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## FAIRER SHORES: TAX HAVENS, TAX AVOIDANCE, AND CORPORATE SOCIAL RESPONSIBILITY

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INTRODUCTION .....	338
I. TAX AVOIDANCE AND TAX HAVENS.....	339
A. <i>What Is Tax Avoidance (Versus Tax Evasion)</i> .....	339
B. <i>The Particular Problems Posed by Tax Havens</i> .....	342
C. <i>Factors Motivating MNCs to Avoid Taxes</i> .....	346
II. HOW THE CSR DOCTRINE CAN HELP.....	349
A. <i>What Is CSR?</i> .....	350
B. <i>Why Is Tax Avoidance a CSR Issue?</i> .....	352
III. HOW TAX AVOIDANCE AND ESPECIALLY TAX HAVENS HARMS CORPORATIONS AND THEIR SHAREHOLDERS .....	354
A. <i>Harms to the Corporation and Its Shareholders</i> .....	354
1. Harm to Corporate Reputation .....	354
2. Encouraging Other Subversive Activities by Management.....	355
B. <i>Tax Avoidance Harms National Governments</i> .....	356
1. Developed Nations .....	356
2. Developing Nations.....	358
IV. SOLUTIONS FOR INCORPORATING THE ANTI-AVOIDANCE DOCTRINE INTO CORPORATE POLICY AND CHANGING CORPORATE TAX AVOIDANCE CULTURE.....	359
A. <i>Consumer Activism</i> .....	360
B. <i>Investor Influence</i> .....	362
C. <i>Voluntary Corporate Leadership</i> .....	363
CONCLUSION.....	365

*Despite the U.S. public's tolerance of and emotional attachment to tax avoidance at the individual level, the tax avoidance practices of modern multinational corporations such as Google, Amazon, Apple, and Starbucks recently have received heavy criticism in the media. This Note argues that the doctrine of corporate social responsibility provides a logical rationale for multinational corporations to adopt anti-avoidance practices, in that the harm caused by tax avoidance outweighs any financial benefit that accrues from these practices. Contrary to the views of some corporate leaders, tax avoidance can cause long-term harm to corporations and their shareholders by damaging corporate reputations and branding efforts, and also by diverting*

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*funds from national infrastructures, skewing the allocation of tax burdens, and causing harm to developing nations operating as tax havens. Fortunately, the same mechanisms that helped turn environmentally sustainable and human rights practices into corporate social responsibility “norms” – consumer activism, investor influence, and voluntary corporate leadership – also can be implemented to lead multinational corporations away from tax avoidance practices, ultimately ending the prevailing antiavoidance tax culture and reducing the harms caused by tax avoidance.*

#### INTRODUCTION

*“Creative tax planning is, for better or worse, a quintessentially American tradition.”<sup>1</sup>*

For today’s multinational corporations (MNCs),<sup>2</sup> tax avoidance and the use of tax havens have become commonplace and even an integral part of modern business practice.<sup>3</sup> Although these practices have recently garnered considerable media attention and public criticism worldwide,<sup>4</sup> some corporate leaders have demonstrated remarkable nonchalance toward or even expressed pride in their tax avoidance practices.<sup>5</sup> For these corporate leaders, if national governments have not (yet) made it illegal, it is not wrong; in fact, in the view of some, fiduciary responsibilities toward shareholders may even require their corporations to engage in such activities. If this attitude prevailed in all areas of business, however, corporations would still engage in environmentally harmful activities, human rights abuses, and other forms of socially irresponsible activity for the sake of maximizing shareholder value. Like other socially irresponsible activities, tax avoidance has the potential to harm a corporation and its shareholders by damaging the corporate reputation and inhibiting its branding efforts. It also imposes costs on individuals outside the corporation that outweigh any potential benefits to the corporation. Corporate

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<sup>1</sup> *Hampshire Grp., Ltd. v. Kuttner*, C.A. No. 3607-VCS, 2010 WL 2739995, at \*31 (Del. Ch. July 12, 2010).

<sup>2</sup> To use a common definition, an MNC is “a national company in two or more countries operating in association, with one controlling the other in whole or in part.” J. Coates, *Towards a Code of Conduct for Multinationals*, 10 PERSONNEL MGMT. 41 (1978), quoted in THOMAS DONALDSON, *THE ETHICS OF INTERNATIONAL BUSINESS* 30 (1989).

<sup>3</sup> RONEN PALAN ET AL., *TAX HAVENS: HOW GLOBALIZATION REALLY WORKS* 4 (2010) (“Tax havens are not working on the margins of the world economy, but are an integral part of modern business practice.”); Mihir A. Desai & Dhammika Dharmapala, *Corporate Tax Avoidance and High-Powered Incentives*, 79 J. FIN. ECON. 145, 177 (2006) (“Tax avoidance activities appear to be increasingly central to corporate financial decision making.”).

<sup>4</sup> See, e.g., Floyd Norris, *The Corrosive Effect of Apple’s Tax Avoidance*, N.Y. TIMES, May 24, 2013, at B1; Eric Pfanner, *European Countries Seek More Taxes from U.S. Multinational Companies*, N.Y. TIMES, Nov. 19, 2012, at B1.

<sup>5</sup> See *infra* note 77 and accompanying text.

tax avoidance diverts funding from national infrastructures and skews the allocation of tax burdens, causing particular harm to the developing nations that attempt to attract investments by operating as tax havens through offers of extremely low tax rates; banking secrecy laws; and quick, anonymous corporate registration.<sup>6</sup> Fortunately, the same mechanisms that helped environmental and human rights advocates convince corporations to engage in nontax socially responsible activity – that is, consumer activism, investor influence, and corporate leadership – have the potential to end the corporate tax avoidance culture and end (or at least mitigate) the harms of international corporate tax avoidance.

To provide some context, Part I defines “tax avoidance,” explains how this differs from tax evasion, and addresses one of the most common ways in which MNCs engage in tax avoidance practices: through the use of tax havens. Part II argues that the doctrine of corporate social responsibility (CSR) provides a separate rationale for MNCs to adopt antiavoidance practices, in that the costs of tax avoidance to third parties outweigh any financial benefit that accrues to a corporation engaging in tax avoidance. Part III argues that tax avoidance practices do not benefit shareholders, but rather cause long-term harm to both shareholders and MNCs by damaging the MNC’s reputation and fostering an atmosphere of managerial misconduct. Part III also discusses the ways in which MNC tax avoidance, specifically the use of tax havens, harms both developed and developing nations. Part IV argues that consumer activism, investor influence, and voluntary corporate leadership can lead MNCs to abandon tax avoidance practices the same way they abandoned other socially irresponsible activity, which would ultimately eradicate the prevailing antiavoidance tax culture and reduce the harms caused by tax avoidance.

## I. TAX AVOIDANCE AND TAX HAVENS

### A. *What Is Tax Avoidance (Versus Tax Evasion)*

Though a handful of scholars use the terms interchangeably,<sup>7</sup> “tax evasion” typically refers to illegally reducing tax payments,<sup>8</sup> while “tax avoidance” generally refers to legally reducing tax payments.<sup>9</sup> Though the distinction is

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<sup>6</sup> See *infra* Part III.B.2.

<sup>7</sup> See, e.g., BORIS I. BITTKER & MARTIN J. MCMAHON, JR., *FEDERAL INCOME TAXATION OF INDIVIDUALS* ¶ 1.3[2] (2d ed. 1995); PALAN ET AL., *supra* note 3, at 10 (“[W]e talk of avoidance and evasion throughout this book without significant differentiation . . .”).

<sup>8</sup> PALAN ET AL., *supra* note 3, at 9 (defining tax evasion as occurring “when a taxpayer fails to declare all or part of his or her income or makes a claim to offset an expense against taxable income that he or she did not incur or was not allowed to claim for tax purposes”).

<sup>9</sup> NIGEL FEETHAM, *TAX ARBITRAGE: THE TRAWLING OF THE INTERNATIONAL TAX SYSTEM* 2 (2011); PALAN ET AL., *supra* note 3, at 10 (defining tax avoidance as “the gray area between tax compliance and tax evasion”); John Hasseldine & Gregory Morris, *Corporate*

primarily a legal one,<sup>10</sup> “tax evasion” refers to conduct involving some level of “deception, concealment, [or] destruction of records,” whereas “tax avoidance” refers to “behavior that the taxpayer hopes will serve to reduce his tax liability but that he is prepared to disclose fully to the IRS.”<sup>11</sup> Tax avoidance practices seek to accomplish one of three things: payment of “less tax than might be required by a reasonable interpretation of a country’s law,” payment of a tax on “profits declared in a country other than where they were really earned,” or tax payment that occurs “somewhat later than the profits were earned.”<sup>12</sup> Individuals who engage in tax avoidance often rely on doubt surrounding the applicable tax laws, as well as tax professionals who wish to exploit this uncertainty.<sup>13</sup>

U.S. courts have employed various tests to distinguish illegal tax evasion activity from legal tax avoidance activity. One of the most well established methods is the “substance-over-form” test,<sup>14</sup> pursuant to which the legal form of a transaction may be disregarded in recognition of its underlying economic substance.<sup>15</sup> Related doctrines include the sham transaction and step-transaction doctrines,<sup>16</sup> as well as the business purpose doctrine applied by Judge Learned Hand in the famous tax case *Helvering v. Gregory*.<sup>17</sup> Courts

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*Social Responsibility and Tax Avoidance: A Comment and Reflection*, 37 ACCT. F. 1, 6 (2013) (“[T]ax evasion can be described as requiring an intention to be fraudulent, corrupt and/or deceitful . . . . In contrast, everything else, which we have called tax avoidance, would lack an intention to be fraudulent, corrupt and/or deceitful.”).

<sup>10</sup> PALAN ET AL., *supra* note 3, at 10 (“Legally, there is a clear difference between evasion and avoidance. . . . The reality, however, is more complicated.”); Hasseldine & Morris, *supra* note 9, at 3 (“[A]ny attempt to understand tax avoidance and the relationship between tax avoidance and tax evasion must accept that both are essentially *legal* concepts.”).

<sup>11</sup> BITTKER & MCMAHON, JR., *supra* note 7, ¶ 1.3[2].

<sup>12</sup> PALAN ET AL., *supra* note 3, at 10.

<sup>13</sup> *Id.*; Boris I. Bittker, *Income Tax “Loopholes” and Political Rhetoric*, 71 MICH. L. REV. 1099, 1102 (1973) (“In popular mythology, indeed, the major activity of tax experts is the search for divergencies [sic] between the letter of the law and its spirit . . .”).

<sup>14</sup> *See, e.g.*, *United States v. Phellis*, 257 U.S. 156, 168 (1921) (“We recognize the importance of regarding matters of substance and disregarding forms in applying the provisions of the Sixteenth Amendment and income tax laws enacted thereunder.”); *Estate of Weinert v. Comm’r*, 294 F.2d 750, 755 (5th Cir. 1961) (calling the substance-over-form principle the “cornerstone of sound taxation”); BITTKER & MCMAHON, JR., *supra* note 7, ¶¶ 1.3[3]-3[4] (explaining the eagerness of courts to “take account of the substance behind the veil of form” and discussing the substance-over-form principle generally).

<sup>15</sup> *E.g.*, HUGH J. AULT & BRIAN J. ARNOLD, *COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS* 153 (2d ed. 2004).

<sup>16</sup> Tracy A. Kaye, *The Regulation of Corporate Tax Shelters in the United States*, 58 AM. J. COMP. L. 585, 588 (2010); Henry Ordower, *The Culture of Tax Avoidance*, 55 ST. LOUIS U. L.J. 47, 51 (2010). For more information on the step-transaction doctrine, see BITTKER & MCMAHON, JR., *supra* note 7, ¶ 1.3[5].

<sup>17</sup> 69 F.2d 809, 810-11 (2d Cir. 1934), *aff’d*, 293 U.S. 465 (1935) (stating that the transactions “were not what the statute means by a ‘reorganization,’” as they were not part

have developed these doctrines over time, as taxpayers have created imaginative new ways to navigate around the intended purpose of the Tax Code.<sup>18</sup> Despite attempts by Congress to codify and thereby clarify some of this jurisprudence<sup>19</sup> (a move that “shocked the tax world”<sup>20</sup>), judicial application of these doctrines and their “interpretive glosses”<sup>21</sup> remains fairly unpredictable.<sup>22</sup> The grey area in the Tax Code creates an incentive for taxpayers to “press the written law to its limits in the hope that the arrangement will either escape detection or ultimately will be blessed as not abusive by the adjudicatory authority.”<sup>23</sup> While no MNC would issue public statements acknowledging its intent to *evade* taxes, some MNCs have openly stated their willingness to *avoid* taxes.<sup>24</sup>

If the distinction between tax avoidance and tax evasion is that the former is legal and the latter is not, why castigate MNCs for engaging in activities that, by definition, fall within legal limits? Tax avoidance, and particularly the use of tax havens, is not only financially detrimental to shareholders of certain types of corporations, but also harms the governments of the nations involved.<sup>25</sup> By treating tax avoidance as a CSR issue, MNCs can eliminate these harms and attract consumers and investors.

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of the conduct of the business and ultimately used to dodge shareholders’ taxes); *see also* Frank Lyon Co. v. United States, 435 U.S. 561, 573 (1978) (“In applying this doctrine of substance over form, the Court has looked to the objective economic realities of a transaction rather than to the particular form the parties employed. The Court has never regarded ‘the simple expedient of drawing up papers,’ as controlling for tax purposes when the objective economic realities are to the contrary.” (citation omitted)); Ordower, *supra* note 16, at 51.

<sup>18</sup> Kaye, *supra* note 16, at 585 (“Even with decades of legislation specifically focused on shutting down corporate tax shelters, some tax advisors continue to create ingenious plans to exploit any tax law inconsistencies.”).

<sup>19</sup> Karen B. Brown, *Comparative Regulation of Corporate Tax Avoidance: An Overview*, in 12 *IUS GENTIUM* 1, 15 (Karen B. Brown ed., 2012) (discussing the codification of the economic substance doctrine in 26 U.S.C. § 7701(o) (2012)).

<sup>20</sup> *Id.*

<sup>21</sup> Ordower, *supra* note 16, at 51.

<sup>22</sup> Brown, *supra* note 19, at 21 (“One of the beauties and mysteries of a tax statute is that it may present the conundrum of precise, detailed, and technically complex language which may be interpreted in many different ways. The unavoidable lack of precision that results, when legislators drafting a statute are not able to anticipate inherent ambiguities in terms, may be exploited by taxpayers hoping to order their affairs as they choose so as to minimize their tax liability.”).

<sup>23</sup> *Id.* at 18 (calling this mentality the “play-the-lottery mind-set”).

<sup>24</sup> *See infra* notes 77-78 and accompanying text (citing articles describing the tax-avoidance goals of MNCs such as General Electric and Google).

<sup>25</sup> *See infra* Part III.B.

B. *The Particular Problems Posed by Tax Havens*

Governments face enormous difficulty taxing MNCs in a global market characterized by cross-border activity and involving intangible assets and transfers accomplished at the push of a button. For example, the wholesale financial market (as opposed to the retail banking of individuals) involves trades of highly mobile “incorporeal” properties that give the sector a unique flexibility.<sup>26</sup> This feature enables financial actors to register, or “book,” transactions in locations other than where the corporation actually conducts its business or maintains its assets.<sup>27</sup> Similarly, Internet businesses like Google and Amazon present regulatory problems due to the “intangible nature of many of the[ir] goods and services that change hands and the ease with which transactions can cross borders.”<sup>28</sup> Though many nations have entered into treaties regarding the taxation of international transactions,<sup>29</sup> these treaties are focused on supplementing domestic laws to eliminate, or at least mitigate, double taxation: “When it comes to ensuring that cross-border income is taxed at least once, the treaties have little to say.”<sup>30</sup>

In a 2012 Senate Permanent Subcommittee on Investigations hearing, Senator Carl Levin condemned MNCs’ use of “complex structures, dubious transactions and legal fictions” to shift profits overseas and avoid paying U.S. taxes.<sup>31</sup> Primarily by shifting profits to subsidiaries in tax havens and through the use of loopholes in the U.S. Tax Code,<sup>32</sup> tax-avoiding MNCs have “push[ed] corporate income tax revenue, as a share of all federal revenue, to historically low levels,” from a high of 32.1% in 1952 to 8.9% in 2009.<sup>33</sup> As of 2012, estimates show that U.S.-registered MNCs store as much as \$1.7 trillion in earnings offshore.<sup>34</sup>

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<sup>26</sup> PALAN ET AL., *supra* note 3, at 20.

<sup>27</sup> *Id.* at 21.

<sup>28</sup> Pfanner, *supra* note 4.

<sup>29</sup> These control the taxation of MNCs that would otherwise potentially be subject to the tax jurisdictions of more than one country. The United States, for example, has income tax treaties with fifty-eight countries. See IRS, DEP’T OF THE TREASURY, PUB. NO. 901, U.S. TAX TREATIES 2, 58-59 tbl.3 (rev. ed. Apr. 2013).

<sup>30</sup> H. David Rosenbloom, *Cross-Border Arbitrage: The Good, the Bad and the Ugly*, 85 TAXES 115, 115 (2007).

<sup>31</sup> *Offshore Profit Shifting and the U.S. Tax Code—Part 1 (Microsoft and Hewlett-Packard): Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Homeland Sec. & Governmental Affairs*, 112th Cong. app. at 77 (2012) (statement of Sen. Carl Levin) [hereinafter *Offshore Profit Shifting Hearing*].

<sup>32</sup> *Id.*

<sup>33</sup> Press Release, U.S. Senate Permanent Subcomm. on Investigations, Subcommittee Hearing to Examine Billions of Dollars in U.S. Tax Avoidance by Multinational Corporations (Sept. 20, 2012), available at <http://www.levin.senate.gov/newsroom/press/release/subcommittee-hearing-to-examine-billions-of-dollars-in-us-tax-avoidance-by-multi-national-corporations>.

<sup>34</sup> *Offshore Profit Shifting Hearing*, *supra* note 31, app. at 77 (statement of Sen. Carl

Several of the methods that modern MNCs use to avoid taxes have a common denominator – the tax haven. The use of tax havens is a common way to evade taxes.<sup>35</sup> Tax havens are naturally a common site for tax avoidance activities, as well. In fact, the vast majority of international tax avoidance involves tax havens.<sup>36</sup> Though there is no authoritative definition of what constitutes a “tax haven,”<sup>37</sup> they are fairly described as “financial conduits that, in exchange for a fee, use their one principal asset – their sovereignty – to serve a nonresident constituency of accountants and lawyers, bankers and financiers, who bring a demand for the privileges that tax havens can supply.”<sup>38</sup> Not to be confused with the broader avoidance activity known as “tax sheltering,”<sup>39</sup> tax havens are distinct locales characterized by extremely low tax rates for nonresidents and banking secrecy laws.<sup>40</sup> Promoters in tax

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Levin).

<sup>35</sup> For example, IRS has identified foreign trust schemes (wherein a corporation appears to transfer a business and assets to a trust, while actually retaining control over them), the establishment of International Business Corporations (IBCs) using the exact name of an existing business, and false billing schemes as the most common forms of illegal “abusive tax schemes.” *What Are Some of the Most Common Abusive Tax Schemes?*, IRS, <http://www.irs.gov/uac/What-are-some-of-the-Most-Common-Abusive-Tax-Schemes%3F> (last updated Mar. 7, 2013).

<sup>36</sup> FEETHAM, *supra* note 9, at 1 (describing the two primary methods of international tax structuring as the use of tax havens, which encompass more than one million offshore entities, and the practice of tax arbitrage, a sector that employs no more than 300 individuals worldwide). These descriptions also loosely correspond to two “areas of concern” identified by the Organisation for Economic Co-operation and Development (OECD): “[p]lanning involving a tax position that is tenable but has unintended and unexpected tax revenue consequences . . . [and] [t]aking a tax position that is favourable to the taxpayer without openly disclosing that there is uncertainty whether significant matters in the tax return accord with the law.” ORG. FOR ECON. CO-OPERATION & DEV., *STUDY INTO THE ROLE OF TAX INTERMEDIARIES* 10-11 (2008).

<sup>37</sup> For a discussion regarding the competing definitions and roots of the term, see PALAN ET AL., *supra* note 3, at 17-45.

<sup>38</sup> *Id.* at 3. *Black’s Law Dictionary* defines a “tax haven” as “[a] jurisdiction, esp. a country, that imposes little or no tax on the profits from transactions carried on there or on persons resident there.” BLACK’S LAW DICTIONARY 1600 (9th ed. 2009). *Black’s* goes on, however, to explain that:

Among the reasons for this complexity [in international taxation] is the elusive nature of tax havens. A tax haven is not always immediately obvious. What makes a particular environment a tax haven is not invariably a low rate of tax, but relations with other tax regimes that permit the ultimate deflection of income to a low-tax environment with which the income may have little indigenous connection.

*Id.* (alteration in original) (quoting JOSEPH ISENBERGH, *INTERNATIONAL TAXATION* 16 (2000)).

<sup>39</sup> See BLACK’S LAW DICTIONARY 1601 (9th ed. 2009) (defining a tax shelter as “[a] financial operation or investment strategy . . . that is created primarily for the purpose of reducing or deferring income-tax payments”).

<sup>40</sup> PALAN ET AL., *supra* note 3, at 30-35 (describing the “ideal type” attributes of tax

havens openly advertise tax “minimization,” as well as the quick and anonymous purchase of offshore shell corporations and bank accounts.<sup>41</sup> Although the term conjures up images of “sun-kissed exotic islands reminiscent of the Garden of Eden where a few billionaires, mafiosi and corrupt autocrats hide their ill-gotten gains,”<sup>42</sup> not all tax havens are so paradisiacal.<sup>43</sup> Many tax havens are developing nations, where a lack of centralized taxation prevents the formation of a beneficial tax infrastructure and paralyzes growth efforts.<sup>44</sup>

MNCs avoid and evade taxes in tax havens primarily through transfer pricing.<sup>45</sup> According to the Organisation for Economic Co-Operation and Development (OECD), a transfer price is “a price, adopted for book-keeping purposes, which is used to value transactions between affiliated enterprises integrated under the same management at artificially high or low levels in order to effect an unspecified income payment or capital transfer between

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havens).

<sup>41</sup> *Id.* at 214; *see also* J.C. Sharman, *Testing the Global Financial Transparency Regime*, 55 INT’L STUD. Q. 981, 990-91, 995-96 (2011) (conducting a study of the relative ease of anonymously setting up shell corporations and offshore accounts in various jurisdictions by contacting service providers advertised in the *Economist* and the offshore finance magazine *Offshore Investment*). Sharman’s study found that service providers in well-known tax havens such as the Bahamas, Bermuda, and the Cayman Islands actually tended to have more stringent identity verification standards than those located in OECD countries. *See id.* at 993-94. In contrast, NBC and NPR conducted successful tests anonymously incorporating, respectively, “Our Shell Company, LLC” in the Caribbean, and “Unbelievable, Inc.” in Belize. *See* Chris Glorioso & Tom Burke, *I-Team: How We Started an Offshore Shell Company*, NBC (Sept. 26, 2012, 5:19 PM), <http://www.nbcnewyork.com/news/local/I-Team--How-we-set-up-an-Offshore-Shell-Company-Designed-to-Avoid-Taxes-170378666.html>; *Episode 390: We Set up an Offshore Company in a Tax Haven*, NPR: PLANET MONEY (July 27, 2012, 6:04 PM), <http://www.npr.org/blogs/money/2012/07/27/157499893/episode-390-we-set-up-an-offshore-company-in-a-tax-haven>.

<sup>42</sup> PALAN ET AL., *supra* note 3, at 1.

<sup>43</sup> *See id.* at 111 (pointing out the often overlooked role of OECD countries, such as the Netherlands and the United States, in providing tax haven facilities); *see also id.* at 41-44 tbl.1.4 (examining eleven frequently consulted lists of tax havens, at least two of which include the United States and the United Kingdom).

<sup>44</sup> *See* ORG. FOR ECON. CO-OPERATION & DEV., PROMOTING TRANSPARENCY AND EXCHANGE OF INFORMATION FOR TAX PURPOSES: A BACKGROUND INFORMATION BRIEF 6, 16 (2010), *available at* <http://www.oecd.org/newsroom/44431965.pdf> (charting the progress of jurisdictions identified as tax havens in implementing OECD-approved tax standards and observing that “[d]eveloping countries often lack the resources and capacity to build effective tax administration”). For a further discussion of the effect of tax avoidance by MNCs in developing tax haven nations, *see infra* Part III.B.2.

<sup>45</sup> PALAN ET AL., *supra* note 3, at 68 (“All the evidence suggests that the main vehicle of tax avoidance/evasion and capital flight through tax havens is the mundane practice of transfer pricing.”).



those enterprises.<sup>46</sup> Transfer pricing does not always involve the use of tax havens,<sup>47</sup> and is a legitimate practice as long as the corporation abides by the “[a]rm’s length principle,” which requires MNCs with subsidiaries in more than one country to value transactions “as if they had been carried out by unrelated parties, each acting in his own best interest.”<sup>48</sup> MNCs can easily abuse the arm’s length principle when assigning a value to assets that have few comparative markers available, such as intellectual property.<sup>49</sup> The transfer pricing process is “widely abused and has resulted in significant revenue loss to the U.S. government.”<sup>50</sup> For example, Microsoft (United States), after selling the rights to market intellectual property in the Americas to Microsoft (Puerto Rico), repurchased a portion of those rights immediately thereafter, enabling Microsoft to save over \$4.5 billion in taxes on goods sold in the United States over the span of three years.<sup>51</sup> Such transfer pricing practices are commonplace among U.S.-based MNCs, and seventy-seven percent of MNCs in twenty-four countries report placing transfer pricing “at the heart of their tax strategy” in 2008-09.<sup>52</sup> The court-developed tests used to distinguish legal from illegal transfer pricing (and accordingly, tax avoidance from tax evasion), such as the arm’s length principle, have failed to keep pace with today’s global economy.<sup>53</sup> The result is widespread opportunity for MNCs to legally avoid taxes, particularly through the use of tax havens.

While several developed nations and international organizations have identified tax havens as a serious problem,<sup>54</sup> it remains difficult to quantify

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<sup>46</sup> *Glossary of Statistical Terms*, ORG. FOR ECON. CO-OPERATION & DEV. (Feb. 20, 2003), <http://stats.oecd.org/glossary/detail.asp?ID=2757>.

<sup>47</sup> PALAN ET AL., *supra* note 3, at 69 (stating that transfer pricing is a widespread practice that can be “applied to any two affiliates of a company, whether in tax havens or not”).

<sup>48</sup> ORG. FOR ECON. CO-OPERATION & DEV., ANNUAL REPORT ON THE OECD GUIDELINES FOR MULTINATIONAL ENTERPRISES: CONDUCTING BUSINESS IN WEAK GOVERNANCE ZONES 176 (2006).

<sup>49</sup> See *Offshore Profit Shifting Hearing*, *supra* note 31, app. at 78 (statement of Sen. Carl Levin) (“Under U.S. tax rules, a subsidiary must pay ‘arm’s length’ prices for these assets, but valuing assets such as intellectual property is complex, so it’s hard to know what an unrelated third party would pay.”).

<sup>50</sup> *Id.*

<sup>51</sup> *Id.* app. at 78-79.

<sup>52</sup> PALAN ET AL., *supra* note 3, at 68 (discussing a 2007 survey of 850 MNCs in twenty-four countries (citing ERNST & YOUNG, 2007-2008 GLOBAL TRANSFER PRICING SURVEY (2007), available at <http://tax.uk.ey.com/NR/rdonlyres/e2mb63gclurh7rejvcsdoma3rnqcucnure3iwwswgzcxIndxv3wp26z3fw63e4tg6a54t7x6betop43zopfop2ia/TaxTPSurvey2007.pdf>).

<sup>53</sup> Michael J. Graetz, *Taxing International Income – Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 54 TAX L. REV. 261, 262-63, 318 (2001).

<sup>54</sup> See, e.g., Press Release, Org. for Econ. Co-operation & Dev., OECD Communiqué on the 7th Meeting of the Forum on Tax Administration “Strengthening Tax Compliance Through Cooperation” (Jan. 19, 2012), available at <http://www.oecd.org/newsroom/tax7th>

precisely how many corporate tax dollars have been lost due to MNCs' use of tax havens.<sup>55</sup> Because empirical research on the subject is in its infancy, the debate has been largely ideological, with tax haven supporters arguing that tax havens enhance financial market competition, which in turn fosters innovation and efficiency.<sup>56</sup> Opponents of tax havens, on the other hand, view tax havens as "vehicles of oppression, a key component in a giant parallel 'shadow economy' that spans the entire world and operates for and by the rich and the powerful."<sup>57</sup> Opponents also accuse tax havens of contributing to the financial crisis of 2008.<sup>58</sup> By all accounts, national tax laws and legal doctrines have thus far failed to mitigate the harmful effects of transfer pricing, tax haven use, and tax avoidance in general.<sup>59</sup> As government leaders, nongovernmental organizations (NGOs), and other international organizations struggle to impose external regulations and "soft law" on MNCs in order to curb tax avoidance, CSR may offer an alternative approach.<sup>60</sup>

C. *Factors Motivating MNCs to Avoid Taxes*

Since tax avoidance is legal (or at least falls within the grey area of the law), is it the morally acceptable, or perhaps even the right, thing for U.S. MNCs to do? After all, the United States was "born of a taxation dispute."<sup>61</sup> Perhaps

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meetingoftheforumontaxadministrationstrengtheningtaxcompliancethroughcooperation.htm ("The 7th meeting . . . concluded with a unified and strengthened commitment to combat offshore tax abuse."); *Tax Us if You Can: The True Story of a Global Failure*, TAX JUSTICE NETWORK 3 (Sept. 2005), [http://www.taxjustice.net/cms/upload/pdf/tuiyc\\_-\\_eng\\_-\\_web\\_file.pdf](http://www.taxjustice.net/cms/upload/pdf/tuiyc_-_eng_-_web_file.pdf).

<sup>55</sup> PALAN ET AL., *supra* note 3, at 64 ("There is a massive lacuna in research on tax havens: there are simply no figures, approximations, or even wild guesses concerning the amount of corporate tax evasion and avoidance.").

<sup>56</sup> *Id.* at 156, 171.

<sup>57</sup> *Id.* at 171.

<sup>58</sup> *Id.* at 2 ("We do not suggest in this book that tax havens caused the financial crisis of 2008-09, but we do believe that they were one of the most important actors precipitating it. We argue that their regulation is key to any future plan to stabilize financial markets.").

<sup>59</sup> This Note does not discuss the most recent international efforts to tackle tax avoidance, but the prominence of these efforts indicates that corporate tax avoidance is very much on the agenda of international leaders. Examples include the G20 Leaders' Declaration in September 2013 and the Stop Tax Haven Abuse Act. *See* Stop Tax Haven Abuse Act H.R. 1554, 113th Cong. (2013) (intending to ultimately "restrict the use of offshore tax havens and abusive tax shelters to inappropriately avoid Federal taxation"); Russia G20, Saint Petersburg, Russia, Sept. 5-6, 2013, *G20 Leaders Declaration* (Sept. 2013), available at [https://www.g20.org/sites/default/files/g20\\_resources/library/Saint\\_Petersburg\\_Declaration\\_ENG.pdf](https://www.g20.org/sites/default/files/g20_resources/library/Saint_Petersburg_Declaration_ENG.pdf) ("Cross-border tax evasion and avoidance undermine our public finances and our people's trust in the fairness of the tax system.").

<sup>60</sup> *See infra* note 92-96 and accompanying text.

<sup>61</sup> ANN MUMFORD, TAXING CULTURE: TOWARDS A THEORY OF TAX COLLECTION LAW 20 (2002).

more in the United States than elsewhere, taxation and tax collection agencies have been vilified in popular culture.<sup>62</sup> In a statement quoted so often that every experienced tax lawyer knows it by heart,<sup>63</sup> Judge Learned Hand proclaimed that, “[a]ny one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one’s taxes.”<sup>64</sup> Such language provides compelling rhetoric for the tax planning industry,<sup>65</sup> and may contribute to today’s “culture of tax avoidance.”<sup>66</sup>

Generally, the majority of U.S. citizens view taxes as necessary to fund beneficial programs such as education, healthcare, and Social Security,<sup>67</sup> but are frustrated by their belief that wealthy citizens are paying less than their fair share in taxes.<sup>68</sup> Indeed, Congress passed the 1996 Taxpayer Bill of Rights<sup>69</sup> in part to address the public’s growing sense of hostility toward the Internal Revenue Service (IRS).<sup>70</sup> The media’s alarmist treatment of the 2012 fiscal cliff debates further reflects U.S. ambivalence towards (or a general misunderstanding of) tax obligations, and indicates disagreement over who should bear the brunt of the burden with respect to reducing the tax deficit.<sup>71</sup>

When it comes to corporations rather than individuals not paying their fair share of taxes, however, U.S. citizens’ sentiments are somewhat clearer. Much the same as reactions to the downfall of rich and famous tax evaders, Americans appear to enjoy seeing big companies go down, regardless of

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<sup>62</sup> *Id.* at 1 (asserting that the United Kingdom lacks comparable references to the U.S. portrayal of tax paying in popular culture, referring in particular to the “[t]ouchstones of American taxpaying experience – 15 April, audits (and Nixon’s infamous abuse of them), Al Capone, Leona Helmsley, countless television shows recounting and creating the perceptions of power surrounding the IRS” (citations omitted)).

<sup>63</sup> BITTKER & MCMAHON, JR., *supra* note 7, ¶ 1.3[2].

<sup>64</sup> *Id.* (quoting *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934), *aff’d*, 293 U.S. 465 (1935)).

<sup>65</sup> See Ordower, *supra* note 16, at 47.

<sup>66</sup> *Id.*

<sup>67</sup> NAT’L PUB. RADIO ET AL., NATIONAL SURVEY OF AMERICANS’ VIEWS ON TAXES 2 (2003), available at [http://www.npr.org/news/specials/polls/taxes2003/20030415\\_taxes\\_survey.pdf](http://www.npr.org/news/specials/polls/taxes2003/20030415_taxes_survey.pdf) (finding that eighty percent of survey participants believed that “maintaining spending levels on domestic programs such as education, health care, and Social Security” was more important than lower taxes).

<sup>68</sup> THE PEW RESEARCH CTR. FOR THE PEOPLE & THE PRESS, WEALTHY NOT PAYING FAIR SHARE TOP COMPLAINT: TAX SYSTEM SEEN AS UNFAIR, IN NEED OF OVERHAUL 1 (2011), available at <http://www.people-press.org/files/legacy-pdf/12-20-11%20Taxes%20release.pdf>.

<sup>69</sup> The Taxpayer Bill of Rights 2, Pub. L. No. 104-168, 110 Stat. 1452 (1996); see also MUMFORD, *supra* note 61, at 44.

<sup>70</sup> MUMFORD, *supra* note 61, at 44-45.

<sup>71</sup> See, e.g., Paul Krugman, *Perspective on the Deal*, N.Y. TIMES (Jan. 1, 2013), <http://krugman.blogs.nytimes.com/2013/01/01/perspective-on-the-deal>.

whether they think the company actually did something wrong.<sup>72</sup> The news media, in turn, is happy to oblige: corporate tax avoiders have been making headlines on a near-daily basis.<sup>73</sup>

Perhaps most indicative of a growing consensus that paying taxes is the socially responsible thing for MNCs to do was that despite the party-line polarization of opinions toward taxes in the 2012 election, there was one survey item that won support from majorities of Democrat and Republican voters alike – limiting tax deductions for large MNCs.<sup>74</sup> Therefore, any reluctance to expand the purview of CSR to encompass antiavoidance doctrine may reflect the hesitation of a powerful minority of global corporate executives to relinquish the tangible benefits produced by such tax avoidance schemes, rather than popular opinion. At the same time, the American public's criticism of current corporate taxation indicates that MNCs and their stakeholders may be well situated to embrace a broader understanding of CSR.<sup>75</sup>

What motivates a corporation to use tax havens, or engage in tax avoidance schemes in general? Several studies indicate that corporate tax avoidance strategies (referred to as “tax planning”) are often pitched to companies as a way to increase financial accounting earnings, thus boosting firm reputation and possibly share price.<sup>76</sup> Some corporate leaders and analysts perceive tax

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<sup>72</sup> See Ordower, *supra* note 16, at 114 n.434 (“I suspect there is considerable *schadenfreude* (pleasure in the suffering of others) when someone who has sought to avoid taxes with clever schemes gets hit with a large tax liability or criminal prosecution. Anecdotally, I know that many members of the tax professional community did gloat over the travails of Jenkens & Gilchrist, KPMG, and earlier, Kanter and Eisenberg without any sense of conviction that those professionals did anything reprehensible.”).

<sup>73</sup> See Richard Lavoie, *Subverting the Rule of Law: The Judiciary's Role in Fostering Unethical Behavior*, 75 U. COLO. L. REV. 115, 181-82 (2004) (“Even more remarkable has been the extent to which [tax sheltering] transactions have struck a cord [sic] with the public. In recent years, the popular press has made a practice of highlighting the existence of aggressive transactions when they come to light. The negative impact of such tax shelter activity for self-assessment is apparent. When the average citizen believes he is a chump for paying his full taxes, the system is in serious trouble.” (footnote omitted)).

<sup>74</sup> THE PEW RESEARCH CTR. FOR THE PEOPLE & THE PRESS, DEEP DIVISIONS OVER DEBT REDUCTION PROPOSALS 4 (2012), available at <http://www.people-press.org/files/legacy-pdf/10-12-12%20Deficit%20Release.pdf> (“[L]imiting tax deductions for large corporations . . . wins support from majorities of both Obama voters (69%) and Romney voters (57%).”).

<sup>75</sup> Although the definition of MNC employed in this Note extends beyond MNCs headquartered in the United States, U.S. consumer culture and stakeholder interests continue to influence MNCs and belie the supposedly stakeholder-centric U.S. CSR model. See BRYAN HARRIGAN, CORPORATE SOCIAL RESPONSIBILITY IN THE 21ST CENTURY 107-08 (2010) (discussing the “US-style corporate constituency laws allow[ing] non-shareholder constituencies and third party effects to be considered by directors,” and discussing whether CSR models are converging towards the Anglo-American model).

<sup>76</sup> John R. Graham et al., *Incentives for Tax Planning and Avoidance: Evidence from the Field* 26 (MIT Sloan Research Paper No. 4990-12, 2013), available at <http://ssrn.com/abstract=2148407> (confirming previous studies that indicated “tax avoidance strategies are

avoidance as unproblematic, pointing to lawmakers' failures to make such practices illegal as an indication of its acceptability. For example, in defending Google's tax arrangements, which reportedly involved the (legal) transfer of "\$9.8bn . . . of revenues from international subsidiaries into Bermuda" in 2011, Google Chairman Eric Schmidt reportedly stated, "I am very proud of the structure that we set up. We did it based on the incentives that the governments offered us to operate."<sup>77</sup> Corporate leaders may even view tax avoidance as obligatory; as part of their fiduciary duties to shareholders. For example, in response to criticism of General Electric's tax practices, GE's 2010 Citizenship Report emphasized that the company "fully compl[ies] with the law and there are no exceptions," but at the same time acknowledged that it has "a responsibility to [its] shareowners to reduce [its] tax costs as the law allows."<sup>78</sup>

On the other hand, in a study analyzing why a corporate tax executive would refuse to engage in tax avoidance strategies, a majority (69.5%) of executives considered the "potential harm to firm reputation" to be an important or very important factor in determining whether or not to adopt a tax avoidance strategy.<sup>79</sup> In fact, the risk of harm to a firm's reputation was a more frequently cited consideration than the "risk of detection and challenge by the IRS."<sup>80</sup> This data suggests that for a company that does adopt tax avoidance schemes, the benefits outweigh the risks of harm to the company's reputation.

Overall, many factors influence corporate leaders' decisions whether or not to engage in tax avoidance practices. The difference between corporations that view tax avoidance as not only acceptable but necessary to fulfill fiduciary duties to shareholders, and corporations that fear tax avoidance will harm their reputation, is likely attributable to the greater reliance on branding and firm reputation in this second category of corporation. Accordingly, corporate reliance on brand and reputation is an important factor in evaluating and mitigating the harms caused by a corporation's tax avoidance activities.

## II. HOW THE CSR DOCTRINE CAN HELP

One might argue that corporations taking advantage of tax havens are merely maximizing shareholder wealth and should not be responsible for moral behavior that exceeds legal requirements. Critics of the CSR doctrine have similarly argued that corporate leaders should not be saddled with duties

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engaged in with a *primary motivation* to improve accounting performance metrics").

<sup>77</sup> *Google's Tax Avoidance Is Called "Capitalism," Says Chairman Eric Schmidt*, TELEGRAPH (U.K.) (Dec. 12, 2012), <http://www.telegraph.co.uk/technology/google/9739039/Googles-tax-avoidance-is-called-capitalism-says-chairman-Eric-Schmidt.html>.

<sup>78</sup> GEN. ELEC. CORP., GE 2010 CITIZENSHIP REPORT 17 (2010), available at [http://files.gecitizenship.com.s3.amazonaws.com/wp-content/uploads/2011/07/ge\\_2010\\_citizenship\\_report.pdf](http://files.gecitizenship.com.s3.amazonaws.com/wp-content/uploads/2011/07/ge_2010_citizenship_report.pdf).

<sup>79</sup> Graham et al., *supra* note 76, at 17. Graham and his coauthors view "tax planning" and "tax avoidance" as interchangeable and as encompassing tax sheltering activity. *Id.* at 1 n.1.

<sup>80</sup> *Id.* at 18.

beyond profit maximization.<sup>81</sup> Despite this opposition, advocates of environmental sustainability and human rights have successfully used CSR to convince corporations to make social responsibility in these areas the “norm.”<sup>82</sup> CSR can provide a conceptual framework and a practical vehicle for MNCs to adopt antiavoidance practices.

A. *What Is CSR?*

Though there are many definitions in circulation,<sup>83</sup> CSR generally refers to the “obligations and inclinations, if any, of corporations organized for profit, voluntarily to pursue social ends that conflict with the presumptive shareholder desire to maximize profit.”<sup>84</sup> Though CSR is much more widely accepted today than forty years ago, the term continues to elicit smirks and teasing references to tree huggers in certain crowds. Critics of CSR tend to support the traditional business management theory, advocated by Milton Friedman in 1970,<sup>85</sup> that “there is . . . only one social responsibility of business – to use its resources and engage in activities designed to increase its profits . . . .”<sup>86</sup> Apart from serving as a vehicle to discuss normative ideas of a corporation’s purpose, however, CSR provides a useful framework for evaluating corporate

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<sup>81</sup> See *supra* notes 77-78 and accompanying text (discussing reasons companies are motivated to avoid taxes).

<sup>82</sup> See LISBETH SEGERLUND, MAKING CORPORATE SOCIAL RESPONSIBILITY A GLOBAL CONCERN: NORM CONSTRUCTION IN A GLOBALIZING WORLD 30 (2010) (discussing the role of social norms in international relations, specifically the “norm cycle model”).

<sup>83</sup> For an in-depth discussion of the varying definitions of CSR, see EDWIN C. MUJIH, REGULATING MULTATIONALS IN DEVELOPING COUNTRIES: A CONCEPTUAL AND LEGAL FRAMEWORK FOR CORPORATE SOCIAL RESPONSIBILITY 7-11 (2012). For an interesting argument on how diverging definitions and lack of a “common language” undermine CSR efforts conceptually, see Michael Hopkins, *Criticism of the Corporate Social Responsibility Movement*, in CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY 543, 544-45 (Ramon Mullerat ed., 2d ed. 2011).

<sup>84</sup> David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 5-6 (1979); see also MUJIH, *supra* note 83, at 202 (“The main argument advanced . . . by advocates of corporate social responsibility is that the company does not exist solely to maximize profits for the shareholders, but also to serve the society on which it depends for its existence.” (citations omitted)).

<sup>85</sup> See MUJIH, *supra* note 83, at 201 (“Criticisms against the concept have been based almost entirely on the premise that the company exists solely to maximize profits for its shareholders, and that corporate social responsibility conflicts with this primary objective of the company.”); *id.* at 201 n.3 (“Proponents of corporate social responsibility can make their point by attacking the premise upon which these criticisms are based; by proving that the company does not exist solely to maximise profits for its shareholders, and that even if it did, corporate social responsibility would not necessarily conflict with such an objective.”).

<sup>86</sup> Milton Friedman, *A Friedman Doctrine – the Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32 (quoting MILTON FRIEDMAN, CAPITALISM AND FREEDOM 133 (1962)).

practices that do not necessarily align with the goal of profit maximization. For this reason, discussions of CSR in an international context often involve the consideration of social, environmental, and sustainability issues.<sup>87</sup>

In the era of globalization, CSR has become much more prominent.<sup>88</sup> MNCs seeking to minimize costs have strong incentives and opportunities to seek out legal environments that less stringently regulate, for example, human rights and environmental abuses.<sup>89</sup> NGOs have, at times, attempted to fill the void where an international legally binding framework did not exist,<sup>90</sup> encouraging “civil regulation” to address MNCs’ environmental and human rights violations.<sup>91</sup> International and intergovernmental organizations such as the United Nations,<sup>92</sup> OECD,<sup>93</sup> and the World Bank<sup>94</sup> also have issued guidelines and other forms of “soft law”<sup>95</sup> to minimize various types of MNC abuses.<sup>96</sup> These efforts at external regulation typically lacked reliable enforcement mechanisms.<sup>97</sup> Nonetheless, an increasing number of MNCs voluntarily began to adopt CSR initiatives targeting the traditional CSR issues of human rights and environmental sustainability.<sup>98</sup> Self-regulation affords MNCs the

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<sup>87</sup> Rosamund Thomas, *Business Ethics, in* CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY, *supra* note 83, at 35, 37 (distinguishing CSR from the concept of “business ethics,” which focuses more on morality issues, while acknowledging the two movements’ convergence).

<sup>88</sup> See SEGERLUND, *supra* note 82 (discussing global development of the concept of corporate social responsibility).

<sup>89</sup> See, e.g., MUJIH, *supra* note 83, at 69-70. In fact, some MNCs have even “taken advantage of their stronger bargaining power *vis-à-vis* host governments to water down standards.” *Id.* at 69.

<sup>90</sup> *Id.* at 151-63.

<sup>91</sup> *Id.* at 155 (“Civil regulation involves business complying not only with its own standards (corporate self regulation) or those of government (legal compliance), but also with norms and standards defined by civil institutions.”).

<sup>92</sup> See, e.g., UN, UNITED NATIONS GLOBAL COMPACT: ANNUAL REVIEW 2010 (2011), available at [http://www.unglobalcompact.org/docs/news\\_events/8.1/UN\\_Global\\_Compact\\_Annual\\_Review\\_2010.pdf](http://www.unglobalcompact.org/docs/news_events/8.1/UN_Global_Compact_Annual_Review_2010.pdf).

<sup>93</sup> See, e.g., ORG. FOR ECON. CO-OPERATION & DEV., OECD GUIDELINES FOR MULTINATIONAL ENTERPRISES: 2011 EDITION (2011), available at <http://www.oecd.org/corporate/mne/48004323.pdf>.

<sup>94</sup> WORLD BANK, THE WORLD BANK OPERATIONS MANUAL (rev. 2013), available at [http://siteresources.worldbank.org/OPSMANUAL/Resources/EntireOM\\_External.pdf](http://siteresources.worldbank.org/OPSMANUAL/Resources/EntireOM_External.pdf).

<sup>95</sup> See MUJIH, *supra* note 83, at 148 (defining “soft law” as “voluntary and not legally enforceable”).

<sup>96</sup> See *id.* at 135-51 (discussing the strengths and weaknesses of UN’s, OECD’s, and World Bank’s efforts). The World Trade Organization could also be mentioned, but its “devotion . . . to free trade means that it is seen by critics as part of the problem rather than part of the solution, as most of its decisions have been in favour of MNCs.” *Id.* at 133.

<sup>97</sup> See *id.* at 167.

<sup>98</sup> See *id.* at 218 (discussing the “trend towards self-regulation”).

opportunity to shape CSR initiatives to balance public (and stakeholder) expectations with corporate needs,<sup>99</sup> in line with the policies underlying the business judgment rule.<sup>100</sup> Thus, if notions of a corporation's obligation to engage in socially responsible activity expand beyond human rights and environmental issues,<sup>101</sup> a self-regulatory CSR approach could halt MNCs' "race to the bottom" and reduce the harms caused by MNCs' aggressive tax avoidance practices.

B. *Why Is Tax Avoidance a CSR Issue?*

Tax avoidance has rarely been discussed in the context of CSR.<sup>102</sup> There is, however, some indication that tax avoidance, as distinguished from tax evasion

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<sup>99</sup> See *id.* at 220-22.

<sup>100</sup> See *Gagliardi v. TriFoods Int'l, Inc.*, 683 A.2d 1049, 1052-53 (Del. Ch. 1996) ("[T]he first protection against a threat of sub-optimal risk acceptance is the so-called business judgment rule. That 'rule' in effect provides that where a director is independent and disinterested, there can be no liability for corporate loss, unless the facts are such that no person could possibly authorize such a transaction if he or she were attempting in good faith to meet their duty."); MODEL BUS. CORP. ACT § 8.31 (2008).

<sup>101</sup> Particularly because self-regulation provides MNCs with the opportunity to shape their own social commitments, modern views of "socially responsible" activity have already greatly expanded. See *infra* note 176 and accompanying text (discussing the expansion of "ethical criteria" depending on investor preferences).

<sup>102</sup> See Mihir A. Desai & Dhammika Dharmapala, *CSR and Taxation: The Missing Link*, LEADING PERSP., Winter 2006, at 4 ("Surprisingly, taxation does not typically figure in the analysis of CSR."); Prem Sikka, *Smoke and Mirrors: Corporate Social Responsibility and Tax Avoidance*, 34 ACCT. F. 153, 154 (2010) ("[L]ittle scholarly attention is paid to the payment of democratically agreed taxes; even though the payment of taxes is central to any notion of responsible citizenship . . . ." (citation omitted)); cf. Hasseldine & Morris, *supra* note 9, at 9 ("[S]tudies show that researchers have been investigating the moral aspects of tax compliance and corporate compliance for many years.").

Those academic articles that do discuss tax avoidance as it relates to CSR unwaveringly suggest that tax avoidance should be considered a CSR issue. See, e.g., John Christensen & Richard Murphy, *The Social Irresponsibility of Corporate Tax Avoidance: Taking CSR to the Bottom Line*, 47 DEVELOPMENT 37, 37 (2004) (arguing that tax systems are crucial for the "infrastructure of justice" and thus tax avoidance should be a CSR issue); Sikka, *supra*, at 157-64 (discussing tax avoidance as a CSR issue). These articles conflate tax evasion and tax avoidance, however, and therefore present a different argument from that presented in this Note. See Christensen & Murphy, *supra* (referring to the money laundering and other illegal practices in which Enron, WorldCom, Tyco, Yukos, Parmalat, and the Big-Four global accounting firms engaged – activities I would consider tax evasion – as examples of the "tax-avoidance mechanisms" that should be considered socially irresponsible); Hasseldine & Morris, *supra* note 9, at 2 (discussing Sikka, *supra*, and pointing out that nearly all of the examples of "tax avoidance" provided in the article involve corrupt or fraudulent behavior typically identified as tax evasion, rather than the type of corporate activities "for which the distinction between tax avoidance and tax evasion is relevant and useful").



(and thus despite its admitted legality), is perceivable as a morally reprehensible business practice.<sup>103</sup> One potential explanation for the lack of attention to tax avoidance with regard to CSR may be that taxation lacks the sensationalist, attention-grabbing nature of environmental and human rights abuses. The media's continued devotion of attention and resources to criticizing the tax practices of Apple,<sup>104</sup> Google,<sup>105</sup> Amazon,<sup>106</sup> and Starbucks,<sup>107</sup> however, may suggest that tax avoidance is indeed becoming a "sexier" topic. Such negative publicity may cause reputational harm to MNCs that engage in tax avoidance practices, which in turn may cause financial harm to their shareholders.<sup>108</sup> MNCs that adopt antiavoidance practices as part of their CSR frameworks, however, could avoid such detrimental effects while potentially boosting investments and sales.<sup>109</sup>

Some CSR proponents insist that engaging in socially responsible activities is not only the right thing to do, but also that it produces long-term financial gains in excess of any short-term gains from engaging in socially irresponsible activities.<sup>110</sup> Another articulation of CSR doctrine, however, acknowledges that CSR may require forgoing profits realized as a result of socially irresponsible activities, but nonetheless advocates socially responsible activity over profit maximization when such a tradeoff is necessary.<sup>111</sup> If CSR is indeed premised

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<sup>103</sup> See, e.g., Christopher Hope, *David Cameron: Tax Avoiding Foreign Firms Like Starbucks and Amazon Lack 'Moral Scruples,'* TELEGRAPH (U.K.) (Jan. 4, 2013), <http://www.telegraph.co.uk/news/politics/david-cameron/9779983/David-Cameron-Tax-avoiding-foreign-firms-like-Starbucks-and-Amazon-lack-moral-scruples.html>.

<sup>104</sup> Norris, *supra* note 4, at B1.

<sup>105</sup> Pfanner, *supra* note 4, at B1 ("Google reported sales of more than \$4 billion in Britain last year. It paid less than \$10 million in taxes. Some tax collectors, lawmakers and competitors of Google in Europe say this is unfair.")

<sup>106</sup> *Id.* (discussing Amazon's tax avoidance strategies as explained during a Parliament committee hearing).

<sup>107</sup> *Id.* (discussing the outrage expressed by members of Parliament as they asked representatives of Starbucks and other corporations about tax avoidance schemes).

<sup>108</sup> See discussion *infra* Part III.A.1 (discussing the reputational effects of negative publicity due to tax avoidance).

<sup>109</sup> See *infra* note 170 and accompanying text.

<sup>110</sup> RAMON MULLERAT, INTERNATIONAL CORPORATE SOCIAL RESPONSIBILITY: THE ROLE OF CORPORATIONS IN THE ECONOMIC ORDER OF THE 21ST CENTURY 40 (2010).

<sup>111</sup> Aneel Karnani, *The Case Against Corporate Social Responsibility*, WALL ST. J. (June 14, 2012), <http://online.wsj.com/article/SB10001424052748703338004575230112664504890.html> ("[T]he fact is that while companies sometimes can do well by doing good, more often they can't. Because in most cases, doing what's best for society means sacrificing profits."); Thomas Lys et al., *Pinpointing the Value in CSR*, KELLOGG INSIGHT (Mar. 4, 2013), [http://insight.kellogg.northwestern.edu/article/pinpointing\\_the\\_value\\_in\\_csr](http://insight.kellogg.northwestern.edu/article/pinpointing_the_value_in_csr) ("We find that CSR expenditures generate insufficient returns and hence reduce shareholder value, consistent with the Friedman view. We also find, however, that companies whose CSR spending exceeds investor expectations experience positive stock returns, consistent with

on the “avoidance of negative externalities” and “the provision of positive benefits,”<sup>112</sup> as some claim, corporations should not engage in tax avoidance practices if the costs to others from this behavior exceed the actual benefits. Because tax avoidance, in general, and the use of tax havens, in particular, may cause long-term financial harm not only to MNCs and their shareholders but also to the citizens and governments of nations that serve as tax havens for these practices, MNCs should treat tax avoidance as they treat environmentally harmful activities or human rights abuses: as a CSR issue that may necessitate the sacrifice of profits to mitigate financial harm to various other stakeholders.

### III. HOW TAX AVOIDANCE HARMS CORPORATIONS AND THEIR SHAREHOLDERS

#### A. *Harms to the Corporation and Its Shareholders*

##### 1. Harm to Corporate Reputation

Many companies already are facing intense scrutiny for their tax avoidance practices.<sup>113</sup> Some analysts suggest that the “pressure not to push avoidance too far is mounting, and . . . companies may have more to fear from the public than from governments.”<sup>114</sup> Consumers’ perceptions of corporate performance are more sensitive to news of socially irresponsible activity than to news of socially responsible activity.<sup>115</sup> Thus, as corporate tax avoidance becomes increasingly publicized and stigmatized, news of a corporation’s engagement in tax avoidance practices likely will have an increasingly detrimental effect on its reputation. Some corporations are more susceptible to reputational harm than others. For example, some studies have assessed the market reaction to

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evidence promoted by CSR proponents.”); Kash Rangan et al., *Why Every Company Needs a CSR Strategy and How to Build It 1* (Harv. Bus. Sch., Working Paper No. 12-088, 2012) available at <http://www.hbs.edu/faculty/Publication%20Files/12-088.pdf> (“The tension between business goals and social/environmental goals cannot be wished away with the hope of co-creating private and public value.”); David Vogel, *CSR Doesn’t Pay*, FORBES (Oct. 16, 2008), [http://www.forbes.com/2008/10/16/csr-doesnt-pay-lead-corprespns08-cx\\_dv\\_1016vogel.html](http://www.forbes.com/2008/10/16/csr-doesnt-pay-lead-corprespns08-cx_dv_1016vogel.html) (“The belief that corporate responsibility ‘pays’ is a seductive one: Who would not want to live in a world in which corporate virtue is rewarded and corporate irresponsibility punished? Unfortunately, the evidence for these rewards and punishment is rather weak.”).

<sup>112</sup> MUJH, *supra* note 83, at 10.

<sup>113</sup> See *infra* note 159 and accompanying text (discussing public outrage and potential boycotts against companies that engage in tax avoidance).

<sup>114</sup> Matthew Valencia, *Storm Survivors*, ECONOMIST, Feb. 16, 2013, at 3, 12-13 (“Companies may feel bound to exploit weaknesses in the [tax] rules, if only because not doing so would put them at a competitive disadvantage.”).

<sup>115</sup> Sankar Sen & C. B. Bhattacharya, *Does Doing Good Always Lead to Doing Better? Consumer Reactions to Corporate Social Responsibility*, 38 J. MARKETING RES. 225, 238 (2011).

news of a corporation's tax avoidance,<sup>116</sup> and have concluded that this publicity has only minimal reputational costs, as measured by "CEO and CFO turnover, changes in advertising expense, auditor turnover, or decrease in sales."<sup>117</sup> Such mild consequences can be explained by the fact that the corporations in these studies likely had little to lose from such a reputational hit to begin with, and the corporations therefore likely decided that the benefits of adopting a tax avoidance strategy outweighed the costs.<sup>118</sup> Conversely, companies whose success depends strongly on their reputations are more likely to eschew a tax avoidance scheme in favor of tax practices that are less likely to attract public scrutiny.

Although some companies have shown resilience to public pressure to engage in socially responsible tax practices,<sup>119</sup> Starbucks decided in December 2012 to pay U.K. tax authorities around ten million pounds (approximately sixteen million dollars) more in taxes than it was required to pay in order to "quell the controversy over its virtually nonexistent tax bill."<sup>120</sup> A corporation like Starbucks that is very much in the public eye – and therefore has more to lose from a hit to its reputation – has a weaker argument than less visible corporations that engaging in tax avoidance practices will provide a net benefit to the corporation and its shareholders.

## 2. Encouraging Other Subversive Activities by Management

Engaging in objectionable tax avoidance schemes may also pave the road for MNCs' management to engage in other subversive activities. Mihir Desai suggests that because "tax avoidance demands obfuscation and this obfuscation can become the shield for actions that are not in the interests of shareholders . . . corporate tax avoidance is often linked to acts of managerial malfeasance."<sup>121</sup> The high-profile cases of managerial misreporting at Enron, Tyco, and Xerox indicate that "the drive to improve reported book profits fosters tax avoidance

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<sup>116</sup> Michelle Hanlon & Joel Slemrod, *What Does Tax Aggressiveness Signal? Evidence from Stock Price Reactions to News About Tax Shelter Involvement*, 93 J. PUB. ECON. 126 (2009) (investigating stock market responses to tax avoidance practices).

<sup>117</sup> Graham et al., *supra* note 76, at 15 (citing John Gallemler et al., *The Reputational Costs of Tax Avoidance*, CONTEMP. ACCT. RES. (forthcoming 2014), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1986226](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1986226)).

<sup>118</sup> *Id.* at 14-16.

<sup>119</sup> See *infra* note 159 and accompanying text (discussing the extent to which consumer boycott power can change a company's tax avoidance practices).

<sup>120</sup> Bruce Bartlett, *Can Publicity Curb Corporate Tax Avoidance?*, FT (Jan. 31, 2013, 1:52 PM), <http://blogs.ft.com/the-a-list/2013/01/31/#axzz2gzWJJwM>; see also *Corporate Taxation: Wake up and Smell the Coffee*, ECONOMIST, Dec. 15, 2012, at 66, 66.

<sup>121</sup> Desai & Dharmapala, *supra* note 102, at 5; see also Andrew K. Rose & Mark M. Spiegel, *Offshore Financial Centres: Parasites or Symbionts?*, 117 ECON. J. 1310, 1329 (2007) (admitting that "successful offshore financial centers encourage bad behavior in source countries, since they facilitate tax evasion and money laundering" but maintaining that their presence "enhances the competitiveness of the local banking sector").

and . . . the drive to limit taxes gives rise to the manipulation of accounting profits and managerial malfeasance.”<sup>122</sup> As a result of this increased likelihood of managerial malfeasance, “corporate tax avoidance is not fully valued in the stock market by investors.”<sup>123</sup>

Because shareholders and tax authorities have a common interest in “containing opportunistic managers,”<sup>124</sup> shareholders in MNCs should hold directors accountable for their decisions to engage in tax avoidance practices. Shareholders also may grow suspicious that a corporation that is willing to cheat the government may be just as willing to cheat its own shareholders.<sup>125</sup>

## B. Harms to National Governments

### 1. Developed Nations

An MNC’s use of tax havens is yet another way its tax avoidance practices can cause harm to third parties. Tax havens have been charged with “undermin[ing] the international financial regulatory environment and taxation policies” of these countries while “skewing the allocation of costs and benefits of globalization.”<sup>126</sup> In fact, one of the biggest difficulties in effecting antiavoidance regulations is the fact that MNCs can avoid such restrictions by simply relocating to countries with more lenient tax regulations.<sup>127</sup> This choice to relocate in order to avoid regulations is especially easy for corporations that transact in intangible goods, such as finance or technology.<sup>128</sup> Several European nations recently have articulated a renewed interest in combating

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<sup>122</sup> Mihir A. Desai, *The Degradation of Reported Corporate Profits*, 19 J. ECON. PERSP. 171, 171 (2005).

<sup>123</sup> Desai & Dharmapala, *supra* note 102, at 5.

<sup>124</sup> *Id.*

<sup>125</sup> Fariz Huseynov & Bonnie K. Klamm, *Tax Avoidance, Tax Management and Corporate Social Responsibility*, 18 J. CORP. FIN. 804, 804 (2012).

<sup>126</sup> PALAN ET AL., *supra* note 3, at 7; *see also* FEETHAM, *supra* note 9, at 1 (“[Tax havens] are said to erode the tax base of high tax jurisdictions and have come under severe pressure over the last 10 years, accused of ‘unfair tax competition’ . . . .”); Christensen & Murphy, *supra* note 102, at 37 (“Tax revenues are the lifeblood of the social contract, vital to the development and maintenance of physical infrastructure and to the sustenance of the infrastructure of justice that underpins liberty and the market economy.”); *cf.* Richard W. Rahn, *In Defense of Tax Havens*, WALL ST. J., Mar. 18, 2009, at A15 (arguing that tax havens “enable[] a better allocation of world capital, leading to higher, not lower, global growth rates”).

<sup>127</sup> FEETHAM, *supra* note 9, at 80.

<sup>128</sup> *See* Harry Grupert, *Foreign Taxes and the Growing Share of U.S. Multinational Company Income Abroad: Profits, Not Sales, Are Being Globalized* 9 (Office of Tax Analysis, Dep’t of the Treasury, Working Paper No. 103, 2012) (“[S]ome companies’ choice of location is more responsive to tax differences. For example, mobile tech companies that serve a worldwide market can easily locate in low tax jurisdictions.” (footnote omitted)).

antiavoidance schemes.<sup>129</sup> In the developed world, one clear consequence of MNCs' use of tax havens is increased tax competition among and within states, as governments have "found themselves under growing pressure to lower taxes on capital and businesses."<sup>130</sup> One of the criticisms of U.S.-based MNCs using tax havens, for example, is that they "benefit from the security and stability of the U.S. economy, the productivity and expertise of U.S. workers and the strength of U.S. infrastructure to develop enormously profitable products here in the United States," while simultaneously "avoiding the taxes that help support [U.S.] security, stability and productivity."<sup>131</sup> Even more alarming is the fact that "corporations bear a much smaller share of the tax burden" than U.S. citizens; indeed, the payroll taxes which "almost every income earner, rich, middle-income and poor, must pay . . . have skyrocketed from 9.7 percent of federal revenue to 40 percent."<sup>132</sup>

Tax avoidance practices cost the U.S. government up to \$100 billion in lost revenue each year,<sup>133</sup> in addition to causing financial harm to the government of the offshore locale, the corporation itself, and the corporation's shareholders. The Tax Code provides that "[i]f a company earns income from an active business activity offshore, it owes no U.S. tax until the income is returned to the United States."<sup>134</sup> These types of deferrals for offshore activity, however, are not permitted for "passive, inherently mobile income such as royalty, interest, or dividend income."<sup>135</sup> The Senate Permanent Subcommittee on Investigations has acknowledged that this rule, along with weaknesses in the tax code's transfer pricing regulations<sup>136</sup> and the Financial Accounting Standards Board's (FASB) accounting standard APB 23,<sup>137</sup> provides strong

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<sup>129</sup> See, e.g., Andrew E. Kramer & Floyd Norris, *G-20 Backs Plan to Curb Corporate Tax Strategy*, N.Y. TIMES, July 20, 2013, at B1 ("The world's richest economies for the first time endorsed a blueprint on Friday to curb widely used tax avoidance strategies that allow some multinational corporations to pay only a pittance in income taxes.").

<sup>130</sup> PALAN ET AL., *supra* note 3, at 154.

<sup>131</sup> *Offshore Profit Shifting Hearing*, *supra* note 31, app. at 77 (statement of Sen. Carl Levin).

<sup>132</sup> Press Release, U.S. Senate Permanent Subcomm. on Investigations, *supra* note 33.

<sup>133</sup> See *Abusive Offshore Tax Avoidance Schemes – Talking Points*, IRS, <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Abusive-Offshore-Tax-Avoidance-Schemes-Talking-Points> (last updated Sept. 18, 2013).

<sup>134</sup> See *Offshore Profit Shifting Hearing*, *supra* note 31, app. at 79.

<sup>135</sup> *Id.*

<sup>136</sup> See 26 U.S.C. §§ 482, 956 (2012).

<sup>137</sup> See generally ACCOUNTING PRINCIPLES BD., AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, OPINIONS OF THE ACCOUNTING PRINCIPLES BOARD NO. 23: ACCOUNTING FOR INCOME TAXES – SPECIAL AREAS (1972), available at <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175820901676&blobheader=application%2Fpdf> (outlining board recommendations and opinions regarding undistributed earnings of subsidiaries, corporate joint ventures investment, savings and loan debt reserves, and policyholders' surplus stock).

incentives for U.S.-headquartered MNCs to shift intellectual property and profits offshore.<sup>138</sup>

## 2. Developing Nations

Some developing nations have “adopted tax haven legislation as a conscious, intentional, and long-term developmental strategy” with varying degrees of success.<sup>139</sup> These governments are fully within their rights as sovereign nations (or city-states) to designate their own laws and regulations regarding taxation and disclosure requirements,<sup>140</sup> and international organizations and NGOs would be hard-pressed to find a mechanism to enforce external prohibitions on nations providing MNCs with favorable tax rates. Tax avoidance practices cause more financial harm to the governments of developing nations than to those of developed nations.<sup>141</sup> Tax haven policies may be attractive to developing nations because they appear to result in high amounts of foreign direct investment (FDI) in host countries.<sup>142</sup> These numbers are misleading, however, because they do not incorporate the problem of capital flight. Perhaps the biggest problem facing tax-haven hosts, capital flight is “the movement across international borders of money ‘that is illegally earned, illegally transferred, or illegally utilized if it breaks the laws in its origin, movement, or use.’”<sup>143</sup> While illicit capital flight “results from deliberate misreporting, . . . it often occurs through channels similar to those used for the legitimate transfer of funds.”<sup>144</sup> These transfers, however, typically are one directional (out of the country), involve transfer pricing, or make a “round-trip” and reappear in the host country disguised as FDI.<sup>145</sup> Consequently, it is very unlikely that reported amounts of FDI actually reflect long-term investments in the tax haven host country.<sup>146</sup>

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<sup>138</sup> See Press Release, U.S. Senate Permanent Subcomm. on Investigations, *supra* note 33.

<sup>139</sup> PALAN ET AL., *supra* note 3, at 22, 182 (“Being a tax haven has proved in a few cases to be a successful developmental strategy. . . . Yet some tax havens are among the poorest nations in the world.”).

<sup>140</sup> See *id.* at 3.

<sup>141</sup> Christensen & Murphy, *supra* note 102, at 40 (“While the tax-avoidance industry is clearly damaging to the interests of developed countries, it is almost certain that harmful tax practices are an even greater problem for economies in transition and developing countries.”).

<sup>142</sup> *Id.* at 41.

<sup>143</sup> PALAN ET AL., *supra* note 3, at 173 (citing RAYMOND W. BAKER, CAPITALISM’S ACHILLES HEEL: DIRTY MONEY AND HOW TO RENEW THE FREE-MARKET SYSTEM 23 (2005)).

<sup>144</sup> *Id.*

<sup>145</sup> *Id.* at 174-75, 181.

<sup>146</sup> For example, this phenomenon has appeared recently in China and in Latin America in the 1990s. See *id.* at 181. But see Dhammika Dharmapala & James R. Hines, Jr., *Which Countries Become Tax Havens?*, 93 J. PUB. ECON. 1058, 1058 (2009) (“Tax haven countries receive extensive foreign investment, and, largely as a result, have enjoyed very rapid

Although a small number of countries have used tax haven policies successfully as a path to development, some tax havens, such as those in the Pacific islands, remain among the poorest nations in the world.<sup>147</sup> Several theories exist as to why certain tax havens are able to use tax haven policies successfully as a development strategy: these include agglomeration, spillover, and no choice theory.<sup>148</sup> According to the agglomeration theory, funds diverted to tax havens are used to develop infrastructure, while the organizations that crop up to support the industry promote hiring.<sup>149</sup> Similarly, the spillover theory suggests that tourism, construction, and offshore finance operations function collectively to boost tax haven economies with a trickle-down effect.<sup>150</sup> Finally, the no choice theory suggests that small nations, with low infrastructure costs and labor forces too small to permit global competitiveness in industries like manufacturing, are effectively required to enter the tax haven market in order to promote development.<sup>151</sup>

Still, Professor Ronen Palan, Richard Murphy, and Christian Chavagneux suggest that there are good reasons to doubt that the wealth brought to tax havens actually does trickle down, and observe that the types of tourism and businesses that develop in order to facilitate tax sheltering activity typically crowd out indigenous populations by bringing their own workforce and raising property values and prices beyond what locals can afford.<sup>152</sup> Therefore, because reported FDI tends to be illusory and wealth remains concentrated in the hands of the MNCs and individuals who make use of tax havens' financial services, tax haven policies tend to have harmful financial effects on developing nations and their populations. Thus, while these MNCs do not employ child labor forces or pollute native habitats, their use of tax havens is exploitative, and corporate management should consider the harmful financial consequences on third parties of tax avoidance policies as part of a comprehensive CSR regime.

#### IV. SOLUTIONS FOR INCORPORATING THE ANTI-AVOIDANCE DOCTRINE INTO CORPORATE POLICY AND CHANGING CORPORATE TAX AVOIDANCE CULTURE

MNC directors and officers inclined to adopt antiavoidance policies and practices face two main obstacles: loss of competitive positioning in the marketplace<sup>153</sup> and opposition by shareholders and investors. Because paying

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economic growth over the past 25 years.” (citing James R. Hines, Jr., *Do Tax Havens Flourish?*, 19 TAX POL'Y & ECON. 65 (2005)).

<sup>147</sup> PALAN ET AL., *supra* note 3, at 182.

<sup>148</sup> *Id.* at 182-85.

<sup>149</sup> *Id.* at 182-83.

<sup>150</sup> *Id.* at 183-84.

<sup>151</sup> *Id.* at 185.

<sup>152</sup> *Id.* at 183, 185-86 (contesting the theory of the agglomeration effect on the ground that tax haven countries become vulnerable by relying too heavily on one industry).

<sup>153</sup> Valencia, *supra* note 114, at 12 (“Companies may feel bound to exploit weaknesses in

more taxes conflicts with the idea of maximizing shareholder wealth, MNCs that adopt antiavoidance policies will encounter many of the same barriers as corporations that practice traditional CSR policies.

How did corporations come to embrace the CSR doctrine despite this (real or perceived) conflict with shareholder objectives? Felix Martin suggests that three principal means of “selling the message” of CSR have been consumer activism, investor influence, and voluntary measures taken by leading corporations.<sup>154</sup> Antiavoidance proponents can use these same tactics to overcome the barriers to competitiveness and investor approval that application of the CSR doctrine to tax avoidance policies may cause.

#### A. *Consumer Activism*

One method of promoting antiavoidance practices from below is consumer activism. CSR advocates have used “name-and-shame” campaigns to successfully “shame” corporations into adopting CSR practices in other contexts,<sup>155</sup> and a similar approach could motivate known corporate tax avoiders to change their ways. For example, the publicity surrounding Nike’s human rights abuses in overseas factories ultimately led Nike to spearhead a supply chain initiative with notable success<sup>156</sup>: the campaign improved both the corporation’s image and factory conditions throughout the industry.<sup>157</sup> Similarly, Walmart’s supply chain initiatives in response to criticism about its environmental abuses have “pressured its retail competitors to adopt the same standards for product sourcing and supply chain efficiency.”<sup>158</sup>

In response to the recent publicity, consumers have used their buying power to influence MNCs’ tax avoidance policies in the absence of external regulations.<sup>159</sup> Yet, while “[t]here is growing evidence that corporations are

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the [tax] rules, if only because not doing so would put them at a competitive disadvantage.”)

<sup>154</sup> Felix Martin, *Corporate Social Responsibility and Public Policy*, in CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY, *supra* note 83, at 95-97.

<sup>155</sup> Richard Welford & Peter Hills, *People’s Republic of China*, in GLOBAL PRACTICES OF CORPORATE SOCIAL RESPONSIBILITY 186 (Samuel O. Idowu & Walter Leal Filho eds., 2008).

<sup>156</sup> Rangan et al., *supra* note 111, at 9.

<sup>157</sup> See Michael Connor, *Nike: Corporate Responsibility at a “Tipping Point,”* BUS. ETHICS (Jan. 24, 2010), <http://business-ethics.com/2010/01/24/2154-nike-corporate-responsibility-at-a-tipping-point>.

<sup>158</sup> Rangan et al., *supra* note 111, at 9.

<sup>159</sup> See Margaret Hodge & Jeff Jarvis, *Should We Boycott Google, Starbucks and Amazon?*, GUARDIAN (Nov. 17, 2012, 1:00 PM), <http://www.theguardian.com/commentisfree/2012/nov/17/should-boycott-google-starbucks-amazon> (“Of course it is up to the government to act, both in the UK and internationally, to ensure that global companies pay tax according to where they make their profit and don’t stash it away in tax havens such as Luxembourg and Bermuda. But consumers can use their power too. By boycotting these



sensitive to the public outcry when they are caught avoiding taxation excessively,<sup>160</sup> some analysts have questioned whether shaming sanctions actually deter corporate tax abuse.<sup>161</sup> Tax havens, in turn, “not only arise and persist in the face of such seemingly overwhelming attack and criticism, they seem to flourish.”<sup>162</sup> For example, corporations exposed in the press for taking advantage of tax havens did not experience a drop in their share prices or major boycotts of their goods.<sup>163</sup> Nor did these corporations’ tax directors face adverse professional consequences.<sup>164</sup> Such outcomes indicate the limited deterrent effect of consumer backlash, and may even “send an unintended positive signal to the members of a corporation’s community. . . . Short-term investors, like hedge and private equity funds, may be attracted to, rather than repelled by, corporations with tax directors who claim tax positions that ‘push the envelope.’”<sup>165</sup> Additionally, corporate tax directors may adopt aggressive tax avoidance strategies because, in accordance with reciprocity theory, “actors may reduce their own contributions toward a public good if they begin to feel like ‘chumps’ for complying while others cheat.”<sup>166</sup>

Nonetheless, as consumer expectations change, tax avoidance could come to be viewed as a socially irresponsible activity, and antiavoidance seen as a CSR “norm.”<sup>167</sup> Antiavoidance advocates already have begun to use modern platforms in pursuit of change, rallying support with the claim that “big corporations need to pay their fair share of taxes”<sup>168</sup> and advocating tax

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companies we not only voice our anger but hit them where it hurts. And any credible government will have to respond to public outrage at unacceptable tax avoidance.”)

<sup>160</sup> Bartlett, *supra* note 120.

<sup>161</sup> See Joshua D. Blank, *What’s Wrong with Shaming Corporate Tax Abuse*, 62 TAX L. REV. 539, 545-46 (2009); John Hayward, *The Global Non-Crime Wave of Tax Avoidance*, HUM. EVENTS (Jan. 13, 2012, 9:42 AM), <http://www.humanevents.com/2012/12/13/the-global-non-crime-wave-of-tax-avoidance> (objecting to the idea of having governments “whip up ‘public pressure’ to force companies to fork over money beyond their legal obligations”).

<sup>162</sup> See Adam H. Rosenzweig, *Why Are There Tax Havens?*, 52 WM. & MARY L. REV. 923, 927 (2010).

<sup>163</sup> Blank, *supra* note 161, at 541.

<sup>164</sup> *Id.* at 541-42.

<sup>165</sup> *Id.* at 541.

<sup>166</sup> *Id.* at 542 (citing Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO ST. L.J. 1453, 1487 (2003)).

<sup>167</sup> See SEGERLUND, *supra* note 82, at 14-15, 26-30 (describing the three-stage process of “norm” creation: emergence, cascade, and internalization).

<sup>168</sup> See, e.g., *Corporations: Pay Your Fair Share*, MOVEON, <http://pol.moveon.org/exxon-taxday> (last visited Nov. 12, 2013); *Raise Revenue Through Corporate Tax Reform*, AM. SUSTAINABLE BUS. COUNCIL, <http://asbcouncil.org/campaigns/corporate-taxes> (last visited Nov. 12, 2013); *Stop Trillions in Tax Breaks for Millionaires and Big Corporations*, FAIRSHAREONLINE, <http://www.fairshareonline.org/budget> (last visited Nov. 12, 2013); *Why Are You Paying More Taxes than G.E.?*, PEOPLE FOR THE AM. WAY, <https://secure.pfaw.org/>

reforms to close loopholes that enable tax avoidance practices.<sup>169</sup> As the public adopts an increasingly negative view of corporate tax avoidance practices, MNCs that adopt antiavoidance practices will gain a competitive advantage. In turn, when customers perceive an MNC's CSR policy as providing a competitive advantage, customers become more likely to purchase the corporation's products and highly evaluate its performance.<sup>170</sup> Consumers may also pressure an MNC to disclose tax payment information in its corporate accountability report in accordance with Global Reporting Initiative (GRI) guidelines (these reports provide consumers with information about a corporation's contribution to overall economic sustainability).<sup>171</sup> It may take only a handful of MNCs caving to public pressure, as Starbucks did,<sup>172</sup> to force others to follow suit.

### B. *Investor Influence*

In addition to becoming involved in "name and shame" campaigns, shareholders and other corporate investors can influence corporations to adopt CSR policies through selective purchasing and other shareholder activism.<sup>173</sup> For example, in 2010, Intel responded to a shareholder resolution calling for the adoption and reporting of sustainability practices by making the implementation and reporting of such practices an official fiduciary duty of Intel's corporate board, and included this change in its corporate charter.<sup>174</sup>

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site/SPageServer?JServSessionIdr004=fzrfey98b1.app341b&autologin=true&pagename=G  
E (last visited Nov. 12, 2013).

<sup>169</sup> See, e.g., *Raise Revenue Through Corporate Tax Reform*, *supra* note 168.

<sup>170</sup> Sen & Bhattacharya, *supra* note 115, at 238.

<sup>171</sup> Angela K. Davis et al., *Taxes and Corporate Sustainability Reporting: Is Paying Taxes Viewed as Socially Responsible?* 7 (May 28, 2013) (unpublished manuscript, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2275633](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2275633)). Interestingly, a sample of corporate accountability reports indicated three conflicting responses from firms. First, some firms disclosed tax information in accordance with GRI guidelines, indicating some level of agreement with the GRI's idea that tax payments reflect the firm's contribution to the larger economic community. *Id.* at 12. Second, some firms expressed a directly inapposite view, disclosing their efforts at reducing corporate tax rates on the basis that high tax rates "discourage innovation and investment and harm job creation, and therefore hurt the ability of the firm to contribute to social welfare." *Id.* at 10. Third, nearly half of the firms in the sample did not disclose any tax information at all, or simply referred readers to the firm's Form 10-K (even though GAAP requirements differ from GRI disclosure guidelines), perhaps indicating that these firms do not consider tax information to be of high importance to stakeholders. *Id.* at 2, 10. These firms all fall within the subcategory of firms who issue corporate accountability reports, thus indicating some degree of commitment to social responsibility.

<sup>172</sup> See *supra* note 120 and accompanying text.

<sup>173</sup> See Martin, *supra* note 154, at 99-100 (discussing how shareholders and investors can take action to influence corporations to adopt socially responsible standards).

<sup>174</sup> Mike Valente, *Shareholder Pressure for Social Responsibility*, SUSTAINABLE BUS. F.

Investors can obtain information on the CSR practices of various corporations through “ethical indexes,” such as FTSE4Good, the Dow Jones Sustainability Index, and Sao Paulo’s Novo Mercado.<sup>175</sup> The number of ethical indexes available has expanded over the years to accommodate new ethical criteria, since ethical concerns evolve and vary among investors.<sup>176</sup>

Investors concerned with corporate tax avoidance can use their purchase power in much the same way as consumers by opting to invest only in corporations with antiavoidance policies in place. As public pressure mounts, ethical indexes charting corporate tax avoidance practices also may emerge, supplementing the negative media coverage to which investors already have access and making informed investment decisions quicker and easier. This tactic, of course, is contingent upon gathering a group of shareholders large enough to influence corporate goals. Further, it requires finding investors willing to take a cut in dividends or future growth in order to motivate the corporation to pioneer antiavoidance policies. Consumers, who have less to lose (at least directly), may be better positioned than shareholders to place such pressure on MNCs.

Overall, the actions of investors and consumers, in combination with ever-growing governmental, NGO, and other international efforts to implement external regulation and guidance, may motivate MNCs to adopt antiavoidance policies as a form of CSR. By adopting the same strategy adopted to advocate CSR in more traditional spheres, antiavoidance proponents can avoid creating competitive disadvantages by making the move toward CSR in the context of tax avoidance so widespread as to become necessary to remain competitive. Proponents also can avoid shareholder disapproval by increasing awareness of the harms of tax avoidance so that investors come to demand, rather than object to, the adoption of antiavoidance policies.

### C. *Voluntary Corporate Leadership*

When it comes to maintaining competitive ground and mitigating investor disapproval of CSR policies, bigger or more well-known companies may be better suited to lead the way.<sup>177</sup> For example, Cisco and Nestle have demonstrated that MNCs can create both private and public value.<sup>178</sup> Precisely

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(Apr. 20, 2010), <http://sustainablebusinessforum.com/mikevalente/47935/shareholder-pressure-social-responsibility>.

<sup>175</sup> Martin, *supra* note 154, at 100.

<sup>176</sup> *Id.* at 100 n.13 (noting that, while useful for investors, this proliferation of issue-specific indexes can “undermine attempts to ‘benchmark’ best practice across all industries and, thus, allows ‘unethical’ companies to continue to exist”).

<sup>177</sup> *See id.* at 98-99.

<sup>178</sup> *See* Rangan et al., *supra* note 111, at 1 (“Cisco’s establishment of Cisco Academies to train networking personnel is often held up as an example of ‘shared value.’ Nestle and its development of Milk Districts in China, India and Pakistan is another oft-cited example . . .”).

because these corporations are “leaders in their respective businesses[,] . . . improvements they make to the societal infrastructure are also likely to benefit them disproportionately.”<sup>179</sup> Larger corporations have the resources and capacity needed to manage multiple CSR projects simultaneously, enabling them to pursue a broader CSR agenda than smaller corporations.<sup>180</sup> Larger corporations also have the ability to “run some projects over longer time-horizons or at lower returns than the industry average without significant risk to their competitive position.”<sup>181</sup> At the same time, it would not be “economically worthwhile . . . for a smaller player to do what the market leaders have done for fear of competitors taking a free-ride on their public investments.”<sup>182</sup>

These same principles hold true for companies wishing to adopt antiavoidance policies. When taken as a form of CSR, antiavoidance policies make more sense for companies in certain industries<sup>183</sup> and companies that are in the public eye.<sup>184</sup> For example, just as global financial services institutions may have the “vast resources and societal influence to launch significant initiatives aimed at financial inclusion and literacy,”<sup>185</sup> these institutions may be well suited to pioneer and publicize adherence to an antiavoidance doctrine. A corporation could assess the adoption of antiavoidance practices and policies in the same way it would any CSR activity – by determining whether taking the risks involved would “influence market and societal perceptions . . . in a way that will deliver value creation for the company.”<sup>186</sup> For example, Patagonia COO and CFO Rose Marcario stated that, while working for other companies, she “might have looked for ways to defer taxes in the Cayman Islands. Here [at Patagonia], we are proud to pay our fair share of taxes. It’s a different philosophy.”<sup>187</sup> Although Patagonia is a closely held corporation sheltered from derivative suits on the basis of fiduciary responsibility, such lawsuits would likely fail, because a decision to pay a “fair share” of taxes

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<sup>179</sup> *Id.* at 2.

<sup>180</sup> Martin, *supra* note 154, at 98-99.

<sup>181</sup> *Id.* at 99 (internal quotation marks omitted).

<sup>182</sup> Rangan et al., *supra* note 111, at 2.

<sup>183</sup> *See id.* at 5 (“[I]t’s neither practical nor logical for every company to engage in the same ‘brand’ of CSR.”).

<sup>184</sup> *See* Virginia Haufler, *Transactional Actors and Global Environmental Governance*, in *GOVERNANCE FOR THE ENVIRONMENT: NEW PERSPECTIVES* 132 (Magali A. Delmas & Oran R. Young eds., 2009) (discussing the particular vulnerabilities of high-profile companies to “name-and-shame” tactics in the context of environmental abuses).

<sup>185</sup> Rangan et al., *supra* note 111, at 5.

<sup>186</sup> Martin, *supra* note 154, at 99 (discussing corporate evaluation of adopting sustainability initiatives); *see also* Hanson Hu Li, *Finding Sustainable Profitability: The U.S. Financial Services Industry’s Pursuit of Corporate Social Responsibility*, 2 *CORP. GOVERNANCE L. REV.* 343, 367-71 (2006).

<sup>187</sup> Seth Stevenson, *America’s Most Unlikely Corporate Guru*, *WALL ST. J. MAG.*, May 2012, at 89.

would fall within the discretion afforded to corporate leaders under the business judgment rule.<sup>188</sup>

MNCs that create their own CSR strategies have the freedom to shape their commitments to maximize the consumer base and reputation-building potential of the CSR doctrine.<sup>189</sup> Since CSR strategies designed to complement existing corporate aims typically have greater success in this regard,<sup>190</sup> a corporation can shape its CSR publicity to connect the benefits of antiavoidance (for example, contributing to the infrastructure of a developing nation) with the corporation's other practices (for example, buying raw materials via fair trade).

#### CONCLUSION

For years, MNCs' use of tax havens and other tax avoidance practices have frustrated tax collection agencies, governments in both the developed and developing worlds, and shareholders. Despite numerous antiavoidance efforts by national governments, NGOs, and other international organizations, MNCs and their tax advisors have managed consistently to maneuver around new regulations and discover new loopholes to exploit. Although name-and-shame strategies provide a proactive, deterrence-oriented approach to combating tax avoidance that many governments have found appealing, these strategies have achieved only limited success.

Though academics rarely have discussed tax avoidance in the context of CSR, antiavoidance practices match many of the characteristics that embody other socially responsible activities. As the financial harms that tax avoidance causes exceed the financial benefits to corporations, MNCs should recognize the social irresponsibility of tax avoidance practices and approach taxpaying as another component of their CSR doctrines. If corporate boards, shareholders, and other stakeholders were to approach tax avoidance as a CSR issue, corporations would be less likely to avoid taxes, because paying the corporations' fair shares would be not only expected but demanded. Yet, unlike a naming and shaming approach, such a strategy mitigates the risks of driving tax advisors toward more aggressive tax avoidance strategies. Therefore, the incorporation of antiavoidance principles into CSR could provide incentives for self-regulation where external regulation proves unsuccessful.

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<sup>188</sup> See, e.g., *Shlensky v. Wrigley*, 237 N.E.2d 776, 781 (Ill. App. Ct. 1968).

<sup>189</sup> See *supra* notes 98-99 and accompanying text.

<sup>190</sup> See Sen & Bhattacharya, *supra* note 115, at 238.