allocate deductions to the United States may be foiled by the Commissioner's use of a provision requiring an accounting system that clearly reflects the income of each taxpayer.[15]

B. Practicality

Practicality in domestic tax provisions usually refers to the clarity of the provision, the precision of the lines it draws, the cost of practical enforcement, and the extent to which its dictates conform to the way taxpayers would normally act.[16] With international tax, a new aspect of practicality is introduced. The tax must be collectible. This is because the United States does not have continued jurisdiction over the taxpayer, and may not have power over the asset when the tax that would otherwise be due remains unpaid.

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13. I.R.C. § 351.
14. *Id.* § 367(a).
15. *Id.* § 482.
16. *See* CONFIGURATIONS, *supra* note 1, at 3 ("Practicality obviously refers to the feasibility of a provision.").

It is for this reason that capital gains on stock, bonds, and other movable assets are not taxed by the United States unless the owner is a U.S. person.[17] This is true even if the stock or debt is issued by a U.S. corporation. The taxpayer is not subject to U.S. power, and the asset that formed the connection to the United States no longer belongs to the taxpayer.

Another example: When a foreign corporation earns income in the United States, the foreign corporation pays U.S. income tax on that income in the year in which it is earned.[18] To equalize the tax treatment of the foreign corporation with that of a U.S. corporation, the foreign corporation should pay a further tax to the United States based on the extent to which the foreign corporation's dividends consist of income earned from U.S. businesses.

Enforcement of the first tax was easy; enforcement of the second tax was difficult. The foreign corporation was never publicly traded; though a foreign corporation, it was kept separate from other businesses of the group to insulate related entities from litigation in the United States. It was difficult for the IRS to discover when the U.S. operation had paid dividends so that it could collect the second tax.

Compare the branch profits tax, which substitutes for the dividend tax. It is triggered when there are earnings that are repatriated from the U.S. operation. This flow of capital from the United States to a foreign location is easier to trace than the payment of a dividend abroad because it uses the banking system, and matching it with a branch interest tax stymies the attempt to avoid it by making the original capital contribution as a loan rather than a stock purchase.[19]

So it is fair to say that practicality is an important criterion of international tax. Another example of provisions that owe their shape to this kind of practicality include the limitations on outbound transfers in corporate organizations and reorganizations.[20]

This is not to say that the world of international tax is devoid of complexity. Many of the rules are of a complexity that rivals the field of deferred compensation. I once heard the Subpart F area referred to as a simple rule overlain with DEELS—Definitions, Exceptions, Exemptions, Limitations, and Special rules. But the areas of complexity are usually matched to taxpayers who can afford good tax counsel, and are normally accompanied by safe harbor provisions guaranteeing taxpayers good results if the safe harbor criteria are matched.

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17. Technically, this is achieved by classifying the sale of an asset by a nonresident as income from outside the United States. I.R.C. §§ 865(a)(2), 871(a)(1).
18. *Id.* § 881.
19. *Id.* § 884.
20. *Id.* § 367.

The largest area of significant unpredictability lies in income allocation involving intangibles. The rules channel the taxpayer toward a costly advanced pricing agreement, as there is no other way to reasonably predict the tax liability, and the penalties for a mistaken guess can be fearsome.[21]

C. Equality

Equality poses significant problems in all its applications. Equality assumes that there is a model to which the subject demanding equality should conform. But no two taxpayers are ever identical, so the question posed by equality is whether they are sufficiently similar to require equal treatment. To give a simple example, a person who believes that the important thing about income is its spendability is likely to believe that an individual with $10,000 in income from wages should be taxed exactly the same as a person who receives the same income, but all of it derived from the sale of stock. There are two ways in which the taxation may vary, the base and the rate. Thus, a person who believes that wage income should be taxed less aggressively than capital gains income might argue that there are expenses of earning wage income, such as commuting, clothes suitable for business, lunches that must be eaten in restaurants, etc., that are not deductible and that do not figure in the cost of earning capital gains. That person might propose that: (1) these expenses be deductible; or (2) a deduction computed as a percentage of salary should be available in lieu of actual expenses, as France makes available to its employees;[22] or (3) the rate of tax imposed on wages should be lower. By the same token, proponents of capital gains income will have reasons why it should be accorded more preferential tax than wage income.

The argument in international tax circles is similar. One group argues that all U.S. citizens and residents should be taxed equally on the same income, regardless of its source. This is called capital-export neutrality (CEN). It requires that the tax abroad always be the same or less than the home-state tax, and requires the home state to completely relieve double taxation. Another group argues that the crucial question is

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21. *See* Rev. Proc. 96-53, 1996-2 C.B. 375 (describing the requirements for an Advance Pricing Agreement); I.R.C. § 6662 (substantially increasing the penalties for mistakes in §482 allocations).

22. France, Code Général des Impôts art. 83-3.

whether everyone carrying on activities in the same place is treated equally. For this group, everyone doing business in the United States should suffer the same level of taxation, regardless of their state of residency or citizenship. This is called capital-import neutrality (CIN), and requires that tax be imposed only at source. This is sometimes called a tax based on territoriality, but this is deceptive, as its message is that the home state must refrain from taxing. We will meet both CEN and CIN again in their most prevalent use, free market compatibility.

Here, however, the question is equality, where the standard discourse relates to fairness, not to economic efficiency. The comparisons to be made in the international field are two: between income earned domestically and income earned abroad, and between income earned in the United States by home-state taxpayers (citizens, residents, U.S. corporations), and by foreign taxpayers.

There are some significant differences in the taxation of income earned abroad by U.S. taxpayers from that of income earned in the United States. The exemption of the first $80,000 of earned income from abroad is one.[23] The fact that income earned abroad through a closed corporation is not taxed by the United States until it is repatriated is another.[24] However, it should be noted that since the 1960s, some income earned abroad by controlled foreign corporations is subject to current tax.[25] Much of this discussion is carried on in economic terms, but much is also couched in terms of equity.

Turning to foreign taxpayers, the basic rule for foreign taxpayers who receive business income from the United States is the same as for U.S. taxpayers, except for the branch profits tax. Foreign taxpayers receiving investment income are subject to substantially different tax treatment.[26] While domestic taxpayers are taxed on their net investment income at ordinary graduated rates, foreign taxpayers are taxed on their gross income at a flat 30% rate.[27] The 30% rate has remained unchanged through successive rounds of tax cuts, so whatever its relationship might have been to the rates in force when enacted, that relationship has changed significantly over the years.

In taxing foreign investment income differently, the justification has been practicality. Because the taxpayer is not subject to U.S. taxing

23. I.R.C. § 911.
24. *Id.* §§ 881–882.
25. *Id.* §§ 951–964.
26. While it can be argued that foreigners are also subject to special rules on the disposition of real estate that are not applicable to U.S. taxpayers, I do not believe that is true. The Foreign Investors Real Property Tax Act (FIRPTA) serves to collect tax on the sale of U.S. realty when a U.S. person would pay it. *Id.* § 897.
27. *Id.* §§ 871(a), 881(a).

jurisdiction as the home state, these different rules are justified as ways to ensure that the tax is collected. There is no requirement in tax law, as there is in certain constitutional law cases, that the least restrictive means be chosen.

D. Stability

Stability is a strange criterion. It refers to the tendency of a tax provision to correct an economy out of equilibrium. If the economy is overheating, a provision that conforms to stability will restrain it. If the economy is insufficiently developed, a provision that conforms to stability will result in increased investment.[28] It assumes the correctness of the Keynesian multiplier-accelerator interaction, and that government investment has less a stimulating effect on the economy than does private investment.

The classic illustration of a provision that provides stability is the progressive rate structure. As incomes grow (inflation), it takes more and more money from the private sector and, as incomes shrink, the tax take shrinks more than proportionally.

It does not appear that this criterion has much bite in international tax. No provisions come to mind that are characterized by their anticyclical effects. Indeed, to the extent that the international sphere is dominated by corporations, where tax rates are only progressive at very low levels, stabilizing provisions are not frequently encountered.

E. Reduced Economic Inequality

Reduced economic inequality is another criterion that is not frequently discussed in international tax circles. In domestic tax circles, it tends to appear with provisions that grant benefits to recipients who turn out to be mostly low income taxpayers. An example is the exclusion for meals and lodging provided in kind on the employer's premises,[29] the largest number of whose beneficiaries are maids and restaurant workers. A second class of economic inequality reducers are provisions that grant benefits that disappear as income increases, such as the dependent care credit, earned income credit, personal exemption, or itemized deductions.[30]

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28. Politicians seldom find the economy overheated, and frequently declare it underdeveloped. Constituents with jobs are thought unlikely to vote out the incumbent.
29. I.R.C. § 119.
30. *Id.* § 21 (dependent care credit); *id.* § 31 (earned income credit); *id.* § 68

On this matter, it is hard to think of a single provision that is exclusively international that satisfies this criterion. Indeed, if anything international can be said on this topic, it is that the failure to tax investment income of foreign residents at progressive rates, and the failure to consider their other (non-U.S. source income) in setting those rates, contravenes reduced economic inequality. But given the sharp decline in progressivity in U.S. tax rates since 1954, this criterion has appeared less important than it was when professor Sneed wrote.[31]

Nor is it clear that the United States cares much about the distribution of assets outside the United States. It can therefore be argued that whatever the position of reduced economic inequality for considering the taxation of American citizens or residents, it has no place in the taxation of foreigners.

F. Free Market Compatibility

Free market compatibility asks that taxes be designed so that they distort as little as possible the investment and spending decisions that would otherwise be made. Put another way, this is a criterion of economic efficiency. The assumption is that persons make investment and spending decisions based on the best economic return after taxes. The economy benefits when those decisions are made based on greatest expected return. Likewise, the greatest satisfaction of societal wants occurs in a situation of perfect competition because prices are competed down to where they only slightly exceed cost. This makes the greatest number of goods and services available at a minimal cost. If this economic situation can be achieved or approached, the function of the tax system is to not destroy it. Decisions should still be made based on economic return, not based on tax considerations.

Any tax will disturb pure economic calculations, but some will disturb

(itemized deductions); *id.* § 151(d) (personal exemptions).

31. An examination of the Internal Revenue Codes in effect in the listed years reveals that the following were the maximum marginal income tax rates for the indicated years:

YEAR	TAX RATE
1954	91%
1964	77%
1974	70%
1982	50%
1987	28%
1992	31%
1998	39.6%

them more than others. For example, a tax imposed at the same rate will disturb economic decisions less than a tax that has different rates for substitutable products. A tax imposed on a large set of similar transactions (like the income tax) is preferable to a tax imposed on a smaller set of transactions (such as an oil extraction tax). A tax imposed at a uniform rate on all investment opportunities would alter investor decisions less than a tax that exempted interest from bonds of state or local governments, or that taxed long term capital gains at a lower rate than periodic income from the same investment. If the tax is to be less general, it is better to impose it on transactions for which there are no readily available substitutes. This goes not to the equity of the tax. The tax may be quite inequitable, but still meet the criterion of free market compatibility because the taxpayer has difficulty avoiding it by substituting a comparable nontaxable transaction.

It is in the criterion of free market compatibility that the battle between capital-export neutrality (CEN) and capital-import neutrality (CIN) reaches its climax.

CEN starts with the proposition that most international tax questions revolve around investment. It postulates that the key decision maker is the investor. The tax system should not distort the investor's decisions. The investor has a choice among many investments, including some that are domestic and some that are located abroad. A tax system that does not distinguish between those investments is CEN because the investor will not consider taxes in deciding whether to invest at home or abroad.

The largest violation of CEN in the U.S. tax system is according deferral to income earned through a foreign corporation. That income is not taxed until repatriated. All other things being equal, that deferral gives the investor in foreign assets through a foreign corporation a big advantage over the investor in a domestic corporation, which would pay U.S. tax annually on its income. With a foreign corporation, the income can be accumulated and reinvested abroad without being diminished by U.S. taxes.[32] While the above assumes that income taxes imposed by foreign countries do not offset the deferred U.S. income tax, that is frequent enough with investment income to be realistic.

Consequently, a great step toward free market compatibility was taken

32. Other benefits of deferral, such as likely monetary inflation making the cost of taxes paid later worth less in real terms, the likelihood that rates will change to the advantage of the taxpayer, and the possibility of using the tax saved to leverage an even greater investment, need not be discussed here.

with the partial enactment of the Kennedy proposals as Subpart F,[33] which ended deferral for many kinds of passive and related-party income earned abroad. While this did not eliminate the difference between working through domestic and foreign corporations, it reduced that difference.

The CEN principle of neutrality also applies to labor-export neutrality. A person, in deciding whether to work at home or abroad, should not be influenced by tax considerations. The earned income exclusion that permits the exclusion from U.S. gross income of the first $80,000 of earned income from abroad, is the principal offender.[34]

Partisans of CIN take a different view. For them, the important thing is to create a perfectly competitive experience. For them, source is all. Persons from many countries will do business in country X. The important competitive equality requires that all persons doing business in country X be subject to the same taxes; otherwise, one will be at a competitive advantage. The inevitable implication of CIN is that only the source country can tax that enterprise. Or, another possibility is that the tax on the enterprise cannot exceed the tax imposed by the source country which could, by tax treaty, cede some of its normal taxing jurisdiction to the host country. In that case, there must also be a limit on the tax jurisdiction of the host country so that the total tax imposed would not exceed the tax imposed by the source country on competing enterprises, such as domestic enterprises, and enterprises of other countries with whom the source country does not have a tax treaty, that do not benefit from tax treaties.

Both deferral for investments through foreign corporations and the earned income exclusion go in the direction of implementing CIN, but not entirely. While there are many European countries that exempt the foreign business income of their enterprises, which is a CIN move, they almost universally count that exempted income in determining the progressive rates to be applied, which is decidedly non-CIN.[35]

G. Political Order

It is not clear that political order has much purchase in the realm of international tax. There do not seem to be great constitutional principles at stake, though the role of federalism seems to be quite strong in the United States' refusal to limit by treaty the taxing power of any of its

33. I.R.C. §§ 951–964.
34. *Id.* § 911.
35. For a helpful discussion, see generally Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 54 TAX L. REV. 261 (2001).

states other than by a nondiscrimination clause.

Likewise, it does not appear that the political parties have sharply differentiated views on international tax questions. While Republican rhetoric has perhaps been more business friendly, there have been no shortage of Democratic votes for export subsidies, and Republican administrations seem as determined as their Democratic counterparts to stamp out international tax evasion.

III. OTHER CRITERIA

A. Job Creation or Preservation

One constantly hears arguments that lead to the creation or preservation of U.S. jobs.

For instance, a persistent part of U.S. international tax policy has been a subsidy for exports. The names change with the seasons as the World Trade Organization ("WTO") declares the provisions in violation of free trade agreements, but the purpose remains constant: to relieve exporters of some of their tax burden. Other countries subsidize exports by relieving them of the value added tax. Lacking a national sales or value added tax, the U.S. solution has been to provide income tax relief. The appeal here is to the jobs created by exports.

Other examples are provisions designed to lure foreign capital to the United States. Exemption from income tax of interest deposited in U.S. banks[36] increases the amount of capital available for loan to U.S. businesses, which in turn permits the creation of more U.S. jobs. There has even been talk of removing tax benefits from U.S. corporations who choose to become foreign corporations.

While these discussions and consequences are real, I prefer to think of them as part of a larger criterion of Balance-of-Payments Enhancement.

B. Balance-of-Payments Enhancement

The balance of payments is a huge accounting game. If the United States buys more goods abroad than it sells abroad, it has a trade deficit. It is a net dollar debtor. Without further activity, the United States will need to give foreign countries gold in order to redeem the dollars the United States has used to buy goods.

36. I.R.C. § 871(h).

Fortunately, trade is not the only activity that causes money to cross national boundaries. There is also the supply of services, tourism, returns on investment such as dividends, interest, and royalties, and investments themselves.

No country can run a long-term balance of payments deficit. No one has enough gold to do that. If it appears that there will be a long-term deficit in its balance of payments, the market will devalue the currency of the deficit-running country. This will make its imports more expensive, and also make it more expensive for its residents to invest abroad. Devaluation makes the country's exports cheaper, and renders investment in the country less costly for foreigners in terms of their currency. So in the long run, the system is self-correcting, and deficits in the balance of payments will disappear. But in the meantime, there may be significant dislocations, which the United States wishes to avoid by keeping exports high and maintaining a high level of incoming investment.

Examples in the tax system are many. In addition to the export subsidies and exemption of income from U.S. bank accounts just mentioned, there is no tax on U.S. capital gains,[37] and most of our tax treaties eliminate tax on interest and royalties, and reduce them on dividends flowing abroad. The most prominent exception is the tax on gains by foreigners on U.S. real estate,[38] thereby reducing its attraction to a foreign investor.

IV. Summary and Ordering

We have seen that the criteria of Reduced Economic Inequality, Stability, and Political Order have little purchase in discussions of international tax policy. Adequacy, Practicality, Equity, Free Market Compatibility, and Balance-of-payments Enhancement seem important international criteria.

It would enhance the utility of the concept if one could rank the importance of these five criteria. While I am unable to assign constant rankings to the criteria, some observations about them can be assayed.

Practicality in the sense of power is an important negative criterion. Tax provisions that wish to reach beyond U.S. territorial grasp seldom see the light of day. On the other hand, the enforcement of subpoenas on sellers of U.S. tax shelters, and the controversy over whether they must disclose the identity of their clients (even where the subject matter lies abroad) indicate that actual practicality may be broader than cynics believe.[39]

37. *Id.* §§ 865(a)(2), 871(a)(1).

38. *Id.* § 897.

39. *See, e.g.*, United States v. BDO Seidman, 337 F.3d 802 (7th Cir. 2003), *cert. denied*, Roes v. United States, 124 S. Ct. 1410 (2004); United States v. Arthur Andersen, L.L.P., 2003-2 T.C. ¶ 50,624 (N.D. Ill. 2003).

Practicality in the sense of ease of application is not a very important international criterion. Most taxpayers with international tax problems are sophisticated, wealthy and well-represented. In the absence of enhanced sanctions, they would sacrifice predictability for a chance at the slightest benefit.

Free Market Compatibility and Balance-of-payments Enhancement are two other criteria much in play. There are few international provisions that do not invoke both of these considerations.

Adequacy should be a criterion much in play, as extracting taxes from people who cannot vote (aliens) or people who do not regularly vote (nonresident citizens) is a basic tenet of politics.[40] Yet one seldom sees international provisions as major revenue enhancers or revenue losers.

Equity is an argument frequently made, though it does not appear to have significant weight outside the area of Free Market Compatibility.

40. The universality of transient occupancy taxes on hotel rooms is good evidence of that. The finance minister to Louis XIV, Jean Baptiste Colbert, put it this way: "The art of taxation consists in so plucking the goose as to obtain the largest amount of feathers with the smallest amount of squealing."