BEPS Action 14 - Arbitration of tax disputes: a Nigerian perspective

But is it really the case that tax matters are not arbitrable? Yes, in the case of domestic tax disputes but no, in the case of international tax disputes.

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In 2015, the Organisation for Economic Cooperation and Development (OECD) issued 15 Action Plans under the Base Erosion and Profit Shifting (BEPS) initiative to update obsolete international tax rules with the aim of curbing harmful tax practices. Each Action Plan contains specific recommendations to be adopted, whether in part, with slight modifications or in their entirety, by countries to amend their tax rules.

While Action Plan 14 recommends that countries update their existing Double Tax Treaties (DTTs) to include mandatory binding arbitration to complement the Mutual Agreement Procedure (MAP) (the existing dispute resolution framework under DTTs), Action Plan 15 requires countries to adopt a multilateral treaty incorporating all 15 Action Plans in one fell swoop to update all their existing DTTs.

On 17 August 2017, in line with Action 15, Nigeria became a signatory to the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* ("Multilateral Treaty" or "MLI"). Signatories to the MLI indicate what Action Plans they will adopt, that is, they state their MLI positions. When signing the MLI, Nigeria indicated that it will not adopt Action 14, that is, it will not introduce mandatory binding arbitration to resolve tax disputes. Its reason for this position is that tax matters are not arbitrable so Nigeria will not subject *its taxes* to arbitration.

Interestingly, on 10 October 2017, the European Council approved a directive for resolving double tax disputes within the European Union. The directive, similar to the Action 14, includes an arbitration procedure for member States to resolve tax disputes where MAP fails. One major difference between the EU directive and the OECD recommendations is that arbitral awards under the former are made public, at least in redacted forms. These public records may form precedents ultimately resulting in more certainty and confidence in the tax system globally. According to Toomas Toniste (Minister for Finance of Estonia which currently holds the EU presidency), *"[T]his new system is a big improvement. It will encourage investment by encouraging a more* *favourable tax environment and reducing costs for businesses'.*

Personally, I share Mr. Toniste's view. **Adopting mandatory binding arbitration to deal with double taxation disputes represents best practice in an era of increasing complexities in global trade and sophisticated business models such as digital economy.** Indeed the hallmarks of an effective tax system includes certainty of tax laws. I imagine multinational enterprises keen to carry on business in Nigeria would be concerned about the robustness (or lack) of its international tax dispute resolution mechanisms. For example where MAP fails to resolve a double tax dispute between Nigeria and a treaty country, what avenues would be available to a multinational to resolve such dispute? This is even worse where the treaty country has embraced mandatory binding arbitration and Nigeria has not. This mismatch creates an atmosphere of uncertainty which is counterproductive to the entire BEPS initiative.

What are Nigeria's DTT partners doing?

Nigeria has entered into DTTs with 19 countries. Only 12 have been ratified. Of this number 5 (Belgium, Canada, France, the Netherlands and the UK) have adopted mandatory binding arbitration, 5 (China, Czech, Pakistan, Romania and South Africa) are silent on whether they would adopt arbitration, 1 (Slovakia) has expressly rejected arbitration and Philippines is yet to submit its position (as at February 2018.) However, Czech, Romania and Slovakia are EU States and have already adopted mandatory arbitration for tax disputes within the EU. Therefore, this could be an indication that arbitration would be extended to their DTTs sooner than later. With respect to DTTs yet to be ratified, both Spain (which, according to the National Bureau of Statistics (NBS), is one of Nigeria's top 3 importers) and Sweden have indicated their intention to adopt arbitration.

According to NBS, UK, Belgium and Netherlands are amongst the top ten sources of capital imported into Nigeria. Similarly, some of the adopting countries are prominent trading partners with Nigeria. Because Nigeria has not adopted arbitration, a mismatch in the tax regime regarding dispute resolution between Nigeria and these countries can increase uncertainties and potentially result in a decline in foreign investments into Nigeria.

Are tax matters really not arbitrable?

Nigeria's reason for not adopting arbitration is that tax matters are not arbitrable. **But is it really the case that tax matters are not arbitrable? Yes, in the case of domestic tax disputes but no, in the case of international tax disputes.** In 2 recent cases (*Esso Petroleum and Production Nigeria Ltd & SNEPCO v NNPC* [*Court of Appeal, Abuja, delivered on 22nd July, 2016*] and *Shell Nigeria Exploration and Production & 3 others v. Federal Inland Revenue Service and another* [*delivered 31 August 2016*]), the Court of Appeal (Court) held that tax matters are not arbitrable. The rationale for this position is section 251 (1) (b) of the Nigerian constitution which, amongst other things, provides that the Federal High Court (FHC) has exclusive jurisdiction over matters relating to the taxation of companies.

This position is correct however, its application should be limited only to domestic tax disputes, that is, disputes arising from the operations of a federal tax legislation or a dispute between Federal Inland Revenue Service (FIRS) and a taxpayer. Therefore, taxes giving rise to domestic tax disputes can be said to be *Nigeria's tax*.

However, in the case of international tax disputes, where 2 sovereign States lay claim to the right to tax the same income or profit, such tax cannot be said to be *Nigeria's tax* because more than one State claims the right to it. For example, where a question arises as to which country as between Nigeria and the UK has the right to impose tax on a company or an economic activity, the dispute is no longer a domestic dispute involving *Nigeria's tax* because it involves the taxing rights of 2 sovereign States.

Therefore, in the case of treaty countries, to guarantee fairness and impartiality, it is not best practice to subject such disputes to Nigerian courts for adjudication. Rather such disputes should be submitted to MAP and then arbitration where MAP fails.

Why mandatory arbitration?

The OECD recommends arbitration because of the deficiencies in the MAP. These include a lack of compulsion on tax authorities to resolve double taxation. The lack of compulsion results in long delays in resolving such disputes. Other shortfalls of MAP include little or no taxpayer involvement, lack of a uniform set of rules as well as a lack of machinery for enforcing MAP decisions. Therefore, it is advisable to adopt binding arbitration complementary to MAP. This is because arbitration provides a guarantee of resolving cases of double taxation. It also infuses integrity and confidence in Nigeria's tax administration as foreign investors and treaty partners need not entertain any fear that international tax disputes would simply be treated as matters involving *Nigeria's tax*. Where the tax laws of 2 sovereign States are involved, Nigeria's domestic courts would not be the most appropriate fora. In addition, arbitration should be adopted because Nigeria's core trading partners and sources of foreign investment have agreed to include arbitration in their dispute resolution process.

Conclusion

Arbitration is not alien to the Nigerian legal system. There is an Arbitration and Conciliation Act which was enacted in 1988. In addition, Nigeria has been a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) since 1970. The New York Convention is an international treaty which allows Nigeria recognize and enforce foreign arbitral awards and allows other countries recognize and enforce awards arising from arbitration proceedings in Nigeria. Furthermore, Nigeria has adopted the United Nations Commission on International Trade Law (UNCITRAL) Rules. These Rules are procedural rules governing the conduct of arbitration proceedings in Nigeria. So arbitration is not a new phenomenon.

International tax disputes will continue to increase as a result of rapidly changing tax rules, increase in global trade and differences in States' tax rules. According to the OECD, there were 8,002 MAP cases as at 1 January 2016 (1,496 of these commenced after 1 January 2016) representing over a 170% increase in the number of MAP cases from 2006. At the end of 2016, about 1,143 of these cases were resolved. The average time to resolve these disputes range between 17 and 30 months. Before BEPS recommendations, many of these cases were not resolved because MAP did not compel States to resolve such disputes. Mandatory binding arbitration, on the other hand, compels State to resolve these disputes.

The MLI allows States to indicate their reservations while adopting BEPS recommendations. Given that States can amend their MLI position, Nigeria still has the opportunity to update its MLI position to include mandatory binding arbitration, as recommended or with modifications, to resolve knotty international tax disputes. This would inject the much needed certainty and robustness in our international dispute resolution mechanism.

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