Review of *Taxation in a Global Economy*, by Andreas Haufler.

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Taxation in a Global Economy. By Andreas Haufler. Cambridge; New York, and Melbourne: Cambridge University Press, 2001. Pp. xii, 340. $65.00. ISBN 0-521-78276-7.

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For as long as economics has been a serious subject it has wrestled with the appropriate role of competition in determining economic outcomes. In the modern era this issue appears and reappears in the context of tax competition. Supporters of tax competition between national governments, between states or provinces within countries, or between jurisdictions within states and provinces, tout the effects of competition in disciplining governments and point to the Tiebout hypothesis that, in certain circumstances, interjurisdictional competition leads to efficient outcomes. Opponents worry that unbridled tax competition produces “race-to-the-bottom” outcomes that generate inefficient tax structures and suboptimal government sizes; such concerns commonly lead to prescriptions that governments should coordinate, or even harmonize, their tax systems.

These issues are of great concern to policy makers and of growing interest to researchers. As a result, there has been a vast increase in international tax research in the last twenty years or so. The goals of this research have been to identify the impact of tax systems and international tax differences on economic outcomes, to understand the conditions under which competition produces tax regimes that promote efficiency, and to evaluate existing institutional arrangements such as tax federations and tax treaty networks. While there has been a very great deal written on these topics, the reader interested in thoughtful surveys of this research still has very few places to turn.

Into this breach steps this fine book by Andreas Haufler. The focus of the book is on identifying the impact of tax competition in a variety of settings, and with a variety of taxes. As is appropriate, much of the book is devoted to explicating the assumptions and implications of various workhorse models of tax competition that have appeared in journal articles over the last 20 years. This is a large literature, often confusing, and sometimes confused, so Haufler’s clear exposition and straightforward treatment of these models (including working through some examples) is most welcome. The book motivates its analysis by considering policy issues raised by international tax competition and the reactions of governments in practice. This is followed by an analysis of models that are, to greater and lesser degrees, relevant to the policy issues. These models then form the basis of subsequent cautious conclusions about economic policy. Brief mention is made of the empirical literature on international taxation along the way, but the weight of the analysis and the real contribution of the book lie in using relatively simple models to consider the process of competition and to enlighten the theoretical findings appearing in the literature.

The basic story is simple enough. Governments of small open economies have incentives not to tax income earned by foreigners who invest in their countries, since such taxes distort production by driving capital abroad and their cost is borne entirely by immobile local factors in the form of lower wages and reduced land prices. From the standpoint of any individual country acting on its own in such a setting, almost any other tax is welfare superior to source-based capital income taxes. If governments nonetheless must rely at least in part on capital income taxes to finance their expenditures, then the distortion associated with the capital taxes gives them incentives to reduce government spending below what would otherwise be the efficient levels. The ability to coordinate capital income taxes between countries makes it possible to overcome this distortion and impose source-based taxes without enormous costs to the taxing government, thereby making it possible to restore efficient government spending levels.

The book, and a good deal of the literature, extend this basic story in several directions, including by considering tax competition between countries of different sizes, the effect of tax competition on income distribution, and the impact of profit shifting by taxpayers. The analysis also entertains the possibility that tax competition serves an important function in disciplining governments that do not always act in the interest of their own citizens. The commodity tax chapters are similar: they start with the simple problems created by lack of uniformity among countries, then layer on additional complexities. Most of the complications stem from the fact that tax policies affect relative prices, and therefore can be used to move the terms of trade in favor of chosen countries or groups within the population. Some of the best and most innovative material in the book comes in the analysis of these extensions to the standard theory, particularly its analysis of the issues raised by policy transitions, interactions of different distorting taxes, and taxation in the presence of imperfect competition.

It is fair to say that there is a European look and feel to the book, and not just because its author is European and its publisher Cambridge University Press. The focus of the book is on applications of theory to policy problems that are prominent in Europe, such as cross-border shopping, the relocation of foreign direct investment, and the implications of tax competition for income distribution. Many pages are lavished on commodity tax competition. The chapters on policy issues and policy conclusions consider European developments almost exclusively; four paragraphs in the book discuss issues facing the United States, Canada gets one, and the rest of the world two (total). There is nothing wrong with finding the answers to European policy problems, and doubtless European insights could be applied elsewhere, but the reader looking for something—anything—about most of the world will come up empty.

People who care about international tax issues want—or should want—analysis that combines theoretical and empirical insights. The book devotes only passing and rather uncritical attention to empirical research, instead using sensible empirical observations to motivate the theoretical analysis of tax problems. If one seeks an understanding of the empirical issues in international taxation, or an introduction to the copious empirical literature, this is not the place to find it. If, on the other hand, one wants to understand the state of the applied theory of international tax competition, this book is an excellent place to go. It is well written, comprehensive, and sensibly reasoned throughout. It is useful not only for those who want to learn about this area for the first time, but also for experienced researchers in this area who might be loathe to admit just how valuable this book really is.

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