

NOTE

**CRYSTALS AND MUD IN INTERNATIONAL TAXATION:
WHY THE PRINCIPAL PURPOSE TEST’S IMPACT WILL
NOT MEET EXPECTATIONS**

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This Note takes a fresh look at the Principal Purpose Test (“PPT”), which has been added to over 2,300 bilateral tax treaties since 2015 in an effort to fight tax avoidance. Under the PPT, countries may deny treaty benefits—such as lower tax rates on cross-border income—if it is reasonable for them to conclude that a taxpayer arranged a transaction principally to obtain those benefits.

Critics are skeptical of this rule. They argue that it is too vague and that it confers too much power on tax authorities. But this Note argues that those concerns may be overstated for two primary reasons. First, legal history shows that flexible standards like the PPT tend to become clearer over time, as courts and tax administrations develop more consistent—and more rule-like—interpretations. Second, although some countries might deploy the PPT aggressively, others can interpret it narrowly in an effort to continue attracting multinational businesses.

Whatever the PPT’s ultimate effect, the test will not dramatically reshape international taxation schemes. The PPT’s practical impact will not just be about the text of the test—it will be determined by how different countries choose to enforce it.

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INTRODUCTION

The early 2010s represent perhaps the only time period in which international tax policy regularly filled the pages of the world’s largest newspapers.¹ With the global economy still reeling from the 2008 financial crisis, national governments in the United States and Europe publicly questioned the tax bills paid by the world’s largest companies.²

¹ See, e.g., Jia Lynn Yang, *Post Analysis of Dow 30 Firms Shows Declining Tax Burden as a Share of Profits*, Wash. Post (Mar. 26, 2013), https://www.washingtonpost.com/business/economy/post-analysis-of-dow-30-firms-shows-declining-tax-burden-as-a-share-of-profits/2013/03/26/3dfe5132-7b9a-11e2-82e8-61a46c2cde3d_story.html.

² For a comprehensive discussion of these investigations and the ensuing public response, see Ruth Mason, *The Transformation of International Tax*, 114 Am. J. Int’l L. 353, 364–65 (2020).

The results of these investigations created a push for international tax changes by entities like the Organisation for Economic Co-operation and Development (“OECD”) and the Group of Twenty (“G20”).³

This Note discusses one component of these changes—a provision called the Principal Purpose Test (“PPT”). The PPT purports to target the abuse of tax treaties by allowing tax administrations to deny treaty benefits to a taxpayer if it is reasonable to conclude the taxpayer entered into a transaction principally to obtain those benefits.⁴ Commentators have described the power of the PPT in the hands of tax administrations in dramatic language, referencing the atomic bomb,⁵ the COVID-19 pandemic,⁶ and Sauron’s Ring of Power.⁷ To those commentators, the PPT promises to fundamentally alter the world of tax treaties for the worse. Their perspective is based upon the PPT’s language, which can be read as broader than most similarly constructed anti-abuse rules;⁸ its authors—a large collection of countries—having specifically encouraged a sweeping interpretation;⁹ and its status as a cornerstone of a global tax initiative aimed at transforming international tax.¹⁰ However, a contextualized approach to predicting the PPT’s effects suggests that commentators have overstated the test’s ultimate impact. This Note situates the PPT within the larger framework of tax competition and looks

³ See Yariv Brauner, *What the BEPS?*, 16 Fla. Tax Rev. 55, 56–57, 60 (2014) [hereinafter Brauner, *What the BEPS?*].

⁴ See OECD, *Model Tax Convention on Income and on Capital* art. 29(9) cmt. ¶¶ 176–177 (2017) [hereinafter OECD, 2017 Model], https://www.oecd.org/content/dam/oecd/en/publications/reports/2019/04/model-tax-convention-on-income-and-on-capital-2017-full-version_g1g972ee/g2g972ee-en.pdf [https://perma.cc/S82G-DH5A].

⁵ Lee A. Sheppard, *The PPT Through the Lens of the India-Mauritius Protocol*, 114 Tax Notes Int’l 1147, 1149 (2024); see, e.g., Eran Levy, *Is the Principal Purpose Test an “Atomic Bomb” and Should It Be Used Against Treaty Abuse?*, Mich. J. Int’l L. Blog (Dec. 2017), <https://www.mjilonline.org/eranlevy/> [https://perma.cc/HN4N-5S6N].

⁶ See Sheppard, *supra* note 5, at 1149.

⁷ See Craig Elliffe, *The Meaning of the Principal Purpose Test: One Ring to Bind Them All?*, 11 World Tax J. 47 (2019).

⁸ For example, the United States’ “business purpose” doctrine identifies and disallows transactions where a taxpayer was “motivated by no business purpose other than obtaining tax benefits.” Mixed tax and business purposes are permissible. *Austin v. Comm’r*, 113 T.C.M. (CCH) 69, 2017 WL 1437879, at *10–11 (Apr. 24, 2017) (first citing *Gregory v. Helvering*, 293 U.S. 465 (1935); and then citing *Rice’s Toyota World, Inc. v. Comm’r*, 752 F.2d 89, 91–92 (4th Cir. 1985)).

⁹ See OECD, 2017 Model, *supra* note 4.

¹⁰ See Mason, *supra* note 2, at 364–65 (arguing that the G20/OECD’s project changed international tax’s participants, agenda, institutions, norms, and legal forms).

to the literature on legal form to paint what may be a more realistic picture of the provision's ultimate impact.

This Note proceeds in five parts. Part I provides background on international tax policy, highlighting recent G20/OECD initiatives to change key elements of the international tax system. Part II introduces the PPT, its intended role in curbing treaty abuse, and the praise and criticism it has received. Part III argues that critics' concerns about legal uncertainties created by the PPT are overstated in terms of the rule's ultimate impact. The literature on legal form recognizes that standards become more rule-like as part of an everlasting oscillation between the two forms, and there is no reason to believe the PPT—currently a standard—is any different. Therefore, a focus on the PPT's initial stage may obscure a future time when the provision will be more certain and targeted in scope. Part IV considers the potential moderating impact of tax competition on the interpretation of the PPT. The literature on legal form allows us to understand that the PPT's open-ended design delegates discretion over its interpretation from the OECD to individual states, some of which wish to encourage defined and manageable corporate tax standards.¹¹ Thus, while the PPT's language might raise overbreadth concerns on first reading, an analysis sensitive to international taxation's competitive structure may indicate a more nuanced story to come. The Conclusion drives home this Note's central thesis: viewed in proper context, the PPT may ultimately not be the “atomic bomb” of international tax.¹²

I. BACKGROUND ON INTERNATIONAL TAX POLICY

A. From the Founding Until the BEPS Project: A System Aimed at Preventing Double Taxation

For over a century, states have worked together to address the problem of double taxation.¹³ Double taxation occurs when two states' domestic laws entitle them to tax the same item of income. This is undesirable

¹¹ See *infra* Part IV.

¹² See Sheppard, *supra* note 5, at 1148–49; Levy, *supra* note 5.

¹³ See Eduardo Baistrocchi, *The International Tax Regime and Global Power Shifts*, 40 *Va. Tax Rev.* 219, 233 (2021) (citing *Gramophone & Typewriter, Ltd. v. Stanley* [1908] 2 KB 89) (explaining that the international tax regime originated in response to the world's first profit allocation dispute in 1908).

because it stymies cross-border trade, investment, and migration.¹⁴ Double taxation frequently results from a business that resides in one state for tax purposes while earning income in another state.¹⁵ For instance, if Domestic Co., a U.S. resident company, earned income from producing and selling Widgets in the United Kingdom, the United States would tax that income, and so would the United Kingdom.¹⁶ But tax treaties allocate taxing rights among jurisdictions with competing claims on the same income with the aim of reducing double taxation.¹⁷

Since 1961, the OECD has occupied a central role in guiding international tax policy, as member states have come together to draft and update a model bilateral double taxation convention (“OECD Model”) and Commentaries thereupon.¹⁸ While the OECD Model does not directly govern the taxation of any cross-border business activity, states’ widespread adoption of treaties based on the Model makes it influential.¹⁹

¹⁴ See Ariane Pickering, *Why Negotiate Tax Treaties 7* (United Nations Dep’t of Econ. & Soc. Affs., Working Paper No. 1-N, 2013).

¹⁵ What I have described here is referred to as a “source-residence conflict,” which occurs when one state claims a right to tax an item of an enterprise’s income by virtue of being the enterprise’s state of residence, while another claims a right to tax the same income because it was earned due to the enterprise’s activities in that state. See Kevin Holmes, *International Tax Policy and Double Tax Treaties: An Introduction to Principles and Application* 37–38 (2d rev. ed. 2014). “Source-source conflict[s]” and “[r]esidence-residence conflict[s]” also exist and would serve equally well as a demonstration of the double taxation problem. See *id.* at 37.

¹⁶ See I.R.C. § 11; *Global Tax Guide to Doing Business in the United Kingdom*, Dentons, <https://www.dentons.com/en/services-and-solutions/global-tax-guide-to-doing-business-in/united-kingdom> [https://perma.cc/5M4P-LCAG] (last visited Jan. 3, 2026).

¹⁷ See Reuven S. Avi-Yonah, *Tax Competition, Tax Arbitrage and the International Tax Regime*, 61 *Bull. for Int’l Tax’n* 130, 131 (2007) [hereinafter *Avi-Yonah, Tax Competition*]. Today, the number of bilateral tax treaties stands at over 3,000. *UN Primer on Double Tax Treaties*, United Nations Dep’t of Econ. & Soc. Affs., <https://www.un.org/esa/ffd/capacity-development-tax/primer-dtt.html> [https://perma.cc/G6XN-BSPW] (last visited Jan. 3, 2026).

¹⁸ See OECD, *Draft Double Taxation Convention on Income and Capital (1963)*, https://www.oecd.org/content/dam/oecd/en/publications/reports/1963/10/draft-double-taxation-convention-on-income-and-capital-1963_g1g96efe/9789264073241-en.pdf [https://perma.cc/HR5G-9HFN]. Revisions have been made to the model periodically. See, e.g., OECD, *Model Tax Convention on Income and on Capital (2010)* [hereinafter *OECD, 2010 Model*], https://www.oecd.org/content/dam/oecd/en/publications/reports/2012/08/model-tax-convention-on-income-and-on-capital-2010-full-version_g1g1c5f3/9789264175181-en.pdf [https://perma.cc/5567-DD4D]. The OECD releases its model convention with Commentaries, a form of persuasive authority that offers the OECD’s interpretation of the model and examples. See Pasquale Pistone, *General Report*, in *The Impact of the OECD and UN Model Conventions on Bilateral Tax Treaties* 1, 4–6 (Michael Lang, Pasquale Pistone, Josef Schuch & Claus Staringer eds., 2012).

¹⁹ It is worth noting that the United Nations and United States each produce their own model treaties, but those models substantially align with the OECD Model on most issues. Compare

The OECD Model represents a substantial cooperative effort to direct the path of international tax policy.

Tax treaties, though they require cooperation to enact, govern a system that has historically been characterized by competition.²⁰ Countries enact international tax rules in domestic law independently of one another and with an eye toward objectives that can include attracting capital investment.²¹ This unilateral process produces differences in states' systems for taxing cross-border activity, some of which intentionally offer savings opportunities for large multinational entities ("MNEs").²² Tax competition—or the lowering of tax rates on foreigners' income to attract direct and/or portfolio investment²³—is a feature of international tax policy, not a bug. While some commentators have argued that tax competition hurts efforts to efficiently allocate resources²⁴ and tax MNEs,²⁵ it has persisted across time because competition is one of the

OECD, 2017 Model, *supra* note 4, arts. II–IV (defining "taxes covered" in Article II, various additional key terms in Article III, and "resident" in Article IV), with United Nations Dep't of Econ. & Soc. Affs., United Nations Model Double Taxation Convention Between Developed and Developing Countries arts. II–IV, U.N. Doc. ST/ESA/PAD/SER.E/213 (2017) (providing substantively identical definitions of "taxes covered," key terms, and "resident"), and U.S. Dep't of Treasury, United States Model Income Tax Convention arts. II–IV (2016), https://home.treasury.gov/system/files/131/Treaty-US-Model-2016_1.pdf [<https://perma.cc/AME7-32VJ>] (providing similar definitions of "taxes covered," key terms, and "resident"). About seventy-five percent of all tax treaty language is taken from the OECD Model, and about eighty-five percent of all cross-border business activity is governed by tax treaties. See Brauner, *What the BEPS?*, *supra* note 3, at 61–62; Yariv Brauner, *Treaties in the Aftermath of BEPS*, 41 *Brook. J. Int'l L.* 973, 977 (2016) [hereinafter Brauner, *Treaties in the Aftermath of BEPS*].

²⁰ Brauner, *Treaties in the Aftermath of BEPS*, *supra* note 19, at 979.

²¹ See Brauner, *What the BEPS?*, *supra* note 3, at 79; Adam H. Rosenzweig, *Why Are There Tax Havens?*, 52 *Wm. & Mary L. Rev.* 923, 940 (2010) (defining "tax competition" as the use of tax laws to artificially attract investment).

²² See Avi-Yonah, *Tax Competition*, *supra* note 17, at 137 (defining "tax arbitrage" as the exploitation of differences between states' tax systems to minimize tax liability).

²³ See Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 *Harv. L. Rev.* 1573, 1575–76 (2000) [hereinafter Avi-Yonah, *Globalization*].

²⁴ See *id.* at 1578 ("From an efficiency perspective, tax competition impairs the optimal global allocation of investment; when the effective tax rate abroad is lower than the effective rate at home, taxpayers will prefer international investments over domestic investments that, but for the tax regime, would provide more efficient returns.").

²⁵ See David C. Elkins, *The Merits of Tax Competition in a Globalized Economy*, 91 *Ind. L.J.* 905, 936 (2016).

few tools available for use by small, natural resource-poor countries in leveling the global economic playing field.²⁶

As suggested above, states engaging in tax competition are often designing a tax system that can be used to MNEs' advantage.²⁷ Some mismatches create space for companies to structure their affairs with the specific intention to obtain a treaty benefit.²⁸ And the OECD Model historically has not comprehensively addressed such efforts, focusing instead on preventing double taxation and leaving much of that responsibility to states' anti-abuse rules and judicial doctrines.²⁹

B. The BEPS Project

The 2008 global financial crisis and several large-scale corporate tax disputes invigorated public interest in revising international tax rules in the early 2010s.³⁰ The G20 charged the OECD with developing a meaningful response.³¹ The OECD's chosen course of action has come to be known as the Base Erosion and Profit Shifting ("BEPS") project.³² BEPS refers to structures and transactions whereby MNEs shift profits to no- or low-tax jurisdictions in amounts that are disproportionate to the economic activity occurring in those jurisdictions.³³ The BEPS project commenced in 2013³⁴ and put forth a final, fifteen-item action plan two

²⁶ See Zaif Hassan Fazal, *Tax Competition: A Blessing in Disguise for Small Countries*, 22 *J. Austl. Tax'n* 60, 61 (2020).

²⁷ See, e.g., *infra* notes 114–16 and accompanying text.

²⁸ See David G. Duff, *Tax Treaty Abuse and the Principal Purpose Test—Part 2*, 66 *Can. Tax J.* 947, 948–49 (2018).

²⁹ See David G. Duff, *Tax Treaty Abuse and the Principal Purpose Test—Part 1*, 66 *Can. Tax J.* 619, 623–27 (2018). Certain treaties did include specific anti-abuse rules that governed the taxation of certain transactions, such as rules designed to prevent conduit arrangements and purpose tests that restricted access to interest and royalty taxation benefits. *Id.* at 661–63, 668.

³⁰ See Brauner, *What the BEPS?*, *supra* note 3, at 56–58, 60.

³¹ See 2012 G20 Summit, G20 Leaders Declaration ¶ 48 (June 18–19, 2012), https://g7g20-documents.org/fileadmin/G7G20_documents/2012/G20/Mexico/Leaders/1%20Leaders%20Language/G20%20Leaders%20Declaration_19062012.pdf [<https://perma.cc/F5WG-U5P9>]; Base Erosion and Profit Shifting (BEPS), OECD, <https://www.oecd.org/en/topics/policy-issue/s/base-erosion-and-profit-shifting-beps.html> [<https://perma.cc/4CDF-NC9F>] (last visited Jan. 3, 2026).

³² Base Erosion and Profit Shifting (BEPS), *supra* note 31.

³³ *Id.*

³⁴ OECD, *Addressing Base Erosion and Profit Shifting 5–7* (2013), https://www.oecd.org/content/dam/oecd/en/publications/reports/2013/02/addressing-base-erosion-and-profit-shifting_g1g2a9bc/9789264192744-en.pdf [<https://perma.cc/G69R-ZUAA>] (introducing the BEPS project).

years later.³⁵ The OECD's plan centered around collective actions by states in their individual capacities.³⁶ This design reflected the G20 and OECD members' view that tax competition-fueled tax avoidance should be addressed with global coordination.³⁷

The BEPS action items, which purport to improve the coherence of international tax rules,³⁸ are implemented through the Multilateral Instrument ("the MLI"), which was designed to provide states a menu of options for use in amending their bilateral tax treaties.³⁹ States can adopt or reject most of the MLI's provisions on a treaty-by-treaty basis, but provisions accepted into the MLI unanimously—known as "BEPS minimum standards"—are mandatory for all signatories.⁴⁰ Adding the PPT into double tax conventions satisfies one such minimum standard.⁴¹

³⁵ See, e.g., OECD, *Addressing the Tax Challenges of the Digital Economy: Action 1—2015 Final Report 3* (2015), https://www.oecd.org/content/dam/oecd/en/publications/reports/2015/10/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report_g1g58cdd/9789264241046-en.pdf [<https://perma.cc/EA27-N5NY>].

³⁶ For example, to satisfy the treaty abuse minimum standard, states must adopt one of the available options into all of their bilateral tax agreements. See OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances: Action 6—2015 Final Report 10, 14, 19* (2015) [hereinafter OECD, *Action 6*], https://www.oecd.org/content/dam/oecd/en/publications/reports/2015/10/preventing-the-granting-of-treaty-benefits-in-inappropriate-circumstances-action-6-2015-final-report_g1g5906e/9789264241695-en.pdf [<https://perma.cc/C48N-NQ2X>]. The mechanism is coordinated, but it is implemented by the states individually.

³⁷ See Brauner, *Treaties in the Aftermath of BEPS*, *supra* note 19, at 991.

³⁸ See, e.g., OECD, *Neutralising the Effects of Hybrid Mismatch Arrangements: Action 2—2015 Final Report 11* (2015), https://www.oecd.org/content/dam/oecd/en/publications/reports/2015/10/neutralising-the-effects-of-hybrid-mismatch-arrangements-action-2-2015-final-report_g1g58cdf/9789264241138-en.pdf [<https://perma.cc/J4U5-T87E>] (combatting MNEs' use of arrangements that are treated differently by the states involved to minimize tax liability).

³⁹ The MLI is not a self-standing treaty or amendment protocol, but rather a tool to facilitate the incorporation of BEPS action items into bilateral treaties. Essentially, the MLI allows states to independently determine how they would like to alter each of their treaties and updates an agreement automatically if both states agree on a particular provision. See *What Is the OECD Multilateral Instrument?*, *Bloomberg Tax* (Feb. 27, 2025), <https://pro.bloombergtax.com/insights/international-tax/oecd-beps-and-the-multilateral-instrument/> [<https://perma.cc/MXG4-3LRR>].

⁴⁰ See *id.* The MLI currently has 105 signatories, meaning that BEPS minimum standards are widely adopted. See *Signatories and Parties to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting*, OECD, http://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/beps-mli-signatories-and-parties.pdf/_jcr_content/renditions/original/beps-mli-signatories-and-parties.pdf [<https://perma.cc/9DBQ-N4NX>] (last updated June 18, 2025).

⁴¹ See OECD, *Action 6*, *supra* note 36, at 10.

II. AN INTRODUCTION TO THE PRINCIPAL PURPOSE TEST: CONTENTS AND CRITICISMS

One of the BEPS minimum standards addresses the granting of treaty benefits in what the BEPS project views as inappropriate circumstances⁴² by targeting two forms of treaty-related tax planning: “treaty shopping”⁴³ and “rule shopping.”⁴⁴ States may implement the BEPS minimum standard against treaty abuse by including in their treaties (1) the PPT alone; (2) the PPT and a simplified or detailed limitation on benefits (“LOB”) rule;⁴⁵ or (3) a detailed LOB rule together with a mechanism to restrict conduit arrangements not otherwise dealt with in tax treaties.⁴⁶

States have overwhelmingly adopted the PPT alone to fulfill the minimum standard,⁴⁷ rendering it “the king” of the treaty benefits portion

⁴² *Id.* at 9–10.

⁴³ Treaty shopping occurs when a taxpayer who is not a resident of either contracting state arranges their affairs to obtain benefits intended for contracting state residents. See *id.* ¶ 17, at 17. If State *A* and State *B* have a bilateral tax agreement, a State *C* resident would engage in prototypical treaty shopping if it incorporated a paper-only subsidiary in State *B* to invest in the State *A* market with the benefit of the treaty’s reduced tax rates. See Frith Crandall, Comment, *The Termination of the United States-Netherlands Antilles Tax Treaty: What Were the Costs of Ending Treaty Shopping?*, 9 *Nw. J. Int’l L. & Bus.* 355, 363 (1988) (offering an illustration of treaty shopping).

⁴⁴ Rule shopping occurs when a contracting state resident enters into a transaction for the purpose of obtaining beneficial treatment under specific treaty provisions. See Błażej Kuźniacki, *The Principal Purpose Test (PPT) in BEPS Action 6 and the MLI: Exploring Challenges Arising from Its Legal Implementation and Practical Application*, 10 *World Tax J.* 233, 236 (2018). If State *A* and State *B* have a bilateral tax agreement that taxes cross-border dividend payments at fifteen percent and cross-border interest payments at zero percent, a resident of State *B* would engage in rule shopping if it structured its investment in a State *A* entity as debt specifically to benefit from the zero percent rate. See Luc De Broe & Joris Luts, *BEPS Action 6: Tax Treaty Abuse*, 43 *Intertax* 122, 125 (2015) (defining rule shopping).

⁴⁵ LOB rules are comprised of a series of objective tests that determine whether or not a contracting state resident is qualified to receive treaty benefits. See Patricia A. Brown, *Policy Forum: What Makes a Dutch Company Dutch? The Evolution of US Limitation-on-Benefits Provisions*, 62 *Can. Tax J.* 741, 743–44 (2014).

⁴⁶ OECD, *Action 6*, *supra* note 36, ¶¶ 19, 22, at 18–19. The treaty abuse minimum standard also encourages MLI signatories to explicitly state their common intention “to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements” in their tax treaty preambles. *Id.* ¶ 22, at 19.

⁴⁷ Every signatory to the MLI adopted the PPT as part of its treaty abuse minimum standard application plan. Kuźniacki, *supra* note 44, at 238. As of 2022, roughly 75 of 2,385 treaties compliant with the minimum standard supplemented the PPT with a detailed or simplified LOB. OECD, *Prevention of Tax Treaty Abuse—Fifth Peer Review Report on Treaty Shopping* ¶¶ 39, 41, at 17–18 (2023) [hereinafter OECD, *Peer Review Report*]. This dominance is unsurprising, as the MLI structurally favors the PPT. For one, the PPT is the

of BEPS.⁴⁸ The PPT, currently represented in Article 29(9) of the 2017 OECD Model, reads as follows:

Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.⁴⁹

As many have lamented, the PPT is incredibly open-ended.⁵⁰ Among the questions it raises are how stringent a burden of proof “reasonable to conclude” poses in practice, what it takes for obtaining treaty benefits to be among an arrangement’s “principal purposes,” and what it means for granting treaty benefits to “be in accordance with the object and purpose of the relevant treaty provisions.” The PPT does not itself define these elements, and, unfortunately, the provision’s accompanying Commentary does not thoroughly cover them either.⁵¹

This lack of specificity has led some commentators to believe the PPT permits an expansive interpretation—a possibility that has drawn critical attention. These commentators have strongly worded criticisms of the PPT, calling the provision “the COVID virus of international taxation”⁵² and “a nuclear weapon in the hands of [tax authorities],”⁵³ and comparing

only rule that can satisfy the action item without supplementation. See Kuźniacki, *supra* note 44, at 238. Additionally, the PPT operates as a default rule when parties to a treaty have adopted different methods of satisfying the treaty abuse action item. See *id.*

⁴⁸ See Kuźniacki, *supra* note 44, at 238.

⁴⁹ OECD, 2017 Model, *supra* note 4, art. 29(9).

⁵⁰ See, e.g., Guilherme Neves de Paiva Navarro, A Critical Analysis of the Principal Purpose Test Rule’s Core Features and Its Practical Applicability, 7 *Rev. Direito Tributário Internacional Atual* 161, 168 (2020) (Braz.).

⁵¹ See Khrystyna Franchuk, The Assistance of Examples of the Application of the Principal Purpose Test Listed in the Commentary on Article 29(9) of the OECD Model in Establishing the Legal Certainty of the Test, 5 *Int’l Tax Stud.*, no. 11, 2022, at 2, 2 (finding that the OECD’s examples were not sufficiently clear or helpful to remedy the provision’s legal certainty problem).

⁵² Sheppard, *supra* note 5, at 1149.

⁵³ See *id.* at 1148. These statements, which are ultimately traceable to the same person, are rhetorically pungent examples of a greater concern with the PPT’s broad and uncertain mandate. See, e.g., Levy, *supra* note 5 (noting a practitioner’s expressed concern regarding the PPT’s overbreadth).

it to Sauron's Ring of Power.⁵⁴ Robert Stack, the U.S. negotiator for BEPS, who criticized the breadth of the PPT in rejecting it for the United States, noted that a company could run afoul of the PPT merely by acting on the advice of its internal tax advisors when structuring its affairs.⁵⁵ Scholars have called for a broad interpretation of the PPT to minimize treaty abuse,⁵⁶ as has the OECD,⁵⁷ deepening concerns among businesses and U.S. policymakers (who may see it as a tool targeted disproportionately at U.S. companies).⁵⁸

The thesis of this Note is that certain commentators may have overestimated the PPT's likely impact because (1) tax competition is still at play, and (2) the overall rules-and-standards paradigm suggests a more nuanced path forward. Overzealous application of the PPT is a valid cause for concern, but the system-wide impact of such regulatory overstepping will likely be less than certain commentators have feared.

III. CRYSTALLIZING THE PPT'S MUDDY STANDARD IN UNILATERAL AND MULTILATERAL VENUES

To fully understand the PPT requires us to consider literature on legal form, which focuses on the different ways a rulemaking institution can design a provision in pursuit of the same objective or underlying principle.⁵⁹ To that end, a few words of background on legal form scholarship are appropriate. The choices of legal form are myriad and lie

⁵⁴ See Elliffe, *supra* note 7, at 47 (discussing the possibility and importance of a unified international interpretation of the PPT).

⁵⁵ NYU School of Law, 22nd Annual David R. Tillinghast Lecture on International Taxation: Robert B. Stack, at 26:12 (YouTube, Sep. 22, 2017), <https://www.youtube.com/watch?v=zcdeiTL-gFE> [<https://perma.cc/RR7G-FGN8>] (expressing concern that the PPT does not make it sufficiently clear that merely receiving input on the location of a subsidiary from a company's tax team would not violate the standard).

⁵⁶ See, e.g., Kuźniacki, *supra* note 44, at 280 (calling for states to apply the PPT "in the broadest manner").

⁵⁷ See OECD, 2017 Model, *supra* note 4.

⁵⁸ See Letter from Orrin Hatch, Chair, Senate Fin. Comm. & Paul Ryan, Chair, House Ways & Means Comm., to Jacob Lew, Sec'y, U.S. Dep't of Treasury (June 9, 2015), *in* Press Release, U.S. House Comm. on Ways & Means, Hatch, Ryan Call on Treasury to Engage Congress on OECD International Tax Project (June 9, 2015), <https://waysandmeans.house.gov/2015/06/09/hatch-ryan-call-on-treasury-to-engage-congress-on-oecd-international-tax-project/> [<https://perma.cc/8BRG-RCN5>] (highlighting the impact of BEPS on U.S. multinationals in a letter written by congressional tax leadership to the Treasury Secretary).

⁵⁹ See Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 *Duke L.J.* 557, 557 (1992) (indicating that rulemaking institutions face a choice whether to promulgate a legal command as a rule or a standard).

along a continuum of legal precision,⁶⁰ but this Note follows the literature's norm of speaking in terms of "rules" and "standards," forms which lie at the continuum's poles.⁶¹ Structuring a legal command as a rule, standard, or any other point along the legal precision continuum comes with a balance between competing virtues, such as certainty and flexibility, that has substantive effects.⁶²

The literature on legal form, which is steeped in the law and economics tradition,⁶³ provides both static and dynamic insights. This Part engages in a dynamic analysis of the PPT, and Part IV explains how the literature's static considerations interact with tax competition to impact interpretation of the PPT.

* * *

When a new development in a field comes with as many unanswered questions as the PPT does, the natural impulse is to say, "Let's take things one step at a time," and to try to understand the here and now before looking forward. However, looking to dynamic considerations from the literature on legal form provides valuable information by placing concerns about and commendations of the PPT in a broader context. The PPT, in all its imprecision, does not represent an end state of tax treaty law. This Part discusses how we can expect tax treaty anti-abuse provisions to shift from standard to rule and back again over the course of time now that comprehensive treatment of the issue is a compulsory feature of bilateral tax treaties.

*A. The Oscillating Path of Legal Form:
From Standard to Rule and Back Again*

An important observation from the literature on legal form is that areas of law oscillate along the continuum of legal precision, rather than

⁶⁰ See James G. Wilson, *Surveying the Forms of Doctrine on the Bright Line-Balancing Test Continuum*, 27 *Ariz. St. L.J.* 773, 773 (1995).

⁶¹ Isaac Ehrlich & Richard A. Posner, *An Economic Analysis of Legal Rulemaking*, 3 *J. Legal Stud.* 257, 258 (1974).

⁶² See *id.*

⁶³ Though much of the literature on legal form has consisted of economic analyses targeted at maximizing the efficiency of the legal system, scholars from the Critical Legal Studies movement have also contributed works questioning whether the rigidity of rules reinforces unfair power dynamics. See, e.g., Duncan Kennedy, *Form and Substance in Private Law Adjudication*, 89 *Harv. L. Rev.* 1685 (1976).

becoming increasingly rule- or standard-like, or settling at some equilibrium point in between, as time progresses.⁶⁴ This occurs in part because each point along the continuum represents a particular trade-off among different costs,⁶⁵ and the relative magnitude of these costs changes as facts change and the law develops.⁶⁶ Additionally, both rules and standards attract disputes that demonstrate their weaknesses—thus leading decision-makers to alter a command’s legal form and perpetuate the oscillation. This Section demonstrates this oscillation and explains its causes so that the next may consider its consequences in the context of tax treaty anti-abuse provisions.

To ground our discussion of the literature on legal form, consider the following two versions of a speeding law. If a state legislature wants to define the offense of “speeding,” it might prohibit “traveling at any speed greater than seventy miles per hour.” However, the legislature could instead choose to prohibit “traveling at an unreasonable speed.” The “seventy miles per hour” rule, like all effectively drafted rules, provides perfect certainty to an individual seeking to determine the legality of a

⁶⁴ See Jason Scott Johnston, *Uncertainty, Chaos, and the Torts Process: An Economic Analysis of Legal Form*, 76 *Corn. L. Rev.* 341, 365–66 (1991) (citing Ehrlich & Posner, *supra* note 61, at 266) (rebutting Professor Ehrlich and Judge Posner’s account of an optimal level of legal precision by illustrating that intervening events demonstrated oscillation back to standards in areas they used as examples of the inevitable trend towards increased precision). While Professor Johnston persuasively responded to this argument, it is not inherently implausible. Take into consideration the observations that rules are comparatively expensive to promulgate up front (because they require precise specification of a law’s prohibitions), but comparatively inexpensive to comply with and adjudicate (because the law’s content is fixed *ex ante*). See Wilson, *supra* note 60, at 790 (noting that an exception with unspecified content allows an otherwise rigid rule to better account for the unknown and unforeseeable); Kaplow, *supra* note 59, at 569–70 (explaining that the costs of legal advice and adjudication are greater under a standard). This cost structure would suggest that areas of law would tend to contain many standards at the outset and eventually become more rule-like over time. See Ehrlich & Posner, *supra* note 61, at 266, 273 (arguing that we should see more precise rules governing an area of law as we become better acquainted with the relevant legal problem).

⁶⁵ See, e.g., Frederick Schauer, *Playing by the Rules: A Philosophical Examination of Rule-Based Decision-Making in Law and in Life* 140–42 (1991) (explaining that rules increase individuals’ ability to rely on a legal command when planning their affairs while decreasing the legal command’s ability to adapt to new circumstances).

⁶⁶ See, e.g., Kaplow, *supra* note 59, at 621 (explaining that rules are preferable to standards when the conduct to be governed occurs frequently because the costs of adjudication under a standard outweigh the savings in promulgation). It is easy to imagine a situation in which a law governs conduct that originally occurs quite infrequently but eventually becomes much more common (e.g., crypto-asset transactions). In such a situation, we should expect a rule to replace a standard because the relative costs of adjudication and promulgation have shifted over time.

future course of action because its content is defined *ex ante*.⁶⁷ Meanwhile, the “unreasonable speed” standard would require the same individual to guess at the outcome of an *ex post* judgment—i.e., “Will a judge think my speed was reasonable?”⁶⁸ The choice between rule and standard is fundamentally a decision between defining the content of a legal command *ex ante* or *ex post*.⁶⁹

Now imagine that a legislature chooses to enact the unreasonable speed standard. As discussed above, even a driver with knowledge of this legal command must guess at the outcome of an *ex post* decision when attempting to determine the legality of their proposed driving speed. However, examinations of areas of law ranging from property⁷⁰ to tort⁷¹ to antitrust⁷² to bankruptcy⁷³ illustrate that this *ex ante* uncertainty does not persist in perpetuity. Here is why.

First, such an open-ended standard in a common law system remains completely unspecified only until the first case makes its way before a judge. Even if the forum in which a dispute is adjudicated represents only persuasive authority,⁷⁴ the existence of a ruling on even just one set of

⁶⁷ The certainty a rule provides is not necessarily perfect because an *ex post* decision-maker (e.g., a judge) may be liable to fashion an equity-based exception or similar adjustment to a rule when faced with unfriendly facts. Such a development would represent an evolution in a legal command’s form, which this Part discusses.

⁶⁸ The theory behind a reasonability standard is that an appropriately diligent individual would be able to correctly judge the legality of their own actions; however, scholars recognize that maxim’s unrealistic assumptions. See, e.g., Max C. Warshawsky, *Mr. Reasonable: The Man, the Myth, the Legend*, *Iowa J. Gender Race & Just. News* (Dec. 3, 2023), <https://jgrj.law.uiowa.edu/news/2023/12/mr-reasonable-man-myth-legend> [<https://perma.cc/4J9R-TR8L>] (noting the subjectivity inherent in the reasonable person standard, the risks that judicial factfinders view themselves as the North Star for reasonability, and the need for a standard which is sensitive to differences in how different people experience the world).

⁶⁹ See Baistrocchi, *supra* note 13, at 225.

⁷⁰ See Carol M. Rose, *Crystals and Mud in Property Law*, 40 *Stan. L. Rev.* 577, 609 (1988).

⁷¹ See Johnston, *supra* note 64, at 392–93.

⁷² See Daniel A. Crane, *Formalism and Functionalism in the Antitrust Treatment of Loyalty Rebates: A Comparative Perspective*, 81 *Antitrust L.J.* 209, 220 (2016) (“It is only a slight exaggeration to say that for every action toward functionalist standards, there is an equal and opposite reaction toward formal rules. This is arguably the correct understanding of U.S. antitrust history since the rise of the Chicago School in the 1970s.”).

⁷³ See Ted Janger, *Crystals and Mud in Bankruptcy Law: Judicial Competence and Statutory Design*, 43 *Ariz. L. Rev.* 559, 614–15 (2001).

⁷⁴ Common law jurisdictions, unlike their civil law counterparts, incorporate a principle of *stare decisis*, which gives precedents near-binding effect. See John Hanna, *The Role of Precedent in Judicial Decision*, 2 *Vill. L. Rev.* 367, 367–68 (1957) (describing *stare decisis* in the context of the U.S. and U.K. legal systems). This is not to say that precedent is valueless in civil law systems. However, it only creates persuasive authority. See *id.* at 375–76.

facts would slide the unreasonable speed standard ever so slightly toward the rule side of the continuum of legal precision.⁷⁵ And, of course, as the number of fact patterns for which guidance exists increases, so too does the degree of legal precision.⁷⁶

Additionally, and regardless of whether a legal command inhabits a common law or civil law system, the cycle of legal form operates through case selection.⁷⁷ Standards and rules each attract a set of cases that expose their weaknesses. Standards, for their part, attract a set of cases reflecting typical behavior.⁷⁸ Essentially, a case where the conduct in question is extreme (e.g., driving 110 miles per hour on an icy freeway) is unlikely to make its way before an adjudicative body. The conduct so clearly falls within the prohibition (e.g., the definition of “unreasonable” speed) that we can expect the case to be culled at some early stage of the process (adherence, settlement, admission of guilt, etc.).⁷⁹ However, the close questions are ones where the conduct lies at the edge of the prohibition. These cases will be litigated again and again, and eventually judges will see a rule within the balancing test and interpose it in the interest of judicial economy.⁸⁰

⁷⁵ See Kaplow, *supra* note 59, at 611 (“To the extent laws are promulgated as standards, predictability will be enhanced by precedent to the extent precedent transforms standards into rules.”).

⁷⁶ To prove this, imagine that a legislature has adopted an unreasonable-rate-of-speed rule. Say that the state’s courts have also made two decisions on that rule—one finding that eighty miles per hour was an unreasonable rate of speed, and the other finding that seventy miles per hour was not an unreasonable rate of speed in the same conditions. This provides the driver with some information, but a third data point declaring seventy-three miles per hour an unreasonable rate of speed on the same road would provide more.

⁷⁷ Johnston, *supra* note 64, at 360–62.

⁷⁸ *Id.* at 360.

⁷⁹ *Id.*

⁸⁰ *Id.* at 361. The history of antitrust law provides an example of this, as *per se* rules have sprung out of the field’s general “rule of reason”—a standard—as specific content has drawn similar results in repeated litigation. See, e.g., *Int’l Salt Co. v. United States*, 332 U.S. 392, 392–96 (1947) (establishing a *per se* rule prohibiting “tying” arrangements). Tying arrangements, in which a seller conditions the purchase of one product on the purchase of another, provide an especially illuminating example of this trend because they are now not deemed *per se* illegal in all contexts. See *Jefferson Par. Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 27–28 (1984) (finding that tying arrangements were only *per se* illegal under certain conditions); *United States v. Microsoft Corp.*, 253 F.3d 34, 84 (D.C. Cir. 2001) (*per curiam*) (determining that platform software ties should be adjudicated under the rule of reason). The fact that tying provisions returned to a pattern of case-by-case analysis after being treated under a *per se* rule indicates that they lie close to the Sherman Antitrust Act’s boundary.

Finally, rules are substantially more costly than standards to promulgate because the lawmaking institution must specify all relevant considerations *ex ante*,⁸¹ and accordingly it must come to a consensus about the law's content at the drafting table. We may therefore expect to see a rule, such as a numerical speed limit, arise in place of a standard when the conduct governed by a rule becomes sufficiently frequent to justify the extra expenditure or the institutional costs of reaching consensus decrease (e.g., the interests of different stakeholders come into closer alignment).⁸²

Just as standards push the law toward rules, rules push the law toward standards. Litigants bring cases that demonstrate a rule's unfairness or inefficiency (e.g., a driver ticketed for traveling seventy-five miles per hour as they sped up to avoid hitting an animal).⁸³ Judges who repeatedly see cases in which a rule appears inapt (either because it imposes harsh consequences on undeserving parties⁸⁴ or deters socially beneficial activity⁸⁵) eventually soften its edges by creating standard-like exceptions⁸⁶ or wholly replace it with an open-textured standard.⁸⁷ Thus, the cycle continues.

⁸¹ See Kaplow, *supra* note 59, at 591, 593.

⁸² These two sets of circumstances reduce the costs of rule promulgation by reducing gridlock, either by eliminating the need to compromise or by making compromise easier to achieve. See Jia Xin Luo, *Gridlock from Polarization: The Current State of the United States Government*, Democratic Erosion Consortium (Nov. 22, 2023), <https://democratic-erosion.org/2023/11/22/gridlock-from-polarization-the-current-state-of-the-united-states-government/> [<https://perma.cc/X78R-4FRZ>] (explaining that “[g]ridlock occurs when the two main parties have such differing ideals to the point that they are unwilling to compromise”).

⁸³ See Johnston, *supra* note 64, at 361.

⁸⁴ For example, Professor Carol Rose highlights the phenomenon of forfeiture in property law as a driver toward standards. She argues it has this effect because decision-makers desire to protect uninformed parties from being taken advantage of by bad actors. See Rose, *supra* note 70, at 603 (“[Judges] lean ever so slightly to mud, in order to save the fools from forfeiture at the hands of scoundrels.”).

⁸⁵ See Johnston, *supra* note 64, at 361 (explaining that plaintiffs will frequently argue that compliance with a rule should not create a safe harbor in situations where the defendant should have overcomplied).

⁸⁶ See Rose, *supra* note 70, at 597 (“[T]he scenario of disproportionate loss by some party . . . seems to drive us to muddy up crystal rules with . . . exceptions . . .”).

⁸⁷ See, for example, the discussion of tying arrangements' return to rule of reason analysis in antitrust law. See *supra* note 80.

B. Certainty on the Horizon for the PPT

Understanding the oscillation between rules and standards allows better understanding of the PPT. Specifically, the winding path of legal form shows us that concerns about the PPT's vagueness will be at least partially mitigated over the course of time. This process will not necessarily narrow the broad readings of the PPT that some states are likely to take;⁸⁸ however, it will increase legal precision, and therefore taxpayer certainty.

1. Certainty in the Near Term on a State-by-State Basis

The unilateral nature of tax treaty enforcement⁸⁹ means that, except to the limited extent that some states treat PPT cases in other jurisdictions as persuasive authority or adopt an international autonomous interpretation of the provision,⁹⁰ legal precision will initially enter the system on a state-by-state basis. This may create a landscape of differing levels of certainty⁹¹—and thus distort investment decisions⁹²—as the first disputes are resolved, but that should not distract from the overarching notion that the PPT will only remain startlingly imprecise for a limited period of time. As with any other standard, the operation of precedent and case selection will push it closer to a rule.

The facts that produce relatively certain outcomes may vary from state to state as the PPT becomes more precise. But eventually, we will have crucial information in relevant jurisdictions about matters such as (1) which sets of facts and circumstances establish that obtaining a treaty benefit was or was not a principal purpose of an arrangement or transaction, (2) what the objects and purposes of various treaty provisions are considered to be, and (3) what sort of evidentiary bar the “reasonable to conclude” standard creates. Therefore, the concerns about the PPT's

⁸⁸ See *infra* notes 131–34 and accompanying text. Just as the choice of legal form has no bearing on the complexity of a provision, see Kaplow, *supra* note 59, at 596, neither does it have a systematic relationship to the breadth of conduct covered.

⁸⁹ See *infra* notes 110–12 and accompanying text.

⁹⁰ For a detailed argument in favor of this approach, see Elliffe, *supra* note 7, at 51, 65, 75.

⁹¹ Two variables that may impact a state's position on this spectrum of certainty are the level of authority it prescribes to past tax decisions and the frequency with which it is faced with PPT disputes. See *supra* notes 74, 76.

⁹² This distortion occurs because “uncertainty tends to discourage business investment.” Jeffrey Trossman, *Tax Certainty: Recent Trends and Suggested Reforms*, Persps. on Tax L. & Pol'y (Can. Tax Found., Toro., Ont.), Mar. 2020, <https://www.ctf.ca/EN/EN/Newsletters/Perspectives/2020/1/200101.aspx> [<https://perma.cc/3ZER-24RJ>].

current black-box status and praise for its remarkable flexibility should both be considered transitory.

2. Certainty in the Long Term on a Regime-Wide Basis

When considering the PPT's long-term future, it is important to note that BEPS mandated continued inspection of the treaty abuse problem at the OECD level.⁹³ Because preventing treaty abuse will remain on the OECD's agenda, we can expect further developments of the soft law (i.e., the OECD Model) "governing" the field to emerge in response to implementing states' experiences and evolving factual circumstances. For example, if states see a pattern of diverging outcomes about whether a common set of facts violates the PPT and a sufficient number of states would prefer a certain result, we can expect to see member states engraft a rule-like safe harbor or sure shipwreck onto the text or Commentary of Article 29.⁹⁴ Thus, to the extent the OECD Model and its accompanying Commentary represent persuasive authority for states interpreting treaty provisions molded in their image,⁹⁵ updates to the OECD Model or Commentary will increase certainty on a global scale.

However, OECD-wide oscillation will likely require a longer period of time to occur. The first two reasons for this are quite obvious: (1) the OECD will not experience certainty increases from the creation of precedent because it does not have a judicial function,⁹⁶ and (2) the OECD Model is only updated every several years, while national tax systems develop continually.⁹⁷ Additionally, the costs of rule promulgation by the OECD are greater than those of any individual country because amending the OECD Model or its Commentaries requires unanimity among thirty-eight member states,⁹⁸ which have widely divergent interests.⁹⁹ This

⁹³ See OECD, Peer Review Report, *supra* note 47, at 3.

⁹⁴ See generally Susan C. Morse, Safe Harbors, Sure Shipwrecks, 49 U.C. Davis L. Rev. 1385, 1401–02 (2016) (discussing how including a specification of conduct that will definitely violate or not violate a standard increases legal certainty and affects parties' behavior).

⁹⁵ See Michael Lang & Florian Brugger, The Role of the OECD Commentary in Tax Treaty Interpretation, 23 Austl. Tax F. 95, 98–100 (2008) (explaining that Articles 31 and 32 of the Vienna Convention on the Law of Treaties provide that the OECD Model and Commentaries serve as "valuable evidence of the intentions of the negotiators" to a bilateral tax agreement based on the OECD Model).

⁹⁶ See *infra* note 111 and accompanying text.

⁹⁷ See OECD, 2010 Model, *supra* note 18, intro. ¶¶ 8–11.1.

⁹⁸ See OECD, 2017 Model, *supra* note 4, intro. ¶¶ 31, 35.

⁹⁹ For a discussion of one important way these interests diverge, see *infra* Part IV. It is important to note that the costs of OECD rule promulgation vary across time. In one of the

consensus-building requires substantial negotiation, which will slow the tides of change.

The introduction of certainty at the OECD level will likely lag behind state-level oscillation, but it should not be ignored because providing any sort of system-wide rule will greatly reduce the cost of complying with the PPT. Put simply, it will be much easier for MNEs to structure their affairs to comply with the PPT when they can look to the OECD Model or Commentaries for generalizable guidance rather than searching the annals of a particular state's domestic law for a case on point.

* * *

While there presently exists a substantial lack of clarity as to which arrangements and transactions will result in a denial of treaty benefits under the PPT, the dearth of legal precision precipitating that concern will become at least somewhat less severe over time. The literature on legal form recognizes that standards tend to eventually become more rule-like as part of an everlasting oscillation between the two forms, and there is no reason to believe the PPT is any different. MNEs might have to wait a while for the introduction of rules at the OECD level, but rules will be created on a state-by-state basis in the interim.

IV. ASSIGNING DISCRETION OVER PPT INTERPRETATION TO COMPETING STATES: A STATIC ANALYSIS

With Part III having demonstrated that the PPT will likely become more certain over time, this Part analyzes how the imprecise standard that presently exists will be implemented. First, Section IV.A explains that as a standard, the PPT assigns discretion over interpretation to ex post decision-makers. Then, Section IV.B clarifies that in the context of an

few articles to date that extensively discusses the oscillation of legal form in the context of international taxation, Professor Eduardo Baistrocchi presents a compelling case that the costs of promulgating a rule among OECD member states are particularly high at present. See Baistrocchi, *supra* note 13, at 249–50. According to his theory, international tax policy tends toward rules when a hegemon has sufficient power to coerce all other states into adopting precise rules that further its interests, and it tends toward standards when no such hegemon exists. See *id.* at 224–26. Baistrocchi views the BEPS project as the transition point from an era of rules to an era of standards because it marked the end of the United States' reign as hegemon. *Id.* at 257. If one is convinced by Baistrocchi, the introduction of rules into the PPT will likely coincide with the rise of a country or bloc to hegemon status. This Note does not take a position on Baistrocchi's argument, but instead notes it for added context.

OECD project, those decision-makers are states' tax administrations and domestic adjudication systems. Finally, Section IV.C argues that continuing incentives for tax competition post-BEPS will result in states using their discretion to arrive at divergent interpretations of the PPT. While some states may advocate for a broad interpretation of the PPT to engage in aggressive tax enforcement, others will read the test narrowly for reasons that may include attracting foreign investment. Importantly, the existence of the latter interpretation will likely limit the PPT's overall impact.

A. Legal Form Allocates Discretion

Commentators have not acknowledged the connection between the PPT and the rules-and-standards literature, but many commentators' concerns about the PPT have implicitly been objections to the OECD's decision to structure its anti-treaty abuse provision as a standard.¹⁰⁰ Consider the LOB—a U.S. anti-treaty abuse provision comprised of specific, objective requirements that MNEs must meet to qualify for treaty benefits—as a foil here for illustration.¹⁰¹ Relative to the LOB, a taxpayer cannot confirm whether a proposed course of action will be entitled to treaty benefits by looking at the language of the PPT. This is because the propriety of its conduct will only be determined *ex post*, which is a difficulty for MNEs that desire certainty.¹⁰² And praise for the PPT's flexibility is also implicitly appreciation for its being a standard. Unlike administrations bound by the LOB's specific requirements, tax authorities can respond to varied fact patterns under the PPT because the provision

¹⁰⁰ See, e.g., Ashish Goel, *Does the Principal Purpose Test (PPT) Throw Tax Certainty to the Winds?*, Kluwer Int'l Tax Blog (May 2, 2019), <https://kluwertaxblog.com/2019/05/02/does-the-principal-purpose-test-ppt-throw-tax-certainty-to-the-winds> [<https://perma.cc/RU6P-Y99D>] (objecting that the PPT's broadness and vagueness violate India's principle of tax certainty).

¹⁰¹ Though this Note compares the PPT to the LOB for illustrative purposes, it takes no position on the relative merits of the two provisions. For a thorough, normative consideration of tax treaty anti-abuse rules, see generally Reuven S. Avi-Yonah, *Limitation on Benefits or Principal Purpose Test? Part 1*, 115 *Tax Notes Int'l* 865 (2024) (examining the relationship between the PPT and the LOB provision); Reuven S. Avi-Yonah, *Limitation on Benefits or Principal Purpose Test? Part 2*, 115 *Tax Notes Int'l* 1033 (2024) (discussing whether the United States should adopt a PPT over the LOB rule).

¹⁰² It is common knowledge among tax planners that clear rules can always be planned around. See NYU School of Law, *supra* note 55, at 50:31–50:40 (indicating that this is the OECD's view). Compliance generally comes with costs but brings certainty and permits tax minimization within the confines of what is allowed.

does not seek to define the sets of allowed and prohibited activity precisely. Both of these reactions to the PPT align with characteristics of standards that have been identified in the literature on legal form;¹⁰³ however, each fails to thoroughly address the consequences of defining a legal command's content *ex post* in the context of the international tax regime.

The choice as to whether a legal command's content is defined *ex ante* or *ex post* is effectively a determination as to which rulemaking institution gets discretion.¹⁰⁴ For example, suppose that the national legislature of Country *X* promulgated a rule establishing that a person is a Country *X* tax resident if they spent 183 or more days during the year in Country *X*.¹⁰⁵ By setting forth a rule with precisely defined content, the legislature retains the discretion over how to pursue the relevant legal principle—taxing the income of individuals with a substantial presence in the country—for itself. Generally speaking, the tax authority and judge, as *ex post* decision-makers, will be confined to the considerations within the legislation's four corners when determining whether a particular individual should be taxed as a resident (i.e., counting days).¹⁰⁶ Meanwhile, when a legislature enacts a standard, it reserves discretion to whichever decision-maker comes into play later in the legal process.¹⁰⁷ Imagine now a national rule in Country *Y* assigning tax residence by determining the country to which an individual has the closest connection.¹⁰⁸ The Country *Y* tax authority and judges would get to decide

¹⁰³ Specifically, rules are viewed as providing greater certainty to those who interact with the law than standards, while standards are touted for flexibility. See Ehrlich & Posner, *supra* note 61, at 277–78.

¹⁰⁴ See Johnston, *supra* note 64, at 396 (noting that vague commands from high-level officials vest more discretion in their lower-level subordinates). Though this Note uses a legislative legal command in this discussion for analytical clarity, the principle holds similarly for judge-made rules and standards. When a court sets forth a precise rule, that rule restrains the discretion of courts later called upon to apply it, whereas a judge-made standard reserves discretion for the later jurist.

¹⁰⁵ Canada is one state that uses this rule. See Deemed Residents of Canada, Can. Revenue Agency, <https://www.canada.ca/en/revenue-agency/services/tax/international-non-residents/individuals-leaving-entering-canada-non-residents/deemed-residents.html> [<https://perma.cc/96FN-39F9>] (last visited Jan. 3, 2026).

¹⁰⁶ See Kaplow, *supra* note 59, at 563 (indicating that rules account for any relevant contingencies at the promulgation phase).

¹⁰⁷ *Id.* at 560.

¹⁰⁸ This example resembles the “centre of vital interests” test, which is a tiebreaker included in the 2017 OECD Model to determine a dual-resident's tax residence for treaty purposes. See OECD, 2017 Model, *supra* note 4, art. 4(2)(a).

for themselves which considerations are relevant to determining residence and where the contours of the category lie (e.g., which sorts of connections to a country matter, how these considerations are weighed, etc.).¹⁰⁹

B. The PPT Allocated Discretion in Preventing Treaty Abuse to the OECD Member States

When states' tax authorities convene at the OECD, their choice of a legal command's form represents, in part, a choice between exercising discretion as a collective of member states or reserving discretion to each state autonomously and to their separate systems of adjudication. This is a function of how international tax policy operates. Rules made at the OECD are intended to reflect consensus and are therefore indicative of the state of play for the whole system;¹¹⁰ however, when the OECD elects not to define a legal command precisely, each state gets to define it for itself, at least to a degree. There is no central tax tribunal to litigate disputes under the system's network of bilateral treaties.¹¹¹ In fact, barring limited arbitration, the system generally admits only of domestic litigation in the state that deems an MNE to have allegedly underpaid its taxes.¹¹²

¹⁰⁹ There are all sorts of reasons for placing discretion with different legal actors that could drive future studies of the PPT with a normative bent. Reasons could include promoting harmonization or protecting tax sovereignty. This Note leaves further consideration of this question for other works.

¹¹⁰ See Brauner, *Treaties in the Aftermath of BEPS*, supra note 19, at 1019.

¹¹¹ See Brauner, *What the BEPS?*, supra note 3, at 109–10.

¹¹² The European Union's system of "state aid," which is an element of European competition law that has been used in recent years to review tax rulings provided by European states to MNEs, is an exception to this statement. The future vitality of this system is unclear, as the European Commission suffered a string of defeats at the European Court of Justice before succeeding in the *European Commission v. Ireland & Apple Sales International* case in 2024. *Case C-465/20, Eur. Comm'n v. Ir. & Apple Sales Int'l*, ECLI:EU:C:2024:724 (Sep. 10, 2024); see James Anderson et al., *Your Homework Will Be Graded: The ECJ's Apple Decision and Its Implications for International Tax*, Skadden (Sep. 26, 2024), <https://www.skadden.com/insights/publications/2024/09/your-homework-will-be-graded> [<https://perma.cc/8JEA-UBNN>]. This is a particularly poor moment to forecast the future relevance of state aid in tax cases, as scholars have aggressively questioned the bona fides of the Court of Justice's approach in *Apple*. See, e.g., Ruth Mason & Stephen Daly, *Rotten to the Core: The EU's Court of Justice Decision in Apple*, 116 *Tax Notes Int'l* 987, 992 (2024).

C. Reserving Discretion to OECD Member States Is Likely to Result in Bifurcated Interpretation of the PPT

Acknowledgment of the unilateral nature of tax treaty enforcement requires consideration of the extent to which states, even as they all adopted the PPT, meaningfully harmonized their tax treaty enforcement. If all individual states shared the same interests with respect to international taxation, we could expect something akin to uniform enforcement. But, as explained below, the presence of continued incentives for tax competition post-BEPS suggests that a bifurcated approach is more likely.

This idea has been noted but not systematically analyzed by scholars discussing BEPS's approach to treaties,¹¹³ as much of the conversation about the PPT's impact has focused on the way it will be implemented by what might be called "more aggressive states" to the exclusion of their less aggressive counterparts. This focus on aggressive tax authorities has likely led to an overstatement of the PPT's projected impact. This Section seeks to paint a more realistic picture by introducing tax competition and explaining that it continues post-BEPS before arguing that the PPT's imprecision will lead to divergent interpretations in international tax's competitive environment.

1. Historical Tax Competition: The Emergence of More and Less Aggressive States

As briefly discussed in Part I, international tax policy has historically been characterized by competition among states. Essentially, some states use their national tax systems to attract investment—reducing the effective tax rate paid by MNEs by confirming a desired interpretation of their tax law to an individual company,¹¹⁴ temporarily exempting income earned by new investors from taxation,¹¹⁵ and even eliminating the

¹¹³ See Elliffe, *supra* note 7, at 51 (expressing a concern that countries will substitute their domestic views for an international autonomous meaning when interpreting the PPT); Philip Baker, *The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting*, 2017 *Brit. Tax Rev.* 281, 283 (expressing worry about the consequences of unpredictable interpretations of the PPT on the system of tax treaty benefits).

¹¹⁴ See Mason, *supra* note 2, at 365–66.

¹¹⁵ These programs are referred to as "tax holidays," and they create a national system in which new capital is taxed at lower rates than existing capital. See Jack M. Mintz, *Corporate Tax Holidays and Investment*, 4 *World Bank Econ. Rev.* 81, 81 (1990) (defining "tax holidays" as a "common form of tax incentive . . . which permits a new company to operate for a given number of years before paying corporate income taxes"); Michael Keen & Kai A.

corporate income tax.¹¹⁶ And once one state starts receiving an outsized share of foreign investment¹¹⁷ because of the tax incentives it has created, other states are prompted to do the same. This creates what scholars have generally referred to as a “race to the bottom,” wherein MNEs’ capital investment trends toward the state that most substantially limits the resulting tax liability.¹¹⁸

Of course, not all states historically have been drawn all the way into tax competition.¹¹⁹ At the risk of collapsing a spectrum of actors into two groups, it is analytically useful to divide states into more and less aggressive categories.¹²⁰

More aggressive states—which tend to have developed economies, large populations, and strong infrastructures¹²¹—generally engage in less

Konrad, *The Theory of International Tax Competition and Coordination*, in *5 Handbook of Public Economics* 257, 302 (Alan J. Auerbach, Raj Chetty, Martin Feldstein & Emmanuel Saez eds., 2013) (explaining the differential tax rates on capital created by tax holidays).

¹¹⁶ See Michael P. Devereux, Ben Lockwood & Michela Redoano, *Do Countries Compete Over Corporate Tax Rates?*, 92 *J. Pub. Econ.* 1210, 1210 (2008) (explaining that governments engage in tax competition over statutory rates). It is worth noting that the value of statutory rate competition will be greatly reduced if Pillar 2, a currently pending OECD attempt at establishing a global minimum tax rate of fifteen percent, is successfully implemented. See Ruth Mason, *A Wrench in GLOBE’s Diabolical Machinery*, 107 *Tax Notes Int’l* 1391, 1393–94 (2022) (describing the process by which Pillar 2’s structure ensures that corporate groups subject to its provisions have a global effective tax rate of at least fifteen percent even if traditionally low-tax states defect from the regime).

¹¹⁷ The share of foreign investment is “outsized” in the sense that tax competition distorts MNEs’ investment decisions relative to a pre-tax baseline, moving money to states that engage in tax competition based on after-tax returns on capital. See Vincenzo Quadrini & José-Victor Ríos-Rull, *International Tax Competition with Rising Intangible Capital and Financial Globalization* 4 (Penn Inst. for Econ. Rsch., Working Paper No. 23-011, 2023) (“Taxes, of course, affect investments . . .”).

¹¹⁸ See, e.g., Romesh Vaitilingam, *Would a Global Minimum Corporate Tax Rate End the ‘Race to the Bottom’?*, *Chi. Booth Rev.* (July 13, 2021), <https://www.chicagobooth.edu/revie/w/would-global-minimum-corporate-tax-rate-end-race-bottom> [<https://perma.cc/3GLY-EM5Y>] (inquiring whether Pillar 2 will be “a step toward ending the ‘race to the bottom’ that occurs when companies strategically relocate in order to pay the lowest [tax] rates”).

¹¹⁹ See Rosanne Altshuler & Harry Grubert, *The Three Parties in the Race to the Bottom: Host Governments, Home Governments and Multinational Companies*, 7 *Fla. Tax Rev.* 151, 156 (2005) (explaining why a high-tax country might reasonably allow income to be stripped from its jurisdiction and relocated to a less aggressive state).

¹²⁰ “Aggressiveness” in this context is stated in terms of a state’s enforcement strategy against the taxpayers by whom it may be owed funds. The more aggressive a state, the more aggressive its enforcement approach.

¹²¹ See Avi-Yonah, *Globalization*, *supra* note 23, at 1639 (explaining that developed countries must try to prevent the erosion of their tax bases).

competitive behavior.¹²² Think of countries like Germany. MNEs operate in Germany for access to its skilled workforce or large consumer base (i.e., nontax business purposes), not to minimize their tax liability.¹²³ Germany and similar states rigorously enforce their tax provisions and attempt to use their political capital to curb competitive behavior.¹²⁴ Meanwhile, less aggressive states¹²⁵—which tend to have developing economies, small populations, and good governance¹²⁶—aggressively attract capital investment in part by offering a friendly fiscal and legal environment for MNEs. Think of the Cayman Islands as an example. An

¹²² This is not to say that more aggressive states' tax systems are not designed in ways that draw capital investment, but only that these states meaningfully tax foreign enterprises in most situations. See, e.g., Daniel J. Hemel, *The United States as the Ultimate Tax Haven: Testimony Before the House Ways and Means Subcommittee on Oversight 2* (Univ. of Chi. L. Sch. Pub. L. & Legal Theory, Working Paper No. 793, 2022) (describing how the United States allows foreigners to earn reliable returns on investment without paying tax); Aparna Mathur, *The US Counterpunch to the OECD BEPS Project*, Am. Enter. Inst. (July 20, 2018) (citing Tax Cuts and Jobs Act of 2017, Pub. L. No. 115-97, 131 Stat. 2054), <https://www.aei.org/articles/the-u-s-counterpunch-to-the-oecd-beps-project/> [<https://perma.cc/Y4FF-CWPE>] (describing the U.S. 2017 tax bill as creating a more competitive tax code); Chris Edwards, *Global Tax Competition*, in *Cato Handbook for Policymakers* 685, 692 (9th ed. 2022); Christian von Haldenwang et al., *Trade, Investment and Tax Cooperation: Tax Competition 3* (2018), https://www.global-solutions-initiative.org/wp-content/uploads/2025/03/GSx-TF-7-Tax_competition-DEF_vf.pdf [<https://perma.cc/V92E-NWUW>].

¹²³ See CT Corp. Staff, *Doing Business in Germany: Advantages and Disadvantages*, Wolters Kluwer (May 14, 2020), <https://www.wolterskluwer.com/en/expert-insights/doing-business-in-germany> [<https://perma.cc/DQZ6-FSZW>] (listing Germany's consumer market and ability to translate research into practical applications as advantages of doing business in Germany and naming "paying taxes" as a disadvantage).

¹²⁴ See Sheppard, *supra* note 5, at 1147 (quoting a British Crown dependency lawyer describing BEPS as "a French and German effort dressed up in ideology").

¹²⁵ The OECD describes less aggressive tax authorities as "tax havens" and has adopted a rough definition of "tax haven" based on likely behaviors which this Note roughly tracks. The OECD's definition highlights "no or low taxes, lack of effective exchange of information, lack of transparency, and no requirement of substantial [economic] activity" as the *sine qua non*s of a "tax haven." See *What Is a Tax Haven?*, Whistleblower Just. Network (citation omitted), <https://whistleblowerjustice.net/what-is-a-tax-haven/> [<https://perma.cc/H39K-H8LE>] (last visited Jan. 3, 2026). This definition conveniently ignores the practices of OECD member states that engage in aggressive tax competition and is specifically not incorporated into this Note.

¹²⁶ See Dhammika Dharmapala & James R. Hines Jr., *Which Countries Become Tax Havens?*, 93 J. Pub. Econ. 1058, 1060–61 (2009) (finding that increased quality of governance and decreased population are each positively associated with the likelihood of a state being a "tax haven"); Mintz, *supra* note 115, at 81 (explaining that about half of developing countries offer tax holidays to encourage investment).

MNE may establish a subsidiary in the Cayman Islands because of the state's zero-percent corporate income tax rate.¹²⁷

2. Continuing Incentives for Tax Competition Post-BEPS

The incentives to compete persisted into the period of BEPS negotiations.¹²⁸ And BEPS itself did nothing to disincentivize countries from continuing to compete. While BEPS is fundamentally aimed at increasing tax system coordination among states,¹²⁹ its treaty benefit efforts lack a fiscal fail-safe, that is, a rule that limits the value of tax competition by giving another state the opportunity to tax an MNE if the state with primary taxing rights fails to do so.¹³⁰ As such, a proper portrayal of the PPT's likely impact must account for less aggressive states' competitive behavior.

3. A Tool for More Aggressive States

To say that the PPT's probable impact has been overstated is not to say that the BEPS project's attempt to curb treaty abuse will not alter the international tax landscape whatsoever. One can expect to see that change in more aggressive states' implementation of the provision.

More aggressive states dominate the OECD, and they pushed for the introduction of a treaty-specific anti-abuse rule in the 2010s.¹³¹ Before the PPT, these states' enforcement efforts were limited by the absence of such a rule. Most aggressive states have a collection of anti-abuse provisions in their domestic law,¹³² but many states determined that their domestic

¹²⁷ See Cayman Islands: Corporate—Tax Credits and Incentives, PWC, <https://taxsummaries.pwc.com/cayman-islands/corporate/tax-credits-and-incentives> [https://perma.cc/CY9C-9LKK] (last updated July 15, 2025).

¹²⁸ See Edwards, *supra* note 122, at 685–87 (discussing tax competition dynamics in the 2010s).

¹²⁹ See Mindy Herzfeld, *The Case Against BEPS: Lessons for Tax Coordination*, 21 Fla. Tax Rev. 1, 1 (2017) (describing BEPS as “an ambitious project of coordinating and harmonizing countries’ international tax rules”).

¹³⁰ See Mason, *supra* note 2, at 373 (defining “fiscal fail-safes” and discussing their use elsewhere in the BEPS project).

¹³¹ In fact, the G20 countries tasked the OECD with completing the BEPS project in short order. See G20 Leaders Declaration, *supra* note 31, ¶ 48, at 8; Brauner, *What the BEPS?*, *supra* note 3, at 111 (explaining that OECD had just two years to develop a final report for the BEPS project).

¹³² The Internal Revenue Service, for example, wields (among other tools) a specific anti-abuse rule limiting the value of shifting profits out of the country, a general statutory requirement that transactions must have economic substance and a business purpose to be

rules were inapplicable in the treaty context.¹³³ Rather than reflecting competitive behavior, these decisions represented a principled view that signing a treaty precluded the application of rules not anchored in the treaty.¹³⁴ However, these holdings nonetheless bound the hands of aggressive states with applicable domestic rules. This is because we can expect an MNE to choose the safer option if doing business in one aggressive state risks liability for treaty abuse while doing business in another comparable state does not. The PPT resolved this dilemma by giving all aggressive states at least one applicable rule to combat treaty abuse,¹³⁵ and one designed for them to apply broadly at that.¹³⁶

4. *A Moderating Influence from Less Aggressive States*

While the PPT provides more aggressive states with an enforcement tool, the test's overall impact on international tax policy will be limited by its imprecision. While norms of international law and domestic pressures to maintain the rule of law would coerce relatively uniform enforcement of a precise rule,¹³⁷ the PPT provides tax authorities with the

respected, and a judicial doctrine that recharacterizes transactions according to their substantive effects if those differ from their form. See I.R.C. § 59A (addressing profit shifting); id. § 7701(o) (requiring economic substance and business purpose); *Gregory v. Helvering*, 293 U.S. 465, 469–70 (1935) (creating the substance-over-form doctrine).

¹³³ See NYU School of Law, *supra* note 55, at 1:07:02–1:07:15; Irma Mosquera, *Interaction Between PPT, Tax Treaty and Domestic GAARs*, Inter-Am. Ctr. of Tax Admins. (July 11, 2019), <https://www.ciat.org/interaction-between-ppt-tax-treaty-and-domestic-gaars/?lang=en> [<https://perma.cc/UX2S-T29L>] (explaining that some countries resolved this conflict on a bilateral basis by introducing conflict-resolving treaty provisions).

¹³⁴ See NYU School of Law, *supra* note 55, at 1:07:02–1:07:15.

¹³⁵ This is not to say that there is no concern about conflict between the PPT and domestic anti-abuse rules. Quite the contrary, scholars have decried a lack of clarity on the subject. Mosquera, *supra* note 133 (“[T]here is not clarity in the interaction between . . . [General Anti-Abuse Rules] and the PPT.”).

¹³⁶ OECD, 2017 Model, *supra* note 4 (calling twice for broad interpretations of components of the PPT).

¹³⁷ For example, states comply with international law in order to receive the continued benefits of the system. If a less aggressive tax authority were to take an unjustifiably loose interpretation of a treaty anti-abuse *rule*, states would discipline it by refusing to ratify treaties or make concessions in negotiations, which would spell doom for the state's attempts to attract capital. See Harold Hongju Koh, *Why Do Nations Obey International Law?*, 106 *Yale L.J.* 2599, 2601 (1997) (reviewing Abram Chayes & Antonia Handler Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (1995); Thomas M. Franck, *Fairness in International Law and Institutions* (1995)) (“In the Chayeses’ view, nations obey international rules not because they are threatened with sanctions, but because they are persuaded to comply by the dynamic created by the treaty regimes to which they belong.”).

opportunity to advocate for differing interpretations of the test’s language. This regulatory diversity will mitigate the PPT’s impact—changing the ways in which MNEs integrate treaties into their tax planning rather than substantially eliminating the enterprise.

Just as more aggressive states can broadly interpret the PPT’s prohibition, very little exists to prevent their less aggressive counterparts from narrowly defining “one of the principal purposes,”¹³⁸ treating “reasonable to conclude”¹³⁹ as a substantial burden of proof, defining “all relevant facts and circumstances”¹⁴⁰ in a more targeted manner, or creating a safe harbor that regularly finds granting treaty benefits to be “in accordance with the object and purpose of the relevant [treaty] provisions.”¹⁴¹ Responses from the OECD’s more aggressive members, such as pushing for added Commentary language, might limit those

¹³⁸ Michael N. Kandev & Jesse A. Boretsky, Canadian Appeal Court Rejects Government’s Treaty-Shopping Arguments Against Luxembourg Holding Company, 98 Tax Notes Int’l 1245, 1248 (2020).

¹³⁹ Jinyan Li, Finding the Purpose of Tax Treaty Provisions Under GAAR: Lessons from *Alta Energy*, 105 Tax Notes Int’l 147, 149 (2022) (quoting OECD, Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting art. 7(1) (2016) [hereinafter OECD, Multilateral Convention to Implement Tax Treaty Related Measures], <https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf> [<https://perma.cc/U2DC-463T>]).

¹⁴⁰ Id. (quoting OECD, Multilateral Convention to Implement Tax Treaty Related Measures, *supra* note 139).

¹⁴¹ Id. (emphasis omitted) (quoting OECD, Multilateral Convention to Implement Tax Treaty Related Measures, *supra* note 139). One way for a state to create such a safe harbor may be for the state to defer to its treaty partners’ formalistic rules, essentially taking its treaty partners as they come. The Supreme Court of Canada took this approach in interpreting the Canadian general anti-abuse rule, which is functionally identical to the PPT, in the context of a Canada-Luxembourg bilateral tax agreement. See *Canada v. Alta Energy Luxembourg S.A.R.L.*, [2021] 3 S.C.R. 590, 614–15 (Can.). *Alta Energy* redomiciled from Canada to Luxembourg—which merely required the company to move its corporate seat—specifically to take advantage of a treaty benefit, but the Court denied the Canadian tax authority’s claim of abuse on the ground that Canada knew of Luxembourg’s formalistic residence rule when it signed a treaty that determined residence according to domestic law and could not use its anti-abuse rule to renegotiate the agreement *ex post*. Id. at 605, 607–09, 615–16. Commentators have suggested that this case might signal a path to be taken in future PPT litigation. See Kandev & Boretsky, *supra* note 138, at 1245 (“[*Alta Energy*] should provide guidance on how the [PPT] . . . should be applied to perceived treaty-shopping cases.”). But see Li, *supra* note 139, at 161 (arguing that the revisions to the OECD Model’s preamble required by the MLI may lessen the impact of *Alta Energy*’s holding on PPT interpretation).

domestic interpretations,¹⁴² but ultimately vague language can lend itself to hawkish or dovish interpretation.

The strong likelihood that less aggressive states will issue taxpayer-friendly PPT interpretations should assuage commentators' concerns that an aggressive approach by some states will encroach on MNEs' efforts to integrate treaties into their tax planning. Specifically, MNEs who fear the uncertainty involved in dealing with an aggressive tax administration can still comfortably seek the benefits offered by a less aggressive state to contracting state residents or enter into transactions that comply with a rule minimizing tax liability in a less aggressive state.

The PPT's broad language is eye-catching, but an analysis sensitive to international taxation's competitive structure tells what may be a more nuanced story. Particularly, the fact that MNEs may still gain favorable interpretations in certain jurisdictions will likely blunt the PPT's supposedly dramatic effects.¹⁴³ The PPT will curb certain behaviors, but planning efforts will continue so long as there are states which use tax competition to attract capital.

CONCLUSION

This Note sought to introduce the literature on legal form to the scholarly discussion of the Principal Purpose Test in order to present a different view of the provision's likely impact that is sensitive to the nature of international tax policy. Sewing these two divergent areas of law together provided for the conclusions that (1) like all other standards, the

¹⁴² See Omri Marian, *The State Administration of International Tax Avoidance*, 7 *Harv. Bus. L. Rev.* 1, 53 (2017) ("Another factor that contributed to arbitrage manufacturing was the fact that the rulings were never made public.").

¹⁴³ A recent treaty interpretation case involving the U.S. branch of McDonald's Luxembourgish subsidiary exemplifies this point. See Commission Decision 2019/1252, 2018 O.J. (L 195) 20, 23 (EU). Under the U.S.-Luxembourg treaty, the United States could tax the branch only if it had a nexus and business profits in the United States according to the U.S. definitions of those terms. *Id.* at 22. The United States determined that the branch did not meet these criteria and thus could not be taxed, but Luxembourg exempted the branch's income based on its independent determination that the United States could tax the income. *Id.* at 36. Despite the treaty's specification that U.S. definitions governed the taxability question, Luxembourg applied its own definitions of nexus and business profits, deliberately reading the treaty in a manner that provided for double non-taxation. *Id.* at 30. Aggressive treaty-based tax planning will persist so long as no fiscal fail-safe disincentivizes Luxembourg's tax-minimizing mode of treaty interpretation. For a more detailed discussion of the European Commission's Decision on *McDonald's*, see Ruth Mason, *Identifying Illegal Subsidies*, 69 *Am. U. L. Rev.* 479, 522–24, 528–30, 552–53 (2019).

PPT will likely become more certain and less flexible, and (2) the PPT, which has been touted and feared for its breadth, will likely have its force mitigated by differing interpretations in different states. The point is not to say that the PPT will be insignificant, but rather that its impact may be more targeted, nuanced, and complex than its original reception might imply.