
Article

Does International Law Matter?

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INTRODUCTION

International law has grown both in significance and volume in recent decades.¹ In this increasingly interdependent world, an important question is whether international law matters.² Despite the criticisms aimed at the effectiveness of international law,³ and the challenges of its enforcement,⁴ there is a

1. Curtis A. Bradley & Jack L. Goldsmith, *Customary International Law as Federal Common Law: A Critique of the Modern Position*, 110 HARV. L. REV. 815, 821 (1997) (stating that our society is “increasingly governed by international law”); Paul B. Stephan, *Privatizing International Law*, 97 VA. L. REV. 1573, 1626 (2011) (“[T]he growth of international law has meant an increase in its domain.”); Edith Brown Weiss, *The Rise or the Fall of International Law?*, 69 FORDHAM L. REV. 345, 351 (2000) (“[B]inding international legal instruments have greatly increased, nonbinding international legal instruments concluded by governments and international intergovernmental organizations have become very significant sources of international law. Moreover, the private sector has concluded important transnational instruments.”).

2. LOUIS HENKIN, *HOW NATIONS BEHAVE: LAW AND FOREIGN POLICY* 47 (2d ed. 1979) (“[A]lmost all nations observe almost all principles of international law and almost all of their obligations almost all of the time.”); George W. Downs et al., *Is the Good News About Compliance Good News About Cooperation?*, 50 INT’L ORG. 379, 379 (1996) (explaining that the message from political scientists and scholars is that a high level of compliance with international law is achieved “with little attention to enforcement”); Jack L. Goldsmith & Eric A. Posner, *A Theory of Customary International Law*, 66 U. CHI. L. REV. 1113, 1113 (1999) (“Governments take care to comply with [customary international law] and incorporate its norms into domestic statutes.”); Oona A. Hathaway, *Do Human Rights Treaties Make a Difference?*, 111 YALE L.J. 1935, 1937 (2002) (noting that international lawyers most often assume that nations observe international law); Laurence R. Helfer & Anne-Marie Slaughter, *Toward a Theory of Effective Supranational Adjudication*, 107 YALE L.J. 273, 276 (1997) (“Supranational adjudication in Europe is a remarkable and surprising success . . . [B]oth [the European Court of Justice and the European Court of Human Rights] developed successful strategies to make their judgments as effective, for the most part, as national court rulings.”); Harold Hongju Koh, *Why Do Nations Obey International Law?*, 106 YALE L.J. 2599, 2600–01 (1997) (reviewing ABRAM CHAYES & ANTONIA HANDLER CHAYES, *THE NEW SOVEREIGNTY: COMPLIANCE WITH INTERNATIONAL REGULATORY AGREEMENTS* (1995) and THOMAS M. FRANCK, *FAIRNESS IN INTERNATIONAL LAW AND INSTITUTIONS* (1995)) (noting an increasing perception that international law matters).

3. See Eric Lane, *Mass Killing by Governments: Lawful in the World Legal Order?*, 12 N.Y.U. J. INT’L L. & POL. 239 (1979) (arguing that international agreements are ineffective at preventing a government from killing its own citizens); John J. Mearsheimer, *The False Promise of International Institutions*, 19 INT’L SECURITY 5, 7 (1994–1995); J.S. Watson, *Legal Theory, Efficacy and Validity in the Development of Human Rights Norms in International Law*, 1979 U. ILL. L.F. 609, 626–35 (arguing that states often speak like they

belief that international law carries weight.⁵ This shared belief underlies the work of international scholars and lawyers who debate about how to make international law more effective.⁶

will follow international law, but their actions indicate the contrary); Jack Goldsmith, *Sovereignty, International Relations Theory, and International Law*, 52 STAN. L. REV. 959, 963 n.13 (2000) (reviewing STEPHEN D. KRASNER, *SOVEREIGNTY: ORGANIZED HYPOCRISY* (1999)) (“Realists are skeptical about cooperation among nations . . . and [believe] that the little cooperation we see is fragile.”).

4. See David S. Ardia, *Does the Emperor Have No Clothes? Enforcement of International Laws Protecting the Marine Environment*, 19 MICH. J. INT’L L. 497, 508–16 (1998) (discussing difficulties in enforcing international environmental agreements); Emeka Duruigbo, *International Relations, Economics and Compliance with International Law: Harnessing Common Resources to Protect the Environment and Solve Global Problems*, 31 CAL. W. INT’L L.J. 177, 189–93 (2001) (arguing that costs associated with compliance and reporting on compliance with international regulations make enforcement difficult); Richard A. Falk, *On Identifying and Solving the Problem of Compliance with International Law*, 58 AM. SOC’Y INT’L PROC. 1, 1 (1964) (arguing that enforcement is difficult because of uncertainty as to the legal rules and procedures governing state behavior); cf. Günther Handl, *Compliance Control Mechanisms and International Environmental Obligations*, 5 TUL. J. INT’L & COMP. L. 29, 30–31 (1997) (arguing that as complexity of the international regime and cost of compliance increase, there is a greater need for compliance control); Christopher C. Joyner, *Sanctions, Compliance and International Law: Reflections on the United Nations’ Experience Against Iraq*, 32 VA. J. INT’L L. 1, 34 (1991) (noting that nations may violate international laws where cost outweighs the benefit of compliance).

5. Cf. Douglass Cassel, *Does International Human Rights Law Make a Difference?*, 2 CHI. J. INT’L L. 121, 122 (“[I]nternational human rights law has shown itself to be a useful tool . . . [and] has brought incalculable, indirect benefits for rights protection.”). There is also a debate about compliance with international laws because of imprecise definitions. See Ardia, *supra* note 4, at 512 (explaining that those who are charged with implementation of environmental treaties have difficulties because their duties are imprecisely defined); Christopher Greenwood, *Ensuring Compliance with the Law of Armed Conflict*, in CONTROL OVER COMPLIANCE WITH INTERNATIONAL LAW 195, 200–01 (William E. Butler ed., 1991) (arguing that nations cannot effectively comply with the law of naval warfare because it lacks clarity regarding modern technologies and situations); Goldsmith & Posner, *supra* note 2, at 1114–15.

6. See generally Abram Chayes & Antonia Handler Chayes, *On Compliance*, 47 INT’L ORG. 175 (1993) (noting that the assumption that underlies their argument is that nations have a propensity to comply with international law and arguing that a shift in focus towards managing sources of noncompliance with “routine international political processes” can improve compliance with international law); Beth A. Simmons, *Compliance with International Agreements*, 1 ANN. REV. POL. SCI. 75 (1998) (noting an increase in voluntary compliance and examining four possible explanations); Koh, *supra* note 2, at 2599–603 (noting that scholars believe international law matters and advance an argument about why nations obey it).

There is a vast literature focused on international compliance.⁷ This literature suffers from two major weaknesses in determining the effectiveness of international law. First, the current theories of international law inappropriately concentrate on states rather than individuals. Whether international law is ultimately effective in accomplishing its goals may depend less on whether a state complies and more on whether sub-state entities act consistently with the goals of international law. This misplaced focus on nations as the primary actors in international law neglects key players in international law: individuals and firms. Nations comply with international law by passing laws and enforcing those laws. Individuals and firms comply with international law by following rather than violating such laws.⁸ Indeed, even though international law imposes duties on nations, the effectiveness of international law depends in large measure on the actions of private individuals, who ultimately determine whether international law is effective.⁹

Second, there is no agreement on what motivates compliance with international law.¹⁰ Two major theoretical camps

7. See *supra* notes 2–5.

8. Technically, individuals or private firms cannot comply with international law as it does not bind private actors, only nation states. Individuals and firms can only act consistently with the dictates of international law. However, for simplicity, throughout this article, we refer to this behavior as “compliance” with international law.

9. See LUNG-CHU CHEN, AN INTRODUCTION TO CONTEMPORARY INTERNATIONAL LAW 76–80 (2d ed. 2000) (noting the role of individuals and that realistically individuals are the ultimate actors within international law); THOMAS M. FRANCK, FAIRNESS IN INTERNATIONAL LAW AND INSTITUTIONS 86 (1995) (“To be effective . . . law needs to secure the habitual, *voluntary* compliance of its subjects; it cannot rely entirely, or even primarily, upon the commanding power of a sovereign to compel obedience.”); Helfer & Slaughter, *supra* note 2, at 308–12 (noting supranational courts that have been successful in focusing on individual litigants).

10. See generally ABRAM CHAYES & ANTONIA HANDLER CHAYES, THE NEW SOVEREIGNTY: COMPLIANCE WITH INTERNATIONAL REGULATORY AGREEMENTS (1998) (arguing that a “managerial model” of compliance in which nations cooperate in a problem solving approach to problems should replace the coercive theories that say nations comply because of sanctions); FRANCK, *supra* note 9, at 7–8 (arguing that international rules perceived as fair are considered more legitimate and are therefore followed more frequently); HANS J. MORGENTHAU, POLITICS AMONG NATIONS: THE STRUGGLE FOR POWER AND PEACE 3–4 (4th ed. 1967) (acknowledging his use of realist political theory in explaining international compliance); Thomas M. Franck, *Legitimacy in the International System*, 82 AM. J. INT’L L. 705, 706 (1988) (arguing that compliance with international law is secured by belief in the legitimacy of the rule, which requires a belief that the rule came into existence through right process); Andrew T. Guzman, *A Compliance-Based Theory of International Law*, 90 CALIF. L. REV.

disagree fundamentally on what causes international compliance: sanctions or norms. Proponents of rationalism believe that nations comply because they fear sanctions or other repercussions when they do not comply.¹¹ On the other side, constructivists argue that nations comply with international law because they want to follow norms and behave appropriately.¹² These opposing frameworks offer two motivations for complying with international law.¹³ The same motivations arguably exist with private actors deciding whether to act consistently with international law. Testing these theories on actors to determine whether norms or sanctions induce compliance—and then exploiting those motivations—could potentially increase the effectiveness of international law.

1823, 1836–40 (2002) [hereinafter Guzman, *Compliance-Based*] (explaining an emerging theory known as international relations theory); Andrew T. Guzman, *Rethinking International Law as Law*, 103 AM. SOC'Y INT'L L. PROC. 155, 155–56 (2009) (noting that a key question in international law is “how well does international law do in its effort to influence state behavior”); Robert O. Keohane, *International Relations and International Law: Two Optics*, 38 HARV. INT'L L.J. 487, 488–94 (1997) (describing the competing “instrumentalist optic” and “normative optic” compliance theories); Benedict Kingsbury, *The Concept of Compliance as a Function of Competing Conceptions of International Law*, 19 MICH. J. INT'L L. 345 (1998) (examining various compliance in the context of theories of law because the concept of compliance does not stand alone, but depends on the theory behind it); John K. Setear, *Responses to Breach of a Treaty and Rationalist International Relations Theory: The Rules of Release and Remediation in the Law of Treaties and the Law of State Responsibility*, 83 VA. L. REV. 1 (1997) (examining breach and compliance with international law from a rationalist perspective of international relations); Beth A. Simmons, *Money and the Law: Why Comply with the Public International Law of Money?*, 25 YALE J. INT'L L. 323 (2000) (examining international compliance with the laws governing money and arguing that nations commit to comply with international law when it is credible and plausible that they can commit).

11. See Kingsbury, *supra* note 10, at 350–56 (describing rationalist theories of international compliance); cf. Charles Lipson, *Why Are Some International Agreements Informal?*, 45 INT'L ORG. 495, 518–19 (1991) (arguing that informal agreements are used in order to avoid the reputational costs of non-compliance associated with treaties).

12. See Kingsbury, *supra* note 10, at 358–60 (describing constructionist theories of international compliance); Dinah Shelton, *Editor's Concluding Note: The Role of Nonbinding Norms in the International Legal System*, in COMMITMENT AND COMPLIANCE 554, 556 (Dinah Shelton ed., 2000) (discussing how norms lead to soft law compliance).

13. Kingsbury, *supra* note 10, at 368 (“[T]he differences of view about the relations of international law to behavior are such that the concept of compliance with international law . . . must be given meaning by reference to authority . . .”). *But see* Kenneth W. Abbott & Duncan Snidal, *Hard and Soft Law in International Governance*, 54 INT'L ORG. 421 (2000) (arguing that actors take both rational incentives and normative processes into account).

Despite the importance of determining why private actors comply with international law, no scholars have ever tested the motivations for private actors complying with international law. And while the two camps have robust theoretical bases to back their beliefs, both rationalists and constructivists lack strong empirical support.¹⁴ The existing studies cannot determine actual compliance because they often suffer from selection bias and a myopic focus on nations rather than other actors.¹⁵ Indeed, neither theory of compliance has been tested internationally in ways that can establish the causality of actors' compliance.

Because of its ability to uncover those causal effects, a large-scale international field experiment is one way to answer these questions.¹⁶ Thus far, however, no experimental studies

14. See, e.g., James G. Apple, *Enforcement of International Law Is Not Dependent on a "Sword" or Enforcement Mechanism*, INT'L JUD. MONITOR (Jan./Feb. 2007), http://www.judicialmonitor.org/archive_0207/generalprinciples.html (discussing three instances in which countries submitted to an international court's authority: Libya's submission to a decision handed down by the International Court of Justice in 1994, Russia's submission to a decision offered by the European Court of Human Rights in 2006, and seventy-nine out of eighty countries submitting to World Trade Organization Appellate Body decisions through 2006); David D. Cardon, *Does International Law Matter?*, 98 AM. SOC'Y INT'L L. PROC. 311, 312 (2004) (explaining that while certain, specific laws were broken, the laws of war were largely adhered to during the Ethiopian-Eritrean War, which took place between 1998 and 2000); Duruigbo, *supra* note 4, at 183–84 (2001) (reporting "impressive" compliance by 1991 with the 1973 International Convention for the Prevention of Pollution from Ships); Elias N. Stebek, *ICJ Judgment (1994) on the Libya/Chad Territorial Dispute: A Brief Overview and Observations*, 3 MIZAN L. REV. 167, 178 (2009) (discussing Libya's submission to a decision handed down by the International Court of Justice in 1994).

15. The cross-national comparisons that exist are typically limited to a certain time period, geographic region, or set of events. Consequently, they shed little insight on the current global state of international law compliance. See Hiram E. Chodosh, *Comparing Comparisons: In Search of Methodology*, 84 IOWA L. REV. 1025, 1038–40 (1999) (discussing the value of comparisons of international laws but lamenting the lack of good studies due to methodological failures).

16. Since the 1960s, social scientists have increasingly used field experiments to explore what motivates individuals to act in specific situations. Specifically, scholars rely on field experiments to study theories on economics, social and criminal behavior, and political economy. See, e.g., Hans P. Binswanger, *Attitudes Toward Risk: Theoretical Implications of an Experiment in Rural India*, 91 ECON. J. 867 (1981) (describing a field experiment to test the theories on the economics of development and attitudes toward risk); Stanley Divorski et al., *Public Access to Government Information: A Field Experiment*, 68 NW. U. L. REV. 240 (1973) (looking at the extent to which information was available from state and local governments); Alan S. Gerber et al., *How Large and Long-Lasting Are the Persuasive Effects of Televised Campaign*

have investigated key theoretical questions such as compliance with international law.¹⁷ Through a randomized international field experiment where we used aliases and posed as international consultants seeking a shell corporation, we assessed the causes of compliance with international financial transparency laws through assigning more than 1000 firms to a variety of treatment and control conditions. The results of this global experiment reveal several interesting and significant findings with potential importance for international law and policy.

In examining whether international law matters, our empirical findings reveal that compliance with international law is 51% at best, as fewer than half the contacted firms complied with financial transparency standards. It turns out that informing firms about the relevant international laws or norms to comply with these laws does not increase the likelihood that firms will actually comply. And surprisingly, informing firms

Ads? Results from a Randomized Field Experiment, 105 AM. POL. SCI. REV. 135, 138–42 (2011) (studying the effect of campaign ads on political behavior); Donald P. Green et al., *Does Knowledge of Constitutional Principles Increase Support for Civil Liberties? Results from a Randomized Field Experiment*, 73 J. POL. 463 (2011) (studying knowledge of constitutional law and political behavior); Gary S. Green, *General Deterrence and Television Cable Crime: A Field Experiment in Social Control*, 23 CRIMINOLOGY 629, 636 (1985) (detailing a field experiment to determine how well a legal threat deters people from committing television signal theft, and finding that two-thirds ceased the illegal practice after receiving notice); Donald P. Hartmann et al., *Rates of Bystander Observation and Reporting of Contrived Shoplifting Incidents*, 10 CRIMINOLOGY 248, 258 (1972) (finding that half of those who did not report crimes in violation of local law described that reporting would have been impractical in some way); Macartan Humphreys & Jeremy M. Weinstein, *Field Experiments and the Political Economy of Development*, 12 ANN. REV. POL. SCI. 367, 370 (2009) (using field experiments to study the political economy of development projects because development agencies and implementing organizations find themselves under pressure to show that their interventions are effective); Richard D. Schwartz & Sonya Orleans, *On Legal Sanctions*, 34 U. CHI. L. REV. 274, 284 (1966) (explaining a field experiment designed to assess tax compliance).

17. There have been several local randomized field experiments measuring international organizations' interventions in local affairs. See James D. Fearon et al., *Can Development Aid Contribute to Social Cohesion After Civil War? Evidence from a Field Experiment in Post-Conflict Liberia*, 99 AM. ECON. REV. 287, 289–90 (2009) (evaluating the effect of a community-driven reconstruction program by the International Rescue Committee in northern Liberia and finding that post-conflict development aid can have a measurable impact on social cohesion); Mary Kay Gugerty & Michael Kremer, *Outside Funding and the Dynamics of Participation in Community Associations*, 52 AM. J. POL. SCI. 585, 589–91 (2008) (finding little evidence that outside funding increased organizational strength of organizations comprised of poor and disadvantaged individuals).

about penalties actually *increases* the likelihood that the firms who respond will violate international law. Thus, norms do not seem to matter and reference to penalties sometimes causes more international law violations. This study also demonstrates a gap between state compliance and private firm behavior and identifies what motivates firms to decide to act consistently with the goals of international law.

This Article unfolds in three parts. Part I sets forth the two dominant theories of compliance with international law, rationalism and constructivism, then introduces the preeminent debate in international law: does international law matter? Part II sets forth the design and results of an experiment considering whether and why individuals comply with international law. Generally speaking, is compliance motivated by fear of sanctions or a sense of duty to accepted norms? We demonstrate, with systematic data whose results may be surprising to both camps of international law theorists, that compliance is lower than expected, despite the importance of such laws on an international level. Part III examines the results of this field experiment in light of the theories of international law, juxtaposing the findings with potential explanations for the counterintuitive results we encounter. Informing firms about the relevant international law does not increase the likelihood that firms will actually comply, and indeed invoking penalties actually motivates some actors to break international law in greater numbers. To provide an explanation for these results, we set forth two new theories of rationalism, which we call the conspirator effect and the weak penalty effect. Under the conspirator effect, the willingness of firms to violate international law is influenced by clients who are willing to conspire in violating international law. The weak penalty effect is that weak international penalties induce lower compliance than a lack of international penalties.

I. THEORIES OF COMPLIANCE

While scholars have criticized the divisions used to explain international law and relations theories,¹⁸ many have relied on

18. See Colin Wight, *Philosophy of Social Science and International Relations*, in *HANDBOOK OF INTERNATIONAL RELATIONS* 23, 24 (Walter Carlsnaes et al. eds., 2002) (noting that these problems include “a bar to constructive dialogue; a hindrance to much-needed research into issues of vital concern; a confused misrepresentation of the issues; and most importantly, a construct of those working in the field.”).

them to explain what motivates compliance with international law. The prevailing theories can roughly be divided into two opposing frameworks: rationalism and constructivism.¹⁹ Rationalists generally believe that nations comply with international law when faced with material sanctions. Constructivists believe that nations comply with international law when the international community sets norms that become broadly accepted. After providing a broad framework for these theories, we make a case that both theories have a misplaced focus on states as the primary actors in international law.

A. RATIONALISM

Rationalists believe that nations only comply with international law when they seek to avoid sanctions or obtain material benefits.²⁰ Rationalism relies formally and informally on rational choice theory, and an explanation of foreign policy through self-interested,²¹ goal seeking behavior.²² Instead of accepting a traditional belief that international law is a powerful check on state behavior, rationalists argue that international law is merely the result of states acting logically to maximize their interests.²³ Rationalists explain state compliance with in-

19. There are more than a dozen distinctions and sub-theories of rationalism and constructivism that are not discussed here. See, e.g., SCOTT BURCHILL ET AL., *THEORIES OF INTERNATIONAL RELATIONS* 105 (4th ed. 2009) (noting a distinction between realism and idealism within rationalism); Emanuel Adler, *Seizing the Middle Ground: Constructivism in World Politics*, 3 *EUR. J. INT'L REL.* 319, 335–36 (1997) (dividing constructivism into four separate camps).

20. Rationalists do not ever “comply” with international law for its own sake, but act consistently with it when compelled. See Judith Goldstein et al., *Introduction: Legalization and World Politics*, 54 *INT'L ORG.* 385, 391–92 (2000). Neoliberal institutionalists generally believe that compliance with international law can be quite high. Simmons is the best example, but there are many others, like Keohane, Snidal, and Abbott, who believe that nations generally comply. See e.g., Simmons, *supra* note 6, at 75.

21. See Anthony Clark Arend, *Do Legal Rules Matter? International Law and International Politics*, 38 *VA. J. INT'L L.* 107, 121–22 (1997–1998).

22. See James Fearon & Alexander Wendt, *Rationalism v. Constructivism: A Skeptical View*, in *HANDBOOK OF INTERNATIONAL RELATIONS*, *supra* note 18, at 54–55.

23. See JACK L. GOLDSMITH & ERIC A. POSNER, *THE LIMITS OF INTERNATIONAL LAW* 3–5 (2005). Some rationalists are realists and believe that a state's primary interest is protecting security interests. See Arend, *supra* note 21, at 124; Goldsmith, *supra* note 3, at 963; see also Tom Ginsburg & Richard H. McAdams, *Adjudicating in Anarchy: An Expressive Theory of International Dispute Resolution*, 45 *WM. & MARY L. REV.* 1229 (2004) (explaining with game theory why countries would comply with decisions rendered by international courts).

international law as a result of either a nation's desire to profit materially or a nation's fear of sanctions. Since states are treated like individual actors, rationalists argue that penalties motivate states to act.²⁴

Rationalists assume that states are the primary actors in the international system.²⁵ As such, states are treated as individual actors that make rational decisions regarding international law and their relations with other states according to a cost-benefit analysis.²⁶ Rationalists largely treat the effects of the international social structure on state interests as "exogenously given."²⁷ Accordingly, state interests are best understood by analyzing the internal conditions or external threats or benefits faced by given states rather than outside social considerations.²⁸

Because self-interest guides nations' decision-making and there are only minor risks of international sanctions with weak and limited enforcement,²⁹ some rationalists posit that compli-

24. This can be analogized to individual actors who are also motivated by the threat of penalties. See Joanne M. Miller & Jon A. Krosnick, *Threat as a Motivator of Political Activism: A Field Experiment*, 25 POL. PSYCHOL. 507, 513-14 (2004) (describing a study showing greatest response from subjects when their political values were threatened).

25. Individualists believe that social structures can be reduced to the independent actions of agents. See ALEXANDER WENDT, *SOCIAL THEORY OF INTERNATIONAL POLITICS* 26 (Steve Smith et al. eds., 1999). But see Arend, *supra* note 21, at 118-19 (citing Robert O. Keohane, *International Institutions: Two Approaches*, 32 INT'L STUD. Q. 379, 386 (1988)); Edward Rubin, *Rational States?*, 83 VA. L. REV. 1433, 1451 (1997) ("Treating collective entities as individuals, with motivations, plans, strategic responses, and the other accouterments of rational actor theory, is extremely convenient. It is much easier than trying to construct their behavior from the behavior of the real individuals who comprise them.").

26. See Uta Oberdörster, Note, *Why Ratify? Lessons from Treaty Ratification Campaigns*, 61 VAND. L. REV. 681, 685 (2008).

27. Arend, *supra* note 21, at 124. But see WENDT, *supra* note 25, at 34; Fearon & Wendt, *supra* note 22, at 56 (arguing that the microeconomic concept of equilibrium is a manner in which rationalism accounts for structure that impinges and influences actors); Oberdörster, *supra* note 26, at 687 (discussing rationalists that argue that the creation of institutions and regimes can independently influence state behavior).

28. See Oona A. Hathaway, *Between Power and Principle: An Integrated Theory of International Law*, 72 U. CHI. L. REV. 469, 479 (2005) ("[These models] share at least two key assumptions: states engage in consequentialist means-end calculations, and state interests can be deduced from the state's material characteristics and the objective conditions it faces.").

29. See Robert A. Pape, *Why Economic Sanctions Do Not Work*, 22 INT'L SECURITY 90, 109 (1997) ("Sanctions have been successful less than 5% of the time.").

ance with international law is limited.³⁰ Thus, as Jack Goldsmith and Eric Posner argue, “nations mouth their agreement to popular ideals as long as there is no cost in doing so, but abandon their commitments as soon as there is a pressing military or economic or domestic reason to do so.”³¹ First, and fundamentally, critics claim that rationalism does not explain how a state determines its interest.³² Some perceive rational choice theory to be circular because the theory explains that a state acts the way it does because the state is pursuing its interests, but determines the state’s interest according to the actions that a state performs.³³ Without guiding principles for a state acting the way it does, rationalism has little explanatory power.³⁴

Second, critics fault rationalism for failing to adequately explain why states consistently enter into and abide by treaties that offer little or no apparent benefit.³⁵ For instance, many states accede to and abide by human rights treaties.³⁶ While

30. See GOLDSMITH & POSNER, *supra* note 23, at 36–37, 87–88.

31. See Jack L. Goldsmith & Eric A. Posner, *Understanding the Resemblance Between Modern and Traditional Customary International Law*, 40 VA. J. INT’L L. 639, 672 (2002).

32. See, e.g., Oona A. Hathaway & Ariel N. Lavinbuk, *Rationalism and Revisionism in International Law*, 119 HARV. L. REV. 1404, 1424 (2006) (suggesting that rationalist theorists should provide information about what interests states pursue in order to better support their theory).

33. See GOLDSMITH & POSNER, *supra* note 23, at 10 (“A successful theory of international law must show why states comply with international law rather than assuming that they have a preference for doing so.”).

34. However, a rationalist response may argue that states serve their interests by increasing benefits and avoiding penalties, with little regard to international norms. The state’s interests are determined by laws that dictate either penalties for noncompliance or benefits for obedience. See Guzman, *Compliance-Based*, *supra* note 10, at 1849 (explaining that a nation’s reputation may be damaged or enhanced by decisions to comply with international law or not; negative effects to reputation serve as penalties and positive effects as benefits). Of course, international penalties and benefits are relevant. See Hathaway, *supra* note 28, at 480 (summarizing a rationalist theory of international law compliance by noting that “states only join treaties [increasing benefits] that require them to act very little differently than they already do [incurring little cost]”).

35. See Hathaway & Lavinbuk, *supra* note 32, at 1427 (arguing that rationalism has “very little” to do with the limits of international law). Assumptions are held “that power and interests matter, that states seek to influence one another in pursuit of often conflicting self-interests, and that self-help through military force is . . . important.” Jeffrey W. Legro & Andrew Moravcsik, *Is Anybody Still a Realist?*, 24 INT’L SECURITY 5, 21 (1999) (internal quotation marks omitted).

36. See Alex Geisinger & Michael Ashley Stein, *A Theory of Expressive International Law*, 60 VAND. L. REV. 77, 78 (2007) (discussing the lack of benefits for states that ratify and abide by human rights treaties).

these treaties impose costs,³⁷ they offer no material benefit to the state.³⁸ It is unclear why a rational state would enter a human rights agreement: a state with a history of human rights compliance would receive no reputational gains,³⁹ and one with a history of abuse would lose much from ratification.⁴⁰ Additionally, rationalists would not agree that a law carries with it a moral sense of obligation to follow it.⁴¹

Thus, according to rationalism, states comply with international law when doing so serves their interests by increasing benefits and avoiding penalties.⁴² International norms are not

37. Hathaway, *supra* note 28, at 479 (“[These treaties] impose substantial sovereignty costs . . .”). A common retort is that entering such treaties is “cheap talk” used by governments to justify their self-interested actions, but the retort fails to explain why “cheap talk” would be valuable. *Id.*; see also EDWARD HALLETT CARR, *THE TWENTY YEARS’ CRISIS: 1919–39*, at 71–75 (2d ed. 1946) (discussing the use of international morality to reflect moral credit on oneself); MORGENTHAU, *supra* note 10, at 11 (“All nations are tempted . . . to clothe their own particular aspirations and actions in the moral purposes of the universe.”); KENNETH N. WALTZ, *THEORY OF INTERNATIONAL POLITICS* 200 (1979) (“Once a state’s interests reach a certain extent, they become self-reinforcing.”).

38. Rationalists argue that states enter such treaties to protect some self-interest, with weaker states feeling coerced by greater states who actually value human rights. See Hathaway, *supra* note 2, at 1946 (“In this view, states comply with human rights norms because they are coerced into doing so by more powerful nations.”). Others explain states complying with international law because of internal pressure created by domestic policies and the costs of possible sanctions. *Id.* at 1946, 1951–52, 1954 (discussing domestic justifications for states entering treaties); see also WALTZ, *supra* note 37, at 136 (“The expected costs of enforcing agreements, and of collecting the gains they offer, increase disproportionately as the group becomes larger.”).

39. But see David H. Moore, *A Signaling Theory of Human Rights Compliance*, 97 NW. U. L. REV. 879, 890–91 (2003) (noting that the damage the United States has suffered from not signing onto various human rights treaties, notwithstanding a history of human rights compliance, suggests otherwise).

40. Harlan Grant Cohen, *Can International Law Work? A Constructivist Expansion*, 27 BERKELEY J. INT’L L. 636, 651–52 (2009) (noting that if a human rights abusing state ratified a human rights treaty, it would harm the state’s reputation for abiding by its agreements).

41. *Id.* at 637, 657–58 (discussing the absence of obligation in rational choice theories). For a theory including moral obligation to the law, see, for example, H.L.A. HART, *THE CONCEPT OF LAW* 89 (1961) (though Hart may not agree that there is necessarily a sense of obligation, but that there may be one); see also FERNANDO R. TESÓN, *A PHILOSOPHY OF INTERNATIONAL LAW* 79, 92–94 (1998) (“What is distinctive about doing our duty is that we are obligated to do it especially when it is costly to us, when doing it frustrates some preference or interest that we have. That is why moral choice cannot be captured by strategic analysis.”).

42. See *supra* note 38 and accompanying text.

relevant except to the extent that following or violating them produces costs or benefits to the state.

B. CONSTRUCTIVISM

Constructivism asserts that states obey international law due to norms.⁴³ To constructivists, international law makes up the structure of the international system: a set of implicit rules upon which meaningful and binding formal agreements are framed.⁴⁴ According to constructivists, states create and follow international law not because of the instrumental benefits or penalties from complying, but because of their moral and social commitment to ideas embodied in treaties.⁴⁵

43. Like rationalism, constructivism encompasses a broad range of theories. WENDT, *supra* note 25, at 1. Constructivism draws from critical theory, postmodernism, feminist theory, historical institutionalism, sociological institutionalism, symbolic interactionism, structuration theory, and others. *Id.* Notably, like with rationalism, constructivism is a broad term wherein much debate rages about what does and should fall beneath its umbrella. However, unlike rationalism, the debate escalates to the point where a single recipe or definition is problematic. See Fearon & Wendt, *supra* note 22, at 56 (“[T]here is a great deal of variation on substantive issues within constructivis[m]”); see also Wight, *supra* note 18, at 34–35 (“[Constructivism] is a very problematic term because there are some very conflicting positions being imported under this label.”). Different scholars have included very conflicting ideas under this same label, raising questions about what it really means. Compare JOHN GERARD RUGGIE, CONSTRUCTING THE WORLD POLITY: ESSAYS ON INTERNATIONAL INSTITUTIONALIZATION 11–28 (1998) (advocating a social constructivist theory that focuses on the nature, origins, and functioning of social facts), with Steve Smith, *Epistemology, Postmodernism and International Relations Theory: A Reply to Østerud*, 34 J. PEACE RES. 330, 333–35 (1997) (defending postmodernist international theories, which challenge assumptions about how knowledge is created). Indeed, some constructivists claim that concern about reputation is a rationalist idea and that constructivists are solely concerned about states acting morally. See, e.g., LARRY MAY, THE MORALITY OF GROUPS (1987) (discussing the effect of social groups, including nation-states, on ethics); LARRY MAY, SHARING RESPONSIBILITY (1992) (arguing that there is a shared responsibility for harms within a community).

44. Arend, *supra* note 21, at 130; see Stephen A. Kocs, *Explaining the Strategic Behavior of States: International Law as System Structure*, 38 INT’L STUD. Q. 535, 538–39 (1994). Kocs has suggested eight constitutive rules. The first three are seen as longstanding principles: “the sovereign equality of states, nonintervention in the affairs of other states, and good faith [pacta sunt servanda].” *Id.* at 539 (citing ANTONIO CASSESE, INTERNATIONAL LAW IN A DIVIDED WORLD (1986)). Five others are seen as more recent: “the self-determination of peoples, prohibition on the threat or use of force, peaceful settlement of disputes, respect for human rights, and international cooperation.” *Id.*

45. Hathaway, *supra* note 28, at 477.

While constructivists focus on social norms and structures,⁴⁶ like rationalists, constructivists focus on states as the central actors in international decision making.⁴⁷ For constructivists, norms and laws exert a profound impact on state behavior, shaping how people think about their state's role and obligations.⁴⁸ Self-interest as the sole motivation is rejected, as constructivists instead believe that states determine their national interests and preferences through the social interaction of individuals, groups, and states.⁴⁹

Constructivists believe international law can modify state preferences.⁵⁰ State interactions create a social structure, which in turn influences state interests.⁵¹ These structures have the ability to influence norms and preferences domestically, to the point where a state's interests reflect the rules of international law.⁵² Accordingly, states are often not convinced that a solution is needed until standards are set by international organizations created and often run by states.⁵³ Constructivists assert that state actors are persuaded by normative arguments that adopt new interests and change behavior.⁵⁴ In a world where

46. MARTHA FINNEMORE, NATIONAL INTERESTS IN INTERNATIONAL SOCIETY 15 (1996) ("They are concerned with the . . . impact of cultural practices, norms of behavior, and social values on political life and reject the notion that these can be derived from calculations of interests."); *see, e.g.*, WENDT, *supra* note 25, at 26 ("People cannot be professors apart from students, nor can they become professors apart from the structures through which they are socialized.").

47. WENDT, *supra* note 25, at 8–9 (arguing that states dictate social relations because they have a practical monopoly on violence).

48. Keohane, *supra* note 10, at 492.

49. OONA A. HATHAWAY & HAROLD HONGJU KOH, FOUNDATIONS OF INTERNATIONAL LAW AND POLITICS 112 (2005) ("[Interests] are constituted or 'constructed' by and through interaction with one another."); Hathaway, *supra* note 28, at 481 ("While acknowledging that state behavior is often motivated by self-interest, normative scholars contend that it is also motivated by the power of principled ideas—ideas that are . . . constructed through interaction among individuals, groups, and states.").

50. Thomas Risse & Kathryn Sikkink, *The Socialization of International Human Rights Norms into Domestic Practices: Introduction*, in THE POWER OF HUMAN RIGHTS 1, 17 (Thomas Risse et al. eds., 1999) ("National governments might then change their rhetoric [and] gradually accept the validity of international human rights norms . . .").

51. Arend, *supra* note 21, at 129.

52. *Id.* at 132 ("The very act of participation can change how states see themselves and what they define as their particular interests.").

53. FINNEMORE, *supra* note 46, at 35 (discussing the role of international organizations in shaping state actions).

54. Oberdörster, *supra* note 26, at 689.

states operate in an environment of uncertainty, they will often imitate the solutions tried by other apparently successful states.⁵⁵

According to constructivists, norms must be accepted and internalized by the state before any action, or inaction, is attempted on the international level.⁵⁶ The degree to which states are persuaded to accept norms is the degree to which norms can influence the state's actions in the international arena.⁵⁷

One of the most prominent constructivist theories on compliance is the managerial model propounded by Abram and Antonia Chayes.⁵⁸ The managerial model posits that states affirmatively want to conform to international norms, as embodied in international law. Indeed, it is the normative effect of international law and not the fear of reprisal that leads to compliance.⁵⁹ And noncompliance is the result of states' lack of sufficient information or the high cost of compliance,⁶⁰ not a

55. FINNEMORE, *supra* note 46, at 65 (analyzing why states imitate the innovations of others).

56. See Risse & Sikkink, *supra* note 50, at 16–17 (describing the internalization of norms, irrespective of individual beliefs about their validity, as the final stage in the socialization process to ensure their implementation).

57. See *id.*

58. The managerial model represents the arguments of a substantial group of international law scholars and a permissible inference from constructivism. See, e.g., HENKIN, *supra* note 2, at 39–45 (describing the effects of international norms on government behavior).

59. CHAYES & CHAYES, *supra* note 10, at 9–10, 25–27, 116 (“Actors subject to a legal system for the most part acknowledge an obligation to obey its norms—an obligation that goes beyond the fear of penalties that may be imposed for violation.”).

60. Managerialism also recognizes that compliance with international law can be costly and expects that wealthy countries are more likely to comply with international law than poor states. Therefore, managerialists argue that one of the best ways to encourage compliance is to offer economic and technical support to developing countries. See Duruigbo, *supra* note 4, at 191–93 (noting that “non-compliance procedures” can provide less capable states with means to cooperate); Ibrahim F.I. Shihata, *Implementation, Enforcement, and Compliance with International Environmental Agreements—Practical Suggestions in Light of the World Bank's Experience*, 9 GEO. INT'L ENVTL. L. REV. 37, 41 (1996) (“[T]echnical and financial assistance should be made available as needed.”); Simon SC Tay, *Southeast Asian Fires: The Challenge for International Environmental Law and Sustainable Development*, 11 GEO. INT'L ENVTL. L. REV. 241, 289–90 (1999) (“Common sense dictates that cooperation will only succeed if, for all parties, the benefits exceed the cost.”). For a critique of managerial theory, see Downs et al., *supra* note 2, at 379–80 (arguing that states will not be willing to pay the cost of compliance for others and enforcement of this capacity building will be difficult).

result of self-interested decisions.⁶¹ In consequence, Chayes and Chayes argue that persuasion and “managing” compliance are more effective than coercing compliance with international law.⁶² Managing compliance includes informing states of international laws that they must abide by and providing states with resources to comply.⁶³ This process relies not on the threat of sanctions but on the fear of “alienation” from international networks that have become “central to most nations’ security and economic well-being.”⁶⁴ Thus, according to the managerial model, the key to international compliance is informing states of the laws, persuading states of their normative import, and helping build capacity to comply with such laws.

Critiques of constructivism target three main flaws. First, critics claim constructivism fails to offer specific expectations of state behavior or explanations of how state decisions are made, apart from that states will join and comply with international law.⁶⁵ Indeed, the mutually constituted relationship shared by state actors and international structures makes it difficult to determine the effect one has on the other.⁶⁶ As such, it is difficult to validate causal arguments with regards to norms.⁶⁷

In a second related concern, a consistent critique of constructivism is its lack of empirical evidence to back its claims and its inability to refute the alternative empirical evidence

61. CHAYES & CHAYES, *supra* note 10, at 10. Rationalists also claim that state noncompliance with international law results from a lack of sufficient information.

62. *Id.* at 25–26 (“We propose that this process is usefully viewed as management, rather than enforcement.”).

63. *Id.* at 26.

64. *Id.* at 27; *see also id.* at 26 (“The process works because modern states are bound in a tightly woven fabric of international agreements, organizations, and institutions that shape their relations with each other and penetrate deeply into their internal economics and politics. The integrity and reliability of this system are of overriding importance for most states, most of the time.”).

65. Hathaway, *supra* note 28, at 483; *see also* ANDREW T. GUZMAN, *HOW INTERNATIONAL LAW WORKS* 19–20 (2008) (arguing that it is difficult for constructivists to predict state behavior because of the flexibility of its assumptions). This proposition faces mixed empirical support as evidenced in Part IV of Hathaway’s article. Hathaway, *supra* note 28, at 513–34.

66. Arend, *supra* note 21, at 135. This criticism hearkens back to the desire to causally explain all relationships. Constructivists are generally not concerned with this in the same magnitude as rationalists. *Cf. id.* (noting that constructivists do not focus on causally explaining relationships because “the actor’s identities and interests are exogenously given”).

67. Keohane, *supra* note 10, at 493.

that contradicts constructivist claims.⁶⁸ Indeed, critics claim that both constructivism and rationalism fail to predict behavior or connect adequately with evidence.⁶⁹ Further, the empirical work that does exist flies in the face of conventional constructivist theory regarding norm internalization.⁷⁰ Constructivists, of course, contest this assertion and point to a growing body of supportive empirical evidence.⁷¹

Demonstrating the validity of an abstract theory of international compliance is no easy task.⁷² Rationalism's and constructivism's claims thus etch the broad outlines of the debates of international law. While disputing many other issues, the two theories generally agree that states are the primary actors to measure in determining compliance with international law. We question this assertion below and demonstrate that the key to compliance may actually be found in another locus of compliance: private actors' decisions to obey international law.

C. WEAKNESSES IN PROMINENT INTERNATIONAL FRAMEWORKS

A key point of agreement between constructivists and rationalists is that states are the primary actors to track in determining international compliance. We make the case that this myopic focus on state actors is actually a weakness in international law theory that has prevented the field from measuring actual compliance with international law and garnering the evidence necessary to support its claims. We address these points in turn. First, most areas of international law require an analysis of individual actors within states to determine actual, rather than pro forma, compliance. Second, relying solely on

68. See, e.g., John Mearsheimer, *A Realist Reply*, 20 INT'L SECURITY 82, 92 (1995) (observing that constructivists "have offered little empirical support for their theory" which is in contrast to realism); see also Arend, *supra* note 21, at 134 (recognizing the lack of empirical support for constructivism).

69. Richard K. Herrmann, *Linking Theory to Evidence in International Relations*, in HANDBOOK OF INTERNATIONAL RELATIONS, *supra* note 18, at 119.

70. See, e.g., Hathaway, *supra* note 28, at 526 (pointing out that states that ratify human rights treaties in order to obtain reputational benefits are more likely to commit human rights violations).

71. See e.g., DAVID HALLORAN LUMSDAINE, MORAL VISION IN INTERNATIONAL POLITICS (1993) (offering statistical evidence that foreign aid is motivated by moral beliefs); Martha Finnemore, *International Organizations as Teachers of Norms: The United Nations Education, Scientific, and Cultural Organization and Science Policy*, 47 INT'L ORG. 565, 565 (1993) (quantitatively testing the causes of state structure evolution).

72. Herrmann, *supra* note 69. Some scholars see such attempts as misguided, nothing more than selecting a favorite political preference. *Id.*

state actors to determine international compliance prevents data collection to support theoretical claims, given that evidence about sovereign governments is limited.⁷³ Further, the evidence collected often suffers from selection bias.

1. States Are Not Primary Actors

Focusing on states as the primary actors in international law does not accurately reflect the effectiveness of international law. If the focus of international compliance is states, the areas to examine include state actions such as legislation, regulation, and enforcement of the laws passed.⁷⁴ Yet to measure compliance in many of the most important areas of international law—human rights, environmental law, global health, labor provisions, and financial regulation—the main focus of international standard compliance is not government.⁷⁵ Instead, ordinary people and firms make specific decisions that aggregate into a pattern of compliance or violation.⁷⁶ For example, an in-

73. *But see* Hathaway, *supra* note 28, at 492–93 (on both domestic and international levels, non-governmental organizations assist with the legal enforcement of states' treaty obligations).

74. *See, e.g.*, Jide Nzelibe, *Strategic Globalization: International Law as an Extension of Domestic Political Conflict*, 105 NW. U. L. REV. 635 (2011) (arguing that individual politicians may have varying preferences for observing international law commitments based on partisan factors).

75. *See, e.g.*, Bing Baltazar C. Brillo, *The Financial Action Task Force and the AMLA of the Philippines: Dynamics Between Veto Players and a Non-Veto Player in Policymaking*, 7 BANWA 40 (2010), available at <http://or.upmin.edu.ph/OJS/index.php/banwa/article/view/78> (arguing that the swiftness of enactment of anti-money laundering laws pursuant to FATF demonstrates the important influence of international bodies on sovereign states); Jordan J. Paust, *Nonstate Actor Participation in International Law and the Pretense of Exclusion*, 51 VA. J. INT'L L. 977 (2011) [hereinafter Paust, *Nonstate Actor*] (documenting the fact that international law has never been merely state-to-state, that formal actors have included states, nations, peoples, belligerents, and insurgents, among other actors, and that other non-state actors have played informal participatory roles); Jordan J. Paust, *The Reality of Private Rights, Duties, and Participation in the International Legal Process*, 25 MICH. J. INT'L L. 1229 (2004) (recognizing that international law is a process involving international, regional, nation, state, corporate, and individual actors); Susan Rose-Ackerman, *Anti-Corruption Policy: Can International Actors Play a Constructive Role?* (Yale Law & Econ. Research Paper No. 440, 2011), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1926852 (emphasizing the role of international organizations and non-state actors to anti-corruption policy).

76. Both realist and liberal institutionalists agree that individual actors are more important than states in many areas of international law. *See, e.g.*, CHEN, *supra* note 9; DANIEL W. DREZNER, ALL POLITICS IS GLOBAL: EXPLAINING INTERNATIONAL REGULATORY REGIMES 63 (2007); Robert O. Keohane et al., *Effectiveness of International Environmental Institution*, in INSTITUTIONS

dividual firm—not the government—makes the decision to comply with the anti-dumping provisions of trade agreements when selling goods abroad.⁷⁷ Individual military, police, and correction officers make decisions to respect or violate the rights of their prisoners.⁷⁸ And corporations and private individuals decide whether or not to pollute, poach endangered species, or otherwise harm biodiversity in a way that violates international environmental agreements.⁷⁹ In one of the landmark pieces on international compliance, Downs studied the maintenance of oil tankers to describe the key behavior of international maritime regimes,⁸⁰ which is clearly outside the normal routine of national governments.

To be sure, the decisions of private actors occur under the umbrella of international laws established by independent sovereign governments coming together through international coalitions. And governments play a vital role in formal compliance with international law by enacting and enforcing domestic laws that implement international agreements. All of the state ac-

FOR THE EARTH: SOURCES OF EFFECTIVE INTERNATIONAL ENVIRONMENTAL PROTECTION 3, 7–8 (Peter M. Haas et al. eds., 1993); Paust, *Nonstate Actor*, *supra* note 75.

77. Though governments also choose whether to enforce these provisions, the private actors ultimately decide (based either on norms or sanctions) whether to follow international law. *See, e.g.*, *Goss Intos Corp. v. Tokyo Kikai Seisakusho, Ltd.*, 321 F. Supp. 2d 1039, 1054–55 (N.D. Iowa 2004) (discussing a Japanese corporation potential violation of international anti-dumping provisions); *Helmec Prods. Corp. v. Roth (Plastics) Corp.*, 814 F. Supp. 581, 582–88 (E.D. Mich. 1993) (discussing a private corporation's violation of federal and international anti-dumping provisions).

78. *See, e.g.*, *United States v. Winters*, 1997 U.S. App. LEXIS 12988 (5th Cir. Jan. 23, 1997) (convicting prison guard after beating escaped prisoner); Jeff Vize, *Torture, Forced Confessions, and Inhuman Punishments: Human Rights Abuses in the Japanese Penal System*, 20 UCLA PAC. BASIN L.J. 329 (2003) (discussing human rights violations in the Japanese penal system).

79. *See, e.g.*, *Hegglund v. United States*, 100 F.2d 68, 69–70 (5th Cir. 1938) (finding the master of a motor tank-ship guilty for discharging oil and permitting it to be discharged from his ship into the Calcasieu River in Louisiana); Lisa Lambert, *At the Crossroads of Environmental and Human Rights Standards: Aguinda v. Texaco, Inc. Using the Alien Tort Claims Act to Hold Multinational Corporate Violators of International Laws Accountable in U.S. Courts*, 10 J. TRANSNAT'L L. & POL'Y 109, 112–17 (2000) (analyzing Ecuadorian claims that Texaco Corporation breached the Rio Declaration on Environment and Development by committing large-scale environmental abuse); Adrienne J. Oppenheim, Note, *The Plight of the Patagonia Toothfish: Lessons from the Volga Case*, 30 BROOK. J. INT'L L. 293, 310–21 (2004) (discussing the Volga River Case where a Russian ship, which was carrying several thousand tons of illegally caught Patagonian toothfish, was seized by Australians).

80. Downs et al., *supra* note 2, at 396–97.

tions help to establish an environment of compliance within a state. The greater the enforcement of international law within a state, the more likely it is that private actors will follow such laws either because of norms or due to benefits or punishments.⁸¹

States set up an environment of compliance (or noncompliance) through the ratification of international law and through the enforcement of domestic law aimed at fulfilling the goals of international agreements.⁸² In order to test the effectiveness of the environment of compliance in a nation, we can do one of two things. First, we can determine what laws states have passed, the resources they have placed into enforcing them, and how often the laws are enforced. This is formal compliance, which we look at. The second method is determining how private actors are reacting to the environment of compliance set up by the states and determining whether the laws in place are actually inducing compliance by those individuals who ultimately make the decision to comply. While the first gives us important information about what actions the state has taken, the method that really gets at the effectiveness of international law is examining individual decisions.

For instance, in examining Norway's compliance with marine antidumping provisions, two options exist: formal and informal compliance. Formal compliance examines the domestic and international laws Norway has in place to stop antidumping, including examining the off-shore police force designated to enforce such laws. A test of informal compliance includes examining whether companies on Norway's shores are actually violating these provisions. While an examination of formal compliance is helpful in this example, only informal compliance gets to the heart of determining the effectiveness of international law. This is not to say that states should be ignored as key actors in considering the effectiveness of international compliance, but rather that the actual effectiveness of international law can only be measured through studying private ac-

81. See Harlan Grant Cohen, *Finding International Law: Rethinking the Doctrine of Sources*, 93 IOWA L. REV. 65, 97 (2007) (describing the theories supporting the notion that, states will comply with international law if the right enforcement mechanisms are arrayed).

82. See *id.* at 95 (indicating that states who ratify international treaties appear less likely to obey those treaties, while states who do not ratify the same treaties are more likely to obey).

tors as well as states.⁸³ Thus, our study looks at both of these—formal and informal compliance: formal compliance by states and informal compliance by individual private actors.

We point out here that we are not necessarily measuring state motivations to comply through the actions of private actors. Since even states as governments are aggregate actors, in order to truly understand why states are complying with international law, the investigator must examine the motivations of all of the state actors who signed, ratified, and enforced international laws.⁸⁴ Given the daunting archival and aggregation challenges involved, we sidestep state motives and instead measure private actors' motivations for complying with international law.⁸⁵ One weakness of this approach may be that private actors' motivations are more likely to be solely driven by the balance of profit and risk while a state may have multifaceted reasons for complying with international law.⁸⁶ Thus, measuring private motivation will not accurately measure state motivation. This may be the case, but there is also a large body of support for the position that states often act indirectly out of profit motives, as frequently the laws enforcing international provisions are thwarted due to the lobbying of financially invested domestic parties.⁸⁷ Therefore, while states may not al-

83. Paul B. Stephan, *Privatizing International Law*, 97 VA. L. REV. 1573, 1574–75 (2011) (“Today the production and enforcement of international law increasingly depends on private actors, not traditional political authorities.”).

84. This could take place through an archival, qualitative assessment, or perhaps by measuring the amount of resources a state invests in enforcing a particular law. We leave this to future researchers, though we note that the framers of the international law will often not be the same individuals who ratify the law or sign it. Consequently, there is a question of which motivations actually matter.

85. The slightly dismissive response to this criticism is that measuring state motivations does not matter as much as private motivations. Motivating private actors to comply with international law induces actual international compliance, thus this is the critical measure to determine on the aggregate why nations are complying with international law. And while it would be interesting to determine the motivations of the state actors who sign on and enforce international laws, ironically, this is not as critical to determining whether private actors actually comply with international law.

86. This may suggest that states are more complex than private actors, and thus a more complex theory should apply to determining state action. This is a possibility to be explored by future researchers. See Stephan, *supra* note 83, at 1618–20.

87. For instance, the Incorporation Transparency bill introduced in the United States would ratify the FATF and UNOTC agreements made by the United States and require identity documents from individuals seeking to incorporate in the United States. Compare Incorporation Transparency and Law

ways be motivated by financial incentives, many are influenced by private actors within them that are indeed profit seekers. Measuring private motivation as a proxy for state motivation is an imperfect metric, but it may be superior to solely measuring state motivations because it is more likely to get us closer to measuring actual compliance—and therefore to improving compliance with international law.

Consequently, are we simply measuring the motivations of private actors to comply with international law or are we actually measuring the effectiveness of international law? We make the case that we are measuring the effectiveness of international law. If the international compliance decision is made by

Enforcement Assistance Act, S.148, 112th Cong. (2011), with United Nations Convention Against Transnational Organized Crime art. 7 ¶ 1(a), adopted Nov. 15, 2000, 2225 U.N.T.S. 209, and FATF, FATF 40 Recommendations: October 2003 no. 5 (2010). This bill has broad support in international law and public opinion. See Declaration of the Summit on Financial Markets and the World Economy, November 15, 2008, G.A. Res. 55/25, art. 7 ¶ 1(a), U.N. Doc. A/RES/55/25 (Nov. 15, 2000); FATF, *supra*; Cyrus R. Vance, Jr., Op-Ed, *It's Time to Eliminate Anonymous Shell Companies*, REUTERS, Oct. 9, 2012, available at <http://blogs.reuters.com/great-debate/2012/10/09/its-time-to-eliminate-anonymous-shell-companies/> (“The Senate bill . . . is supported by a broad array of law enforcement groups, including the Justice Department, the Society of Former Special Agents of the FBI, and the Fraternal Order of Police.”); Letter from Civil Soc’y Orgs. to Congress (May 16, 2012), available at http://www.gfintegrity.org/storage/gfip/documents/FACT/fact_cso_and_business_support_ltr_for_s1483.pdf (forty-one civil society organizations calling on Congress to pass the Information Transparency and Law Enforcement Assistance Act). However, it may not pass due to the lobby of incorporation firms in the United States who stand to gain from their relatively lax standards compared to foreign competitors and considering the influence special interests groups can have on domestic policy. See, e.g., David P. Baron, *Review of Grossman and Helpman’s Special Interest Politics*, 40 J. ECON. LITERATURE 1221 (2002) (noting the political influence of special interest groups on securing benefits for their members through lobbying activities); *Charge Corruption in the Wool Tariff: Carded Wool-Makers Ask Taft Not to Sign Payne-Aldrich Bill Till an Inquiry Is Made*, N.Y. TIMES, Aug. 5, 1909, at 2 (describing the carded wool manufacturers’ requests for President Taft to withhold signing a bill into law until investigating the role another class of wool manufacturers played in its formulation); Nicholas Confessore, *Varied Bills for Special Interests Move Quietly Through Albany*, N.Y. TIMES, June 30, 2010, http://www.nytimes.com/2010/07/01/nyregion/01handouts.html?_r=0 (discussing a bill that would only benefit the owner of a large tobacco store, allowing his store to be exempt from strict antismoking laws); Rebecca Menes, *Corruption in Cities: Graft and Politics in American Cities at the Turn of the Twentieth Century* 5 (Nat’l Bureau of Econ. Research, Working Paper No. 9990, 2003) (“At the end of the nineteenth century, the governments of many (though not all) large American cities came to be dominated by what was known at the time as ‘machine’ politics—patronage based political systems where the government dispensed private favors in exchange for votes.”).

private actors, then this is where we must measure the level of compliance and the motivations for compliance.

An example illustrates this point. If the goal is to stop the excessive number of terrorist shell companies from being formed, we would want to determine how well nations are complying with laws targeted at stopping the formation of such companies. We would also want to determine what motivates compliance with these laws so that we can increase compliance. One way is to examine the framework of laws put into place by state actors to stop the formation of these companies and determine whether these laws are enforced against such companies. But since what we really care about is whether these shell companies are being formed, we must also examine the private bodies within the nation who actually form terrorist shell companies and determine why they are allowing the formation of such companies.⁸⁸

Since it is ultimately private behavior that we want to influence, we want to know whether private actors fear sanctions or realize there are international norms against formation of such corporations. Thus, the motivation of private actors to comply provides insight on how effective international laws are and what motivates compliance with such laws. We note as well that ultimately, state actors do not make the decision to comply—their private citizens do. Although we measure private actors, this gives us important insights into the environment of compliance that the state has established and how the state can alter its framework to improve compliance. Thus, when we determine that private actors comply more often with international law, we may reveal a greater motivation of that state for encouraging compliance with such laws, but we certainly also demonstrate that international law is effective in that state.

Examining state action is important to measure formal ratification of international law and evaluate how effective the enforcement regime is in ensuring compliance. But to gain important insights into the effectiveness of the international law, measuring private action is vital. Thus, both rationalist and constructivist scholars have misplaced their emphasis on states as primary actors, when obtaining a pulse on the true impact of international law often requires measuring private actors. With this improper emphasis on states, international scholars have

88. This is of course assuming that we do not care about the expressive power and the effect of such laws aside from how they affect behavior.

largely failed to garner robust evidence to support their claims.⁸⁹

2. Compliance Studies Fail Without Robust Evidence

Though international scholars place a prominent focus on studying compliance with international law,⁹⁰ they have in large part failed in garnering evidence to support their claims. A central unresolved difficulty of international law is whether international commitments arise from compliance and are thus subject to strong selection bias.⁹¹ Selection bias presents a problem where it is difficult to determine how unobserved factors limit the ability to establish causality.⁹² With compliance research, the underlying problem with selection bias is determining whether countries that comply with international law are in some way fundamentally different than the countries that do not comply. Prior research on compliance with international law suffers from an inability to determine the effects of unobservable factors that create selection bias.⁹³ For instance, in claiming that nations comply with international law due to strong norms, constructivists fail to account for the fact that nations may comply with laws that are easiest to adhere to or the fact that nations complying with international law are fundamentally different than those who fail to sign on.⁹⁴

To explain the significance of selection bias in studying international law, we examine a prominent debate among leading international scholars in the managerial school. In their foundational article, Abram and Antonia Chayes argue that compliance with international law is the norm and noncompliance results due to ambiguities and a lack of capacity to comply with international law, rather than deliberate defiance.⁹⁵ In re-

89. *But see* Hathaway, *supra* note 28, at 492–93.

90. *See* CHAYES & CHAYES, *supra* note 10; Downs et al., *supra* note 2, *passim*; Kal Raustiala & Anne-Marie Slaughter, *International Law, International Relations and Compliance*, in HANDBOOK OF INTERNATIONAL RELATIONS, *supra* note 18, at 538; Simmons, *supra* note 6.

91. *See* Downs et al., *supra* note 2, at 383; Simmons, *supra* note 6, at 76–77; Jana Von Stein, *Do Treaties Constrain or Screen? Selection Bias and Treaty Compliance*, 99 AM. POL. SCI. REV. 611, 611 (2005).

92. *See* Richard A. Berk, *An Introduction to Sample Selection Bias in Sociological Data*, 48 AM. SOC. REV. 386, 386–88 (1983) (describing external and internal validity problems associated with selection bias and the resulting difficulty establishing causality).

93. *See* Von Stein, *supra* note 91, at 611.

94. *See id.*

95. CHAYES & CHAYES, *supra* note 10, at 9–28.

sponse to the optimism of the “managerial” school, George Downs brings to light the nontrivial challenges posed by selection problems.⁹⁶ Compliance with international standards might be the norm precisely because states acceded to those standards that are easy to meet.⁹⁷ If this is so, compliance is explained by selection bias rather than the constraining power of international law.⁹⁸

Founded on rationalist insights regarding compliance motivations, Beth Simmons counters with a defense of compliance.⁹⁹ With an empirical lens, she focuses on conventions prohibiting currency restrictions.¹⁰⁰ She discusses the theoretical potential for endogeneity and selection problems, attempting an empirical correction.¹⁰¹ Simmons suggests that international standards foster compliance, but the effect stems from reputational issues that states face if they back out of an agreement.¹⁰² Employing observable variables to lessen the problem of non-random selection, she concludes that reputational factors do in fact induce compliance to agreements proscribing currency restrictions, especially when neighboring countries also commit to and abide by legal standards.¹⁰³ Thus, from a rationalistic viewpoint, nations basically respond to the economic and social pressure generated by the actions of nearby countries and often observe such standards.

Tackling Simmons’s alleged failure to address selection bias, Jana Von Stein analyzes the same set of conventions proscribing currency controls, finding that countries began complying with international standards long *before* acceding to

96. Downs et al., *supra* note 2, at 383 (“[A] treaty is an endogenous strategy because states choose the treaties they make from an infinitely large set of possible treaties. If some treaties are more likely to be complied with than others or require more enforcement than others, this will almost certainly affect the choices states make [S]tates will rarely spend a great deal of time and effort negotiating agreements that will continually be violated. This inevitably places limitations on the inferences we can make from compliance data alone [W]e do not know what a high compliance rate really implies.”).

97. See DREZNER, *supra* note 76, at 40 (suggesting that “a government’s ideal point on regulatory issues is its domestic status quo”); Raustiala & Slaughter, *supra* note 90, at 539.

98. See Chayes & Chayes, *supra* note 6, at 178–79 (noting that once nations have decided to ratify they tend to comply because (1) it is easier to make decisions and (2) nations presumably ratified because it was in their interest).

99. Simmons, *supra* note 10.

100. *Id.*

101. See *id.* at 343–44.

102. *Id.* at 327.

103. *Id.* at 350, 360.

international agreements.¹⁰⁴ Apparently, numerous unobservable factors conditioned states for international compliance, and states joined international agreements only after undergoing this alteration.¹⁰⁵ Von Stein's reanalysis implies that countries signing on to international treaties are inherently different than those refraining from doing so, which suggests selection bias.¹⁰⁶ Von Stein's work is quite compelling, but it fails to explain the *actual* causes of compliance with international standards, leaving the question vague, unresolved, and unobserved.¹⁰⁷

As the debate described above illustrates, much of the controversy surrounding the causes of compliance turns on selection bias. Yet all present studies exclusively rely on conceptual arguments or tests that use observational data that cannot explain the causes of compliance.¹⁰⁸ While by no means a panacea, field experiments have the potential to allow a better evaluation of the causes of compliance, particularly when combined with theoretical analysis and critique. This Article uses randomization in a field experiment to avoid the problem of selection bias that exists in previous tests of whether countries comply with international law.

Other fields have addressed selection bias by employing experiments that use random assignment to the treatment and control conditions.¹⁰⁹ When correctly carried out, any outcome-based differences between groups are causally attributed to the intervention, because in expectation the randomization process balances and neutralizes the effects of any other observable

104. Von Stein, *supra* note 91, at 613–14.

105. *Id.* at 614–15.

106. *Id.*

107. It is important to determine whether Von Stein believes that complying states and noncomplying states are fundamentally different or whether she just points out that pre-adoption trajectories for the two types of states are different.

108. And indeed, international scholars like Von Stein have lamented the failure of subjective experiments to uncover cause and effect in international relations. Von Stein, *supra* note 91, at 612. The implication: if they could be used, randomized trials might shed light on unresolved questions.

109. This approach continues to achieve prominence and success in fields such as economics and international political economy. See Humphreys & Weinstein, *supra* note 16, at 368–69 (2009) (describing the value of randomized field experiments where the units of analysis are normal individuals that can be treated as research subjects); Steven D. Levitt & John A. List, *Field Experiments in Economics: The Past, the Present, and the Future*, 53 *EUR. ECON. REV.* 1 (2009).

and unobservable factor.¹¹⁰ The problem embedded in conventional international law analysis is clear: sovereign governments have typically been the objects of inquiry.¹¹¹ This creates a misplaced focus as much of international law is complied with or violated by private actors rather than states.¹¹² But as demonstrated above, the key to actual compliance with international law is private actors, who are observable.¹¹³ Furthermore, manipulating sovereign nations to gather solid empirical data presents serious practical and ethical difficulties. As a result, international law theory has been limited by a lack of robust evidence as to why nations comply with international law. And thus, in measuring state action as well as private compliance with international law through a field experiment, we can form a test of actual compliance with international law while avoiding the selection bias of traditional empirical analysis in this area.

D. TESTING INTERNATIONAL COMPLIANCE

With the goal of determining the level of compliance with international law and the motivation for complying with such laws, we measure both formal and informal compliance. In other words, we measure what states claim to be doing to follow international law and what they are actually doing, and give insight as to why they are doing it.

While we hope to shed light on the two key questions in international law, we do not intend to affirmatively resolve the question of why nations comply with international law. To do so would require an understanding of the motivations of a large sample of state and private actors in a natural setting, which is impossible to do in one area of law, let alone every area of international law. Our aim is also limited by an imperfect metric of state action, which examines the environment of compliance in a state and in the actions of private actors. Nonetheless, what we show tells us something very important about how effective international law is at capturing state compliance in one

110. See Humphreys & Weinstein, *supra* note 16, at 369.

111. See Anne-Marie Slaughter, *International Law in a World of Liberal States*, 6 EUR. J. INT'L LAW 503, 507 (1995).

112. See Andrew Moravcsik, *Liberal Theories of International Law*, in INTERNATIONAL LAW AND INTERNATIONAL RELATIONS: THE STATE OF THE ART (Jeffrey L. Dunoff & Mark A. Pollack eds.) (forthcoming 2012) (manuscript at 24), available at http://www.princeton.edu/~amoravcs/library/int_law.doc.

113. The other key here is that private actors can be not only observed but manipulated, allowing a testing.

important domain, and it provides insight on *why* such compliance occurs.

1. Distinguishing Formal and Actual Compliance

Compliance occurs when nations behave as their governments have agreed to under international law; conversely, violations of international law result when nations depart from agreed upon actions.¹¹⁴ Determining the effectiveness of international law requires examining compliance by the national government as well as the actions of private actors regulated by the international law at play.¹¹⁵ As discussed above, the two tests of international compliance are formal and actual compliance.¹¹⁶ Formal compliance with international law is relatively easy to determine. Formal compliance involves examining the regulatory framework that nations have put in place to enforce international laws. It looks strictly at what national laws have been passed and the level of enforcement of such laws. Actual compliance is much more difficult to ascertain. It examines whether private actors in these nations, which are the real targets of these laws, are actually complying with the regulations and thus fulfilling the goals of the laws. Since private bodies may not honestly admit to violating international law, we use a field experiment to test actual compliance.

a. *Why Financial Transparency?*

We choose international financial transparency as the area for our field experiment for several reasons. First, it is at the intersection of corporate law, global security, and international criminal law. Financial transparency law is an area where the world has allegedly come together with one voice to ratify global standards,¹¹⁷ with the belief that they are critical to stopping

114. ORAN R. YOUNG, COMPLIANCE AND PUBLIC AUTHORITY 104 (1979) (defining compliance as “actual behavior” following “prescribed behavior” and defining noncompliance or a violation as “actual behavior [that] departs significantly from prescribed behavior”).

115. See *supra* text accompanying notes 111–13.

116. See *supra* Part I.D.

117. See, e.g., International Convention for the Suppression of Acts of Nuclear Terrorism art. 7, *adopted* Apr. 13, 2005, 2445 U.N.T.S. 89 (agreeing to take “all practicable measures” to prohibit illegal activities of entities that knowingly finance enumerated offenses related to nuclear terrorism); International Convention for the Suppression of the Financing of Terrorism, *adopted* Dec. 9, 1999, 2178 U.N.T.S. 197.

international terrorism and corruption.¹¹⁸ Particularly as it comes to money laundering and cross-border terrorism, the international community has purportedly committed to a collaborative approach to make headway against these crimes.¹¹⁹ Thus, in an area with substantial international agreement, we can examine whether private actors really comply with the laws set forth by their nations and what motivates them to comply when they do.

Second, international financial transparency law is an area of law that includes strong norms in following financial transparency laws, and it is also an area that generates sanctions for noncompliance. Financial transparency standards include both hard¹²⁰ and soft laws,¹²¹ which may involve sanctions for breaking or not complying with international legal norms.¹²² This

118. This also provides a large pool of countries to test, as 180 countries have signed on to international financial transparency laws. See FATF, AN INTRODUCTION TO THE FATF AND ITS WORK 2 (2010).

119. See U.N. Secretary-General, *Uniting Against Terrorism: Recommendations for a Global Counter-Terrorism Strategy: Rep. of the Secretary-General*, ¶¶ 100–04, U.N. Doc. A/60/825 (Apr. 27, 2006) (discussing the importance of counter-terrorism coordination and information sharing to stop terrorism); Elizabeth MacDonald, *Shell Games*, FORBES, Feb. 12, 2007, at 96, 98 (explaining that there is no cooperation or united front in the United States to force states to verify ownership of corporations, allowing the formation of roughly 1.9 million private companies each year with less information than is required to obtain a driver's license); David S. Cohen, Assistant Sec'y for Terrorist Fin., U.S. Dep't of the Treasury, Remarks on Terrorist Financing Before the Council on Foreign Relations (Jan. 28, 2010) (as prepared for delivery), available at <http://www.treasury.gov/press-center/press-releases/Pages/tg515.aspx> (explaining that “the Taliban and al Qaeda understand the critical role that a strong, sound and transparent financial system plays in safeguarding a nation's security” and that such financial systems expose weaknesses in laws that enables the financing of terrorism).

120. Hard laws are those that have legal binding force. Gregory C. Shaffer & Mark A. Pollack, *Hard vs. Soft Law: Alternatives, Complements, and Antagonists in International Governance*, 94 MINN. L. REV. 706, 714–15 (2010).

121. Soft laws are laws that may be quasi-legal and without binding force. They may also have weaker enforcement than hard laws. See Andrew T. Guzman & Timothy L. Meyer, *International Soft Law*, 2 J. LEGAL ANALYSIS 171, 172–73 (2010).

122. Prior scholarship distinguishes international commitments into hard law and soft law, which have varying degrees of rigor. Hard law agreements obligate states in precise legal ways, with governments sometimes delegating both interpretation and enforcement to an independent organization. Abbott & Snidal, *supra* note 13, at 421–22. On the other hand, soft law outlines presumably weaker standards of conduct that are likely either less precise or less independently enforced. *Id.* at 422. Debates in the international literature discuss the relative effectiveness of soft and hard law on international compliance. Financial transparency with respect to company ownership is governed

provides a good testing ground for the theories of rationalism and constructivism, which disagree on the relative import of penalties and norms on inducing compliance. This creates an ideal testing ground, in an area about which the international community claims to be serious, to reveal how determined governments in fact are and whether relevant private actors are motivated by strong norms or the threat of sanctions.

Finally, we test international transparency standards because one of the front lines of the war on terrorism is financial.¹²³ Indeed, the laws at the heart of this article have powerful implications for security, crime, and international political economy. The first step in stopping terrorism sometimes includes stopping formation of suspect anonymous entities used to finance terrorism and launder money, leading to billions in damages each year.¹²⁴ As such, international laws now require that to form a corporation, individuals must provide identity information.¹²⁵

by both soft and hard law. This intersection between hard and soft law makes financial transparency an ideal testing ground as it includes both standards, including standards that contain penalties. Employing an experiment in the area of financial transparency allows a close look at whether legal penalties or international norms cause compliance with international law.

123. Lisa Anderson, *Global Partnership to Combat Corruption Launched*, TRUSTLAW (Sept. 22, 2011), <http://www.trust.org/trustlaw/news/global-partnership-to-combat-corruption-launched> (explaining that incorporation transparency is “designed to thwart tax evaders, money launderers, corrupt politicians and even terrorist organizations from hiding behind American shell companies” and noting that “the demand for transparency is unstoppable and the technology makes it irresistible”).

124. See PAUL ALLAN SCHOTT, WORLD BANK, REFERENCE GUIDE TO ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM 1-6 to 1-7 (2d ed. & Supp. on Special Recommendation IX 2006). President Obama has said that “his administration will support passage of the Incorporation Transparency and Law Enforcement Assistance Act, which would require U.S. states where companies are registered to collect information about the true owners,” in compliance with FATF standards. Anderson, *supra* note 123.

125. United Nations Convention Against Transnational Organized Crime art. 7, ¶ 1(a), *adopted* Nov. 15, 2000, 2225 U.N.T.S. 209; see also FATF, FATF 40 RECOMMENDATIONS: OCTOBER 2003 (2010). Acceptable identity data often include a notarized passport copy and certified utility bill. See *id.* at 7; *General Guide to Account Opening and Customer Identification*, BANK FOR INT’L SETTLEMENTS (Feb. 2003), <http://www.bis.org/publ/bcbs85annex.htm>. Without such documentation, individuals can form anonymous, untraceable “shell” corporations. J.C. Sharman, *Shopping for Anonymous Shell Companies: An Audit Study of Anonymity and Crime in the International Financial System*, 24 J. ECON. PERSP. 127, 129 (2010).

b. *Testing Compliance with Financial Transparency*

As with most international laws, compliance with international financial transparency occurs when individual actors decide whether to comply with laws requiring identity disclosure of beneficial owners. As such, when an individual tries to legally incorporate a company, international standards require the corporate services provider—a for-profit body specializing in setting up legal entities for others—to obtain important identifying information. International law requires these firms to obtain a notarized copy of the individual’s identification and proof of address, such as a utility bill.¹²⁶ Non-compliance with financial transparency standards permits the formation of anonymous “shell” corporations that cannot be traced to the real person or people in control, facilitating corruption, organized crime, money laundering, and terrorism.¹²⁷ According to the World Bank, some of the world’s most destructive and threatening activities are carried out through such shells.¹²⁸ For instance, shell companies have been traced to rogue activities by Muammar Gaddafi in Libya,¹²⁹ a covert nuclear program in Iran,¹³⁰ Russian arms dealing,¹³¹ North Korean weapons stockpiling,¹³² and al-Qaeda terrorist activities.¹³³

126. See *supra* note 125 and accompanying text. We note here that FATF Recommendation 24 does not state that notarized identification is essential, but practically speaking, this is how many countries comply with the language of the Recommendation. See FATF, INTERNATIONAL STANDARDS ON COMBATING MONEY LAUNDERING AND THE FINANCING OF TERRORISM & PROLIFERATION: THE FATF RECOMMENDATIONS 20, 82–87 (2012) [hereinafter FATF, STANDARDS]. There are three options for satisfying Recommendation 24: strong investigative powers, information at the registry, and information collected by the corporate service provider. See *id.* at 88 (describing potential sources of identity information). Many countries have ended up complying using the third option, which has evolved into requiring notarized identification documents.

127. See Sharman, *supra* note 125.

128. SCHOTT, *supra* note 124, at 1-5 to 1-9.

129. Philip Shenon, *Dirty Dictator Loot: Obama Talks Tough, but the U.S. Remains a Haven for the Ill-Gotten Gains of Bloodthirsty Despots*, NEWSWEEK, Mar. 21, 2011, at 18 (noting that while freezing assets owned by Gaddafi’s children, the United States is looking the other way with Teodoro Obiang, son of Equatorial Guinea’s brutal dictator).

130. 157 CONG. REC. E2068 (daily ed. Nov. 16, 2011) (statement of Rep. Carolyn B. Maloney) (noting the “movement of funds through banks in New York by entities controlled by the Iranian Military through domestic shell companies opened in two different states to further secret Iranian interests”).

131. *Undeclared Beneficial Ownership: Licence to Loot*, ECONOMIST, Sept. 17, 2011, at 64, available at <http://www.economist.com/node/21529021> (noting

Indeed, anonymous shell corporations have caused billions in damage to nations,¹³⁴ demonstrating the harm of a lack of financial transparency and noncompliance with international financial disclosure.¹³⁵ Thus, not only does our experiment shed light on whether international law is effective but it also may aid governments in stopping the formation of anonymous corporations and help combat a range of financial crimes.

To test formal compliance with international financial transparency law, we examine applicable soft and hard international laws. The distinctions between soft law and hard law

that Iran, al-Qaeda, and a Russian arms trader have all benefited from America's regime that allows "lax" shell company formation).

132. Michael Field, *NZ Firms Linked to Money Laundering*, SUNDAY STAR TIMES, May 29, 2011, <http://www.stuff.co.nz/national/5069771/NZ-firms-linked-to-money-laundering> (noting that Mexican drug cartels, Russian organized crime organizations, and North Korean arms smugglers all have used New Zealand-based shell corporations).

133. Dan Izenberg, *A Critical Step in Terrorism Prevention*, JERUSALEM POST, Nov. 11, 2004, at 6 (discussing legislation that would allow the government to "more easily prevent payments to the widows and orphans of suicide bombers and other terrorists killed in action"); *The G20 and Tax: Haven Hypocrisy*, ECONOMIST, Mar. 28, 2009, at 87, available at <http://www.economist.com/node/13382279> (discussing America's attractiveness to those looking to form shell corporations); Kelly Carr & Brian Grow, *Special Report: A Little House of Secrets on the Great Plains*, REUTERS, June 28, 2011, available at <http://www.reuters.com/article/2011/06/28/us-usa-shell-companies-idUSTRE75R20Z20110628> ("Criminals use U.S. shell companies to commit financial fraud, drug trafficking, even terrorist financing, in part because our states don't require anyone to name the owners of the companies they form." (internal quotation marks omitted)).

134. In 2002, the Kenyan government called for bids to create a new national passport system. Although a French firm bid €6 million, the Kenyan government secretly chose to award the contract to a British company called Anglo-Leasing and Finance Company, which bid €30 million. Upon acceptance of its bid, Anglo-Leasing immediately subcontracted the work out to its French competitor for €6 million. A low-level government official disclosed the deal to the media, creating public outrage in both England and Kenya. Upon inquiry, it turned out that the company, Anglo-Leasing, was nothing more than an English postal address; it was an anonymous "shell" corporation. The investigation was derailed because the real names of the firm's owners could not be discovered. See CHALLENGING THE RULERS: A LEADERSHIP MODEL FOR GOOD GOVERNANCE 15 (Okoth Okombo et al. eds., 2011). See generally MICHELA WRONG, IT'S OUR TURN TO EAT: THE STORY OF A KENYAN WHISTLE BLOWER (2009).

135. See *Keeping Foreign Corruption Out of the United States: Four Case Histories, Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Homeland Sec. & Governmental Affairs*, 111th Cong. 80–86 (2010) (prepared statement of David T. Johnson, Assistant Secretary, Bureau of International Narcotics and Law Enforcement Affairs); FATF, THE MISUSE OF CORPORATE VEHICLES, INCLUDING TRUST AND COMPANY SERVICE PROVIDERS 1 (2006).

may not indicate one being more effective, stricter, or yielding greater compliance, but we use these distinctions to demonstrate the standards that apply. One applicable soft law we test is set by a non-state actor, the Financial Action Task Force (FATF), an intergovernmental body tasked with promoting international financial transparency.¹³⁶ Its members consist of nation-states that set and monitor enforcement of regulations to counter both money laundering and terrorist financing.¹³⁷ The FATF published forty-nine recommendations that countries should adopt if they are serious about not harboring unscrupulous financial activity domestically.¹³⁸ These recommendations are in actuality enforced,¹³⁹ and have been endorsed by the United Nations Security Council¹⁴⁰ and the Bretton Woods institutions.¹⁴¹ Specifically, the FATF Recommendations 10, 22,

136. GUZMAN, *supra* note 65, at 231 n.41 (describing the FATF as an exception to other soft laws because it includes both monitoring and sanctions and does not, like other soft laws, “omit formal sanctions . . . and other devices that serve to amplify the costs of a violation or allow states to avoid an obligation while remaining in compliance with the precise language of the agreement”); Ben Saul, *Terrorism and International Criminal Law: Questions of (In)Coherence and (Il)Legitimacy*, in INTERNATIONAL CRIMINAL JUSTICE: LEGITIMACY AND COHERENCE (Gideon Boas et al. eds., forthcoming 2012) (discussing the importance of the FATF Recommendations as international soft law on terrorism).

137. *Who We Are*, FATF, <http://www.fatf-gafi.org/pages/aboutus/whoweare/> (last visited Nov. 29, 2012).

138. FATF, *supra* note 125. The FATF is specifically geared towards assessing a country’s compliance with Recommendations, not private individuals’ compliance. FATF, *METHODOLOGY FOR ASSESSING COMPLIANCE WITH THE FATF 40 RECOMMENDATIONS AND THE FATF 9 SPECIAL RECOMMENDATIONS 3* (2009) [hereinafter FATF, COMPLIANCE]. Under the FATF, incorporation services are defined as DNFBPs (Designated Non-Financial Businesses and Professions). See FATF, *supra* note 125, at 15. DNFBPs are included with financial institutions and are equally required to comply with Recommendations 10, 20, 23 when it relates to creation of companies. See FATF, COMPLIANCE, *supra*, ¶¶ 12.1, 16.1, 16.1 n.27 (2009) (Recommendation numbers altered to reflect changes FATF instituted in February 2012); FATF, *STANDARDS*, *supra* note 126.

139. See *supra* notes 121–23 and accompanying text.

140. See JAMES K. JACKSON, CONG. RESEARCH SERV., RS 21904, *THE FINANCIAL ACTION TASK FORCE: AN OVERVIEW 1–2* (2012) (stating that the U.N. Security Council adopted a resolution urging implementation of the Recommendations).

141. See generally *FATF Releases 8 Special Recommendations on Terrorist Financing*, BRETTON WOODS PROJECT, <http://www.brettonwoodsproject.org/art-62721> (last visited Nov. 29, 2012). Bretton Woods is a system of monetary management that sets forth rules for financial and commercial relations among industrialized countries. See ARMAND VAN DORMAEL, *BRETTON WOODS: BIRTH OF A MONETARY SYSTEM* (1978).

and 24 require financial institutions to undertake customer due diligence measures “including identifying and verifying the identity of their customers,” when “establishing business relations . . . [and] [where] there is a suspicion of money laundering or terrorist financing.”¹⁴² The FATF also requires nations to pass laws to sanction private institutions for noncompliance.¹⁴³

On the whole, the FATF requires financial institutions to identify their customers and verify the true owners when they establish business relations or where there is suspicion of money laundering or terrorism.¹⁴⁴ The FATF explains that not only should countries formally comply with standards but that they should also demonstrate that they have been effectively implemented by private institutions in their country.¹⁴⁵ And further, when a country signs on to FATF standards, it is obligated to impose mandatory requirements with sanctions for noncompliance with the FATF.¹⁴⁶ Indeed, the FATF spells out that countries should ensure that “dissuasive criminal, civil or administrative sanctions” are available to deal with violators of FATF Recommendations, including senior management of firms.¹⁴⁷

142. FATF, STANDARDS, *supra* note 126, at 14–15, 19–20, 22 (interpretive notes also require these basic obligations to be set out in laws or regulations); *see* FATF, COMPLIANCE, *supra* note 138, at 9. Lawyers, law firms, and companies are defined as financial institutions or legal persons depending on the context. *Id.* at 65–67. *See* FATF, STANDARDS, *supra* note 126, at 4–5 for comparison of Recommendation numbers prior to February 2012 with current Recommendation numbers.

143. FATF, COMPLIANCE, *supra* note 138, at 9–10, 12 (explaining that these sanctions should be “effective, proportionate and dissuasive” and “directly or indirectly applicable for a failure to comply”).

144. FATF, *supra* note 125, at 4–5; *see also id.* at 7, 11–12 (dealing specifically with forming a corporation). The Recommendations also require financial institutions and DNFbps to assess and manage or mitigate money laundering and terrorism financing risks. Assessed risks should be documented and risk management controls identified and monitored. *See* FATF, STANDARDS, *supra* note 126, at 33. Countries are required to designate a competent authority within the country to monitor and ensure compliance by DNFbps with the power to sanction if necessary. *See* FATF, COMPLIANCE, *supra* note 138, at 32–33.

145. FATF, COMPLIANCE, *supra* note 138, at 7 (stating that effective implementation of the FATF includes that “the requisite law, regulation or other enforceable means is in place and is being effectively implemented . . . [using] quantitative data and qualitative and other information”).

146. *See id.* at 9 (explaining that businesses and institutions “should be required by law or regulation” to comply with FATF Recommendations).

147. FATF, *supra* note 125, at 9 (Recommendation 17). Note that Recommendation 17 has been renumbered as Recommendation 35. *See* FATF, STANDARDS, *supra* note 126, at 5.

Governments must also require their financial institutions to report suspicious activity in the creation of a corporation.¹⁴⁸

The FATF has enjoyed considerable success in diffusing its rules, with 180 countries committed to follow these international standards.¹⁴⁹ Hold-outs have been publicly blacklisted such that otherwise recalcitrant states have been persuaded to incur domestic regulatory costs rather than risk reputational damage and possible disinvestment.¹⁵⁰

Beyond the FATF, there are a few notable hard international law conventions that require financial transparency. The United Nations adopted two agreements requiring identity disclosure of corporate owners which have been ratified by almost all U.N. members. For example, the U.N. Convention Against Transnational Organized Crime (UNTOC) commits member states to compel identity disclosure in business dealings. Article 7 of the UNTOC states that parties “shall emphasize requirements for customer identification.”¹⁵¹ The other hard law that requires essentially the same information is the International Convention for the Suppression of the Financing of Terrorism.¹⁵² Specifically, Article 18 concentrates on combating anonymous corporations and explicitly requires parties to implement and enforce domestic legislation requiring firms to obtain “information concerning the customer’s name, legal form,

148. Recommendation 20 says a “financial institution . . . should be required, by law, to report promptly its suspicions to the financial intelligence unit (FIU)” when it “suspects or has reasonable grounds to suspect that funds are the proceeds of a criminal activity.” FATF, STANDARDS, *supra* note 126, at 19. Recommendation 22 holds DFNBPs to the Recommendation 20 requirements during the “creation, operation or management of legal persons.” *Id.*

149. The FATF recommendations promoting financial transparency have achieved considerable legitimacy and support worldwide, gaining endorsements from the U.N. Security Council (Resolution 1617) and G20 for example. Press Release, White House Office of the Press Secretary, Declaration of the Summit on Financial Markets and the World Economy (Nov. 15, 2008), *available at* <http://cdm16064.contentdm.oclc.org/cdm/singleitem/collection/p266901coll4/id/2648/rec/5>.

150. DREZNER, *supra* note 76, at 142–45; J.C. Sharman, *The Bark is the Bite: International Organizations and Blacklisting*, 16 REV. INT’L POL. ECON. 573 (2009).

151. G.A. Res. 55/25, art. 7 ¶ 1(a), U.N. Doc. A/RES/55/25 (Nov. 15, 2000). UNTOC rapidly gathered 146 signatures from 178 countries; 125 states have since ratified and another 30 acceded by simultaneously signing and ratifying. See United Nations Convention Against Transnational Organized Crime art. 7 ¶ 1(a), *adopted* Nov. 15, 2000, 2225 U.N.T.S. 209.

152. *International Convention for the Suppression of the Financing of Terrorism*, 10 MSU-DCL J. INT’L L. 641 (2001). It has a total of 173 parties as well as four states that signed but have not yet ratified.

address, directors and provisions regulating the power to bind the [corporate] entity.”¹⁵³ While these hard laws have identity requirements like the FATF, they do not go as far in creating severe consequences, such as blacklisting and sanctions, as the soft law provisions of the FATF.¹⁵⁴

Taken together, the soft (FATF) and hard (U.N.) laws all require information on the identity of corporate owners in order to form a corporation. The countries that have signed on to the FATF have agreed not only as a nation to enact domestic legislation requiring financial transparency but they have also agreed to effectively implement these laws and require private bodies within their borders to comply. Thus, in this study we test both formal compliance by nations with FATF provisions and actual compliance by private bodies within these nations, as the FATF requires both forms of compliance.

2. Three Tests of Formal Compliance

To determine formal compliance, we review the legislative, regulatory, and enforcement structures put in place to implement FATF provisions. The FATF is the gold standard in international financial transparency, money laundering, and counter-terrorist financing, and thus we start there in this test of formal compliance. We examine 100 countries who have signed on to the FATF and UNTOC to determine their level of formal compliance with international financial transparency laws.¹⁵⁵

To test formal compliance with international laws on financial transparency, we examine three areas. First, and most simply, we examine which countries have become members of the FATF,¹⁵⁶ as thirty-six countries have done.¹⁵⁷ Becoming a

153. G.A. Res. 54/109, U.N. Doc. A/RES/54/109 (Dec. 9, 1999).

154. As of October 2010, FATF membership extends to thirty-six nations, including the United States, the other OECD countries, and South Africa, Singapore, Russia, Hong Kong, China, Brazil, and Argentina. *See FATF Members and Observers*, FATF, <http://www.fatf-gafi.org/pages/aboutus/membersandobservers> (last visited Nov. 29, 2012).

155. For current list of FATF countries, see *Countries*, FATF, <http://www.fatf-gafi.org/countries/> (last visited Nov. 29, 2012).

156. Note that while 180 countries have committed to comply with FATF provisions through external bodies, only thirty-six have actually become FATF members. *See supra* notes 153–55.

157. Current member states include Australia, Belgium, Brazil, Canada, China, Denmark, France, India, Japan, The Netherlands, Mexico, New Zealand, Norway, Republic of Korea, Russian Federation, Singapore, South Africa, Spain, Turkey, United Kingdom, and United States. *See supra* note 154.

member of the FATF requires a country to demonstrate political support for the forty-nine FATF Recommendations and maintain a high level of compliance with them.¹⁵⁸ We presume that countries that are FATF members may demonstrate higher compliance with its provisions than other nations that have simply signed on to comply with its standards.¹⁵⁹ Second, we examine whether according to a multilateral peer review initiated by the FATF, FATF signatories achieve compliance with its financial transparency provisions.¹⁶⁰ This evaluation determines the level of compliance by each country with all forty-nine Recommendations based on the regulatory framework and enforcement mechanisms they have put into place. Finally, we examine separately the domestic regulations each country has in place that require identity verification upon incorporation.

On the first test, FATF member countries fare no better in a comparison of formal compliance than non-member countries. After an examination of extensive peer reviews,¹⁶¹ FATF member nations, who are required to exhibit higher compliance with FATF provisions than other nations, do not in fact demonstrate higher compliance.¹⁶² In fact, non-FATF members actually demonstrate higher compliance rates, though these results are not statistically significant.¹⁶³ Against expectations, FATF

The difference between FATF members and others who are members of satellite bodies is that the former are rule-makers concerned with implementation whereas all regional bodies are bound to adopt FATF standards.

158. *FATF Membership Policy*, FATF, <http://www.fatf-gafi.org/pages/aboutus/membersandobservers/fatfmembershippolicy> (last visited Nov. 29, 2012).

159. Though we are not sure that FATF membership means any more than signing on to the FATF as part of a FATF-like regional organizations. *See, e.g., supra* note 155 (listing the European Commission and Gulf Cooperation Councils members of FATF). We test the difference between member and nonmember states, though, in case there is a difference.

160. This multi-lateral peer review includes a review team from various countries that review and visit the various countries to determine their level of compliance with FATF provisions. *See Mutual Evaluations*, FATF, <http://www.fatf-gafi.org/topics/mutualevaluations/> (last visited Nov. 29, 2012).

161. Peer reviews are called mutual evaluations by the FATF. These evaluations are the primary way that the FATF determines whether countries are complying with its provisions. The evaluations must be independent, objective, and accurate and are cross-checked by the FATF with other enforcement bodies. *See Key Principles for Mutual Evaluations and Assessments*, FATF, <http://www.fatf-gafi.org/topics/mutualevaluations/documents/keyprinciplesformutualevaluationsandassessments.html> (last visited Nov. 29, 2012).

162. *See infra* app. C.

163. *See infra* app. E.

members that have accepted higher obligations and that should be more likely to accept norms, show no better formal compliance than other countries.

Now we examine how FATF signatories overall fare with formal compliance with international FATF provisions. Thus far, more than 100 countries have undergone a mutual evaluation that examines how well the country has instituted regulations to enforce the FATF Recommendations. According to the mutual evaluations, an average of 40% of countries were fully or largely nationally compliant with the 49 FATF standards.¹⁶⁴ In contrast, only 1.94%, 1.94%, and 7.76% of these same countries were fully compliant with Recommendations 10, 22, and 24, respectively.¹⁶⁵ The rate for full formal compliance is extremely low, though for Recommendations 24 and 10, considering countries that have taken steps to comply but had not reached full compliance, the compliance rate jumps to 79.59% and 63% respectively.¹⁶⁶ Overall, with this second test, there is some indication of low formal compliance with the FATF.

Finally, we examine the level of formal compliance with identity requirements for incorporation outside of the FATF framework. We do this by examining which countries by domestic law require identity information to create a corporation and whether they require notarized identity documents.¹⁶⁷ This test actually demonstrates a high level of compliance. Of the forty-eight countries we examine, 79% require identity documents, though only 25% require these documents to be notarized.¹⁶⁸ We note that most of these identity documents would

164. Only 14.66% of countries were fully compliant with FATF standards, 35% partially compliant, and 22.5% noncompliant. *See infra* app. B.

165. The full chart on compliance by these 100 countries with FATF recommendations is contained in Appendix B. *See* FATF, STANDARDS, *supra* note 126, at 4–5 (listing a comparison of Recommendation numbers prior to February 2012 with current Recommendation numbers).

166. A similar analysis (including partial compliance, largely compliant and full compliance) brings the total to 63.09% for Recommendation 10 and to 35.91% with Recommendation 12. For definition of noncompliance, compliance, partial compliance, and largely compliant, see *infra* app. B. For a comparison of Recommendation numbers prior to February 2012 with current Recommendation numbers, see FATF, STANDARDS, *supra* note 126, at 5.

167. Arguably, faking notarized documents is possible but much more difficult given strict government regulations of notaries in many countries and the fact that it often constitutes fraud. *See, e.g.*, *Guar. Co. of N. Am. v. Wainwright*, No. 2:09-CV-1003-MEF, 2011 WL 1807454, at *5 (M.D. Ala. May 11, 2011) (“[A] claim for breach of notary duty is essentially a constructive fraud claim.”).

168. *See infra* app. D.

not be subject to any verification and would not satisfy the compliance requirements for our field experiment.¹⁶⁹

Overall, the three tests of formal compliance provide no conclusive results and only give some indication of the level of formal compliance with international financial transparency laws. The goal of the FATF is to ensure that all international corporations are formed only after receiving identifying information. While many countries have signed on to FATF provisions and require corporate identities by law, full formal compliance with the FATF is low. The key question that is left unanswered is whether the level of compliance countries demonstrate is enough to achieve the goals of the FATF.

Even after analysis of formal compliance, the two key questions we began with still remain: is international law effective and if so, why? Given the varied levels of formal compliance, we cannot ascertain the precise extent of compliance with international financial transparency law. We can only reach this by examining actual compliance with these provisions by private bodies within these nations. Since private bodies are the ones who actually apply (or fail to apply) financial transparency laws (requiring identity documents or incorporating without such documents), they are the key to determining actual compliance with international law. And especially absent in this analysis thus far is the *cause* of such compliance. Do firms comply with international incorporation laws because they fear FATF sanctions or because it has become an accepted international norm? The analysis of formal compliance generally does not attempt to assess the causes of international compliance.

We demonstrate below how a field experiment is one approach that avoids this failure and helps shed light on whether international law is effective and why individuals comply with it.

II. THE FIELD EXPERIMENT

The central controversies of international law compliance include whether committing to international standards induces compliance, or merely reflects a prior law-abiding disposition. Thus far, however, no experimental studies have investigated compliance with international law.¹⁷⁰ And indeed, scholars crit-

169. The identity requirements in Appendix C require a list of shareholder and director names but not identity documents. Thus, those listed as partially compliant in Appendix C would be noncompliant in our experiment.

170. See sources cited *supra* note 6. And none have specifically examined

icize field experiments for not addressing the larger and important theoretical questions, instead focusing on policy studies of “what works.”¹⁷¹ This field experiment is unique in that it targets the major theoretical questions in the international law and relations literature. Whether and why international regulations are followed or flouted are important questions that strike at the heart of major disputes as to whether compliance with international law results due to sanctions or norms.¹⁷²

Through a randomized international field experiment where we use aliases and pose as international consultants seeking a shell corporation, we assess the causes of compliance with international financial transparency laws through assigning more than 1000 firms to a variety of treatment and control conditions.

The experimental approach we employ provides the potential answer to the question of whether international law is effective and why individuals comply with it. After describing the nature and construction of the field experiment and sample, we explain the logic behind the placebo and treatments and explain how they test the two dominant international law theories. The coding procedure then outlines how we determine compliance rates. Finally, we present the findings in terms of response and compliance rates.

the effectiveness of international anti-terrorism policies. Daniel G. Arce et al., *Terrorism Experiments*, 48 J. PEACE RES. 373, 373 (2011) (noting that field experiments are unique in anti-terrorism policies, with “few field experiments hav[ing] been run in this domain”). *But see* Michael Tomz, *Reputation and the Effects of International Law on Preferences and Beliefs* 32 (Draft, Feb. 2008), available at <http://www.stanford.edu/~tomz/working/Tomz-IntlLaw-2008-02-11a.pdf> (using a field experiment to understand “how international law affects preferences and beliefs,” Tomz demonstrated that international treaties may change cost/benefit calculations, stemming from an increased commitment to international law and a reputational cost of reneging on international commitments).

171. Susan D. Hyde, *The Future of Field Experiments in International Relations*, 628 ANNALS OF AM. ACAD. POL. & SOC. SCI. 72, 75 (2010) (noting that field experiments are often criticized for dealing with insignificant phenomena, failing to address the big questions).

172. This experiment is not assuming though that the subjects are working under a blank slate. Obviously, their impressions will be based not only on the treatments we give them but also on their various levels of knowledge about international laws and their opinions and business practices relating to such laws. We try to address this concern through randomization which should provide a good sampling of different subjects for each of the various treatments.

A. WHY A FIELD EXPERIMENT?

An additional advantage of the field experimental design is that it ameliorates the external validity difficulties that have limited the usefulness of laboratory experiments, and it also addresses selection bias in a way that enables the identification of causal effects.¹⁷³ While experiments offer a uniquely powerful method to identify causal effects, critics have challenged the external validity of such exercises when taking place in a lab.¹⁷⁴ Our study sidesteps many of these dangers: incorporation firms are the actual subjects of interest, the subjects are unaware they are being analyzed, and no one is self-selecting into the experiment. This advance is quite significant because, to the degree that experiments have been employed in international law, they are almost all laboratory experiments.¹⁷⁵

This study promises comparatively high external validity because it draws subjects from almost every country in the world.¹⁷⁶ Moreover, our web-based design allows us to surmount common geographical limitations. We also cluster the subject pool into major blocs of countries, such as the Organization for Economic Cooperation and Development (OECD), tax havens, and low-income countries. As a result, our international experiment does not require extrapolating findings from one region of the world to another, but rather promises results that match what we can expect in the real world.¹⁷⁷

173. See Berk, *supra* note 92, at 396.

174. For example, Levitt and List demonstrate that when subjects know they are being scrutinized (such as in laboratory experiments), and when volunteers self-select into experiments, this creates strong limits on any generalized conclusions. Stephen D. Levitt & John A. List, *What Do Laboratory Tests Measuring Social Preferences Reveal About the Real World?* 21 J. ECON. PERSP. 153 (2007).

175. See sources cited *supra* note 6. *But see*; Susan D. Hyde, *The Observer Effect in International Politics: Evidence From a Natural Experiment*, 60 WORLD POL. 37 (2007).

176. When Cohen and Dupas claimed that the results of their experiment in Western Kenya proved that free distribution of mosquito nets was more effective at preventing malaria than selling nets, they were met with critics that challenged their extrapolation of findings from one region of one country to the rest of the developing world. Jessica Cohen & Pascaline Dupas, *Free Distribution or Cost Sharing? Evidence from a Randomized Malaria Prevention Experiment*, 125 Q. J. ECON. 1, 41–43 (2010); *see also* Angus Deaton, *Evidence-Based Aid Must Not Become the Latest in a Long String of Development Fads*, in MAKING AID WORK 55, 60–62 (2007); Dani Rodrik, *The New Development Economics: We Shall Experiment, But How Shall We Learn?* 12–14 (Harvard Univ. Kennedy Sch. Of Gov., Working Paper No. RWP08-055, 2008).

177. This results in greater external validity than laboratory experiments.

B. EXPERIMENTAL DESIGN AND TREATMENTS

We used aliases and posed as international consultants seeking confidential incorporation in 182 countries. We assessed the causes of compliance with international financial transparency standards through random assignment of 1015 incorporation firms (hereinafter “firms”) worldwide to a variety of treatment and control conditions. These treatments and placebo conditions varied the information provided about international law and the rationale behind the standards. Following the success of previous social science studies,¹⁷⁸ we relied on a large pool (N > 1000) of firms worldwide.¹⁷⁹

Each experimental condition confronted firms with a decision to comply or refuse to comply with international financial transparency standards. Each e-mail made an inquiry about incorporating abroad while seeking to safeguard confidentiality and limit tax and legal liability. We used aliases to send e-mails to each service provider posing as consultants requesting confidential incorporation, which contravenes international standards. To determine compliance with international law, we examined (1) whether the firm responded to the e-mail and (2) whether or not the firm demanded certified identity documents in accordance with international law.

The experimental design included a control and three treatments that are described below.¹⁸⁰ We examined the differences between treatment and control groups to assess the effects on firms’ propensity to (1) respond to the e-mail inquiry and (2) comply with international law by requiring the disclosure of applicants’ identity.¹⁸¹ Results from this examination

178. See, e.g., Donald P. Green et al., *Getting Out the Vote in Local Elections: Results from Six Door-to-Door Experiments*, 65 J. POL. 1083, 1092 (2003) (using a sample size of 18,933 to study voting patterns in the United States); Hyde, *Experimenting*, *supra* note 175, at 517 (using a sample size of 1822 village-level observations to test whether international observers impacted the quality of democratic elections).

179. The final sample included more than 2100 international service firms and 1400 service firms in the United States.

180. The full experiment includes several other treatments, which are described in another work. See generally Baradaran, Findley, Nielson, and Sharman (forthcoming) (on file with author).

181. Treating firms as individual actors is a necessary simplification. Many firms are no doubt quite large and those responding to e-mails are likely low level employees with little discretion to deviate from company policy. However, regardless of the prominence of the employee responding to the e-mail, the response is still indicative of the effectiveness of international law.

formed the basis of characterizing a firm as being in “soft” or “hard” compliance.¹⁸²

1. Placebo

The placebo e-mails originated from aliases associated with wealthy, low-corruption OECD countries,¹⁸³ which we collectively identify as “Norstralia.” The placebo simply requested confidential incorporation with no mention of any international laws that may apply. In the placebo condition, the consultant purported to be from one of a basket of wealthy countries (Denmark, New Zealand, Finland, Sweden, Netherlands, Australia, Norway, or Austria). We also varied the name and location of the consultant to mitigate potential response bias based on a particular country of original or geographic proximity.¹⁸⁴ This “control” group of nations, “Norstralia,” should typically be associated with fairly rigid practices, come from the least corrupt countries ranked on the Transparency International’s Corruption Perceptions Index (CPI), and should generally not be perceived to be associated with international terrorism. All of the subsequent experimental conditions discussed below make use of the Norstralia countries.

2. International Standards

The first treatment invoked international standards. Through this treatment, we sought to test the regulatory power of an international institution, the FATF, which has broad support of the global community. The treatment was agnostic about *why* nations may comply with international law but did assess whether actors are more likely to comply if they know of the existence of such laws and what they require.

This treatment began with the consultant explaining FATF requirements on disclosure of identifying information when

182. See generally *infra* Part III C.3.a–b for a discussion on “hard” and “soft” compliance.

183. The OECD is composed of twenty countries including those listed in the text as well as other relatively wealthy countries such as the United States and the United Kingdom.

184. Only a few of the top ten least corrupt on the Corruption Perceptions Index (Switzerland and Singapore, for example) are excluded because they are associated with financial secrecy or other “tax-haven” conditions. Interviews and other material from the corporate sector indicate that the prospective client’s country of residence and nature of business are the primary indicators of risk to the finance industry. See KPMG INT’L, GLOBAL ANTI-MONEY LAUNDERING SURVEY 25 (2007), available at <http://us.kpmg.com/microsite/fslibrarydotcom/docs/AML2007FULL.pdf>.

forming a corporation. The consultant then stated that he would still like to maintain confidentiality and limit disclosure as much as possible. Like the control and other treatments, the consultant then asked specifically what documentation may be required to form a corporation. The managerial school of international law would expect that service providers worldwide should be more likely to follow international standards when they receive a prompt about the existence of these standards.¹⁸⁵

3. Rationalism

The second treatment invoked rationalism as well as references to international law. Like the first treatment, the consultant's e-mail in the second treatment informed the firm of the existence of the FATF, and its standards for disclosure of identifying information when forming a company. To probe a rationalist mechanism, this treatment also indicated that legal penalties may follow with a violation of these standards. The consultant stated that he would still like to avoid disclosure of private information, subtly stating that he is willing to violate international law. This treatment probed how firms respond to rationalist references to international standards and helped to evaluate if firms are less likely to comply with international law when they run the risk of costly punishment. Rationalists expect that compliance with international law should increase here relative to the placebo, and the International Standards treatment, due to existence of sanctions.

4. Constructivism

The final treatment is a constructivist one where the e-mail evoked norms of appropriateness and widespread conformity as the rationale for complying with international law. This treatment specifically informed the firm that most countries have signed on to FATF standards that require disclosure and notes that "as reputable businessmen," both the applicant and firm want "to do the right thing" by international rules, although it still asked for nondisclosure of private information, if possible.¹⁸⁶ According to constructivists, actors act ethically to ensure their behavior conforms to generally shared conceptions of appropriate conduct.¹⁸⁷ Thus, constructivism would expect that normative statements will make service providers more

185. See *supra* Part I.A.

186. See *infra* app. A for sample language for each treatment and control.

187. See *supra* Part I.B.

likely to comply with international law than the placebo condition.

C. CONSTRUCTING THE SAMPLE

This experiment required extracting data to create a subject pool of firms willing to incorporate new businesses on behalf of a client for a fee.¹⁸⁸ At the start of this experiment, no sampling frame for firms existed.¹⁸⁹ We therefore built a non-random frame from available government data and Internet information, which had not been catalogued or organized previously in a systematic way.¹⁹⁰ Some firms exist primarily as Internet entities.¹⁹¹ Others are long-established traditional companies that provide incorporation assistance, while still others are specialized law firms that offer incorporation as one of many services.¹⁹² The final result was a large sample pool of firms broadly representative of global incorporation firms that have an Internet presence.

D. BLOCKING AND RANDOM ASSIGNMENT

Before randomly assigning our treatment and control conditions, we administered a “blocking” procedure on the dataset to improve the sample design.¹⁹³ Blocking is a technique that

188. In this study, the fee ranged between \$1000 and \$3000.

189. We collected information on firms, including name, contact information, locations, service areas, and costs. In addition, to reduce bias in the selection of firms, we avoided commercially sponsored links and took great care not to duplicate correspondence to the same firms. Many firms have multiple names or are closely affiliated with other providers. Sending two e-mails to the same provider could both bias our sample and allow for detection.

190. To obtain our sample, we extracted government data and conducted extensive Internet searches to ensure a comprehensive selection of services from each nation in the sample. For the international sample, we relied almost exclusively on Google searches but also obtained data from government and commercial listings. With such an enormous market and the possibility of underground markets, it was impossible to obtain all incorporation firms. However, with extensive searching by seven researchers over a period of five months, we feel confident that we have captured a large portion of the most accessible parts of the market. Given their public presence, these firms may be more likely to be compliant than firms that are “off the radar,” as the former firms are more likely to be scrutinized by regulators and law enforcement. Therefore, we recognize there may be selection bias in this study design favor of compliance in the experiment, making this a conservative test.

191. See, e.g., THE COMPANY CORPORATION, <http://www.incorporate.com> (last visited Nov. 29, 2012) (an Internet incorporation company).

192. See, e.g., LAWINC, <http://www.lawinc.com> (last visited Nov. 29, 2012) (an Internet law firm providing incorporation services).

193. At the outset, we must note that we omit a discussion of balance sta-

places units of analysis into groups that are similar to one another. In such a situation, the experiment will better compare “like with like” and improve the experimenter’s ability to draw inferences from observed effects. Blocking is performed by taking covariates that are expected to influence the outcome of interest and using them to create natural groupings in the sample.

For the international sample, we used country groupings and service-type classifications to create the experimental blocks. We presume that countries falling into similar classifications should have more homogenous business practices.¹⁹⁴ Countries were grouped according to OECD membership, tax-haven status, relative income, and ratings for ease of doing international business. First, we clustered OECD and tax haven countries into their own strata.¹⁹⁵ To classify the remaining host countries in the sample, we formed three additional strata according to the World Bank’s *Ease of Doing Business Index*,¹⁹⁶

tistics for the blocking strata. Unfortunately, the nature of our data is such that the current dataset has no quantifiable variables with which to evaluate the homogeneity of the observations within blocks as well as heterogeneity between blocks. While a quantitative balance test would be preferable, our blocking criteria are theoretically sensible and, we would argue, sufficient for creating relatively homogeneous experimental blocks.

194. As an additional blocking criterion, we grouped firms by service type, separating law firms from specialized incorporation services. We presume that these different types of providers may respond differently to our requests and deem the covariate notable enough to warrant inclusion in the block design. We used the Coarsened Exact Matching routine in Stata to generate the statistical blocks. *See generally* Matthew Blackwell et al., *CEM: Coarsened Exact Matching in Stata*, 9 STATA J. 524, 524 (2009) (discussing the use a coarsened exact matching to improve “the estimation of causal effect by reducing imbalance in covariates between treated and control groups”). Within each blocking stratum, a treatment or control condition employing standard Stata routines was randomly assigned.

195. We generally used four OECD factors for determining whether a jurisdiction was a tax haven: (1) no or only nominal taxes, (2) low transparency in the government, (3) laws that prevent the effective exchange of information for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation, and (4) an absence of a requirement that the activity be substantial.

196. *Ease of Doing Business Index*, WORLD BANK.ORG, <http://data.worldbank.org/indicator/IC.BUS.EASE.XQ> (last visited Nov. 29, 2012). Note that some critiques of the World Bank *Doing Business* indicators provide that these indicators are problematic and push compliance with particular policy objectives which make it possible for countries to appear like great business destinations when their compliance with World Bank indicators is paper-based and not rooted in reality. *See, e.g.*, Simon Commander & Jan Svejnar, *Do Institutions, Ownership, Exporting and Competition Explain Firm Performance? Evidence from 26 Transition Countries* (IZA, Discussion Paper Series No. 2637, 2007),

with subsets for high, medium, and low “friendliness” to business among the developing countries.

We then randomly assigned an alias (and country of origin), the text of the e-mail, and the subject line of the e-mail.¹⁹⁷ We gave each treatment condition, alias, e-mail text, and subject line a unique identifying integer, and randomly assigned the integers within blocks for each corresponding condition.¹⁹⁸

E. CONDUCTING THE EXPERIMENT

We purposely conducted the entire experiment via e-mail; firms received the placebo e-mail or one of the treatment e-mails.¹⁹⁹ Each e-mail was sent from a professed consultant expressing a desire to incorporate a firm to enhance confidentiality and simultaneously limit legal liability and tax obligations.

This experiment involved deception: we sent all e-mails under aliases to service providers.²⁰⁰ Researchers generated fictitious male identities for each country identified in the e-mails to use with the correspondence.²⁰¹ While deception should be

available at <http://ftp.iza.org/dp2637.pdf>; Benjamin P. Eifert, *Do Regulatory Reforms Stimulate Investment and Growth? Evidence from the Doing Business Data, 2003–07* (Ctr. for Global Dev., Working Paper No. 159, 2009), available at http://www.cgdev.org/files/1420894_file_Economic_Response_FINAL.pdf. See generally *Doing Business*, THE WORLD BANK <http://www.doingbusiness.org/> (last visited Nov. 29, 2012) (providing reports and research from the Doing Business project).

197. See *infra* app. A.

198. We varied these slightly to avoid the risk of detection if a firm accidentally received two e-mails.

199. Examples of each are included in Appendix A.

200. Twenty-one aliases were created with associated e-mail accounts; each alias corresponded to a country used in the experiment.

201. We did not interject gender as a potential difference between treatments as all of the aliases were based on the most popular male names in the country the inquirer was based. By using the most popular name in a country, we reduced the potential for bias through minority discrimination. See Marianne Bertrand & Sendhil Mullainathan, *Are Emily and Greg More Employable Than Lakisha and Jamal? A Field Experiment on Labor Market Discrimination*, 94 AM. ECON. REV. 991, 997 (2004) (determining that, in two United States cities, people with traditionally white names were 50% more likely to receive callbacks in response to help wanted ads than those with traditionally African-American names); David Neumark, *Detecting Discrimination in Audit and Correspondence Studies* (Nat'l Bureau of Econ. Research, Working Paper No. 16448, 2010) (discussing methods for identifying discrimination through correspondence). Each e-mail address was created by combining an alias with a Gmail extension in the following form: “alias@gmail.com.” The names were carefully vetted so that no special connotation would accompany any alias, such as a famous actor or athlete.

avoided when possible in research, the creation of fictitious personas enabled systematic variation of the placebo and the treatments. Furthermore, this fairly low level of deception may have helped to create an environment in which the subjects behaved most naturally. This is an essential motivation for field experiments,²⁰² especially where the behavior of subjects may be inappropriate.²⁰³

Furthermore, we drafted thirty-three unique e-mails and randomly assigned them to each observation. We wrote each e-mail according to the same criteria but infused them with different styles, syntax, and diction to ensure uniqueness.²⁰⁴ Employing a wide variety of approach e-mails both minimized the possibility of detection and mitigated the outlier effects of any particular e-mail text.²⁰⁵ Furthermore, the strategy allowed us to control for individual e-mail effects in our final analysis, ensuring that an alternatively-worded e-mail evincing strong fixed effects did not bias our results.

F. CODING PROTOCOL

For full compliance, the FATF mandates that firms require certified identity documents from customers before creating a company.²⁰⁶ International standards dictate that firms should then maintain this documentation so that the company's true owners can be uncovered by law enforcement if necessary. Without such identity documents, there is no way to determine

202. See ROYCE SINGLETON, JR. ET AL., *APPROACHES TO SOCIAL RESEARCH* 451 (1988) ("The basic rationale for deception is that it is necessary in order to place research participants in a mental state where they will behave naturally . . . subjects typically will act so as to present the most favorable impression of themselves . . .").

203. No laws were violated by the subjects in this study.

204. With aliases originating in countries where English is not the native language, we introduced two minor grammar, syntax, or spelling errors to increase authenticity.

205. We carefully reviewed each e-mail to ensure that no details were presented disproportionately, thereby biasing treatment effects and creating potential outliers. Despite the similarities, each e-mail differed enough to limit detection potential if one service was to receive two of our experimental e-mails. None of the specific texts were found to be statistically related to outcome measures, so the textual differences did not bias the results. Likewise, none of the aliases linked to specific countries were significantly related to outcomes, indicating no meaningful differences across the aliases.

206. This includes a certified copy of at least one official photo identity document like a notarized copy of a passport picture page or national identification card. For full compliance, proof of address is required, which can come for instance with a notarized utility bill. See *supra* Part I.D.1.b.

who is really in control of the new corporation. The company becomes in effect anonymous and thus a perfect vehicle for engaging in a wide range of illicit activities.

We coded responses to e-mails as compliant, partially compliant, non-compliant with international standards, or as a refusal of service.²⁰⁷ Codes were also assigned for the specific documents that service providers requested from the alias consultant.²⁰⁸ We categorized firms that required notarized/certified photo identification as “compliant.”²⁰⁹ We coded firms that only required a non-notarized/uncertified copy of photo identification as “partially compliant.”²¹⁰ Finally, we classified firms that do not request any kind of documentation as “non-compliant.”²¹¹ For the firms that refused to provide assistance, we distinguished between non-respondents and refusal to provide service.²¹² This detailed coding scheme allowed us to develop a categorical, unordered set of outcomes that captured

207. If more than five business days passed with no response from providers, the researcher playing the consultant role sent a standardized, brief second e-mail. When a firm’s initial response to the approach e-mail failed to specify the requirements for identity documentation (if any), researchers pulled from a standardized pool of response scenarios and drafted a suitable follow-up e-mail. In each case, the researchers responded to as many questions as prudent, and then referred back to the initial e-mail and requested information pertaining to the service’s requirements for identifying documents.

208. The e-mails are cross-checked to ensure reasonable standardization before sending them out. For example, when providers requested a Skype or phone conversation, research assistants stressed that travel commitments made this unworkable, and that communication must occur via e-mail. When providers suggested multiple options for incorporation (e.g., a choice of a Nevada or Delaware company), the protocol was to choose the option preferred by the provider, or where there was no preference, to select the first option mentioned. With respect to questions about taxes, research assistants indicated that this was being addressed domestically.

209. See *supra* note 126 for discussion of notarized documents.

210. See *supra* note 126 for discussion of notarized documents.

211. To more carefully distinguish between “compliant,” “partially compliant,” and “non-compliant” services, we further parsed response codes according to the specific types of documents required by each service. Using a series of “document codes,” we recorded each relevant identifying document as outlined and clarified by the FATF and the Basel Committee, respectively. See BASEL COMM. ON BANKING SUPERVISION, CUSTOMER DUE DILIGENCE FOR BANKS 9–13 (Oct. 2001), available at <http://www.bis.org/publ/bcbs85.pdf>. For example, we recorded whether the service requires a notarized passport copy, a passport copy, or an in-person visit. We also capture requests for address proof (such as an original utility bill), bank reference letters, business plans, funding source disclosure, curriculum vitae, and a variety of other identifying documents that are suggested by the Basel Committee.

212. We also analyzed the content of the received e-mails to trace motives and rationales.

more fully the levels of compliance with international standards.

Once we obtained the specified information about identity documents, researchers informed firms that their “needs have been met” and they no longer needed the firms’ assistance. To maintain the experiment’s security, all correspondence occurred through specially created e-mail accounts and telephone numbers used to verify the accounts.²¹³ We used proxy servers to randomly assign IP addresses around the globe (with a concentration in East Asia and Europe) to prevent firms from determining that e-mails actually came from the United States. To maintain anonymity of subjects, once we received the correspondence from the firm, we deleted all identifying information and analyzed subject companies using only their randomized identification numbers.²¹⁴

III. RESULTS FROM A TEST OF COMPLIANCE

To accurately determine the effectiveness of international law, we must examine response rates and compliance rates, both formal and informal, with international law. First, we determined whether the international firms responded to an inquiry about confidential incorporation. Next, we tested whether they complied with international laws requiring disclosure of identity. This test involved formal and informal compliance. For our purposes, formal compliance was measured by examining the acts taken by the sovereign nation to implement and enforce international financial transparency laws. To gain insight, we examined an earlier analysis of the international law commitments undertaken by the nations relating to financial transparency.²¹⁵ This provided some useful information that demonstrates a nation’s willingness to comply with international law. But, as discussed above, formal compliance cannot tell the entire story.²¹⁶ Despite laws and procedures, it remains to be seen whether anonymous shell corporations can still be formed in each nation. A test of actual compliance at the level of private actors measures the effectiveness of the nation in implementing and enforcing international law and disseminat-

213. We used foreign cellular accounts to avoid detection.

214. Before filing copies of correspondence for future reference, we purged all identifying information from them. Copies of correspondence are on file with the authors.

215. See *supra* Part I.D.1.b.

216. See *supra* Part I.D.2.

ing such rules to the firms in the jurisdiction.²¹⁷ To the extent these firms ignore international law, it is an indication that their nation is not conforming to global standards that require sanctioning of firms that do not comply with these provisions. After preliminary results examining response rates in Part III.A, Part III.B discusses compliance rates that indicate surprising results about the proportion of private actors likely to comply with international law. We discuss the implications of the results and compliance rates in the next section.

A. EXPERIMENTAL RESULTS ACROSS TREATMENT AND CONTROL CONDITIONS

We now turn to an analysis of response rates across treatment and control conditions. We report experimental results for 1015 firms here.²¹⁸ The subject must make a decision to reply to an e-mail request in the first place, following which compliance with international requirements to demand identity documents is a second step. But that initial decision to respond can be analyzed in its own right and should indicate something important about the effects of the treatments on the willingness of subjects to correspond with the potential customers. After all, if firms do not reply, they cannot violate international standards. In a key way, then, non-response for some subjects may indicate a “soft refusal” to do business with a potential customer and is certainly less costly or bold than outright withholding of services. Our background interviews with service providers strengthened this interpretation.²¹⁹ While many of the non-responses may be the result of disinterest or poor management of correspondence on the part of subjects, randomization across treatments should have balanced these tendencies across the subject pool. Any significant differences in response rates should then indicate meaningful treatment effects for subjects’ propensity toward soft refusal.²²⁰

217. See *supra* Part I.D.1.

218. The balance of subjects received alternative treatments and are reported elsewhere. See Baradaran et al., *supra* note 180. Note that some services either returned error messages indicating invalid e-mail addresses or responded in a foreign language.

219. Before conducting our experiment, we interviewed firms and collected information on them regarding services, costs, contact information, and locations.

220. Before conducting our experiment, we surveyed fifty-nine international studies scholars to gauge their expectations of our response outcomes (survey results on file with authors). On average, the scholars guessed that 42% of

Table 1 lists the response rates and compliance rates for the placebo and treatment conditions. Firms were classified as “compliant” if they demanded notarized identification, thereby being fully compliant, or refused service. Otherwise they were scored as non-compliant (partially compliant firms are categorized here as non-compliant). Table 1 also lists the response rates for the placebo and treatment conditions indicating statistically significant mean differences from the control condition.²²¹

Table 1: Response and Compliance Rates Across Experimental Conditions²²²

Condition	Total Sent	Number of Responses	Response Rate as a Percent	Number Compliant	Compliance Rate as a Percent of Responses
Control	268	153	57.1	82	53.6
Int'l Standards	232	126	54.3	66	52.4
Rational	254	120	47.2**	51	42.5***
Construct	261	142	54.4	68	47.9

Notably, only the rationalism treatment led to a significant decrease in response rates compared to the placebo condition—with nearly 10% fewer responses.²²³ These differences in response rates suggest that some firms exercise discretion in their correspondence with potential clients. Apparently, if the subjects are primed about law *and* its consequences, a significant set of firms fail to respond to the request for incorporation.

subjects would respond, with a standard deviation of 22%. The actual response rate averaged 51%; the actual rate was higher than the experts expected.

221. Analysis of experimental data typically proves more straightforward than is often the case with observational studies. The values of confounding variables—both observed and unobserved—have been balanced across the conditions, and the blocking procedure likely improved the balance yet further. Thus, simple difference of means tests employing *t*-statistics can be used to report treatment effects. In the far right column we report compliance rate as a percent of responses.

222. Difference from control condition in two-tailed *t* test: * significant at .1 level, ** significant at .05 level, *** significant at .01 level.

223. This is a difference that is statistically significant at the .05 level in a two-tailed *t* test.

The rationalist treatment also caused a significant decrease in compliance rates for those firms that did respond as compared to the placebo, with compliance falling more than 11%: from 53.6% in the placebo condition to 42.5% in the rationalist condition. Thus, the rationalism treatment led to an increase in “soft compliance,” by a larger number of firms refusing to respond, but when firms did respond, they were less likely to comply.

Interestingly, we found no statistically significant response rates for the other conditions. Mention of international standards and the FATF alone (without noting possible consequences) had no significant effect on response rates or compliance rates. The constructivist treatment, which explicitly mentioned that being “reputable businessmen” required compliance with international norms, did not induce differences in response or compliance rates compared to the placebo condition.²²⁴

We now turn to examining response and compliance rates broken down by country groups, including tax havens, OECD countries, and high, middle, and low income countries. In the overall sample, 28% of the service providers contacted and 53% of those who actually responded were willing to defy international standards in providing a shell company without requiring notarized proof of the customer’s identity.²²⁵

224. Arguably, individuals who seek to act illegally may also rely on constructivist norms, but our field experiment examines whether the firm interprets this cue as a reason to comply with international law or not comply. This is the relevant decision.

225. See *supra* note 126 for discussion of notarized documentation.

Table 2: Non-Compliance Rates Across Country Groups²²⁶

Country Group	Number of Firms	Number of Responses	Response Rate as a Percent	Number of Non-Compliant Firms	Non-Compliance Rate as a Percent of Responses
OECD	246	137	55.7	68	49.6
Tax Havens	254	172	67.7***	65	37.8
Upper, Middle, and Lower Income Countries	515	231	44.9***	152	65.8

“Tax haven” countries showed a 12% higher response rate than OECD countries, with the difference statistically significant at the .01 level.²²⁷ Upper-middle and lower-income countries,²²⁸ however, replied at rates nearly 20% lower than tax haven countries, again significant at the .01 level.²²⁹ Middle- and lower-income countries also responded at significantly lower rates compared to OECD countries, perhaps indicating that firms in wealthy countries are better equipped to deal with international requests for incorporation.²³⁰

B. COMPLIANCE RATES WITH INTERNATIONAL LAW ACROSS CONDITIONS

We first provide the raw results on compliance that do not incorporate response rates. Following, we discuss how to esti-

226. Significant at .01 level compared to OECD in two-tailed *t* test; ** at 0.05 level.

227. See *supra* Table 2.

228. Here, we grouped lower-middle and lower-income countries together.

229. We then created a measure of compliance, employing a dichotomous variable with non-compliance and part-compliance scored as “0” and compliance and refusal scored as “1” (with non-responses excluded). When we tested the differences in compliance levels among country groups, the disparities remain statistically significant at the .01 level compared to the tax-haven countries.

230. This could be due to the importance of their complex and sensitive financial sectors.

mate a selection model that permitted us to adequately account for selection into the compliance analysis through an e-mail response. Finally, although we feel non-response likely reflects soft refusal, we discuss additional tests we performed to consider the chance that non-respondents were not “treated” and consequently estimate the potential treatment effect on the treated.²³¹

Beyond response rates, we also constructed a measure that assesses how the treatments affect the propensity to comply with international standards. We undertook this analysis a bit more cautiously, however. It seems clear that compliance rates depended crucially on response rates. That is, if a failure to reply to a request may—for some significant set of subjects at least—indicate a soft refusal of service, then any inferences drawn from rates of compliance must also consider response rates.²³² Thus, an accurate analysis of compliance rates may require the inclusion of response rates.

We categorized both non-compliance (a failure to request any kind of identifying documents) and partial compliance (requiring only uncertified documents) as “non-compliance” and then scored them 0 in a binary indicator of compliance.²³³ We did this because while requiring non-notarized documents may be better than not asking for any documents, photocopies of both driver’s licenses and passports are notoriously easy to fake.²³⁴ Thus, firms employing such a relaxed application of international standards will likely facilitate many more untraceable shell corporations than firms requiring certified docu-

231. In this analysis, we dealt with e-mails that were undeliverable or returned in a foreign language by treating them as untreated observations. *See supra* note 218. Untreated observations are so few that they are statistically insignificant, but this analysis nonetheless enables us to rule out “failure to treat” as a potential source of bias.

232. For example, one provider accidentally forwarded us an internal e-mail discussion after receiving a follow-up e-mail from our alias. One firm employee asks another: “This one has also come back again. Will I pretend it went into junk or reply?” The actions of this provider demonstrate that, some services may purposely not respond, indicating a soft refusal to violate international law. This is why we account for response rates and compliance rates in two separate analyses.

233. These results are robust as to treating partial compliance as compliance.

234. *See, e.g.,* Oriana Zill, *Crossing Borders: How Terrorists Use Fake Passports, Visas, and Other Identify Documents*, PBS FRONTLINE (Oct. 2001), <http://www.pbs.org/wgbh/pages/frontline/shows/trail/etc/fake.html>.

ments.²³⁵ Additionally, we categorized firms that refused service or required notarized documents as “compliant.”²³⁶ Table 3 below reports the results for compliance ratios with international law comparing the experimental conditions with the control.²³⁷

Table 3: Compliance Rates across Experimental Conditions

Condition	Compliance Rate Across Conditions
Placebo	53.6
Int'l Standard	52.4
Rational	42.5
Construct	47.9

In analyzing compliance rates, the rationalist treatment, which combines mention of the FATF with a reference to possible legal penalties, has a significant effect on compliance rates as measured, and the effect is negative—it induces *less* compliance than the placebo condition.²³⁸ This result was unexpected and is discussed in Part III.C. The rationalist treatment also induced more soft refusal than hard compliance, meaning firms receiving the rationalist treatment preferred ignoring a firm to directly refusing service.²³⁹

235. We note that since some e-mails indicated familiarity with the FATF some firms may have thought that they could ask for documents and assume that they must be notarized. We made sure to avoid this problem with following up on the request to determine if they required notarized documents if the initial response did not make this clear.

236. We gave them a score of 1 in the binary indicator. Non-response is considered in the first stage of the selection analysis as prior to compliance or non-compliance.

237. One difficulty is that most two-stage models cannot identify the model without the addition of different information. We thus used a selection model allowing the same identification parameter—in this case treatment condition—to see how it affected both selection (response) and the outcome (compliance). See Anne E. Sartori, *An Estimator for Some Binary-Outcome Selection Models Without Exclusion Restrictions*, 11 POL. ANALYSIS 111, 111 (2003) (providing “[a] new maximum likelihood estimator for selection models with dichotomous dependent variables when identical factors affect the selection equation and the equation of interest”). The selection model also enabled us to analyze intravariation relations between response and compliance, thereby obtaining highly statistically significant results.

238. This finding is significant at the .01 level. See *infra* app. F.

239. This finding further suggests an intravariation relationship between response and compliance, which reinforces our need for using a selection mod-

These results confirm the descriptive statistics showing that OECD countries have higher response and non-compliance rates as compared to response rates generally. A similar effect occurs for the rationalism treatment in OECD countries. These results thus suggest some additional differences in the treatment effects, especially as it relates to country grouping that will be discussed in the next section.²⁴⁰

These results also support in some ways the expectations about OECD countries developed in international law theory, but they are surprising in others: mainly, the relatively high soft compliance rates in conjunction with relatively low hard compliance rates.²⁴¹ The expectation for results would be a lower response rate matched with a *higher* compliance rate, for OECD countries. Some firms would react to the treatment information by not responding, while others would react by being more conscientious in requiring identity documents.²⁴² Yet virtually no firms reacted by informing clients that the requested activities were illegal, regardless of whether the client already knew.²⁴³ Thus, the statistically lower response rate for rationalism, and lower response rates generally, indicate that the treatments may have induced some soft compliance. But why did they not also simultaneously induce hard compliance? In other words, why is it that on the one hand the rationalism treatment made firms more likely to comply with international

el. *See supra* note 237.

240. Finally, we reanalyzed the results considering all non-responses as though the treatment e-mails never arrived. Thus, as opposed to the exercise above where non-response was considered as substantively meaningful, here we regarded the problem merely as a statistical fix. We included the bounced e-mails as well as the foreign language replies. The results when we estimated the treatment effect on the treated are similar to those contained in Table 2: each condition displays a negative treatment effect. The rationalism treatment is still statistically significant at the levels reported in Table 2, but now constructivism is also negative and significant for compliance at the 0.1 level.

241. To compare compliance rates with expected compliance rates, we also surveyed international studies scholars to predict the compliance rates across the field experiment. They actually over-estimated compliance rates, estimating that, on average, 64% of firms would comply with international law. This was considerably more optimistic than the observed compliance rate of 49%, demonstrating lower actual compliance than expected compliance internationally.

242. To be sure, by agreeing to break the law versus just allowing the client to break the law, the firms may have been acting in a more risky manner.

243. Our finding, that firms across different treatments were all reticent to employ hard compliance, suggests that treatment alone does not account for firms' preference for soft compliance. Rather, some other consideration seems to dictate this preference.

law through non-response, but at the same time, less likely to follow international law through hard compliance? This is in essence what is happening with the mismatched response and compliance rates with the rationalism treatment. A few explanations of this phenomenon and other counterintuitive results follow below.

C. DISCUSSION WITHIN INTERNATIONAL THEORETICAL FRAMEWORK

To gain an understanding of how effective international law is, we analyze the nations' formal compliance with laws (regulatory and enforcement mechanisms put into place to enforce international law domestically) and actual compliance (the actions of individual private firms). To test actual compliance with international law we must look to the private actors in these nations in a natural setting. Whether a group of firms comply with international law demonstrates whether the international law agreed to by their home nation is effective. Thus, the effectiveness of the law in this area is an accumulation of individual firms' decisions that may result due to norms or incentives put into place by a nation, and motivations of the firm. The decision of these firms to comply or not comply with international law expresses the weaknesses (or strengths) of the formal structures put into place by their nations and also sheds light on which international theory best determines compliance. Since firms are the key players in following or violating international law, their motivations prove significant in determining whether international law is effective and how effectiveness can be improved. With that, we now turn to exploring whether individuals comply with international law and what their motivations are when they do comply.

1. Do Individuals Comply with International Law?

International law requires identity information to ensure transparency while forming a corporation.²⁴⁴ The following reply to one of our inquiries from a U.S. firm indicates the disregard of such international laws: "All that you need to do is to provide the name you want for your new company, that's it."²⁴⁵

244. See *supra* note 126 (discussing notarized documents) and notes 133–139 (discussing FATF requirements).

245. A similar response stated: "We don't need a whole lot of info from you. You can place the order on our website under 'starting your company.' It should only take 10 minutes and that is all the information we need from you."

The subjects respond to the inquiry to form a confidential corporation as the first step in determining whether nations comply with international financial transparency laws. To get a broad picture of overall international compliance, we review the results from a test of formal compliance,²⁴⁶ and examine actual compliance below.

To determine whether countries comply with international law, we compare formal compliance rates with actual compliance demonstrated by our field experiment. To get at both formal and actual compliance, we examine the national legal framework as well as the actions of private actors in each nation who carry out the obligation of the nation to comply with international laws. Next, we briefly examine blocks of states (OECD members, tax haven, high-middle income and low-middle income states) to see if we detect any significant differences in formal and actual compliance between blocks of countries.²⁴⁷

Overall, formal compliance results are mixed. Over 180 countries have signed and ratified the FATF and international transparency laws and have accepted its framework.²⁴⁸ Digging deeper, we examine the percentage of these countries that are actually complying with these laws. Formal compliance indicates mixed results. Ninety-six percent of countries have ratified national laws requiring identity documents upon incorporation.²⁴⁹ Yet FATF evaluations show that only 40% of countries comply with FATF provisions,²⁵⁰ though closer to 75% of countries are largely and partially compliant with these provisions.²⁵¹ With formal compliance numbers, it is hard to determine whether countries are actually complying with international laws, since there is no way to know based on the legal landscape how easy it is to form a shell company in the particular jurisdiction. Thus, we turn to actual compliance to

246. See *supra* note 232 and accompanying text for a discussion of the test of formal compliance.

247. Significant discussion of differences in results between blocks of countries and individual countries will be dealt with at length in a follow-up piece.

248. See *supra* note 149 and accompanying text.

249. See *infra* app. B.

250. See *infra* app. B.

251. See *infra* apps. B & D. This brings up the question of what percentage compliance would demonstrate appropriate compliance. For instance, would a state comply with an antiterrorism provision if fifty illegal shell companies were formed each year? One hundred? We do not reach this important question here but leave this discussion for future researchers.

determine whether the aims of financial transparency laws are being met internationally.

To determine actual compliance, we exclude non-responses and examine the level of compliance by private actors with international laws. Our field experiment reveals a lower than predicted result: only half of countries (49%) complied with international law, as measured by reviewing the laws passed in compliance with international law and the level of their enforcement, which may surprise both rationalists and constructivists.²⁵² The international laws at stake are relevant here. The laws tested here are the international standards of financial transparency, which have been ratified and deemed significant to the worldwide effort to stop corruption and the financing of terrorism.²⁵³ The importance of these laws and the consensus about the import of these norms suggest that we should see higher rates of compliance than for ordinary international laws.

We first examine the rationalist and constructivist reaction to the moderate international compliance findings. Given the strength of the international norms supporting these laws, constructivists might expect high rates of compliance.²⁵⁴ Constructivists would be surprised that despite the high acceptance of these laws and the norms of global cooperation surrounding these laws, that compliance with them is still weak.²⁵⁵ Constructivists would likely be most surprised by the relatively low levels of compliance by FATF member countries, who have agreed to uphold these laws and thus should demonstrate the highest level of compliance among all of the signatories.²⁵⁶ However, these member countries actually demonstrate lower compliance rates in our field experiment compared to non-member countries.²⁵⁷

252. International scholars predicted that 64% of international services would comply with international law.

253. See notes *supra* 123–29 discussing high profile nefarious activities taken behind the protection of anonymous shell companies by Iran, Libya, al-Qaeda and North Korea; see also *Undeclared Beneficial Ownership: Licence to Loot*, *supra* note 131, at 64 (“An al-Qaeda fund-raiser (using a company called Truman Used Auto Parts), Iran (which owned a Manhattan skyscraper), and Viktor Bout (arms trader now facing trial) are among those that America’s lax regime has benefited.”).

254. See *supra* Part I.B.

255. See *supra* Part I.B.

256. See *supra* Part I.B.

257. See *infra* app. E.

Some rationalists may also be surprised at the relatively high level of compliance with international laws, as they generally expect low compliance with international law, due to the low risks of sanctions and weak enforcement of international law.²⁵⁸ Rationalists might explain higher than expected compliance with the threat of potential sanctions that result for countries that fail to comply.²⁵⁹ And while the private actors here are not directly subject to such sanctions that are targeted at the national government, international law requires that governments sanction private bodies that do not comply with FATF provisions, and the compliance rate by private actors shows how important the fear of sanctions is to that government.²⁶⁰ Thus, governments that comply with such laws and fear sanctions for noncompliance would allow such fear, through sanctions, to trickle down to the bodies that have the responsibility for implementing these international laws.²⁶¹ Overall, the results demonstrated by our field experiment showing nearly 50% compliance with international law leave room for further debate by optimists and pessimists as to the significance of international law. Even if we consider all of the non-responses as compliant, the non-compliance rate—where firms failed to require notarized identification—would still range between 26 and 28%.²⁶² This suggests that savvy customers would, on average, have to contact fewer than four firms to find one that would make anonymous incorporation relatively easy.

2. Who Complies with International Law?

After examining whether firms comply with international law, an important remaining question is *which* countries' firms tend to comply. While we do not undertake an in depth country-by-country analysis here, we present broad trends which chal-

258. See *supra* Part I.A.

259. See *supra* Part I.A.

260. Fear of sanctions may not outweigh the cost of developing the capacity to comply or investing the resources to comply with provisions.

261. However, our experimental results only partly support this conclusion. A treatment priming the threat of legal penalties indeed decreased the proportion of responses from subjects, but the same prompt also decreased the proportion of those responding who complied with international law. Only for some subjects did the threat of sanctions move them. Others were willing to offer anonymous incorporation despite the primed risk of legal penalties.

262. See *supra* note 168 and accompanying text.

lunge the premise of managerial theory.²⁶³ The managerial school theorizes that national compliance depends on relative wealth and resources and an ability to enforce international laws. Interestingly, our results are inconsistent with managerial theory by demonstrating that relative wealth levels do not influence compliance rates.²⁶⁴ We find that when it comes to *formal* compliance, the results are just as the managerial school would predict—the highest compliance rates are among high-income countries, then middle-income followed by low-income countries. However, in examining *actual* compliance, tax haven countries show the highest response and hard compliance rates. Indeed, we demonstrate that tax havens actually have 12% higher response and compliance rates than OECD countries, and more than 20% higher response and compliance rates than developing countries.²⁶⁵

High response rates from tax havens may be explained by the fact that these firms are almost exclusively focused on foreign customers, and so they may be more accustomed to responding to inquiries from abroad. Their counterparts in middle and low-income countries may be less accustomed to foreign businesses and thus may be less likely to follow up on e-mail inquiries. The greater response and compliance rates in tax havens compared to OECD countries demonstrate that there is not a strong relationship between income and compliance.²⁶⁶ This finding undermines managerialist school expectations, which maintain that violations are more likely to be a product of a lack of resources or knowledge rather than deliberate transgressions.²⁶⁷ Indeed, when we explicitly gave subjects in-

263. We reveal a more in depth country-by-country analysis in a forthcoming piece.

264. See *infra* app. D. Upper-middle and lower-income countries, however, replied at rates nearly 20% lower than tax haven countries, again significant at the .01 level. The response rates for lower-income countries being less than tax havens may support managerial theory. However, there is no statistically significant difference between middle- and lower-income countries and OECD countries.

265. This is statistically significant at the .01 level. Firms based in the low- and middle-income countries and middle-high income countries were also significantly less likely to respond (at the .05 level) than those in the OECD countries and replied at rates 20% lower than tax haven countries (at the .01 level). We grouped lower-middle and low income countries together, based on the *World Bank Ease of Doing Business Index*. See *supra* note 196 and accompanying text.

266. There is no significant income difference between tax haven and OECD countries; we classify both as high-income countries.

267. See *supra* Part I.B.

formation about international law in our experiment, it did not improve compliance rates—rather, it decreased compliance, albeit not in a statistically significant way. The findings also suggest that the emphasis placed on improving international standards through “capacity building” or training may be misdirected.²⁶⁸ Thus, we find little consistent relationship between wealth of countries and compliance rates in our field experiment. Therefore, we explore an alternative explanation for differences in compliance rates.

3. Why Comply with International Law?

Based on the international law theory expressed, our field experiment reveals varying response rates as well as varying compliance rates if we analyze non-responses separately.²⁶⁹ It thus sheds light on why firms comply with international law. The results in this area are complicated and deserve some discussion. The discussion that follows first addresses response rates or “soft compliance,” then actual compliance rates, or “hard compliance.” While the last section discussed overall compliance, this section examines the effect of the various treatments—or theories of international law—and how they influence compliance.

a. *Soft Compliance*

We noticed increased soft compliance, as demonstrated by lower response rates, only with the rationalist treatment. We note here, however, that a relatively small proportion—roughly 10 to 20% of the overall subject pool—might be considered “soft” refusals by failing to reply. We followed up on non-responses with several rounds of inquiries from different aliases, culminating with a “non-response check” that was the most innocuous we could design: the e-mail made no mention of a need for confidentiality, taxes, or legal liability and did not inquire after documents. In essence, this check sought to verify that the subject firm was still in business and assisting customers. Fully 52% of the non-responses failed to reply even to this no-threat inquiry, suggesting that only a minority of non-responses are soft refusals.

Nevertheless, for a non-trivial share of firms, the appropriate interpretation appears to be that non-responses are tanta-

268. See *supra* note 247 and accompanying text.

269. It is proper to analyze non-responses separately because most reflect exogenous factors that limit firms’ capacity or desire to respond.

mount to soft compliance. One observation that supports rationalism is that a significant share of firms are more likely to demonstrate soft compliance with international law when prompted that it exists and when told that there are penalties associated with noncompliance. Another observation is that neither mention of international standards nor a normative rationale for following them (constructivist treatment) induced significantly higher compliance than the placebo condition, where there was no mention of these standards. These findings are discussed in turn below.

International firms were more likely to demonstrate soft compliance with international law when informed about the existence of such law and when informed that penalties are associated with noncompliance with these laws. As such, firms responded at statistically significantly lower rates to the inquiry when penalties were invoked than when there was no mention of international law or when there was mention of international law without warning of penalties.²⁷⁰ When we informed subjects that international laws had associated penalties (rationalism treatment) and told them about the law and what it required, subjects who responded were less likely to comply. Indeed, the overall compliance rate (summing compliant responses with refusals) was 20% for the rationalist condition versus 31% for the placebo. This is mixed evidence for the rationalist camp, which argues that nations are more likely to comply when informed of penalties or sanctions associated with international law, rather than when they are simply made aware of the law.

One set of subjects appeared to comply “softly” through no response. But among the rest of the subjects that did reply, they were significantly less likely to follow international law. What is more, these effects seem offsetting, suggesting that many of the subjects failing to respond were those that would likely have complied if they had replied.²⁷¹ Indeed, despite a prompt about legal penalties, it appears that a significant number of firms are willing to offer anonymous incorporation regardless of the threat of sanctions.

Surprisingly, firms were not more likely to show soft compliance with international law when they were informed that it

270. Both low response rates of the rationalist treatment were significant as compared to the control, which made no mention of international law.

271. This result is what clinicians call a “heterogeneous treatment effect,” meaning that the treatment affected some subjects differently than others.

was the international norm to comply with such laws. In the constructivist treatment, we explicitly mentioned the FATF and its disclosure standard, discussed that most countries have signed onto the standard, and remarked that we understood that we were operating as “reputable businessmen.” Notwithstanding these clear prompts and reference to widely accepted international norms,²⁷² the constructivist treatment induced response rates statistically indistinguishable from the control condition and from simply mentioning the international standards. Thus, an appeal to shared norms and reputation makes little difference to firms when weighing whether or not to comply with international law.²⁷³ We find this result both surprising and quite interesting as it undermines constructivist accounts of compliance with international standards.²⁷⁴

However, it is important to note here that appeals to international norms may be more persuasive to government representatives than private actors. Thus, if the subjects of our study were government actors, they may have been more likely to comply if they were informed of norms because they may place a greater emphasis on international reputation.²⁷⁵ This result may still demonstrate something important for obtaining better general compliance with international law. The ineffectiveness of appealing to norms may demonstrate that the government should favor threats and sanctions over appeals to norms for private actors. Overall, thus far, there is little support for the hypothesis that reputational concerns will prove sufficient to motivate compliance.²⁷⁶ Instead, this finding tends to support the rationalist view of rules and compliance as a product of

272. Note though that as “clear” as these prompts may be, the client is stating that he wants to keep information secret notwithstanding the law that requires the information to be made known. See *infra* Part III.C.4 discussing conspirator theory of rationalism.

273. Arguably, shared norms have also been internalized and may be significant to subjects without mention. If this is the case, these norms are still not able to induce the level of compliance as fear of legal penalties, under the rationalist model. Being reminded of legal penalties induces compliance at a much higher level than reminding subjects of the international norms at play.

274. *E.g.*, THOMAS M. FRANCK, THE POWER OF LEGITIMACY AMONG NATIONS 16 (1990); Jeffrey Checkel, *Why Comply? Social Learning and European Identity Change*, 55 INT’L ORG. 553, 557–59 (2001).

275. FRANCK, *supra* note 274, at 16.

276. See Beth A. Simmons, *International Law and State Behavior: Commitment and Compliance in International Monetary Affairs*, 94 AM. POL. SCI. REV. 819, 819 (2000) (noting that most studies are not able to show credibly that international rule compliance is based on anything other than immediate state interests).

power.²⁷⁷ The next section goes beyond response rates to determine hard compliance with international law, and to determine why international firms that responded decided to comply with international financial transparency laws.

b. Hard Compliance

Thus far we have only discussed soft compliance, or whether the subjects refused to entertain our inquiry for a confidential corporation in the first place. Now we examine hard compliance to determine, when subjects decide to comply or not comply with international law, why they do so. We arrive at this result by examining whether nations require the requisite information and documentation from the potential clients, as required by the FATF and other international law. Overall, the findings indicate—against our intuition and rationalist expectations—that mention of legal penalties results in *lower* hard compliance with international law.²⁷⁸

Hard compliance rates were highest when we made no mention of international law (control), followed by when they were prompted about the existence of international standards and, finally, when prompted about associated norms against noncompliance. Interestingly, firms were *less* likely to manifest hard compliance with international law when they were informed about penalties associated with such laws. At first blink, a rationalist would expect that a firm would be more likely to comply with international law when informed that there are penalties for noncompliance. However, the opposite result occurs, with lower hard compliance rates with the rationalist treatment.²⁷⁹

There may be several explanations for why the threat of penalties produces both lower response rates and lower rates of hard compliance. As noted above, it seems that the firms' initial choice of whether or not to reply creates a sub-set of firms that is more risk-acceptant or risk-insensitive than the initial sample. According to this logic, those most likely to be compliant with international standards, most attuned to the dangers of providing anonymous shell companies, or most uncomfortable

277. DREZNER, *supra* note 76, at 204–05.

278. See *supra* Part I.A (discussing rationalism). We were not alone in this intuition. We surveyed an expert panel of sixty-three international political economy scholars prior to conducting the research, and 69% expected that the rationalist condition would increase compliance compared to the placebo.

279. These results are statistically significant at the .01 level.

with expectations of international law, choose not to respond in the first place, altering the sample of responding firms to favor those who may be less likely to comply. Firms seem to respond to risk by refusing service, rather than by changing their propensity to apply international standards. If a firm is content to accept a customer, they then follow their standard customer due diligence procedure—which may be little or nothing. While this explains low response rates at the outset, it does not explain why hard compliance rates are actually *lower* when the firm is informed about penalties for noncompliance. We offer explanations for this counterintuitive result in the form of two conjectures.

4. Conspirator Effect of Rationalism

One way to explain the discrepancy between higher compliance at the outset followed by lower compliance once responses are received is by what we call a conspirator theory of rationalism.²⁸⁰ The high soft compliance (low response) followed by lower hard compliance may provide information about what the firm believes that the potential client knows, and the firm's potential fear (or lack of fear) of being caught. What the firm believes the client knows affects the firm's decision. A noncompliant firm once placed on notice by a client that it is being asked to do something illegal has received a signal that the client is a co-conspirator and less worried that it will be reported to the authorities. Indeed, this signal that the client is willing to violate international law is strongest with the rationalist treatment because under that treatment the client wants to violate international law even though she understands and explicitly acknowledges that penalties may result from doing so. On the other hand, if the potential client were naïve and realized that she had been asked for something illegal, she may be more likely to report the violator (the firm) to the authorities.

So the savvy firm, which is aware of international law, feels safer with the conspirator's request and is more likely to offer services that do not comply with the law to that individual than to the naïve client. This may explain why the rationalist treatment induces lower response rates than the other treatments. This first step weeds out some firms that are either un-

280. The conspirator theory relies on game theoretical logic. For a discussion of game theory and how it can affect the way actors behave, see generally DOUGLAS G. BAIRD ET AL., *GAME THEORY AND THE LAW* (1994), for a discussion of game theory and how it can affect the way actors behave.

comfortable with what international law requires or are honest and do not want to deal with a client who appears to be willing to violate international law. But, once the firm responds, the rationalist treatment also leads to lower hard compliance rates by firms.

Under the conspirator effect, the logic here is that once the firm knows it has a savvy client who is willing to conspire in violating international law, the firm is now more willing to violate international law—even in the face of legal penalties. Thus, the conspirator effect is greater when the firm is certain that the consequences for violating international law are serious (i.e., penalties), and thus follows the signal that the client will have no problem violating the law.²⁸¹ This then explains why the mention of legal penalties leads to lower compliance with international law among the firms that respond to the query.

This conspirator effect gains support in the difference in results between OECD countries and non-OECD countries. OECD countries actively participate in an international forum on best economic practices and are generally wealthier countries with sophisticated markets. The OECD is comprised of a set of countries required to preserve international economic order through strict regulation.²⁸² Because OECD countries are

281. The theory here is that individuals are more willing to conspire where the penalties are more severe because they are sure that their co-conspirator is committed.

282. OECD countries are more likely to comply with international financial regulations because the economies of OECD countries are so integrated one with another that they need to coordinate internationally. See Allison Christians, *Networks, Norms, and National Tax Policy*, 9 WASH. U. GLOB. STUD. L. REV. 1, 2 (2010) (“Increasing economic integration inevitably draws states to coordinate their tax policies . . .”). Indeed, OECD countries are more likely to accept norms favoring international cooperation. See William Bradford, *International Legal Compliance: Surveying the Field*, 36 GEO. J. INT’L L. 495, 519 (2005) (“[T]ransnational legal process theory . . . postulates that repetitive interactions within transnational epistemic communities consisting largely of foreign policy elites give rise to norms favoring cooperation and that the internalization of these norms in domestic law and legal institutions fosters the progressive evolution of rule-governed cooperation.”). OECD countries “are in an iterative relationship in which they learn over time to deepen the natural and rational propensity” to comply with OECD related international rules. *Id.* at 529. It may also be that OECD countries are more likely to comply with international financial regulation because OECD countries have self-interests in complying with international financial regulations and their membership in the OECD is simply a reflection of those self-interests. See Jack L. Goldsmith & Eric A. Posner, *International Agreements: A Rational Choice Approach*, 44

arguably more invested in international financial stability and their international reputation for upholding financial regulations, their citizens are more likely to comply with such laws—particularly when they perceive them to be serious (i.e., connected with penalties for noncompliance).²⁸³ Presumably, among the country blocks, they are less likely to be baited by an open conspirator who is willing to violate international law. This is exactly the result we found. Our results indicate that citizens of OECD countries are more likely to comply with international law when informed of penalties for noncompliance than non-OECD countries.²⁸⁴ Indeed, the OECD countries have a reputation for accepting international norms and complying with international financial regulations. However, other countries—less wealthy and with an arguably less sophisticated regulatory regime—are more likely to fail to comply with international law when they are confronted with a willing conspirator, because they have less fear of hypocrisy upon getting caught or less fear of sanctions due to noncompliance.²⁸⁵

As this section makes clear, the conspirator theory of rationalism suggests that individuals are more likely to break international law when dealing with another open, willing violator of international law. We see the effects of this theory as a significant sub-set of firms are more likely to violate international law when they are informed of penalties for violating international law than when they are not informed about penalties. The conspirator effect has less of an influence with actors in more sophisticated markets, such as those in OECD countries.²⁸⁶ Where nations are a part of creating international norms, their private actors are less likely to conspire to break

VA. J. INT'L L. 113, 119 (2003) (discussing why states abide by treaty obligations).

283. See CHAYES & CHAYES, *supra* note 10, at 1–28.

284. The effect of the rationalist treatment is different when comparing OECD countries with non-OECD countries. In non-OECD countries, rationalism induces lower compliance rates ($p < 0.05$), which is the overall result for most countries. But in OECD countries, the rationalist treatment (or threat of legal penalties) results in a higher compliance rate ($p < 0.1$). See *supra* Part III, for further discussion of results.

285. There is a possibility that less wealthy countries are more likely to fail to comply with international law because they have a less sophisticated regulatory regime.

286. This may be an example of external outcasting in international law, such that members of the OECD enforce the law by exclusion of noncompliant members from community benefits and cooperation. See Oona Hathaway & Scott J. Shapiro, *Outcasting: Enforcement in Domestic and International Law*, 121 YALE L.J. 252, 308 (2011).

those norms. Thus, the conspirator effect is mitigated with prominent international players that set international norms.

5. Weak Penalty Effect

Another potential explanation of the contradictory rationalism compliance rate is that weak international penalties induce lower compliance than a lack of international penalties. Some individuals who are informed that penalties accompany noncompliance are deterred from responding to the client query compared to the placebo condition where no laws or penalties are mentioned. But those individuals who do not comply may not be violating rationalist logic. The rationalist treatment may receive a lower hard compliance rate than the other two treatments (though a lower response rate) because of the low perceived fear of actual penalties under international law.

The firms who decide to ignore the potential penalties may not fear actual penalties for two reasons. First, the firm who receives the query may disregard the potential penalties they are informed of because they have never heard of the FATF or the international penalties invoked and know based on experience in the field that such penalties are either light or not enforced in their country.²⁸⁷ Rather than indicating that this individual is contradicting her self-interest by failing to avoid penalties, this may simply be a statement on the lack of fear of any actual penalties that may result from violating international law. Of course, the firm here is not violating international law but this fear of sanctions indicates the level of a state's compliance.²⁸⁸ This theory has some support in the finding that middle- and lower-income countries responded at significantly lower rates compared to OECD countries, perhaps indicating that firms in wealthy countries were more likely to be aware that the FATF is soft law and garners no real sanctions.²⁸⁹

Second, the individuals may do some very quick research to see whether there are in fact legal penalties and how high they may actually be. They may soon realize that penalties that may apply in not requiring disclosure are in fact light or so far removed from her firm (and generally apply only to the national

287. Though, this individual may have been less likely to respond if informed that a domestic body may penalize them for noncompliance, than an unknown international body.

288. Indeed, the more a firm fears prosecution, the more likely it is that the state enforces international laws domestically.

289. See *supra* note 138 and accompanying text discussing this finding.

government) such that she is willing to take the risk of incorporating as normal, despite such standards.²⁹⁰ Thus, the lower compliance rate in the rationalism condition may be an indication that many individuals perceive international penalties for noncompliance to be weak or unlikely, which causes them to behave less appropriately than they would without this knowledge. So it appears that individuals may be less likely to comply with international law when there are weak international standards than when they are uninformed about international law. Indeed, the existence of weak penalties may create a disincentive to comply rather than a greater incentive to comply with international law.

6. Potential Confounding Effects

An issue that needs to be addressed is that potentially these treatments are marrying client type and international law type and creating a confounding effect. This argument is that potentially the three treatments are signaling that there is a particular type of customer: the uninformed customer, the disobedient customer, and the obedient customer.²⁹¹ Arguably, the responses by the firm are based on the signal received from the three customers rather than on the three international law responses: international standards, rationalism, and constructivism. Thus, what we are measuring is not the firm's proclivity to comply with international law but simply their response to the signal given from the different customers. In other words, some firms may be sophisticated enough to calibrate their responses based on the information they receive from prospective clients.

In response, we argue that, first, international law primarily governs the nation and then the firm, not the individual customer. This may even include sanctions on the firm for noncompliance. So, the firm may be watching for signals but ultimately must still consider how international laws bind them. Additionally, assuming that the treatments effectively combine client type with international law compliance, this may not

290. This could apply to the responses to all of the treatments.

291. The semi-informed customer (FATF treatment) states that the FATF requires disclosure but the individual is not sure what documents are required. The disobedient customer (rationalism) states that international law requires disclosure and penalties may follow, but despite those penalties he still does not want to disclose information. And the hesitatingly obedient customer (constructivism) states that international law requires disclosure and that he would really like to comply with the law, even though he does not want to disclose this information.

pose a problem for this analysis. We are testing the effects of client type on firms' willingness to follow international law. But international standards explicitly enjoin nations (and their private entities) from scrutinizing customers based on their profile (and relative risk), which is significant as the potential customers are all seeking to avoid complying with international law. And as far as the FATF is concerned, all the treatments express the same knowledge of international law and the same inquiry, so the knowledge level and request to learn about document requirements are consistent across treatments.²⁹² Thus, while we cannot separate subjects' judgments about client type from their decisions to comply with international law, we hold enough constant across the international standards, rationalist, and constructivist treatments to make a good case that the treatments are measuring the target causal effects, if any.

Another issue may be that the firm may say anything or agree with the potential client and then make them comply with international law after they have received a commitment for service. Thus, the firm may state up front that they would not require any documentation, because the client's letter indicates that he values privacy. Then, after receiving fees for incorporation, the firm may then state that due to domestic or international law it must have the following documents in order to incorporate. This bait-and-switch approach arguably could be used by firms, though our research indicates that this is unlikely.²⁹³ Judging from interviews and previous research in international transparency, we know that providers request a fee and documents at the same time, not sequentially. Thus, the bait-and-switch approach is unlikely to play a role here, and even if it does, the tendency should be balanced across experimental conditions by randomization.²⁹⁴

292. Indeed, the language expressing knowledge of the FATF requirements is identical across the treatments, and the inquiry after documents is also consistently employed across the thirty-three individual e-mails.

293. All of the letters ask for anonymous incorporation, so there should be relatively consistent incentives for the bait-and-switch across the treatments. Thus, even if a bait-and-switch approach is being used by incorporation services there is a balance induced by the randomization that the bait-and-switch services are evenly distributed across the conditions.

294. See Sharman, *supra* note 150, at 573. To the extent bait-and-switch plays a role, this would be when a website advertises "anonymous" companies and maybe bank accounts as well, then in the correspondence requires identification, though promises not to give it to others unless the customer is engaged in serious crime. We short circuit this by directly asking about identification rather than relying on the website. Also, while the treatments do

The implications of these results are that firms are not more likely to comply with international law if informed about the existence of the law, if aware of norms to follow such law, or if primed about possible sanctions for failing to comply. Indeed, as it turns out, many firms are actually less likely to comply with international law, particularly when they are made aware of penalties that may follow. Two different rationales indicate that lower compliance rates in the rationalist treatment may be due to the fact that firms who are fully aware of penalties under international law will still act contrary those laws when conspiring with a willing and open violator of international law or when they anticipate that international sanctions will be weak. Additionally, nations more closely involved in creating international law, with more sophisticated markets, are more likely to comply with international law when informed about penalties for noncompliance.

CONCLUSION

So, as a whole, does international law matter? The answer depends on whether we examine formal state compliance or informal compliance by private actors. As far as formal compliance with international regulations, most states require some financial transparency for incorporation, though most only partially enforce key international laws. A look at informal compliance exposes results that may be encouraging to some believers in the efficacy of international law: about two-thirds of the time, firms complied with international standards.²⁹⁵ This informal test also provides a more accurate test of financial transparency by actually addressing whether firms in such nations are willing to act contrary to international standards targeted at terrorist financing. This informal test resulted in a much less reassuring finding: roughly one in seven international firms require no identity documents at all, suggesting a

indicate a desire for confidentiality, they do not indicate that the potential client will not incorporate if asked to disclose documents. Arguably as well, it is typical for a client's initial request to innocently ask what information and documents they may have to gather in order to expedite the incorporation process. Moreover, in the prior Sharman study, the author took all of the steps toward incorporation—save transferring the money—in forty-two cases and in three additional cases he followed through and actually purchased shell companies. *Id.* In no case did Sharman encounter a bait-and-switch on required documents. *Id.*

295. These results may be encouraging to some supporters, given that both response rates and compliance rates were higher than predicted by international studies scholars. *See supra* notes 220, 241.

willingness to form anonymous shell corporations capable of major corruption or terrorism. Nearly half of those who responded—more than one fourth overall—were willing to act contrary to international law by failing to require that identity documents be notarized or otherwise certified. By choosing to serve clients with unverified identities rather than refusing service, these firms enable easier formation of anonymous shell companies.²⁹⁶

Beyond the overall picture of international compliance, an analysis of our field experiment provides several significant findings. It appears that reference to legal penalties significantly lowers response rates. However, while referencing penalties reduced response rates (as might be expected), it also decreased compliance with international transparency standards. Thus, mentioning penalties that would apply for not following international law actually made some firms *less*, not more, likely to follow the law.²⁹⁷ This finding is at odds with the idea that threats of sanctions increase compliance, which is at the core of the rationalist theory that actors are guided by fear of penalties and maximizing self-interest. Though with a conspirator effect of rationalism and a theory based on perceived weakness of international law, we provide potential explanations of why information about sanctions results in lower compliance. Actors may be more likely to violate international law rather than directly decline service when they know that their client is a conspirator, and thus open to ignoring international law, and also when they perceive international penalties to be weak rather than when they learn nothing about penalties. Understanding these motivations can help increase compliance with international law in the context of financial transparency and in other areas. These findings may also aid governments in stopping the formation of anonymous shell companies that have caused billions in damage worldwide, and aid in combating a range of financial crimes, including the bankrolling of terrorism.²⁹⁸

296. Our data mark by far the most robust picture available of global compliance with rules on financial transparency. Compare FATF, *supra* note 135, with World Bank, *supra* note 124. The fact that we discern a significant level of non-compliance helps to address the objection that studies of international standards create a false impression of a rule-governed world. This is thanks to the confirmation bias produced by endogeneity and selection effects. See *supra* Part I.C.2.

297. This result also took the response rate into account. See *supra* Part III.C.4.

298. See *supra* notes 123–30.

Second, compliance with international law is unrelated to national capacity or wealth. Surprisingly, as a general rule, the level of compliance in low and middle-income countries is not significantly lower than that in wealthy countries. This runs counter to the managerialist presumption and conventional wisdom that compliance is at least in part a matter of having the expertise and wherewithal to implement international standards. The positive implication of this finding is that if low-income countries can secure a high level of compliance, most other countries should be able to do likewise without major expense. The negative implication is that many countries with a low level of compliance have simply chosen not to follow the rules.

Third, and of greatest significance to international law scholars, compliance with international rules is no higher when nations are prompted about the existence and contents of these rules or international norms to comply with such rules. This is a major blow to both the constructivist and managerial schools. The managerialist school argues that ignorance, rather than opportunism, may underpin much non-compliance, as actors are simply unaware of what they should be doing. At least in the case of international financial transparency law, however, more information about the standards has no effect on compliance rates. And prompts about international norms to comply with international law had no significant effect on response or compliance rates.

Finally, we articulate a rationale and demonstrate with evidence that states are not the most important actors in all important realms when it comes to determining whether international law is effective. We show that international compliance is not a straightforward product of formal domestic or international regulations and enforcement, but a consideration of informal compliance by private firms and individuals. If compliance were purely driven by whether or not domestic law mandated collecting identity documents for those forming shell companies, we would expect near-perfect compliance from jurisdictions with such a law, and near-zero compliance from those without. However, we see substantial variation as firms in various nations comply or choose not to comply with international standards that their nations agreed to.²⁹⁹ And overall, *formal* compliance with international law by any of the

299. With the exception of a few tax havens, of course. *See supra* Table 2.

measures does not usually match *actual* compliance.³⁰⁰ These differences indicate that compliance with international law cannot be measured solely by examining a nation's regulatory framework, but must consider how individuals and firms—at the locus of compliance—in fact behave. Thus, against the prominent frameworks of international law, we conclude that states may not be the only primary players in determining whether international law is effective. Indeed, the private actors within them may significantly determine if—and why—international law matters.

300. This assertion is debatable in the aggregate and depends on what we measure.

APPENDICES

APPENDIX A: EXAMPLE LETTERS FOR INTERNATIONAL SAMPLE³⁰¹**Control**

Dear **[name/company]**

I am contacting you as I would like to form an international corporation for my consulting firm. I am a resident of **[Norstralia]** and have been doing some international consulting for variuos companies. We are now growing to a size that makes incorporation seem like a wise option. A lot of our newer business is in your region.

My two associates and I are accustomed to paying **[Norstralia]** income tax, but the rising tax rates make incorporation in another country a more economic alternative. Also, our contracts grow larger and more complicated, so reducing personal liability through incorporation seems more attractive.

As I am sure you understand, business confidentiality is very important to me and my associates. We desire to incorporate as confidentially as we can. Please inform us what documentation and paperwork is required and how much these services will cost?

I would like to start the process of incorporation as soon as possible. Also, how much can we expect your fees to be?

Due to numerous professional commitments, I would prefer to communicate through email. I hope to hear from you soon.

Thank you very much,

[alias]

301. All typos and misspellings in the treatments are intended to make the treatments appear more authentic. These letters simply provide sample language from the many treatment letters that were drafted and distributed.

Treatments**1. International Standard**

Dear **[name/company]**

I am contacting you regarding a business I am trying to set up. I am a consultant and my colleagues and I are seeking to establish an international corporation. I am a **[Norstralia]** resident, but I do business both locally and with some international client, including some in your region. Our business has been growing substantially, and our goal is to limit tax obligations and business liability.

We would like as much business confidentiality as possible in these early stages of formation. **My internet searches show that the international Financial Action Task Force requires disclosure of identifying information. But I would rather not provide any detailed personal information if possible.**

So, we would like to know what identifying documents will be required to establish this company. We would also like to know what start-up costs will be.

Due to my travel schedule, email will be the best way to reach me. I look forward to hearing from you soon.

Regards,

[alias]

2. Rationalism

Dear [name/company]

I am seeking information on how to incorporate an international company. I hope that you might be able to offer what I need.

I am a consultant, and my business associates and I live in [Norstralia]. Much of our business originates here, where we operate, but our company also grows quickly among international clients. Many of them are in your area. So, we feel that incorporation is a necessary option for us. We hope to limit taxes obligations and business liability.

We would like to know if you feel that you will be able to service us with a corporation. What identifying documents will you request for this transaction? We would prefer to limit disclosure as much as possible.

My internet searches show that the international Financial Action Task Force sets standards for disclosure of identifying information when forming a company. I also understand that legal penalties may follow violation of these standards. But I would like to avoid providing any detailed personal information if possible. If you could answer these questions and also let us know about your prices, we very much appreciate it.

Thank you for the time to address our query. Business obligations make communication difficult, so we would prefer to correspond with email.

Until we speak again,

[alias]

3. Constructivism

Dear [name/company]

I am a resident of [Norstralia] and would like to inquire about your process to form international corporations. With several associates, I operate consulting firm in [Norstralia]. We deal with a growing number of international clients, many that come from your area, and would like to pursue incorporation options for liability and taxes purposes.

We are particularly concerned with keeping business interactions private; thus, we are eager to limit information disclosure as much as possible. **My internet searches show that the international Financial Action Task Force sets standards for disclosure of identifying information when forming a company and most countries have signed on to these standards. As reputable businessmen, I am sure we both want to do the right thing by the international rules. But I would like to avoid providing any detailed personal information if possible.**

Can you please inform me what your start-up costs are and what kind of identification or documents we will need to provide? We are all fairly burdened with commitments, so email communication is preferable.

Thank you in advance,

[alias]

APPENDIX B: INTERNATIONAL FORMAL COMPLIANCE WITH FATF
FORTY-NINE RECOMMENDATIONS

GLOBAL RESULTS (AS PERCENTAGES)					
FATF Forty Recommendations	Non-Compliant (NC)	Partially Compliant (PC)	Large-ly Compliant (LC)	Compliant (C)	Not Applicable (NA)
1. ML offence	5.82%	50.48%	38.83%	4.85%	
2. ML offence—mental element and corporate liability	1.94%	28.15%	50.48%	19.41%	
3. Confiscation and provisional measures	4.85%	38.83%	43.68%	12.68%	
4. Secrecy laws consistent with the Recommendations		15.53%	31.06%	53.39%	
5. Customer due diligence	36.89%	51.45%	9.70%	1.94%	
6. Politically exposed persons	64.07%	19.41%	13.59%	0.97%	
7. Correspondent banking	54.36%	19.41%	17.47%	8.73%	
8. New technologies & non face-to-face business	34.65%	34.65%	18.81%	11.88%	
9. Third parties and introducers	21.78%	27.72%	10.89%	10.89%	28.71%
10. Record keeping	8.73%	32.03%	36.89%	22.33%	
11. Unusual transactions	21.35%	47.57%	25.24%	5.82%	
12. DNFBP—R.5, 6, 8-11	64.07%	32.03%	1.94%	1.94%	
13. Suspicious transaction reporting	20.79%	51.48%	24.75%	2.97%	
14. Protection & no tipping-off	5.82%	27.18%	25.24%	41.74%	
15. Internal controls, compliance & audit	12.68%	55.33%	30.09%	1.94%	
16. DNFBP—R.13-15 & 21	58.25%	35.92%	3.88%	1.94%	
17. Sanctions	15.53%	54.36%	26.21%	3.88%	
18. Shell banks	10.67%	45.63%	21.35%	22.33%	
19. Other forms of reporting	14.56%	7.76%	9.70%	67.96%	
20. Other NFBP & secure transaction techniques	15.53%	21.35%	24.27%	38.83%	
21. Special attention for higher risk countries	42.71%	36.89%	13.59%	6.79%	
22. Foreign branches & subsidiaries	39.60%	24.75%	20.79%	5.94%	8.91%
23. Regulation, supervision and monitoring	16.83%	56.43%	25.74%	0.99%	
24. DNFBP - regulation, supervision and monitoring	58.41%	35.64%	5.94%		
25. Guidelines & Feedback	32.67%	41.58%	21.78%	3.96%	
26. The FIU	15.53%	29.12%	42.71%	12.68%	
27. Law enforcement authorities	4.95%	30.69%	37.62%	26.73%	
28. Powers of competent authorities	0.97%	8.73%	18.44%	71.84%	
29. Supervisors	5.82%	40.77%	40.77%	12.68%	
30. Resources, integrity and training	16.83%	49.50%	30.69%	29.70%	
31. National co-operation	6.93%	34.65%	42.57%	15.84%	
32. Statistics	26.21%	39.80%	32.03%	1.94%	

33. Legal persons–beneficial owners	20.38%	54.36%	17.47%	7.76%	
34. Legal arrangements–beneficial owners	12.68%	29.12%	9.70%	8.73%	39.80%
35. Conventions	6.86%	48.03%	37.25%	7.84%	
36. Mutual legal assistance (MLA)	2.97%	23.76%	53.46%	19.80%	
37. Dual criminality	1.94%	18.44%	34.95%	44.66%	
38. MLA on confiscation and freezing	6.79%	34.95%	42.71%	15.53%	
39. Extradition	7.92%	11.88%	48.51%	31.68%	
40. Other forms of cooperation	4.85%	33.98%	38.83%	28.15%	
Nine Special Recommendations					
SR.I Implement UN instruments	24.27%	51.45%	20.38%	3.88%	
SR.II Criminalize terrorist financing	24.27%	39.80%	29.12%	6.79%	
SR.III Freeze and confiscate terrorist assets	36.89%	45.63%	15.53%	1.94%	
SR.IV Suspicious transaction reporting	37.86%	30.09%	24.27%	7.76%	
SR.V International cooperation	19.41%	27.18%	43.68%	9.70%	
SR VI AML requirements for money/value transfer services	34.31%	33.33%	22.54%	8.82%	0.98%
SR VII Wire transfer rules	51.45%	28.15%	16.50%	3.88%	
SR.VIII Non-profit organizations	36.63%	41.58%	15.84%	5.94%	
SR. IX Cross border declaration & disclosure	37.62%	39.80%	14.85%	4.95%	1.98%

*** Margin for Error: 0.02% (totals for each recommendation are never lower than 99.98% or higher than 100%.)**

Data compiled from either 101, 102 or 103 Mutual Evaluation Reports, depending on the recommendation (March 2009).

Compliant: The Recommendation is fully observed with respect to all essential criteria.

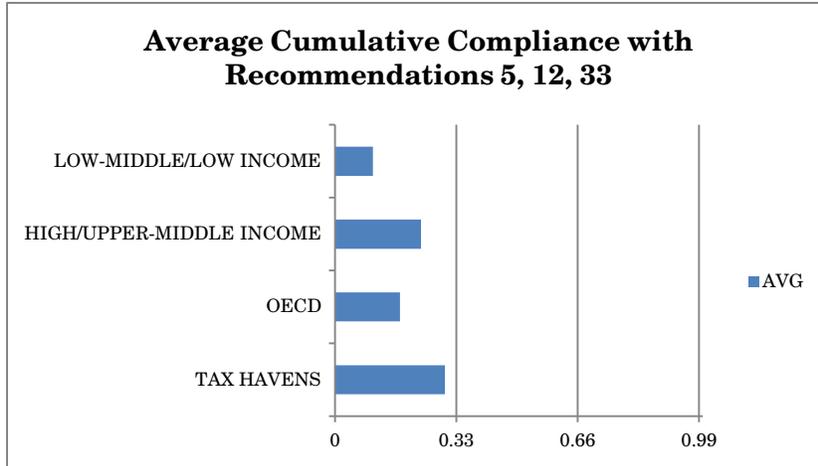
Largely compliant: There are only minor shortcomings, with a large majority of the essential criteria being fully met.

Partially compliant: The country has taken some substantive action and complies with some of the essential criteria.

Non-compliant: There are major shortcomings, with a large majority of the essential criteria not being met.

Not applicable: A requirement or part of a requirement does not apply, due to the structural, legal or institutional features of a country (e.g., a particular type of financial institution does not exist in that country).

APPENDIX C: FORMAL COMPLIANCE WITH INTERNATIONAL
FINANCIAL TRANSPARENCY LAW



This chart illustrates the average cumulative compliance by country group with Recommendations 10, 22, and 24. Compliance with each individual recommendation is valued as follows: NC = 0, PC = 0.0825, LC = 0.0165, C = 0.33. Compliance by country with each recommendation is shown in the table below.

	Rec 10	Rec 22	Rec 24
Argentina*	NC	NC	NC
Australia*	NC	NC	LC
Austria*	PC	PC	PC
Bahamas	PC	PC	LC
Belize	NC	PC	NC
Bermuda	NC	NC	C
Brazil*	PC	NC	PC

British Virgin Islands ³⁰²	LC	PC	PC
Bulgaria	PC	PC	LC
Canada*	NC	NC	NC
Cayman Islands	LC	PC	C
Chile	PC	NC	PC
China*	PC	NC	NC
Colombia	PC	PC	C
Cyprus	PC	PC	LC
Czech Republic	PC	PC	PC
Denmark*	LC	LC	PC
Ghana	NC	NC	PC
Hong Kong*	PC	NC	PC
India*	PC	NC	PC
Indonesia	PC	NC	NC
Isle of Man	PC	PC	LC
Israel	PC	NC	PC
Jordan	PC	NC	PC

302. The follow-up evaluations for the British Virgin Islands, the Cayman Islands, Denmark, Spain, and the United Kingdom, identified that compliance with Recommendation 10 had improved and accordingly they are categorized here as LC; additionally, the follow-up evaluation in Denmark also identified that compliance with Recommendation 22 had improved to the level of LC. CARIBBEAN FINANCIAL ACTION TASK FORCE, SECOND FOLLOW-UP REPORT: VIRGIN ISLANDS 10 (June 1, 2010), *available at* http://www.cfatf-gafic.org/downloadables/Follow-Up_reports/Virgin_Islands_2nd_Follow-Up_Report_%28Final%29_English.pdf; CARIBBEAN FINANCIAL ACTION TASK FORCE, THIRD FOLLOW-UP REPORT: CAYMAN ISLANDS 7 (Oct. 28, 2010), *available at* http://www.cfatf-gafic.org/downloadables/Follow-up_reports/Cayman_Islands_3rd_Follow-p_Report_%28Final%29_English.pdf; FATF, MUTUAL EVALUATION THIRD FOLLOW-UP REPORT, ANTI-MONEY LAUNDERING AND COMBATTING THE FINANCING OF TERRORISM: KINGDOM OF DENMARK 12, 26 (Oct. 22, 2010), *available at* <http://www.fatf-gafi.org/dataoecd/58/32/46253145.pdf>; FATF, MUTUAL EVALUATION FOURTH FOLLOW-UP REPORT, ANTI-MONEY LAUNDERING AND COMBATTING THE FINANCING OF TERRORISM: SPAIN 14 (Oct. 22, 2010), *available at* <http://www.fatf-gafi.org/dataoecd/59/15/46253063.pdf> [hereinafter FATF, SPAIN]; FATF, MUTUAL EVALUATION FOURTH FOLLOW-UP REPORT, ANTI-MONEY LAUNDERING AND COMBATTING THE FINANCING OF TERRORISM: UNITED KINGDOM 11 (Oct. 16, 2009), *available at* <http://www.fatf-gafi.org/dataoecd/59/15/46253063.pdf>; FATF, MUTUAL EVALUATION THIRD FOLLOW-UP REPORT: ANTI-MONEY LAUNDERING AND COMBATTING THE FINANCING OF TERRORISM: KINGDOM OF DENMARK 12, 26 (2010), *available at* <http://www.fatf-gafi.org/dataoecd/58/32/46253145.pdf>.

Kenya ³⁰³	NC	NC	NC
Liechtenstein	PC	PC	PC
Malaysia	LC	PC	PC
Malta	LC	LC	C
Mexico*	PC	NC	NC
Panama	LC	PC	NC
Peru	LC	PC	C
Poland	NC	NC	PC
Romania	PC	NC	LC
Serbia	PC	NC	PC
Seychelles	NC	NC	NC
Singapore* ³⁰⁴	LC	PC	PC
Spain*	LC	LC	PC
St. Kitts and Nevis	NC	PC	LC
Switzerland*	PC	PC	NC
Thailand	NC	NC	PC
Turkey*	NC	NC	PC
UK*	PC	PC	PC
Ukraine	PC	NC	PC
United Arab Emirates	NC	NC	PC
Uruguay	NC	NC	NC
USA Incorp. Services	NC	NC	NC

303. There is no FATF Mutual Evaluation Report available for Kenya on the FATF website; however, in an FATF Public Statement dated June 24, 2011, the FATF has previously discussed Kenya's noncompliance generally and in relation to some specific recommendations. *See* Public Statement, Financial Action Task Force, High-Risk and Non-Cooperative Jurisdictions (June 24, 2011), *available at* <http://www.fatf-gafi.org/topics/high-riskandnon-cooperativejurisdictions/documents/fatfpublicstatement-24june2011.html>.

304. The follow-up evaluations for Singapore and Spain identified improved compliance. In Singapore, compliance with Recommendations 22 and 24 improved but not to the level of LC, and has been categorized here as PC. FATF, MUTUAL EVALUATION SECOND FOLLOW-UP REPORT, ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM: SINGAPORE 5 (Feb. 25, 2011), *available at* <http://www.fatf-gafi.org/dataoecd/3/61/47221430.pdf>. In Spain, compliance with Recommendation 22 improved to a sufficient level of compliance that has been categorized here as LC. Compliance with Recommendation 24 improved but not to the level of LC, and has been categorized here as PC. FATF, SPAIN, *supra* note 302, at 5.

USA Law Firms	NC	NC	NC
USA Overall*	PC	NC	NC
Vietnam	NC	NC	PC

* Indicates country is an FATF member.

APPENDIX D: INTERNATIONAL FORMAL INCORPORATION IDENTITY REQUIREMENTS³⁰⁵

Country	Identity Required	Type	Notarized Identity	Type
Argentina	X	Identification of all shareholders. Commercial Companies Law, "Sociedades Comerciales," Law 19,550, Mar. 30, 1984, B.O. of Apr. 3, 1972, t.o. 1984 [D. 841 of Mar. 20, 1984] (Arg.) as am'd by Law 23,576 of, July 19, 1988 as am'd.	X	Notarized signatures of founding partners. http://doingbusiness.org/data/exploretopics/starting-a-business .
Australia	X	List of directors and subscribers. Corporations Act § 117.		
Austria		1980 Law on Limited Liability Companies and the Stock Company or Corporation; Aktiengesetz [AktG] [Stock Corporation Act] BUNDESEGESETZBLATT [BGBl] No. 94/1965 (Austria). 1965 Austrian Corporation Law.		
Bahamas		Companies Act, 1992, §§ 3, 6, 48, 118 (Bah.); Business Licenses Act, 1980 (Bah); International Business Companies Act, 2000 §§ 181, 184, 185 (Bah.).		
Belize		Regulations of June 2001; Companies Act, (2003) Cap. 250 §§ 5, 38, 251 (Belize).		
Bermuda	X	The names, addresses and nationalities of the persons who subscribe their names to the memorandum. Companies Act (CA) (Act No. 59/1981) §§ 6, 53, 62(1-2), 91(1-2), 98, 133 (Berm.); Companies Amendment Act (Act No. 38/2009) (Berm.).		
Brazil	X	List of shareholders names. Lei 6404 de 15 de Dezembro de 1976, as am'd; C.C. arts. 1088, 1089.		
British Virgin Island		Business Companies Act (BCA) 2004, §§ 5, 9; BCA Amendment 2005 §§ 2, 55, 67-77, 132; International BCA 2000, §§ 185, 186.		

305. [Editor's Note: This table was compiled and verified by the authors.]

Bulgaria	X	Notary certification of manager(s)' signature. Arts. 158-252 LC.	X	Notarized manager's signatures. Arts. 158-252 LC.
Canada	X	Registered names of managers/directors. Business Corporations Act §§ 5, 14, 100, 118, 119, 136.		
Cayman Islands	X	Each subscriber of the memorandum of association shall write opposite to his name the number of shares he takes. Companies Law (CL) (2009 Revision) §§ 26, 163, 179, 229(1), 230.		
Chile	X	The names of shareholders in notarized deed. Doing Business in Chile, Laws 18045, 18046 of Oct. 21, 1981, both as amended.	X	Names of shareholders notarized. http://www.pkf.com/media/131770/doing%20business%20in%20chile.pdf .
China	X	Photocopy of the identity card of the individual shareholders. 1988 Registration Regulations, Art. 4; <i>Starting a Business in China</i> , DOING BUS., http://doingbusiness.org/data/exploreconomies/china/starting-a-business (last visited Nov. 29, 2012); 1988 Registration Regulations Art.	X	Identity card. http://doingbusiness.org/data/exploreconomies/china/starting-a-business .
Colombia	X	Name, nationality and domicile of shareholders. C. Com. 98-121, 373-376.		
Cyprus	X	Registered names of managers/directors and officers. Companies Law, Cch. 113, §§ 14, 75, 81, 102, 192, 197, 347.		
Czech Republic	X	Registered names of legal owners, officers, and managers/directors. Obchodní zákoník [Commercial Code] č. 513/1991 Sb. §§ 24, 28, 62, 156, 175, 184(5), 194(5,7), 217(a).		
Denmark	X	Government obtained digital signature required to register business. Act on Central Business Undertaking Register, Consolidated Act No. 653 of June 15, 2006; <i>Starting a Business in Denmark</i> , DOING BUS., http://doingbusiness.org/data/exploreconomies/denmark/starting-a-business (last visited Nov. 29, 2012).		

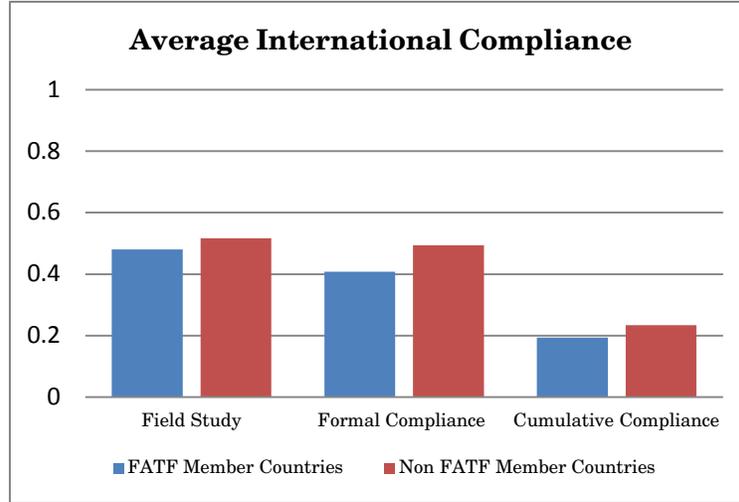
Ghana	X	Subscriber, shareholder and directors names and information. Ghana Companies Code 1963 (Act 179); <i>Starting a Business in Ghana</i> , DOING BUS., http://doingbusiness.org/data/exploreconomies/ghana/starting-a-business (last visited Nov. 29, 2012).		
Hong Kong	X	Managers/directors, legal owners, officers. Hong Kong Companies Ordinance, Cap. 32 §§ 14, 73, 143(B), 154, 333.		
India	X	Register names of directors and secretary. Companies Act 1956, No. 1 of 1956, INDIA CODE (1993), <i>available at</i> http://indiacode.nic.in .	X	Government obtained DIN number required which requires proof of identity. http://doingbusiness.org/data/exploretopics/starting-a-business .
Indonesia	X	Full name and information of managers, directors, commissioners, members and partners of business. Law No. 3 of 1982; Commercial Registration, MARTINDALE-HUBBLE INDONESIA LAW DIGEST, at 7 (2008).	X	Identity card of President required for trade license. http://doingbusiness.org/data/exploretopics/starting-a-business .
Isle of Man	X	Each subscriber must write opposite to his name the number of shares he takes. Companies Act 1931 §§ 5, 12, 64, 312.		
Israel	X	List of directors. Business Names, MARTINDALE HUBBLE ISRAEL LAW DIGEST, § 2.03 (2010); Companies Law 2005.	X	Authenticated directors signatures. http://doingbusiness.org/data/exploretopics/starting-a-business .
Jordan	X	Each subscriber must write opposite to his name the number of shares he takes. Companies Law No. I of 1989.		
Kenya	X	Particulars of Directors and Secretary. The Companies Act, (2009) Cap. 486 § 17 (Kenya); World Bank Group, <i>Starting a Business in Kenya</i> , DOING BUS., http://www.doingbusiness.org/data/exploreconomies/kenya/starting-a-business/ (last visited Nov. 29, 2012).		
Liechtenstein	X	Registered name of managers/directors. Personen- und Gesellschaftsrecht [PGR] [Persons and Company Law], arts.180,		

		279, 291, 263 (Liech).		
Malaysia	X	Particulars of at least two shareholders and two Malaysian directors. Companies Act 1965, (1973) Act 125 (Malay.); Registration of Businesses Act 1956, (1978) Act 197 (Malay.); World Bank Group, <i>Starting a Business in Malaysia</i> , DOING BUS., http://doingbusiness.org/data/exploreconomies/malaysia/starting-a-business (last visited Nov. 29, 2012).		
Malta	X	Name and information of subscribers and directors Companies Act (Act XXV of 1995), (1996) Cap. 386 (Malta); MARTINDALE-HUBBELL MALTA LAW DIGEST 2.03 (eBook 2011).		
Mexico	X	Names, nationality and residences of incorporators. Ley General de Sociedades Mercantiles [LGSM] [General Law for Commercial Corporations], <i>as amended</i> , Diario Oficial de la Federación [DO], 28 July 1934 (Mex.); MARTINDALE-HUBBELL MEXICO LAW DIGEST 2.03 (eBook 2011).		
Panama	X	Registered names of managers/directors. Corporation Law, No. 32 (1927) (Pan.).		
Peru	X	Name, occupation and domicile of incorporators. Martidale-Hubble Peru Law Digest, 2.03; General Law of Societies, Law 26887 of Dec. 5, 1997 as am'd.		
Poland		The application for registration of the company shall be signed by all members of the management board. The Code of Commercial Partnerships and Companies (2000) arts. 164, 166.		
Romania		Law 31/1990.		
Serbia	X	Authenticated signatures of founder(s). http://doingbusiness.org/data/exploretopics/starting-a-business ; Law on Business Companies 2003.	X	Authenticated signatures. http://doingbusiness.org/data/exploretopics/starting-a-business .
Seychelles		Companies Ordinance (1972) §§ 3, 10.		

		21, 100, 164, 310.		
Singapore	X	Registered names of managers/directors and officers. Companies Act, (2006) Ch. 50, §§ 19, 66, 126, 145, 171, 172, 367; Business Registration Act, (2004) Ch. 32, § 6.		
Spain	X	The public deed of incorporation must have the identity of the shareholders, including a fiscal identification number for each. <i>Starting a Business in Spain</i> , WORLD BANK (June 2011), http://www.doingbusiness.org/data/exploreeconomies/spain/registering-property/ ; R.C.L 1784, 1996.	X	Fiscal Identification number. http://doingbusiness.org/data/exploretopics/starting-a-business .
St. Kitts and Nevis	X	Registered names of managers/directors and officers. Companies Act 1996 (No. 22 of 1996, Registered office 1996), §§ 4, 8, 51, 72, 73, 195.		
Switzerland		Code of Obligations, CODICE DELLE OBLIGAZIONI [CO], CODE OF OBLIGATIONS [CO], Oct. 17 2007 Ordinanza sul registro di commercio del 17 ottobre 2007 (Stato 1° gennaio) art. 66-68.		
Thailand	X	Name of owner. Martindale-Hubbe Thailand Law Digest § 2.03; Commercial Registration Act (No. 2), B.E. 2549 (2006).		
Turkey	X	Notarized identity cards of company managers <i>Starting a Business in Turkey</i> , WORLD BANK (June 2011), http://doingbusiness.org/data/exploreeconomies/turkey/starting-a-business/ ; Com. C. 35.	X	Notarized identity cards. http://doingbusiness.org/data/exploretopics/starting-a-business .
Ukraine		Law of Ukraine "On business companies." Law No. 1576-XII dd. Sept. 19, 1991) enacted under Decree of the Supreme Rada of Ukraine (Decree No. 1577-XII as of Sep. 19, 1991) Companies Law, Sept. 19, 1991.		
United Arab Emirates	X	Registered names of managers/directors. Companies Law 2009, DIFC LawNo. 2 of 2009, Art. 11, 38, 51,115.	X	Passport copy of partners. http://doingbusiness.org/data/exploretopics/starting-a

				business.
United Kingdom	X	Statement of company's proposed officers. (Martindale-Hubble England Law Digest, 2.03; Companies Act 2006); James E. Goold, <i>Companies Act 2006</i> , MARTINDALE-HUBBLE (Oct. 2009), http://www.martindale.com/business-law/article_Jones-Day_808798.htm .		
United States		DELAWARE CODE ANN., Title 8, Ch.1, §§ 101, 132, 141(a), 145, 158, 371 (West 2012).		
Uruguay	X	Registered names of managers/directors and officers. Ley N° 16.060 Sociedades Comerciales, art. 13; Ley N° 17.904, art. 13, 16.		
Vietnam	X	Must maintain register of members or register of shareholders. Law on Enterprises, Art. 9, 1992.	X	Copy of people's identity card, passport. Law on Enterprises, Art. 16, 1992.

APPENDIX E: AVERAGE INTERNATIONAL COMPLIANCE: FORMAL (NATIONAL REGULATIONS) AND INFORMAL (FIELD EXPERIMENT)³⁰⁶



FATF Member Country and Non-Member Country Compliance: Two-Sample Difference in Means T-Test Results³⁰⁷

	FIELD STUDY	FORMAL COMPLIANCE	CUMULATIVE COMPLIANCE
Difference in FATF/Non-FATF Means:	0.053	0.083	0.04
T-Statistic:	0.7571	1.145	1.072
Degrees of Freedom:	45	44	63
P-Value:	0.4538	0.26	0.286

306. Cumulative compliance is the sum of countries' compliance with recommendations 10, 22, and 24. The difference in average compliance between FATF member countries and Non-FATF member countries in the field study, formal data, and cumulative compliance data was 0.053, 0.085, 0.04 respectively. Difference in means tests show that these differences are not statistically significant. For the field study, a two-tailed t-test yielded a p-value of 0.45; for the formal compliance data, the p-value was 0.26; for the cumulative compliance data, the p-value was 0.2857.

307. Cumulative compliance is the sum of countries' compliance with recommendations 10, 22, and 24. For purposes of the difference in means tests, the null hypothesis is that the difference in average compliance between FATF and Non-FATF countries is zero. Thus, p-values reflect the degree of confidence with which we can reject that hypothesis. For example, a p-value of 0.4538 means we are about 54% confident that the difference in means is not

APPENDIX F: SELECTION MODEL OF RESPONSE AND COMPLIANCE³⁰⁸

Treatments	Re- sponse	Compliance	Resp. Constant	Comp. Con- stant	N
Int'l Standards	-0.070 (0.113)	-0.062 (0.119)	0.179** (0.077)	-0.507*** (0.080)	500
Rationalism	-0.248** (0.179)	-0.332*** (0.120)	0.179** (0.077)	-0.507*** (0.080)	522
Constructivism	-0.068 (0.109)	-0.134 (0.116)	0.179** (0.077)	-0.507*** (0.080)	529

zero.

308. Standard errors in parentheses: *** p<0.01, ** p<0.05, * p<0.1.