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Proportionality and the fight against international tax abuse: comparative analysis of judicial review in EU, international investment and WTO law

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ABSTRACT
This contribution considers the use of the principle of proportionality to review measures combatting international tax abuse (avoidance and evasion). Our claim is that proportionality, which tends to be viewed as the key analytical tool to balance tax equity against the interests of taxpayers, is ill-suited to the review of such measures. This we will demonstrate from a theoretical angle, but also through the analysis of the CJEU, international investment tribunals and WTO adjudicatory bodies: rather than balancing tax certainty against tax equity or focusing on the efficiency of the anti-tax abuse measures in the pursuit of substantive policy goals (the types of enquires normally associated with proportionality), what we observe is an assessment and gradual demarcation of the rightful territorial extent of the State's taxation powers.

KEYWORDS
Tax avoidance; tax evasion; dispute resolution; judicial review; legal reasoning

I. Introduction

Addressing tax abuse by multinationals has become one of the top priorities of states in the last ten years. Defining abuse in tax law leads to linguistic, conceptual, and practical discrepancies around the two practices that it is usually said to encompass: tax evasion and tax avoidance.[1] In most tax systems, while tax evasion involves fraud and is a criminal offence punishable by fines or imprisonment, unacceptable tax avoidance involves the reduction of tax by legal means rather than by fraud, non-disclosure or misrepresentation.[2] All states

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[1]On the conceptual and linguistic discrepancies on the concepts of anti-avoidance and tax evasion, which go beyond the scope of this contribution, there is abundant literature. See e.g. V Uckmar, 'General Report' in *IFA Cahiers, Tax Avoidance/ Tax Evasion* (IFA, 1983) vol. 68a, 23; M Mössner, 'Tax Avoidance Concepts and European Tax Education – Professors of Tax Law Hold First Meeting in Osnabrück' (1999) 39 *European Taxation* 92; S van Weeghel, 'General Report' (2010) 95A *IFA Cahiers, Tax Treaties and Tax Avoidance: Application of Anti Avoidance Provisions* 19; P Piantavigna, 'Tax Abuse and Aggressive Tax Planning in the BEPS Era: How EU Law and the OECD Are Establishing a Unifying Conceptual Framework in International Tax Law, despite Linguistic Discrepancies' (2017) *World Tax Journal* (online edition) 9; C Öner, 'Is Tax Avoidance the Theory of Everything in Tax Law? A Terminological Analysis of EU Legislation and Case Law' (2019) 27 *EC Tax Review* 96.

[2]B Arnold, 'Protecting the Tax Base of Developing Countries Through the use of General Anti-Avoidance Rules' (2019) *UN Nations Practical Portfolio* 9.

share a preoccupation with curbing both practices, but their efforts at doing so sometimes run into the limits posed by international economic law, as interpreted by international or supranational tribunals. This contribution focuses on this area of judicial review, with an emphasis on the legal reasoning and particular norms that it has produced.

While states have a legitimate interest in thwarting abusive practices that erode their tax bases and enforce tax equity (duty to contribute to the public spending), taxpayers usually object to this broad power of the tax authorities under the legal certainty principle. For the purpose of solving this conflict of principles, tribunals often resort to the principle of proportionality. This article delves into the particularity and significance of proportionality as a highly specific form of legal reasoning to question whether it is the right analytical tool to approach the review of measures combatting international tax abuse. As we will see, its widespread use often hides a different type of reasoning – one focused not on balancing, but on the rightful territorial extent of the State's competence and certain 'good governance' principles.

The structure of this contribution is as follows. Section II is devoted to putting forward our theoretical claims, namely the distinctiveness of proportionality as a form of legal reasoning and the reasons why proportionality is ill-suited for the review of measures combatting tax abuse. In Section III, we focus on the practical dimension to show how the legal reasoning followed in such cases also strays from the standard understanding of proportionality, even if formally conducted under its banner. The decisions will be drawn from the Court of Justice of the EU ('CJEU'), international investment arbitration, and the World Trade Organization ('WTO') dispute settlement bodies. We have picked these three contexts, even if formally non-tax, for various reasons: they all share a high degree of judicialization (i.e. the review performed by courts or adjudicatory bodies occupies a central place within each of them) and the same tendency to resort to proportionality, and they have all come to extend their purview to taxation matters (including the review of anti-tax abuse measures). We will conclude in Section IV with some general reflections about the value of our contribution, both descriptive (in relation to a more accurate understanding of the interactions, which the form the object of this Symposium, between the trade, investment and taxation regimes at an international level),[3] and normative (by suggesting a more appropriate manner of approaching discussions on international tax abuse).

II. Proportionality and international tax abuse

This section analyses the role of proportionality in relation to tax abuse at an abstract or theoretical level. While Section II.A briefly identifies the main features of proportionality as a highly specific form of reasoning, Section II.B examines its adaptation to the context of international taxation, particularly the review of measures against tax abuse.

A. The distinctiveness of proportionality as a form of legal reasoning

The proportionality principle is today omnipresent. Courts everywhere, domestically and internationally, are called upon to review a wide variety of measures. Despite the different

[3]Chaisse and Mosquera, in this *Asia Pacific Law Review* special section 'The future of international tax disputes' at Section III.

contexts, proportionality is by far the preferred tool. This means that adjudicators will examine whether the measure in question meets the various subtests of the proportionality principle: the legitimacy test (it must pursue a legitimate goal), the adequacy test (it causally contributes to that goal), the necessity test (that goal could not have been attained through less restrictive means) and the balancing test (the benefits attained do not outweigh its costs).[4]

Why is proportionality so widespread? At a very fundamental level because it seems so common-sensical. The four components can be said to capture an essential requirement of rationality that could apply to all forms of decision making, regardless of the domain involved and even outside the legal field. Indeed, who could object to ensuring that any form of action (from the most banal like going out for a walk, to the most complex such as regulating a particular industry) is motivated by legitimate reasons, is an effective way of attaining them, etc.? The simple idea that any particular problem raises a multitude of competing and equally legitimate claims, interests and considerations, and that the essential function of judges is to find an appropriate compromise between them has such intuitive appeal that it has become almost impossible to imagine judicial reasoning in any other way.[5]

However, there is no reason to assume that proportionality is well-suited to deal with every issue. Contrary to its apparent intuitive appeal, proportionality is a highly specific form of reasoning, which leads the adjudicator to frame problems in a way that highlights specific aspects but also serves to obscure others.[6] The distinctiveness of proportionality as a form of legal reasoning hinges on two key features, which we will briefly explain below.

The first is that it frames issues in purely instrumental terms, that is, in terms of a means-ends relationship. Indeed, it views any measure under a review as a tool to advance a particular goal (security, welfare, etc.) and leads the adjudicator to judge it on this basis (how efficiently does it attain that goal?). While this may be a legitimate angle to take in certain circumstances (it makes sense to judge a hammer primarily based on its ability to hit a nail), it is not the only potentially relevant angle in the legal context. For instance, the law should not be indifferent to arguments of authority (e.g. was the measure adopted by the competent authority, regardless of the goals it pursues?), process (e.g. was it adopted following appropriate procedures?) or of principle (e.g. is it consistent with human dignity?). Nevertheless, because of the instrumental framework that proportionality imposes, these dimensions are obscured and ultimately either excluded or addressed through tools other than proportionality.

The second relates to the nature of the goals that the measure under review is said to pursue instrumentally. Those goals need to take the form of universal values,[7] i.e. goods that are presented as being universally and uncontroversially valid, regardless of the context. Thus, considerations such as security, privacy, the rule of law, or the promotion of investment all have this quality. People may legitimately debate how these various

[4]The literature is vast. The most influential analysis is that of R Alexy, *A Theory of Constitutional Rights* (2002).
[5]D Kennedy, 'A Transnational Genealogy of Proportionality in Private Law' in R Brownsword, H-W Micklitz, L Niglia and S Weatherill (eds), *The Foundations of European* Private Law (2011) 185.
[6]T Marzal, 'From Hercules to Pareto: Of bathos, Proportionality, and EU Law' (2017) 15 *International Journal of Constitutional Law* 621.
[7]Kennedy (n 5).

considerations should be balanced against each other, and different societies may reach different compromises at different times, but no one will be able to argue that security as such is not a worthy concern. Conversely, this means that proportionality does not allow for the interests of specific groups or individuals to be weighed against each other.

B. The mismatch between proportionality and the review of measures combatting international tax abuse

Tax law is no stranger to the general spread of proportionality. When reviewing fiscal measures, generally and in particular those combatting tax avoidance, tribunals everywhere, both in the domestic and international domain, have seemingly embraced the vocabulary of proportionality (as we will see in Section III).

Such a move fits with a certain idea of what tax law is about, as animated by a tension between two fundamental principles: legal certainty and tax equity. On the one hand, taxpayers have the right to organize their business in the most tax-efficient way under standards of certainty and predictability, but on the other hand, tax authorities enjoy a broad margin of discretion to determine and enforce an equitable distribution of fiscal burdens among taxpayers. Such powers extend to combatting abusive schemes, which breach the fair duty to contribute to the general public spending. The tension between these two competing principles appears in the OECD language under the tax certainty block within Pillar I: 'considerable bureaucracy to comply with tax legislation, including documentation requirements' and 'unpredictable or inconsistent treatment by the tax authority'.[8]

On this basis, the legislator's work will be seen as seeking a reasonable compromise between the conflicting (and equally legitimate) principles of legal certainty and tax equity, whereas that of the judge will be to assess whether the compromise is appropriate. Proportionality naturally seems the perfect analytical tool to accomplish this judicial operation by breaking it down into the different subtests of the principle.[9] For instance, anti-abuse legislation enacted by states to react against base erosion and profit shifting practices by multinationals should, if subject to proportionality analysis, be examined from the perspective of its contribution to tax fairness, whether it is needlessly restrictive of the rights of taxpayers, and ultimately condemned as disproportionate if imposing too large a sacrifice on legal certainty.

Such a simple scheme seems intuitively unobjectionable. It is, however, deceptively so. From a conceptual point of view, the nature of international taxation disputes, and particularly those involving anti-tax abuse measures, makes them ill-suited to the kind of assessment that proportionality implicates. Indeed, such disputes tend to be about efforts by States at protecting their own tax base (and therefore their self-interest, rather than promotion of any particular value with a universal appeal), and the difficulties involved in coordinating the exercise of fiscal authority by a multitude of States in that

[8]IMF/OECD Report for the G20 Finance Ministers, March 2017, p 9 <www.oecd.org/tax/tax-policy/tax-certainty-report-oecd-imf-report-g20-finance-ministers-march-2017.pdf>; see also OECD, *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint* (2020) 168 <www.oecd-ilibrary.org/docserver/beba0634-en.pdf?expires=1625476400&id=id&accname=guest&checksum=796DE97CA3D28C20A897A76F7C9EBBA5>.

[9]D Rolim, 'Proportionality and Fair Taxation' (2015) 43 *Intertax* 405; M Hilling, 'Justifications and Proportionality: An Analysis of the ECJ's Assessment of National Rules for the Prevention of Tax Avoidance' (2015) 41 *Intertax* 303.

same pursuit (and thus necessarily involve questions about the proper extent of their legitimate authority). These are precisely the type of issues that proportionality is unable to address.

Take a typical case involving a scheme set up by a multinational to transfer its profits to a low or no-tax jurisdiction (of the kind that feature in the case law examined below). The State wherefrom those profits have been transferred may react through measures that formally reclassify those profits as located in its own jurisdiction (e.g. because the multinational does not pursue any meaningful activities in the transfer-to jurisdiction), to maintain their taxable quality. Imagine that such measures are then subject to judicial review. The two key characteristics of proportionality as a form of legal reasoning identified earlier will obscure the stakes involved in such a case.

First of all, it is awkward to present the goal of such anti-tax avoidance measures as serving an abstract value that is common to all peoples. Instead, these measures are ultimately motivated by the desire of that particular State to maximize or protect its tax revenue. In other words, the driving motivation is a 'selfish' (yet legitimate) one, in contradiction with one of the basic assumptions of proportionality. Secondly, the crux of the case, as in other international tax avoidance cases, will be whether the State is guilty of some form of regulatory overreach by claiming as taxable income that properly belongs outside the space of its tax authority. For instance, there may be arguments as to the reality of the transfer or the activities pursued by the multinational in the transfer-to jurisdiction. Thus, the adjudicator will ultimately be called upon to define the proper scope of fiscal competence of the State – with the latter arguing for a more flexible definition and the taxpayer contending it should be interpreted more rigidly. Again, this is precisely the type of question that proportionality is not well suited to answer, as it concerns the limits of authority to adopt a particular measure rather than the consequences that follow from its adoption.

III. Proportionality and tax abuse in comparative practice

We have established above that proportionality should not be viewed as a one-size-fits-all doctrine, and that the framework that it carries is ill-suited to the review of measures combatting international tax abuse. Given these insufficiencies, how is it possible that proportionality has spread to most jurisdictions and branches of the law, including the review by international adjudicatory bodies of precisely those kinds of measures?

The simple answer is that, as proportionality has spread to a wide variety of legal contexts, its content has been adapted and reinterpreted, at times rendering it radically different from its original model.[10] Indeed, a closer look at how courts apply proportionality reveals that practice is much richer than the unanimous appeal to this principle would suggest – and with good reason, since proportionality, as we have described it, is often not a good fit. Even though it is true that the vocabulary of proportionality has gained enormous currency, one finds under the banner of this principle a wide variety of forms of reasoning that are incompatible with the assumptions that we outlined earlier. Variations may include the elision of certain components of the full proportionality

[10]See J Bomhoff, 'Balancing, the Global and the Local Judicial Balancing as a Problematic Topic in Comparative (Constitutional) Law' (2008) 31 *Hastings International and Comparative Law Review* 555.

assessment, most commonly its last limb (the balancing test). However, the variations may also be more radical. In certain cases, as we will see in the examples below, the assessment is not conducted by reference to universal values or even from the perspective of the measure's instrumental rationality.

Proportionality's propensity for transformation when encountering a particular context is again relevant to the fiscal context. As we will now illustrate through the analysis of three international or supranational contexts of judicial review, our usual understanding of proportionality obscures the reasoning actually conducted. In the first two contexts that we will examine (EU law and investment arbitration), involving anti-tax avoidance measures, the enquiry focuses on whether these exceed the rightful 'territorial' boundaries of the State's competence and are consistent with certain 'good governance' principles (such as legal certainty or a proper allocation of the burden of proof). In the third and final context (WTO), involving not tax avoidance but the prevention of evasion, the assessment involves some balancing, but by reference to territorially defined prerogatives and with a high level of deference granted to national authorities.

A. EU law: Cadbury Schweppes *and SIAT*

Member States have always sought to prevent the erosion of their tax bases and profit shifting strategies of the multinational groups by introducing anti-avoidance legislation. Such legislation may hinder the functioning of the internal market, e.g. by making it more difficult for a corporation to establish itself in another EU jurisdiction.[11] Even though a measure may be found in breach of the EU market freedoms, the CJEU has traditionally allowed Member States to justify them, subject to a review of proportionality. The justificatory reasons invoked include 'the need to maintain the balanced allocation of taxing rights',[12] 'the prevention of abusive practices and tax evasion (wholly artificial arrangement)',[13] or 'combatting tax havens'.[14]

In EU law literature, the proportionality principle is presented as a balancing exercise between preserving the internal market and promoting the public interests, broken down into the standard four sub-tests.[15] In reality, however, the CJEU generally refuses to engage in any sort of balancing.[16] More importantly, for our purposes, the reasoning conducted when dealing with anti-tax avoidance measures is very different from the standard picture. Instead of focusing on the instrumental rationality of such measures, the CJEU has actually, under the banner of proportionality, assessed the territorial limits of the Member States' fiscal authority, and the principles of good governance to which their action should be subject to in this domain. We will illustrate this through the following two cases.

Cadbury Schweppes concerned an attempt by British authorities to tax the profits of an Irish subsidiary of a UK parent company based on UK legislation on controlled foreign

[11]CJEU, Case C-371/10, *National Grid Indus*, ECLI:EU:C:2011:785.
[12]CJCE, Case C-446/03, *Marks & Spencer*, ECLI:EU:C:2005:763, para 49; CJCE, Case C-196/04, *Cadbury Schweppes*, [2006] ECR I-0799, para 56; CJEU, C-318/10, *SIAT*, ECLI:EU:C:2012:415, paras 45–47.
[13]CJEU, Case C-451/05, *ELISA*, ECLI:EU:C:2007:594, para 81; *Cadbury Schweppes* (n 12) para 55; *SIAT* (n 12) para 40.
[14]CJEU, C-80/12, *Felixstowe Dock and Railway Company*, ECLI:EU:C:2014:200, para 32.
[15]S Prechal, 'Free Movement and Procedural Requirements: Proportionality Reconsidered' (2008) 35 *Legal Issues of Economic Integration* 201.
[16]Marzal (n 6).

companies ('CFCs'). The reason invoked to justify this measure, accepted as legitimate by the CJEU, was the prevention of 'abusive practices', in particular, the fight against 'wholly artificial arrangements which do not reflect economic reality'.[17] On this basis, the assessment of the CJEU, through the prism of proportionality, focused on how to determine whether there was such an arrangement in place. In other words, proportionality here becomes an enquiry into the extent and solidity of the (economic) connection between the subsidiary and the Irish jurisdiction (rather than an assessment of the substantive goals advanced by British legislation, which could be nothing other than to prevent a loss of revenue). For this purpose, the CJEU concludes that this enquiry should take the form of a subjective test (intention to obtain a tax advantage) and an objective test (fictitious establishment not carrying out any genuine economic activity in the territory of the host Member State), both of which must concur.[18] It then becomes a matter of proof to establish whether these tests are met, and the parties should have the opportunity to bring all necessary evidence. While the tax authorities, by means of procedures of collaboration and exchange of information, had the opportunity to obtain the information on whether the controlled company established in the host Member State carried on genuine economic activities there, 'the resident company, which is best placed for that purpose, must be given an opportunity to produce evidence that the CFC is actually established and that its activities are genuine'.[19]

Thus, rather than a balancing exercise or a means-end assessment, territoriality, or the territorial extent of the State's tax authority, is the focus of the Court's enquiry. Its 'proportionality' assessment is actually one about the proper scope of that authority, with the effect that UK is entitled to tax Irish CFCs provided that the arrangement is qualified as a wholly artificial arrangement after conducting subjective and objective tests of abuse. The exercise of this territorially defined authority is further anchored in a proper distribution of the burden of proof between the tax administration and the taxpayer.

Moving on to the SIAT case, here the Belgian tax authorities had denied the deduction of business expenses by Belgian taxpayers when the payment was made to a recipient in another Member State, in which the latter was either not subject to income taxation or to a tax regime that was appreciably more advantageous than the applicable regime in Belgium. The CJEU again affirmed the territoriality of Belgian fiscal authority to allow it to deny the deductibility of expenses provided that such payments are connected to wholly artificial arrangements. It nevertheless considered the Belgian legislation disproportionate, essentially on two grounds of a procedural nature or related to principles of good governance.

Indeed, the first argument related to an improper attribution of the burden of proof: it should be for the tax administration to provide evidence of the existence of a wholly artificial arrangement in the set of transactions. Instead,

> the special rule requires the Belgian taxpayer to provide, as a matter of course, proof that all the services are genuine and proper and that all related payments are normal, without the tax authority being required to provide even prima facie evidence of tax evasion or avoidance.[20]

[17] *Cadbury Schweppes* (n 12) para 55.
[18] Ibid, para 64.
[19] Ibid, para 70. See also, CJCE, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation*, [2007] ECR I-2107, para 82.
[20] *SIAT* (n 12) para 56.

Thus, even if under the banner of proportionality, the CJEU is enforcing a proper distribution of the burden of proof between taxpayer and tax administration properly. Such a principle is consistent with the preclusion of domestic general irrebuttable presumptions of fraud or abuse found elsewhere in EU law.[21] Likewise, the ECtHR has stressed that a breach of the right to property in Article 6 ECHR occurs when the taxpayer cannot challenge the evidence of abuse provided by the tax administration.[22]

Second, the Belgian government itself recognized the absence of proper rules to determine 'a tax regime which is appreciably more advantageous than the applicable regime in Belgium'.[23] The CJEU, therefore, concluded that the regime was in breach of the principle of legal certainty ('rules must be clear, precise and predictable').[24] As Hilling observes, legal certainty was thus assessed as a part of the proportionality test. This is again inconsistent with its usual understanding, as consisting in balancing a measure's purpose against its effect.[25]

To sum up, the proportionality review of the CJEU produces two different enquiries. On the one hand, a substantive dimension reaffirms the competence of Member States to introduce anti-avoidance legislation to protect their tax base and thus restrict free movement within the internal market. The proper extent of the State's fiscal authority is defined territorially,[26] the territoriality argument being embedded within the justifications alleged by the Member States (namely the fight against tax avoidance and the balanced allocation of taxing powers). On the other hand, the exercise of this fiscal authority is constrained by a procedural or 'good governance' dimension: the burden of proof between taxpayer and tax administration must be properly distributed, and States must respect a general requirement of legal certainty.[27]

B. International investment law: Cairn Energy v India

Investor-State dispute settlement mechanisms offer the taxpayer a powerful tool to challenge the host State's taxation measures.[28] In this field, the review performed by international arbitral tribunals increasingly resorts to proportionality, a trend that has attracted considerable scholarly attention.[29] Again, scholars tend to view proportionality in this context in the usual manner, as consisting of the four well-known steps and ultimately equivalent to a balancing operation.[30] It is thus seen as the appropriate tool to

[21]CJEU, joined cases C-504/16 and C-613/1620, *Deister Holding*, ECLI:EU:C:2017:1009; CJEU, C-6/16, *Eqiom*, ECLI:EU:C:2017:641.
[22]ECtHR, *Hentrich v France*, Decision of 22 September 1994; ECtHR, *Riener v Bulgaria*, Decision of 12 April 1996.
[23]*SIAT* (n 12) paras 57 and 26–28.
[24]Ibid, paras 57–58.
[25]Hilling (n 9) 303.
[26]W Schön, 'Neutrality and Territoriality – Competing or Converging Concepts in European Tax Law?' (2015) 69 *Bulletin for International Taxation*, issue 4/5.
[27]D Weber, 'The Reasonableness Test of the Principal Purpose Test Rule in OECD BEPS Action 6 (Tax Treaty Abuse) versus the EU Principle of Legal Certainty and the EU Abuse of Law Case Law' (2017) 1 *Erasmus Law Review* 38.
[28]On a review of the tax measures by Investor-State dispute settlement and the limits on the host State's power in this Symposium, see P Ranjan, 'Investor-State Dispute Settlement and Tax Matters'.
[29]V Vadi, *Proportionality, Reasonableness and Standards of Review in International Investment Law and Arbitration* (2018). In the context of tax disputes, see J Chaisse, 'Investor-State Arbitration in International Tax Dispute Resolution: A Cut above Dedicated Tax Dispute Resolution' (2016) *Virginia Tax Review* 149.
[30]B Kingsbury and S Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality' in S Schill (ed), *International Investment Law and Comparative Public Law* (2010).

manage the tensions between the different principles at stake in investor-State disputes, and it is argued that investment arbitrators should apply it more rigorously in the image of other more experienced bodies such as the ECtHR.[31]

As already stated, however, this traditional reading of the principle of proportionality does not match the practice of international investment tribunals. When reviewing the compatibility of anti-tax avoidance measures with investment protection standards, the enquiry focuses on the proper territorial limits of the State's fiscal powers, as well as their compliance with procedural best practices, rather than on the instrumental rationality of the measures under review in the pursuit of universal goals. We will illustrate this point through an examination of the *Cairn Energy v India* award, dealing with the retroactive application of Indian law to tax an offshore transfer of participations.[32]

In the award, the arbitration tribunal makes reference to proportionality as the appropriate tool to balance the different interests at stake in order to determine whether the fair and equitable treatment ('FET') standard has been violated. On the one hand, the State has the power to take measures in pursuance of a public purpose, namely fighting against tax avoidance schemes that erode the tax base, but on the other hand, such measures must comply with the requirements of legal certainty and predictability.[33] Neither interest is paramount or absolute.[34]

To justify legislating with retroactive effects, the State cannot simply allege that there is a need to increase taxable base and fiscal income.[35] However, the tribunal does accept that retroactivity may be warranted when used as part of the State's power to combat abuse.[36] Thus, tax legislation may apply retroactively to close a loophole exploited by taxpayers and guarantee its effectiveness:

> the legislator is warning taxpayers that are actively seeking and exploiting tax loopholes does not pay off, since the State may shut them off with retroactive effect and the taxpayers will not benefit, even temporarily, from their own wrongful conduct.[37]

Moreover, the tribunal questions whether 'taxpayers that actively engage in abusive practices' even have a 'legitimate interest' that is protected under the FET standard.[38]

Thus, even though the issue is framed through the usual 'balancing framework', the case ultimately turns on the concept of abuse – its specific meaning in the context of investment treaty arbitration and its application to the case at hand. Indeed, it was because India failed to persuade the tribunal that the 2006 transactions should be viewed as abusive,[39] that the award is decided in favour of the latter – and not because the interests of the investor were found to be weightier than those of the State.

[31] See E De Brabandere and P Baldini Miranda da Cruz, 'The Role of Proportionality in International Investment Law and Arbitration: A System-Specific Perspective' (2020) 89 *Nordic Journal of International Law* 471.
[32] *Cairn Energy PLC and Cairn UK Holdings Limited v The Republic of India*, PCA Case No 2016-07, Award, 21 December 2020. On the detailed facts of *Cairn Energy* dispute, see in this Symposium, Ranjan (n 29).
[33] *Cairn Energy* (n 32) paras 1787–88.
[34] Ibid, para 1788.
[35] Ibid, para 1791.
[36] Ibid, para 1796.
[37] Ibid.
[38] Ibid.
[39] Ibid, paras 1260–591. The tribunal also rejected India's argument that the amendment was passed to combat systemic tax abuse by foreign investors (para 1813).

In relation to the interpretation of what constitutes abuse, an analysis of the tribunal's reasoning reveals that India could have been more successful had it not focused entirely on the fact that arrangement was exempt from any taxation. The tribunal insists that non-taxation is not equal to abuse: 'The 2012 Amendment does not target foreign investors who evade or wrongly avoid taxes; it applies to any indirect transfer, whether tax abusive or not'.[40] Not every situation of double non-taxation derived from the transfer of Indian assets through the transfer of shares of a foreign holding company is automatically abusive.[41] Moreover, much like the CJEU in the aforementioned cases, the arbitral tribunal clarifies how the burden of proof between taxpayer and tax administration ought to be divided on this matter: the burden is on the tax authorities to allege and establish abuse,[42] which the Indian ones failed to meet.

In requiring more than mere non-taxation, the *Cairn Energy* award supports the distinction between unintended and intended double non-taxation.[43] Intended double non-taxation may be caused by States enacting tax breaks to attract foreign investment (i.e. tax holidays) in a tax competition environment and thus should not be seen as abusive. Conversely, un-intended double non-taxation reflects multinationals engaging in wholly artificial arrangements (i.e. letterbox companies) to avoid paying any taxes and is therefore abusive. Indeed, under Article 6(1) of its Multilateral Instrument to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ('MLI'), the OECD gave its blessing to double non-taxation outcomes provided no abuse exists. This is where India's argumentation is found lacking since it put exclusively the focus on the outcome on the arrangements ('multinationals not paying taxes anywhere in the world')[44] without entering into the proper analysis of the artificiality of the set of transactions (as in SIAT and *Cadbury Schweppes*). Even though it alleged that the dominant purpose was to avoid tax,[45] no arguments are presented by India on the lack of commercial justifications to constitute the Jersey holding, or the fact that this sham arrangement challenged the object and purpose of the Indian legislation at stake.[46]

Thus, even if formally accomplished under the mantle of proportionality, the contribution of the award is mainly to the interpretation of the concept of tax abuse, as the limit beyond which no FET protection can be claimed. In so doing, the decision helps define the extent of India's fiscal powers to treat offshore transactions as if territorially located in India and therefore subject to its authority, even with retrospective effect (to clarify that more is needed than evidence of double non-taxation, as abuse requires showing that the taxpayer employed a wholly artificial arrangement to obtain a tax advantage). This is again a competence question, intertwined with the procedural

[40]Ibid, para 1815.
[41]Ibid, para 1428.
[42]Ibid, paras 1437–38.
[43]Only unaccepted or unintended double non-taxation should be combatted by States as entailing abuse: see A Martín Jiménez, 'Tax Avoidance and Aggressive Tax Planning as an International Standard – BEPS and the "New" Standards of (Legal and Illegal) Tax Avoidance' in AP Dourado (ed), *Tax Avoidance Revisited in the EU BEPS Context* (IBFD 2017) EATLP vol 15, pp 32 and 49, Books IBFD; FD Martínez Laguna, 'Abuse and Aggressive Tax Planning: Between OECD and EU Initiatives – The Dividing Line between Intended and Unintended Double Non-Taxation' (2017) 9 *World Tax Journal* (Online Journal IBFD).
[44]*Cairn Energy* (n 32) para 1813.
[45]Ibid, para 1451.
[46]On a detailed analysis of the constituent elements of abuse, see Arnold (n 2) 97–121.

requirement related to the allocation of the burden of proof, that the instrumental or balancing framework usually associated with proportionality cannot but obscure.

C. WTO law: Argentina – measures relating to trade in goods and services

The WTO treaties, namely the General Agreement on Tariffs and Trade ('GATT') and the General Agreement on Trade and Services ('GATS'), steer in the direction of liberalization of trade, which means the substantial reduction of tariffs and other barriers to trade and the elimination of discriminatory treatment in international commerce. Both Article III of the GATT and Article XVII of the GATS establish the national treatment principle, which precludes States from introducing taxes or internal charges that directly or indirectly discriminate imported products or services against domestic ones. However, this principle is again not absolute. Article XX of the GATT and Article XIV of the GATS allow States to introduce discriminations against imported services and goods if justified for reasons of public interest. Adjudication under WTO law thus often focuses on how to strike an appropriate compromise between these opposing values.[47] The situation again seems to call for some balancing analysis, for which proportionality is the most apparent model on offer.

Even though the WTO treaties do not contain any explicit reference to proportionality, and legal practice in this context is somewhat more complex than in EU law or investment arbitration, the literature here also tends to view the reasoning of WTO panels and the Appellate Body ('AB') as involving a balancing or weighing operation between trade liberalization principles (i.e. free trade and non-discrimination) and other societal values (such as public morals, or environmental or social protection).[48] The latter values, which are labelled as 'General exceptions' under Article XX of the GATT and Article XIV of the GATS, cannot be applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries (the so-called '*Chapeau*'). When conducting the review, the panel or the AB will first analyse the relationship between the objective pursued and the measure at issue (is the measure suitable to achieve the goal? How important are the objectives pursued by the legislation at stake?),[49] followed by an analysis of the existence less trade-restrictive alternative measures (are there fewer trade-restrictive measures available to achieve the same goal?).[50] In looking for alternative measures, it is generally required that they should be reasonably available, thereby discarding those that impose an undue burden, or are merely theoretical.[51]

Against this background, we will now turn to the case of *Argentina – Measures relating to trade in goods and services*, to analyse how the WTO system confronts tax abuse.[52] The

[47]On striking a proper balance between the power of a State to introduce tax measures, namely anti-avoidance legislation, and the WTO's constraints to design tax policy. See Luca Rubini, in this *Asia Pacific Law Review* special section 'The future of international tax disputes'.

[48]M Andenas and S Zleptnig, 'Proportionality: WTO Law: In Comparative Perspective', (2007) 42 *Texas International Law Journal* 371; T Cottier, R Echandi, R Leal-Arcas, R Liechti, T Payosova and C Sieber-Gasser, 'The Principle of Proportionality in International Law' (Swiss National Centre of Competence in Research on Trade Regulation, December 2012) Working Paper No 2012/38.

[49]AB Report, Brazil – Measures Affecting Imports of Retreaded Tyres, adopted 17 December 2007, AB-2007-4, WT/DS332/AB/R, para 178.

[50]See Rolim (n 9) 106; AB Report, Brazil – Retreaded Tyres (n 49) para 145.

[51]AB Report, US – Measures Affecting the Cross-Border Supply of Gambling and Betting Services, adopted 20 April 2005, AB-2005-1, WT/DS285/26, para 308.

[52]Further details on the fact of the case, see Rubini (n 47).

issue involved here is slightly different from those analysed previously. The measures at stake did not concern attempts to tax profits that, even though formally located outside the State's jurisdiction, were claimed to be rightfully covered by it (anti-avoidance scheme). Instead, the case concerned eight 'preventive' or 'defensive' tax measures by Argentina to stop its tax residents from engaging in tax evasion (rather than mere avoidance) by taking advantage of the lack of transparency offered by 'non-cooperative jurisdictions' who do not share information with that State's fiscal authorities.

Under the 'General Exception' test, Argentina contended (and the Panel agreed), that its defensive measures did not have to be linked to the exceptions explicitly provided in Article XIV(c)(i) of the GATS, but could be justified generally as seeking to 'secure compliance' with its domestic laws (fiscal, criminal and constitutional).[53] It was argued that the various measures sought to protect the integrity of the tax collection system (against the risks posed by the harmful tax practices of non-cooperative jurisdictions for tax transparency purposes) and to prevent the risks posed by laundering money of criminal origin. Both were accepted as interests of the 'utmost importance', from a domestic as well as an international perspective (given the recommendations of the OECD's Global Forum in establishing a comprehensive regulatory framework to address the risks posed by harmful tax competition to the integrity and stability of its tax system).[54] It was also accepted that the measures contributed to these objectives,[55] and that their restrictive effect on trade was limited.[56] Panama claimed that alternatives existed, for example, via *ex-post* exchange of information,[57] but this argument was dismissed on the grounds that some of the measures were rebuttable presumptions and that the legislation contributed to discourage *ex-ante* harmful tax practices in conformity with the legitimate regulatory goals pursued.[58]

Given the attention paid to the importance of the objectives at stake and to the degree of the impact on them, it is clear that in this case, unlike the instances described in the EU and investment arbitration contexts, the reasoning did involve some form of balancing operation. This does not however mean that the case conforms to the model commonly associated with proportionality. Several aspects need to be underlined in that regard. The first is that, significantly and contrary to the popular narrative, the case was not framed as pitting the value of tax certainty against that of tax equity. Such a narrative seemed present in Panama's argument, as it had specifically argued that Argentina's interest in collecting taxes had to be interpreted in conjunction with, and weighed against, the citizen's interest in measures that conform to the rule of law and the principle of equality in tax matters.[59] It was thus implied that the Argentinian measures were disproportionate for their excessively unpredictable character. The Panel explicitly rejected the very framework on which this argument was based:

[53]Panel Report, Argentina – Measures Relating to Trade in Goods and Services, adopted on 9 May 2016, WT/DS453/R, para 7.578–83.
[54]Ibid, paras 7.662–81.
[55]Ibid, paras 7.683–717.
[56]Ibid, paras 7.718–28.
[57]Ibid, para 7.545.
[58]Ibid, para 7.536. AB Report, Argentina – Measures Relating to Trade in Goods and Services, adopted on 9 May 2016, AB-2015-8, WT/DS453/R, para 6.241.
[59]Panel Report, Argentina – Goods and Services (n 53) para 7.677.

> the principles of conformity with statute and tax equality are not 'other interests' but form an inherent part of the interest or common value of ensuring the integrity of the national tax collection system and, consequently of protecting it against the risks posed by harmful tax practices of non-cooperative jurisdictions.[60]

In other words, there is no conflict as such between tax certainty and tax collection to be resolved through the principle of proportionality. Instead, what is put in the balance on Argentina's side is not a universal value such as 'tax fairness', but a territorially defined prerogative, that is, its sovereign right to ensure tax collection over those residents in its territory who engage in tax evasion. At stake is the extent to which Argentina may defensively impose a differentiated tax regime on transactions involving foreign jurisdictions to protect that sovereign right.

Moreover, the proportionality review is made somewhat toothless by the large amount of deference shown to national authorities. As stated earlier, it is entirely for Argentina to single out the objectives, either enshrined in international or national norms, that the legislation at stake can aim to secure compliance with, absent any link to the objectives explicitly listed under Article XIV(c) of the GATS.[61] Such broad discretion makes it very difficult for Panama to counter-argue that the legislation neither pursued these objectives nor that there were less restrictive alternatives. It becomes almost impossible, a sort of '*probatio diabolica*', to demonstrate that the eight Argentinian measures do not have as an ultimate goal the prevention of tax-evading behaviour as stated in the objectives laid down in international fiscal transparency norms. Indeed, the Panel confirmed that Panama could not identify

> any measure reasonably available to Argentina and less trade-restrictive that Argentina could take in order to achieve the same objectives, that is, to achieve the same level of tax collection and, as regards measure 8, achieve the same level of protection against money laundering.[62]

The margin of appreciation granted by the Panel and the AB to the State is thus extremely large, since the objectives of the legislation are selected by Argentina itself in compliance with international standards.[63]

Ultimately, therefore, the main limits to the territorially defined prerogatives of the Argentinian tax administration do not derive from the countervailing interest in preventing trade restrictions, as assessed through a balancing operation, but instead from the principle of non-discrimination enshrined in the *Chapeau*. Argentina lost the case simply because it was found to have subjected Panama to worse conditions than comparable states. Panama argued that Argentina had recognized multiple other countries as cooperative jurisdictions, despite not having in force an agreement on the exchange of information, simply because negotiations for such an agreement had begun. The Panel and the AB declared such differentiated treatment arbitrary and unjustified.[64] However, it should be noted that the Chapeau analysis is not relevant from a proportionality analysis since it turns on an analysis of comparability rather than the instrumental rationality of the measures at stake.

[60]Ibid, para 7.678.
[61]Ibid, para 7.583.
[62]Ibid, para 7.739.
[63]On the difficulties to determine whether a differential treatment should be regarded as protectionist and thus discriminatory, see Rubini (n 47).
[64]Panel Report, Argentina – Goods and Services (n 53) para 7.751.

Thus, even though a balancing exercise is part of the assessment carried out by WTO adjudicating bodies, it differs nevertheless from the one traditionally associated with the proportionality principle. For one, it does not involve the weighing of universal values, but instead, as in the other previous cases in EU law and international investment law, a territorially defined prerogative against tax evasion practices that jeopardize the integrity of the tax system. Moreover, the case that we have discussed shows an important particularity, in relation to the scope of the adjudicator's review. In dealing with tax avoidance schemes, both the CJEU and the *Cairn Energy* tribunal required the State to provide enough evidence of the taxpayer's abusive behaviour. In contrast, in *Panama – Argentina* the inquiry is performed at the legislative level, by linking the Argentinian rules with the ultimate goal of preventing tax-evading behaviours.

IV. Conclusion

With regards to the judicial review of international taxation measures, including those seeking to combat tax abuse, proportionality has been traditionally upheld as the analytical tool to solve the tension between two fundamental principles: legal certainty and tax equity. As we have shown, however, such reasoning is not only ill-suited to deal with efforts to combat tax abuse, which ultimately concern the reality and intensity of the territorial connections of particular arrangements with the jurisdiction at stake: it is also an inaccurate representation of the actual reasoning of international adjudicatory bodies. Indeed, even if formally conducted under the banner of proportionality, the said reasoning tends to engage in a very different type of enquiry to the one usually associated with proportionality. Rather than balancing tax certainty against tax equity or focus on the rationality and efficiency of the anti-tax avoidance measures in the pursuit of substantive policy goals, what we observe is an analysis of the territorial extent of the taxation powers of States, the contours of which these cases all help to define.

Beyond a proper understanding of the legal reasoning conducted in the various settings that we have focused on, our analysis illustrates that, even though the contexts are very different, they are all swept through by similar tendencies in relation to international tax abuse: from the use of the common vocabulary of proportionality, to a practical application of this principle that significantly strays from its usual understanding to focus on the territorial extent and proper manner of exercise of the state's fiscal powers, to even a converging understanding of tax avoidance (as the EU law and investment arbitration cases particularly show). The analysis thus corroborates the starting hypothesis of this Symposium, that of a strong interaction between taxation and international law regimes, as brought about through the exercise of the judicial function.[65]

Furthermore, it bears mentioning that our argument also carries normative implications. The mainstream position is not just descriptive, it carries important consequences since it allows for a critique of general anti-abuse norms. This is, for instance, the case with the 'Principal Purpose Test' (PPT) contained in Article 7(1) of the OECD MLI. For several authors, the wording of the PPT in that Article[66] is criticized as too broad, or

[65]Chaisse and Mosquera (n 3).

[66]Which reads: 'if it is reasonable to conclude having regard to all relevant facts and circumstances, that obtaining that benefit was one of its principal purposes of any arrangement advantage'.

disproportionately harmful for taxpayers' certainty.[67] This implies that national measures seeking to further tax equity should be subject to review per the sub-tests into which the proportionality principle is usually broken down (suitability, necessity, balancing). Such a vision is precisely the one that we have called into question, based both on theoretical arguments and an observation of adjudicatory practice. It is to be hoped that discussions on efforts at curbing international tax abuse move past the reductive balancing framework to focus instead on the more fundamental problem of the respective limits of States' territorial prerogatives and their coordination.

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[67] See ECCM Kemmeren, 'Where is EU Law in the OECD BEPS Discussion?' (2014) 23 *EC Tax Review* 190; E Kokolia and E Chatziioakeimidou, 'BEPS Impact on EU Law: Hybrid Payments and Abusive Behaviour' (2015) 55 *European Taxation* 149; E Pinetz, 'Final Report of Action 6 of the OECD/G20 Base Erosion and Profit Shifting Initiative: Prevention of Treaty Abuse' (2016) 70 *IBFD Bulletin* 113. Contrary to such interpretation, see Weber (n 27).