The choice between source-based and residence-based taxation has defined the terms of the debate for the international tax regime since its inception in the early 1900s. As an economic matter, residence taxation has generally been considered superior to source taxation, but recently source taxation has begun to receive increasing support from both policy-makers and academics alike, especially as the concept of residence has come under attack as losing any significance in the modern, globalized world. Regardless of one’s preference in this debate, the terms of the debate seem to be set – source versus residence, two opposing poles for all purposes.

The thesis of this Article is that the construct of source and residence as two competing and irreconcilable doctrines is largely incorrect as a legal matter. Rather, both source rules and residence rules should be used as instrumental tools to be used to divide taxing authority in a globalized world with mobile capital. Under this approach, there is no reason why “source” rules as a doctrinal matter need to be used only for “source” taxation as an economic matter, or that “residence” rules as a doctrinal matter need be used for “residence” taxation as an economic matter. Instead, the source rules as a doctrinal matter can actually be used to solve the problems of the residence rules as a doctrinal matter. If it is true that residence as a conceptual matter is becoming increasingly meaningless in the globalized world, tying the doctrinal rules of residence to the doctrinal rules for source can better effectuate the ultimate goals of the international tax regime. This Article will do so, introducing a proposal to define the residence of entities as domestic for purposes of US tax law based on the source of the income of such entities. In its most simplistic form – an entity would be a US Person if it earns too much US Source income. Of course, such an approach would prove more complex than such a simple statement, but the basic premise holds. The Article then demonstrates how such an approach could be used to resolve two of the most difficult and pressing issues confronting the modern US international tax regime: corporate inversions and offshore hedge funds.