HAVENS IN A STORM

THE STRUGGLE FOR GLOBAL TAX REGULATION

J.C. SHARMAN

Havens in a Storm

A book in the series

Cornell Studies in Political Economy

Edited by Peter J. Katzenstein

A list of titles in this series is available at www.cornellpress.cornell.edu.

Havens in a Storm

THE STRUGGLE FOR GLOBAL TAX REGULATION

J. C. SHARMAN

CORNELL UNIVERSITY PRESS

Ithaca and London

First published 2006 by Cornell University Press

Printed in the United States of America

Library of Congress Cataloging-in-Publication Data

Sharman, J. C. (Jason Campbell).
Havens in a storm : the struggle for global tax regulation / J. C. Sharman.
p. cm. — (Cornell studies in political economy)
Includes bibliographical references and index.
ISBN-13: 978-0-8014-4504-0 (cloth : alk. paper)
ISBN-10: 0-8014-4504-3 (cloth : alk. paper)
1. Tax havens. 2. Taxation—International cooperation. I. Title. II. Series.
K4464.5.S52 2006
343.05′23—dc22
2006019348

Cornell University Press strives to use environmentally responsible suppliers and materials to the fullest extent possible in the publishing of its books. Such materials include vegetable-based, low-VOC inks and acid-free papers that are recycled, totally chlorine-free, or partly composed of nonwood fibers. For further information, visit our website at www.cornellpress.cornell.edu.

Cloth printing 10 9 8 7 6 5 4 3 2 1

To my family and Bilyana

WHERE the remote Bermudas ride
In the ocean's bosom unespied,
From a small boat that row'd along
The listening winds received this song:
"What should we do but sing His praise
That led us through the watery maze
Unto an isle so long unknown,
And yet far kinder than our own?
Where He the huge sea-monsters wracks
That lift the deep upon their backs,
He lands us on a grassy stage
Safe from the storms, and prelate's rage."

—Andrew Marvell (1621–78)
"Bermudas"

CONTENTS

ACKNOWLEDGMENTS

The idea that became this book germinated after I had taught anarchist political philosophy in Bulgaria. With an instinctively realist outlook, students were incredulous that the tiny self-governing political units that anarchists demanded as the price of direct democracy could ever survive without being conquered or colonized. I began to wonder how very small states survive, why they have multiplied, and how they make their way in the international system. After a few abortive starts and a move to Sydney, I randomly happened on a report by the OECD that set up a struggle between the powerful member states of this organization and a group of tiny states and semi-sovereign political units labeled as tax havens. I knew nothing about tax havens, but this issue seemed to provide a good case from which to explore what happens when large and small states come into conflict. Whether small states can get away with annoying big states seems to be a question with a lot of potential for getting at some central issues in the field of International Relations.

The various drafts that became this book took shape over the following four years. During this time I learned much, mainly by seeking out the experts and practitioners in this very specialized field, from academia, government, international organizations, and the financial services industry. Somewhat to my surprise, but also to my infinite benefit, I found that people from each of these backgrounds were generally willing to give up their time to speak with someone with little or no background in the field, who offered nothing in terms of fees, relief from other pressing work, or even favorable publicity. Although I was an anonymous and jet-lagged junior scholar from a distant country, pitching up on some foreign shore, the people I spoke with were extremely patient and generous with their time. It is to these people, the majority of whom may not agree with much of the content of this book, that any contributions it might make are due.

Both outside and inside academia some people have made an especially prominent contribution in helping me along. From those on either side of the polarized politics of the issue, special thanks go to those involved in the cut and thrust: Andreas Antoniou, Richard Murphy, John Christensen, and especially Ben Coleman. The small, energetic and incredibly supportive group of political scientists, lawyers, anthropologists, economists, accountants, and business studies scholars working in and around this area have been consistently welcoming and willing to help, particularly Ronen Palan, Sol Picciotto, and Mark Hampton in the United Kingdom, Michael Webb and Ian Goldman in Canada, Greg Rawlings and Anthony van Fossen in Australia, and Bob Kudrle and David Spencer in the United States.

In Sydney, Graeme Gill, Darryl Jarvis, and John Hobson have provided crucial feedback after being repeatedly lumbered with various portions of this text. Gil Merom and Len Seabrooke provided the idea and encouragement to get in touch with Cornell University Press, and I have been extremely lucky in this match. Several research assistants were invaluable in tracking down a mountain of data on the most obscure topics I could come up with, and I am very grateful to Jesse Dillon Savage, Hugh Wehby, Ryan Thew, Jamie Drysdale, Sharni Chan, Michael Cohen, and especially Abhilash Puljal and Carla Wilshire for their hard work. The Consortium for Qualitative Research Methods workshop at Arizona State University and the European Consortium for Political Research workshop on International Organization and Implementation in Uppsala were both incredibly stimulating and exciting environments for me to reflect on many aspects of the book; the organizers and participants should know how beneficial these events were.

Two anonymous reviewers from Cornell University Press went above and beyond the call of duty in providing very incisive and helpful comments on matters large and small. I am extremely fortunate to have had such expert and generous readers and I am very grateful for all their hard work.

All the travel associated with the book has caused many to wonder if I spend all my time sipping cocktails on the beaches of exotic tropical islands, and others to suspect (I subsequently found out) that I was being bankrolled by one or more intelligence agencies. Unfortunately, the truth is far less glamorous. I would, however, like to thank the University of Sydney for its unstinting financial support and the Australian Research Council for Discovery Grant DP0452269, as well as my travel agent Catherine George for knowing the best way from Road Town to Rarotonga via Vaduz.

Finally, my greatest thanks are to Bilyana for her patience and for holding the fort during my frequent absences.

J. C. Sharman

Sydney, Australia

Havens in a Storm

Introduction

Tax is an area where states are most in need of international cooperation but least able to achieve it. This situation reflects the tension between contemporary economic changes and traditional sovereign prerogatives in a particularly stark form. From the early 1990s, policy makers in the world's richest and most powerful countries worried that changes in the international economy might severely undermine their ability to tax. Discussions about what could and should be done to address this new threat took place within several clubs of rich states: the Group of Seven nations (G7), the European Union (EU), and especially the Organisation for Economic Co-operation and Development (OECD), which was entrusted with formulating a response. The centerpiece of the strategy developed in 1996–98 was targeted at small states, labeled tax havens. These states were accused of fostering "harmful" tax competition at the global level by bidding for mobile investment with fiscal and regulatory concessions. The OECD sought to pressure tax havens to adopt a standard package of tax, financial, and banking regulations in order to tame this competitive dynamic and avert a "race to the bottom" in tax rates. The ensuing struggle between the two sides was above all a rhetorical contest. Both sides tried to garner the support of third parties, and the result of this contest hinged on concerns about losing face in the eyes of various transnational audiences. By 2002 the small state tax havens had prevailed, and the campaign to regulate international tax competition had failed. This book is devoted to explaining the nature and outcome of this struggle.

Why is this particular issue, an attempt to impose global regulations on tax havens, important enough to warrant a book? In economic terms, the sums at stake are huge, amounting to hundreds of billions of dollars of tax revenue and trillions of dollars of investment. The effort to establish global tax standards also sheds light on the problem of implementing international regulation that creates losers as well as winners. If the policy outcome of interest is regulation, then the conceptual goals are to advance our understandings of the use of language for political ends, as well as how actors' concerns about the way they are thought of by others affect their decisions and behavior. In international politics as in everyday life, actors spend a lot of effort and time talking to one another and worrying about what others think of them. These concerns are crucial for explaining the development and outcomes of the tax competition controversy, but also many other disputes in world politics.

Since the 1980s one of the defining issues in the field of International Relations has been the significance of security fears versus utility gains in establishing cooperation between self-interested states in the international arena. Perhaps even more important has been the division between a rationalist approach, imported from economics, and a constructivist approach emphasizing culture, norms, and identity. Overlaying these concerns has been the more popular public discussion of globalization, especially in terms of what growing international economic flows and technological developments mean for the future of the state. The events to be examined are important for each of these controversies. If the transformative effect of economic globalization is to be seen anywhere, it should be in the area of international tax competition. For those scholars interested in solutions to international market failures and collective action problems, the initiative to establish global tax regulation is an important case of the limits of crafting and implementing regulatory solutions. Rather than the proposed regulations creating benefits all around, they threatened to create definite winners (the OECD and its member states) and losers (the tax havens). As such, the conflict is a study in power political economy. The centrality of conflict between state actors thus gives the tax competition controversy a strong affinity with realist concerns. The account of the initiative against harmful tax competition presented in this book aims both to address conceptual criticisms of constructivist explanations in general and to expand the coverage of this approach into international economics. Particular attention is given to several concepts associated with language use for political ends, such as rhetorical action, speech acts, and argument. The second major conceptual focus is on reputation in world politics, that is, on how actors are affected by the opinions others hold of them. These two concepts work together: the way an actor is perceived affects the impact of its rhetoric; the rhetoric of an actor, or of third parties about that actor, in turn affect the way others perceive it.

After examining the political and scholarly significance of the struggle between the OECD and tax havens, I lay out the basic shape of the argument, first as a whole and then in somewhat more detail by previewing the major points to be made in each chapter to follow. I move from sketching out the policy and intellectual background of the struggle (chapter 1), to analyzing the nature of the conflict and surveying the main themes of the rhetorical contest (chapters 2 and 3), and finally providing an explanation of the result centered around the concepts of rhetoric and reputation (chapters 4 and 5).

Globalization, Corporate Power, and Collective Action Problems

Unlike most arcane and abstruse terminology at the center of debates within political science, the term "globalization" has gained wide currency in the media and among politicians. Since the 1990s, many observers became increasingly convinced that "something must be done" to rein in globalization, with the idea of tax competition crystalizing more general fears about global capitalism run wild. The maximalist view of globalization emphasizes the sheer novelty and depth of change associated with the phenomenon. A basic element of this thesis is that economic change, particularly the rise in cross-border trade and financial flows, has far outpaced states' capacities to control it. As a result, governments are said to have less control over economic outcomes and to be losing power to corporations and impersonal market forces. The issue of tax competition is at the heart of disputes and speculation about globalization. International tax competition includes all the main elements of the conventional globalization story. A credible exit option for capital at the domestic level and a severe collective action problem among states at the international level leads to the ascendance of global markets over national polities.

The bare bones of the globalization thesis are that recent advances in communications, information, and transport technology drive and combine with economic deregulation and liberalization to provide the owners of capital with much more mobility than they have had previously ("at the click of a mouse," as the cliché has it). An increasingly large range of goods and services can be produced in more locations, thus fostering competition between countries for scarce investment. In turn, because governments are competing with one another for scarce capital, they must adopt market-friendly or, more narrowly, investor-friendly policies for fear of seeing capital locate in or relocate to other jurisdictions. Capital flight and disinvestment wreck governments' macroeconomic plans, but they also and more directly undermine their capacity by eroding the tax base. Governments that cannot tax effectively cannot do much else, and thus international tax competition for mobile capital—particularly intangible financial assets–threatens to undermine states' power. Taxation is crucial to economic sovereignty. If proponents of globalization as corporate power eclipsing state power are right in the area of tax competition, they can afford to be wrong about a lot of other things and still carry great weight.

At first glance, this version of the globalization thesis seems to provide a good fit with the failure to regulate tax competition. When states are center stage, the result is an upset: small states win out against the interests of core states. Yet if international capitalism as a system, capitalists as a class, or corporations as actors are seen as dominant, then the result becomes much less surprising. Thanks to globalization, corporate interests trump or determine those of even the most powerful states, and the actions of small states become largely irrelevant. This version of events would be an important challenge to our continuing preoccupation with the state as the central actor in world politics.

A different emphasis on the globalization dynamic (closer to that adopted by the OECD) retains states as the prime movers in international standard-setting but sees them as severely constrained by collective action problems. Even if a group, or the majority of the world's states, cooperate to tame the demands of mobile capital, the remaining free-riders will benefit by attracting more capital with the resulting economic benefits. The larger the cooperative group, the larger the benefit accruing to jurisdictions that opt out of such collaborative arrangements. Thus the familiar story: if a group or even all other states cooperate to regulate mobile capital, each state is better off defecting to attract the foreign investment looking for a home. And if other nations are not cooperating, then each nation is once again better off by "giving in" to investors' demands, particularly by cutting taxes. This version of the story is reminiscent of neoliberal institutionalism, a gently obsolescing term for scholars drawing on the conceptual tools of micro and new institutional economics to understand how rational states strive to achieve mutually beneficial cooperation. In line with the globalization thesis, this school is also impressed by the importance of collective action problems facing states looking to regulate the international economy, and again tends to put economic concerns at center stage. How is international tax competition important to this research program? Empirically, investigations of international economic cooperation have tended to concentrate on trade and monetary relations, and only then with finance and investment. Yet although international tax competition may mark an empirical departure from the usual questions considered by neoliberal scholars, the structure of the issue marks it out as conceptually at the core of their agenda. This book takes issue with the idea that the toughest problem in global regulatory solutions is solving collective action problems and deterring cheating. Instead, it argues that in this instance there is a conflict of preferences between high-tax and low-tax states and that the latter stand to lose out under the proposed regime.

Power, Conflict, and Constructivism

The attempt to regulate international tax competition quickly developed as a distributional conflict. Rather than overcome a collective action problem in search of mutual advantage, each coalition tried to impose its preferred solution over the opposition of the other. Given realists' emphasis on latent or actual conflict as the defining feature of international relations, the struggle over tax competition and regulation seems to fit squarely within their bailiwick. A realist explanation of the struggle over global tax regulation would lend further credibility to a view of international political economy built on an underlying competition for survival between states, especially as the outlines of the case confirm realist presuppositions concerning the centrality of conflict and power. Among realists, Stephen Krasner has been particularly influential in arguing that disputes over the distribution of gains resulting from international cooperation are more of an obstacle to this sort of collaboration than the fear of being cheated by free-riders. Finding solutions to a given problem of international coordination is at best only half the battle, because states are not indifferent to alternative solutions that produce different distributions of benefits. Which equilibrium solution is picked depends on states exerting their power over other states to secure a disproportionate share of the benefits. Thus, far from power concerns being distinct from international cooperation, Krasner and others have maintained that they are intimately related.

In fact, the struggle over global tax regulation is connected with an ever more basic realist presumption, one less concerned with the distribution of benefits but that instead emphasizes conflicts that create winners and losers in absolute terms. For tax havens confronted with the OECD initiative, the issue was not a contest over the division of benefits but instead the prospect of absolute losses. This case is relevant to recent realist works that focus on how international collaboration in the economic arena can leave some states worse off than they were at the status quo.[1] There was conflict between two large coalitions of states (for realists the OECD is not an autonomous actor) with opposed preferences over an issue of great importance to each side. These features mean that the struggle over global tax regulation is well within core realist territory. However conceived, the outcome largely hinged on power concerns. But the outcome of the struggle poses a challenge to realist assumptions in that the weak defeated the strong; this is an important anomaly that needs to be explained.

In studying the struggle over tax competition, constructivists have an opportunity to step in and explain an anomalous result: there are good theoretical reasons to believe such a conflict should have been resolved by coercion in favor of large rich states, yet it was not. In this way my book includes a competitive test of alternative explanations. Critics of constructivism have rightly pointed out, however, that this approach has a variety of weaknesses. These include a failure to specify causal mechanisms; the "finding" of a norm to explain every event; an inability to explain deviations from norms; unfalsifiable hypotheses; and the static cast of explanations. For example, structural accounts based on shared conceptions of appropriate behavior for a given actor in a given context (regulative norms) have difficulty with variation and change. However, proponents of norms as resources may abandon the distinctive contributions of constructivist research by reinstating a utilitarian approach to social action. Calls to reconcile both views are by themselves not very helpful without showing how this is to be achieved, conceptually and empirically. Constructivists are, however, rising to this challenge, and the controversy over global tax regulation provides an opportunity to respond to critics with better answers.

If the campaign to impose global standards on tax havens marks a departure from realism's traditional concern with "high politics" and security, this is also the case for constructivism, which has until recently tended to shy away from economic issues.[2] As Benjamin J. Cohen noted in 2002, "Even less has constructivism, as a formal analytical approach, yet begun to enter the mainstream of research on financial issues."[3] A major aim of this work is to show that contests over international economic regulation occur in a social context that is vital for understanding the nature and outcomes of these interactions. The focus is on political events and policy developments, not theoretical clashes. Despite my generally constructivist orientation, I emphasize conflict, interstate power plays, and calculated (rhetorical) strategies. This eclecticism allows for the inclusion of insights provided by other perspectives in the field.[4]

Reputation is central to the argument and is defined as the shared totality of thoughts and associations that actors hold for one another. This is consistent with sociological and dictionary definitions of reputation but broader than the definition common in political science and economics. In this sense, reputation is a quintessentially "social" concept, consistent with the book's broader goal of showing that international economic relations are also social relations. Equally important, rhetoric is defined as the deliberate use of language as a means to political ends. In this sense, rhetoric is not signaling or "cheap talk," but potentially can be persuasive independent of material factors. I aim to build on, but also advance, existing scholarship concerning rhetoric, argument, speech acts, and general political discourse. One contribution is the treatment of blacklisting as a speech act. Another is to show how the irreducible plurality of meanings in language can sometimes enable the weak to use the principles of the strong for their own subversive ends. Rhetoric and reputation are inseparably linked. This connection builds on the simple idea that the impact of speech often depends at least as much on who is speaking as on what is said. Much of the book is devoted to illustrating the recursive links between rhetoric and reputation in the struggle for global tax regulation.

Overall, I suggest that norms are somewhat more "up for grabs" and subject to contestation than is often assumed but that reputation is less susceptible to actors' control than the conventional view would have it. The ambiguity and uncertain fit between norms and rhetorical themes on the one hand and the interests of the powerful on the other leaves room for calculated moves from both the strong and the weak. For example, in chapter 2 I illustrate how particular norms come to be relevant to particular issues; how the same norm may have different effects on different actors; and how the effect of a norm on the same actor may change over time. This discussion also explores why actors comply with norms as shared beliefs about appropriate behavior, why they look at the consequences to reputation when norms are violated, and how these views in turn may generate material costs.

The rhetoric in the struggle over global tax regulation was overwhelmingly, though not exclusively, public, often aimed at third parties as much as the direct interlocutor. More than a thousand texts are part of the public record because the protagonists made and rebutted charges in the media, on their websites, through commissioned papers on the subject, and many other sources. Thus there is a clear trail to follow in studying the rhetorical contest. Equally important is the contemporaneous commentary from more or less neutral third parties. In addition to tracing the various rhetorical gambits, the media coverage, and related material give an indication of the fluctuating reputations of the parties involved. But by itself this public material is not sufficient to substantiate some of the most important points in the argument, in particular, the reconstruction of crucial decisions and the discovery of the intentions and motivations behind particular acts.

To remedy this shortcoming, and to push beyond conventional practice in the field, this book is heavily based on fieldwork and interviews conducted by the author with key participants in Antigua and Barbuda, Aruba, Australia, Austria, Barbados, Belgium, the British Virgin Islands, Canada, the Cayman Islands, the Cook Islands, Fiji, France, the Isle of Man, Jersey, Liechtenstein, Mauritius, Montserrat, Seychelles, St. Kitts and Nevis, the United Kingdom, the United States, and Vanuatu in the period 2002–2005. Those interviewed are from many different backgrounds: the public and private sectors in tax havens and OECD member states; the OECD and international organizations that opposed the OECD; third party international organizations who were publicly neutral, such as the World Bank, International Monetary Fund, Financial Action Task Force, UN Ad Hoc Group of Experts on International Cooperation in Tax Matters, and UN Office on Drugs and Crime; nongovernmental organizations and think tanks like Oxfam and the Center for Freedom and Prosperity; and academia and the media. The strongest degree of confirmation is given when different sources of evidence converge on a common picture or explanation. For instance, public and private (interview) sources from opponents and supporters of the OECD, as well as relatively independent third parties, agree that Bush administration criticism of the OECD in May 2001 was a product of ideologically motivated persuasion rather than corporate pressure. Often (and unsurprisingly) interviewees were more willing to admit errors committed by their own government or international organization than representatives of those same institutions did in public. For example, in public and in private opponents, third parties, and supporters outside the OECD itself agreed that the OECD was losing the rhetorical contest in 2000–2001, and that changes to the initiative around this time marked a major backdown. Private sources inside the OECD also square with this picture, but in public the organization has insisted that there were only "misunderstandings," and that the changes merely served to "refocus" the initiative. In line with the OECD's obvious interest in putting the best face on a bad situation, its public statements need to be heavily discounted in this context.

In engaging with the evidence, the first step is to derive the maximum number of observable implications from each element of the argument. These are than tested against material on the public record and interview evidence, with mutually confirming streams of independent evidence indicating strong support for a particular proposition.[5] The depth of interviews and fieldwork also allows for a detailed investigation of the process of policy implementation rather than just policy formulation.[6] Where appropriate, a competitive test of explanations against available evidence is performed, particularly in chapter 2, with regard to corporate power. Nonetheless, this book is not based on a winner-take-all battle royal between constructivist and rationalist alternatives. In one sense the book is a single case study. But "what is a case?" is more a question of approach than a given. And, as noted above, the book concentrates on maximizing observations for testing rather than simple description.[7]

Argument Summary

The main response to international tax competition has taken the form of a struggle between the OECD, on one hand, and three dozen small tax haven jurisdictions, on the other. I trace the course of this struggle as the large states delegated the conduct of the campaign to the OECD, which attempted to induce tax havens to reform their tax and financial codes in line with an OECD-devised blueprint. The stakes for both sides were high, including hundreds of billions of dollars of tax revenue each year for OECD member states, and a crucial source of economic viability for targeted small states. Despite their power, the large-state coalition failed in its central goal of preventing tax havens from using tax concessions to attract foreign investment.

It is necessary to explain not only the nature of the struggle but also why the contest was rhetorical and not a test of corporate lobbying or of economic or, worse, military strength. My goal is to explain how the striking outcome (small states prevailing over powerful ones) came about as it did, and why the rhetorical struggle went in favor of the tax havens as opposed to the OECD. Reputational issues are central to this story.

Regulative norms, generally shared conceptions of appropriate behavior, limited the scope of the struggle by ruling out certain means as illegitimate or unbecoming for members of the international community. Most prominently this included the use of military force, even though tax havens were essentially defenseless. However, these normative prohibitions also extended to the use of economic coercion. Unlike the clear and unambiguous prohibition of gunboat diplomacy, economic coercion is less strictly regulated by norms. Why did norms rule out economic pressure in this context? This strange reluctance to use materially efficient means, despite the presence of only an uncertain normative restraint, is explained by a determined rhetorical campaign waged by targeted states, the Commonwealth secretariat, and certain

U.S. lobby groups. This campaign persuaded key decision-makers to interpret the issue of economic coercion in terms of the principle of nonintervention, instead of the OECD's preferred parlance of legitimate "defensive measures." Another factor was uncertainty within the OECD secretariat itself over whether sanctioning small, developing nonmember economies really constituted appropriate behavior for a community of experts charged with furthering international prosperity and amity. Regulative norms of varying scope and specificity thus ensured that the conflict did not take the form of a military showdown or a campaign of economic coercion.

An alternative explanation might be that business interests, acting to protect their tax shelters, were crucial in sabotaging the OECD campaign. Although superficially plausible, a close investigation of the evidence fails to support this view. Corporate interests were deliberately shut out in the formative stages of the initiative, when they otherwise might have had most influence. Big business subsequently failed to mount a lobbying campaign along the lines of those conducted in response to other international tax policy issues. Interview evidence from participants on all sides, particularly relating to developments in Washington, also tends to disconfirm the existence of a powerful behind-the-scenes business lobbying effort.

Instead, the contest took the form of a rhetorical battle. Each side tried to associate itself with a few generally accepted principles, while accusing opponents of transgressing these principles. The resulting debate coalesced around several themes. The OECD portrayed the havens as "poaching" taxes rightfully belonging to others and facilitating criminal activities. It further claimed the role of the reasonable, enlightened interlocutor and champion of fair competition or the "level playing field." Conversely, those resisting the initiative characterized it as a coercive and hypocritical exercise in big-power bullying by states and organizations that sought to rewrite the rules of international economic competition in their own favor. Targeted jurisdictions claimed that they were the real guardians of fair competition and accused the OECD of being uninterested in genuine dialogue and reasoned debate. Detailing the course of the debate raises the question of why states or other international actors should care about being seen to be in the wrong, or why they should devote energy to putting their opponents in this position. In both cases the answer is reputation.

Although eschewing the use of economic sanctions, the OECD could exert pressure on targeted jurisdictions by formally blacklisting them. Rather than empty bombast ("mere rhetoric"), this approach threatened tax havens in an extremely sensitive area: their reputation in the eyes of international investors. Tax havens spent (and spend) a great deal of effort trying to project an image of stability, security, and probity to potential foreign investors, and negative judgments by authoritative international actors threatened to wreck these carefully cultivated reputations. Blacklisting is in itself an action that brings about a change in the condition of the referent. Rather than being a description or signal for an action that changes some part of the world, blacklisting *is* an action that changes some part of the world. In this context, once jurisdictions were blacklisted, their reputations were changed. They were left vulnerable to capital flight because third party investors were more likely to either avoid or withdraw from listed states.

Targeted jurisdictions countered with a more indirect strategy. They declared that the OECD was in violation of the very same principles it was created to uphold, particularly the virtues of market competition and the need to bring about change by consensus. Opponents sought to delegitimize the organization, win the sympathy of third parties, and split the coalition of states arrayed against them. By 2002 they had achieved these aims. The OECD had to be sensitive to what others thought of it, as it was dependent on its narrow functional identity and reputation to achieve policy influence in the absence of other means (such as conditional loans), and to convince its members who paid the bills that they were getting value for their money. To the extent that third parties were persuaded by targeted states and other critics that the OECD was being untrue to its own values and was acting inappropriately in the tax competition campaign, the OECD suffered a loss of institutional standing that directly reduced its effectiveness. The authority of the OECD depends on its being perceived as an impartial, expert, rational-legal bureaucracy. The OECD couldn't afford to ignore the verdict of the rhetorical contest. The OECD backed down not only because it feared negative consequences in the future but also because by 2000–2002 there were signs that these consequences already existed. The tide of opinion ran against the initiative, and the previous dominance of the OECD's Committee on Fiscal Affairs in setting international tax standards came under threat from newly created competitors.

The secretariat and member states also faced internal pressures and had to decide on the appropriate, rather than just the instrumentally optimal, course of action. With the unexpectedly tough resistance to the campaign, doubts emerged within the OECD secretariat about whether the organization should be in the business of imposing its recommendations on nonmembers instead of seeking to persuade them. Canada, Australia, and New Zealand came to favor a more consensual solution without blacklisting or sanctions—in part because of Commonwealth links with tax havens. Finally, Caribbean jurisdictions made common cause with conservative think tanks in Washington, such as the Center for Freedom and Prosperity, which convinced congressmen, senators, and new political appointees to the Bush administration Treasury Department to withdraw U.S. support for the campaign in May 2001.

Given the particular restrictions that applied to the OECD and the eventual result, it may be asked why core states did not foresee these problems and choose a different institutional steward. However, the weaknesses of the OECD that eventually stymied the campaign were the same qualities that had initially recommended it: its reputation for technical expertise and impartiality and, most of all, its ability to facilitate consensus among its members on sensitive topics. In 1996 securing a common position on tax regulation that the United States, France, Germany, Britain,