Unitary Taxation of Multinational Enterprises for a Just Allocation of Income: Nigeria as a Case Study of Africa's Largest Economies.

By

Alexander Ezenagu

Faculty of Law
McGill University
Montreal, Quebec, Canada

April 2019

A Thesis submitted to McGill University
In partial fulfilment of the requirements of the degree of

Doctor of Civil Law

LIST OF ABBREVIATIONS

ACMT	Alternative Corporate Minimum Tax
AfCFTA	African Continental Free Trade Agreement
ALP	Arm's Length Principle
APA	Advance Pricing Agreement
ATAF	African Tax Administration Forum
AU	African Union
BEPS	Base Erosion and Profit Shifting
BEPS Project	BEPS Project of the OECD
CAMA	Companies and Allied Matters Act
CbCR	Country-by-Country Reports
CCCTB	Common Consolidated Corporate Tax Base
CFC	Controlled Foreign Corporation
CUP	Comparable Uncontrolled Price
ECOWAS	Economic Community of West African States
EOI	Exchange of Information
EU	European Union
FDI	Foreign Direct Investment
FIRS	Federal Inland Revenue Service
FPI	Foreign Portfolio Investment
GVCs	Global Value Chains
GPNs	Global Production Networks
GWCs	Global Wealth Chains
HLP	High Level Panel
IFF	Illicit Financial Flow
IMF	International Monetary Fund
MLI	Multilateral Instrument
MNE	Multinational enterprise
OECD	Organisation for Economic Co-operation and Development
OECD MTC	OECD Model Tax Convention on Income and on Capital

PCT	Platform for Collaboration on Tax
PE	Permanent Establishment
PSM	Profit Split Method
SDGs	Sustainable Development Goals
TIWB	Tax Inspectors Without Borders
TNMM	Transactional Net Margin Method
TP	Transfer Pricing
TPGs	Transfer Pricing Guidelines
UN	United Nations
UN MTC	UN Model Double Taxation Convention between Developed and Developing Countries
UNECA	United Nations Economic Commission for Africa
UNHRC	United Nations Human Rights Council
US$	United States Dollar
WP6	OECD Working Party 6

SHORT TABLE OF CONTENTS

TABLE OF CONTENTS

Chapter 4: Unitary Taxation of Multinational Enterprises in Nigeria and within the AfCFTA Framework

Table of Content

Table of Content

ABSTRACT

This thesis makes a case for the tax law treatment of multinational enterprises (MNEs) as unitary firms by Nigeria and other African countries under the recently negotiated African Continental Free Trade Agreement (AfCFTA).

MNEs strategically exploit their legal structures in order to shift their global profits to low or no tax jurisdictions and away from the countries where their real economic activities occur. Treating MNEs as unitary firms has the potential to significantly curtail these tax avoidance practices. Doing so is particularly important for African countries because they are more dependent on corporate income tax revenues for their national budgetary needs. Most of the corporate tax revenue in these countries must come from foreign-owned firms as these firms dominate the large revenue-generating sectors of their economies, such as oil and gas, mining, agriculture and manufacturing.

Two of the main obstacles to the adoption of unitary taxation for MNEs are the corporate legal structures that divide companies across legal jurisdictions, followed closely by the lack of consensus on a workable strategy to implement unitary taxation on a global scale. This thesis answers both of these challenges by providing theoretical and doctrinal support for the unitary approach and by showing the practical aspects and impacts of such adoption through the use of a case study.

The thesis accomplishes the first task by revisiting the theories and principles guiding the international tax system and their limitations in today's global and integrated economic environment. Using Stephen Hymer's theory of foreign direct investment (FDI) and the single enterprise theory, the thesis demonstrates that treating related entities in MNEs or subsidiaries and their parent companies as unitary firms is both legally and economically coherent despite the traditional view of the corporation as an entity separate from its owners.

The thesis then uses Nigeria's experience in taxing MNEs as a case study to demonstrate how unitary approach would significantly reduce tax avoidance and protect the domestic tax base. It extends its recommendations to other African countries as the AfCFTA comes into effect.

Résumé

Cette thèse plaide en faveur d'un traitement fiscal des entreprises multinationales (EMN) en tant qu'entreprises unitaires par le Nigéria et d'autres pays africains dans le cadre de l'accord AfCFTA (African Continental Free Trade Agreement).

Les entreprises multinationales exploitent les structures juridiques de manière stratégique afin de transférer leurs profits globaux aux juridictions à faible imposition ou sans imposition fiscale, et hors des pays où leurs activités économiques sont réellement exercées. Traiter les entreprises multinationales comme des entreprises unitaires pourrait potentiellement limiter considérablement ces pratiques d'évasion fiscale. Cela est surtout important pour les pays africains, qui dépendent particulièrement des impôts sur les sociétés pour répondre à leurs besoins budgétaires nationaux. La majeure partie des recettes fiscales des sociétés dans ces pays doit provenir d'entreprises étrangères, qui dominent les grands secteurs générateurs de revenus de leur économie, tels que le pétrole et le gaz, les mines, l'agriculture et l'industrie manufacturière.

Deux obstacles principaux empêche l'adoption d'une fiscalité unitaire pour les entreprises multinationales: soit des structures actuelles qui permet la division des entreprises entre régions juridiques, ainsi que l'absence de consensus sur une stratégie viable pour mettre en œuvre la fiscalité unitaire à l'échelle mondiale. Cette thèse répond à ces deux défis en apportant un soutien théorique et doctrinal à l'approche unitaire, et en montrant les aspects pratiques et les impacts d'une telle approche à l'aide d'une étude de cas.

La thèse accomplit la première tâche en revisitant les théories et les principes qui guident présentement le système fiscal international et leurs limites vis à vis le context global et l'environnement économique d'aujourd'hui. En utilisant la théorie de l'investissement direct étranger (IDE) de Stephen Hymer et la Théorie de l'entreprise unique, cette thèse montre que le traitement des filiales et leurs sociétés mères ou les entités des EMNs en tant qu'entreprises unitaires est à la

fois juridiquement et économiquement cohérent, malgré la vision traditionnelle que l'entreprise devrait être une entité distincte de ses propriétaires.

La thèse utilise ensuite l'expérience du Nigéria et leur taxation des EMNs comme étude de cas pour démontrer en quoi une approche unitaire permettrait de réduire de manière significative l'évasion fiscale et de protéger l'assiette fiscale nationale. Il étend ses recommandations à d'autres pays africains au fur et à mesure de l'entrée en vigueur de l'AfCFTA.

Acknowledgment

Indeed, it takes a village to raise a child.

My sincere appreciation and gratitude to Professor Allison Christians for guiding me through this journey. It has been one of self-discovery, learning, unlearning and relearning. Her supervision from the time of conceptualisation of the thesis topic to its conclusion has ensured that I appreciate the issues and write them down in a coherent manner. I am very grateful for the lessons and support, Professor Allison Christians.

To my committee members, Prof. Pierre-Emmanuel Moyse and Prof. Peter Dietsch, I am grateful for the time spent reading drafts of this thesis and providing valuable comments and guidance. I am grateful to my external examiner, Prof. Lyne Latulippe for her review and comments.

I am grateful to the Faculty of Law and McGill University for the financial support, which has made this doctoral thesis a reality. Thank you to Prof. Richard Gold, his team and the entire McGill community for the generosity. I am grateful to the Centre for International Governance Innovation (CIGI) Canada for the generous financial support given to me for three years, through its International Law Research Program Scholarships. I am very grateful CIGI. I am grateful to Brigitte Alepin and Louise Otis of TaxCoop Canada who provided the environment to discuss and critique international tax issues through collaborative projects. I am grateful.

I am grateful to Sol Picciotto, Mick Moore, Michael Durst, Simon Rees and everyone at the International Centre for Tax and Development (ICTD) who have contributed to this journey. To Sol Picciotto, my special gratitude for taking me under your wings and mentoring me since our first meeting in 2016. Thank you for your books and papers which have formed my views on international tax issues. I am eternally grateful for the support and for the opportunity to work with you.

I am particular grateful to Professor Attiya Waris for her immense contribution to the development of the thesis. To Luckystar, Victor Adegite, Mustapha Ndajiwo, Jason Braganza, Kenneth Njuguna, Catherine Ngina, Aruna Bolaky Bineswaree, Will Fitzgibbon, Alvin Mosioma, thank you for being great friends and awesome colleagues at the same time. I have enjoyed greatly the intellectual exchanges. I am grateful to Milly Nalukwago of Uganda Revenue Authority and Dr. Femi Akinfala and Tyem Pirfa of the Federal Inland Revenue Service of Nigeria for their help with obtaining sample data for the research on transfer mispricing in both Uganda and Nigeria.

To my family, thank you for the support and prayers. To my friends, this is for you. I shall attempt an exhaustive list but apologies ahead to anyone I miss to mention, your contributions are highly appreciated. To Yemisi, thank you for the love, support, care and friendship. Thank you for always being there. To Noble Igbokwe, Ehi, Sixtus, Pamela Addo, Afoma Ofodile, Ngozi Okokwu, I am grateful for the years of support and friendship. To Goodness Obiorah and Nkechi Azinge-Egbiri, thank you for always having my back and believing in me. To Ayo Akenroye, Eytan Tepper, Idris Malik, Demola, Gbolahan, Sandra Ubah, Adama Dellou, Michelle Manks, Laurie, Jean-Moise Jeanty, Timiebi Jeanty, Adepetu Temitope, thank you for being my family in Montreal.

I am grateful to Chinwe Odigboegwu, Tola Bella, Stella Duru, Kehinde Ojuawo, Okey Ejibe, Yetunde Oshunrinde, Ayodele Oni, Sola Ori, Chidiebere Eze-Ajoku, Tunji Olalere, Lanre Agboola, Akinsola Fadeyi, Thebe Ikalafeng, Alex Schmid, Beulah Adeoye, Ifunanya Moneke, Lydia Gana, Doreen Ndishabandi, Adaora Okafor, Christiana Vann, Grace Atuhaire, Sia Biwott, Eyitene Iwere, Tope Oyedeji, Ifeoluwa Ogunbufunmi, Pitan Akhihiero, Alexander Harutyunyan, Tope Lawal, Taye Balogun, Ngozi Otti, Meghnar Kumar, Grace Mbogo, Mercy Adhiambo, Lanre Adeloye, Dissi Obanda, Adaora Nwajiaku, Kayode Fasominu, Chris, Chijioke Oji, Emmanuel Lawan, Onazi Aboh, Yewande Alimi, Irene Nwaukwa, Tomiwa Sage, Remi Soile, Fali Hamu, Uchendu Jennifer, Ayo Sogunro, Aly Ramji, Stanley Uche, Obiajulu Umeh, Bryan Okichie, Egbiri Egbiri, Gomiluk Otokwala, Mayfield Bado, Tyndale, Akintola Olapeju, Nimmo Elmi, James Babatunde-Osho, Zuwa Matondo, Desmond Ogba, Temple Uchegbune, Adetola Onayemi, Steva Nyawade, AliceWanja, Purity Maina, Sornaatah Nubari Nke-ee, Ugochi Igbojekwe, Obayan Bimbo, Japhet Omojuwa, Frances Aggrey, Tobi Ricketts, Charles Eromosele, Jake Effoduh, Ebenezer ThankGod, Olivia Muia, Nnaemeka Nwachukwu, Anita David-Akoro, Olaronke Thomas, Chikamadu Okoroafor, Nora Alabi, Kasiemobi Eze, Makua Igbokwe, Esther Okoro, Emeka Okoli, Boddhi Satva, Adaeze Ezeh, Salihu Umar, Adashu Ashu, Baba Kam Selem, Claudia Auko, Ayoola Odeyemi, Rahina Zarma, Marilyn Okowa, Bala Banda, Sahmak Chirtau, AnneSofie Misiani and Kike Oyerinde. Thank you for the encouragements and contributions.

To my mentors, Prof. Abiola Sanni, Prof. Fidelis Oditah, Osita Chidoka, Akpata Olu, Kenneth Odidika, Demola Akinrele, Dapo Otunla, Edem Andah, Fola Jaiyesimi, thank you guiding me on the right part. To my partners at Bandaree, thank you for your support.

This PhD thesis is dedicated to all those who have not been limited by the circumstances of their birth or background. Your dreams are valid.

Chapter 1: Introduction- Setting the Stage

Table of Contents

1.1 Executive Summary of the Thesis

With activities in multiple countries, MNEs would face the likelihood of double or even multiple taxation on their profits but for unilateral and international mechanisms that allocate income across countries. The present international mechanism to avoid double taxation of MNEs is modelled after the OECD Model Tax Convention on Income and on Capital (OECD MTC)[1] and the UN Model Double Taxation Convention between Developed and Developing Countries (UN MTC),[2] though, the OECD has assumed supranational status with wide reach and influence through its model tax treaty, commentaries, guidelines and recommendations.

[1] OECD (2017), Model Tax Convention on Income and on Capital: Condensed Version 2017, OECD Publishing, Paris.
[2] United Nations (2017) Model Double Taxation Convention between Developed and Developing Countries 2017. United Nations: New York.

Integral to the present-day model tax treaties (both the OECD MTC and UN MTC) is the popularity of the separate entity and arm's length approach to income allocation. This separate entity and arm's length approach treats subsidiaries of an MNE as unrelated entities for accounting and tax purposes. It requires these related entities to act with each other on market terms when fixing the prices of goods and services transferred to each other (transfer pricing). This approach to income allocation has been adopted by the largest economies in Africa (Nigeria, South Africa, Egypt, and Algeria) and provides the framework for avoiding double taxation arising from cross-border economic activities.

While these model tax treaties, adopted in bilateral agreements between countries, have aided countries to attract foreign direct investments, they have been used by MNEs to avoid taxation with far-reaching consequences for the revenue and sustainable development of states. The avoidance of taxes by MNEs is common in African countries. For instance, a report commissioned by both the African Union Commission (AUC) and the United Nations Economic Commission for Africa (UNECA) in 2015 through a high level panel headed by former South African president, Thabo Mbeki (the Mbeki Report)[3] revealed that African countries lose over US$50 billion annually in illicit transfer of funds out of the continent. This illicit transfer of funds, known as illicit financial flows (IFFs) in the literature occurs through both criminal and unacceptable methods. One such unacceptable method is the manipulation of prices of goods and services transferred between related entities who take advantage of their corporate structure, a practice known as transfer mispricing.

As a result of the opportunities for tax avoidance brought about by the adoption and implementation of these model tax treaties, stakeholders have called for the reform the global tax system. One such ongoing reform is the Base Erosion and

[3] United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf

Profit Shifting (BEPS) Project led by the OECD in line with the mandate of the G20.[4] The BEPS Project sets out to reform the international tax rules to ensure that MNEs are taxed "where economic activities occur, and value is created".[5] Other discussions are taking place at the IMF, the World Bank, the UN, the EU, sovereign states and civil society organisations, all desirous to see a change in the global tax architecture. The focus on reforming the global tax rules is increasing and alternatives to the current tax system are being recommended by interested parties.

As discussion continues on the international stage on reforming the global tax rules, this thesis aims at contributing to the debate through the lens of African countries. The thesis makes a strong case for the tax law treatment of MNEs as unitary or single firms[6] by Nigeria and other African countries. This treatment of MNEs as unitary firms, the thesis argues will reduce significantly tax avoidance practices of MNEs through the erosion of tax bases in countries where real economic activities occur and shifting of corporate profit to low or no tax jurisdictions.[7] This is particularly more important for African countries as they

---

[4] The Group of 20 is a forum for the world's leading industrialised and emerging economies. Members of the G20 are Argentina, Australia, Brazil, Canada, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Korea, Turkey, United Kingdom, United States of America, China, South Africa and the European Union.

[5] G20 (2013), "Tax Annex to the Saint Petersburg G20 Leaders Declaration", G20 Information Centre. Online: <http://www.g20.utoronto.ca/2013/2013-0905-tax.html> OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing online: <http://dx.doi.org/10.1787/9789264202719-en >; OECD (2014), Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project, OECD. <www.oecd.org/tax/beps-2014-deliverables-explanatory-statement.pdf>

[6] Unitary taxation will prevent the use of intragroup contracts to effectuate divergence between the countries in which income is generated through value-adding activities, and the country in which the income is treated as earned for tax purposes. See: Michael Durst, "Beyond BEPS: A Tax Policy Agenda for Developing Countries" (2014) ICTD Working Paper 18.

[7] Oxfam International argues that: "Erosion of a country's tax base takes place when TNCs reduce their tax burden by avoiding the payment of taxes where income is generated. Base erosion constitutes a serious risk not only to the tax revenues needed by governments to finance public services, but also to tax sovereignty and tax fairness. Put simply, base erosion perpetuates poverty and contributes to increasing inequality": Oxfam International, "Fixing the Cracks in Tax: A Plan of Action" Joint recommendations to the G20 and OECD for tackling base erosion and profit shifting, online: <https://d1tn3vj7xz9fdh.cloudfront.net/s3fs-public/file_attachments/fix-the-cracks-in-tax_0.pdf>

are more dependent on corporate income tax,[8] which are susceptible to base erosion and profit shifting by foreign-owned firms who dominate the large revenue-generating sectors of their economies, such as oil and gas, mining, agriculture and manufacturing.

The thesis is discussed within two contexts: Nigeria as a sovereign, federal state; and the recently negotiated AfCFTA.

Nigeria, Africa's largest economy remains largely capital importing, with significant reliance on FDIs and foreign portfolio investments (FPIs) by MNEs. A handful of its home-grown companies are present in other African countries, carrying out business as MNEs. In addition to granting tax incentives, exemptions and holidays to MNEs to attract investments, the Nigerian government signs tax treaties with capital-exporting countries and trade partners, for the prevention of double taxation. However, it suffers significant revenue loss as a result of transfer mispricing. Sample data obtained from the Federal Inland Revenue Service of Nigeria (FIRS) and reported in this thesis reveal that tax avoidance in the country may be as high as 300 per cent of declared returns of subsidiaries of MNEs tax liable in Nigeria. This thesis seeks to offer an effective way of taxing these MNEs with the result of curtailing IFFs through transfer mispricing.

In addition, the thesis argues that the recommended adoption of the unitary approach by Nigeria should be adopted by African countries as a continental framework for taxing MNEs, especially as the AfCFTA comes into effect in 2019. In March 2018, heads of governments of African countries negotiated and agreed to establish the African Continental Free Trade Agreement (AfCFTA). The AfCFTA seeks to create a single market akin to the European Union Single Market. While the AfCFTA represents an important development in the industrialization, sustainable and inclusive socio-economic development of the

[8] Crivelli, de Mooij & M Keen claim that corporate income tax in low-income countries (which include African countries) accounts for 16 per cent of the revenue of the countries, as against 8 per cent in high-income countries. see: Ernesto Crivelli, Ruud de Mooji & Michael Keen, "Base Erosion, Profit Shifting and Developing Countries" (2015) IMF Working Paper No 15/118.

African continent, its expected benefits may not be achieved if the potential transfer mispricing opportunities created by the AfCFTA are not addressed. To ensure that the tax revenue gains of the AfCFTA are obtained by participating countries, the thesis recommends the adoption of the unitary approach. Failure to adopt this may constitute a non-tariff barrier to the effective implementation of the AfCFTA, while discouraging FDIs into countries for fear of loss of tax revenue.[9]

1.2 Objectives of the Thesis

This thesis has set out to answer two questions. First, what should be Nigeria's (and Africa's) appropriate tax law treatment of MNEs engaged in cross-border economic activities if we are to guarantee the just allocation of income, arising from cross-border economic activities? Second, how should Nigeria's model tax treaty be amended to reflect this tax law treatment of MNEs?

It proceeds to propose the unitary approach in the tax law treatment of MNEs. Unitary taxation operates from the understanding that the profits generated by MNEs, arise from the integration of its activities. Under this approach, a consolidated account for the integrated firms in a corporate group is furnished and intra-firm price transfer denied. A global profit is generated for all the related entities. The global profit is then allocated to tax jurisdictions using a pre-determined formula based on pre-agreed factors (commonly, payroll, asset, sale), reflecting the economic activities in each tax jurisdiction by related entities of the corporate group liable to tax in the jurisdiction.

The thesis argues that the continuous treatment of MNEs as separate entities and the application of the arm's length principle is to dwell in self-denial of the purpose

[9] Michael Durst, "Developing Country Revenue Mobilisation: A Proposal to Modify the 'Transactional Net Margin' Transfer Pricing Method" (2016) ICTD Working Paper 44. In his discussion of the transactional net margin method of transfer pricing, Durst opines: "It seems likely to this author that the apparent toleration by most developing country governments of tax planning structures based on TNMM reflects, in large part, a homeostatic equilibrium that has developed in recent decades between countries' desire for tax revenue on one hand, and their countervailing desire to keep corporate tax burdens low to avoid discouraging inbound investment".

and structure of MNEs, and the economics of scale obtained from integration of the entities and central ownership and control.

The timing of the thesis is fitting, as the world debates the international tax rules which should guide the allocation of income among related entities. The thesis offers new insights to the discourse, while recognising existing arguments and contributions to the discourse. The thesis' support for the unitary approach to income allocation— a radical departure from the current tax system— is premised on sound arguments.

First, the relevance and study of MNEs and FDIs by MNEs took center-stage after the second world war, while the international tax principles were established in the 1920s. Thus, the roles of MNEs in the global economy and the ownership, control and internalization attributes of the MNE structure, coupled with the benefits of FDIs for companies were not taken into consideration during the negotiations. The opportunity to set the global tax rules taking into account the nature of MNEs and their business models is offered today.

Second, in the 1930s, international trade consisted mostly of trade in tangible goods, which were trackable and involved the actual movement of goods and persons. Today, significant volume of trade occurs in the service industry and as such the existing structure fails at actively capturing trade in this sector. Though this thesis is focused on the commodities industry, the recommendations therein are appropriate for trade in intangibles and services.

Third, the Information Age, with the advent of the digital economy presents difficulties for tax authorities in capturing business activities through these channels under the existing system. The OECD recognized this limitation when it stated in its BEPS Action 1 Report: "The options analyzed by the TFDE to address the broader direct tax challenges, namely the new nexus in the form of a significant economic presence, the withholding tax on certain types of digital transactions and the equalization levy, would require substantial changes to key international tax standards and would require work."[10]

In addition, globalization, alongside economic integration defines today's world order and reinforces the limitations of the existing system. In the 1930s, foreign companies manufactured in their home states and sold finished products to related entities that were liable to tax in the host states. Transfer pricing practices were limited to the pricing of finished products sold by manufacturing entities of parent companies to their related distributing entities. However, with the advent of global production networks (GPN) and global value chains (GVCs), a finished product, represents inputs from multi-jurisdictions. The iPhone is an example of such assemblage of multiple jurisdictions. Thus, there is increased reliance on inputs from other countries and MNEs today are structured to actively capture such inputs. Effectively pricing these intermediate products and increasing transactions between related entities has proven difficult for tax authorities to the advantage of MNEs who are able to manipulate the prices for tax gains.

To deny the importance of GPNs and GVCs in the tax treatment of MNEs, is to facilitate global wealth chains (GWCs). Seabrooke and Wigan define GWCs as "transacted forms of capital operating multi-jurisdictionally for the purposes of wealth creation and protection".[11] They argue that wealth chains hide, obscure and relocate wealth to the extent that they break loose from the location of value creation and heighten inequality.[12] Nigeria, as most African countries, remains the investment destination of MNEs on the African continent, providing both raw materials and intermediate goods to the world, thus, attracts large number of

---

[10] OECD (2015), "Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report" OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, online: <https://www.oecd-ilibrary.org/docserver/9789264241046-en.pdf?expires=1554247343&id=id&accname=guest&checksum=CAC6593CCD9BD4751254CCAD63C0BA28.

[11] Leonard Seabrooke & Duncan Wigan, "The Governance of Global Wealth Chains" (2017) Review of International Political Economy, Vol 24, No 1, at 1–29 at para 3.

[12] Ibid at 5.

MNEs competing for the nation's resources. It is important that it is able to tax the economic activities that take place in its jurisdiction.

Thus, the economic integration of MNEs, the high volume of intra-firm transactions and the way MNEs are structured today defeat the treatment of companies as separate entities, given that for MNEs to optimally function, integration is a key factor.

Lastly, there is the argument of non-representation. During the negotiations in the 1920s, most African countries were colonies of imperial masters and as such were at the command of the negotiators. The interests of African countries were unimportant then. This is not the case today, necessitating the need to re-consider the global tax principles countries abide by. This thesis adds to the voice of African countries as they contribute to the debate on the formulation of the new global tax rules.

1.3 Methodology

This thesis adopted a desktop-based approach with focus on analysis of the doctrines germane to the allocation of taxing rights. I analysed tax theories, concepts and principles relevant to the argument for a shift to the unitary taxation of MNEs.

I undertook a literature review of the concepts of income apportionment, transfer pricing, separate entity, unitary taxation, tax avoidance, and IFFs, in order to identify the key legal and quasi-legal texts by reference to their relevant prevalence in international tax law scholarship. I undertook the study and analysis of model tax conventions, guidelines, norms and standards promulgated by the OECD, the UN, the EU and the African Tax Administration Forum (ATAF). I have taken into account the recent efforts of the Platform for Collaboration on Tax (PCT) to address some of the challenges of the present international tax system. Nigeria's treatment of MNEs and cross-border economic activities was examined, alongside a review of the negotiated AfCFTA.

In addition, the thesis has benefitted immensely from the sample data received from the revenue authorities of both Nigeria and Uganda. While the tax avoidance practices of MNEs have always been argued in the literature and the effects of their practices in numbers present in mainstream media, this thesis introduces numbers and discussions from the African continent to the global discourse. Sample data obtained and informal interviews conducted by me were to simply help me understand the concepts and issues in this discourse better and point me towards relevant texts. The sample data used in the thesis are anecdotal. No interviews, consultations, or archival research have been carried out to verify their accuracy. As such, their accuracy is not guaranteed. At best, they should be read as anecdotal confirmation of claims that transfer mispricing occurs in these countries, and serve to corroborate arguments, facts and figures highlighted in other parts of this thesis.

Furthermore, I have situated the socio-legal study and impact review on the existing tax system in African countries, bringing to the attention of the readers the tax avoidance practices and effects in Africa. I elected to use a case study approach to adequately situate the processes, experiences and impacts of tax avoidance.[13]

I chose Nigeria as my case study for these reasons. First, Nigeria is Africa's largest economy in terms of GDP, with the largest share of the exports, imports, FDI and FPI activities taking place in the ECOWAS region. Second, Nigeria possesses a fair number of its home MNEs doing businesses in the ECOWAS region and other

---

[13] A case study offers the opportunity for a holistic study of an issue. It provides the time and space to achieve a comprehensive understanding of the issue, its application and impacts on a subject. It also provides presumptive basis for other subjects where the subjects have similarities. It avoids the temptation to make a discussion solely based on theories and doctrines and provides the platform to situate it in real experiences. It bridges theories and practice in an effective manner. See, Allison Christians, "Case Study Research and International Tax Theory" 55 SLUL J 331 (2011).

African countries. Nigeria wields political and economic dominance in the ECOWAS region and as such guides the policy direction of the region. Nigeria has tax treaty agreements with its major trading partners-Canada, South Africa, Netherlands, China, France and Italy.

Given Nigeria's federal system of government, it provides useful analysis in the consideration of the application of the unitary taxation, whether at the state, regional, continental or world-wide level. Furthermore, Nigeria represents a reflection of the largest African economies and their competition for foreign investments, both direct and portfolio. Thus, my research provides a template to be adopted by other African countries. I have discussed this thesis within the context of the AfCFTA.

Limitations

Nigeria's transfer pricing (TP) regime is nascent (the TP regulations were enacted in 2012) and subsequently reviewed in 2018, and the TP unit is relatively new with limited expertise and capacity. To the best of my knowledge, TP audits and investigations are just commencing, with a few cases before the tax appeal tribunal. As at today, there is no record of concluded transfer pricing cases and as such, no official data on court ruling on transfer mispricing is available. Given that tax returns and audits are highly confidential matters, except where they have been brought before a court or tribunal, this thesis has had to rely on sample data provided by the Nigerian tax authority and other information contained in the literature, especially reported cases from other jurisdictions.

This absence of data on transfer mispricing occurs in many African countries whose transfer pricing rules are just developing and are yet to be tested in courts or tribunals. As such, reported cases from the continent are scarce and sparsely used in this thesis. I have produced here and relied upon the few transfer mispricing cases on the African continent, which have been adjudicated upon and made publicly available. However, the presence of transfer pricing abuses on the continent and impacts are not in doubt, as the literature reveal.

1.4 Outline of the Project

This thesis proceeds as follows. Chapter 1 sets the stage for the discussion. Here, I provide a background to the thesis, explaining briefly what the issues are and how they came up. I explain the traditional theories of taxation and their relevance in today's global economy and activities of MNEs.

In chapter 2, I discuss tax avoidance and its forms. I undertake an in-depth study of the two principles upon which the present international tax system is built upon: the separate entity treatment of related entities; and the arm's length standard requirement in business relations of related entities. This chapter evaluates the common-law case of Salomon v Salomon (corporate personality test) and its extension to the treatment of multinational entities. The chapter considers the introduction of the arm's length principle in treaties and its use. The chapter proceeds to discuss transfer pricing, its application and implication for cross-border businesses and tax avoidance opportunities presented by its use. The chapter concludes by showing how the present system encourages tax avoidance and why it is maladapted to contemporary global economic order and unsuitable for a just tax system.

In chapter 3 of this thesis, I present the efforts of the global community to reform the existing tax system. This chapter focuses on the ongoing reform processes both at the international level and on the African continent. It unpacks the reforms of the OECD, especially through the Base Erosion and Profit Shifting Project (BEPS Project) and the revised Transfer Pricing Guidelines. It considers the activities of the UN through its tax committee, in addressing tax avoidance and evasion. The chapter looks at the recently-formed PCT and its efforts at contributing to the design of a fair tax system. Focusing on the African continent, this chapter looks at ongoing reform actions, especially led by the African Tax Administration Forum (ATAF) through its model treaties and transfer pricing guidelines.

In Chapter 4 of this thesis, I focus on the unitary approach of income allocation of MNEs. Having established in previous chapters, that the existing international tax system is designed to fail in today's global economy, to deprive developing countries of their wealth, and to encourage base erosion and profit shifting; this chapter makes a case for the adoption of the unitary approach. It defines, analyses and advocates for the adoption of a unitary approach to taxing the income of MNEs. It discusses the contemporary application of unitary taxation by countries and their historical development. It focuses on the legal and economic implications of the unitary approach. The chapter concludes by unpacking and addressing the challenges to implementing the unitary approach of income allocation for MNEs.

In chapter 5 of the thesis, I discuss the legal and political steps necessary for achieving a shift to the unitary taxation approach. Proceeding from the general discussion of unitary taxation in Chapter 4 of this thesis, this chapter sets out to recommend reforms to the tax law treatment of MNEs in Nigeria. It looks at the legislative and regulatory treatment of multinational entities in Nigeria, by considering the provisions of the Companies and Allied Matters Act (CAMA) and the Companies Income Tax Act (CITA). It looks at the model tax treaty of Nigeria and its treatment of multinational entities. I provide textual suggestion for a new article 9 of model treaties, and by extension, provision on treatment of MNEs in the national laws. I argue that to garner the needed political will, both at the national and global level, adopting a broad definition and scope of IFFs to include transfer mispricing (as already seen in some literature) is needed. This is particularly important considering that addressing IFFs is part of the UN SDGs.

In chapter 6 of the thesis, I conclude and re-emphasize my support for the unitary approach.

2. Background to the Thesis

The economies of a sizeable number of African countries are dominated, in terms of value of trade, by MNEs who export capital into host states with the expectation of making profits and repatriating the profits to their home countries.[14] To ensure that governments provide and maintain the necessary infrastructure for business, profits made by these companies are taxed. This tax is justifiable on the benefits these companies obtain from the use of the physical and social infrastructure provided in these countries. A major aspect of this taxation is corporate taxation, that is, the taxation of the profits of the MNE as a legal entity.

Corporate taxation is important to African countries, in part due to the exploration of its abundant natural resources by companies; and largely informal sector with minimal record-keeping taking place, leading to difficulty in tax collection. Hence, corporate taxation, which accounts for 16 per cent of revenues of developing countries, compared to 8 per cent for high-income countries, attracts strong interests from revenue authorities, civil societies and individual taxpayers on the continent and globally.[15] However, in Nigeria, as in other African countries, expected revenue from corporate taxation is lost to tax avoidance practices of MNEs, aided by the existing international tax system.

MNES have justifiable reasons to defend their profits. By virtue of the cross-border economic activities they engage in, they are exposed to tax liabilities in more than one jurisdiction: the home state and the host state and could be tax liable in multiple states where they have some form of presence or obtained economic value there.[16] The conflicting tax claims by states leads to a double taxation problem. Beyond determining jurisdiction to tax the profit of the MNE, determining the

[14] Attiya Waris, "How Kenya has Implemented and Adjusted to the Changes in the International Transfer Pricing Regulations: 1920–2016" (2017) ICTD Working Paper 69. Waris's paper shows the presence of MNEs in the East African region, the sectors of the economy they participate in and their activities.

[15] Sol Picciotto, "Taxing Multinationals as Unitary Firms" (2016) ICTD Working Paper 53.

[16] Brian Arnold & James Wilson, "Aggressive International Tax Planning by Multinational Corporations: The Canadian Context and Possible Responses" (2014) SPP Research Papers, Vol 7, Issue 29. The authors argue that the proliferation of income tax systems and the increase in tax rates during the 20th century made it necessary for multinationals to engage in defensive tax planning to eliminate double taxation and reduce excessive taxation by source countries.

quantum of profit to be allocated to each of the conflicting states poses a second conflict. Resolving these issues of double taxation and the allocation of profit has posed great challenges to the international tax community for decades, and as at today, a widely-accepted resolution is yet to be reached.

Almost a century ago, tax experts from the then superpowers gathered under the auspices of the International Chamber of Commerce, and subsequently, the League of Nations, to address the double taxation international firms were exposed to.[17] These experts resolved, amongst a host of others, two important principles that will come to influence greatly where multinational entities pay taxes and what they pay. These principles are: that related entities in a corporate group be treated as separate from each other; and secondly that the allocation of profits between related entities be based on the principle that the parties act as independent parties would- the arm's length principle. These principles are enshrined in Article 9 of the OECD MTC and the UN MTC and have been adopted in bilateral treaties modelled on either. The provisions of article 9 are found in the national laws of many countries, including African countries, which possess power of adjustment provisions in their local laws.[18]

These two principles- the separate entity treatment and the arm's length principle- have come to influence both domestic tax laws of countries and the international tax system. Admittedly, they have provided order in an area characterized by unhindered display of fiscal sovereignty.[19]

Though these model tax treaties have achieved the creation of a global tax system, which has aided trade among countries, investment in foreign countries by capital-exporting countries and have significantly prevented the double taxation of MNEs,

[17] Mitchell Carroll, "Prevention of International Double Taxation and Fiscal Evasion: Two Decades of Progress under the League of Nations" (1939), League of Nations; see also, Mitchell Carroll, "International Tax Law" (1968) The International Lawyer, Vol 2, 692; Mitchell Carroll, "Allocation of Business Income: The Draft Convention of the League of Nations" (1934) Columbia Law Review, Vol 34 at 473–498.
[18] The Corporate Income Tax Act of Nigeria, c 21 s 22.
[19] Arnold & Wilson, supra note 16.

they have however created a system which is vulnerable to the erosion of tax bases and the shifting of taxable profits from high-tax jurisdictions to low-tax jurisdictions. They have encouraged retaining losses and expenses in high-tax jurisdictions as a way of out-stripping profits out of the high-tax jurisdiction. As the Paradise Papers[20] reveal, MNEs take advantage of gaps in the interactions between domestic laws and tax treaties and guidelines and the impracticability of the current tax system, to erode the tax bases of countries and shift profits out of them to favorable jurisdictions.[21]

The impacts of base erosion and profit shifting are worse for African countries, who are already behind the rest of the world in the provision of infrastructure, public services and social welfare for its citizenry, and in dire need of every dollar if it is to achieve the SDGs.

Critics have accused the existing approach of income allocation, of brokering double non-taxation, in its bid to avert double taxation.[22] It has been accused of not being fit for purpose and as such should be revised or replaced with a new system of taxation of cross-border economic activities.[23]

Some critics of the current tax system demand a shift to a unitary taxation and formulary apportionment approach[24] to profit allocation among entities in a

[20] Publications by the award-winning International Consortium of Investigative Journalists (ICIJ), focused on revealing the tax avoidance and evasion practices of companies. Details on the activities and publications can be found online: <https://www.icij.org/>

[21] Rosanne Altshuler & H Grubert, "The Three Parties in the Race to the Bottom: Host Government, Home Governments and Multinational Companies" (2005) CESifo Working Paper, No 1613.

[22] Brian Arnold, "The Role of a General Anti-Avoidance Rule in Protecting the Tax Base of Developing Countries" (2017) in A Trepelkov, H Tonino & D Halka, eds., United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries 2nd ed., New York: United Nations; Action Aid, "Calling Time: Why SABMiller Should Stop Dodging Taxes in Africa" (2010; updated 2012), ActionAid UK.

[23] Reuven Avi-Yonah, "The Rise and Fall of Arm's Length: A Study in the Evolution of U.S. International Taxation" (2007) Law and Economics Working Paper, University of Michigan Law school.

[24] Also described in this thesis as unitary approach or unitary taxation. In chapter 4 of the thesis, I discuss the distinction between both and the choice of the phrase, unitary approach.

corporate group.[25] They strongly believe that treating related entities in a corporate group, or subsidiaries and their parent companies as unitary firms, will significantly reduce tax avoidance by MNEs, protect the domestic tax bases of countries, without disincentivizing international trade and FDIs. They are convinced that a shift to the unitary taxation and formulary apportionment approach to profit allocation will achieve inter-nation equity, inter-taxpayer equity and neutrality. This thesis agrees with these claims. This thesis predicates its demand for an alternative approach to income allocation on the failure of the existing system, and the changing economic models and realities.[26]

The limitations of the global tax system established by the League of Nations were known from its creation.[27] Mitchell Carroll had set out clearly the difficulty of arriving at a global tax system. He held the view that:

> "The subject of allocation may be described as being at the crossroads of all sciences. It involves not only the fiscal sovereignty of States, and civil, commercial and sometimes penal law, but also commercial, geography, economics, business management, and last, but not least- accounting"[28]

Realizing this difficulty of establishing a consensus and just global tax system, palliatives and patchy reforms are regularly introduced by supranational organisations charged with fixing the global tax system. Today, both the OECD and the UN assume such responsibility, proffering solutions, in form of revised treaties, commentaries, guidelines, recommendations and policies, all aimed at effectively addressing the biting tax evasion and avoidance practices of MNEs.

[25] Stanley Langbein, "The Unitary Method and the Myth of Arm's Length" (1986) Tax Notes 30: 625.

[26] For a broader discussion on the difficulties of implementing the existing tax system in the African context, see: Waris, supra note 14.

[27] Bret Wells & Cym Lowell, "Tax Base Erosion and Homeless Income: Collection at Source is the Linchpin" (1965) Tax Law Review at 65. In their paper, they state that: "Even the early debates recognized that the flaw in the foundational premise was that MNEs could create holding companies in tax favorable jurisdictions that could produce income not materially taxed in any country (that is, income that is not taxed in the source country and is earned in a country of residence that chooses not to tax, which we refer to as 'homeless income').

[28] Carroll, supra note 17.

While measurable gains have been made, there is strong scepticism in some quarters, especially among developing nations.

The recommendations and guidelines emanating from the BEPS Project have been met with great criticism by dissatisfied governments, civil societies and tax experts, who claim that the recommendations therein do not effectively address the issues facing the taxation of global companies. For example, Picciotto claims that the BEPS project outputs have not resolved fundamental problems of how to apportion MNE profits, especially in the digitalized economy.[29]

Hence, the question arises: is unitary taxation of MNEs the obvious solution to the issues which arise from the current system of taxation of MNEs for Nigeria and other African countries? This question is the crux of the thesis.

The conclusion of this thesis and the discussion herein are in line with the overarching goal of Nigeria's company tax laws: to adequately return to the purse of the government taxes from the exploration of the state's resources. For instance, the 2018 transfer pricing rules of Nigeria has as one of its objectives: "ensure that Nigeria is able to tax on an appropriate taxable basis corresponding to the economic activities deployed by taxable persons in Nigeria, including in their transactions and dealings with associated enterprises."[30] The argument is that the current tax system does not guarantee that the objective of aligning the taxation of profits with where economic activities are deployed will be met. The alternative of unitary taxation guarantees that.

This position is supported by other experts. For example, Durst, is of the view that one way of taxing profits where the economic activities occur, is for countries to "revise transfer pricing rules so as to disregard the claimed effects of contracts made between members of commonly controlled groups, and instead look to the

[29] Sol Picciotto, "Problems of Transfer Pricing and Possibilities for Simplification" (2018) ICTD Working paper 86.
[30] The Income Tax (Transfer Pricing) Regulations, 2018, pursuant to the Federal Inland Revenue Service (Establishment) Act, 2007, r 2(a).

actual geographic locations of the group members' business activities- for example, where their employees are stationed and where their customers are located- in determining how income should be apportioned between group members."[31] This suggested approach by Durst effectively adopts the unitary taxation with formulary apportionment treatment of multinational entities.

The concept of unitary taxation of related entities is not a new one.[32] Wells and Lowell claim that Hungary and Poland on May 12, 1928, executed a tax treaty, treating related entities as unitary firms, coupled with the use of formulary apportionment in allocating the combined income of the non-resident company and its subsidiaries based on the relative gross income derived from the various establishments.[33] The United States is reputed to have treated related entities as unitary firms, applying formulary apportionment in the 19th century to the railroad trade practices.[34] Weiner writing on the U.S. practice, writes that rather than measuring the property value in each state, companies measured their total property value (railroad track, rolling stock, franchise, etc.) as a single unit and distributed that total across the states according to the value of the railway lines located in each state relative to the total value in all of the states.[35] Canada, for its part, uses formulary apportionment for companies with permanent establishments across provinces.[36] However, discussions on the application of unitary approach in Africa and adoption by African countries are scarce in the literature.

[31] Michael Durst, "Limitations of the BEPS Reforms: Looking beyond Corporate Taxation for Revenue Gains" (2015) ICTD Working Paper 40.
[32] Marco Runkel & Guttorm Schjelderup, "The Choice of Apportionment Factors under Formula Apportionment" (2007) CESifo Working Paper Series, No 2072, CESifo Group Munich.
[33] Bret Wells & Cym Lowell, "Income Tax Treaty Policy in the 21st Century: Residence vs. Source" (2013) Columbia Journal of Law, Vol 5, No 1.
[34] Reuven Avi-Yonah & Kimberly Clausing, "Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment" (2007) Law & Economics Working Papers Archive: 2003-2009, Art 70. In their paper, they consider the application of formulary apportionment for taxing the corporate income of multinational firms liable to tax in the United States.
[35] Joann Weiner, "Formulary Apportionment and Group Taxation in the European Union: Insights from the United States and Canada" (2005) Working Paper, No 8: Joann Weiner, "An Economist's View of Income Allocation under the Arm's Length Standard and under Formulary Apportionment" (2010) The State and Local Taxpayer. Symposium Edition at 25–56.
[36] Durst, supra note 6.

The adoption of unitary taxation comes with its controversies and difficulties.[37] For one, on consolidating or combining separate entities, the question is whether to delineate the group in terms of legal or economic relationships. Another consideration is whether to apply the formulary apportionment to worldwide income or a "water- edge"[38] limitation. The political and administrative complexity, alongside the international cooperation required for a transition away from the present system to a unitary taxation, may stand against its adoption.[39] Avi-Yonah and Tinhaga have argued that a shift to the unitary taxation of multinational entities can be compatible with most of the tax treaties, and that developing countries in particular can adopt it in most cases with or without a tax treaty.[40]. This thesis addresses these controversies and difficulties of implementing the unitary approach.

Finally, it is the conclusion of this thesis that African countries are well-positioned to significantly benefit from this alternative approach, contrary to the experience under the current global tax system.

3. Understanding the Right to Tax

---

[37] For a broad discussion of the limitations of adopting the unitary taxation with formulary apportionment of income allocation, see: Alexander Ezenagu, "Faltering Blocks in the Arguments against Unitary Taxation and the Formulary Apportionment Approach to Income Allocation" (2017) Asper Review of International Business and Trade Law, Vol XVII.

[38] Limiting the consolidated group to a country, region or continent, as against a worldwide consolidation of entities in a corporate group. See, Walter Hellerstein, "State Taxation of Corporate Income from Intangibles: Allied Signal and Beyond" (1993) Tax Law Review, Vol 48, No 4 at 739–879

[39] Jinyan Li, "Global Profit Split: An Evolutionary Approach to International Income Allocation" (2002) Canadian Tax Journal, Volume 50, No 3.

[40] Reuven Avi-Yonah & Zachee Tinhaga, "Unitary Taxation and International Tax Rules" (2014) ICTD Working Paper 26. In their paper, they argue that unitary taxation will be governed by article 7 of model treaties, ordinarily applicable to the treatment of permanent establishments. Li holds the view that formulary apportionment is applicable within the provision of article 9 of model treaties. In exact words: "A strong argument can be made that article 9 does not compel or plainly imply the required use of comparable pricing methodologies to the exclusion of formula-based methods. There is reported agreement among tax experts that the arm's length principle and formulary apportionment should not be viewed as polar extremes; rather, they should be viewed as part of a continuum of methods, ranging from CUP to predetermined formulas." See: Li, supra note 39.

The discussion on the allocation of income is a determination of the right to tax and how that right is exercised. Throughout the course of this thesis I shall refer to the exercise of countries' right to tax and the implications of that for income allocation. As a result, I discuss below some theories of taxation relevant to the right to tax.

3.1 Fiscal Sovereignty Theory

The fiscal sovereignty theory presupposes the unrestricted powers of a sovereign to impose tax on its subjects.[41] The power to tax its inhabitants and/or citizenry is central to the exercise of the sovereignty of a state.[42] It traditionally explains the power of the sovereign to fix its tax policies and protect its revenue streams, with no external interference. Hobbes "Leviathan" represents such a sovereign who is a revenue-maximizing ruler, not affected by electoral constraints or external influences.[43] This ruler exercises the power to tax and spend public finance, with no restraints. Brennan and Buchanan[44] recognized the possession of such power by a sovereign. They however propose the control of the leviathan through a fiscal constitution, which reflects the choices of the electorate. Whether a leviathan government exists in today's world and a country can exercise its fiscal sovereignty without interference or limitation remains controversial.[45]

First, preceding the power of a sovereign to tax its subjects is the political and economic allegiance of the governed to the state.[46] The political allegiance presupposes a contractual agreement between a state and its subjects, wherein

[41] The discussion here is limited to the tax component of fiscal sovereignty. See, Diane Ring, "What's at Stake in the Sovereignty Debate? International Tax and the Nation-State." (2008) Virginia Journal of International Law 49, at 55–234.
[42] For instance, the Nigerian constitution mandates all citizens to declare their income honestly to appropriate and lawful agencies and to pay their taxes promptly. See: The Constitution of the Federal Republic of Nigeria, C23, LFN 2004, s 24 (e).
[43] Thomas Hobbes, "Leviathan" Richard Tuck ed., (Cambridge: Cambridge University Press, 1996).
[44] Geoffrey Brennan & James Buchanan, "The Power to Tax: Analytical Foundations of a Fiscal Constitution" (2000) Library of Economics and Liberty.
[45] Jefferson VanderWolk, "A Look Ahead: A Multinational Prescription for Global Tax Policy" (2018) Tax Notes, 17.
[46] Allison Christians, "Sovereignty, Taxation and Social Contract" (2009) 18 Minn. J. Int'l L. 99.

the subjects give up some rights to the state, alongside the assumption of duties, for a collective re-ordering of their actions. Consent is at the foundation of such statehood, with reciprocal rights and duties. Where the state fails to perform its end of the bargain, the subjects withdraw their political allegiance and renege on their duties. This situation is characteristic of a failing or failed state, and manifests in African countries in the forms of military takeovers, secessionist movements and civil unrests.[47]

Historically, Nigeria witnessed civil unrest as far back as 1929 due to the imposition of taxes on a group of taxpayers. This is more remarkable given that the country was a colony of the British government. In 1929, in the Eastern part of Nigeria, Igbo market women opposed the imposition of special taxes on them, which they believed, threatened their livelihood.[48] The women participated in a protest march against the imposition of tax by the colonial masters through district chiefs.[49]

In recent times, citizens have risen to protest the unconscionable imposition of taxes by national or sub-national governments, and in some cases, succeeded in reversing the actions of the government in fiscal matters or influencing legislation. The ability of the citizens to protest, oppose, vote out and question the legitimacy of a government, demonstrate that the power of the sovereign to tax is not without limitations. Thus, while in theory, the idea of a fiscal sovereign will appear present, the reality speaks otherwise. Taxation— a tool to redress social, political, and economic grievances— remains a leading cause of uprising in any state, thus,

[47] Nigeria since gaining independence from the British in 1960 has experienced military rule for most of her independent years. The country till this day also battles with secessionist movements by parts of the country, especially the Igbo population.

[48] Islamic philosopher, Ibn Khaldun had argued that increased tax rate would lead to decreased tax revenue and a reduction to industrialization. See: Abdul Ghafar Ismail- Abu Bakar Jaafar, "Tax Rate and its Determinations: An Opinion from Ibn Khaldun" IRTI Working Paper Series, WP# 1435-01; Attiya Waris & Laila Abdul Latif, "Towards Establishing Fiscal Legitimacy Through Settled Fiscal Principles in Global Health Financing" (2015) Health Care Analysis 23(4), 376–390.

[49] Nina Mba, "Nigerian Women Mobilized: Women's Political Activity in Southern Nigeria (1900–1965)", (1982) University of California Institute of International Studies, Research Series, No. 48.

threatens the legitimacy of the sovereign where it is unjustly imposed.

In modern times, tax evasion and avoidance practices by MNEs headquartered in powerful countries, have replaced the colonial era exploitation of resources and wealth of African countries, ushering us into an era of neo-colonialism.[50] Tom Burgis aptly describes it:

> "The Looting of Africa's resources has witnessed shameless pillage during the colonial era, to more institutionalized robbery through the acts of supranational bodies, such as the World Bank and the IMF. In the tax space, the League of Nations and the OECD, contributed and still contribute to the plunder of the resources of African countries, through carefully-designed international tax system, which favours resident states, or better put, developed countries."[51]

A contribution to tax avoidance is the competitive nature of tax jurisdictions to attract FDI or act as conduit for MNEs to erode tax bases and shift profits. This tax competition is a major cause of uneven development among countries, wherein countries gain at the expense of other countries. International efforts at tax coordination and harmonization have been to ensure that weaker countries are not "recolonized" through tax planning, unhealthy tax competition and tax arbitrage. According to Christians, "every nation has an interest in sharing the gains they help create by participating in globalization".[52] Christians opines that "if governments fail to claim an adequate share of gains from international business and investment, they will be forced to look ever more intensely to sources of revenue that are less intentionally contested, namely payroll and consumption taxes."[53]

[50] Characterised by the use of economic, political and cultural pressures to control other countries especially weaker and dependent countries. Usually used to refer to the economic, political and cultural relationships between former colonial masters and their colonies.
[51] Tom Burgis, "The Looting Machine: Warlords, Tycoons, Smugglers, and the Systematic Theft of Africa's Wealth" (2016), New York, NY: PublicAffairs.
[52] Allison Christians, "How Nations Share" (2012) Indiana Law Journal, Vol 87. The paper analyzes the role of law in creating and resolving international tax disputes.
[53] Ibid.

This is the reality in many African countries where governments rely on increased use of indirect taxes and the arbitrary imposition of levies and fees on individuals in a bid to meet their revenue demands. These kinds of taxes are regressive and harm the poor, who already have to contend with bad infrastructure or inadequate public services. Shifting the tax burden to poor individuals goes against the ability to pay principle of taxation and the exchange theory of taxation, each of which is discussed below. Therefore, it is important that governments continuously work out an effective and fair way of sharing the gains they help create.

At the international level, the limitation of information, the conflicting interests of other states and the influences of supranational bodies, limit the fiscal sovereignty of a state. The rise and influence of supranational bodies in managing the fiscal sovereignty of states can be traced to the formulation and mandate of the International Chamber of Commerce (ICC) and subsequently, the League of Nations.[54] Without such supranational bodies, countries would engage in tax competition, unhindered. Countries are more connected in today's economy than they were in the 19th century and their domestic tax policies have far-reaching implications for others, thus attracting global attention, engagement and regulation. Wesley puts it thus:[55]

> "As the world slowly emerges from its worst recession in thirty years, it has become painfully evident that no nation-state rich or strong is insulated from the actions of its neighbors. Ours is a global economy. "Recessions, inflation, trade relations, monetary stability, gluts and scarcities of products and materials…are international phenomena" affecting all national participants. The realities of economic life push toward global

[54] Carroll supra note 17 at 473–498.
[55] Roger Wesley, "Problems in Regulating the Multinational Enterprise- An Overview" (1976), The International Lawyer, Vol 10, No 4, at 613–622.

> interdependence, discrediting in the process outgrown concepts of economic determinism."[56]

The implication of this is that a claim to fiscal sovereignty by states is fast being eroded.

The limitation of the fiscal sovereignty of a state and the rise of supranational bodies has developed into an interesting area of jurisprudence in recent times[57]. The OECD, gaining from the recognition of powerful countries of its importance and work, wields significant global influence on tax issues[58]. The need for cooperation on tax matters to achieve equitable environment has resulted in the increasing importance of the roles of the OECD in global tax discourse. For instance, most tax treaties and bilateral tax agreements (BTAs) between countries are based on the OECD MTC, alongside the commentaries, guidelines and prescriptions. As states accede to a global tax architecture, led by supranational bodies such as the OECD, one may argue that the world is observing the voluntary surrender of fiscal sovereignty of states.

The formation of the European Union supports the claim above. The decision of the European Court of Justice (ECJ) in relation to Apple's tax activities and liabilities in Ireland is a useful example of the erosion of fiscal sovereignty of individual states. In August 2016, the European Commission ruled that Ireland granted undue tax benefits (state aid) to Apple, to the value of €13 billion[59] ordering Apple to pay back this sum to the Irish government. The decision in this

---

[56] Important to note that the global impacts of recessions are attributable to the presence of MNEs abroad and the increase in FDI by firms.

[57] Christians, supra note 45 at 28; see also Ring, supra note 40 at 28.

[58] The OECD Model Tax Treaty, with commentaries, guidelines and prescriptions, largely influence tax agreements between countries and even internally. See: Kenneth Abbot and Duncan Snidal, "Hard and Soft Law in International Governance" (2000) in International Organization, Vol 54, No 3, Legalization and World Politics, at 421–456; Hugh Ault, "Reflections on the Role of the OECD in Developing International Tax Norms" (2009) Brooklyn Journal of International Law, Vol 34, Issue 3; Hugh Ault, "Some Reflections on the OECD and the Sources of International Tax Principles" (2013) Tax Notes International, Vol 70, No 12.

[59] Available online: <www.europa.eu/rapid/press-release_IP-16-2923_en.html.>

case is important for the discussion on fiscal sovereignty, as both the Irish government and Apple appealed the ruling, seeking to overturn the ECJ's decision.

This case highlights the growing influence of supranational bodies. This decision has led to legal, economic and political controversies, across the globe. One such controversy is the unhindered power of states to direct their fiscal affairs. Second, states, other than Ireland, have laid claim to the €13 billion, alleging that part of the profits should have been paid to them, on the basis of being home, in the case of the United States, and host countries in the case of other countries to where the significant economic activities of Apple take place. These controversies, while reflective of the advancing tax competition among countries, could lead to a more equitable international tax community, if well-managed. Borrowing the words of Wesley, economic and fiscal determinism are outgrown concepts, which must give way to global cooperation.

Prior to the Apple's case, the US had, arguably, encroached on the fiscal sovereignty of states through the enactment of the Foreign Account Tax Compliance Act (FATCA) of 2010.[60] FATCA requires financial institutions around the world to disclose to the Internal Revenue Service (IRS) large accounts of U.S. persons operating in their territories or with connections to their territories, or face a 30% withholding tax on the institution's earnings made in the US. This imposition of 30% withholding tax has forced financial institutions around the world, nearly 200,000, to agree to disclose to the IRS any large account of a U.S. client. Consequently, countries, following the U.S. FATCA, are setting up similar bank account disclosure systems with global reach. The U.S. FATCA reinforces the limitation of the claim to fiscal sovereignty of states, given that tax disclosures are generally confidential between the taxpayer and the revenue authority and can only be disclosed on the order of a court of law, in most jurisdictions.

[60] United States Internal Revenue Services, online, <https://www.irs.gov/businesses/corporations/foreign-account-tax-compliance-act-fatca.>

Furthermore, the growing involvement of investigative journalists in unearthing tax evasion and avoidance practices across the globe, with far-reaching political and economic implications for sovereign states, belies claim of fiscal sovereignty by states. The Panama Papers leaks of 2016,[61] by the International Consortium of Investigative Journalists (ICIJ) could be accused to have "violated" the fiscal sovereignty of states, by making public hitherto secret information of legal persons held and protected by tax jurisdictions. Notwithstanding the breach of fiscal sovereignty of states, the leaks have encouraged increased calls for a global action to address the revelations. The leaks have aided the recovery of stashed funds by governments.[62] In 2017 and 2018, data leaks on the tax avoidance practices of MNEs were released by the ICIJ in a set of publications known as the Paradise Papers.[63] [These developments (the Panama Papers and the Paradise Papers) weaken the powers of countries to exercise fiscal sovereignty without recourse to other jurisdictions. They, on the other hand, assist countries with the repatriation of stashed funds in other jurisdictions, which the countries lay claims to.

3.2 Ability to Pay Principle

This principle stipulates that the contribution of a taxpayer to the revenue purse should be determined by the relative resources of the taxpayer. Thus, the greater

---

[61] Took 370 journalists working in 25 languages digging into 11.5 million documents to reveal Mossack Fonseca's inner workings, tracing the secret dealings of the firm's clients, revealing the use of shell companies by the rich for fraud, tax evasion, money laundering, amongst many other lawful or unlawful purposes.

[62] International Consortium of Investigative Journalists, "Panama Papers Helps Recover More than $1.2 Billion Around the World" (2019), available online: <https://www.icij.org/investigations/panama-papers/panama-papers-helps-recover-more-than-1-2-billion-around-the-world/.>

[63] Publications by the award-winning International Consortium of Investigative Journalists (ICIJ), focused on revealing the tax avoidance and evasion practices of companies. Details on the activities and publications can be found online at: <https://www.icij.org/.> The author advises the International Consortium of Investigative Journalists on the tax avoidance practices of multinational entities in Africa. See: "Tax Haven Mauritius' Rise Comes at the Rest of Africa's Expense" (2017), online:<https://www.icij.org/investigations/paradise-papers/tax-haven-mauritius-africa/>; "Africa's Satellite Avoided Millions Using a Very African Tax Scheme" (2018), available online at: <https://www.icij.org/investigations/paradise-papers/africas-satellite-avoided-millions-using-african-tax-scheme/.>

one's ability to pay, the higher the tax that should be imposed on the taxpayer. Adam Smith is credited with popularizing this principle.

Smith, writing in The Wealth of nations (1776) claimed:

> "Such things as defending the country and maintaining the institutions of good government are of general benefit to the public. Thus, it is reasonable that the population should contribute to the tax costs. It is reasonable to demand certain other things of a tax system- for example, that the amounts of tax individuals pay should bear some relationship to their abilities to pay…Good taxes meet four major criteria. They are (1) proportionate to incomes or abilities to pay; (2) certain rather than arbitrary; (3) payable at times and in ways convenient to the taxpayers and (4) cheap to administer and collect."[64]

To Smith, a state achieves fairness by taxing its residents on their ability to pay. Utz, on his part, claims that there is a broad, if not universal agreement that fair taxation should be in accordance with the ability to pay, or the capacity of the taxpayer to bear the tax burden.[65] Under this principle, the burden of tax is relative to the wealth of the taxpayer, in fixing the tax payable.[66] This principle justifies the use of proportional or progressive tax by jurisdictions and has been argued to be a fair apportion of taxing liabilities.

This ability to pay theory of taxation was the starting premise of the work of the League of Nations in arriving at the division of taxing rights for countries caught within the global tax community almost a century ago. The academic experts of the League of Nations had considered the ability to pay, or the faculty theory, as superior to earlier theories of taxation for the global community.[67] They held the

[64] Adam Smith, "An Inquiry into the Nature and Causes of the Wealth of Nations (1776) Edwin Cannan, ed., Methuen & Co (1925) at 310.

[65] Stephen Utz, "Ability to Pay" (2002) Faculty Articles and Papers, 133.

[66] Edwin Seligman, "The Theory of Progressive Taxation", Political Science Quarterly, Vol 8, No 2 (1893), at 220–251.

[67] Lindsay Celestin, "The Formulary Approach to the Taxation of Transactional Corporations: A

view that the “modern tax system is based on the ability to pay, which therefore favoured taxation by the country of residence”.[68]

This may be the right position almost a century ago when one recalls that many of the source states during the 1920s negotiations were colonies under the control of their imperial masters, possessing no independent revenue. However, the ability to pay principle was not adopted by the participating countries during the negotiations. Picciotto has argued that the economists acknowledged that considerations of pure theory might have to yield to the practical needs of national budgets[69]. Notwithstanding the colonial relationship which existed at that time between source and residence states, it was important that source states could tax income to meet their developmental needs, leading to the abandonment of the ability to pay principle for the economic allegiance theory, which I shall discuss later.

The ability to pay principle faces limitations in its applicability at an international level. There is yet to be consensus on the definition of “fair share’ and no scale to guide tax authorities in ascertaining what one’s ability is and what a fair return will represent.[70]

Second, discussion on fair share of tax operates largely at the national level[71], though recently, the phrase has been used in cross-border transactions.[72] It is

---

Realistic Alternative?” (2000) PhD Dissertation (Unpublished work) University of Sydney, online: <https://ses.library.usyd.edu.au/bitstream/2123/846/1/adt-NU20020917.13313801front.pdf.>

[68] Sol Picciotto, “International Business Taxation: A Study in the Internationalization of Business Regulation” (1992) London: Weidenfeld and Nicholson, at 19.

[69] Ibid.

[70] Nancy Kaufman, “Fairness and the Taxation of International Income” (1998) Law and Policy in International Business, Vol 29, No 145.

[71] The ability to pay theory is enshrined in the constitutions of some taxing jurisdictions, thereby giving it constitutional power. For instance, article 64 and 19 of the constitutions of Algeria and Equatorial Guinea, respectively, provide that taxes should be paid by everyone, in accordance with his contributory capacity or according to his revenues. See the February 2017 edition of the International Tax Review, online: (<www.internationaltaxreview.com >)- “Constitutions: Could Paying a ‘Fair Share’ of Tax Already be Enshrined in Law?” (2017) online publication: <https://www.internationaltaxreview.com/Article/3656591/Constitutions-Could-paying-a-fair-share-of-tax-already-be-enshrined-in-law.html?ArticleId=3656591.>

[72] Kaufman, supra note 70.

limited to the payment of tax, and not to the determination of taxing rights, therefore, works on the assumption that the taxing right must have been determined. Just as important as the amount of tax paid, is the jurisdiction to tax. Many disputes which arise from cross-border economic activities are as a result of the determination of the right to tax, prior to determining the amount of tax.

Notwithstanding its limitations, the "Ability to Pay" principle provides useful basis for demanding that MNEs pay increased taxes in host states and re-echoes the growing demands of governments and civil societies that MNEs pay a "fair share" of their taxes.

3.3 The Cost and Benefit Theory

Smith is credited as the proponent of the cost and benefit theories of taxation (jointly described as the exchange theory). He had in establishing the ability to pay principle of tax taxation, stated that, "…such things as defending the country and maintaining the institutions of good government are of general benefit to the public. Thus, it is reasonable that the population should contribute to the tax costs…"[73]. Smith acknowledged the contribution of the state to the accumulation of wealth by taxpayers, and the obligation on the part of taxpayers to pay, proportional to their liability to the state.[74] He assumed that the state's actions of defending the country and maintaining good institutions benefit the public, and beneficiaries of such public infrastructure and services must share in the cost of providing for them.

The exchange theory of taxation advocates the imposition of tax liabilities based on the advantages derived by the taxpayers and the cost to the government for providing the benefits enjoyed by taxpayers. Seligman described this as "premiums of insurance which individuals pay to the collective insurance

[73]Adam, supra note 64 at 310.
[74] Ibid.

company- the state- to enjoy their possession in peace and security".[75] As such, a man with large wealth could be adjudged to have benefited more from the state, and is expected to contribute a higher premium, reflecting benefit obtained.

The second assumption is that the greater the reliance of one on the infrastructure of a state, the higher the tax liabilities of such a person. This divides the cost of infrastructure provided by the state among beneficiaries of the infrastructure, based on use. Such tangible and intangible infrastructure, or better still the social and economic infrastructure of a country, creates the enabling environment for wealth creation, and as such must be maintained by taxpayers.

The exchange theory has influenced the imposition of taxation for centuries and is believed to be integral to the social contract theory. It is in this regard that it is limited. Taxation is premised on territorial connection, which may be based on residence or world-wide taxation jurisdiction emanating from citizenship. For example, the United States of America exercises a world-wide taxation on its citizens, notwithstanding the residence of the citizens, though it grants unilateral reliefs to mitigate double taxation. Nigeria, on the other hand, taxes based on residence, denying itself taxing jurisdiction over Nigerians outside the state.[76]

In respect of MNEs, while some jurisdictions possess express provisions mandating all foreign companies doing businesses in the jurisdiction to be incorporated, thus not recognizing the use of branches, other jurisdictions permit both branches and subsidiaries of foreign companies to engage in business activities in their jurisdictions. The implication of this, from a theoretical perspective is that countries with the incorporation-only rule possess no jurisdiction over non-incorporated companies, if one were to rely on the social contract theory. This is because no statehood or status is conferred on the foreign company, and as such, no reciprocal duty is owed to the state.

[75] Seligman, supra note 66.
[76] The Personal Income Tax Act, P8, 2004, s 2.

For countries which permit both subsidiaries and branches of foreign companies to carry out business activities in their jurisdictions, a reciprocal duty or claim can be placed or made on such companies in return for the status conferred on them. This is an important limitation of the exchange theory as MNEs may argue that, in the absence of physical presence in the state or absence of any conferment of status, they benefit nothing from a state and should not be required to contribute to the cost of the infrastructure.

One way of addressing this feature of the exchange theory has been through tax treaties. Using the permanent establishment (PE) rules in the OECD and UN model tax treaties, MNEs could be tax liable to states even in the absence of any legal status. For example, article 7 (1) of the OECD MTC provides:

> "profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits that are attributable to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other state."[77]

The implication of this provision is this: profits of a corporation are only taxable in the home state, except where the corporation carries on business in the host state through a PE.

A PE is defined in article 5 of the OECD MTC as: "a fixed place of business through which the business of an enterprise is wholly or partly carried on."[78] This includes: a place of management; a branch; an office; a factory; a workshop; a mine, an oil or gas well, a quarry or any other place of extraction of natural resources; and a

[77] OECD, "2017 Model Tax Convention on Income and Capital" (2017), 7th ed., Paris, online: <https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#.>

[78] Ibid, article 5. Article 5 of the Model Convention covers what would constitute a permanent establishment.

building site or construction or installation project if it lasts more than twelve months.

Article 7 (4) of the OECD MTC exempts the following from being classified as PEs: facilities used solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise; maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery; maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character; and maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs (a) to (e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

While both the OECD and UN model treaties would appear to grant taxing rights to host states, in the absence of conferment of status on branches of MNEs by the home state, the excluded items in article 7 (4) create gaps as they fail to adequately allocate income to taxing jurisdictions. The OECD recognizes this limitation and has set out, in its BEPS Project, to recommend changes to the allocation of taxing rights among states. These recommendations seek to extend more taxing rights to host states, thereby expanding the benefit theory of taxation. However, as presently constituted, the exchange theory of taxation is unsuitable for international tax law, as it is territorial and vulnerable to manipulation by tax planners.

3.4 Economic Allegiance Theory

The League of Nations, having narrowed down the issue to the conflicting interests between source and residence states, and realizing the importance of allocating taxing rights to both states, adopted the economic allegiance theory as the theoretical foundation for allocating taxing rights between source and residence states. Before advancing, I hold that the economic allegiance theory is relevant today as it was in the 1920s. However, it must be applied in conjunction with other important theories to achieve a just allocation of income. These other theories are considered in other chapters of this thesis.

The theory of "economic allegiance" credited to Georg Von Schnaz, measures the relationship between a taxing state and the income being taxed. It requires beneficiaries of states to pay taxes to the states wherein they obtain significant benefits.[79] The economic allegiance theory recognizes the rights of resident and source states to tax. The exercise of such right and the quantum of profits to be taxed, provide the core of the conflict. Per Schnaz, a resident owed significant responsibility and allegiance to the territory, in which it carried out business or obtained value, as compensation for the resources, infrastructure, protection and domicile benefitted from the territory.

According to Celestin, Schanz posited that economic allegiance to a state could be based on either consumption, or business activities, including investments. Where based on consumption, taxing jurisdiction should go to the residence state; and where based on economic activities, then both states possess taxing jurisdictions.[80] Therefore, revenue should be shared between both states based on the benefits derived from each taxing jurisdiction or the contribution of the taxing jurisdiction to the generation of the total revenue.[81]

Applying the economic allegiance theory, the League of Nations was of the opinion that it was only after the analysis of the constituent elements of the economic allegiance theory that they would be able to determine where a person ought to be

[79] Klaus Vogel, "Worldwide vs Source Taxation of Income- A Review and Re-evaluation of Arguments" (1988) Intertax No 8–9.
[80] Celestin supra note 67.
[81] Schanz believed that the primary right to tax should accrue to the state where income is produced. He attributed three-fourths of the revenue to that state, and the remaining one-fourth for the residence state where the foreign income would be consumed. See: Celestin, supra note 66.

taxed or how the division ought to be made as between the various sovereignties that imposed tax.[82] It identified the factors to be considered in the implementation of the economic allegiance theory as:[83] the origin of wealth or income; the situs of wealth or income; the enforcement of the rights to wealth or income; and place of residence or domicile of the person entitled to dispose of the wealth or income. These factors were to guide the election of a method of allocating taxing rights.

Arriving at a method of allocating the taxing rights in line with the economic allegiance theory posed a higher challenge[84]. The Economists identified four possible approaches to the allocation of taxing rights:

Option 1: country of residence would concede all taxing rights to the source state;
Option 2: country of source would concede exclusive taxing jurisdiction to the residence state;
Option 3: proportional allocation of income between the countries of residence and source; or
Option 4: classification of income and an assignment of the primary right to tax such income to the country of residence or source depending on the type of income.

According to Picciotto,[85] option 1 was to concede priority to the source state, while retaining residual rights for the country of residence. The residence state was to give tax credit to its residents on taxes paid to the source state. Option 2 granted priority to the residence state, with source state granting exemption to income derived from its territory, and residence state exercising exclusive jurisdiction to tax the income.[86] The third option, formulary apportionment, consolidates the income made in both the residence and source states and apportions the income to

[82] League of Nations (1923), at 4024
[83] Edwin Seligman is credited as joint proponent of the "Economic Allegiance" theory in his report as a member of the Group of Economists appointed by the League of Nations to study and address the issue of double taxation.
[84] According to Picciotto, "The report therefore accepted that agreement on the allocation of jurisdiction to tax could not be reached on the basis of any simple general principle." See, Picciotto, supra note 68, at 19.
[85] Picciotto, supra note 68.
[86] It must be pointed out that this was the preferred method by most capital exporting countries as it gave them exclusive taxing rights over the profits of MNEs.

both jurisdictions on the basis of contributions from each state or economic activities taking place in each jurisdiction.[87]The fourth option, classification and assignment, which was adopted by the League of Nations, classified income into categories, assigning taxing jurisdiction based on the classification. This classification and assignment approach is the foundation of the existing model treaties. This political compromise represents, at best, an arbitrary decision by the League of Nations.

Having relied on Schanz's economic allegiance theory, which provided that revenue should be apportioned according to contribution, recommending a 75:25 sharing formula between source and residence states, it is difficult to appreciate the election of the classification and assignment approach by the League of Nations. The accurate election should have been option 3 (proportional allocation of income) as recommended by Schanz in his economic allegiance theory.

Therefore, this thesis argues that the economic allegiance theory, though established in 1892, is still relevant in today's discussion of the allocation of income among countries engaged in cross-border business activities.[88] This is even more important, since the increased use of foreign direct investments by MNEs, today's integrated global economy and the importance of global value chains in production and generation of global profits. This theory will guide the appreciation of the right to tax and the quantum of tax. It supports the goal of aligning where profit is taxed with where the economic activities occur. It supports the application of pre-determined formula in the apportionment of global profits of MNEs to the constituent tax jurisdictions.

---

[87] This approach is strongly advocated for today and the EU is in the process of adopting it as the mode of allocation of income in the EU through its Common Consolidated Corporate Tax Base (CCCTB).

[88] LI, supra note 39; see: Jinyan Li, "Tax Sovereignty and International Tax Reform: The Author's Response" (2004) Canadian Tax Journal Vol 52, No 1. Li argues that the beginning of the 21st century, with an increasingly global economy, offers a golden opportunity to re-evaluate and reform the international tax system, which is largely a creature of the industrial age at the beginning of the 20th century. She insists that the theoretical foundations of the international tax system (that is the economic allegiance theory and the benefit theory) remain valid and should be given their original intent and state.

Conclusion

This chapter commenced with a discussion on the mischief the thesis seeks to address. I have discussed some relevant theories of taxation, which would inform the rest of thesis in terms of the discussion on taxing rights and the allocation of income. In the next chapter, I shall discuss the two principles of income allocation of profits of corporate groups responsible largely for the tax avoidance practices of MNEs.

Chapter 2: Tax Avoidance and Enablers of Tax Avoidance in Africa

1. Introduction
    1.1 Executive Summary of the Chapter
    1.2 Objectives of the Chapter
    1.3 Outline of the Chapter

2. Tax Avoidance: Facts, Numbers and Myths

3. Addressing the Separate Entity Principle
    3.1 The Separate Entity Principle
    3.2 The Salomon vs Salomon case
    3.3 Piercing the Corporate Veil
        3.3.1 Fraud
        3.3.2 Agency
        3.3.3 Tax evasion
        3.3.4 Single Economic Unit Theory

4. Arm's Length Principle,

    4.1 Description of the Arm's Length Principle
    4.2 The Limitations of the Arm's Length Principle

5. Transfer Pricing
    5.1 Legal Construction of Transfer Pricing
    5.2 Application of Transfer Pricing
    5.3 Challenges of Transfer Pricing Methodologies
    5.4 Linkage between Transfer Pricing and Tax Avoidance

1. Introduction

a. Executive Summary of the Chapter

This chapter engages in the discussion of tax avoidance, the causes and the effects in numbers. It discusses the two principles behind the allocation of income of MNEs, viz: the separate entity principle and the arm's length principle. In discussing the two principles, the chapter highlights the rationale behind them and their limitations in today's global economy. The chapter proceeds to discuss transfer mispricing and its connection with tax avoidance.

The chapter argues that the separate entity treatment of companies enshrined in company's law and practice of tax jurisdictions and the global tax architecture should be abandoned in the tax law treatment of MNEs. It argues that the arm's length principle has failed in its bid to allocate income among tax jurisdictions in a just and effective manner.

b. Objectives of the Chapter

The objective of this chapter is to unpack the legal principles, which inform the current allocation of profit approach. By discussing the principles of separate entity treatment and the arm's length principle, I prepare the ground to advocate for a shift from the current global standard to the unitary approach.

c. Outline of the Chapter

This chapter continues as follows. Section 2 of the chapter discusses tax avoidance, the controversies around its definition, the examples of tax avoidance and the scope of tax avoidance. Section 3 of the chapter discusses the separate entity principle. Here, I make a case that while the treatment of companies as separate from their shareholders is an important part of our legal jurisprudence, legal instruments and judicial decisions provide grounds for departing from such treatment. I argue that such ground for piercing the corporate veil should be extended to the treatment of MNEs and their related entities. Section 4 of the chapter discusses the arm's length principle, its substantive and procedural limitations. The result of the adoption of both the separate entity and arm's length principles is the establishment of transfer pricing rules and practice. Section 5 of the thesis discusses transfer pricing, transfer mispricing and the connection with tax avoidance.

2. Tax Avoidance: Facts, Numbers and Myths

As explained in chapter 1, the need for an international tax system arose out of the complaints of firms engaged in international trade, whose profits were being subjected to double taxation. This economic double taxation[89] occurred both in the host (source) state and the home (residence) state. The deliberations culminated in the draft of model tax treaties, which are to be used in the negotiation of bilateral treaties by interested parties.

At the time of the treaty discussions and draft of the first model tax treaties, international investment by firms were mainly in the form of portfolio investments, which were either through debt or equity participation. The firms were not actively engaged in the management of their portfolio investments. The model treaties reflected this business model with the source countries given the primary right to tax active income (business profits), while the residence state taxed primarily passive returns on investment (interest, dividends).[90]

[89] The taxation of same income in the hands of two different taxpayers, in this case, a parent company and its subsidiary or two related entities of a parent company.
[90] Ke Chin Wang, "International Double Taxation of Income: Relief Through International Agreement 1921−1945" (1945) Harvard Law Review, Vol 59, No 1, at 73−116; Donald Brean,& Richard Bird, "The Interjurisdictional Allocation of Income and the Unitary Tax debate" (1986) Canadian Tax Journal, Vol 34, 1377; Robert Green, "The Future of Source-Based Taxation of the Income of Multinational Enterprises" (1993) Cornell Law Faculty Publications. Paper 952.

Given that firms did not actively participate in the management of their portfolio investments abroad, it was common sense to treat foreign affiliates and or PEs of firms as separate from the parent company and other subsidiaries and branches. Where they (the parent and subsidiaries) transacted with each other, they were expected to act as independent entities would, or what is known as the arm's length principle. The independent entity principle extended to the preparation of accounts as each unit of the multinational group accounted for its transactions. These principles of independent entity and arm's length treatment became part of the model treaties drafted by the League of Nations and later adopted by the OECD. These principles can be found in article 7 (covers branches or permanent establishments) and article 9 (covers subsidiaries) of the OECD MTC.

Article 9 (1) of the OECD MTC enclosing both principles is reproduced here:

> "Where
>
> a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or
> b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State.
>
> and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprises and taxed accordingly."[91]

The substance of the article 9 of the OECD MTC is to treat related companies as independent entities, while returning a party to the position it would have been if

[91] OECD MTC, supra note 1 article 9.

transactions were negotiated on market terms or at arm's length. The implications of this provision and the contribution towards tax avoidance are discussed in this section and other parts of the thesis.

Tax avoidance represents the activities of taxpayers to underpay or fail to pay taxes due, by carefully planning their tax affairs to take advantage of grey areas in the law or regulations. Steenkamp characterises tax avoidance "by open and full disclosure, where a taxpayer has arranged affairs in a perfectly legal manner so that he has either reduced his income or has no income on which tax is payable".[92] Diaz-Berrio, offering a more expansive definition, defines tax avoidance as, "although legal, involves the abusive exploitation of loopholes in national and international laws that allows multinational corporations (hereinafter MNCs) to shift profits from country to country, often to or through tax havens with the intention of reducing the amount of taxes they pay".[93]

Oguttu sees tax avoidance by MNEs, as the use of gaps in the "interaction between different tax systems to reduce taxable income artificially or shift profits to low-tax jurisdictions in which little or no economic activity is performed".[94] She views it as the use of legal methods to arrange one's affairs in order to pay less tax. This, according to Oguttu, is achieved by "using loopholes in tax laws and exploiting them within legal parameters".[95]

One common attribute of tax avoidance activities is that they have over the decades been treated as completely legal, though in the eyes of some, immoral and

---

[92] Lee-Ann Steenkamp, "Combating Impermissible Tax Avoidance through Efficient Administrative Approaches: What SARS can Learn from its Canadian Counterpart" (2012) The Comparative and International Law Journal of Southern Africa, Vol 45, No 2, at 227−257.
[93] José Luis Escario Díaz-Berrio, "The Fight against Tax Havens and Tax Evasion: Progress since the London G20 Summit and the Challenges Ahead" (2011) Documento de Trabajo 59.
[94] Annet Wanyana Oguttu, "Tax Base Erosion and Profit Shifting in Africa-What Should Africa's Response be to the OECD BEPS Action Plan? - Part 1" (2015) The Comparative and International Law Journal of Southern Africa, Vol 48, No 3, at 516−553.
[95] Ibid.

left to the conscience of the facilitators.[96] The legality of these activities distinguishes them from other activities which come under tax evasion, such as fraudulent declarations or intentional act of non-declaration of tax returns. These tax avoidance activities encompass taking advantage of ambiguity in tax provisions and exploiting the gaps. Their legal acceptance, enshrined in the statement of Lord Tomlin in Inland Revenue Commissioners ("IRC") v Duke of Westminster ("The Duke of Westminster Doctrine")[97], to wit: "Every man is entitled, if he can, to order his affairs so as that the tax attaching under the appropriate acts is less than it otherwise would be…" has come under severe criticism and departed from in some recent court decisions.

In England, in the case of W.T. Ramsay Ltd. V. IRC,[98] clearly departing from the Duke of Westminster Doctrine, the House of Lords decided that, "…while the techniques of tax avoidance progress and are technically improved, the courts are not obliged to stand still." The court held that to "force the courts to adopt, in relation to closely integrated situations, a step by step, dissecting approach which the parties themselves may have negated, would be a denial rather than an affirmation of the true judicial process…" This approach by the English court was recently followed in the Tanzanian case of African Barrick Gold Plc[99] by the tax appeal tribunal.

In recent literature, the term, "base erosion and profit shifting" (BEPS) has been used by supranational bodies, academics, experts and stakeholders to describe the tax avoidance activities of MNEs. This can be seen in the current BEPS Project of the OECD, which seeks to address the tax avoidance activities of multinational entities. I shall, in line with recent literature, use base erosion and profit shifting,

---

[96] Helia Ebrahimi, "Starbucks, Amazon and Google Accused of Being 'Immoral'" (2012) The Telegraph: online:<https://www.telegraph.co.uk/finance/personalfinance/tax/9673358/Starbucks-Amazon-and-Google-accused-of-being-immoral.html>
[97] Inland Revenue Commissioners ("IRC") v Duke of Westminster (1935) All ER 259 (H.L).
[98] WT Ramsay Ltd. v Inland Revenue Commissioners (1981) All ER 865 (H.L).
[99] African Barrick Gold Plc vs Commissioner General, Tanzania Revenue Authority [2013] Tax Appeal No 16 of 2015.

and its acronym BEPS, and tax avoidance interchangeably. In the next section, I illustrate how tax avoidance occurs and its scope.

Examples of Tax Avoidance.

Tax avoidance occurs through the use of complex structures by MNEs, which take advantage of gaps in domestic laws and international rules to shift, place, hide or situate profit across different jurisdictions.

For example, a Canadian company (Parentco A) may seek to invest in Nigeria. The company law of Nigeria demands that every foreign company which seeks to do business in Nigeria must incorporate a company, thereby eliminating the use of PEs by foreign companies.[100] As such, Parentco A incorporates a subsidiary in Nigeria (Subco B) through which it carries on business in Nigeria. To provide capital to Subco B, Parentco A may decide to provide equity or loan financing or a combination of both. In most cases, a mixture of both debt and equity is used. The return for equity capital is dividend, and subsequent repatriation of the equity through share sale or other repatriation measures as provided by the laws of the host country. The return for loan is periodic interest payment, and subsequent repayment of the loan.

The next step for Parentco A is to determine the ratio of debt to equity in the capital provision to Subco B. This is an important decision to make by Parentco A, since in most taxing jurisdictions, interest paid on loan is deductible from the gross profit of companies before taxation. A base erosion and profit shifting mechanism that can be adopted by the taxpayer will be to over-capitalize Subco B through debt, while equity takes a small portion of the capital.[101] From experience, companies go as high as a 20:1 debt to equity capitalisation of companies. By over-

[100] The Companies and Allied Matters Act of Nigeria, 2004, C 20, s 54.
[101] Over-capitalisation of capital through debt is a phenomenon where investors elect to capitalize a company using significant more debt than equity.

capitalizing Subco B, Parentco A A strips the earnings of Subco B, through interest deductible earnings.

Take the case of Nigeria. The required minimum share capital for a Nigerian private company is Ten Thousand Naira (₦10,000, approximately USD 30) and Five Hundred Thousand Naira (₦500,000, approximately USD 1500) for a public company formed by Nigerians. For a company with a foreign shareholder, covering multinational entities, the minimum share capital is Ten Million Naira (₦10,000,000, approximately USD 30,000). Given that Nigeria has no thin capitalization rules and in the absence of specific industry requirements or standards like those provided for in the banking and insurance sectors, Parentco A is legally permitted to capitalize Subco B with as much debt as it desires. Its only restraint may come from the exercise of the administrative powers of the tax authority to recharacterize transactions it deems artificial or fictitious. It must be stated here that companies do not always set out to avoid taxes when they capitalize their subsidiaries. In some cases, the capital requirement for the industry demands that they deploy more debt capital than equity capital.

This power of recharacterization of transactions of related companies is not common practice in Nigeria, for a number of reasons. First, the country is focused on attracting investments and desires to be seen as not interfering in the business decisions of private persons. Second, some sectors such as the resource sector demand very costly equipment and high liquidity, which may not be readily available to investors, hence, the desire to borrow from financial institutions. Third, the country is reputed to be a high-risk investment destination and as such investors tend to share the risks with others and secure their investments by demanding collateral from the companies. The reasons given may inform the election of more debt capitalization than equity capitalization by the parent companies of subsidiaries located in offshore jurisdictions. The company may over-capitalize subsidiaries as a way of out-stripping profits from the tax jurisdiction through interest deductions thereby reducing the taxable profit in the tax jurisdiction.

The subject of thin capitalization is not the focus of this thesis and shall not be discussed. The focus on this thesis is transfer mispricing, which is discussed next.

A second potential example of tax avoidance from the scenario above is the rate of interest charged on the loan from Parentco A to Subco B. Parentco A may decide to fix an interest rate of 30% while the market rate may be 15-20%. However, for countries with transfer pricing rules, this rate (30% fixed by Parentco) may be challenged by the tax authority as not being an arm's length rate. As will be shown in later discussion, implementing the transfer pricing rules to transactions between related entities is a complex, resource-intensive, difficult and often ineffective exercise.[102] The international tax system, which treats entities in a corporate group as separate entities requiring them to act as independent entities would, fails at is foundation and implementation. We shall return to this later and analyze how such a system has created the opportunity for tax avoidance practices by MNEs.

Returning to the general discussion of tax avoidance, the tax avoidance practices of multinational entities are not limited to the two examples discussed above (use of thin capitalization and transfer mispricing to erode tax bases and shift profits). To fully appreciate the scope of tax avoidance, the OECD BEPS Project is instructive. The OECD BEPS Project consists of 15 action plans by the OECD to combat tax avoidance activities of MNEs. Many of the action plans highlight the potential tax avoidance practices of MNEs.[103]

Action 1 addresses BEPS issues arising from the digital activities of taxpayer (digital economy).[104] Action 2 seeks to address the effects of hybrid mismatch arrangements. Hybrid mismatch arrangements, according to the OECD, are cross-

---

[102] OECD, supra 76.
[103] OECD (2015), Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[104] OECD (2015), Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report, OECD/G20Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

border arrangements that take advantage of differences in the tax treatment of financial instruments, asset transfers and entities to achieve double non-taxation or long-term deferral outcomes which may not have been intended by either country.[105] Action 3 addresses activities of parent companies with controlling interest in a foreign low-taxed subsidiary by shifting income to the low-taxed subsidiary to avoid taxation, through strengthening controlled foreign companies' rules.[106] Action 4 of the BEPS Project addresses base erosion via interest deductions and other financial payments.[107]

Action 5 of the BEPS Project addresses the harmful tax practices of taxpayers by requiring substantial activities for any preferential regimes and improved transparency, including compulsory exchange of information on certain tax rulings.[108] Action 6 addresses the abuse of treaties, through treaty shopping by taxpayers, and insists on countries including minimum standards in negotiated treaties.[109] These minimum standards include a "limitation-on-benefits" rule, a "principal purpose test" rule, and a preamble inserted in tax treaties, expressly stating that states that enter into a tax treaty intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including treaty shopping. Action 7 addresses BEPS by preventing the artificial avoidance of permanent establishment status.[110] Actions 8-10 of the BEPS Project are to ensure that transfer pricing outcomes are aligned with the

---

[105] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[106] OECD (2015), Designing Effective Controlled Foreign Company Rules, Action 3 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[107] OECD (2015), Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 -2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[108] OECD (2015), Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[109] OECD (2015), Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[110] OECD (2015), Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

value creation of the MNE group.[111] Action 11 of the BEPS Project addresses BEPS by establishing methodologies to collect and analyse data on BEPS and the actions to address it.[112] Action 12 requires taxpayers to disclose their aggressive tax planning arrangements.[113] Action 13 re-examines transfer pricing documentation.[114] Action 14 recommends making dispute resolution mechanisms more effective.[115] Action 15 takes a bold step in achieving global support and consensus for the BEPS Action Plans by developing a multilateral instrument to implement the recommendations.[116]

What the scenario and the OECD BEPS Project reveal is the extent of tax avoidance activities that arise from the international tax system, which treats entities in a corporate group as separate entities for tax purpose, demanding from them to act as independent entities would. However, the focus of this thesis is the tax avoidance activities of taxpayers, through transfer (mis)pricing. In the next two sections, I discuss the two relevant principles which cause and encourage transfer mis(pricing): the separate entity principle and the arm's length principle.

3. Addressing the Separate Entity Principle

a. The Separate Entity Principle

At the time the League of Nations embarked on its mission to avoid the double taxation of related entities, it discovered that majority of the countries studied

[111] OECD (2015), Aligning Transfer Pricing Outcomes with Value Creation, Actions 8–10 - 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[112] OECD (2015), Measuring and Monitoring BEPS, Action 11 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[113] OECD (2015), Mandatory Disclosure Rules, Action 12 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[114] OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[115] OECD (2015), Making Dispute Resolution Mechanisms More Effective, Action 14 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[116] OECD (2015), Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 -2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris

already treated subsidiary companies as separate legal personalities from their shareholders or parent companies. Adopting same approach for the treatment of firms was a reasonable decision at the time.

Such treatment of companies was enshrined, prior to the works of the League of Nations, in the Companies Act of 1862 of the United Kingdom, which had statutorily provided for the limited liability of companies formed by a group of people. Section 6 of UK Companies Act of 1862 expressly stated that: "Any seven or more persons associated for any lawful purpose may, by subscribing their names to a memorandum of association, and otherwise complying with the requisitions of this Act in respect of registration, form an incorporated company, with or without limited liability."[117] This provision granted corporate status to the company formed by a group of persons, separate and distinct from the individuals who comprised it.

Section 7 of the UK Companies Act, 1862, provided that, "The liability of the members of a company formed under this Act may, according to the memorandum of association, be limited either to the amount, if any, unpaid on the shares respectively held by them, or to such amount as the members may respectively undertake by the memorandum of association to contribute to the assets of the company in the event of its being wound up".[118] This granted the status of limited liability to the company, that in the event of liquidation of the company, the liability of its shareholders will be limited to the unpaid value of shares held by the shareholders.

This statutory enactment was given judicial support in the English case of Salomon v Salomon.[119] The application of this principle of independent entity to corporate groups was established in the Albazero case,[120] where the court held

[117] The Companies Act of England 1862, s 6.
[118] The Companies Act of England 1862., s 7.
[119] Aron Salomon (Pauper) Appellant v A. Salomon and Company Limited, Respondents [1897] A.C.22.
[120] Albacruz (Cargo Owners) v Albazero 'The Albazero' [1977] AC 774.

that, "…each company in a group of companies…is a separate legal entity possessed of separate legal rights and liabilities." [121]

Thus, the common law of England enshrined the corporate legal personality in its law. This (the separate entity treatment) was and remains the practice in common law countries, as well as civil law countries. Below, I discuss the case of Salomon v Salomon.

a. The Salomon vs. Salomon Case

In this case, a trader sold his solvent business to a UK limited company, whose shares were held by the trader, his wife, daughter and four sons, in compliance with the provisions of the UK Companies Act, 1862.[122] The trader was issued a floating security in part payment of the purchase-money debentures. The trader was issued twenty thousand shares, paid for out of the purchase-money. His 20,000 shares gave the vendor the power to outvote the other six shareholders, who held a share each. The trader was appointed managing director of the incorporated company. When the company was wound up, the trader redeemed his debentures from the company, leaving the company with insufficient funds to pay the ordinary creditors. In an action brought before the court to treat the company as one and the same with his majority shareholder, Aaron Salomon, the court of first instance held that:

> "…the proceedings were not contrary to the true intent and meaning of the Companies Act 1862; that the company was duly formed and registered and was not the mere 'alias' or agent of or trustee for the vendor; that he was not liable to indemnify the company against the creditors' claims; that there was no fraud upon creditors or shareholders; and that the company (or the

[121] Albacruz (Cargo Owners) v Albazero 'The Albazero' [1977] AC 774

[122] The Companies Act, 1862, had required that a memorandum of association of a company be signed by at least seven persons, who are to take a share each at least.

> liquidator suing in the name of the company) was not entitled to rescission of the contract for purchase."[123]

On appeal to the House of Lords, the House of Lords ruled that:

> "It is not contrary to the true intent and meaning of the Companies Act 1862[124] for a trader, in order to limit his liability and obtain the preference of a debenture-holder over other creditors, to sell his business to a limited company consisting only of himself and six members of his own family, the business being then solvent, all the terms of sale being known to and approved by the shareholders, and all the requirements of the Act being complied with."[125]

On the question of the separate entity treatment of a company from its shareholders, Lord Halsbury held:

> "My Lords, the important question in this case, I am not certain it is not the only question, is whether the respondent company was a company at all-whether in truth that artificial creation of the Legislature had been validly constituted in this instance; and in order to determine that question it is necessary to look at what the statute itself has determined in that respect."[126]

Lord Halsbury advanced to hold that short of proof of fraud in the incorporation of the company, it is impossible to dispute that once the company is legally incorporated, it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in

---

[123] Aron Salomon (Pauper) v. A. Salomon and Company Limited [1897] AC 22, at 23.
[124] The Companies Act, 1862, is the progenitor of the UK Companies Act of 2006.
[125] Lee v Lee's Air Farming Ltd [1961] AC 12, where the Court held that a wife was entitled to compensation under the Worker's Compensation legislation against the defendant company for death of her husband, though her late husband was a controlling shareholder of the defendant company and the directing mind of the company.
[126] Salomon, supra note 125 at 29.

the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are.[127]

The effect of the Salomon case was to create a veil of incorporation over the company, separating the company from its shareholders. It protected the shareholders of the company from liabilities incurred by the company[128]. The shareholders of the company may be natural persons or corporate persons and are protected from the liabilities of incorporated companies[129]. This protection extends to related entities in corporate groups, and each entity is treated as a separate legal corporate personality from its shareholders and parent company. Thus, parent or holding companies are not liable for the debts of subsidiaries and subsidiaries are not liable for the debt of other subsidiaries or the parent companies; neither is either held responsible for the acts or omission of the other party.

The decision in Salomon v Salomon applies outside the UK and has been given statutory backing in other jurisdictions. This is the case in Nigeria, a former colony of the UK, with the common law of England still part of its laws. For instance, section 18 of the Companies and Allied Matters Act (CAMA) of Nigeria, provides:

> "…any two or more persons may form and incorporate a company by complying with the requirements of this Act in respect of registration of such company."[130]

Section 37 of the CAMA states the effect of incorporation of a company thus:

---

[127] Ibid.
[128] For historical and conceptual analyses of the principle of corporate legal personality, see the following: Arthur Machen, "Corporate Personality" (1911) Harvard Law Review, Vol 24, No 4; John Dewey, "The Historic Background of Corporate Legal Personality", (1926), Yale Law Review, Vol 35, No 6.
[129] See the ruling of Roskill LJ in The Albazero [1977] AC 774, where the learned judge held: "…each company in a group of companies…is a separate legal entity possessed of separate legal rights and liabilities."
[130] The Companies and Allied Matters Act (CAMA), C20, 2004, s 18.

"As from the date of incorporation mentioned in the certificate of incorporation, the subscriber of the memorandum together with such other persons as may, from time to time, become members of the company, shall be a body corporate by the name in the memorandum, capable forthwith of exercising all the powers and functions of an incorporated company including the power to hold land, and having perpetual succession and a common seal, but with such liability on the part of the members to contribute to the assets of the company in the event of its being wound up as is mentioned in this Act."[131]

The Nigerian court ruled in African Continental Bank Plc., v. Emostrade Limited[132] that, what needed to be proven to establish the juristic personality of the plaintiff was whether there was evidence that it was duly incorporated. Where this is proven through the production of a certification of incorporation, the company shall be given the full benefits of incorporation. This decision, the Nigerian court reinforced in FDB Financial Services Ltd. V Adesoza where it held:[133]

"The consequence of recognizing the separate personality of a company is to draw a veil of incorporation over the Company. One is therefore generally not entitled to go behind or lift his veil. However, since a statute will not be allowed to be used as an excuse to justify illegality or fraud it is a quest to avoid the normal consequences of the statute which may result in grave injustice that the Court as occasion demands have to look behind or pierce the corporate veil."[134]

This veil of incorporation or separation of a company from its founders is the practice in civil law countries. For instance, article 301 of the Quebec Civil Code

[131] The Companies and Allied Matters Act (CAMA), C20, 2004, s 37.
[132] [2002] 8 NWLR part 770 at 501.
[133](2002) 8 NWLR (Pt 668) 170 at 173. See: Adeyemi v Lan & Baker (Nigeria) Ltd. (2002) 7 NWLR (663) 33 at 51.
[134] Ibid.

grants full enjoyment of civil rights to legal persons. Article 303 of the Quebec Civil Code advances to provide that, "Legal persons have capacity to exercise all their rights, and the provisions of this Code concerning the exercise of civil rights by natural persons are applicable to them, adapted as required. They have no incapacities other than those which may result from their nature or from an express provision of law."[135] Article 315 of the Quebec Civil Code states that "The members of a legal person are bound towards the legal person for anything they have promised to contribute to it, unless otherwise provided by law."[136] These provisions are similar to the provisions in the companies' laws of the UK and Nigeria.

The treatment of entities in a corporate group as separate and independent from each other remains controversial, as argued in other parts of this thesis. Experts have called for multinational corporations to be taxed as single and unified firms, arguing that the existing tax treatment of multinational corporations where they are treated as separate entities and taxed as such, enable the corporations "to shift their profits and revenue between subsidiaries to benefit from lower taxes in certain nations, such as Ireland and Luxembourg".[137] They argue that from the economic and business perspectives, multinational corporations operate as integrated firms, though tax law treats them as separate and independent entities. The European Union reckons that the treatment of multinational corporations as separate entities is the underlying problem of the international tax system today. In its position paper on unitary taxation, it opines:

> "The underlying problem in the international tax system today is that the legal entities of multinational corporations are treated as 'separate entities'

---

135 See: Article 303 of the Civil Code of Quebec. Chapter CCQ-1991 (Updated 2019), online: <http://legisquebec.gouv.qc.ca/en/pdf/cs/CCQ-1991.pdf>

136 This provision limits the liability of shareholders of a company to the shares subscribed for in the company and their liabilities do not extend to their personal property.

137 Joseph Stiglitz, "The Global Tax System is Broken" (2015), online: <https://money.cnn.com/2015/06/02/news/economy/global-tax-system-stiglitz/index.html> Joseph Stiglitz, "How Can we Tax the Footloose Multinationals" (2019), online: <https://www.theguardian.com/business/2019/feb/14/how-can-we-tax-the-footloose-multinationals>

for the purposes of taxation. By treating the entities of multinational corporations as separate for the purposes of taxation, firms are able to allocate profits around the world to jurisdictions which allow them to minimise their tax liabilities to governments. The idea of allowing a group of companies under common control to be treated as separate tax-paying entities has created incentives for firms to route profits from high-tax to low-tax jurisdictions.

Multinational firms achieve profit-shifting in two primary ways. Firstly, by setting up subsidiaries in low-tax jurisdictions and attributing profits to these. Secondly, by adjusting the prices of transfers between the entities of a multinational firm, thereby shifting profits from high-tax to low-tax jurisdictions. The consequence of the 'separate entity' approach to taxation means that companies are able to play one country off against another, and that the way firms are taxed bear little to no relation to where a firm's economic activity actually takes place."[138]

How can corporate groups be treated as unitary firms? Below in this section, the instances where the veil of corporation may be pierced, and the corporate group treated as a unified firm are considered.

b. Piercing the Corporate Veil

Though courts appear determined to uphold the sanctity of the corporate legal personality, the veil of incorporation may be pierced in limited circumstances, to hold the parent company or shareholders of the company liable for the liabilities of the company. Piercing the corporate veil implies disregarding the separate personality of the company, treating the company as one and the same as its shareholders- a single or unitary firm. This is provided for in both the legislative

[138]European Union, "Position Paper on Unitary Taxation – A Sustainable Tax Model for the 21st Century", European Union.

enactments of some taxing jurisdictions and recognised by judicial decisions in most countries across the world.

Under the civil law, the Code expressly provides instances where the veil of incorporation may be pierced. For instance, article 316 of the Quebec Civil Code provides that, in case of fraud, with regard to the legal person, the court may, on the application of an interested person, hold the founders, directors, other senior officers or members of the legal person who have participated in the alleged act or derived personal profit therefrom liable, to the extent it indicates, for any injury suffered by the legal person.[139] Article 317 provides that, "The juridical personality of a legal person may not be invoked against a person in good faith so as to dissemble fraud, abuse of right or contravention of a rule of public order".[140]

Under the common law, the courts have been more active in piercing the corporate veil. Lord Denning, M.R. cautioned in the case of Littlewoods Stores Ltd. V I.B.C.[141] that:

> "The doctrine laid down in Salomon's case has to be watched very carefully. It has been supposed to cast a veil over the personality of a limited liability company through which the Court cannot see. But that is not true. The Court can, and often does, draw aside the veil. They can and often do pull down the mask. They look to see what really lies behind."

Pulling down the mask was exactly what the court did in the case of Jones v. Lipman.[142] In this case, the defendant who had agreed with the plaintiff to transfer his land to the plaintiff in a sale agreement intended to not honour the agreement by incorporating a company and transferring ownership of the land to the company. In a case of specific performance brought against the defendant, the

[139] Article 316 of the Quebec Civil Code, Chapter CCQ-1991 (Updated 2019), online: <http://legisquebec.gouv.qc.ca/en/pdf/cs/CCQ-1991.pdf>
[140] See: Article 317 of the Quebec Civil Code, Chapter CCQ-1991 (Updated 2019). Online: <http://legisquebec.gouv.qc.ca/en/pdf/cs/CCQ-1991.pdf>
[141] [1969] 1 WLR 1241.
[142] [1962] 1 WLR 832.

defendant, relying on Salomon v Salomon claimed that he was unable to perform the contract since the ownership of the subject transferred to the company, a separate and distinct body from its shareholders. Russell J, ordering the specific performance of the agreement, held: "…the defendant company is the creature of the first defendant, a device and a sham, a mask which he holds before his face in an attempt to avoid recognition by the eye of equity."

Below, I discuss the instances where courts may pierce the veil of incorporation as are contained in statutes and judicial decisions.

i. Fraud

One instance where the corporate veil has been pierced is where the corporate legal personality has been used to perpetrate fraud or for fraudulent purposes. Denning LJ in Lazarus Estates Ltd. V Beasley held that:[143]

> "No court in this land will allow a person to keep an advantage which he has obtained by fraud. No judgment of a court, no order of a Minister, can be allowed to stand if it has been obtained by fraud. Fraud unravels everything. The court is careful not to find fraud unless it is distinctly pleaded and proved; but once it is proved, it vitiates judgments, contracts and all transactions whatsoever…"[144]

This reasoning (where fraud vitiates the veil of incorporation) has been given judicial support by Nigerian courts. In a recent decision by the apex court of Nigeria, the Supreme Court of Nigeria, the court reinforced fraud as an exception to the principle of corporate personality. In Mezu v CB (Nig) Limited,[145] the Supreme Court held that the appellant, Mezu and its incorporated company, Mezu International Ltd., were one and the same and the appellant was hiding behind

[143] [1956] 1 QB 702.
[144] Ibid at 712.
[145][2013] 3 NWLR (pt 1340) 188.

the guise of the existence of a limited liability company to perpetrate fraud on unassuming persons. In recounting Lord Justice Russell statement in Jones v Lipman,[146] the Supreme Court held that the incorporated company was "a devise and a sham, a mask which he holds before his face in an attempt to avoid recognition by the eyes of equity".[147]

Applying the exception of fraud in tax avoidance practices remains a tricky one. The global consensus is that tax avoidance is not illegal, but an immoral act, though there is strong case for tax avoidance to be considered an illicit practice.[148] The implication of this (tax avoidance as illicit practice) is yet to be determined, though illicit grants it a stronger status in terms of being a ground for piercing the corporate veil.

Notwithstanding the treatment of tax avoidance as permissible, though frowned upon, it is difficult to accept that the complex structures deployed by multinational entities to shift profits and erode bases, are not intended to wilfully defraud taxing jurisdictions revenue owed them. This is another case where law lags behind economic reality. Snyder writing from a U.S. perspective and on the development in the financial industry, elaborates this conflict between law and economic reality:

> "The landscape of the world's financial markets has changed dramatically over the past several years. Advances in communications and computer technologies, innovations in financial products, and changes in the regulatory scheme have empowered the world's financial institutions to conduct their trading activities around the globe, twenty-four hours a day. Tax laws and regulations, however, have not kept pace with the globalization of trading practices. Traditional U.S. tax regimes based on geographic identifications have become inadequate to tax these operations,

[146][1962] 1 WLR 832.
[147] Mezu v CB (Nig) Limited [2013] 3 NWLR, PT 1340, 188.
[148] In chapter 5, I engage in the definition of the word, "illicit" and its relationship with tax avoidance.

given that the development of global computerized trading activities has diminished the ability to associate products or transactions with specific geographic locations."[149]

Snyder's claims are as valid for other sectors of the economy and are not limited to the United States. There is an obvious conflict between law and economic reality, which demands a global approach.

ii. Agency

Another instance where the veil of corporate legal personality may be pierced is where the court establishes agency.[150] Agency arises where the facts show that the company is and acts as the agent of the shareholder. Legally, directors and managers of a company are the agents of the company, with powers to bind the company.[151] Denning L.J in Bolton (Engineering) Co. Ltd v Graham and Sons succinctly described the company law practice when he said:

> "A company may in many ways be likened to a human body. It has a brain and nerve centre, which controls what it does. It also has hands, which hold the tools and act in accordance with direction from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the Company and control what it does…"[152]

[149] Andrew Snyder, "Taxation of Global Trading Operations: Use of Advance Pricing Agreements and Profit-Split Methodology" (1995) The Tax Lawyer, Vol 48, No 4, at 1957−1073; See: Michael Graetz & Rachael Doud, "Technological Innovation, international competition, and the Challenges of International Income Taxation" (2013) Columbia Law Review, Vol 113.
[150] Adams v Cape Industries [1990] CH 433.
[151] This act of agency is provided for under civil law. Article 311 of the Quebec Civil Code provides that, "Legal persons act through their organs, such as the board of directors and the general meeting of the members." Article 312 of the Quebec Civil Code provides that, "A legal person is represented by its senior officers, who bind it to the extent of the powers vested in them by law, the constituting act or the by-laws."
[152] Bolton (Engineering) Co. Ltd v Graham [1957] 1 QB 159.

Viscount Haldane L.C., aptly described this relationship when he held in Lennards Carrying Co. v Asiatic Petroleum Ltd:

> "A Corporation is an abstraction, it has no mind of its own any more than it has a body of its own; its active and directive will must consequently be sought in the person of somebody who for some purposes may be called an agent but who is really the directing mind and will of the corporation, the very ego and centre of personality of the Corporation."[153]

This principle of agency is enshrined in statute. For instance, section 63 of the CAMA, provides that:

> "(1) A company shall act through its members in general meeting or its board of directors or through officers or agents, appointed by, or under authority derived from the members in general meeting or the board of directors.
>
> (2) Subject to the provisions of this Act, the respective powers of the members in general meeting and the board of directors shall be determined by the company's articles.
>
> (3) Except as otherwise provided in the company's articles, the business of the company shall be managed by the board of directors who may exercise all such powers of the company as are not by this Act or the articles required to be exercised by the members in general meeting."

Thus, both statutes and judicial decisions recognize that a company is represented by its directors and decisions taken on the company's behalf by its directors, for the sole benefit of the company, bind the company. These directors of the company may be shareholders of the company, a situation the law recognizes and

[153] Lennard's Carrying Co. v Asiatic Petroleum Ltd [1915] AC 705.

guarantees. However, where the company acts as agent of a shareholder or shareholders in ways to benefit the interest of the shareholder(s), the law makes provisions for piercing the veil of corporate legal personality, treating the company and its shareholders as one and the same.

For instance, section 315 of the CAMA which empowers the Corporate Affairs Commission (CAC)[154] to appoint one or more competent inspectors, acting upon the order of a court of law, to investigate the affairs of a company and report on them in such manner as it directs, if the court declares that its affairs ought to be so investigated, empowers the Commission to extend its investigation to related entities of the company being investigated. In exercise of the mandate to investigate the affairs of a company, the investigators may pierce the corporate veil. This is provided for in section 316 of the CAMA to the effect that:

> "(1) If an inspector appointed under section 314 or 315 of this Act to investigate the affairs of a company thinks it necessary for the purposes of his investigation to investigate also the affairs of another body corporate which is or at any relevant time has been the company's subsidiary or holding company, or a subsidiary of its holding company or a holding company of its subsidiary, he shall report on the affairs of the other body corporate so far as he thinks that the results of his investigation of its affairs are relevant to the investigation of the affairs of the company first mentioned above."[155]

In conclusion, statutory provisions and judicial interpretations deny the separate legal personality of a company, treating it as one with its shareholders where agency is established. However, it is a question of facts whether a company is acting as agent for its shareholder. The manipulative tax structures used by multinational entities reveal the use of companies as agents and for the benefit of the shareholders.

---

[154] This is the body responsible for the regulation of companies in Nigeria.
[155] Company and Allied Matters Act, c-20, s 316.

iii. Tax evasion

Courts have shown willingness to pierce the corporate veil, where there is proof of tax evasion by the corporate entity. In England, in the case of Apthorpe v Peter Schoenhofen Brewery Co LTD, the shares of a New York company were held by an English company.[156] The Court of Appeal held that the business of the New York Company was that of the English company and therefore subjected to the English income tax and the device was to evade taxes which the court must not allow.

In Uganda, the case of Commissioner General, Uganda Revenue Authority v. Zain International BV is instructive of the willingness of some courts to pierce the corporate veil where the corporate structure is considered to have been deployed to evade tax.[157] In this case, Zain International BV, which held 100 per cent of the shares in Zain Africa BV, sold all of its shares in Zain Africa BV to BhartiAirtel International. All three companies engaged in the sale of the shares were resident in the Netherlands as at the time of the transaction.

Zain Africa BV, the subject of the sale agreement, held 100 per cent shareholding in Celtel Uganda Holdings BV which owned 99.99 per cent of shares of Celtel Uganda Limited. This sale did not include the direct transfer of the shares held in Celtel Uganda Ltd, nor the transfer of the physical assets of Celtel Uganda Ltd. The Uganda Revenue Authority, however, raised an assessment for capital gains tax for the transfer of the shares held by Zain International BV in Zain Africa to BhartiAirtel International. The claim of the revenue authority was that the transaction was an indirect transfer of the assets of Celtel Uganda Ltd and as such should be subject to capital gains tax.

[156] [1899] 80 LT 395.
[157] [2014] UGCA 120.

In 2014, the Court of Appeal of Uganda ruled that the Uganda Revenue Authority had the jurisdiction to tax the gains arising from a transaction between two non-resident companies, where the transaction involves the sale or transfer of assets in Uganda, whether directly or indirectly. The Uganda Revenue Authority had argued that the transaction was to evade the payment of taxes in Uganda. This decision reversed an earlier decision by the High Court of Uganda, which held that the Uganda Revenue Authority had no jurisdiction to impose capital gains tax on a transaction between two non-resident entities. The precedent set by the appellate court in its decision is to pierce the veil of incorporation allowed the Uganda Revenue Authority to go after the parent company and controlling shareholder of a company resident in Uganda. This caused the parent company and controlling shareholder to be liable for the debts of its subsidiary.[158]

I foresee that courts in Africa, in the near future, will go the way of the Ugandan court in the interpretation of tax transactions, especially among related entities. It is expected that other African countries will expand the definition of tax evasion and blur the demarcating line between tax evasion and tax avoidance.[159]

iv. Single Economic Unit Theory

Proceeding from the agency exception of the separate entity principle, is the single economic unit theory or group enterprise theory exception. This theory proceeds from the assumption that in certain circumstances a corporate group acts in such a way that members of the group are indistinguishable, and it is only proper to treat the corporate group as a unitary firm, effectively, piercing the corporate veil.[160] In these circumstances, the parent companies are liable for the acts of their subsidiaries.

---

[158] See the judgment in the Indian case of, Vodafone International Holdings v Union of India & Anor [2012] 6 SCC 613.

[159] Going by the judgment in the African Barrick Gold case, it would appear that the court disregarded the distinction between tax evasion and avoidance and treated both as same. See, Commissioner General, Tanzania Revenue Authority, supra note 99.

[160] John Matheson, "The Modern Law of Corporate Groups" An Empirical Study of Piercing the Corporate veil in the Parent-Subsidiary Context" (2009) North Carolina Law Review, Vol 87, at1091–1155.

The case for the corporate group to be treated as a single entity is stronger where the corporate group shares the services of directors, officers, employees or there exists a strong partnership relationship among the entities in a corporate group. Other factors to consider are ownership, decision-making autonomy, assumption of risks, etc. The court in the Australian case of Bluecorp Pty Ltd (in liquidation) v ANZ Executors and Trustee Co. Ltd.[161], remarked that:

> "The inter-relationship of the corporate entities here, the obvious influence of the control extending from the top of the corporate structure and the extent to which the companies were thought to be participating in a common enterprise with mutual advantages perceived in the various steps taken and plans implemented, all influence the overall picture."

In the English case of DHN Food Distributors Ltd v. London Borough of Tower Hamlets,[162] the parent company of a subsidiary company had brought a case before the court, asking that the veil of incorporation be pierced in a land compensation matter. Lord Denning, quoting Gower, opined that "there is evidence of a general tendency to ignore the separate legal entities of various companies within a group and to look instead at the economic entity of the whole group".[163] Lord Denning opined that:

> "This is especially the case when a parent company owns all the shares of the subsidiaries- so much so that it can control every movement of the subsidiaries. These subsidiaries are bound hand and foot to the parent company and must do just what the parent company says…This group is virtually the same as a partnership in which all the three companies are partners. They should not be treated separately so as to be defeated on a technical point…The three companies should, for present purpose, be

[161] [1995] QCA 487.
[162] [1976] 1 WLR 852.
[163] DHN Food Distributors Ltd v. London Borough of Tower Hamlets [1976] 1 WLR 852.

treated as one, and the parent company D.H.N. should be treated as that one."[164]

Goff LJ, concurring with Denning LJ remarked:

> "I wish to safeguard myself by saying that so far as this ground is concerned, I am relying on the facts of this particular case. I would not at this juncture accept that in every case where one has group of companies, one is entitled to pierce the veil, but in this case the two subsidiaries were both wholly owned; they had no separate business operations whatsoever…"[165]

Both Denning LJ and Goff LJ in their judgments relied on the earlier case of Harold Holdsworth& Co (Wakefield) Ltd v Caddies.[166] In that case, Lord Reid had remarked:

> "It was argued that the subsidiary companies were separate legal entities each under the control of its own board of directors, that in law the board of directors of the appellant company could not assign any duties to anyone in relation to the management of the subsidiary companies and that therefore the agreement cannot be construed as entitling them to assign any such duties to the respondent.
>
> My Lords, in my judgment this is too technical an argument. This is an agreement in re mercatoria and it must be construed in light of the facts and realities of the situation. The appellant company owned the whole share capital of British Textile Manufacturing Co. Ltd., and under the agreement of 947 the directors of this company were to be the nominees of the appellants. So, in fact, the appellants could control the internal management of their subsidiary companies, and, in the unlikely event of

[164] Ibid at 861.
[165] Ibid at 862.
[166] [1955] 1 WLR 352.

> there being any difficulty, it was only necessary to go through formal procedure in order to make the decision of the appellants' board fully effective."[167]

However, the principle established in both the decisions in DHN Food Distributors Ltd v. London Borough of Tower Hamlets and Harold Holdsworth& Co (Wakefield) Ltd v Caddies, were overruled by subsequent English decisions in Woolfson v Strathclyde Regional Council,[168] and Adams v Cape Industries Plc.[169], reinstating the corporate legal personality treatment of companies.

In a 2013 case, Prest v Petrodel Resources Ltd, the English Supreme Court ruled on the doctrine of piercing the corporate veil.[170] The court restated that piercing the corporate veil could only be done in limited situations. Such situations were limited to: evasion of existing legal responsibilities; fraud; abuse of corporate legal personality to evade the law or to frustrate the enforcement of the law. This is the present position of the UK courts on when the veil of incorporation may be pierced.

Notwithstanding the court's decision in Prest v Petrodel, the decisions in both cases of DHN Food Distributors and Harold Holdsworth remain instructive and persuasive in arguing for the unitary treatment of corporate groups. Outside the United Kingdom, courts are more favorable to the single economic unit principle.

In India, the Supreme Court of India would appear to uphold the single economic unit treatment of corporate groups. In the case of Vodafone International Holdings v Union of India & Anor, the Supreme Court of India ruled that: [171]

> "…if an actual controlling Non-Resident Enterprise (NRE) makes an indirect transfer through 'abuse of organisation form/legal form and without

[167] Harold Holdsworth & Co (Wakefield) Ltd v Caddies [1955] 1 WLR 352.
[168][1978] UKHL 5. A House of Lords decision.
[169] Cape Industries supra note 149. Arnold, supra note 22
[170] [2013] UKSC 34.
[171] [2012] 6 SCC 613.

> reasonable business purpose' which results in tax avoidance or avoidance of withholding tax, then the Revenue may disregard the form of the arrangement or the impugned action through use of Non-Resident Holding Company, re-characterize the equity transfer according to its economic substance and impose the tax on actual controlling Non-Resident Enterprise."[172]

In this case, Vodafone International Holdings BV, resident in the Netherlands, sought to acquire 100% shares in CGP Investments (Holdings) Ltd, a company resident in the Cayman Islands, which held shares in Hutchison Essar Limited, a company resident in India. The acquisition of shares of CGP Investments (Holdings) Ltd would ultimately result in the acquisition of controlling shares in the Indian company by the company resident in Netherlands. The Indian tax authority sought to tax capital gains on the transaction. The Supreme Court of India, per Kapadia, held:

> "…In the application of a judicial anti-avoidance rule, the Revenue may invoke the 'substance over form' principle or 'piercing the corporate veil' test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant. To give an example, if a structure is used for circular trading or round tripping or to pay bribes then such transactions, though having a legal form, should be discarded by applying the test of fiscal nullity. Similarly, in a case where the Revenue Authority finds that in a Holding Structure, an entity which has no commercial/business substance has been interposed only to avoid tax then in such cases, applying the test of fiscal nullity it would be open to the Revenue Authority to discard such inter-positioning of that entity."[173]

[172] Union of India & Anor, supra note 157.
[173] Ibid.

Australia provides conflicting jurisprudence. On one hand, there exists strong judicial reluctance to treat corporate groups as single entities. In the Australian case of Industrial Equity Ltd v Blackburn, the High Court ruling on whether a parent company could order its subsidiary to declare and pay dividend out of its profits held that:[174]

> "It has been said that the rigours of the doctrine enunciated by Salomon v Salomon and Co. Ltd, have been alleviated by the modern requirements as to consolidated or group accounts…But the purpose of these requirements is to ensure that members of, and for that matter persons dealing with a holding company are provided with accurate information as to the profit or loss and the state of affairs of that company and its subsidiary companies within the group… However, it can scarcely be contended that the provisions of the Act operate to deny the separate legal personality of each company in a group. Thus, in the absence of contract creating some additional right, the creditors of Company A, a subsidiary company within a group, can look only to the company for payment of their debts. They cannot look to company B, the holding company, for payment."[175]

True, the mere presence of control over subsidiaries should not be reason enough to treat them as single entities. However, where there is evidence that there is concert for the benefit of the parent company, or that the subsidiary acts as agent of the parent company to achieve the set expectations of the parent company, then the parent company and its subsidiary should be treated as a single firm. Deciding otherwise results in a divergence between the "realities of commercial life and the applicable law".[176] This reasoning was followed in another Australian case.

[174] [1977] 137 CLR 567.
[175] Ibid at 577.
[176] Rogers CJ's dictum in Qintex Australia Finance Ltd v Schroders Australia Ltd [1990] 3 ACSR 267.

Succinctly putting it, Rogers CJ had held in the Australian case of Qintex Australia Finance Ltd v Schroders Australia Ltd thus:[177]

> "As I see it, there is today a tension between the realities of commercial life and the applicable law in circumstances such as those in this case. In the everyday rush and bustle of commercial life in the last decade it was seldom that participants to transactions involving conglomerates with a large number of subsidiaries paused to consider which of the subsidiaries should become the contracting party. A graphic example of such an attitude appears in the evidence of Ms. Ferreira, a dealer in the treasury operations department of the defendant. In her written statement…she said: 'In my discussions with either Craig Pratt or Paul Lewis when I confirmed deals undertaken for Qintex, it was not my practice to ask which of the Qintex companies was responsible for the deal. I always treated the client as Qintex and did not differentiate between companies in the group. Paul Lewis and Craig Pratt always talked as being from Qintex without reference to any specific company.'…
>
> It may be desirable for parliament to consider whether this distinction between the law and commercial practice should be maintained. This is especially the case today when the many collapses of conglomerates occasion many disputes. Regularly, liquidators of subsidiaries, or of the holding company, come to court to argue as to which of their charges bears the liability… As well, creditors of failed companies encounter difficulty when they have to select from among the moving targets the company with which they consider they concluded a contract. The result has been unproductive expenditure on legal costs, a reduction in the amount available to creditors, a windfall for some, and an unfair loss to others. Fairness or equity seems to have little role to play."[178]

[177] [1990] 3 ACSR 267.
[178] Ibid.

This treatment of related entities of a corporate group as single firms is also found in other areas of the law. For instance, under EU Competition Law, the European Court of Justice upholds the treatment of related entities as single economic unit, where it is established that from an economic point of view, the companies are in concert.[179] In the Viho Europe BV case,[180] the ECJ ruled that Parker and its subsidiaries formed a single economic unit, where the subsidiaries did not enjoy real autonomy in determining their course of action in the market but acted on the orders of Parker. In this case, Parker held 100 per cent shares of its subsidiaries in Germany, Belgium, Spain, France and the Netherlands and had established an area team which directed the sales and marketing activities of the subsidiaries, controlling sale targets, gross margins, sales costs, cash flows and stocks. This central team laid down the range of products to be sold, monitored advertising and issued directives concerning prices and discounts.

This recognition and treatment of corporate groups as single and unified entities is recognised in the tax law and practice of some taxing jurisdictions, through their Controlled Foreign Company rules (CFC rules).[181]

A controlled foreign corporation (CFC) is a company resident in a country other than that of its parent company or relevant controller. These CFCs ordinarily should pay returns on investments to the parent companies, in the forms of dividends, interests or capital gains. However, controlling companies could defer the repatriation of income to shift profits or evade taxes, payable in the tax jurisdiction of the parent company or controlling company. Similarly, the subsidiaries could refuse to distribute dividends or defer payment to the shareholders or parent companies.

---

[179] Carsten Koenig, "Comparing Parent Company Liability in EU and US Competition Law" (2018) World Competition Law: Law and Economics Review, Vol 41, No 1, at 69–100. The author states that it is a well-established principle of EU Competition Law that parent companies can be fined for antitrust infringements of subsidiaries.
[180] ECJ Case C-73/95 Viho Europe BV v Commissioner of the European Communities (24 October 1996) paras 15, 16 & 17.
[181] Wells & Lowell attribute the adoption of CFC rules by countries to the need to safeguard the domestic tax base, as a result of the creation of holding companies by multinationals in tax favorable jurisdictions. See: Wells, supra note 27.

To prevent the shift of profits abroad or the non-repatriation of taxable profits back to the taxing jurisdiction of the parent company or controlling company, some tax jurisdictions enact CFC rules.[182] These CFC rules are enacted by tax jurisdictions to limit or prevent the artificial deferral of tax in other countries, by taxing certain forms of income earned by foreign controlled companies as if distributed to shareholders.[183] These CFC rules differ for tax jurisdictions, with the common attribute of taxing non-distributed passive income to the controlling company as though distributed.[184]

For example, in Sweden, resident companies, individuals and non-resident companies with PEs in Sweden are subject to the CFC rules where they have control over or maintain a holding in a foreign legal entity.[185] The Swedish CFC rules prescribe a minimum of 25% holding of the capital or voting rights in the foreign legal entity by a Swedish resident company, either alone or together with persons of interest to the shareholder, for the CFC rules to apply. In the UK, a company resident outside the UK, with 25 per cent or more of its shares held by UK resident companies or individuals will be caught under the CFC rules.[186] In the United States,[187] the CFC rules apply to a foreign corporation where more than

---

[182] UN Practical Manual on Transfer Pricing for Developing Countries, (New York: United Nations 2017), at B.1.7.7.
[183] Ibid.
[184] Durst, supra note 30; Graetz, supra note 148.
[185] EY, "Swedish Ministry of Finance Proposes Amendments to CFC Legislation" (2018) EY Global Tax Alert Library, online: <https://www.ey.com/Publication/vwLUAssets/Swedish_Ministry_of_Finance_proposes_amendments_to_CFC_legislation/$FILE/2018G_01616-181Gbl_Sweden%20proposes%20amendments%20to%20CFC%20legislation.pdf> Markus Pettersson, "The Compatibility of Swedish CFC Legislation with Article 43 EC: A Case Study of an Advance Ruling" (2006) Master's Thesis (Unpublished) J ÖNK Ö P ING INT E RNA T I ONA L B U S INE S S S CHO O L: JÖNKÖPING UNIVERSITY.
[186] HM Revenue & Customs, "Controlled Foreign Companies Regime", online: <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/179249/controlled_foreign_companies.pdf.pdf> EY, "UK Takes Steps to Implement EU Anti-Tax Avoidance Directive" (2018) EY Global Tax Alert Library, online: <https://www.ey.com/Publication/vwLUAssets/UK_takes_steps_to_implement_EU_Anti-Tax_Avoidance_Directive/$FILE/2018G_010206-18Gbl_UK%20takes%20steps%20to%20implement%20EU%20ATAD.pdf>
[187] Sol Picciotto, "Towards Unitary Taxation of Transnational Corporations", (2012). Online Publication of Tax Justice Network, online: <https://www.taxjustice.net/cms/upload/pdf/Towards_Unitary_Taxation_1-1.pdf>

50 per cent or more of its shares in value or voting rights is owned by US shareholders.[188]

Canada, on her part, enacted the Foreign Accrual Property Income (FAPI) rules, which empowers the Canada Revenue Authority to apply the article of the law that tax the passive income of a controlled foreign company of a Canadian resident company. The Income Tax Act of Canada defines a "foreign affiliate" of a taxpayer resident in Canada as a non-resident corporation in which, at that time: the taxpayer's equity percentage is not less than 1%; and the total of the equity percentages in the corporation of the taxpayer and each person related to the payer…is not less than 10%."[189] In South Africa[190], if a South African company holds more than 50% of the shares or voting rights of a controlled foreign corporation, CFC rules are applicable. [191]

What CFC rules achieve in effect is to disregard the corporate legal personality of companies and tax the parent company or controlling company on the undeclared or unremitted profits retained by its subsidiary, as though distributed. CFC rules generally impute the net income of the CFC to its parent or controlling shareholder in proportion to the number of shares or voting rights held in the CFC.[192] This is generally achieved via statutory provisions aimed at piercing the corporate veil for tax purposes.[193] Durst, supporting the adoptions of CFC rules by countries, argues

---

[188] Section 957 of Subpart F. The new US CFC Rules provide that if a foreign parent company has 100% shares in a US subsidiary and a 100% share in a foreign subsidiary, the US subsidiary is under the new rules considered to own 100% of the foreign subsidiary, thereby creating a CFC.
[189] The Income Tax Act, RSC 1985, c. 1 (5TH Supp.),s 94 as amended; Yaroslavna Nosikova, "The FAPI Regime and CFC Rules under the BEPS Action Plan 3" (2015) Canadian Tax Foundation, online:
<https://www.google.ca/url?sa=t&rct=j&q=&esrc=s&source=web&cd=12&cad=rja&uact=8&ved=2ahUKEwj1h6WM5bThAhWNtlkKHYzaAVE4ChAWMAF6BAgAEAI&url=https%3A%2F%2Fwww.ctf.ca%2Fctfweb%2FCMDownload.aspx%3FContentKey%3D6c2a7d46-e452-4ad6-9bb7-184ae6527661%26ContentItemKey%3D2b6b0276-4050-46a5-9478-4e8ae56f9b10&usg=AOvVaw1CiJEytzbKS4uOCV5gtxJV>
[190] Nigeria has no controlled foreign company rules.
[191] The Income Tax Act, No 58 of 1962, s 9 (d).
[192] OECD (2015), Designing Effective Controlled Foreign Company Rules, Action 3 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. The Report in Ch. 6 (rules for attributing income) states that the amount of income to be attributed to each shareholder or controlling person should be calculated by reference to the proportion of ownership.
[193] Income Tax Act, 1962 of South Africa, s 9D.

that it removes from multinational groups the financial incentive for income shifting.[194] Picciotto, commenting on the history of the US CFC rules, writes that: "…in 1962, the United States took new countermeasures against the use of tax havens with its rules against what came to be called Controlled Foreign Corporations (CFCs). These enabled the United States to tax the profits of affiliates based in tax havens as if they belong to the parent company, in effect disregarding that they are separate entities".[195]

While the OECD opposes the shift to the unitary taxation of MNEs as a way of addressing base erosion, it supports the adoption of and strengthening of CFC regimes by countries in which MNEs are based, as an effective way of addressing profit shifting and base erosion.[196] The implication of this is that the OECD supports the abandonment of one of the fundamental bases upon which the present international tax system is based- the separate entity treatment of members of corporate groups. It impliedly supports the treatment of corporate groups as unitary firms, in the fight against base erosion and profit shifting. It is only apt that countries and supranational bodies, such as the OECD, explicitly adopt the unitary taxation of MNEs, to effectively tackle base erosion and profit shifting.

In conclusion, treating MNEs as a single unit is not new to law as judicial decisions and statutory enactments reveal. It is ever more important today, to tax MNEs as unitary firms, as "the separate entity approach may not always account for the economies of scale and interrelation of diverse activities created by integrated entities".[197] It must be acknowledged and accepted by the supranational bodies responsible for "dictating" the global tax system, that in an "increasingly global

[194] Durst, supra note 30.
[195] Picciotto, supra note 155 at 5.
[196] OECD, Designing Effective Controlled Foreign Company Rules, Action 3 – (2015) Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241152-en.pdf?expires=1554327987&id=id&accname=guest&checksum=431E33E8EC630F3313887DAB5661049D>
[197] Paragraph 1.10 of Chapter 1 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

economy, it is difficult to assign profits to individual countries, and attempts to do so are fraught with opportunities for tax avoidance."[198]

It is high time that tax law and practice caught up with the economic reality of how and why MNEs are formed and how they do business. As shown above, courts in a number of jurisdictions have shown willingness to treat MNEs as single firms. It would be appropriate for lawmakers to codify the treatment of MNEs as unitary firms and tax them accordingly.

4. Arm's Length Principle

a. Description of the Arm's Length Principle

The arm's length principle represents an international standard that compares the transfer price between related parties with the price of similar transactions carried out between independent parties at arm's length.[199] Article 9 of the OECD MTC, while not expressly containing the words, "arm's length" has been interpreted by the OECD and most tax jurisdictions to establish the arm's length principle.[200] This claim has been challenged by some tax jurisdictions and experts who have argued that compliance with article 9 must not be limited to the adoption of the arm's length principle. For instance, Brazil has defended strongly its fixed margins approach as compatible with article 9 of the OECD MTC.[201]

Notwithstanding the controversies, Article 9 of tax treaties deals with the taxation, adjustment and corresponding adjustment of business profits derived from transactions between related entities.[202] According to Solilova and Steindl, "The objective of article 9 is to ensure that transactions between associated

[198] Avi-Yonah, supra note 33.
[199] Wells, supra note 32, "In their paper, they state that the allocation of income between residence and source countries is accomplished via the associated enterprises and related articles of the model treaties, commonly referred to as transfer pricing ("TP"), which principles have evolved over many years within this conceptual framework.
[200] Richard Collier & Joe Andrus (2017) Transfer Pricing and the Arm's Length Principle after BEPS" (2017), Oxford: Oxford University Press.
[201] Picciotto, supra note 28.
[202] Collier, supra note 199.

enterprises comply with the arm's length principle, which means that these transactions must be treated as if they had been carried out between two wholly independent enterprises".[203]

Theoretically, the arm's length principle presents a neutral concept, which guarantees that the conditions of transactions between related enterprises are not distorted by the relationship between them, or special conditions are not imposed on the related enterprises.[204] At formation, the arm's length principle was designed to reduce the incidence of economic double taxation.[205] This was the major concern of taxpayers which led to the negotiation of tax treaties.[206] It aimed at achieving capital neutrality between foreign and domestic enterprises, single and multi-firms by removing any benefit that may accrue through transfer mispricing.[207]

The OECD summarizes the objectives of the arm's length principles as, "securing the appropriate tax base in each jurisdiction and avoiding double taxation, thereby minimizing conflict between tax administrations and promoting international trade and investment.[208] For tax authorities, the arm's length principle provides the legal basis to adjust the declared profits of taxpayers and tax accordingly, where the tax authority believes that the profit declared may not be accurate. The arm's length principle combined with the developed transfer pricing methodologies provide some level of certainty and comfort for taxpayers who have

---

[203]Veronika Solilova & Steindl, "Tax Treaty Policy on Article 9 of the OECD Model Scrutinized" (2013) Bulletin for International Taxation, Vol 3, at 128–136.
[204] Wenli Cheng & Dingsheng Zhang, "The Arm's Length Principle, Transfer Pricing and Foreclosure under Imperfect Competition" (2010) Discussion Paper, Vol 20, No 10, Department of Economics: Monash University.
[205] Avi-Yonah, supra note 23.
[206] Mitchell Carroll, "Income Tax Conventions as an Aid to International Trade and Investment" (1962) Section of International and Comparative Law Bulletin, 6(3), 16-30.
[207] See paragraph 1.8 of Chapter 1 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. The OECD claims that a major reason for the adoption of the arm's length principle by member countries is that it provides broad parity of tax treatment for members of MNE groups and independent enterprises. The arm's length principle avoids the creation of tax advantages or disadvantages that would otherwise distort the relative competitive positions of members of MNE groups or independent entities, by putting both on a more equal footing for tax purposes.
[208]OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017, para 7 of Preface.

to comply with only one approach of income allocation, thereby reducing compliance costs and aiding business decision-making.[209]

In addition, the arm's length principle is a transaction-based approach. It requires both taxpayers and tax authorities to benchmark the price set by related parties for the transfer of goods and services on the price non-related entities would have fixed, or a price fixed by a related entity and a non-related entity.[210]

The determination of the arm's length price for transactions depends on the presence of comparables. To achieve this, a comparability analysis is undertaken where the conditions and terms of a controlled transaction are compared with the terms and conditions of an uncontrolled transaction.[211] The purpose of the comparability analysis is to equate, as closely as possible, the terms and conditions in a controlled transaction with those of an uncontrolled transaction.[212] If the terms and conditions between the controlled transaction and the uncontrolled transaction are similar, then the arm's length principle is satisfied, and no adjustment is necessary.[213] Where the terms and conditions of the controlled transaction differ from those of the uncontrolled transaction, especially as it concerns the price of the transaction or the profits declared, then the affected tax jurisdiction may adjust the terms and conditions to achieve an arm's length price.[214] This adjustment could be an increase of the income declared or the reduction of deductible expenses claimed by the associated enterprise.[215] To be comparable, the compared transactions do not have to be identical to each other in all respects in order to be used in the comparability analysis.[216]

---

[209] Ibid.
[210] Francois Vincent & Ian Freedman, "Transfer Pricing in Canada: The Arm's Length Principle and the New Rules" (1997) Canadian Tax Journal, Vol 45, No 6.
[211] Allison Christians & Laurens Van Apeldoorn, "Taxing Income Where Value is Created" (2018) Florida Tax Review, Vol 22, No 1.
[212] UN Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations (2017) para. B.2; OECD, "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration 2017, para A31.
[213] Ibid.
[214] The OECD MTC, art 9 (1); The Corporate Income Tax Act, C-21, 2004, s 22.
[215] Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Transfer Pricing) Regulations, 2018, r 4.
[216] Ibid, r 11.

The comparables may be external or internal.[217] An example of an external comparable is given. If Parentco A sells a commodity to Subco B for $1,000, to determine whether $1,000 is a fair price, both parties have to seek a similar transaction for a similar product by two non-related entities and benchmark the price set by those parties with their set price. That is, the price of $1,000 must approximate to the price fixed by two unrelated parties for a similar transaction and similar product.

For the taxpayer, this implies seeking at the time of concluding transaction with a related entity or at the time of preparing the required documentation for the transaction, similar transactions by other non-related parties and the terms of the transaction, including the price.[218] An internal comparable differs in the sense that it uses transactions entered between a related entity and a non-related entity as the comparable for bench-marking.[219]

To arrive at a conclusion that two transactions are comparable, a functional analysis of both transactions is undertaken.[220] In this process, the functions performed, assets used, and risks assumed by the parties involved in the transactions are evaluated to determine their comparability.[221] According to the 2017 OECD TPGs, "…the functional analysis seeks to identify the economically significant activities and responsibilities undertaken, assets used or contributed, and risks assumed by the parties to the transactions.[222] The analysis focuses on what the parties actually do and the capabilities they provide. Such activities and capabilities will include decision-making, including decisions about business strategy and risks."[223]

---

[217] UN Practical Manual, supra note 215, para B.1.5, at 38.
[218] Ibid.
[219] OECD, supra note 169 at para A42.
[220] OECD, supra note 169 at para D12.
[221] Ibid.
[222] Ibid.
[223] OECD, supra note 169 at para 1.51.

In sum, article 9 (1) of the OECD MTC highlights the important attributes of MNEs and the potential for profit manipulation. First, it covers companies which are related. This relationship is shown through participation either in the management, control or capital of other enterprise.[224] Second, as a result of the existing relationship, conditions may be imposed or made between the related enterprises that would not have been made or imposed if they were separate or independent entities.[225] Third, where this is the case or feared to be the case, tax authorities or a Contracting State may adjust the profit declared for the purpose of taxing it.[226]

b. The Limitations of the Arm's Length Principle

The separate entity treatment of MNEs for tax purposes, coupled with the requirement to deal with each other on market terms, create the opportunity for profits arising from activities taking place among related entities to be manipulated for the sole benefit of the ultimate parent company. Given the frequency and volume of transactions that occur among related entities, this potential for profit manipulation may result in profit being declared and taxed in a low tax jurisdiction, where real economic activities may not have taken place.[227] It could mean that understated profits or high losses may be declared in a high tax jurisdiction where the economic activities take place.

Avi-Yonah and Clausing argue that the existing system of taxing multinational entities provides an artificial tax incentive to earn income in low-tax countries, rewards aggressive tax planning, and is not compatible with any common metrics of efficiency.[228] This potential for manipulation contradicts the principles of inter-

224 OECD MTC, supra note 1, art. 9.
225 Ibid.
226 Ibid.
227 Clifton Fleming, Robert Peroni, & Stephen Shay, "Getting Serious about Cross-Border Earnings Stripping: Establishing an Analytical Framework" (2015) North Carolina Law Review, Vol. 93 at 673.
228Avi-Yonah, supra note 33.

nation equity and inter-taxpayer equity. Baistrocci decries that, "transfer pricing manipulation produces two major consequences. First, it puts national tax jurisdictions under stress because it is an income shifting system that allows MNEs to maximize after-tax profits by channeling taxable income to jurisdictions with lower taxes. Second, it raises horizontal equity issues because it provides a substantial advantage to MNEs over non-MNEs; only the former can use this type of international tax planning strategy."[229]

As acknowledged by the OECD, the relationship among members of an MNE group may permit the group members to establish special conditions in their intra-group relations that differ from those that would have been established had the group members been acting as independent enterprises operating in open markets.[230] Durst summarizes this potential for manipulation thus:

> "Transfer pricing laws typically allow tax authorities some latitude to challenge the bona fides of these contracts if the relationships between companies specified in the contracts depart manifestly from the parties' actual dealings. But the test for overriding contracts generally is highly subjective, and tax authorities' theoretical ability to challenge the bona fides of taxpayer contracts has not in practice resulted in meaningful constraints on profit shifting. The result has been the tremendous expansion of profit shifting that has given rise to today's BEPS process."[231]

In this section, I discuss and analyze the reasons for the inefficiency of the arm's length principle, especially for African countries. The limitations of the arm's length principle are two-fold: foundational and procedural.

The arm's length principle suffers from a foundational flaw. First, it would appear there is a misconception of the intent of article 9. A careful reading of article 9 of

[229] Eduardo Baistrocchi, "The Transfer Pricing Problem: A Global Proposal for Simplification" (2006) Tax Lawyer, Summer 2006.
[230]OECD TPGs, supra note 169 at para 6 of the Preamble.
[231]Durst, supra note 30.

the OECD MTC reveals that it refers to profits which would have accrued to a tax jurisdiction, and not the pricing of the transaction, as is currently being implemented. The purport of this claim is that article 9 of model tax treaties focuses on the apportionment of profits of a corporate group whose related entities have transacted with each other and not the prices to be fixed for the transactions themselves. As has been argued and will be seen in subsequent discussions, the arm's length principle focuses on the determination of prices of transactions entered into between related entities. This global practice, which has led to the establishment of transfer pricing rules would appear to be a misinterpretation of the letter and spirit of article 9.

To buttress this point , there are five (5) common transfer pricing methodologies globally issued and accepted as tools to establish the arm's length price for transactions between related entities.[232] These transfer pricing methods are the comparable uncontrolled practice method, the cost-plus method, the resale price margin, the transactional net margin method and the profit split method.[233] Of all five methods, only the comparable uncontrolled price method has the price fixed for transactions between the related entities as its financial indicator.[234] All other four transfer pricing methods have a form of profit as their financial indicators.[235] As demonstrated in more detail below, focusing on the price of transactions makes application of the arm's length principle difficult and impractical for jurisdictions, especially African countries.[236]

Furthermore, the preferred transactional approach limits the analysis of the relationships between entities in a corporate group to individual facts and

[232] Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Transfer Pricing) Regulations, 2018, r 5.
[233] Ibid.
[234] Paragraph 2.4 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[235] Paragraph 2.46 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[236] David Spencer, "Transfer Pricing: Will the OECD Adjust to Reality?" Article published on the website of the Tax Justice Network, online: <https://www.taxjustice.net/cms/upload/pdf/Spencer_120524_OECD_.pdf>.

circumstances analysis of each transaction entered into by related entities.[237] This approach fails to recognise the economies of scale, scope, synergy and the interrelation of diverse activities created by integrated business, which are integral to the corporate group.[238] It denies the fact that the commercial activities of related entities are not necessarily decided on standalone transaction basis. Business transactions between related entities are structured to promote the common enterprise and increase the total profit of the corporate group.[239]

This lack of appreciation of the unique attributes of multinational entities and the business model used by the multinational entities has led to unsuccessful searches for comparable transactions by both taxpayers and tax authorities all in the aim to determine the arm's length price[240]. The uniqueness of the goods or service being developed may not be comparable to others in the market. For example, a core and highly centralised function of a multinational group is research and development (R&D), which may be premature to put a price on until the product is manufactured.[241] Demanding that a price be put on the research and development phases of product manufacturing and that comparables be found for those phases, certainly encourage fictional allocation of prices by taxpayers.[242]

The industry of the taxpayer provides consideration. Some industries are highly integrated and taxpayers within those industries boast of providing features or services their competitors don't provide, thereby making it difficult to find similar transactions or comparable terms in the market. The automobile industry is illustrative. In this very highly integrated industry, the sale mantra of each

237 Jens Wittendorff, "Transfer Pricing and the Arm's Length Principle in International Tax Law", (2010) The Netherlands: Alphen aan den Rijn; Wolters Kluwer Law & Business.
238 Stephen Hymer, 'The Efficiency (contradictions) of Multinational Corporations' (1970) American Economic Review, 60 (2), 411−18; Ronald Coase, 'The Nature of the Firm' (1973) Economica, 4 at 386–405; reprinted in G.J. Stigler & KE.
239 OE Williamson, 'The modern corporation: origins, evolution, attributes' (1981), Journal of Economic Literature, 19, 1537−68
240 Picciotto (2018), supra note 29 at 15.
241 Picciotto, supra note 29 at 14.
242 William Petty II & Ernest Walker, "Optimal Transfer Pricing for the Multinational Firm" (1972) Financial Management, Vol 1, No 3 at 74−87. The authors argue that the earnings of an MNE can be altered to varying degrees by its internal pricing policies.

carmaker is the uniqueness of its goods or services, distinct from other carmakers.[243] To insist on applying the arm's length principle in such an industry is to encourage fictional allocation of price, which is vulnerable to the erosion of tax bases and shifting of profits to more favorable tax jurisdictions.[244]

Furthermore, corporate groups can take and manage high risks, the legal ownership of which can be moved around the entities in the group to achieve a better tax result.[245] Their business models permit making losses in one jurisdiction, setting it off with profits made in other jurisdictions.[246] Independent entities may be unable to take such high risk or commit the capital needed in a high-risk venture.[247] This is common practice among related entities, which independent entities are not built for, thus, making it difficult to find relevant comparables.[248]

From a procedural angle, applying the arm's length principle requires a high cost of documentation, unpredictability of outcome, months spent going through audit, possible adjustment of taxable profits and potential liability to payment of penalties.[249] This procedural difficulty, the OECD itself recognises in its 2017 TPGs where it admits that, applying the arm's length principle could be a resource-intensive process, and could impose heavy administrative burden on taxpayers and tax administrations, exacerbated by both complex rules and resulting compliance demands.[250]

---

243 Richard Langlois & Paul Robertson, "Explaining Vertical Integration: Lessons from the American Automobile Industry" (1989) The Journal of Economic History, Vol 49, No 2.
244 John Jacob, "Taxes and Transfer Pricing: Income Shifting and the Volume of Intrafirm Transfers" (1996) Journal of Accounting Research, Vol 34, No 2 at 301−312.
245 Thomas Rixen, "From Double Tax Avoidance to Tax Competition: Explaining the Institutional Trajectory of International Tax Governance" (2010) Review of International Political Economy, Vol 18, Issue 2; Peggy Musgrave, "International Tax Base Division and the Multinational Corporation" (1972), Public Finance, Vol 27.
246 James Eustice, "Tax Problems Arising from Transactions Between Affiliated or Controlled Corporations" (1968), Tax Law Review 23.
247 Ibid.
248 Crivelli, supra note 8.
249 Alexandra Readhead, "Preventing Base Erosion in Africa: A Regional Study of Transfer Pricing Challenges in the Mining Sector" (2016) Natural Resource Governance Institute.
250 OECD TPGs supra note 169 at para E 1.4.95.

I provide context. The transfer pricing unit of the Kenya Revenue Authority consists of 12 people divided into two teams of 5 members each, with two supervisors overseeing the two teams.[251] The level of training and experience of each member of the team varies between 2-3 years and 5-6 years. Meanwhile, Kenya has 310,000 registered companies,[252] with a number of them being multinational companies and subject to transfer pricing rules.[253] Even if just 1% of the registered companies were subject to transfer pricing rules, that is quite a significant number (3,100) for a team of 12 people to handle, on a yearly, transactional basis.

This is the common experience of transfer pricing units in African countries, which have transfer pricing rules. Nigeria, with its big market has about 30 people in its international tax department, including those who primarily work on transfer pricing.[254] These 30 people are responsible for auditing the tax returns of hundreds of big multinational companies who do business in the country. The transfer pricing unit of KPMG Nigeria consists of 18 dedicated, well-trained and incentivized staff who daily advise their clients on transfer pricing matters.[255] KPMG is just one of several large accounting firms in Nigeria[256] and there are number of small ones providing accounting services to clients.[257] It is easy to see the mismatch here.[258]

5. Analysis of Transfer Pricing and Particular Limitations

[251] Waris, supra note 14 at 20.
[252] Ministry of Industry, Trade and Cooperatives, "Number of Companies Registered in Kenya Increases by 53%" (2018) Republic of Kenya Ministry of Industry, Trade and Cooperatives, online: <http://www.industrialization.go.ke/index.php/media-center/blog/333-number-of-companies-registered-in-kenya-increases-by-53>
[253] Waris, supra note 14.
[254] Information obtained from staffers of the Federal Inland Revenue Service, Nigeria. 20 September 2017. Notes on file with the author.
[255] Information obtained from Victor Adegite of KPMG Nigeria. 20 September 2017. Notes on file with the author.
[256] E.g. PriceWaterHouse Coopers, Ernst & Young, and Deloitte all have offices in Nigeria.
[257] Ugo Obi-Chukwu, "Total Number of Audit Firms in Nigeria 916, 655 Each Have One Owner?" (2012) Nairametrics, online: <https://nairametrics.com/2012/10/08/total-number-of-audit-firms-in-nigeria-916-655-each-have-one-owner/>.
[258] Sol Picciotto, "Is the International Tax System Fit for Purpose, Especially for Developing Countries?" (2014) ICTD Research in Brief 8.

a. Legal Construction of Transfer Pricing

The discussion in section 4 of this chapter looked broadly at the arm's length principle. In this section, I shall analyse the limitations of transfer pricing and their relationship with tax avoidance. The aim here is to show the difficulties with applying the transfer pricing methods and transfer pricing documentation requirements prescribed in the OECD TPGs.

Transfer pricing is the result of the application of both the separate entity principle and the arm's length principle. It is the process of pricing the transfer of goods and services between related entities when they transact with each other.[259] The OECD in its 2017 TPGs defines transfer pricing as "the prices at which an enterprise transfers physical goods and intangible property or provides services to associated enterprises".[260] It is the term used for the pricing of intragroup, cross-border business transactions between related entities. According to Christians and Van Apeldoorn, transfer pricing rules "fundamentally exist in order to address the possibility of valuation errors when parties transact with other parties which they control, or which are under common control…"[261]

To assist tax payers and tax authorities to harmonize their application of the arm's length principle so as to minimize disputes, and to ensure a global standard of interpretation and application of the arm's length principle, and resolution of disputes arising therefrom, the OECD in 1995[262] commenced the issuance of transfer pricing guidelines (TPGs)[263]. These TPGs, which are revised periodically to address rising transfer pricing challenges, aim at assisting tax payers and tax

[259] For a comprehensive discussion on transfer pricing, see Richard Collier & Joseph Andrus, "Transfer Pricing and the Arm's Length Principle After BEPS" (2017): Oxford University Press.
[260] OECD TPGs supra note 169.
[261] Christians, supra note 170.
[262] Prior to the 1995 Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, the OECD had in 1979 issued the Report on Transfer Pricing and Multinational Enterprises.
[263] OECD MTC, supra note 1.

authorities in determining the arm's length prices for transactions entered into by related entities.

These TPGs influence the enactment of transfer pricing regulations in the domestic laws of many tax jurisdictions. In some cases, they are expressly adopted in domestic laws as applicable in the resolution of disputes between taxpayers and tax authorities. For instance, the Nigerian Transfer Pricing Regulations 2018 follows the guidance provided in the OECD TPGs, while at the same time expressly referencing the OECD transfer pricing guidelines in the resolution of disputes between related entities. The latest transfer pricing guidelines issued by the OECD is the 2017 OECD Transfer Pricing Guidelines (2017 TPG).[264]

b. Application of Transfer Pricing to Transactions between Related Entities

The TPGs introduce transfer pricing methods to be used by taxpayers and tax authorities to determine the arm's length price for transactions entered into between related entities.

Selecting the appropriate transfer pricing method is important in effectively arriving at an arm's length price. The OECD cautions that "the selection process should take account of the respective strengths and weaknesses of the OECD recognized methods; the appropriateness of the method considered in view of the nature of the controlled transaction, determined in particular through a functional analysis; the availability of reliable information (in particular on uncontrolled comparables) needed to apply the selected method and/or other methods; and the degree of comparability between controlled and uncontrolled transactions, including the reliability of comparability adjustments that may be needed to eliminate material differences between them."[265]

---

[264] OECD TPGs, supra note 169.
[265] Paragraph 2.2 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

The Nigerian transfer pricing regime re-echoes the provision of the 2017 OECD TPG, by providing in Regulations 5 (2) that:

> "(2) in each case, the most appropriate transfer pricing method shall be used taking into account-
>
> (a) the respective strengths and weaknesses of the transfer pricing method in the circumstances of the case;
>
> (b) the appropriateness of a transfer pricing method having regard to the nature of the controlled transaction determined, in particular, through an analysis of the functions performed, assets employed, and risks assumed by each person that is a party to the controlled transaction;
>
> (c) the availability of reliable information needed to apply the transfer pricing method; and
>
> (d) the degree of comparability between controlled and uncontrolled transactions, including the reliability of adjustments, if any, that may be required to eliminate any differences between comparable transactions."[266]

The OECD categorizes these transfer pricing methods into two: traditional transactional methods and transactional profit methods.[267] The traditional transactional methods are the comparable uncontrolled price method (CUP method), the resale price method, and the cost-plus method. The transactional profit methods are the transactional net margin method and the transactional profit split method.[268]

While the OECD claims that there is no suitable method in every situation, it however prefers the application of the traditional transactional methods, arguing

---

[266] The Income Tax (Transfer Pricing) Regulations No 1, 2018, r 2(2); see: Ahmed Olatunjilsau, "Transfer Pricing: The Nigerian Perspective" (2014) Internal Journal of Accounting and Taxation, Vol 2, No 2 at 23–38.

[267] Paragraph 2.1 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

[268] Ibid.

they are the most direct means of establishing whether conditions in the commercial and financial relations between associated enterprises are arm's length.[269] This, it attributes to the ease of substituting the price in a comparable uncontrolled transaction for the price of the controlled transaction.[270] The OECD, however, recognizes that in situations where each of the parties makes unique and valuable contributions to the controlled transactions or where the commercial activities are highly integrated, the transactional profit methods may be more appropriate in those circumstances.[271]

We learn from Picciotto that seventeen African countries have enacted transfer pricing rules modelled after the OECD's TPGs.[272] For example, regulation 5 of the transfer pricing regulations of Nigeria[273] requires that one of the transfer pricing methods— comparable uncontrolled price method, resale price method, cost plus method, transactional net margin method and the traditional profit split method— be used in determining whether the result of a transaction or series of transactions are consistent with the arm's length principle. These transfer pricing methods are briefly explained below:

Comparable Uncontrolled Price Method (CUP)

The CUP method searches for identical transactions between independent parties, using the price fixed by such independent parties in assessing the transfer price fixed by related entities.[274] In other words, it compares the price charged for the sale of goods or services in a controlled transaction to the price charged for the sale of goods or services in an uncontrolled transaction in comparable circumstances. According to the OECD:

[269] Paragraph 2.3 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[270] Ibid.
[271] Paragraph 2.4 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[272] Picciotto (2018), supra note 29.
[273] Regulation 5 of the Income Tax (Transfer Pricing) Regulations No 1, 2018.
[274] OECD TPGs, supra note 209.

"an uncontrolled transaction is comparable to a controlled transaction (i.e. it is a comparable uncontrolled transaction) for purposes of the CUP method if one of two conditions is met: a) none of the differences (if any) between the transactions being compared or between the enterprises undertaking those transactions could materially affect the price in the open market; or b) reasonably accurate adjustments can be made to eliminate the material effects of such differences."[275]

To effectively arrive at a comparable price, the CUP method deploys detailed transactional analysis, taking into consideration, necessary adjustments to the price.[276] The relevant financial indicator here is the price fixed between the related parties.[277] If there are price differences, it may indicate a non-arm's length transaction, with the likely consequence of transfer pricing adjustment.[278]

The comparables may be internal or external. It is internal where transactions between a controlled entity and an unrelated party exists and is compared to the transaction between two controlled entities.[279] It is external where the comparable is a transaction between two unrelated parties, compared to the transaction between two related/controlled entities.[280] The OECD recommends the use of the CUP method as the most direct and reliable way to apply the arm's length principle, where it is possible to locate comparable uncontrolled transactions.[281]

Resale Price Method (RPM)

[275] Paragraph 2.15 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[276] Paragraph 2.14 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[277] Paragraph 2.18 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[278] Paragraph 2.17 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[279] Ibid.
[280] Paragraph 2.19 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[281] OECD TPGs, supra note 213.

The RPM takes into consideration the price at which the product purchased from an associated enterprise, is resold to an independent enterprise (resale price).[282] It advances to subtract from the resale price, an appropriate gross margin to arrive at an arm's length price for the original transfer of goods and services between the associated enterprises.[283] According to the OECD, the gross margin represents the amount out of which the reseller would seek to cover its selling and other operating expenses, and in the light of the functions performed (taking into account assets used and risks assumed), make an appropriate profit.[284]

The RPM in the controlled transaction may be compared with the resale price in a transaction between the controlled party and an uncontrolled party (internal comparables) or between two uncontrolled parties (external comparables).[285] The focus here is the gross profit margin obtainable in comparable uncontrolled transactions in ascertaining what the arm's length price should be in the controlled transaction.[286] It is a one-sided method, which requires the selection of a tested party, necessarily the party that purchases the product in the controlled transaction and resells.[287] The relevant financial indicator here is the gross margin on sales, which is compared with the gross margin from comparable uncontrolled transactions.[288] Just as the CUP, the comparables may be internal or external.[289]

Cost-Plus Method (CP)M

---

[282] Paragraph 2.27 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[283] Paragraph 2.27 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[284] Paragraph 2.27 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[285] Paragraph 2.28 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[286] Ibid.
[287] Paragraph 2.28 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[288] Paragraph 2.28 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[289] Paragraph 2.28 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

The CPM proceeds from the cost incurred by a supplier of goods or services in a controlled transaction for goods or services transferred to an associated enterprise, and advances to determine an appropriate mark-up in arriving at an arm's length price for the goods or service for the controlled transaction.[290] The appropriate mark-up is determined by reference to the mark-up earned by independent entities in comparable uncontrolled transactions (external comparabes) or by the same supplier when he supplies to an uncontrolled party in comparable uncontrolled transactions (internal comparable).[291]

According to the OECD, an uncontrolled transaction is comparable to a controlled transaction (i.e. it is a comparable uncontrolled transaction) for purposes of the CPM if one of two conditions are met: a) none of the differences (if any) between the transactions being compared or between the enterprises undertaking those transactions materially affect the cost plus mark up in the open market; or b) reasonably accurate adjustments can be made to eliminate the material effects of such differences.[292]

The CPM is a one-sided method, which takes into account the cost-plus markup earned by a seller of a good or service.[293] It requires the selection of a tested party, in this case, the party that supplies the product or service in the controlled transaction.[294] The relevant financial indicator here is the mark-up on direct and indirect costs incurred in the supply of goods and services.[295] Just as other traditional transactional methods, the comparables may be internal or external.[296]

---

[290] Paragraph 2.45 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[291] Paragraph 2.46 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[292] Paragraph 2.47 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[293] Paragraph 2.45 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[294] Paragraph 2.45 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[295] Paragraph 2.46 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017
[296] Paragraph 2.46 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017

The OECD states that this method is most useful in the cases of semi-finished goods, joint facility agreements or long-term buy-and-supply arrangements or the provision of services, between associated enterprises.[297]

Transactional Net Margin Method (TNMM)

The TNMM examines the net profit made by a tested party in a controlled transaction and compares it with that made in an uncontrolled transaction by an uncontrolled party.[298] Unlike the resale price method and the cost-plus method, the TNMM looks at the operating profit (net profit) made by the tested party and compares same with that which an independent party would make in an uncontrolled environment. The TNMM is a one-sided method and focuses on the net profit,[299] a factor affected largely by other indices other than the transfer price.[300] The relevant financial indicator here is the margin of operating profit (net profit) from the transaction.[301]

Profit Split Method

The profit split method examines the combined profit arising from the controlled transaction and splits the profit between the related parties, using some economic indicators or basis.[302] According to Andrus and Collier, "…the profit split method first seeks to identify the relevant profit to be split and then splits that profit between the associated enterprises on an economically valid basis that approximates the division of profits that would have been anticipated and

---

297 Paragraph 2.45 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

298 Paragraph 2.64 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

299 Paragraph 2.69 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

300 Paragraph 2.70 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

301 OECD TPGs supra note 224.

302 Paragraph 2.114 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

reflected in an agreement made at arm's length."[303] They opine that the profit split method does not rely on the availability of closely comparable transactions, but highly dependent on identifying the respective contributions of the parties, typically through a detailed functional analysis.[304]

The profit split method seeks to split the profit between the related parties based on the functions performed, assets employed, and risks assumed by the parties.[305] Under the profit split method, the goal is to allocate profits between the related parties in the controlled transaction, with reference to the split of profits in similar transactions between independent parties.[306] The relevant financial indicator is the profit split between the parties, based on the contributions of the parties to the combined profit. This is a two-sided transfer pricing method, as it considers both parties involved in the transactions.[307]

c. Challenges of Applying Transfer Pricing Methods in Africa

The above discussion outlined common difficulties of arm's length transfer pricing that apply to all countries. However, African countries face additional, specialized difficulties that must be examined in order to understand why systemic change is necessary.

A major impediment for African countries in applying the arms' length standard is that local tax administrations do not possess the requisite experience, knowledge, training and incentives needed to engage in transfer pricing audit or negotiations. This shortcoming plays to the advantage of the big accounting firms, who deploy highly incentivized accountants to take advantage of the regulatory

[303] Joseph Andrus & Richard Collier, "Transfer Pricing and the Arm's Length Principle After BEPS" (Oxford: Oxford University Press, 2017).
[304] Ibid.
[305] Paragraph 2.117 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.
[306] Ibid.
[307] Paragraph 2.119 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

gaps and absence of technical capacity.[308] According to Durst, the complexity of corporate tax law effectively acts as a shield against significant public scrutiny which allows tax avoidance to flourish.[309]

A second challenge for African countries in particular is that the resources needed to effectively carry out a transfer pricing assessment if available at all, come at a high cost to both taxpayers and tax authorities.[310] While taxpayers may be able to transfer such costs to their clients, tax authorities are in a worse situation than their counterparts in other countries owing to broad institutional challenges. They must compete among other government bodies, ministries, and infrastructural needs for scarce public resources.[311] For a country struggling with public finances, expending more limited resources on capacity building, trainings and workshops, which in most cases are held abroad, may seem like a waste of already limited resources.[312]. ATAF seeks to address this particular problem,[313] and the OECD works with them through the TIWB project, to address the issue of capacity. It is pre-mature to assess the success or otherwise of these measures, but progress is being made.[314]

The combined effects of the absence of technical capacity and lack of resources to effectively carry out transfer pricing assessment may lead to the disregard for the transfer pricing legislation, or adoption of creative and poorly designed

---

308 See Paragraph 1.12 of Chapter 1 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017, where the OECD admits that "the arm's length principle may result in an administrative burden for both the taxpayer and the tax administrations of evaluating significant numbers and types of cross-border transactions".

309 Durst, supra note 31.

310 Merima Ali, "Regulatory Burdens in Tax Administration and Firms' Compliance Costs in Africa" (2018) ICTD Working Paper 78.

311 Michael Durst, "Pragmatic Transfer Pricing for Developing Countries" (2012) Tax Notes International; Michael Durst & Robert Culbertson, "Clearing Away the Sand: Retrospective Methods and Prospective Documentation in Transfer Pricing Today" (2003) Tax Law Review, Vol 57 at 37–84.

312 OECD (2017), "Tax Inspectors Without Borders- Bolstering Domestic Revenue Collection through Improved Tax Audit Capacities' OECD, Paris. http://www.oecd.org/tax/tax-inspectors-without-borders-bolstering-domestic-revenue-collection-through-improved-tax-audit-capacities.htm.

313 ATAF, "Suggested Approach to Transfer Pricing Legislation" (2017), Pretoria: ATAF, https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/ATAF%20Suggested%20Approach_revise_green_HR.pdf.

314 Ibid.

enforcement by the tax authority. Local tax authorities face systemic disadvantages when compared to sophisticated accountants who are highly incentivized to test the boundaries of applicable rules, many of which are aided by their counterparts in developed countries where they are headquartered. The consequences of poor enforcement of the transfer pricing process is the erosion of the tax base, capture by powerful taxpayers of the TP assessment process and other tax avoidance effort.[315]

In addition, uncertainty of the potential tax exposure among taxpayers decreases investors' confidence, broadly viewed as an important condition for investment.[316] Uncertainty of the tax system or potential exposure may lead to increased transaction costs, unwillingness to invest in the affected jurisdiction or a transfer of a company's business to friendlier countries.[317] Ease of tax compliance is an important indicator of the World Bank Group Ease of Doing Business Index, and a significant factor in the decision of a company on where to invest, and as such tax certainty goes a long way to aid the decision.[318]

Furthermore, at the heart of the application of the arm's length principle is the comparability analysis needed to determine that the transactions conducted among associated enterprises are at arm's length.[319] As previously stated, a

---

[315] Alex Cobham & Peter Jansky "Global Distribution of Revenue Loss from Tax Avoidance: Re-estimation and Country Results" (2017) WIDER Working Paper 2017/55, Helsinki: UNU-WIDER.
[316] IMF, OECD, UN and World Bank (2015) Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment, Report to the G-20 Development Working Group, 15 October 2005, Washington: International Monetary Fund.
[317] Ruud de Mooij, R.A. & Li Liu, "At a Cost: The Real Effects of Transfer Pricing Regulations" (2018) Working Paper 18/69, Washington DC: IMF. The paper argues that MNEs reduce their investment by over 11 percent following the introduction of transfer pricing regulations.
[318] Joel Cooper, et al., "Transfer Pricing and Developing Economies: A Handbook for Policy Makers and Practitioners" (2016) Directions in Development—Public Sector Governance. Washington, DC: World Bank; The World Bank, "Ease of Doing Business Index 2017: Nigeria", (2017), World Bank Group, https://data.worldbank.org/indicator/IC.BUS.EASE.XQ?locations=NG. Important to state that the World Bank Index was in 2018 shown to be riddled with errors, if not fraud. Despite these known problems, foreign investors likely rely on such faulty indicators because there are no ready alternatives. See: Daniel Runde, "The World Bank's Doing Business Indicators Still Work" (2018) Foreign Policy, https://foreignpolicy.com/2018/02/23/the-world-banks-doing-business-indicators-still-work/.
[319] Paragraph B.1.6 of Chapter 2 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017.

controlled transaction is deemed comparable to an uncontrolled transaction where there are no material differences between them that could affect the price being determined, and where there are differences, adequate adjustments can be made to eliminate the effects of those differences. In other words, "the economically relevant characteristics of the two transactions and the circumstances surrounding them are sufficiently similar to provide a reliable measure of an arm's length result."[320] In considering whether transactions are comparable, some factors are especially pertinent, including:

- The contractual terms of the transaction;
- The functions performed by each of the parties to the transaction, taking into account assets used and risks assumed, including how those functions relate to the wider generation of value by the multinational enterprise (MNE) group to which the parties belong, the circumstances surrounding the transaction, and industry practices;
- The characteristics of the property transferred, or services provided;
- The economic circumstances of the parties and of the market in which the parties operate; and
- The business strategies pursued by the parties.[321]

Durst aptly captures the problem of engaging in comparability analysis by developing countries:

> "On economic grounds, there are reasons to expect close comparables for the activities performed by members of multinational groups to be difficult to locate, even in wealthy countries with highly developed economies. The difficulty of locating satisfactory comparables appear especially acute in developing countries, where few independent companies of any kind are

[320] United Nations, Practical Manual on Transfer Pricing for Developing Countries (2017) Department of Economic & Social Affairs. United Nations: New York.
[321] OECD Transfer Pricing Guidelines and the UN Practical Manual on Transfer Pricing.

likely to exist that are publicly traded, and therefore do not report financial data in a format that is useful for analysis under TNMM."[322]

The absence of comparables, as explored by Durst, is a common barrier in the search for arm's length prices for intermediate goods, services and intangible property rights, such as patents and copyrights.[323] There is enormous difficulty in obtaining relevant or applicable data on comparables needed to apply the arm's length principle in African countries. Where data on comparables are available, they may not be easily accessible or adaptable to local circumstances. For instance, there is no African-generated database of comparables, so most African countries rely on other continental databases such as Amadeus and Orbis.[324] Comparables obtained from these foreign databases must be adjusted to align with local circumstances of the African tax jurisdiction, thus, presenting opportunities for taxpayers to manipulate their expenses, losses or profits to achieve better tax results.[325] Each such adjustment creates a burden for the tax authority in terms of time needed to become aware of the issue, investigate and analyze the particular facts and circumstances, and examine counterfactuals which are likely to be contested by the taxpayer.

Even where available, information may be difficult to interpret as a result of language differences, accounting or reporting systems and legal systems. Furthermore, the information may be incomplete for the use intended by the tax jurisdiction thus, not providing a reliable database. Confidentiality and privacy of taxpayers' information may prevent accessibility of relevant information for purposes of comparison. Since the arm's length principle requires that transactions between related entities be comparable with those that would have occurred between independent parties under similar circumstances, applying and

[322] Durst, supra note 9.
[323] Reuven Avi-Yonah, Kimbery Clausing & Michael Durst, "Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split" (2009) Florida Tax Review, Vol 9, No 5.
[324] Waris, supra note 15 at 27.
[325] Ibid.

enforcing it becomes difficult where comparables or relevant information cannot be found or obtained.[326]

The combined effects of the limitations of the arm's length principle and the challenges of application of transfer pricing methods is the widespread presence of transfer pricing abuses (transfer mispricing), which forms part of the tax avoidance discussion. In the next section, I discuss transfer mispricing and provide examples of transfer mispricing on the African continent.

d. Linkage between Transfer Pricing and Tax Avoidance

Where the price set for the transactions between related entities is not consistent with what parties at arm's length would be expected to pay, transfer mispricing or abusive transfer pricing may have occurred.[327]

Transfer mispricing is the manipulation of transfer price to shift profit from one jurisdiction to another, usually from a high tax jurisdiction to a low-tax jurisdiction.[328] This is achieved through the use of multiple tax structures and tax-friendly jurisdictions to shift, place, hide or situate profit across different jurisdictions (base erosion and profit shifting (BEPS). Structures such as "Double Irish with a Dutch Sandwich"[329] and tax-friendly jurisdictions such as Mauritius,

---

[326] See generally: The Platform for Collaboration on Tax, "A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses" (2017) Platform for Collaboration on Tax. Washington, DC: World Bank Group. The PCT puts the difficulties of implementing the arm's length standard and the use of comparables as: cost of licence of data; presence of little relevant information relating to a specific jurisdiction or even region; differences in the comparables of regions or jurisdictions, thus not identical leading to the use of imperfect data by transfer pricing practitioners.

[327] Alexandre Readhead, "Transfer Pricing in the Extractive Sector in Ghana" (2016) Natural Resource Governance Institute Case Study, online: <https://resourcegovernance.org/sites/default/files/documents/nrgi_ghana_transfer-pricing-study.pdf>

[328] Ruud de Mooij supra note 316.

[329] The Irish Times, "'Double Irish' and 'Dutch Sandwich' saved Google $3.7bn in Tax in 2016" (Jan 2, 2018) The Irish Times, online: <https://www.irishtimes.com/business/economy/double-irish-and-dutch-sandwich-saved-google-3-7bn-in-tax-in-2016-1.3343205>. This structure entails a U.S. parent company incorporating an Irish Subsidiary 1 which is controlled from Bermuda. An Irish Subsidiary 2 is incorporated as a wholly-owned subsidiary of Irish Company 1. Finally, a Dutch Company is incorporated as a conduit to outstrip the revenue between Irish Subsidiary 1 and Irish Subsidiary 2. For comprehensive discussion on this tax avoidance structure, see Clemens Fuest et

are popular for enabling base erosion and profit shifting, through the exploitation of the various definitions of the residence of legal persons and the source of income.[330] The 'Paradise Papers"[331] curates some of the multiple and complex structures used by MNEs to shift profits across the globe and erode tax bases in some tax jurisdictions.[332] Through incorporating shell companies in tax friendly jurisdictions, introduction of artificial transactions and taking advantage of complex transfer pricing methodologies, these MNEs are able to singlehandedly determine where profit is realised and declared, most time, in contradiction with where economic activities occur or value is created. This, they achieve by manipulating the transfer price of goods and services transacted and/or payment to related entities in a tax-friendly country for artificial transactions.

Below, I discuss some of the transfer pricing cases in Africa.

The first case is the Kenyan case of Unilever Kenya Limited v. The Commissioner of Income Tax,[333] decided by the High Court of Kenya in 2005. In this case, Unilever Kenya Limited (UKL), a subsidiary of Unilever Plc (a company incorporated in the United Kingdom) entered into a contract with Unilever Uganda Limited (UUL), another subsidiary of Unilever Plc, for the manufacture and supply of certain products.[334]

---

al, "Profit Shifting and 'Aggressive' Tax Planning by Multinational Firms: Issues and Options for Reform" (2013) ZEW Discussion Papers, No. 13-078, Zentrum fur Europaische Wirtschaftsforschung (ZEW), Mannheim; Andrew Fischer, "A Comprehensive Approach to Stateless Income" (2015) The George Washington Law Review, Vol. 83, pp. 1028–1057; Gabriel Zucman, "Taxing across Borders: Tracking Personal Wealth and Corporate Profits" (2014) Journal of Economic Perspectives, Vol 28, No 4, at 121–148.

[330] Picciotto, supra note 15.

[331] Publications by the award-winning International Consortium of Investigative Journalists (ICIJ), focused on revealing the tax avoidance and evasion practices of companies. Details on the activities and publications can be found online: <https://www.icij.org/>.

[332] The author advises the International Consortium of Investigative Journalists on the tax avoidance practices of multinational entities in Africa. See: "Tax Haven Mauritius' Rise Comes at the Rest of Africa's Expense" (2017), online: <https://www.icij.org/investigations/paradise-papers/tax-haven-mauritius-africa/> "Africa's Satellite Avoided Millions Using a Very African Tax Scheme" (2018), online: <https://www.icij.org/investigations/paradise-papers/africas-satellite-avoided-millions-using-african-tax-scheme/>

[333] [2005] eKLR.

[334] Ibid at 1.

These products were sold by UKL to UUL during the 1995 and 1996 fiscal years.[335] UKL during these periods manufactured and sold the same goods to the Kenyan domestic and export markets, and to independent entities.[336] On audit, the Kenyan Revenue Authority (KRA) determined that UKL charged lower prices for goods sold to its related entity in Uganda, UUL, than it charged for similar goods sold to independent parties and the Kenyan domestic and export markets.[337] The KRA determined that the sales to UUL were therefore not at arm's length prices as required by section 18(3) of the Income Tax Act of Kenya.[338] The KRA subsequently adjusted the prices of goods sold by UKL to UUL and assessed UKL for additional tax.[339]

Unilever Kenya appealed against the assessment of the Kenya Revenue Authority.[340] The judgment of the High Court judge, Alnashir Visram, focused on the applicability of transfer pricing methodologies contained in the OECD's Transfer Pricing Guidelines to Kenya's domestic tax laws in determining an arm's length price. The judgment did not rule on the arm's length prices for the products sold by UKL to UUL, instead it focused on the methodology to be used in determining the arm's length prices.[341] However, the case reinforced the arm's length principle and the adjustment powers of revenue authority to adjust the declared taxable profit of a taxpayer where the special relationship that exists between the taxpayer and its offshore counterpart cause prices which are not arm's length to be assigned to their commercial transactions.[342]

The second case is the Malawian case of The State & The Commissioner General of Malawi Revenue Authority v. Ex-Parte Eastern Produce Malawi Limited,[343] which was decided in July 2018. In this case, Eastern Produce Malawi Limited,

[335] Ibid.
[336] Ibid at 2.
[337] Ibid.
[338] Ibid.
[339] Ibid.
[340] Unilever supra note 336 at 1.
[341] Ibid at 12.
[342] Ibid at 13.
[343] [2018] MWHC 800.

the applicant in the case, engaged in the growing, production and processing of tea in Malawi.[344] The Malawi Revenue Authority, the respondent in this case, conducted tax audit on the applicant from 13th to 31st October 2014. At the end of its audit, the revenue authority issued notices of amended assessments to the taxpayer for income tax for the years June 2009, June 2010, June 2011, June 2012 and June 2013.[345]

The transfer pricing dispute in this case was the payment of a commission to a related entity of the applicant, RBDA for services rendered to the applicant.[346] The revenue authority argued that 94.4% of the commission paid to the related entity was disallowed because of the 126 visits that were budgeted and paid for, RBDA actually carried out only seven visits to the applicant in Malawi.[347] The revenue authority stated that the allowed 5.6% of the commission paid to RBDA represented a fair value of the services really rendered to the Malawian company and were granted on humanitarian grounds.[348]

The taxpayer sought the court's relief in form of a declaration that the decision by the revenue authority to disallow 94.4% of the 4% commission (and effectively imposing a commission of only 0.0024% of turnover) paid to RBDA under the transfer pricing analysis was irrational and unreasonable.[349]

The court quashed the decision by the revenue authority to disallow 94.4% of the 4% commission paid to RBDA on humanitarian grounds.[350] However, the court ordered the taxpayer to submit to the revenue authority all documentation needed to undertake a comprehensive analysis of the transfer pricing issues and arrive at an appropriate transfer pricing method.[351]

[344] Ibid at 1.
[345] Ibid at 2.
[346] Ibid at 6.
[347] Ibid.
[348] Ibid.
[349] Ibid at 3.
[350] Ibid at 16.
[351] Ibid at 16.

A third example of transfer mispricing on the African continent is the unreported Kenyan case of Karuturi Limited v. Commissioner of Domestic Taxes (undecided), which was discontinued by the parties for out-of-court settlement.[352] In this case, Karuturi, a Kenyan company, entered into agreement with a related party, tax resident in Dubai, Flower Express, to sell its flowers to Flower Express.[353] The flowers were sold to Flower Express at free-on-board Jomo Kenyatta International Airport, Nairobi (JKIA)' terms.[354] Before the flowers left JKIA, some of the flowers were sold to third party exporters at a significantly higher price, who then exported the flowers to Europe and other markets served by Flower Express.[355] A transfer pricing audit was carried out by the Kenya Revenue Authority on the sale of flowers between Karuturi and Flower Express and an additional tax assessment of approximately 960 million Kenyan Shillings ($10,347,830) was demanded from Karuturi Limited by the Kenya Revenue Authority.[356] Whether and how this case was resolved is not public information.

The three examples above provide examples of the kinds of transfer pricing issues faced in African countries. Transfer mispricing by companies is rarely reported in the news, and data on transfer pricing and tax avoidance in Africa are limited or unavailable. While African countries may have effectively taxed companies for the last half-century, their tax laws are still quite new and developing. Regulations needed to effectively tax MNEs are either not in force or are just being put in place. For example, Nigeria, Africa's largest economy in GDP terms, enacted its transfer pricing regulations in 2012[357] while Uganda enacted its transfer pricing rules in

[352] Information about this case are available to the public only through press releases, which provide minimal detail. See, George Omodi, 'CfC Bank Puts Naivasha flower grower Karuturi up for sale', Business Daily, (26 January, 2015) online: <http://www.businessdailyafrica.com/Corporate-News/CfC-Bank-puts-Naivasha-flower-grower-Karuturi-up-for-sale-/-/539550/2603130/-/31qfx0/-/index.html>.
Two other publications report the case. See, Waris, supra note14; Moses Ado, "Transfer Pricing Disputes in Kenya: Advance Pricing Agreements the Way Forward?" (2015) Master Thesis, Lund University, online: <http://lup.lub.lu.se/luur/download?func=downloadFile&recordOId=5435405&fileOId=5435420>.
[353] Waris, supra note 351 at 21.
[354] Ibid.
[355] Ibid.
[356] Ibid.
[357] The Income Tax (Transfer Pricing) Regulations No 1, 2012.

2011.[358] These years of enacting transfer pricing regulations, compared to OECD member-countries who adopted their rules decades earlier, show the evolution of transfer pricing practice in these countries. To date, there is no record of a decided case on transfer mispricing in Nigeria. Analysis is hampered because taxpayer's information is highly confidential.[359] Confidentiality contributes to the lack of comparables for benchmarking purpose and encourages tax avoidance and collusion with tax authorities.[360] This absence of transparency the OECD seeks to address through its improved transfer pricing documentation requirements, including country-by-country-reporting (CBCR) by large MNEs.[361]

Because publicly available information is scarce owing to taxpayer confidentiality, I consulted the tax authorities in Ghana, Nigeria, Kenya, Uganda, and Tanzania to seek aggregated information from relevant multinational taxpayers' returns including aggregated audit outcomes.[362] While the data collected are anecdotal rather than comprehensive in nature, they confirm claims of tax avoidance on the continent reflected in many accounts of researchers and non-governmental organizations.[363]

---

358 The Income Tax (Transfer Pricing) Regulations 2011 under sections 90 and 164 of the Income Tax Act c340, online: <http://www.drtp.ca/wp-content/uploads/2015/02/Uganda-Transfer-Pricing-Regulations-2011.pdf>

359 Regulation 23 of the Income Tax (Transfer Pricing) Regulations of Nigeria provides that information provided by the taxpayer shall only be used for tax purposes or as may be legally required.

360 Nara Monkam, et al, "Tax Transparency and Exchange of Information (EOI): Priorities for Africa" (2018) T20 Cooperation with Africa, online: <https://www.g20-insights.org/policy_briefs/tax-transparency-and-exchange-of-information-eoi-priorities-for-africa/>.

361 OECD (2015) Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, Paris: OECD Publishing, online: <https://doi.org/10.1787/9789264241480-en>

362 Data solicited include post 2011 audit discoveries, aligning with the years both Uganda and Nigeria enacted transfer pricing regulations. Data solicited included informal discussions and electronic documents soliciting specified information via templates provided by the author. See Appendix II(a) and Appendix II(b). Discussions took place in person and by email communication with officials who wish to remain anonymous. Notes on file with the author. Data received are anonymous, and do not contain names or revealing information about any taxpayers.

363 Ludvig Wier, "Tax-motivated Transfer Mispricing in South Africa" (2018) SA-TIED Working Paper, No 23; Cobham, supra note 314.

Summary of Data from Nigeria

The information here represents analysed sample data received from the revenue authority of Nigeria. As shall be seen, there is significant difference between the taxes returned by the companies and the amount assessed to be payable by the taxpayers after tax audits by the revenue authority.

1. Case 1- a multinational company in the shipping industry, for the period 2011-2014, declared combined tax returns of ₦293 million and US $170,180.00. However, assessment by the FIRS revealed that the shipping company should have made returns of ₦796 million and US $498,292.39. The audit started on June 07, 2016 and was concluded on March 20, 2017, a 10-month period. The case is unresolved and is on appeal at the Tax Appeal Tribunal (details are unavailable).
2. Case 2- a multinational company in the construction industry had declared combined tax returns of ₦1.6 billion for the period 2013-2014. However, assessment by the FIRS revealed that the company should have made returns of ₦3.4 billion, to which the company agreed. The audit started on August 07, 2015 and was concluded on June 27, 2016, an 11-month period.
3. Case 3- a multinational company in the manufacturing industry had declared combined tax returns of ₦1 billion for the period 2013-2015. However, assessment by the FIRS revealed that the company should have made returns of ₦1.2 billion, which the company complied with, an additional return of ₦116 million. The audit started on September 8, 2015 and was concluded on July 5, 2017, a 23-month period.
4. Case 4- a multinational company in the FMCG industry had declared combined tax returns of ₦1.9 billion for the period 2013-2015. However, assessment by the FIRS revealed that the company should have made returns of ₦2.7 billion which the company complied with, an additional return of ₦789 million. The audit started on November 19, 2015 and was concluded on February 28, 2017, a 15-month period.

5. Case 5- a multinational company in the distribution industry had declared combined tax returns of ₦59 million for the period 2012-2016. However, assessment by the FIRS revealed that the company should have made returns of ₦122 million, which the company complied with. The audit started on July 05, 2016 and was concluded on March 17, 2017, a 9-month period.

In Case 1, the FIRS demands circa 300 per cent increase in the tax returns of the taxpayer; in case 2, the FIRS obtained from the taxpayer a 200 per cent increase in tax returns of the taxpayer; in case 3, an additional 10 per cent was collected from the taxpayer; in case 4, the FIRS collected from the taxpayer an additional 40 per cent of tax initially returned; in case 5, the FIRS collected from the taxpayer an additional 200 per cent of tax initially returned by the taxpayer.

Summary of Data from Uganda

The information here represents analysed sample data received from the revenue authority of Uganda. As in the cases provided by Nigeria's tax authority, the Ugandan cases indicate a significant difference between the taxes returned by the companies and the amount assessed to be payable by the taxpayers after tax audits by the revenue authority.

1. Case.1- a multinational company in the construction industry returned nil returns for the 2011 and 2012 financial years. The URA assessed the taxpayer tax liabilities of UGX5.2 billion and UGX3 billion for the 2011 and 2012 financial years, respectively. Following legal battles in court, the taxpayer and the URA agreed to payment of the sum of UGX5.4 billion as settlement for the tax liabilities.
2. Case 2- a multinational company in the oil and gas industry returned the following tax returns, UGX2.3 billion and UGX1.9 for the 2013, and 2014 financial years, respectively. The returned sum by the taxpayer for those

years totalled UGX4.2 billion. The URA assessed the taxpayer additional taxes of UGX963 million and UGX2.5 billion, for the financial years 2013 and 2014, an additional total amount of UGX3.5 billion, which the taxpayer agreed to and subsequently returned. Thus, total tax returns paid by the taxpayer for the years amounted to UGX7.7 billion.

3. Case 3- a multinational company in the manufacturing industry returned the following tax returns, UGX1.7 billion, UGX16 million, UGX2.5 billion, UGX3 billion and UGX4 billion for the 2009, 2010, 2011, 2012 and 2013 financial years, respectively. The returned sum by the taxpayer for those years totalled UGX11 billion. After transfer pricing adjustments, the URA assessed the taxpayer additional taxes of UGX214 billion, UGX286 million, UGX229 million UGX179 million and UGX155 million for the financial years 2009, 2010, 2011, 2012 and 2013, respectively, an additional total amount of UGX1.1 billion, which the taxpayer agreed to and subsequently returned. Thus, total tax returns paid by the taxpayer for the years amounted to UGX12 billion.
4. Case 4- a multinational company in the services industry returned the following tax returns, UGX40 million, UGX64 million, UGX76 million, UGX138 million and UGX82 million for the 2009, 2010, 2011, 2012 and 2013 financial years, respectively. The returned sum by the taxpayer for those years totalled UGX400 million. After transfer pricing adjustments, the URA assessed the taxpayer additional taxes of UGX40 million, UGX152 million, UGX252 million, UGX296 million and UGX370 million for the financial years 2009, 2010, 2011, 2012 and 2013, respectively, an additional total amount of UGX1 billion, which the taxpayer agreed to and subsequently returned. Thus, total tax returns paid by the taxpayer for the years amounted to UGX1. 5 billion.
5. Case 5[364]- a multinational company in the food and beverages industry returned the following tax returns, UGX0, UGX402 million, UGX444 million, and UGX1.5 billion for the 2013, 2014, 2015, and 2016 financial years, respectively. The returned sum by the taxpayer for those years

[364] Reported as Case 9 in the populated dataset returned by the URA.

totalled UGX2.4 billion. After transfer pricing adjustments, the URA assessed the taxpayer additional taxes of UGX835 thousand, UGX436 million, UGX444 million, and UGX1.5 billion for the financial years 2013, 2014, 2015, and 2016 respectively, an additional total amount of UGX2.4 billion which the taxpayer agreed to and subsequently returned. Thus, total tax returns paid by the taxpayer for the years amounted to UGX4.8 billion.

In Case 1, the URA collected UGX5,414,252,777 in tax revenue, which had not been returned or declared prior by the taxpayer; in case 2, the URA collected from the taxpayer an 80 per cent increase in tax returns; in case 3, an additional 10 per cent was collected from the taxpayer; in case 4, the URA collected from the taxpayer an additional 370 per cent of tax initially returned; in case 5, the URA collected from the taxpayer an additional 200 per cent of tax initially returned by the taxpayer.

How Significant and Damaging is Transfer Mispricing?

What is the scale of transfer mispricing by MNEs? From the sample data provided, it could be as high as 300 per cent of potential tax revenue. The sample being anecdotal, broad conclusions are not warranted. However, the sample reflects claims made in the literature on IFFs, especially the literature on the commercial component of IFFS.[365] The commercial component of IFFs includes transfer mispricing.[366] McKenzie argues that the commercial component of IFFs amounts to 60-65% of the global total.[367]

To arrive at an estimate for transfer mispricing on the African continent, a 2008 study by Ndikumana and Boyce put illicit flows from 40 sub-Saharan African

[365] Chapter 5 of the thesis discusses IFFs, making a case for the inclusion of tax avoidance in the definition of IFFs.
[366] The components of IFFs are commercial component- manifested in trade mispricing, transfer mispricing, base erosion and profit shifting and tax evasion; criminal component- drugs, arms and human trafficking, oil and mineral theft; and the corruption component.
[367] Rex McKenzie, 'The Africa Rising Narrative-Whither Development" (2016) Economics Discussion Papers, No 9, School of Economics, Kingston University London. (estimating the corruption component of IFFs as 3% and the criminal component as 30–35% of the global total).

countries between 1970 and 2004 at USD$420 billion in 2004 dollars.[368] The Mbeki Report puts the yearly value of IFFs out of Africa at USD$50 billion.[369] As a percentage of gross domestic product (GDP), sub-Saharan Africa sustains the biggest loss, with IFFs averaging 5.5% of GDP, in excess of the global average of 3.9%.[370]

In sub-Saharan Africa, West Africa, led by Nigeria, leads the continent in terms of volume of IFFs. Nigeria accounts for a large percentage of the IFFs out of sub-Saharan Africa.[371]. For example, GFI in 2010 reported that illicit financial flows out of Nigeria were: USD$6.3 billion in 2000; USD$5.4 billion in 2001; USD$5.1 billion in 2002; USD$9.7 billion in 2003; USD$15 billion in 2004; USD$18.7 billion in 2005; USD$23 billion in 2006; USD$34.7 billion in 2007; USD$51.7 billion in 2008.[372]

Adopting the claim by the Mbeki Report that Africa loses conservatively, US$50 billion per annum to illicit financial flows and applying the lower rate of 60% stated by McKenzie,[373] to the US$50 billion, US$30 billion is lost to the commercial component of illicit financial flows. If 20% of the US$30 billion is as a result of transfer mispricing, which is a conservative estimate, US$6 billion would be lost

---

[368] Leonce Ndikumana & James Boyce, "New Estimates of Capital Flight from Sub-Saharan African Countries: Linkages with External Borrowing and Policy Options" (2008) Political Economy Research Institute Working Paper Series, No 166, University of Massachusetts: Amherst, at 6.

[369] United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf.

[370] Dev Kar & Joseph Spanjers, "Illicit Financial Flows from Developing Countries 2003-2012" (2014) Global Financial Integrity, Washington DC; Global Financial Integrity, "Illicit Financial Flows to and from Developing Countries: 2005-2014" (2017) Washington DC: Global Financial Integrity.

[371] Leonce Ndikumana & James Boyce, "Capital Flight from Africa: Updated Methodology and New Estimates" (2018) Political Economy Research Institute (PERI) Research Report, University of Massachusetts: Amherst; Leonce Ndikumana & James Boyce, "Public Debts and Private Assets: Explaining Capital Flight from Sub-Saharan African Countries" (2003) World Development, Vol 31, Issue 1, at 107–130.

[372] Global Financial Integrity, "Illicit Financial Flows from Africa: Hidden Resources for Development" (2010). Washington DC: Global Financial Integrity; Global Financial Integrity, "Illicit Financial Flows to and from 148 Developing Countries: 2006–2015" (2019) Washington DC: Global Financial Integrity.

[373] Petty, supra, at note 241.

yearly out of Africa as a result of transfer mispricing. At the 2008 estimate of USD$51.7 billion, transfer mispricing out of Nigeria may amount to more than USD$6 billion a year. This is significant for a country whose total yearly budget is under USD$30 billion.

The numbers on IFFs above should be treated with caution, as they may be either conservative or exaggerated, depending on the dataset used. Due to their limitations, experts call for caution and conservative approaches in their use. For developing countries, some have argued that data on IFFs from developing countries is unreliable.[374] This is largely because the data used to measure IFFs is fraught with problems, such as the secret nature of the illicit activities, under-reporting of the illicit activities, especially in African countries.[375] Notwithstanding the accuracy or otherwise of the data available, there are strong arguments that commercial practices of MNEs contribute significantly to the amount of IFFs.[376]

In conclusion, despite the absence of conclusive data and empirical work in this field, there appears to be consensus that the current global tax system creates the opportunities for low profit to be declared in the countries where economic activities occur. The nature of the OECD BEPS projects indicates the clear existence of a problem, even if the exact scale is immeasurable.[377] Low profits declared in the countries where the economic activities occur could be interpreted as lost billions of dollars that would have assisted these countries in the provision of social amenities and needed infrastructure. Some authors argue that these flows out of Nigeria and Africa reduce the funds available to provide infrastructure, social goods, public services and other development needed by these countries.[378]

---

374 Alessandra Fontana, "'What does not get Measured, does not get done'. The Methods and Limitations of Measuring Illicit Financial Flows" (2010) U4 Brief, Chr. Michelsen Institute.
375 Ibid.
376 Thomas Torslov, Ludvig Wier & Gabriel Zucman, "The Missing Profits of Nations" (2018) NEBR Working Paper, No 24701.
377 Reuven, supra note 33.
378 Ikechukwu Acha, Essien Akpanuko & Okaro Unuafe, "Illicit Financial Outflows from Africa and Their Developmental implications: Experience from Nigeria" (2013) Management, Vol 3, No 7,

Conclusion

The base erosion and shifting of profits among taxing jurisdictions have both domestic and international influences, though there exists an interplay between both. At the international level, tax treaties and the international tax standards, contained in tax guidelines, recommendations, manuals, practices, etc. are the enablers of this erosion of tax bases and profit shifting activities of multinationals.[379]

In this chapter, I discussed the foundational principles accountable for transfer mispricing on the continent: the separate entity principle and the arm's length principle. In the next chapter, I discuss the reform processes taking place to address the base erosion and profit shifting of profits activities of MNEs as a result of the application of article 9 of model tax treaties.

at 417–426; Amah Ogbonnaya & Okezie Ogechukwu, "Impact of Illicit Financial Flow on Economic Growth and Development: Evidence from Nigeria" (2017) International Journal of Innovation and Economic Development, Vol 3, Issue 4, at 1933; RexMcKenzie, supra note 366.

379 Sebastian Beer & Jan Loeprick, "Profit Shifting: Drivers and Potential Countermeasures" (2013) WU International Taxation Research Paper Series, No 3. The paper's hypothesis is that MNEs operating in industries and countries with more opportunities and incentives to shift profits post a lower share of earnings in their subsidiaries operating in high tax jurisdictions.

Chapter 3: Simplified Alternatives to Transfer Pricing and Global Efforts at Addressing Tax Avoidance

1. Introduction
   - 1.1 Executive Summary of the Chapter
   - 1.2 Objectives of the Chapter
   - 1.3 Outline of the Chapter

2. Simplified Measures used by Countries
   - 2.1 Safe Harbours
   - 2.2 Alternative Corporate Minimum Tax
   - 2.3 Fixed Margin System
   - 2.4 The Sixth Method
   - 2.5 Use of Secret Comparables
   - 2.6 Advance Pricing Agreements

3. Reforming the Present System of International Taxation
   - 3.1 The OECD'S BEPS Project and 2017 Transfer Pricing Guidelines
   - 3.2 The UN's Reforms
   - 3.3 The EU's CCCTB
   - 3.4 Reform Efforts by the African Tax Administration Forum (ATAF Reforms)

4. Other Collaborative Efforts at Reforming the Present System of International Taxation
   - 4.1 International Monetary Fund's Papers
   - 4.2 Independent Commission for the Reform of International Corporate Taxation's Papers
   - 4.3 BEPS Monitoring Group's Reports

5. Conclusion

1. Introduction

a. Executive Summary of the Chapter

This chapter is split into two parts. The first part discusses simplified alternatives to the full application of transfer pricing. Many of the alternatives are embedded within the current tax system, based on the determination of the arm's length price for transactions between related entities through application of transfer pricing rules. What they offer are simple ways of arriving at the determination of the arm's length price. The alternative corporate minimum income tax, however, ignores the need to arrive at the arm's length principle. It does not recognize deductible expenses or costs, neither does it tax the profit of the company. It taxes a company on its turnover before expenses or interests are deducted.

The second part of the chapter examines ongoing global efforts at addressing the erosion of tax bases of countries and shifting of profits from high tax jurisdictions to low or no tax jurisdictions. In this part, I present efforts by the OECD, the United Nations and the Platform for Collaboration on Tax (PCT), through revised model conventions, transfer pricing guidelines and practical manuals, to improve the global tax system.

At the continental level, the African Tax Administrations Forum (ATAF) has over the years provided tools and solutions to aid African tax administrators better administer the international tax rules, with the goals of increasing revenue collection and stemming profit shifting.

b. Objectives of the Chapter

The tax law treatment of MNEs as separate entities for tax purpose and the insistence on the arm's length principle have failed to reconcile with the changing times and the economic model of business today. The effect of this misalignment has meant that companies continue to erode tax bases and shift profits, notwithstanding the wide reforms taking place globally and locally. At the end of this chapter, I make the case that the broad reforms in the last decade have failed to significantly address base erosion and profit shifting, hence, the need for fundamental change.

c. Outline of the Chapter

This chapter proceeds as follows. Section 2 discusses some of the simplified measures observed in practice. These simplified measures are introduced to ameliorate the experiences of tax administrators and taxpayers when interacting with the current global tax system. Section 3 discusses the recent efforts by the OECD, UN, EU and the ATAF to improve the global tax system. Finally, section 4 discusses other collaborative efforts such as the PCT, the IMF, ICRICT, all geared at improving the global tax system.

2. Simplified Measures used by Countries

To mitigate the challenges of applying the arm's length principle to income allocation, primarily through the application of the OECD's transfer pricing methodologies in ascertaining arm's length price of goods and services transferred among related entities, tax authorities in some jurisdictions apply simplified alternatives to transfer pricing. These simplified alternatives reduce the need for taxpayers to conduct comparability analysis for each related party transaction, alongside preparing detailed transfer pricing documentation, in a bid to justify the price fixed for goods and services transferred among related entities. In most cases, they bring simplicity, certainty and predictability to tax administration and compliance. In this section, I shall discuss briefly some of these simplified measures and their contribution to improving the global tax system.

2.1 Alternative Corporate Minimum Tax

A suggested substitute for strict application of the arm's length principle to corporate income allocation across jurisdictions is the alternative corporate minimum tax (ACMT). Michael Durst in his 2019 book, advocates for lower-income countries to adopt ACMT when taxing MNEs that do business in their jurisdictions.[380]

An ACMT would typically impose tax at a low rate (such as 1 percent) on the gross revenue of companies carrying on business within the jurisdiction. Usually, corporate taxes are imposed at higher nominal rates on the net profit of a company, i.e. profit after accounting for expenditure, deductions and interest.[381] Under an ACMT, the tax is on the total revenue (turnover) of the company before any deductions. The ACMT is owed if it is higher than the taxpayer's regular tax liability (i.e. what the taxpayer would have paid if the normal corporate tax of the jurisdiction applied).[382]

Durst argues that an ACMT serves as a tool for limiting base erosion and profit shifting.[383] This is because since an ACMT is a tax on turnover and not profit, expenses, interest and other transfer pricing cost, which are subject to manipulation, are not taken into account.[384] An ACMT is efficient in terms of tax administration, especially for African countries. Given the challenges of applying the arm's length standard to related party transactions and the potential for transfer mispricing, an ACMT presents a predictable, simple and effective way of revenue collection.[385] For the taxpayer, the cost of compliance is significantly reduced. Accounting cost is reduced since the taxpayer only has to ascertain its turnover for the fiscal year and apply the minimum tax to it. For the tax authority, cost and burden of administration and audit are significantly reduced, since tax

[380] Michael Durst, "Taxing Multinational Business in Lower-Income Countries: Economics, Politics and Social Responsibility" (2019) Institute of Development Studies.
[381] The nominal or statutory rate is distinct from the effective tax rate on the profit of the taxpayer. For example, the statutory corporate income tax rate in Nigeria is 30 percent while the effective tax rate is approximately 6 percent. Source needed for the 6% estimate. Is that for all companies? Usually we see higher effective rates for some industries than others.
[382] Durst, supra note 379 at 96.
[383] Ibid at 97.
[384] Ibid at 98,
[385] Ibid at 96.

audit is focused on the turnover of the taxpayer and not the transactions or profit.[386] Applying the minimum tax to the turnover is easy to administer.[387]

A disadvantage of the ACMT is that since it is tax on turnover, investors are exposed to risk of taxation even where they have not made economic profit.[388] This is particularly problematic for many African countries where doing business is relatively expensive and companies have to provide their own infrastructure.[389] This explains why governments grant tax incentives to companies for years to recoup their initial investments.[390] It explains why companies make losses or low profits over a longer period than their counterparts in other developed countries.[391] Durst admits that the AMCT is economically inefficient.[392]

The AMCT could be a disincentive to invest in a country as it departs from business expectations of investors and known tax practices of countries. It is vulnerable to underpricing of goods and services, which reduces the tax revenue of the tax jurisdiction.

However, for African governments that suffer significantly from the erosion of their tax bases and shifting of profits out of their jurisdictions, the inconvenience and potential inefficiency of applying this alternative would appear to be a small cost to bear compared to their experience under the current transfer pricing rules. In addition, taxpayers who have genuine cases can appeal to the tax authority or tax tribunal for review of their tax liability or position. Finally, given that 19 countries, as reported by Durst, have some version of an ACMT in their tax

[386] Ibid at 96.
[387] Ibid at 96
[388] Ibid at 98.
[389] Acha Leke, Mutsa Chironga & Georges Desvaux, "Africa's Business Revolution: How to Succeed in the World's Next Big Growth market" at 19. (Harvard Business Review Press, Boston Massachusetts, 2018)
[390]IMF, OECD, UN & World Bank (2015) Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment, Report to the G-20 Development Working Group, 15 October 2005, Washington: International Monetary Fund
[391] Ibid.
[392] Ibid at 98.

regimes, Durst argues that countries see the ACMT as a promising model for corporate taxation.[393]

Before discussing the next alternative, Durst has proposed a radical alternative- the complete abandonment of the corporate income tax regime. Durst advocates a shift from reliance on corporate income tax to other alternative revenue sources, "which may well offer greater prospects for substantial revenue gains, even if BEPS reforms can be successfully implemented."[394]

Durst claims that the effectiveness of corporate income tax lies in the ability of the tax administration to enforce the fair market valuation (arm's length pricing) of goods and services that are sold between related parties.[395] He highlights two limitations of the corporate income tax as: small valuations in product prices can lead to very large understatements of a taxpayer's tax liability; and corporate income tax is much more vulnerable to avoidance through incorrect valuations than alternative kinds of taxes that governments might use to raise revenue from MNEs operating in their countries, including excise taxes and ad valorem royalties on extracted natural resources.[396]

---

[393] Some of the countries are Cambridia, Cameroon, Chad, Gabon, Guina, Guyana. See, Michael Durst (2019) at 97. Best, Brockmeyer, Kleven & Soinnewijn, "Production versus Revenue Efficiency with Limited Tax Capacity: Theory and Evidence from Pakistan" (2015) 123 Journal of Political Economy, 1311.
[394] Durst, supra note 31.
[395] Ibid at 9.
[396] Ibid at 10.

Durst mentions increased use of excise taxes[397] and royalties[398] as alternatives to corporate income tax.[399] He is convinced they offer more effective ways of taxing revenue gains from extracted natural resources.[400]

It should be stated here that the imposition of corporate taxes on companies is essential attribute of its treatment as juristic personalities, similar to the imposition of personal income taxes on individuals.[401] Taxing companies on their income acknowledges that they benefit from the infrastructure of the jurisdiction where they carry on business and they contribute to the cost of providing and maintaining the infrastructure. Excise taxes paid by taxpayers are in many cases, transferred to the final consumer as increased cost of the goods sold. As such, companies do not bear the burden of excise taxes. Royalties, on their part, may be argued to be non-tax payment for the value and volume of extracted natural resources, and not for being resident in a country or obtaining and the status of being a legal person.[402]

Notwithstanding the arguments above, Durst's radical recommendations provide useful policy considerations for African countries, which are resource-rich.

2.2 Safe Harbours

A suggested simplified measure to the strict application of the arm's length principle is the application of safe harbor rules. A safe harbor is an administrative

[397] Excise taxes are taxes imposed on manufactured goods. In some instances, they are imposed on goods such as cigarettes, alcohol, gambling, gasoline, as a way of discouraging their use and generating significant revenue for the government. When used this way, they are described as "sin taxes".
[398] A royalty tax is tax paid to the owner of an asset (tangible or intangible) for the right to ongoing use of the asset. For example, companies in the oil and gas industry in Nigeria are required to pay royalties to the Federal Government of Nigeria.
[399] Ibid at 10. Durst recommends two legal reforms: revising transfer pricing rules to focus more on the actual geographic locations of the group members' business activities; strengthening of the CFC rules, removing from multinational groups the financial incentive for income shifting.
[400] Ibid at 11.
[401] See the discussion in chapter 2 above on the legal personality of companies.
[402] Bryan Land, "Resource Rent Taxes: A Re-appraisal" (2010) in P Daniel, M. Keen & C. McPherson eds., The Taxation of Petroleum and Minerals: Principles, Problems and Practice, Routledge.

simplification which is in principle optional for taxpayers. It consists for instance of a simplification when determining arm's length prices by using a pre-established transfer pricing method and margin rates and/or of an alleviation of the transfer pricing documentation requirement.[403]

The OECD, in its 2017 TPGs, defines a safe harbour as "a provision that applies to a defined category of taxpayers or transactions and that relieves eligible taxpayers from certain obligations otherwise imposed by a country's general transfer pricing rules".[404] It may be defined as the "full or partial exemption of a group of taxpayers or transactions from specified TP compliance requirements(s), anchored on the use of pre-established transfer pricing method or financial indicators (price, margin, rates, etc.)."[405] From the definitions, a safe harbor regime may be described as a tool for simplifying the administration of a transfer pricing regime. This it achieves by exempting eligible taxpayers or transactions from transfer pricing rules or documentation preparation; prescription of the transfer pricing method to be used by taxpayers and the financial indicators to be applied; or mere prescription of financial indicators to taxpayers, which will be deemed as acceptable to the tax authority.

Safe harbor regimes have important benefits for taxpayers in African countries. First, they simplify compliance process and reduce compliance costs.[406] Where a taxpayer adopts the safe harbor regime and complies with its provisions, the taxpayer may not be required to prepare transfer pricing documentation, which

[403] Alain Charlet, Caroline Silberztein & Gerard Pointe, "Transfer Pricing Study on the Feasibility of Introducing Safe Harbour Provisions in ECOWAS Countries: Results and Analysis of the Questionnaires Sent to Governments, Businesses and the Civil Society" (Luxembourg: Publications of the European Union, 2016).

[404] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para 4.102 at 205.

[405] Definition offered by Mr. Matthew Gbonjubola at the June 2017 International Tax Conference, organized by the ICTD in Lagos, Nigeria. The UN Practical Manual defines safe harbor rules as provisions whereby if a taxpayer's reported profits are within a certain range or percentage or under a certain amount, the taxpayer is not required to follow a complex and burdensome rule, such as applying the transfer price methodologies. See, United Nations (2017) Practical Manual on Transfer Pricing for Developing Countries (2017) Department of Economic & Social Affairs. United Nations: New York, para B.1.7.6 at 49.

[406] Para 4.107 of Section E, Chapter IV of OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017

are time-consuming, very expensive and complex. Because the safe harbor regime already prescribes pre-established transfer pricing methodologies or margin rates, all that is required of the taxpayer under the safe harbor regime is to come under the prescriptions. A taxpayer that has complied with the provisions of the safe harbor regime is protected from audit or investigation by the tax authority.[407] The tax authority, however, may conduct a limited audit to ensure that the taxpayer has met the eligibility conditions of the safe harbor regime and complied with the safe harbor provisions. This arrangement provides certainty of tax treatment for the taxpayer, who is confident of the treatment of his tax affairs. This encourages investment by investors as the ease of doing business provided by the tax certainty is essential for investment decision-making by potential investors.

For tax authorities, safe harbor regimes significantly reduce administrative costs related to transfer pricing audits and /or litigation.[408] This causes tax authorities to redirect the limited resources to other transactions or taxpayers, not covered by the safe harbor regime, which are usually more complex or higher risk transactions and large taxpayers.[409] Given the dearth of skilled capacity in most tax administrations of African countries and heavy reliance on a few well-trained individuals, this saving is important in managing scarce resources and distributing them to more important sectors, industries or taxpayers.[410]

The Platform for Collaboration on Tax (PCT)— a joint initiative of the IMF, OECD, United Nations (UN) and World Bank Group— argues that a merit of the safe harbor regime is that it reduces the need to find data on comparables and to perform a benchmarking study, in every case.[411] It states that "carefully constructed safe harbours could be particularly useful for common types of

[407] Para 4.108 of Section E, Chapter IV of OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017
[408] Para 4.109 of Section E, Chapter IV of OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017
[409] Ibid.
[410] Ibid.
[411] The Platform for Collaboration on Tax, "A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses" (2017) Platform for Collaboration on Tax. Washington, D.C.: World Bank Group, Part IV, at 69.

transactions where comparables information is unavailable or unreliable.[412] This is particular important for African countries that struggle with finding comparables or accessing relevant data for their transfer pricing practice.

The safe harbor regime represents a trade-off between strict adherence to the use of the arm's length standard and ease of administration, thus being attractive to both taxpayers and tax authorities. It replaces the need to go through a rigorous assessment of transactions using the complex transfer pricing methodologies to arrive at the arm's length price for products sold and services performed.[413]

Safe harbours have disadvantages, influencing their cautious adoption by countries.[414] First, there is the possibility of double taxation.[415] Double taxation in a safe harbor regime arises where one party to tax treaty unilaterally enacts a safe harbor regime for eligible taxpayers, while the other proceeds to carry out corresponding adjustment of the taxpayer's returns, in line with article 9(2) of the model tax treaty, without taking into account the safe harbor regime of the first contracting party. This is likely to occur since treaties empower tax jurisdictions to adjust the returns of covered taxpayers to achieve an arm's length price.[416] Because safe harbor regimes provide for pre-established methods or rates, the other contracting party may not accept the pre-established methods or rates or may be unaware of them.

412 The Platform for Collaboration on Tax, "A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses" (2017) Platform for Collaboration on Tax. Washington, DC: World Bank Group, Part IV, at 83.
413 Victor Adegite & Ngozi Onyebezie, "Nigerian Transfer Pricing Safe Harbor Provisions Revisited" (2019) Tax Notes International, online: <https://www.taxnotes.com/tax-notes-international/compliance/nigerian-transfer-pricing-safe-harbor-provisions-revisited/2019/03/25/296k9>
414 OECD (2012) "Multi-Country Analysis of Existing Transfer Pricing Simplification Measures-2012 Update" (2012), OECD Publishing, Paris.
415 OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para E.4.110.2, Ch. IV, at 208.
416 Article 9 (1) of the OECD MTC.

Another suggested disadvantage of safe harbour regimes is that they do not strictly comply with the arm's length standard.[417] Given that pre-established methods and rates are prescribed for eligible taxpayers, it eliminates the search for actual comparables by the taxpayer and tax authorities. It eliminates the individual facts and circumstances analysis of each transaction between related entities, a hallmark of the arm's length principle.[418] While the two parties may come to a price acceptable to both of them, however, such price may not be the market/arm's length price for the transaction, in question, and may not reflect actual economic relations between associated enterprises.

The OECD strongly held this view (and still does especially in cases where a jurisdiction unilaterally enacts a safe harbor regimes), which accounted for its unsupportive stance towards safe harbor regimes until recently.[419] However, the arm's length standard is not a scientific exercise; instead it depends on the basic fiction of treating commonly controlled companies as separate and independent. A system that achieves certainty, predictability, saves cost and approximates to the arm's length price is preferable even if it does not strictly comply with the arm's length principle.

A third disadvantage of a safe harbor regime is that it may create discriminatory or distortionary effects, if not well-managed. Selecting a category of taxpayers or transactions to benefit from the safe harbor regime may be viewed by taxpayers not covered as giving undue advantage to others.[420] This could distort the economy of the country, as investors may be influenced by the presence of a safe harbor regime in deciding which industry or sector of the industry to invest in.[421] The

[417] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para E.4.110.1, Ch. IV, p 208.
[418] Tommaso Faccio & Sol Picciotto, "Alternatives to the Separate Entity/Arm's Length Principle for Taxation of Multinational Enterprises" (2017) ICRICT Briefing Paper, at 25.
[419] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para E.4.110.1, Ch. IV, at 208.
[420] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para E.4.110.4, Ch. IV, at 208.
[421] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para. E.4.110.4, Ch. IV, at 208.

effects of this on the economy of a country are obvious, since other sectors or industries may remain untapped or neglected.

Furthermore, a safe harbor regime may provide opportunities for aggressive tax planning and transfer pricing manipulations.[422] Tax planners may arrange their affairs to come under the category of transactions or taxpayers on paper while in effect, conducting other transactions. Prescribing pre-established rates or methods may lead to creative devices by taxpayers to fall within the pre-established margins, even though that may not be the case.

Notwithstanding the advantages of adopting and implementing safe harbor regimes, the cost-saving and simplicity attributes of them make them attractive to African tax administrations as strong policy considerations.

2.3 Fixed Margin System

Similar to the discussion on safe harbours above, fixed margin system presents a simplified measure. This system, practiced in Brazil, substitutes the need for comparable transactions with fixed margins for gross profits and markups.[423] The fixed margin could be a percentage of the production cost or resale price, as acceptable profit margin to be made by the company on given transactions. This effectively combines the application of the conventional transfer pricing methods (specifically, cost plus method and resale price methods) with fixed margins.[424] These fixed margins are applied to different economic sectors, approximating as close as possible to the industry price.[425]

---

[422] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para. E.4.110.3, Ch. IV, at 208.

[423] Faccio, supra note 415.

[424] Marcos Valadao, "Some Comments on Brazilian TP System with Fixed Margins for the Resale Price Method (RPM) and Cost Plus Method (CPM)", online publication of Tax Justice Network: <https://www.taxjustice.net/cms/upload/pdf/Marcus_Valadao_text_1206_Helsinki.pdf>

[425] Deloitte, "Doing Business in Brazil" (2017), Deloitte, online: <https://www2.deloitte.com/content/dam/Deloitte/br/Documents/doing-business/Doing-Business-Brazil-Deloitte-Corporate-Taxation-Indirect-Taxes.pdf>

By applying widely-applicable fixed margins to all transactions, this approach eliminates the burden of seeking specific comparables on a case by case basis.[426] This prevents discrimination against taxpayers since all taxpayers are subject to the same tax burden and treatment. The fixed margin strategy offers predictability and certainty to the taxpayers, while easing the enforcement burden on the tax administration.[427]

The limitation of the fixed margin approach is that it provides a "one size fits all" approach in dealing with taxpayers.[428] This broad-brush approach to transfer pricing may not account for the individual circumstances of a taxpayer. To address this, a taxing jurisdiction may put in place review mechanisms for aggrieved or dissatisfied taxpayers to present their unique positions. For example, Brazil's tax laws allow for the modification of the fixed margins where a taxpayer can prove, accompanied by relevant documentation, that the margin used by the taxpayer approximates that used by unrelated parties under comparable circumstances.[429]

2.4 The Sixth Method

In addition to the substitute and simplified measures discussed above, the sixth method presents an additional alternative to the strict application of the arm's length principle. This method uses quoted prices on a material exchange as benchmarks for ascertaining the arm's length price of commodities exported from a country.[430] It does away with the need for comparability analysis as publicly quoted prices are relied on for commodities.[431] The Sixth Method promotes

[426] Faccio, supra note 415 at 25.
[427] Marcos Valadao, "Developing Countries and the Contemporary International Tax System: BEPS and other Issues" (2019) South Centre Tax Cooperation Policy Brief No 7.
[428] Tatiana Falcao, "Brazil's Apprach to Transfer Pricing: A Viable Alternative to the Status Quo?" (2012) Bloomberg, BNA, Tax Management Transfer Pricing Report, Vol 20, No 20.
[429] Article 20 of Law 9430, as amended; Isabel Calich & Joao Rolim, "Transfer Pricing Disputes in Brazil" (2012) in Eduardo Baistrocchi & Ian Roxan eds., Resolving Transfer Pricing Disputes, (Cambridge: Cambridge University Press,2012) at 519–554.
[430] UN Practical Manual on Transfer Pricing for Developing Countries, (New York: United Nations, 2017) para B.1.5.10.
[431] UN Practical Manual on Transfer Pricing for Developing Countries, (New York: United Nations, 2017) para B.3.4.1.3.

transparency, reliability, simplicity, certainty and predictability.[432] It is often used for specified commodities and is common in countries such as Argentina, Brazil, the Dominican Republic and El Salvador.[433]

However, the sixth method is not fool-proof. It does not account for variations in quality and volume of the commodity transferred, trade terms, shipment costs, local circumstances, risk coverage and individual circumstances.[434] It is vulnerable to tax planning.[435] This occurs where, for example, an affiliate producing commodity for export sells the commodity to a related entity offshore (usually in a low tax jurisdiction) without the commodity being shipped out of the country of origin.[436] The new buyer advances to sell the commodity to a third party for a higher price than the first transaction and ships the commodity abroad.[437] In the transaction described above, usually the shipment date differs from the date of the original sale, and as such a different price (in most cases, a higher price) is declared as the transfer price of the commodity.[438]

Victor Adegite of KPMG Nigeria, opines that the sixth method "targets a fact pattern where an associated enterprise, engaged in the business of exporting commodities, invoices an associated enterprise related to the sale of the

432 UN (2017) Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations, para B.3.4.1.5; Alexandra Readhead, "Special Rules for Commodity Sales: Zambia's Use of the 'Sixth Method" Natural Resource Governance Institute Case Study, online: <https://resourcegovernance.org/sites/default/files/documents/special-rules-for-commodity-sales-zambia-sixth-method.pdf>

433 UN (2017) Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations, para B.3.4.2.1.1.

434 Cooper, supra note 24.

435 Fleming, et.al define tax planning as a strategy which involves "a higher-tax affiliate making deductible payments to a low-or zero-tax affiliate to reduce the MNE's global effective tax rate and, in the process, erode the corporate tax bases of countries where its economic activity otherwise would be more highly taxed". See, Clifton Fleming, Robert Peroni & Stephen Shay, "Getting Serious about Cross-Border Earnings Stripping: Establishing an Analytical Framework" (2015) North Carolina Law Review, Vol 93 at 673. See Joe Andrus & Paul Oosterhuis, "Transfer Pricing After BEPS: Where Are We and Where Should We Be Going?" (2017) Taxes-The Tax Magazine, Vol. 95, Issue 3.

436 Victor Adegite, "Nigerian Perspectives on UN Transfer Pricing Manual" (2017) in Tax Management Transfer Pricing Report, Vol. 26, No. 14, Bloomberg BNA

437 Ibid.

438 Ibid; Veronika Solilova & Danuse Nerudova, "Sixth Method as a Simplified Measurement for SMEs?" (2015) European Financial and Accounting Journal, Vol 10, No 3 at 45–61.

commodities, yet ships the commodities to a different party in another jurisdiction."[439] To address profit shifting in such transactions, the quoted price on the day of shipment is relied on by tax authorities as the intercompany price between related entities, prior to the sale to unrelated entities.[440] In some jurisdictions, the higher of the intercompany price and the shipment price is adopted as the transfer price between related entities.[441]

2.5 Use of Secret Comparables

In addition to the alternatives above, some countries adopt the use of secret comparables in transfer pricing assessment.[442] This is aimed at addressing the paucity of comparables required for comparability analysis or setting the benchmarks.[443] These secret comparables, unavailable to the taxpayer under review, are derived from returns of other taxpayers and used in determining the arm's length prices in specific transactions.[444] In some instances, such as in Peru, they are used to determine which taxpayers should be inspected.[445]

---

[439] Adegite, supra note 433.
[440] UN (2017) Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations, para. B.3.4.2.1.3.
[441] Veronica Grondona, "Transfer Pricing: Concepts and Practices of the 'Sixth Method' in Transfer Pricing" (2018) South Centre Tax Cooperation Policy Brief No 2; Solilova supra note 435 at 45−61.
[442] EuropeAid & PWC (PricewaterhouseCoopers) "Implementing the Tax and Development Policy Agenda: Transfer Pricing and Developing Countries: Final Report". Brussels: EuropeAid and PWC, online:<https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/transfer_pricing_dev_countries.pdf> at 10, footnote 24. Wright, TN, "Kenyan Practitioner Decries Government's Aggressive Tactics in Transfer Pricing Audits" 2010, Tax Management Transfer Pricing Report 920, International Tax Centre, 13 January 2011. The Report mentions the use of secret comparables by the Kenya Revenue Authority to validate transfer pricing, "to the disadvantage of bona fide taxpayers that do not have access to such data and hence are not able to verify such comparisons".
[443] Joel Nitikman, "Obtaining Disclosure of Secret Comparables in Canadian Transfer Pricing Litigation: Policy and Practice" (2002) Canadian Tax Journal, Vol 50, No 1.
[444] OECD, "Transfer Pricing Comparability Data and Developing Countries" (2014) OECD Publishing, Paris, online: <https://www.oecd.org/ctp/transfer-pricing/transfer-pricing-comparability-data-developing-countries.pdf>.
[445] KPMG, "Global Transfer Pricing Review: Peru" (2015) KPMG, online: <https://home.kpmg/content/dam/kpmg/pdf/2015/10/tp-review-peru-v3.pdf>.

The use of secret comparables is adjudged to be incompatible with the arm's length principle.[446] The OECD discourages its use unless the data can be disclosed to the taxpayers, within the limits of confidentiality, so that they may evaluate it and defend themselves against an adjustment. [447]Countries are split on its use. [448]

Some jurisdictions, focused on maximizing revenue collection, have prioritized this approach for transfer pricing assessment. Countries which use secret comparables in transfer pricing assessment include China, Mexico, and Turkey. [449]

For countries opposed to its use, it is the kernel of the arm's length principle that taxpayers have access to the information necessary to defend their position.[450] This basic principle of "fair hearing" is denied a taxpayer where she is denied access to the data upon which an assessment has been made.[451] This arbitrary process by tax authorities places the taxpayer in a difficult position when challenging the findings of the tax authorities through a judicial review or any other legitimate appellate process.[452]

---

[446] KPMG, "Comments on the OECD Paper on Transfer Pricing Comparability Data and Developing Countries" (2014) KPMG, online: <https://home.kpmg/content/dam/kpmg/pdf/2014/04/oecd-transfer-pricing-comparability-data-april-2014.pdf>.

[447] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris, para A.4.3.3.36, Ch. III, at 158.

[448] Online: <https://tax.thomsonreuters.com/site/wp-content/pdf/transfer-pricing/Bloomberg-BNA-TP-Forum-Examines-Treatment-Of-Secret-Comparables.pdf> The article lists Austria, Belgium, Brazil, Denmark and France as some of the countries opposed to the use of secret comparables. India, Italy, Mexico and Australia are some of the countries which use secret comparables.

[449] Kevin Bell, "Bloomberg BNA Transfer Pricing Forum Examines Treatment of Secret Comparables" Thomson Reuters, online: <https://tax.thomsonreuters.com/site/wp-content/pdf/transfer-pricing/Bloomberg-BNA-TP-Forum-Examines-Treatment-Of-Secret-Comparables.pdf>

[450] PriceWaterHouseCoopers, "Commentary: Public Invitation to Comment on a Series of Draft Issue Notes" (2006), OECD, online: <https://www.oecd.org/tax/transfer-pricing/37854363.pdf>. Bloomberg BNA, Transfer Pricing Forum: Transfer Pricing for the International Practitioner" (2016), Bloomberg BNA, online: <https://www.nera.com/content/dam/nera/publications/2016/Article%20BBNA%20Madelpuech%20France%20Comparables.pdf>.

[451] UN (2017) Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations, para B.1.6.32.

[452] Waris, supra note 14 at 34; OECD, "Transfer Pricing Comparability Data and Developing Countries" (2014) OECD Publishing, Paris, online: <https://www.oecd.org/ctp/transfer-pricing/transfer-pricing-comparability-data-developing-countries.pdf>

Secret comparables "generates legal and economic uncertainty for taxpayers, which potentially precludes commitments with respect to investment decisions and business development".[453] Notwithstanding their shortfalls, they present much-needed data by tax authorities to comply with the arm's length standard or set necessary margins or benchmarks.[454]

2.6 Advance Pricing Agreements

Finally, advance pricing agreement (APA) provides an alternative to the strict application of the arm's length principle and is adopted by some tax jurisdictions to manage transfer pricing disputes and enforcement. An APA is a private agreement between a taxpayer and the tax authority.[455] It entails an ahead-of-time negotiation of the terms and price of the transfer of goods and services between related parties with the tax authority of the jurisdiction in question.[456] The agreement could be on the preferred transfer pricing methodology to be used by the taxpayer, price margins, acceptable rates or the process of arriving at the transfer price.

APAs are resource-efficient since an agreement covers a period of time, usually 3-5 years.[457] This allows for the unused resources in the coverage years to be channeled to other demanding areas.[458] It obviates the need to seek comparables

---

[453] EuropeAid and PWC (PricewaterhouseCoopers) "Implementing the Tax and Development Policy Agenda: Transfer Pricing and Developing Countries: Final Report". Brussels: EuropeAid and PWC, online: <https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/transfer_pricing_dev_countries.pdf>

[454] Norway v Total E&P Norge AS [2015] Supreme Court 2014/498, ref no. HR-2015-00699-A. In this case, the Supreme Court of Norway allowed the use of secret comparables though called for caution in its use so that the interests of each taxpayer are protected in a reasonable manner.

[455] Johannes Becker, Ronald Davies & Gitte Jakobs, "The Economics of Advance Pricing Agreements" (2014) CESifo Working Paper Series No 5079.

[456] Zvika Afik & Yaron Lahav, "Risk Transfer Valuation in Advance Pricing Agreements between Multinational Enterprises and Tax Authorities" (2016) Journal of Accounting, Auditing & Finance, Vol 31, No 2 at 203–211.

[457] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017, OECD Publishing, Paris, para F.1.4.134, Ch IV at 214

[458] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017, OECD Publishing, Paris, para F.1.4.155, Ch. IV at 214

for each transaction, at every financial year as the APA usually applies to a reasonable period of time. [459]

However, APAs have been accused of lacking transparency, as the agreements entered, in most cases, are confidential.[460] This creates the potential for "corporate capture".[461] The Luxembourg Leaks[462] revealed the danger of confidentiality in tax rulings or negotiations. Nigeria's transfer pricing regulations provide for an APA regime[463], though not fully in effect as at the time of writing.

3 Reforming the Present System of International Taxation

This section discusses some of the global tax reforms ongoing to improve the international tax rules, improve transparency and address the paucity of comparables.

3.1 The OECD'S BEPS Project and 2017 Transfer Pricing Guidelines

In 2012, the G-20 meeting in Los Cabos tasked the OECD to develop an action plan to address the corporate tax planning strategies by MNEs to erode tax bases and shift profits from high tax jurisdictions to low tax jurisdictions.[464] In 2013, at the St. Petersburg Summit, the G-20 approved the 15 Action Plans laid out at the

[459] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017, OECD Publishing, Paris, para F.1.4.153, Ch. IV at 214

[460] Kristin Hickman, "Should Advance Pricing Agreements be Published?" (1998) Northwestern Journal of International Law & Business, Vol 19, Issue 1.

[461] A situation where companies unduly influence the decisions and policies of public institutions. See, Lorraine Eden & William Byrnes, "Transfer Pricing and State Aid: The Unintended Consequences of Advance Pricing Agreements" (2018) Transnational Corporations, Vol 25, No 2, at 9–36.

[462] International Consortium of Investigative Journalists, "European Authorities Launch Probe into Secret Lux Leaks Tax Deal" (March 7, 2019) ICIJ Publications, online: <https://www.icij.org/investigations/luxembourg-leaks/european-authorities-launch-probe-into-secret-lux-leaks-tax-deal/.>; Simon Bowers, "Luxembourg Tax Files: How Tiny State Rubber-Stamped Tax Avoidance on an Industrial Scale" The Guardian (5 November 2014), online: <https://www.theguardian.com/business/2014/nov/05/-sp-luxembourg-tax-files-tax-avoidance-industrial-scale.>

[463] Income Tax (Transfer Pricing) Regulations, 2018, r 9.

[464] G20 (2012), "G20 Leaders Declaration" (2012) Mexico, online: <https://www.mofa.go.jp/policy/economy/g20_summit/2012/pdfs/declaration_e.pdf.>

Summit by the OECD.[465] According to the OECD, these actions plans set out to ensure that profits are taxed where the economic activities generating the profits are performed and where value is created.

In chapter 2, I discussed briefly the 15 Action Plans. In this section, I focus on some of the action plans pertinent to ameliorating the experiences of taxpayers and tax authorities with implementing the arm's length principle and applying transfer pricing methodologies.

i. Actions 8, 9, 10: Ensure that transfer pricing outcomes are in line with value creation[466]

This Action Plan recognises the limitations when implementing the arm's length principle and sets out to ensure that transfer pricing outcomes are in line with value creation. The OECD acknowledges that:

> "...multinationals have been able to use and/or misapply those rules to separate income from the economic activities that produce that income and to shift it into low-tax environments."[467]

It defines three areas of specific importance to Actions 8. 9, 10: the transfer of intangibles and other mobile assets for less than full value; the over-capitalisation of lowly taxed group companies; and contractual allocations of risk to low tax environments in transactions that would be unlikely to occur between related parties.

---

[465] G20 (2013), "Tax Annex to the Saint Petersburg G20 Leaders Declaration", G20 Information Centre. Online: <http://www.g20.utoronto.ca/2013/2013-0905-tax.html>; OECD (2014), Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project, OECD, online: <http://www1.oecd.org/ctp/beps-2014-deliverables-explanatory-statement.pdf.>

[466] OECD (2015), Aligning Transfer Pricing Outcomes with Value Creation, Actions 8–10 - 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online:<https://www.oecdilibrary.org/docserver/9789264241244en.pdf?expires=1554422010&id=id&accname=guest&checksum=5FAB11638FA8847653B9B8A606DE6821>.

[467] OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing, at 19, online: <https://www.oecd.org/ctp/BEPSActionPlan.pdf>.

Action 8, on intangibles, seeks to prevent BEPS, carried out through moving intangibles among group members.[468] This it seeks to achieve by: adopting broad definition of intangibles; assuring that transfer and use of intangibles are allocated to the jurisdiction or economic activities which created the value; developing rules or special measures for transfers of hard-to-value transactions; and updating guidance on cost contribution agreements.[469] These action plans are contained in a special report on Actions 8, 9, and 10[470] and reflected in the 2017 OECD TPGs.

Action 9 of the BEPS Project addresses the allocation of risks and over-capitalisation of group members. This involves preventing the accrual of inappropriate returns to an entity solely because it has contractually assumed risks or has provided capital. Action 9 recommends that returns from the assumption of risk should align with value creation. In addition, the work on Action 9 co-ordinates with the work on interest deductions and other financial payments.[471]

Finally, Action 10 deals with other high-risk transactions. This seeks to develop rules to prevent BEPS which arise from related entities engaging in transactions which would not occur, or rarely occur between unrelated parties. It prescribes rules for: clarifying the circumstances in which circumstances can be

---

[468] OECD (2014), Guidance on Transfer Pricing Aspects of Intangibles, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, online: <https://www.oecd-ilibrary.org/docserver/9789264219212-en.pdf?expires=1554423475&id=id&accname=guest&checksum=8A7BEF7BABF737D0531E33650F11DA67>

[469] OECD (2018), Guidance for Tax Administrations on the Application of the Approach to Hard-to-Value Intangibles-BEPS Actions 8-10, OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris, online: <www.oecd.org/tax/beps/guidance-for-tax-administrations-on-the-application-of-the-approach-to-hard-to-value-intangibles-BEPS-action-8.pdf>

[470] OECD (2015), Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241244-en.pdf?expires=1554422314&id=id&accname=guest&checksum=0D9C681CA9EF94590AE26C5931E3CB40>

[471] OECD (2015), Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241244-en.pdf?expires=1554422314&id=id&accname=guest&checksum=0D9C681CA9EF94590AE26C5931E3CB40>

recharacterized; clarifying the application of transfer pricing methods to profits arising out of global value chains, especially the use of the profit split method; allocation and measurement of management fees and head office expenses.[472]

These reforms are committed to ensuring that pricing methods will allocate profits to the most important economic activities. However, the focus on prices of transactions, and not on the global profits of the MNE, and the OECD's insistence on the arm's length principle, contradict the reform goals. Where the OECD is desirous of aligning where profits are allocated with where the economic activities occur, then it must abandon the arm's length principle, which is price-focused and focus on the global profits of the MNE.

ii. Action 11: Ensuring transparency while promoting increased certainty and predictability

The absence of data for comparables and information on the businesses and activities of taxpayer make tax compliance and administration difficult for both taxpayers and tax administrators. Over the years, global coordinated efforts to address this challenge have been established. One such effort is the establishment of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) by the OECD. The Global Forum, established in 2000 and restructured in 2009, creates the platform for its members to achieve tax transparency and standards for the exchange of information for tax purpose. It establishes the framework for the automatic exchange of information between tax jurisdictions. Action 11 achieves this by providing for data exchange, types of data to be exchanged and methodologies for analysing the data.[473]

472 OECD (2018), Revised Guidance on the Application of the Transactional Profit Split Method: Inclusive Framework on BEPS: Action 10, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris, online: <http://www1.oecd.org/tax/transfer-pricing/revised-guidance-on-the-application-of-the-transactional-profit-split-method-beps-action-10.pdf>

473 OECD (2015), Measuring and Monitoring BEPS, Action 11 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241343-

While the Global Forum achieves significant progress, the OECD acknowledges that combatting BEPS requires a more holistic approach through improved transparency on all fronts, such as beneficial ownership and information on the structure and activities of multinational entities.

iii. Action 13: Re-examine transfer pricing documentation

This Action Plan reviewed existing transfer pricing documentation in a bid to improve transparency for tax administration, provide relevant information to tax authorities, while taking into account the compliance costs for businesses. The recommended rules set out to provide relevant tax authorities and governments with information on the global activities of MNEs, alongside data on economic activities in each jurisdiction where they operate.[474] It discloses information on taxes paid to countries by MNEs and their organisational structure. Information on production factors and sales of the corporate group are made available.

To achieve this wide and detailed disclosure of relevant information, the OECD under this action plan recommended the preparation of country by country report (CBCR), master file and local file by taxpayers as part of their transfer pricing documentation.[475]

The CBCR requires MNEs to report annually, income for each tax jurisdiction in which it carries on business, profit before income tax and income tax paid and

en.pdf?expires=1554422939&id=id&accname=guest&checksum=A8F5033B45CFFCCAC11B997623176D3D>

[474] OECD (2014), Guidance on Transfer Pricing Documentation and Country-by-Country Reporting, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, online: <https://www.oecd-ilibrary.org/docserver/9789264219236-en.pdf?expires=1554423403&id=id&accname=guest&checksum=E9267BD6E0C0776313A44178CC86C192>

[475] OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241480-en.pdf?expires=1554423542&id=id&accname=guest&checksum=DB9BF7A39B0DECE306F08E41C0B03360>

accrued.[476] Other information to be contained in the CBCR include total employment, capital, retained earnings and tangible assets of the MNE in each tax jurisdiction; business activities carried on by each entity in the corporate group in each tax jurisdiction. The OECD has cautioned that the information in the CBCR should not be used as substitute for detailed transfer pricing analysis of individual transactions and prices based on a full functional analysis and a full comparability analysis.[477] It has cautioned that the information contained in the CBCR is not conclusive evidence that transfer prices are appropriate or not and should not be relied on by tax administrations to propose transfer pricing adjustments based on a global formulary apportionment of income.

Note that not all taxpayers are subject to comply with the CBCR regulation. To be eligible, the OECD's CBCR Guidance prescribes that the taxpayer's annual consolidated revenue must be seven hundred and fifty million euros (EUR 750 million) or more.[478] Tax jurisdictions have adopted the OECD's CBCR Guidance in their domestic laws for compliance by MNEs in their jurisdictions.[479]

[476] OECD (2018), Guidance on the Implementation of Country-by-Country Reporting – BEPS Action 13, OECD, Paris, online: <www.oecd.org/tax/guidance-on-the-implementation-of-country-by-country-reporting-beps-action-13.pdf>

[477] OECD (2017), BEPS Action 13 on Country-by-Country Reporting – Guidance on the appropriate use of information contained in Country-by-Country reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris, online: <www.oecd.org/tax/beps/beps-action-13-on-country-by-country-reporting-appropriate-use-of-information-in-CbC-reports.pdf> OECD (2018),Country-by-Country Reporting – Compilation of Peer Review Reports (Phase 1): Inclusive Framework on BEPS: Action 13, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online: <https://www.oecd-ilibrary.org/docserver/9789264300057-en.pdf?expires=1554424085&id=id&accname=guest&checksum=40AC43D0A19907D2C5BE6F626A911907>

[478] OECD (2017), Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment, OECD, Paris, online: <www.oecd.org/tax/beps/country-by-country-reporting-handbook-on-effective-tax-risk-assessment.pdf>.

[479] OECD (2018), Guidance on the Implementation of Country-by-Country Reporting: Compilation of Approaches Adopted by Jurisdictions, OECD, Paris, online: <https://www.oecd.org/tax/beps/CbC-Compilation-of-approaches-adopted-by-jurisdictions.pdf> OECD (2018), Guidance on the Implementation of Country-by-Country Reporting – BEPS Action 13, OECD, Paris, online: <www.oecd.org/tax/guidance-on-the-implementation-of-country-by-country-reporting-beps-action-13.pdf>.

Nigeria, in June 2018, introduced its CBCR Regulations[480] and in July 2018, released detailed guidelines for CBCR in Nigeria.[481] in chapter 4 of the thesis, I discuss in detail, Nigeria's CBCR Regulations.

One criticism of the OECD's CBCR Guidance is the high monetary threshold requirement to be eligible to provide CBC Reports. The minimum annual turnover of EUR 750 million (approximately, US$ 1 billion) excludes many MNEs doing business in Africa. We learn from Acha Leke, et. al, that Africa has about 400 companies with an annual turnover of US$ 1 billion or more.[482] This is a small number compared to the thousands of MNEs carrying on businesses in Africa. Such high threshold does not take into account the economies of African countries and their relative strengths and positions. It excludes many MNEs, thus keeping away relevant information needed for income allocation. It is recommended that monetary threshold requirement for compliance with the CBCR be tailored to each region and industry.

The master file provides a high-level overview of the group business of the MNE including the transfer pricing policies of the business, the global business operations and the global allocation of income and economic activities of the business. The aim of the information above is to assist tax administrations with identifying significant transfer pricing risks emanating from the cross-border economic activities in their tax jurisdictions.[483]

---

[480] Income Tax (Country by Country Reporting) Regulations, 2018, pursuant to the Federal Inland Revenue Service (Establishment) Act, 2007, online: <https://www.firs.gov.ng/sites/Authoring/contentLibrary/d9dae9a0-3d22-48fa-bdec-34e59d7a001bOfficial%20Gazette%20of%20Income%20Tax%20CbC%20Regulations%202018.pdf>

[481] FIRS (2018), Guidelines for the Appropriate Use of information Contained in CBC Reports, FIRS, Abuja, online: <https://www.firs.gov.ng/sites/Authoring/contentLibrary/ca4577b5-cb38-4aff-a532-42938a3589f2Guidelines%20on%20the%20Appropriate%20Use%20of%20CbC%20Reports.pdf>

[482] Leke, supra note 388 at 19.

[483] OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, at 25.

The local file provides more detailed information on intercompany transactions between related entities. The aim of the local file is to establish that the taxpayer has complied with the arm's length principle in the tax jurisdiction where it is tax liable. A local file contains information on related party transactions, comparability analysis, selection and application of the most appropriate transfer pricing method.[484]

These reforms in transfer pricing documentation, it is believed, would provide the relevant information needed for the adoption and application of the unitary approach to income allocation. They cumulatively provide information on the global operations of the MNE group, making it possible to assess the contribution of each jurisdiction and apply the formulary apportionment.

iv. Action 15: Develop a Multilateral Instrument

To achieve ease of amending existing bilateral tax treaties between tax jurisdictions, the OECD recommended the use of a multilateral convention to implement tax treaty related measures to prevent base erosion and profit shifting (MC-BEPS).[485] This multilateral instrument contains the measures developed in the course of the BEPS Project, with the aim of amending bilateral tax treaties between tax jurisdictions.[486] According to the OECD, the multilateral instrument provides an "innovative approach to international tax matters, reflecting the rapidly evolving nature of the global economy and the need to adapt quickly to this

484 OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, at 27.

485 OECD (2017), Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, OECD Publishing, Paris, online: <http://www1.oecd.org/tax/treaties/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf>; OECD (2016) Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, OECD Publishing, Paris, online: <http://www1.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf>

486 OECD (2017), Frequently Asked Questions on the Multilateral Instrument, OECD Publishing, Paris, online: <http://www1.oecd.org/tax/treaties/MLI-frequently-asked-questions.pdf>

evolution".[487] Borrowing from public international law, the multilateral instrument adopts a hard law approach to amending existing bilateral tax treaties by countries. With more than 3000 bilateral tax treaties in effect, the multilateral instrument presents an effective and efficient way of amending the provisions of those treaties, without going through the rigour of bilateral negotiations between countries. [488]

The OECD highlights three important advantages of the multilateral instrument: the multilateral instrument is highly targeted at the important BEPS issues; it allows existing bilateral tax treaties to be modified in a synchronised way without individually addressing each tax treaty; and it responds to the political imperativeness of the BEPS project, while balancing sovereignty issues countries may have.[489] The ownership element of the multilateral instrument by countries discourages the use of unilateral and uncoordinated measures in addressing BEPS.[490]

The MC-BEPS contains minimum standard commitments and recommended common approaches countries participating in the BEPS process have to meet.[491] The minimum standards commitments are: amendment of the preambles of DTAs

---

[487] OECD (2014), Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, OECD/G20Base Erosion and Profit Shifting Project, OECD Publishing, at 10, online: <https://www.oecd-ilibrary.org/docserver/9789264219250-en.pdf?expires=1554425020&id=id&accname=guest&checksum=C854605AB9915308C4F6E15D1620817A>.

[488] OECD (2015), Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 -2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264241688-en.pdf?expires=1554424333&id=id&accname=guest&checksum=3E33178D823D74CAED659D5B40506EB1>.

[489] OECD (2014), Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, OECD/G20Base Erosion and Profit Shifting Project, OECD Publishing.

[490] See for instance, plans by the Spanish Finance Ministry to introduce digital tax for firms engaged in the digital economy, such as Airbnb and Uber: El Pais, "Spanish Finance Ministry to Introduce Digital Tax for Firms like Airbnb and Uber", (2018) published online: <https://elpais.com/elpais/2018/10/05/inenglish/1538741424_819871.html>

[491] The BEPS Monitoring Group, "Explanation and Analysis of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting" (2017) online publication of The BEPS Monitoring Group: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4dc10f950b78091d69b0d/1525996565723/explanation-and-analysis-of-mc-beps-final-rev.pdf?

between countries to state that the DTAs are intended to eliminate double taxation, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance;[492] an inclusion of a principal purpose test (PPT) provision in DTAs to prevent the grant of treaty benefits if reasonable to conclude that the treaty was entered into primarily to take advantage of the benefit of the treaty; and commitment by competent tax authorities to be aware of mutual agreement procedure (MAP) requests by taxpayers in order to give their views on the disputes.[493]

Considering the number of countries that have signed up to MC-BEPS process, one can say that it has been well-received by countries, including African countries.

3.2 The UN's Reforms

The UN has, in the last decade, been very active in the global tax reform process. One platform for engaging in the global tax discourse is through the UN Committee of Experts on International Cooperation in Tax Matters.[494] Some of the responsibilities of the Committee include: review and update of the United Nations Model Double Taxation Convention between Developed and Developing Countries and the Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries;[495] advising the United Nations on how to

---

[492] DTAs until now only contained provisions stating they are to eliminate double taxation, with no mention of non-taxation or reduced taxation.

[493] The BEPS Monitoring Group, "Explanation and Analysis of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting" (2017) online publication of The BEPS Monitoring Group: online: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4dc10f950b78091d69b0d/1525996565723/explanation-and-analysis-of-mc-beps-final-rev.pdf>

[494] United Nations (2004), Committee of Experts on International Cooperation in Tax Matters: ECOSOC Resolution 2004/69, United Nations, online: <https://www.un.org/en/ecosoc/docs/2004/resolution%202004-69.pdf>; United Nations (2006), Committee of Experts on International Cooperation in Tax Matters: ECOSOC Resolution 2006/69, United Nations, online: <https://www.un.org/en/ecosoc/docs/2006/resolution%202006-48.pdf>.

[495] United Nations, Committee of Experts on International Cooperation in Tax Matters: Terms of Reference, United Nations, online: <https://www.un.org/esa/ffd/tax-committee/about-committee-tax-experts.html>

improve cooperation among tax authorities and the role of new and emerging tax issues in the discourse of tax cooperation; making recommendations on capacity building and provision of technical assistance to developing countries.[496]

Another important initiative of the United Nations is its joint project with the OECD- the Tax Inspectors Without Borders (TIWB) programmes. [497]The TIWB "facilitates the deployment of international tax audit experts to work alongside tax administrations in developing countries on complex international tax audits".[498] The TIWB supports developing countries to strengthen domestic resource mobilisation through the transfer of technical know-how and skills to local tax auditors, as well as engaging in audit processes with local tax authorities.

The United Nations is engaged in the publication of handbooks, practical manuals, guidelines and policy recommendations, geared towards protecting the tax base and addressing BEPS. In 2017, it published the second edition of its Handbook on Selected Issues in Protecting the Tax Base for Developing Countries.[499] The Handbook takes a developing country perspective in addressing the issues therein.

The Handbook addresses issues such as: protecting the tax base of developing countries; taxation of income from services; taxation of non-residents' capital gains; limiting interest deductions; neutralizing effects of hybrid mismatch arrangements; preventing tax treaty abuse; preventing avoidance of permanent establishment status; protecting the tax base in the digital economy; tax incentives in developing countries; transparency and disclosure; taxation of rents and royalties; the role of a general anti-avoidance rule in protecting the tax base

---

[496] United Nations, Committee of Experts on International Cooperation in Tax Matters: Terms of Reference, United Nations, online: <https://www.un.org/esa/ffd/tax-committee/about-committee-tax-experts.html>
[497] TIWB, Frequently Asked Questions, online: <http://www.tiwb.org/about/faq/>
[498] OECD (2017), "Tax Inspectors Without Borders- Bolstering Domestic Revenue Collection through Improved Tax Audit Capacities' OECD, Paris, online: <http://www.oecd.org/tax/tax-inspectors-without-borders-bolstering-domestic-revenue-collection-through-improved-tax-audit-capacities.htm>
[499] Alexander Trepelkov, Harry Torino & Dominika Halka, "Handbook on Selected Issues in Protecting the Tax Base of Developing Countries" (2017) UN, New York, online: <https://www.un.org/esa/ffd/wp-content/uploads/2017/08/handbook-tax-base-second-edition.pdf>

of developing countries. The Handbooks seeks to assist developing countries to increase domestic resource mobilisation through broadening the tax base, while protecting the existing tax base.

The United Nations asserts that the Handbook aids developing countries in three important ways: "a) engagement and effective participation in relevant international norm-setting and decision-making processes, including in the OECD fora; b) assessment of relevance and feasibility of different options to protect and broaden their tax base, including those proposed in the context of the OECD work on BEPS; and c) effective and sustained implementation of the most suitable options from which they would benefit".[500]

The United Nations rightly recognises the challenges of developing countries in the international tax environment as inclusion in global tax discourse, technical capacity and available resources to engage in the global tax discourse and protecting their tax base through implementing the most suitable options for their jurisdictions. This approach departs from the insistence of a one-size-fits-all global tax system and takes into account the peculiar needs of developing countries.

In addition, the United Nations Practical Manual on Transfer Pricing for Developing Countries (United Nations Practical Manual)[501] has become reference guides for developing countries, though it shares strong similarities with the OECD TPGs. The 2017 United Nations Practical Manual builds on the OECD BEPS Report and incorporates some of the recommendations of the BEPS Project.

Though the UN receives praise for advancing the interest of developing countries in the global tax discussion, its continuous adoption and protection of the OECD's arm's length principle and reluctance to advance radical reforms diminishes its

[500] Ibid.
[501] United Nations, Practical Manual on Transfer Pricing for Developing Countries (2017) Department of Economic & Social Affairs. United Nations: New York.

efforts in the global tax space.[502] Its reform efforts are at best patchy, without going beneath the surface and addressing strongly, the issue of allocation of taxing rights.

3.3 The Platform for Collaboration on Taxation

The Platform for Collaboration on Taxation (PCT) is a joint initiative of the United Nations, the International Monetary Fund (IMF), the World Bank and the OECD. It is aimed at intensifying cooperation on tax issues among these supranational bodies, in order to provide capacity-building support. It seeks to jointly develop guidance on tax issues and share information on best practices and technical knowledge for the benefit of developing countries.[503]

The PCT focuses on providing guidance and toolkits for addressing the tax challenges countries face when implementing the global tax rules, with the important goal of protecting their tax bases. In 2017, the PCT issued a Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses (Toolkit on Transfer Pricing).[504] The Toolkit on Transfer Pricing proffers ways developing countries can overcome the lack of data necessary for implementing the transfer pricing rules. It contains recommendations for countries as they set rules and practices for businesses in their tax jurisdictions. The Toolkit on Transfer Pricing contains recommendations on pricing of minerals sold in an intermediate form.

[502] Michael Lennard, "The UN Model Tax Convention as Compared with the OECD Model Tax Convention- Current Points of Difference and Recent Developments" (2009) Asia-Pacific Tax Bulletin, IBFD: Amsterdam; Diane Ring, "Who is Making International Tax Policy? International Organizations as Power Players in a High Stakes World" (2010) Fordham International Law Journal, Vol. 33, No. 3, pp. 649-722.

[503] The Platform for Collaboration on Tax, "The Platform for Collaboration on Tax: A Major Step to Boost International Cooperation in Tax Matters" (2016). United Nations Headquarters, New York, online publication, online: <https://www.un.org/esa/ffd/wp-content/uploads/2016/10/se-tc-presentation.pdf>

[504] Platform for Collaboration on Tax, "A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses. Including a Supplementary Report on Addressing the Information Gaps on Prices of Minerals Sold in an intermediate Form" (2017), Platform for Collaboration on Tax.

Similarly, the PCT released a discussion draft on the taxation of offshore indirect transfers.[505] This seeks to provide recommendations, through a toolkit, on the taxation of the sale of an entity owning an asset located in a tax jurisdiction by a resident company of another tax jurisdiction. This became important given the experience of countries where they lose taxable profits arising from the sale of assets in their jurisdictions, as a result of the imposition of artificial corporate structures by MNEs for tax gains. I discussed this previously in chapter 2 above.

The Ugandan case of Heritage Oil & Gas Ltd v. Uganda Revenue Authority[506] provides an illustration. In this case, Heritage Oil & Gas Ltd (Heritage) had entered into a Production Sharing Agreement (PSA) for petroleum exploration, development and production with the Republic of Uganda (the Government) on 1st July 2004. In 2010, Heritage sold its interests under the PSA to Tullow Uganda Limited under a sale and purchase agreement. The Uganda Revenue Authority (URA) issued a tax assessment for capital gains tax on Heritage on the basis of the sale and purchase agreement.

One of the contentions of Heritage was that the sale of the assets took place outside Uganda and as such the income should not be taxed for capital gains in Uganda, since it cannot be attributed to activities in Uganda. The contract was negotiated in the Channel Islands with discussions in the United Kingdom and the Netherlands. The respondent, URA, submitted that the income derived from the disposal of the assets was subject to taxation in Uganda by virtue of section 17 of the Income Tax Act of Uganda.

Section 17 of the Income Tax Act of Uganda provides for the taxation of business income. Section 17(2) of the Income Tax Act specifically provides that the gross

---

505 The Platform for Collaboration on Taxation, "Discussion Draft: The Taxation of Offshore Indirect Transfers- A Toolkit" (2017), Platform for Collaboration on Tax, available online: <https://www.oecd.org/tax/discussion-draft-toolkit-taxation-of-offshore-indirect-transfers.pdf>
506 Heritage Oil & Gas Ltd v. Uganda Revenue Authority (Civil Appeal No 14 of 2011) [2011] UGCOMMC 97.

income of a non-resident person includes only income derived from sources in Uganda. The respondent cited section 79 (g) of the Income Tax Act, to the effect that income is derived from sources in Uganda to the extent to which it is derived from disposal of an interest in immovable property located in Uganda. The respondent concluded that Heritage through the sale and purchase agreement, sold the rights and interests in immovable property catered for under section 79 of the Income Tax Act.

The court, ruling in favour of the respondent, held that the tax liability of a non-resident arises where the source of income originates and where the contract is signed is not of paramount importance. The court ruled that there was evidence of activities having taken place in Uganda, thereby making the income taxable in Uganda, in line with section 79(s) of the Income Tax Act. Other case of note is the case of Vodafone International Holdings B.V. V Union of India discussed in chapter 2 above.

In concluding, the report and toolkit on the taxation of offshore indirect transfers provides analysis and options for the treatment of offshore indirect transfers. The two main proposals for the treatment of offshore indirect transfers, outlined by the report are: the treatment of offshore indirect transfers as transfer of the underlying asset in the location country; or treatment of the transfer as being made by the actual seller, offshore, but the gain on the transfer is sourced from the location country, enabling the location country to tax the gain on the transfer. This toolkit is of great importance to African countries as its recommendations address one of the main reasons for tax avoidance under the current tax system: the separate entity treatment of related entities in a corporate group.

3.4 Reform Efforts by the African Tax Administration Forum (ATAF Reforms)

The African Tax Administration Forum (ATAF) has over the decade promoted mutual cooperation among tax authorities on the continent. It is regarded on the continent as the African voice on setting global tax rules. This, it achieves, through knowledge dissemination, developing capacity on the continent, providing platform for exchange of ideas and knowledge and contributing actively to regional and global tax agenda.

ATAF, as a continental body has published a model tax convention agreement and model transfer pricing regulations and guidance as part of its transfer pricing project. It contributes to the OECD's BEPS project and publishes other instruments/tools to guide African tax authorities at improving their domestic revenue mobilization efforts.[507]

Its Model Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (ATAF Model Agreement)[508] borrows largely from the OECD's model convention. For instance, the provisions of Article 9 (1) and (2) of ATAF Model Agreement is in tandem with the OECD's Article 9 provision. However, the ATAF Model Agreement contains an Article 9(3) provision, akin to that in the UN model convention. Article 9(3) exempts a country from the duty of corresponding adjustment where it is established through a judicial, administrative or other legal proceeding, one of the entities concerned is liable to a penalty with respect to fraud, gross negligence or wilful default and the adjustment in Article 9 (1) should not be allowed to stand.[509]

---

507 ATAF, "Suggested Approach to Transfer Pricing Legislation" (2017), Pretoria: ATAF, Online: <https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/ATAF%20Suggested%20Approach_revise_green_HR.pdf>

508 ATAF, "ATAF Model Tax Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income", ATAF Publication: Pretoria, Online: <https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/ATAF%20Model%20Tax%20Agreement_Highres.pdf> ATAF, "ATAF Model Tax Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income: Commentary on the Articles", ATAF Publication: Pretoria, online: <https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/ATAF%20Model%20Taxagreement_commentary%20_Highres.pdf>

509 Article 9(3) of the ATAF Model Agreement.

ATAF has contributed significantly to the development of transfer pricing rules at both the global and continental realms. In 2017, the continental body made significant changes to the global tax standards. At the November 2017 meeting of Working Party 6 of the OECD[510], held in Paris, France, ATAF, through its delegates, made presentations on the additional guidance on the attribution of profits to a permanent establishment and revised guidance on the use of profit split method for transfer pricing purposes. It successfully inserted an African-based example in the TPGs discussion on the profit split method. This arose out of the concern of ATAF that examples that reflected the types of transactions seen on the African continent were not included in the profit split method discussions and the examples inserted in the TPGs were of limited value to African countries. ATAF's example referred to transactions where the African taxpayer provided unique and valuable contribution to the exploitation of natural resources in the African country. This unique and valuable contribution contributes to some of the residual profit of the group entity. The Working Party 6 of the OECD accepted this example and included it in the TPGs.[511]

ATAF's contribution to the improvement of the tax systems of African countries is appreciated in the continent and recognised globally. Countries such as Nigeria, South Africa and Liberia have benefitted, in no small way, from the technical capacity of ATAF. At the global level, it has assumed a representative organisation of African tax administrations and the gateway to interacting with tax authorities.

However, its major failure is that it has failed to depart from the global tax system, which has been proven to be impractical and inefficient. As such, the body contributes little to significantly addressing the base erosion and profit shifting taking place on the continent. Its adherence to the global standards set by the OECD raises question of capture by the Global North. It collaborates with the

---

[510] Working Party 6 of the OECD on Taxation of Multinational Enterprises.

[511] ATAF, "Resolving African Challenges in Transfer Pricing. ATAF makes Critical Contribution to Affect Global Tax Standards", Medium, online: <https://medium.com/african-tax-administration-forum/resolving-african-challenges-in-transfer-pricing-44868cfacb64>

OECD on many of its projects, thereby questioning its independence. It may be that Africa needs its own truly independent continental tax body, which will push for fundamental changes that ensure that profits made on the continent are taxed on the continent.

4 Other Relevant Efforts at Reforming the Present Global Tax System

In this section, I shall discuss some of the very recent papers that shape the reforms of the global tax system. They come from the IMF, the ICRICT and the BMG.

4.1 The International Monetary Fund

Two papers from the IMF are of special relevance to the changing landscape of the global tax system. The first is a 2014 policy paper, "Spillovers in International Corporate Taxation"[512] which contains important observations and recommendations. The paper argues that globalization has made increasingly fragile, the concepts of residence and source of income, on which the current international tax agreements rest on. MNEs possess many devices to reduce their total tax bills. As such, traditional tax agreements that are felt to result in unfair allocation of the tax base may cause countries to seek unilateral measures, that undermine the coherence of the global tax system.

These unilateral measures are likely to lead to spillovers (base spillovers[513] and strategic spillovers[514]), which potentially lead to collective loss of revenue and welfare. The paper recommends clearer and simplified rules and guidance for developing countries to cope better with the challenges of transfer pricing, alongside capacity building of tax administrations. It identifies formulary

[512] IMF Policy Paper, "Spillovers in International Corporate Taxation" (2014), IMF: Washington, DC, online: <https://www.imf.org/external/np/pp/eng/2014/050914.pdf>.
[513] Where the actions of one country directly affect the corporate income tax bases of other countries.
[514] Where the actions of one country induce changes in the tax policies of other countries.

apportionment as one option to deal better with spillovers, arguing that it would limit conventional transfer pricing. However, it notes that formulary apportionment would create new difficulties around the factors used to apportion profits across jurisdictions and would not necessarily shift tax base towards developing countries. In chapter 4, I shall examine this last claim of the IMF-factors of formulary apportionment and whether it achieves shift of the tax base towards developing countries.

A more recent paper of the IMF was published in March 2019. The paper, "Corporate Taxation in the Global Economy"[515] supports, unequivocally, a fundamental change in the global tax system. It precisely states that "…limitations of the arm's length principle-under which transactions between related parties are to be priced as if they were between independent entities-and reliance on notions of physical presence of the taxpayer to establish a legal basis to impose income tax have allowed apparently profitable firms to pay little tax."[516] It reiterates that tax competition among countries remains unaddressed and concerns with the allocation of taxing rights across countries continue. It observes that recent unilateral measures jeopardize multilateral cooperation on reforming the global tax system. It concludes that "there now seems quite widespread agreement that fundamental change to current norms is needed-but no agreement, as yet, on its best form".[517]

The paper admits that OECD's call for taxation "where value is created" has proved inadequate for real progress of the current tax system. In chapter 5, I discuss why the OECD's mantra "…where value is created" is impractical and inadequate for the allocation of income in today's global economy. The paper analyses some of the commonly discussed alternative directions to the current tax

---

[515] IMF Policy Paper, "Corporate Taxation in the Global Economy" (2019), IMF, Washington, DC, online: <https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/08/Corporate-Taxation-in-the-Global-Economy-46650>
[516] Ibid at 6.
[517] Ibid.

system. I briefly highlight them, with specific relevance to their discussions on developing countries, which captures African countries.

On minimum taxes, the IMF argues that minimum taxes on inbound investment may be a straightforward measure of base protection for developing countries. It recommends the use of minimum taxes as part of the core system, and not as an alternative approach. This position I agree with and discussed previously in section 2 (a) of this chapter.

On border-adjusted profit taxes, such as the destination-based cash flow tax, (DBCFT) it argues that if adopted universally, it would largely eliminate both profit shifting and tax competition. This, it claims, is attributed to the treatment of tax liability under the DBCFT, which is only on the treatment of the sale to final consumers. It opines that for "resource-rich countries, a destination-based cash flow tax-and destination taxation more generally-should be supplemented by source-based taxes focused on capturing any location specific rents".[518] It admits that under the DBCFT, the likelihood of revenue losses is much higher in resource-intensive countries. It concludes that for developing countries the implications for DBCFT are unclear but used in addition with source taxation for natural resources, it should not be adverse.

The conclusion of the IMF on the DBCFT echoes the position of others who have cautioned against the adoption of a single factor allocation system or a VAT-method of allocation of income. It is my opinion that insistence on the demand-side of profit generation and not taking into account the supply-side divide, leaves African countries worse off.

On formulary apportionment, it argues that "subnational experiences indicate that, as economic integration proceeds, formula apportionment presents itself as better suited than the arm's length principle for dividing profits of related

[518] Ibid para 67 at 28.

companies across jurisdictions".[519] It agrees that formulary apportionment would greatly reduce profit shifting. It states that applying formulary apportionment would be simpler to administer and comply with than the current tax system, while reducing administrative costs for the tax authorities. For developing countries, revenue gains are expected to increase and be significantly higher if heavy weight is attached to employees.

However, it notes that securing international agreement on a common tax base will be challenging. Other highlighted challenges of the formulary apportionment are the presence of tax competition where factors used for apportionment are mobile; valuation of assets; and definition of the unitary base. I discuss these concerns in both chapters 4 and 5 on the adoption and implementation of the unitary approach.

On the adoption of sharing residual profit, it maintains that scope for tax competition remains, including in relation to routine profit. Under a residual profit allocation method, the transfer pricing methods (save for the profit split method) is used to apportion routine profit to the related entities for associated costs incurred. The residual profit is then apportioned to the related entities using the profit split method, taking into account the unique contributions of the entities which are hard to value. The allocation of routine profit still possesses the challenges of applying the transfer pricing rules, thus, presenting opportunities for manipulation.

In conclusion, the IMF posits that no suggested allocation scheme is without difficulty. It supports coordinated approaches by countries to reform the international tax system, stating that unilateral and uncoordinated measures observed could create disorder in the global tax architecture. Coordinated approaches will minimise adverse spillovers in addressing the challenges of the global tax system and adopting an alternative approach.

[519] Ibid para 77 at 31.

4.2 Independent Commission for the Reform of International Corporate Taxation

The Independent Commission for the Reform of International Corporate Taxation (ICRICT) is a group of leaders championing significant reform of the international corporate tax system.[520] It is a coalition of ActionAid, Alliance-Sud, the Arab NGO Network for Development, the Center for Economic and Social Rights, Christian Aid, the Global Alliance for Tax Justice, OXFAM, Public Services International, South Centre, Tax Justice Network and the World Council of Churches.

ICRICT's contribution to the reform of the global tax architecture has come in the forms of publications, public engagements and media posts. Of relevance to the thesis, are the publications.

In January 2019, it published a paper, "The Fight Against Tax Avoidance"[521] which argues that "by failing to collect the revenue that is being lost through tax avoidance schemes by multinationals, governments are failing in their obligation to mobilize all available resources towards the realization of human rights and the sustainable development goals (SDGs) and thereby condemning millions of people across the developing world to poverty, lack of opportunity and lower living standards".[522] It argues that the OECD's BEPS Project, while proposing helpful solutions has failed to deal with the core mechanisms of tax avoidance, especially through transfer pricing. It admits that the international community is at a crossroads. It questions whether the OECD should keep imposing marginal reforms to a system adjudged to be inadequate and impractical or does it adopt

[520] Independent Commission for the Reform of International Corporate Taxation: About Us, online: <https://www.icrict.com/about-icrict>.

[521] ICRICT, "The Fight Against Tax Avoidance. BEPS 2.0: What the OECD BEPS Process has Achieved and what Real Reform Should Look Like" (2019) ICRICT Publication, online: <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5c409495f950b7e303b71a45/1547736215689/thefightagainsttaxavoidance_FINAL.pdf>.

[522] ICRICT, "The Fight Against Tax Avoidance. BEPS 2.0: What the OECD BEPS Process has Achieved and what Real Reform Should Look Like" (2019) ICRICT Publication, Executive Summary at 3.

fundamental solutions fit for the 21st century? To this question, it supports a radical change in the global tax system.

The paper supports the call for unitary taxation of multinational entities. It understands that multinationals are unitary businesses whose profits can only be achieved through the integration of the activities of the related entities across jurisdictions, and the value of the multinational as a whole is bigger than the sum of its individual parts. It unequivocally calls for governments represented in the Inclusive Framework, the UN Tax Committee and all multinational institutions to move away from the transfer pricing system and adopt the unitary taxation of multinationals. It recommends that the unitary taxation system be based on formulary apportionment, underpinned by a global effective minimum tax rate.

On formulary apportionment, it argues that a formulaic approach will allocate global profits and by extension, associated taxes according to objective factors such as sales, employment, resources used by the multinational enterprise in each country where it operates and has a subsidiary/branch. This will depart from the current system of allocation of profits to where MNEs locate their different functions, such as procurement, marketing, funding, etc. and claim their intellectual property, it argues.

On the adoption of a global effective minimum tax, the paper argues that such adoption would reduce the incentives to shift profits to low tax jurisdictions by MNEs and the race to the bottom by countries seen in the reduction of countries' tax rates. This approach shares similarities with the alternative minimum corporate tax discussed above, though this is applied on the taxable profit of the company, and not on the turnover of the company. Imposing a global effective minimum tax on tax jurisdictions could be resisted on the principle of fiscal sovereignty. However, recent observations reveal that global cooperation on tax matters is well established with countries willing to give up their fiscal sovereignty to advance multilateralism and consensus in the global tax architecture.

Its 2019 paper supports an earlier 2018 paper by ICRICT, "A Roadmap to Improve Rules for Taxing Multinationals"[523] where it calls for the adoption of the unitary taxation of multinational entities. It recommends to states that multi-factor global formulary apportionment with a minimum corporate tax rate presents the fairest and most effective version of the unitary taxation approach. In this paper, it distinguishes the different types of unitary taxation to include worldwide residence-based taxation, destination-based cash-flow tax, and formulary apportionment. Recognizing that the fundamental change to the global tax architecture is a long-term project, it calls on global leaders to adopt short-term measures, which are effective and easier to administer in the interim, while focused on long-term fundamental solutions.

4.3 BEPS Monitoring Group[524]

The BEPS Monitoring Group (BMG) is a network of researchers who are concerned with the effects of tax avoidance of MNEs on the development of countries.[525] The group produces reports on proposals for the reform of the international tax system, alongside making submissions to the supranational tax bodies responsible for setting the global tax system. As its name depicts, the BMG is focused primarily on base erosion and profit shifting issues, attributed to MNEs, coupled with producing reports on the OECD's BEPS Action Plan.

In its December 2018 submission to the IMF on the analysis of international corporate taxation, the BMG recommended the IMF considered the micro-economic aspects of aggressive tax avoidance, especially the abuse of dominant position and rent-seeking resulting from corporate concentration.[526] It re-echoes

---

523 ICRICT, "A Roadmap to Improve Rules for Taxing Multinationals" (2018) ICRICT Publication, online: <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5a78e6909140b73efc08eab6/1517872798080/ICRICT+Unitary+Taxation+Eng+Feb2018.pdf>

524 The author is a member of the BEPS Monitoring Group (BMG).

525 The BEPS Monitoring Group: About Us, online: <https://www.bepsmonitoringgroup.org/about-us>.

526 BEPS Monitoring Group, "Submission to the International Monetary Fund on Analysis of International Corporate Taxation" (December 2018), Publication of The BEPS Monitoring Group, online:

the position of others that the OECD BEPS Project has failed to ensure that profits of MNEs are allocated to and taxed where the economic activities occur.

The BMG supports calls for a shift to a system which treats MNEs in accordance with the economic reality that a large part of these profits results from the economies of scale and scope and the synergies due to operating as unitary firms under centralised strategic direction. It recommends the improvement of the profit split method[527] as interim measure, while the world moves towards formulary apportionment which it claims will take time and needs preparation.

In September 2018, in its submission to the United Nations Committee of Experts on International Cooperation in Tax Matters on the revision of the UN Practical Manual on Transfer Pricing for Developing Countries,[528] the BMG suggested that high priority be given to the study of possible simplified transfer pricing methods. This, it claims, is to ameliorate the experience of developing countries with implementing the transfer pricing rules.[529]

Finally, in May 2017, it published its comments on the proposed Common Consolidated Corporate Tax Base (CCCTB) by the European Commission.[530] It

---

<https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5c19432470a6adbb26cd4317/1545159465605/BMG+to+IMF+on+Corporate+Taxation+final.pdf>

[527] The BEPS Monitoring Group, "Comments on the Public Discussion Draft on Revised Guidance on Profit Splits" (September 2017) Publication of The BEPS Monitoring Group, online: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4df8b70a6ad984c86a28d/1525997456624/psm-final.pdf>

[528] The BEPS Monitoring Group, "Submission to the Subcommittee on Article 9 (Associated Enterprises): Transfer pricing of the Unites Nations Committee of Experts on International Cooperation in Tax Matters on Revision of the UN Practical Manual on Transfer Pricing for Developing Countries" (September 2018), Publication of The BEPS Monitoring Group, online: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5bac9e071905f4689fd51b02/1538039306826/BMG+Submission+to+UNTC+article+9+final.pdf>

[529] See: The BEPS Monitoring Group, "Submission on Revision of Chapter IV of the Transfer Pricing Guidelines on Administrative Approaches to Avoiding and Resolving Transfer pricing Disputes" (June 2018), Publication of The BEPS Monitoring Group: https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5b3242961ae6cf9812ba9e7c/1530020506821/Administrative+Approaches+to+TP+Disputes.pdf.

[530] The BEPS Monitoring Group, "Comments on the European Commission's Proposals for a CCTB and for a CCCTB" (May 2017), Publication of The BEPS Monitoring Group, online: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4dcc60e2e72299b765c2b/1525996746863/ccctb-2017-final.pdf>.

submitted that the aim should be to achieve a global level playing field in relation to tax that is not limited to the European Union. Failure to do achieve this, would lead to tax competition among EU member states, who would offer tax preferences to MNEs from outside the EU. It acknowledges that the EU CCCTB adopts a sound approach to taxation of MNEs by treating them as unitary firms. It opines that the EU's adoption of the three-factor approach (sales, assets and employees) provides an effective way of ending both tax competition between states to offer tax incentives and the activities of MNEs who shift income between affiliates for tax gains.

5 Conclusion

This chapter discussed the proposed alternatives to the transfer pricing system. It discussed ongoing reforms by the OECD, the UN, IMF and other stakeholders aimed at improving the global tax architecture. While many of these reforms have contributed meaningfully to the improvement of the global tax architecture, their patchy approaches have failed to address significantly the base erosion and profit shifting practices of MNEs. In chapters 4 and 5, I discuss the adoption and application of the unitary taxation and formulary apportionment approach to income allocation.

Chapter 4: Unitary Taxation of Multinational Enterprises in Nigeria and within the AfCFTA Framework

Table of Content

4.2.2 The Global Economy Perspective

5. Conclusion

1. Introduction

1.1 Executive Summary of the Chapter

This chapter considers the application of unitary taxation within the African context. The continent's largest economies- Nigeria, South Africa, Egypt and Algeria- all possess power to adjust profit provisions similar to article 9 of the OECD MTC in their domestic tax laws and have enacted transfer pricing rules, modelled after the OECD TPGs.[531] As such, they are exposed to the limitations and impracticability of the current global tax system. They are vulnerable to the erosion of their tax bases and shifting of taxable profits out of their jurisdictions to other jurisdictions.

I discuss a multilateral (at the continental level) application of the unitary approach within the recently adopted African Continental Free Trade Agreement (AfCFTA), which is akin to the EU's single and internal market.

I argue here that the shift to the unitary approach to income allocation is necessary and overdue if Nigeria (and indeed Africa) is to avert the erosion of its tax bases and keep hold of due taxable profits within its jurisdiction.[532] At a continental level, the adoption of the AfCFTA by African countries provides the

[531] Picciotto, supra note 29. In his paper, Picciotto reveals that most African countries have provisions in their domestic laws akin to article 9 of the model conventions.

[532] Giammarco Cottani, "Formulary Apportionment: A Revamp in the Post-Base Erosion and Profit Shifting Era?" (2016) 44 Intertax, Issue 10, at 755−760. Cottani's paper examines the application of the unitary approach from a developing country perspective, which African countries are. Cottani argues that the unitary approach would allow more developing countries to share more profit in the global value chain of the MNE group and address the issues of lack of comparables and absence of public data of comparables, which makes the application of the arm's length principle, difficult.

right opportunity for African countries to overhaul their tax systems and adopt a tax system that ensures that profits are declared and taxed where the economic activities occur.

Multinationals have no incentive to pay more taxes than required by law and may be expected to minimise their tax liabilities to the fullest legally permissible extent in order to appease their shareholders.[533]

Achieving a distribution of income that aligns where profit is declared with where the economic activities occur requires effective taxation regulations. This is where African governments can lead. As such, the responsibility is on African governments to agree on an international regulatory framework that ensures that countries are adequately compensated for the exploration of their resources.[534]

1.2 Objectives of the Chapter

There exists an increasingly rich literature on the unitary approach to income allocation.[535] However, recent literature on the subject is sparse in its applicability, workability and acceptability with respect to the African continent, both as a continent and at country-level.[536] This chapter contributes to the

[533] Avi-Yonah, supra note 322 at 497–553. In their paper, they argue that the current system provides incentive to earn income in low-tax jurisdictions, rewards aggressive tax planning and not compatible with any common metrics of efficiency.
[534] SPERI, "Paying a 'Fair Share' Global Political Economy Brief, No 8. Richard Munang & Robert Mgendi, "Deeper Regional Integration: An Opportunity for Africa" (2015), online: <https://thisisafrica.me/deeper-regional-integration-an-opportunity-for-africa/>; Munang and Mgendi argue that regional integration is an imperative whose time has come and should be urgently embraced by every citizen of Africa. They envisage that enhancing regional integration- both movement of people and trade- could potentially add US$ 20 billion annually in agricultural trade. The potential tax returns from this trade is enormous for the countries involved.
[535] Andrus supra note 432 at 89–107; Sol Picciotto, "International Corporate Taxation" (2016) ICTD Summary Brief 3; Sol Picciotto, Unitary Alternatives and Formulary Apportionment" (2017) in Taxing Multinational Enterprises as Unitary Firms. Institute of Development Studies, 2017; Clifton Fleming, Jr., Robert Peroni & Stephen Shay, "Formulary Apportionment in the U.S. International Income Tax System: Putting Lipstick on a Pig?" (2014) Michigan Journal of International Law, Vol 36, No 1.
[536] Erika Siu et al, "Unitary Taxation in Federal and Regional Integrated Markets" (2014) ICTD Research Report 3; Erika Siu et al, "Unitary Taxation in the Extractive Industry Sector" (2015) ICTD Working Paper 35. Though these papers reference African countries, due to their political

discussion on the applicability of the unitary approach in Africa, with a particular focus on the commodities industry.[537] Commodities here is given an expansive meaning to include the extractives sector, agricultural sector, manufacturing sector and other tangible goods sector. The economies of African countries are largely based on commodities, with the reported tax avoidance literature focused on the activities of multinational entities in the commodities industry. This claim does not undermine the importance of the service or intangible sector, which is keenly linked to the commodities industry, nor does it discount the upswing in the digital economy being experienced on the continent and across the globe. The arguments here are, however, relevant to most industries and economy-types, with minor deviations.

1.3 Outline of the Chapter

The chapter proceeds as follows. Section 2 considers the background to this discussion; the definition of unitary taxation, its attributes and origin. I briefly explore the history of unitary taxation without digging deep into its rich history. I conclude section 2 by discussing some of the controversies surrounding its application, showing how some of the arguments are not applicable today. Section 3 of the chapter analyses how multinational entities will be treated as unitary firms. Here, I focus on the concepts of ownership, control and management. I discuss the hurdles to implement unitary taxation and how these hurdles can be overcome. Section 4 of the chapter concludes by analysing the theoretical support for the global treatment and national treatment of multinational entities as unitary firms. The conclusion here is that treating multinational entities as unitary firms is in line with the nature of multinational entities, the foreign direct

composition and wealth of natural resources, they however, do not focus on the applicability of the unitary approach in African countries or as a continent. This thesis corrects this gap.

[537] Manuel Montes, Daniel Uribe & Danish, "Stemming 'Commercial' Illicit Financial Flows & Developing Country Innovations in the Global Tax Reform Agenda" (2018) South Centre Research Paper 87. This paper explores the introduction of a unitary method to the taxation of the extractive industries in developing countries.

investment model adopted by multinational entities and today's economic realities.

2 Background, Definition, Attributes and Origin of Unitary Taxation

2.1 Background to this Chapter

It is important to reiterate the reason for intensified calls for a unitary approach to taxing multinationals.[538] It arises out of the growing concern that the arm's length principle has failed in today's globalized world and the digital age.[539] The OECD's insistence on separate entity accounting and the continued relevance of comparability analysis in arriving at arm's length prices is unworkable for income allocation since in most business situations, comparables cannot be found and related entities do not act as independent entities.[540] As demonstrated in the preceding chapters, this allocation of income, based on the fiction of separate entity treatment and the arm's length principle, has resulted in a legal system that is incompatible with economic reality.[541] The result for countries has been the erosion of their tax bases and shifting of profits out of their jurisdictions to tax-favorable jurisdictions.[542]

Even the OECD, the main defender of the arm's length principle, concedes that "the integration of national economies and markets has increased substantially in recent years, putting a strain on the international tax rules, which were designed

[538] Baistrocchi, supra note 228 at 41–979.
[539] Monica Gianni, 'Transfer Pricing and Formulary Apportionment" (1996) Riverwoods, Vol 74, Issue 3, at 169; Avi-Yonah, supra note 528.
[540] Avi-Yonah, supra note 23.; Reuven Avi-Yonah & Ilan Benshalom, "Formulary Apportionment-Myths and Prospects Promoting Better International Tax Policy by Utilizing the Misunderstood and Under-Theorized" (2010) U of Michigan Public Law Working Paper No 221.
[541] Mold argues that the fiction of the arm's length principle has become unsustainable and costly for host countries. see, Andrew Mold, "A Proposal for Unitary Taxes on the Profits of Transnational Corporations" (2014) CEPAL Review 82, at 37–53.
[542] Avi-Yonah, ibid at 535.

more than a century ago."[543] In reaffirming consensus positions regarding the core principles of the global tax system, the OECD has stated that "the weaknesses in the current rules create opportunities for base erosion and profit shifting (BEPS), requiring bold moves by policy makers to restore confidence in the system and ensure that profits are taxed where economic activities take place and value is created."[544]

Such recent bold move by the OECD, is the 2018 Revised Guidance on the Application of the Transactional Profit Split Method (Guidance on TPSM).[545] The Guidance on TPSM signals a departure from the OECD's strong stance on income allocation based on the separate entity treatment and arm's length principle, and harmonizes with the unitary taxation approach in some respects, as explained more fully below.[546] Its recent policy note on the digital economy (Policy Note)[547] informed the public that the OECD was considering "solutions that go beyond the arm's length principle."[548] This is significant given that the OECD had over the decades strongly held to its conviction of the workability of the arm's length principle.[549]

---

[543] OECD (2018), Revised Guidance on the Application of the Transactional Profit Split Method: Inclusive Framework on BEPS: Action 10, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris, Foreword, at 3, online: <www.oecd.org/tax/beps/revised-guidance-on-the-application-of-the-transactional-profit-split-method-beps-action-10.pdf>.

[544] OECD (2018), Revised Guidance on the Application of the Transactional Profit Split Method: Inclusive Framework on BEPS: Action 10, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris, Foreword, at 3, online: <www.oecd.org/tax/beps/revised-guidance-on-the-application-of-the-transactional-profit-split-method-beps-action-10.pdf>.

[545] OECD (2018), Revised Guidance on the Application of the Transactional Profit Split Method: Inclusive Framework on BEPS: Action 10, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris, online: <www.oecd.org/tax/beps/revised-guidance-on-the-application-of-the-transactional-profit-split-method-beps-action-10.pdf>.

[546] Robert Robillard, "BEPS: Is the OECD Now at the Gates of Global Formulary Apportionment?" (2015) 43 Intertax, Issue 6, No 7, at 447−453.

[547] OECD (2019), "Addressing the Tax Challenges of the Digitalisation of the Economy- Policy Note" OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris.

[548] OECD (2019), "Addressing the Tax Challenges of the Digitalisation of the Economy- Policy Note" OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris, at 3.

[549] See OECD, "2017 Model Tax Convention on Income and Capital" (December 2017), 7th ed., Paris, online: Online: <https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#>.

The unitary approach is one solution that is fundamentally different from the arm's length principle. As discussed in chapter 1 above, the unitary approach to income allocation requires consolidation of accounts of related entities to arrive at a global profit and the apportionment of the global profit to taxing jurisdictions based on a pre-determined formula.[550] Under a unitary approach, the concept of "related entities" captures both controlled subsidiaries and permanent establishments of a corporate group.[551]

The alternative of unitary taxation has become more appealing than ever. Its proposed adoption by the EU for its single market and recent discussions by the World Bank and the IMF on its applicability, have encouraged research and policy interests by relevant stakeholders.

For the EU, adopting the unitary approach to income allocation is premised on adopting an effective tool for attributing income to where the value is created.[552] It seeks to adopt an allocation system that supports the proper functioning of the internal market, by shaping the corporate tax environment in the EU in accordance with the principle that companies pay their fair share of tax in the jurisdiction(s) where their profits are generated.[553] The relevant questions here are whether the African continent is prepared for such shift in its tax system and whether structures are in place for the adoption of a unitary taxation approach. My answer to both questions is yes.

---

[550] Wolfgang Eggert & Andreas Haufler, "Fiscal Policy in Action- Coordination cum Tax Rate Competition in the European Union" (2006) FinanzArchiv/ Public Finance Analysis, Vol 62, No 4, at 579–601.
[551] Reuven Avi-Yonah, "Three Steps Forward, One Step Back? Reflections on 'Google Taxes and the Destination-Based Corporate Tax" (2016) Nordic Tax J, Vol 2, at 69–76
[552] European Parliament, "Draft Report on the Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)" (2017) Committee on Economic and Monetary Affairs 2016/0336(CNS), online: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-%2F%2FEP%2F%2FNONSGML%2BCOMPARL%2BPE-608.035%2B01%2BDOC%2BPDF%2BV0%2F%2FEN>
[553] Christian Valenduc, "Corporate Income Tax in the EU, the Common Consolidated Corporate Tax Base (CCCTB) and Beyond: Is it the Right Way to Go?" (2018) European Trade Union Institute Working Paper 06.

As explained in Chapter 1, in March 2018, African leaders in Kigali, Rwanda, adopted the African Continental Free Trade Agreement (AfCFTA). The AfCFTA, when in force, will remove tariff and non-tariff barriers to intra-African trade of goods and services. It seeks to promote the development of regional and continental value chains. As at April 2019, 23 countries have ratified the AfCFTA, thereby bringing the AfCFTA into force.[554]

The AfCFTA contains no provision on the allocation of taxable income among trading countries. As such, the AfCFTA arguably adopts the current global tax system, which treats companies in a group as separate from each other. Since countries subject to the AfCFTA will trade goods and services in other countries (what we call host countries) through subsidiaries[555] or through PEs, tax minimisation through base erosion and profit shifting activities is possible.[556] Countries that have signed up to the multilateral agreement will have to deal with the national tax laws of 53 other signatories to the AfCFTA. The difficulties this brings are evident in the literature and the EU's decision to adopt a Common Consolidated Corporate Tax Base (CCCTB)— the EU's version of the unitary approach to income allocation—in its single and internal market. As Africa moves to adopt a regional trade regime, following the footsteps of the EU, it must learn from the experiences of its European counterpart.[557]

This is particularly important considering that Africa has the lowest level of intra-continental trade among continents of the world.[558] Encouraging intra-continental trade demands the removal of tariff and non-tariff barriers among the AfCFTA parties. As shown by the AfCFTA, this should rank top in the priorities of African

[554] Twenty-two countries were required to ratify the AfCFTA in their countries for it to come into force.
[555] Some countries' laws, such as Nigeria, make the incorporation of companies by foreign entities that intend to carry out business compulsory.
[556] Weiner, supra note 35 at 25−56.
[557] Danuse Nerudova, "Common Consolidated Corporate Tax Base: Sharing the Tax Base under Formulary Apportionment" in Stavárek D & Vodová, eds., 2011; Proceedings of the 13th International Conference on Finance and Banking at 279–288. Karviná: Silesian university in Opava.
[558] Munang supra note 529.

government.[559] A unitary taxation approach removes, to a significant extent an important non-tariff barrier (transfer mispricing, in this case) to intra-Africa trade.[560]

Nigeria, on its part, occupies a special place on the African continent. The country has retained for decades, the title of being "the Giant of Africa".[561] It is the largest economy in Africa with a GDP of USD 375.7 billion and a population of over 190 million people[562], placing it strategically as a large market for goods and services within the continent. The country is a commodities economy, with large oil and gas reserves, accompanied by a strong agricultural economy. There is a rich untapped mining industry, which is gradually gaining traction from the government and investors. For these reasons, the country is a major attraction to MNEs, both home-grown and foreign. As explained in chapter 2 above, the transfer pricing rules of Nigeria are modelled after the OECD's MTC and TPGs. The transfer pricing rules expressly incorporate the OECD's transfer pricing guidelines and convention[563] exposing the country to high level of IFFs, through transfer mispricing.

This discussion is very important today given the realisation that as the AfCFTA takes effect, intra-Africa trade will be dominated by MNEs, who make

[559] Siu, supra note 531.

[560] Li recommends the adoption of unitary approach on a regional basis, for example within the EU and the North American Free Trade Agreement.

[561] Peter Holmes, "Nigeria: Giant of Africa" (London: Swallow Editions, 1987).

[562]2017 World Bank data, accessible online: <http://databank.worldbank.org/data/views/reports/reportwidget.aspx?Report_Name=CountryProfile&Id=b450fd57&tbar=y&dd=y&inf=n&zm=n&country=NGA.>

[563] Regulations 12, 18 and 19 of the Income Tax (Transfer Pricing) Regulations, 2018, pursuant to the Federal Inland Revenue Service (Establishment) Act, 2007. Regulation 18 of the Transfer Pricing Rules provides thus:

"Subject to the provisions of regulation 19 of these Regulations, this regulation shall be applied in a manner consistent with-

a. the arm's length principle in Article 9 of the UN and OECD Model Tax Conventions on Income and Capital for the time being in force; and
b. the OECD Transfer Pricing Guidelines for Multi-National Enterprises and Tax Administrations, 2017 and the UN Practical Manual on Transfer Pricing for Developing Countries, 2017, as may be supplemented and updated from time to time.

extraordinarily high profits on the continent[564]. Africa must be equipped to effectively tax these profits. Given that intra-firm trade accounts for a significant amount of world trade,[565] the potential international income allocation issues, which is more complex in intra-firm transactions[566] must be addressed.[567]

2.2 Definition and Attributes of Unitary Approach

The unitary approach to income allocation is used in this chapter to represent two phenomena: treating related entities of a corporate group as a single firm; and the formulary apportionment of the global profit arising from such unification. The phrase "unitary taxation" is distinct from the phrase "formulary apportionment".[568] As such, controversy exists on the appropriate description of the allocation approach.

Some authors adopt the phrase "unitary taxation" to represent both the acts of consolidating accounts of entities in a corporate group and the subsequent apportionment of the global profit using a formula. Others have distinguished these functions, arguing in some cases, that they are mutually exclusive. They argue that a taxing jurisdiction can adopt the unitary taxation of companies, without adopting formulary apportionment; and vice versa. This is seen in the arguments for residence-based taxation,[569] destination-based cash flow transaction (DBCFT),[570] which are non-formulary allocation methods based on the unitary treatment of companies.

---

564 Mold, supra note 536. Mold argues that "the profitability of the investing firms in poor regions like Sub-Saharan Africa is extraordinarily high…there is growing evidence that transnational corporations (TNCs) are paying less and less in terms of tax".
565 Cooper, supra note 241.
566 Li, supra note 39 at 823–833.
567 Jon Bischel, "Tax Allocations Concerning Inter-Company Pricing Transactions in Foreign Operations: A Reappraisal" (1973) Virginia Journal of International Law, Vol 13 at 90–515.
568 Runkel supra note 32.
569 Julie Bouthillier, "Residence-Based Taxation and FAPI: A World of Fictions" (2005) Canadian Tax Journal, Vol 53, No 1;
570 Avi-Yonah, supra note 546 at 69–76; Alan Auerbach, et al, "Destination-Based Cash Flow Taxation" (2017) Oxford University Center for Business Taxation, Working Paper, 17/01.

Others have posited that formulary apportionment is applicable to the separate entity treatment of companies, and companies do not have to be treated as unitary firms before apportioning their profits using a formula.[571] This is the practice in Canada, which applies the formulary apportionment method to provincial level corporate income taxes without consolidating the entities.[572] Without engaging in these arguments, which all have merits, I have carefully adopted the phrase, "unitary approach" for convenience and clarity, to imply unitary taxation and formulary apportionment, individually and collectively.[573]

The unitary approach describes a tax system where multinational corporations are taxed as single economic entities.[574] The single economic entity produces consolidated accounts and one income and profit statement. The profit (or loss) is then divided among the entities, based on pre-agreed formula, designed to represent the contributions of the related entities to the profit, or the economic activity or presence of the group activities in the taxing jurisdictions.[575] In other words, this approach "employs a formula for dividing the income of a multinational business among the locations in which it is earned".[576] The use of a pre-determined formula distinguishes the unitary approach from the transactional profit split method.

Three factors- assets, labour and sales- are the most widely adopted factors in the apportionment formula, which in some cases are weighted equally (the Massachusetts Formula) or unequally, reflecting the relevant importance of each

[571] Avi-Yonah & Benshalom, supra note 535. They argue that formulary apportionment can be applied to MNE income without consolidating the income of the entire MNE group; see, Avi-Yonah supra note 40.

[572] Weiner, supra note 35 at 25–56.

[573] This phrase was adopted by Nerudova and Solilova in their paper on the impact of the CCCTB on Czech Republic. See, Danuse Nerudova and Veronika Solilova, "The Impact of the CCCTB Introduction on the Distribution of the Group Tax Bases Across the EU: The Study for the Czech Republic" (2015), Prague Economic Papers, University of Economics, Prague, Vol. 2015, Issue 6, at 621–637.

[574] Li, supra note 39 at 823–833.

[575] Jamie Morgan, "Corporation Tax as a Problem of MNC Organisational Circuits: The Case for Unitary Taxation" (2016) The British Journal of Politics and International Relations, Vol 18, No 2, at 463–481.

[576] Nerudova supra note 568 at 621–637; see, Hilda Wasson & Robert Weigand, "Unitary Taxation: A Search for Fairness" (1988) Business Horizons, Vol. 31, Issue 2, at 45–50.

factor to the profit generation.[577] It is the conviction of proponents of unitary approach that these factors are linked to the place where a company derives profit and as such are more resilient to aggressive tax planning than the current arm's length standard.[578]

In addition, the unitary approach to income allocation is theoretically sound. It captures the essence of the MNE. As shall be seen later in the discussion of Hymer's theory of FDI and MNE, MNEs make extraordinarily high profits as a result of the ability to integrate their functions across borders or businesses.[579] This ability to integrate takes advantage of economies of scope and scale, and significantly reduces costs. Reduction in research and development costs, managerial cost, operation cost, information gathering and sharing cost, transaction cost, financing cost, regulatory cost implies that the MNE is better off than its solely domestic counterpart.[580] The managerial practice of a MNE is akin to that of a sole proprietorship or partnership, with the decision-making being made by one individual or group of individuals. If sole proprietorships or partnerships are not treated as separate from their owners, treating MNEs as separate entities is at crossroads with actual business practices. This, the unitary approach seeks to correct. The unitary approach to income allocation may be applied at a national level or cross-border.[581]

Furthermore, the unitary approach acknowledges that from a business perspective, MNEs operate as integrated firms, and not as separately incorporated companies in various countries, as treated by law.[582] As one author puts it, the "relationships between members of the MNE group are governed predominantly

[577] Massimo Agostini, "US Perspectives of Worldwide Unitary Taxation" (1989) Penn State International Law Review, Vol 7, No 2.
[578] Estefania Llopis, "Formulary Apportionment in the European Union" (2017) 45 Intertax, Issue 10 at 631–641.
[579] Mold, supra note 536.
[580] Stephen Hymer, The International Operations of National Firms: A Study of Direct Foreign Investment, (Cambridge, MA: MIT Press,1976)
[581] European Commission, "Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)" European Commission COM (2016)
[582] Spencer, supra note 235.

by control, not by legal contract."[583] It recognises that the entire business of a corporate group contributes to its ultimate profit. According to Swan, this allocation formula "is a reasonably good proxy for where income is earned".[584] This system of income allocation has been described as "far more legitimate and simpler to implement than the current system".[585]

The unitary approach disregards intra-group transactions, and as such, transfer pricing. It addresses the deep structural flaw in the existing system, which treats related entities in a multinational group as separate from each other.[586] It discounts the relevance of the comparability analysis, thus, eliminating the need to find comparables for benchmarking purpose. Firms may still have opportunities to shift profits to preferred taxing jurisdictions, however, this time around this shift is accompanied by real investment and economic activities, unlike the present use of shell companies and paper investment. Tax havens, who do not provide the enabling environment for real economic activities will lose out on the income allocation as they will not be caught under the pre-determined formula.[587]

Finally, the unitary approach is a system of source taxation, making redundant the residence of the company, thereby limiting the relevance of traditional tax havens and the use of hybrid structures.[588]

2.3 Historical Discussion of Unitary Approach

The United States presents a rich history of the application of unitary approach to income allocation, which dates back to the early 20th century.[589] The system,

---

[583] Li, supra note 39. Li argues that while contract may have real economic substance to independent parties who bargain for its terms, it may have no or insignificant meaning to related parties.
[584] John Swain, "Same Questions, Different Answers: A Comparative Look at International and State and Local Taxation" (2008) 50 Ariz. L. Rev 111
[585] Picciotto, supra note 186.
[586] Montes supra note 532.
[587] Ibid.
[588] Sol, supra note 485.
[589] Shu-Chen Chen, "Tax Avoidance in the Sales Factor: Comparison Between the CCCTB Directive and USA's Formulary Apportionment Taxation" (2017) Indian Journal of Tax Law, 2017.

which arose as a way of apportioning income from railway business in the 1870s[590] has grown to become the common practice in more than 40 US states today.[591]

U.S. courts have set the standards for determining whether activities of related entities are unitary for the purpose of being consolidated as a whole. In Butler Bros, the court held a unitary business to be present where there is: (1) unity of ownership; and (2) unity of operations, such as joint purchasing, advertising, accounting and management.[592] Unity of ownership goes to the legal relationship between the entities in a corporate group. The unity of operations refers to the economic relationship between the entities. Another standard established by the U.S. Supreme Court in the determination of a unitary business is the "contributions to income resulting from functional integration, centralization of management, and economies of scale".[593] This standard emphasizes the economic relationship between the entities.

Uniformity in the application of the unitary approach in the United States came as a result of the enactment of the Uniform Division of Income for Tax Purposes Act (UDIPTA) in 1957, which recommended the unitary approach to income allocation to states. The UDIPTA recommended a three-factor apportionment formula- property, payroll and sales- weighted (the Massachusetts Formula). This apportionment formula acknowledges the production side of income generation (property and payroll) and the market side of income generation (sales).[594] According to Swain, the property represents the ratio of the taxpayer's in-state property to its property everywhere; the payroll factor represents the ratio of the

[590] State Railroad Tax Cases (1876) 92 US 575. See the Underwood Typewriter case, decided by the United States Supreme Court, approving the use of formulary apportionment in the allocation of income of a single corporation among several states. See, Underwood Typewriter Co. v. Chamberlain (1920) 254 US. 113.
[591] Morgan, supra note 570 at 463–481.
[592] Butler Bros v. McColgan [1942] 315 U.S. 501; see, Kimberley Reeder, Sarah McGahan & Jon Sedon, "The Unitary Group's Identity Crisis: Is There Really an 'I' in Unitary?" (2008) The State and Local Tax Lawyer. Symposium Edition, at 83–114.
[593] Mobil Oil Corporation v. Commissioner of Taxes of Vermont. (1980) 445 US. 425; see, Mark Segal, "The Unitary Tax Reconsidered" (1994), Journal of Applied Business Research, Vol 10, No 3, at 1–9.
[594] Swain, supra note 579.

taxpayer's in-state payroll to its payroll everywhere; and the sale factor is the ratio of the taxpayer's in-state sales to its sales everywhere.[595]

Ten years later, the United States enacted the Multistate Tax Compact (MTC) Act, which adopted the recommendations of the UDIPTA.[596] However, while states in the United States still practice the unitary approach, a good number of them have departed from the Massachusetts Formula, prescribed by the UDIPTA. Some states have adopted a single-sales factor, while others still applying the three-factor formula, have varied the weights to attract and retain investments.

Canada, on its part, adopts a two-factor apportionment factor with equal weights to payroll and sales by destination.[597] However, going by the EU's CCCTB proposal, it would seem the Massachusetts Formula (weighted factors formula) is representative of the factors of production and the sale of goods. We shall return to this in later discussion below.

2.4 Debates and Controversies Surrounding the Application of Unitary Taxation

The case for the adoption of the unitary approach to income allocation has drawn mixed reactions from stakeholders. Some are convinced it is a more effective way of profit allocation than the current system.[598] Others are those who are convinced that there is no better alternative; that the current system can be improved upon; or that the unitary approach will not bring about the desired change.[599]

Given the nature of global tax rules, which though are soft laws, yet, are almost universal in adoption and application by countries, any proposed shift would

---

[595] Ibid.
[596] Shu-Chen Chen, supra note 489.
[597] Katerina Krchniva, "Comparison of European, Canadian and U.S. Formula Apportionment on Real Data" (2014) Procedia Economics and Finance, Vol 12, at 309−318.
[598] Ezenagu, supra note 36.
[599] Clifton Fleming, Robert Peroni & Stephen Shay, "Formulary Apportionment in the U.S. International Income Tax System: Putting Lipstick on a Pig?" (2015) Michigan Journal of international Law, Vol 36, No 1.

require the buy-in of the supranational bodies, especially the OECD, whose position on the unitary approach has unfortunately, become "law" at the global level.[600]

Its long-held position on the adoption of a unitary approach as the global tax system, is that it would not be acceptable in theory, implementation or practice.[601] Holding strongly to the viability of the current global tax system,[602] it argues that "a move away from the arm's length principle would abandon the sound theoretical basis on which the arm's length principle is founded and threaten the international consensus, thereby substantially increasing the risk of double taxation".[603]

It opines that the most significant concern with the global formulary apportionment is achieving a system that protects against double taxation and ensures single taxation.[604] In its opinion, addressing the concern would require substantial international coordination, consensus on the predetermined formula and composition of the group.

Other concerns of the OECD towards the move to global formulary apportionment are: the use of pre-determined formula for all transactions as against a case-by-case formula determination, which it finds arbitrary; the measurement of the global tax base; consensus of the common accounting system; and failure of the global formulary apportionment method to recognize important geographical

[600] OECD, "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration 2017, para C1 of Ch I.
[601] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para 1.15, at 38
[602] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para. 1.14, at 38. Wolfgang Schon, "International Taxation of Risk" (2014) Working Paper of the Max Planck Institute for Tax Law and Public Finance No 2014–03.
[603] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para 1.15 at 38.
[604] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para 1.22 at 40.

differences, and separate company efficiencies.[605] Its conclusion is that reaching an agreement on global formulary apportionment would be time-consuming and extremely difficult, and "it is far from clear that countries would be willing to agree to a universal formula".[606] Other authors have questioned the viability of the unitary approach in addressing tax avoidance and achieving a fair distribution of income.[607]

Nonetheless, a good number of governments, policy-makers, academics, and researchers in civil society groups and think-tanks are convinced that a shift to a unitary approach will ensure that profits are taxed where the economic activities occur, and value is created.[608] In addition, if recent publications by the OECD are to be relied upon, it appears that the OECD may be open to considering other allocation approaches that go beyond the arm's length. For instance, the Policy Note on the Digitalisation of the Economy will consider other allocation approaches beyond the arm's length principle, especially in the allocation of residual profit.[609]

Some of the pillars to inform the allocation approach, as identified by the OECD include the: allocation of taxing rights according to user contribution; marketing intangible approach, which takes into account the market jurisdiction contribution to the profit and allocating taxing right to the market jurisdiction; significant economic presence approach, which departs from the PE rule; and finally a tax back approach, which allows taxing jurisdictions to tax back profit shifted to no or low tax jurisdictions, by resident and source countries.[610]

---

[605] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para 1.25, at 41.
[606] OECD (2017) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 2017. OECD Publishing, Paris OECD, para 1.22, at 38.
[607] Julie Roin, "Can the Income Tax be Saved? The Promise and Pitfalls of Adopting Worldwide Formulary Apportionment" (2008) Tax Law Rev, Vol 61, No 3; Arthur Cockfield, "Formulary Apportionment Versus the Arm's Length Principle: The Battle Among Doubting Thomases, Purists, and Pragmatists" (2004) Canadian Tax Journal, Vol 52, No 1; Gianni, supra note 534.
[608] See chapter 3 of this PhD thesis on reform efforts of the IMF, ICRICT and BMG, which support the adoption of the unitary approach.
[609] OECD (2019), "Addressing the Tax Challenges of the Digitalisation of the Economy- Policy Note" OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris.
[610] Ibid.

These recent developments at the OECD level are encouraging and have evoked mostly positive reactions from stakeholders.

3 Treating Multinational Entities as Unitary Firms

In this section, I focus on the issues surrounding the adoption and implementation of the unitary approach by Nigeria. The discussion here applies to the adoption of the unitary approach at a multilateral level, such as the AfCFTA framework. This is by no means an exhaustive discussion of the issues. I have limited the discussion here to the continuous relevance of the OECD's transfer pricing methods (domesticated in most national laws), especially the transactional profit split method; establishing the consolidated group; the weighting of the factors; and finally, the issue of tax sovereignty and tax cooperation. In a 2017 paper, I had addressed other challenges to the implementation of a unitary approach not addressed here.[611]

3.1 OECD's Insistence on Transactional Approach and Comparability Analysis

The 2018 Guidance on the Transactional Profit Split Method (Guidance on TPSM)[612] issued by the OECD indicates adoption of a practical approach to income allocation. This Guidance on TPSM aligns with the existing practice of tax authorities, who rely on the profit split method, in the absence of market comparables. It must be observed here that the Guidance on TPSM 2018 is comparatively, a formulary approach to income allocation, albeit an inefficient one. I discuss this below.

[611] Ezenagu, supra note 36.; Cottani, supra note 527 at 755–760.

[612] OECD (2018), Revised Guidance on the Application of the Transactional Profit Split Method: Inclusive Framework on BEPS: Action 10, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris, online: <https://www.oecd.org/tax/transfer-pricing/revised-guidance-on-the-application-of-the-transactional-profit-split-method-beps-action-10.pdf>.

The Guidance on TPSM recommends the use of the profit split method by taxpayers and tax authorities in given circumstances. These circumstances are where: (1) each party makes unique and valuable contributions to the controlled transaction; (2) the business operations are highly integrated, so the contributions of the parties cannot be reliably evaluated in isolation from each other; and/or (3) the parties share the assumption of economically significant risks, or the parties separately assume closely related economically significant risks.[613] Paragraph 2.133 of the Guidance on TPSM describes high integration of parties as “the way in which one party to the transaction performs functions, uses assets and assumes risk is interlinked with, and cannot reliably be evaluated in isolation from, the way another party to the transaction performs functions, uses assets and assumes risks.”[614]

The Guidance provides two approaches to splitting profit- a contribution analysis and a residual analysis. The contribution analysis splits the profit among the entities based on the split of profits that would be expected between independent entities- an arm’s length split of profit. This is technically, the application of one-sided transfer pricing method to the contribution of each party to the transaction. This is appropriate where information on uncontrolled comparables for benchmarking purposes is available.

The residual analysis, on its part, first splits profits between the parties based on their routine contribution, as in the contribution analysis, and then splits the remaining combined profits between the entities based on the analysis of the relative value of the second category of contributions by the parties.

Similar to the unitary approach, the Guidance recommends profit split factors that may be adopted by the entities. These are: (1) a proportional figure, such as a 30%-

[613] Paragraph 2.126 of the Guidance on TPSM.
[614] Paragraph 2.133 of the Guidance on TPSM.

70$ split;[615] (2) asset/capital-based factors, such as operating assets, fixed assets, intangibles; (3) cost-based factors, such as research and development expenses, marketing expenses, engineering expenses; (3) labour factor, such as headcount; sales based factor, such as incremental sales, employee compensation for value generation.[616] These factors may be applied individually or collectively, depending on the circumstances of the transaction.[617]

Though the Guidance on TPSM attempts to achieve a measure that ensures profits will be reported "where the economic activities that generate them are carried out and where value is created",[618] it fails for obvious reasons. One reason is its insistence on the arm's length standard, which is a limitation of the current system. Paragraph 2.114 of the Guidance on the TPSM provides that the "transactional profit split method seeks to establish arm's length outcomes or test reported outcomes for controlled transactions in order to approximate the results that would have been achieved between independent entities engaging in a comparable transaction or transactions".[619] This implies that the TPSM relies on the inefficient comparability analysis.

This position of the OECD is quite confusing, given in that in paragraph 2.119 of the Guidance on TPSM, it mentions the main strength of the TPSM as offering a solution to cases where both parties make unique and valuable contributions to the transaction, and no reliable comparables information exist for the parties. It admits that comparables for unique and valuable contributions by each party to the transaction are "seldom found because they are a key source of economic advantage",[620] and "are not comparable to contributions made by uncontrolled parties in comparable circumstances".[621]

---

[615] Paragraph 2.170 of the Guidance on TPSM. This is akin to Schanz "economic allegiance theory" recommendation of a 25%-75% split for resident and source jurisdictions, respectively; Klaus Vogel, supra note 79.
[616] Paragraph 2.171 of the Guidance on TPSM.
[617] Paragraph 2.169 of the Guidance on TPSM.
[618] The Guidance on TPSM, Foreword.
[619] Paragraph 2.114 of the Guidance on TPSM.
[620] Paragraph 2.130 of the Guidance on TPSM.
[621] Paragraph 2.130 of the Guidance on TPSM.

In addition, the Guidance on TPSM provides that if information on reliable comparable uncontrolled transactions is available, it is unlikely that the TPSM will be the most appropriate method.[622] Since the OECD admits to the unavailability of comparables information, and the importance of the TPSM in those circumstances where comparables information is unavailable, demanding an arm's length standard for transactions which are not comparable falls on its face and is impractical.

The other limitation of the TPSM is its insistence on its application on an individual transaction basis. The OECD prescribes that the process of the transactional profit split should have regard to the commercial and financial relations between the associated enterprises, including an analysis of what each party to the transaction does, and the context in which the controlled transactions take place.[623] This makes the process of tax compliance and enforcement complex, expensive and time-consuming for both taxpayers and tax authorities. This is especially the case for African countries, that do not have the capacity and resources of their Global North counterparts.[624] A unitary approach applies to all taxpayers within the taxing jurisdiction or members of an industry or business sector, when applied as a form of safe harbour regime. It is to the unsuitability of the arm's length principle in today's modern economy, that the proposal for unitary approach is made. Next, I consider the relationship that must exist for a multinational group to be treated as a single entity for tax purpose.

3.2 Legal or Economic Control

The first step towards adopting and applying the unitary approach is to determine the consolidated group subject to the allocation method. This implies identifying the entities which have relationship with the parent entity for tax purpose. After

[622] Paragraph 2.143 of the Guidance on TPSM.
[623] Paragraph 2.125 of the Guidance on TPSM.
[624] Wier, supra note 362.

identifying these entities, their accounts are consolidated with that of the parent entity to form one consolidated account. Determining the entities in a consolidated group could be based on the legal relationship between the entities or on their economic relationship. In some instances, it is based on both relationships.

Determining the consolidated group based on legal relationship relies on the ownership of stock in the companies. In most cases, an ownership value of more than 50% of the stock value of the companies will be sufficient to establish legal relationship. This ownership could be direct or indirect, as determined by the local law of the countries involved.

An economic relationship determination of the corporate group relies on common control, shared management, single trade or business and in some cases, rights to the profits of the companies. For instance, California law requires all the business income from all activities of a unitary business to be combined into a single report. The unitary business in California refers to all of the elements comprising a single trade or business.[625]

The company law of Nigeria prescribes a simple majority of the stock ownership of a company for a shareholder to be treated as a controlling shareholder of the company. In practice, controlling shareholders hold more than fifty percent of the total shareholding of the company.[626] In some cases, a special majority, as prescribed by the parties may be required to control the company.[627] The simple majority, arguably, should be sufficient to establish a legal relationship between the parties. However, from practice, one sees instances where a shareholder with less than 50% of the ordinary shares and/or voting shares of the company weighs significant power over the affairs of the company, to be considered the parent company of the group. This is common in many African countries where foreign

[625] RK Wiederstein, "California and Unitary Taxation: The Continuing Saga" (1992) Indiana International & Company Law Review, Vol 3, No 135; Bronwyn McNeill, "California's Recent legislation on Unitary Taxation and Barclay's Bank PLC v. Franchise Tax Boards of California" (1994) The Tax Lawyer, Vol 48, No 1.
[626] Companies and Allied Matters Act, c 20, 2004, s 233.
[627] Companies and Allied Matters Act, c 20, 2004, s 46.

participation in specific industries is limited to a minimum shareholding.[628] Lawyers and accountants have been known to find creative ways to still place control of the company in the minority shareholder.

As a result, legal relationship is insufficient to establish a consolidated group for tax purposes. An effective approach is to base the determination of the consolidated group on both legal and economic relationships. This recommendation is in agreement with the EU CCCTB proposal. The proposal recommends a two-part test to establish the consolidated group. The first test is a legal control test, which has been set as having more than 50% of the voting rights of related entities. The second test is an ownership test, described as owning more than 75% of equity or owning more than 75% of rights giving entitlement to profit. Both control thresholds must be met throughout the tax year or the failing company will not be included in the consolidated group.[629]

The recommendation here is that Nigeria, and indeed African countries desirous of adopting the unitary approach, adopt both legal and economic control, individually and or jointly in determining the companies in the corporate group for tax purpose. This determination of the legal and economic relationships may be determined on an industry basis or broadly for MNEs doing business in the countries or on the continent, as the case may be.

On unilateral adoption of the unitary approach, the threshold of legal relationship may be determined by taking into account the national law stipulation of the tax jurisdiction on majority ownership in a company. Some tax jurisdictions prescribe maximum ownership a shareholder (mostly, foreign shareholders) may own in a company. This prescription could be directed to certain industries as a protectionist regime in the form of local content regulations.[630] Where a

---

[628] For instance, the Nigerian Oil and Gas industry Content Development Act 2010, Act No 2, provides that 51% of shares of a Nigerian subsidiary will have to be owned by Nigerians.
[629] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final).
[630] See, for instance, the Nigerian Oil and Gas industry Content Development Act 2010, Act No 2 (Local Content Act), online: <https://www.ncdmb.gov.ng/images/GUIDELINES/NCACT.pdf>. The

multilateral adoption of the unitary approach is the case, an agreement on the threshold to establish the legal relationship must be agreed upon by countries involved. The recommendation here is to adopt a simple majority threshold, protected by economic relationships.

The determination of economic relationship presents a more difficult consideration. As stated in chapter 2 of the thesis, management service agreements, technical service agreements and franchise agreements are some of the forms of economic relationships which exist between related entities. It is important to determine other forms of economic relationships, which exist in the tax jurisdiction where a unilateral adoption is considered, or the aggregate forms of economic relationships present on the continent where a multilateral adoption is considered. A general anti-avoidance rule (GAAR) should be implemented, where regardless the form of a relationship between parties, if the substance suggests the presence of economic relationship between the parties, the parties should be treated as unitary firms for tax purpose.

3.3 Selection of the Factors and Weighting Formula

It must be stated here that the factors and weight to be adopted in the apportionment formula stem from a policy choice, and not from a precise measurement of the contribution of each related entity to the global profit. Understanding this takes away the pressure from African countries to achieve a perfect apportionment formula. The focus should be on arriving at a formula which ensures that taxable profits, commensurate to their contributions to the global profit of the corporate group, are declared and returned in their jurisdictions.

The common factors, recommended here for Nigeria are assets, labour and sales. I shall discuss these factors.

Local Content Act prescribes thresholds for the use of local services and materials in the oil and gas industry.

i. Assets

The assets factor in the unitary approach recognises the contribution of the production aspect of income generation. Assets are split into tangible assets and intangible assets.[631] Recent literature has questioned the validity of the assets factor in the apportionment formula, for obvious reasons. One, it is vulnerable to manipulation if not carefully delineated. For instance, the recognition of intangible property in the asset factor may create opportunities to shift profits as these assets are easily mobile.[632] Valuing intangible assets is a herculean task as there are no comparables, in most cases for benchmarking purpose.[633]

For tangible assets, valuation of the assets poses challenges. Should the value of the assets be based on historical cost or actual cost of the assets?[634] A historical cost will fail to take into account the appreciation or depreciation of the assets in a fiscal year, and as such, the real contribution of the assets to the global profit. Actual cost will pose administrative difficulty for the tax authority who would have to audit the valued figures presented by the taxpayers. For the taxpayer, it will increase cost of tax compliance, since taxpayers will be required to obtain the services of asset valuers in each fiscal year to determine the actual cost of the assets for the fiscal year. There exists potential for disputes between the taxpayers and tax authorities as they may not agree on the value of the assets. Where there does not exist an agreeable scientific measurement standard or a binding opinion of a third party, this dispute could cause significant delay in the tax compliance and administration process. An approach that may be adopted is the stipulation of agreeable ranges by the tax authority. These ranges may be based on location, years of use or importance of the assets to the business.

[631] Walter Hellerstein, "The European Commission's Report on Company Income Taxation: What the EU Can Learn from the Experience of the US States" (2004) International Tax and Public Finance, Vol 11, Issue 2, at 199–220.
[632] Thomas Eichner & Marco Runkel, "Why the European Union Should Adopt Formula Apportionment with a Sales Factor" (2008) The Scandinavian Journal of Economics, Vol 110, Issue No 3.
[633] Li, supra note 39.
[634] Avi-Yonah supra note 535.

While intangible assets are the "crown jewels"[635] of the modern corporation, their acceptance in Nigeria is still evolving. As such, a valid suggestion is to exclude intangible assets from the asset factor, limiting the factor to tangible assets. This position aligns with the views of others who believe that since it is impossible to determine the location and value of intangibles, they should be ignored as a factor. According to McLure, including intangibles as a factor would force one into analysis similar to that under the separate accounting standard.[636] This opens the unitary approach to the challenges of the separate accounting standard it seeks to address. Hellerstein gives two reasons why intangibles should be excluded as a factor: one, intangibles are nebulous with respect to location, benefits and protections furnished by the state and the social costs incurred; secondly, their inclusion could be highly distorting.[637] Li argues that the cost of intangibles can be included in the payroll factor as salaries paid to engineers, scientists, managers and workers who participate in the research and development; as part of the asset factor for the equipment purchased to carry out the research and development or the value of products produced with the tangibles; as part of the sales factor for the cost of marketing the intangibles. Li's recommendation effectively allocates the value of intangibles on the basis of the payroll, sales and tangible property factors.[638]

The proposed EU CCCTB limits the assets factor to all fixed tangible assets owned, rented or leased.[639] It includes the asset factor in the economic owner and where the economic owner cannot be identified, the asset shall be included in the asset factor of the legal owner. Land and other non-depreciable fixed tangibles assets are to be valued at their historical cost. Depreciable fixed tangible asset is to be valued at the average of its value for tax purposes at the beginning and at the end

[635] Charles McLure, "Harmonizing Corporate Income Taxes in the European Community: Rationale and Implications" (2008) Tax Policy and the Economy, Vol 22, No 1, at 151–195. The author described intangibles as the crown jewels of the modern corporation.
[636] Charles McLure Jr, "Taxation of Electronic Commerce: Economic Objectives, Technological Constraints, and Tax Laws" (1997) Tax Law Review, Vol 52, No 3, at 269–423.
[637] Hellerstein, supra note 38 at 739–879.
[638] Li, supra note at 849.
[639] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final).

of a tax year. Leased or rented assets shall be valued at eight times the net annual rental or lease payment due, less any amounts receivable from sub-rentals or sub-leases.

Given the absence of any record of implementation of the unitary approach in any African country and the soundness of the EU CCCTB, especially at a continental level, my recommendation is that Nigeria (applicable to African countries under the AfCFTA) adopts the CCCTB's treatment of assets. It provides a logical start point for policy-making and implementation.

ii. Labour

The labour factor in the unitary approach takes into account the human capital production aspect of income generation.[640] It rewards the individuals who ensure the corporate group remains profitable. Controversies surrounding labour include the treatment of independent contractors and fringe benefits. Also, the composition of the labour factor.[641]

With regard to composition of the labour factor, experiences of states differ. In the U.S., under the UDIPTA, labour factor consists only of the total amount of payroll of the group.[642] Contrarily, in the proposed EU CCCTB, the labour factor shall consist of one-half of the total amount of payroll and one-half of the number of employees of the group.[643] The EU reasoning behind this is that, given the disparities in wages amongst Member States, a payroll-only factor will fail to achieve a fair distribution of income. As such, half of the labour factor should go to headcount of employees. This EU's approach is particularly relevant to African countries.[644]

[640] Erika Siu, supra note 531;
[641] Kerry Sadiq, "Unitary Taxation of the Finance Sector" (2014) ICTD Working Paper 25.
[642] Chen Chen, supra note 584.
[643] Picciotto, supra note 186.
[644] Ibid.

The EU CCCTB proposal is applicable and apt for African countries, where wages are very low relative to Global North countries. for instance, as at November 2018, the minimum monthly wage in Nigeria is 18,000 Naira (circa, USD 50).[645] This amount is less than a day's minimum wage in Canada. However, it is likely the case that most of the employees of a corporate group in the extractives and agricultural industries will be resident in Nigeria, though the total amount of the payroll therein, may not match the payroll of a few employees of the same multinational group resident in Canada. Headcount labour-factor could correct this disadvantage by allocating one-half of the income apportioned to the labour factor, to jurisdictions with the higher number of employees, as the case may be.[646] In the long run, this could influence higher wages for the employees in African countries, either as a result of improved compensation arising from more revenue or as a way of claiming more taxable profits allocated to the labour component of the formula.

As a tax avoidance scheme, the EU CCCTB prescribes that an employee shall be included in the jurisdiction where she physically exercises her employment under the control and responsibility of a group member, notwithstanding that the group member is not the original employer of the employee, nor the group member who pays the remuneration of the employee.[647] This is to safeguard source taxation of the jurisdiction where the employee physically exercises her employment. This is a practical approach and favourable to African countries who experience the influx of expats from other countries though they are not employees of the local companies. From a theoretical perspective, this recommendation reconciles with the cost and benefit theory of taxation, as these employees are made to contribute

[645] Felix Onuah, "As Election Nears, Nigeria Recommends 50 percent Minimum Wage Rise" (22, January 2019) Reuters, online: <https://www.reuters.com/article/us-nigeria-wage/as-election-nears-nigeria-recommends-50-percent-minimum-wage-rise-idUSKCN1PG1UX>
[646] Alex Cobham & Simon Loretz, "International Distribution of the Corporate Tax Base: Implications of Different Apportionment Factors under Unitary Taxation" (2014) ICTD Working Paper 27. The authors argue that apportionment according to the number of employees will benefit jurisdictions with lower per capita income. They claim that apportionment according to payroll will harm the lowest-income countries, while apportionment according to the number of employees will increase the size of their tax base.
[647] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final).

to the countries where they obtain benefits from and share in the cost of governance and infrastructure.

On the payroll factor, the EU CCCTB proposes that the payroll shall include all costs of salaries, wages, bonuses and all other employee compensation, including related pension and social security costs borne by the employer. This is in line with the current employee compensation standard in MNEs operating in Nigeria.

iii. Sales

The sales factor represents the demand side of the global profit.[648] The US UDITPA defines sales to capture gross receipts, not allocated as non-business income.[649] This definition covers the sale of goods, services, rentals and royalties. For sale of goods, the state of destination of the goods is credited with the income arising therefrom. For sale of services or sales other than tangible commodity, the sale is attributed to the state where the service is performed.[650]

This is similar in the proposed EU CCCTB. Under the CCCTB, sale of goods shall be attributed to the group member located in the Member State of the last identifiable location of the goods.[651] Supplies of services are included in the sales factor of the group member located in the Member State where the services are physically carried out or actually supplied.[652]

The controversy around the sales factor is whether the profit should be allocated to the destination of the goods or the origin of the goods, or to both destination and origin.[653] A destination of sales factor may not be advantageous to African countries. This is because such a factor rewards purchasing power, while

---

[648] Weiner, supra note 35. The author argues that by including sales in the formula reflects the notion that demand creates value; see, Cobham & Loretz, supra note 641.
[649] Chen Chen, supra note 584.
[650] Ibid.
[651] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final), at 14.
[652] Ibid.
[653] Swain, supra note 579.

excluding the origin of sale country.[654] Given that most African countries do not have large purchasing power, they may be locked out of potential income. This is a common reality for most developing countries. One way to address this is to recommend an origin-based plus destination-based factor, weighted equally. This will ensure that countries who are largely exporter of commodities will benefit from the income split.

To prevent tax avoidance arising from the sale of goods and services to state with no taxing jurisdictions, throwback provisions are included in the unitary approach.[655] A throwback provision attributes the sale to the state of origin where the state of destination cannot tax the income arising therefrom.[656] The EU's throwback provision deviates slightly from this. Under the EU CCCTB, where there is no group member in the Member State where the goods are delivered, or the services are supplied, or where goods are delivered, or services are supplied in a third country, the sales of goods and supplies of services shall be included in the sales factor of all group members in proportion to their labour and asset factors. Where the Member State where the goods are delivered, or the services are supplied, has more than one group member, the sales shall be included in the sales factor of all group members located in that Member State in proportion to their labour and asset factors. [657]

As observed, a throwback rule will increase the income of the jurisdiction(s) whose taxpayer(s) benefit from the sales to tax haven or jurisdiction which does not tax. It averts double non-taxation by ensuring that the income is taxed in a jurisdiction. It does not lead to double taxation since it only applies when the taxpayer in the tax haven or no-tax jurisdiction is not subject to tax in the state.[658]

[654] Peggy Musgrave, "Principles for Dividing the State Corporate Tax Base" (1984) in McLure, Jr., ed., The State Corporation Income Tax: Issues in Worldwide Unitary Taxation, Stanford Ca: Hoover Institution Press, at 228–246.
[655] Weiner, supra note 35 at 23; David Shipley, "The Limits of Fair Apportionment: How Fair is Fair Enough?" (2007) The State and Local Tax Lawyer. The Symposium Edition, at 93–134.
[656] Weiner, supra note 650.
[657] Deloitte, "EU Developments: C(C)CTB and Corporate Tax Reform" (27 October 2016), Deloitte, online: <https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/Tax/ie-Tax-EU-Developments-ccctb-and-corporate-tax-reformV3.pdf>.
[658] Shipley, supra note 555.

This rule is advantageous to African countries who experience the outstripping of earnings through artificial transactions and or shift of profits to tax havens, leaving little or nothing in the jurisdictions where the economic activities take place.

iv. Weighting of the Factors

Some authors have suggested that a single-factor unitary approach should be adopted at the global level. The sales factor is the popular factor among these authors.[659] To these proponents of an only sales-based formula, they believe this formula is "far less responsive to tax differences across markets, because the customers themselves are far less mobile than are firm assets or employment".[660] While the demand (market) side of the equation contributes significantly to the global profit, it is dependent on the production (supply) of the goods. In addition, in a lot of cases, the assets and labour which produce the goods to be sold are located in African countries, and a sale-only factor will only lead to the continuous exploitation of the resources of these countries, without commensurate return.

While it may appear that developing countries are largely importing countries, the proportion of the sales into these countries is little compared to the volume and value in developed countries.[661] Furthermore, most imports into developing countries are basic commodities, such as food and health care commodities, which form a small portion of global trade.[662] Thus, the apportionment formula must balance the production and consumption measures of economic activity.[663]

---

659 Avi-Yonah, supra note 528 at 497–553; Eichner, supra note 627 at 567–589.
660 Reuven Avi-Yonah & Kimberly Clausing, "Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment" (2007) in Path to Prosperity: Hamilton Project Ideas on Income Security, Education, and Taxes, at 319–344. Washington: Brookings Institution Press, 2008.
661 Montes, supra note 532.
662 Graetz & Doud, supra note 148.
663 Siu, supra note 531.

Therefore, the factors to be chosen and the weight to be attached to those factors, must ensure that taxable profits are taxed where the economic activities occur.[664] They must support the sustainable development of the jurisdictions involved.[665] An -weighted three-factor approach will ensure that countries like Nigeria attain a just allocation of the income, due to it.

I provide a scenario. Suppose Parentco A, resident in Canada, is engaged in the manufacturing of bags and owns 100% of the shares in a Nigerian company, Subco B. Its assets and factories are located in Nigeria. Of its 3,000 global employees, 2,700 of those employees work for the Nigerian subsidiary, Subco B and are resident in Nigeria for tax purpose. Suppose Parentco A has a subsidiary in the Netherlands, Subco C, who is responsible for its marketing, management, financing affairs of the group and owns the rights to both the tangible and intangible assets of the group. Under the current tax system, it is conceivable that most of the total profits will be declared in the Netherlands, even though the income may actually be realised in Nigeria, where the real economic activities occur.

Treating each entity as separate from each other means that every exchange of value has to be priced and the price transferred to an entity. This creates the opportunity to erode tax bases by interposing artificial entities and transactions for the purpose of avoiding tax, while fixing transfer prices that may not be arm's length.

Using the same scenario above and assuming the group made total profit of USD$9,000,000 for the financial year. Applying the unitary approach and the Massachusetts formula gives a different outcome. Splitting the profit into three equal parts- USD$3,000,000 to assets, USD$3,000,000 to labour and USD$3,000,000 to sales. Nigeria, being the location of all the assets (assuming all

[664] Cottani, supra note 527 at 755–760

[665] Robert Bird & Karie Davis-Nozemack, "Tax Avoidance as a Sustainability Problem" (2018) Journal of Business Ethics, Vol 151, No 4, 1009–1025.

assets of the group are in Nigeria) will be allocated the USD$3,000,000 for assets. Given that 90% of the labour of the group is in Nigeria, Nigeria will receive additional taxable profit of USD$2,700,000 (assuming labour is purely on headcount). Without accounting for sales (assuming sales is on the basis of destination and not origin), Nigeria will be allocated a total taxable profit of USD$5,700,000 out of the group's total profit of USD$9,000,000. Recall that under the current system, most of the total profit of USD$9,000,000 could easily have been declared in the Netherlands, if prevailing literature and common knowledge are to be trusted.

The argument here is that Nigeria stands to be in a better position under the unitary approach. While the scenario and the calculations are simplistic, the conclusion agrees with the available literature on unitary approach.[666]

3.4 Tax Sovereignty and Tax Cooperation

As discussed in chapter 1 of the thesis, tax sovereignty represents the power of a state to enact its tax system without interference.[667] The corollary to this is that states, in their exercise of tax sovereignty are eager to tax profits with the minimum connection to their jurisdictions. However, given the potential double taxation of this unhindered exercise by states, countries have agreed to a global standard on income allocation, thereby, giving up some part of their tax sovereignty.[668] Only countries disconnected from the global economy, can claim to still exercise unhindered tax sovereignty. In today's globalized world, it is hard to find countries not affected, directly or indirectly, by the global tax system.

[666] Prem Sikka & Richard Murphy, "Unitary Taxation: Tax Base and the Role of Accounting" (2015) ICTD Working Paper 34, Brighton: International Centre for Tax and Development; Siu, supra note 531.

[667] Geoffrey Brennan & James M. Buchanan, "The Power to Tax: Analytical Foundations of a Fiscal Constitution" (London: Cambridge University Press, 1980) at xiv, 231; see Susan Rose-Ackerman, "A New Political Economy" (1982) Faculty Scholarship Series, 587; Li, supra note 88.

[668] Jack Mintz, "Globalization of the Corporate Income Tax: The Role of Allocation" (1999) FinanzArchiv/Public Finance Analysis, Vol 56, No ¾ at 389–423.

However, given the accepted limitations of the present global tax system, countries are adopting unilateral measures to counter transfer mispricing and protect their income base.[669] While aggressive and unilateral measures are inevitable in these circumstances, they lead to double taxation.[670] The competing interests of states, if not properly managed, could have adverse economic impacts on "warring" countries, and may discourage trade and investment. As such, countries often seek to cooperate on tax matters through tax treaties, trade agreements, and other tax-related arrangements and agreements. This cooperation on tax matters, on a global scale, dates back to the early 20th century, through the work of the League of Nations

Opponents of the unitary approach argue that a shift from the current global tax system to a unitary approach will demand a high level of tax cooperation among countries and a strong political will from leaders. They are convinced that a multilateral agreement cannot be achieved, and unilateral measures will only lead to double taxation. To a large extent, they are right when one considers the erosion of tax sovereignty, and its capture by big MNE in today's globalised world.

However, recent observations from Africa and Europe show that countries are, more than ever before, reclaiming and exercising their tax sovereignty. For instance, some European countries have shown impatience for a global agreement on the taxation of the digital economy.[671] Countries, such as Spain have concluded plans to introduce digital tax, unilaterally,[672] though there are collective efforts both at the European Union and the OECD, to conclude digital tax frameworks. Recent decisions from African countries (Uganda, Tanzania, Malawi) have revealed the attitude of the courts to adopt a purposive approach in the

[669] Cooper et al, supra note 317.
[670] Mintz, supra note 663.
[671] For instance, France's decision to unilaterally introduce digital tax in 2019. See: BBC, "France to Introduce Digital Tax in New Year", online: <https://www.bbc.com/news/business-46591576>
[672] El Pais, "Spanish Finance Ministry to Introduce Digital Tax for Firms like Airbnb and Uber", (2018) online: <https://elpais.com/elpais/2018/10/05/inenglish/1538741424_819871.html>.

interpretation of tax laws and practices.[673] Given that tax is one area of the law where courts follow a literal interpretation rule[674], this move to a purposive interpretation[675] may spell doom for MNEs engaged in tax avoidance practices.

In addition to this, there is no effective global tax framework to prevent countries from reclaiming their tax sovereignty. Notwithstanding the heralded importance of multilateral tax convention and transfer pricing guidelines and rules, they have to be domesticated by countries in their local laws to have any useful effects. As such, compliance with the global tax system remains a unilateral decision of countries. This re-emphasizes the powers of states to exercise their fiscal sovereignty.

It is true that unilateral measures by countries may isolate countries from the global community, however, the danger of this is overstated. Recent study by World Bank staff shows that tax treaties do not necessarily increase foreign direct investment and their relevance is overstated.[676] Previous studies have revealed that tax consideration does not rank top in the factors investors consider before investing in a country.[677] Even so, African countries are blessed with unique natural resources, assets which are not easily found elsewhere and movable to other countries.

---

673 Eastern Produce (2018). The State v the Commissioner General Malawi Revenue Authority, ex parte Eastern Produce Malawi Ltd. [2018] MWHC 800, online: <https://malawilii.org/mw/judgment/high-court-general-division/2018/800>.
674 According to the letter of the law.
675 According to the spirit of the law.
676 Mary Hallward-Driemeier, "Do Bilateral Investment Treaties Attract Foreign Direct Investment? Only a Bit…and They Could Bite" (2003) Policy Research Working Paper 3121, Development Research Group: The World Bank; Laura Gomez-Mera, et al, "New Voices in Investment: A Survey of investors from Emerging Countries" (2015) World Bank Study: World Bank Group; World Bank Group, "Global Investment Competitiveness Report 2017/2018" (2017) World Bank Publication: Washington DC. The Report claims that political stability, security and regulatory environment are leading factors driving decisions to invest in developing countries.
677 OECD (2015), "Options for Low Income Countries' Effective and Efficient Use of Tax incentives for Investment: A Report to the G-20 Development Working Group by the IMF, OECD, UN and World Bank" (2015) OECD Publishing, Paris, online: <https://www.oecd.org/tax/options-for-low-income-countries-effective-and-efficient-use-of-tax-incentives-for-investment.pdf>.

Thus, while not understating the importance of tax cooperation, Nigeria can lead the rest of Africa by advancing a move away from the OECD's separate entity accounting and arm's length approach to income allocation and adopt the unitary approach. The dangers of such unilateral measures may not outweigh the potential benefits of increased revenue and reduction of illicit financial flows out of the country.

4 Support for the Unitary Approach

4.1 The EU's Common Consolidated Corporate Tax Base

Support for the adoption of the unitary approach comes from the proposed EU's CCCTB. The EU's CCCTB is a response to the conclusion that "the current rules for corporate taxation no longer fit the modern context".[678] The view in the EU is that there exists a conflict, where corporate income tax still occurs at the national level, while the economic environment of taxpayers has become more globalized, mobile and digital.[679] Where national tax laws are drafted without considering the cross-border dimension of business activities, conflicts are likely to arise between differing national tax laws, leading to the risks of double taxation and double non-taxation.[680]

The differing national tax laws aids aggressive tax planning[681] by taxpayers who are able to easily shift profits to favourable tax jurisdictions.[682] This affects the effective functioning of the internal market.[683] Addressing this unilaterally (protecting the tax base, countering profit shifting and achieving the effective

---

678 Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final), online: <https://ec.europa.eu/taxation_customs/sites/taxation/files/com_2016_683_en.pdf>.

679 Ibid at 5.

680 Ibid.

681 The European Commission defines "aggressive tax planning" as consisting of taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability. See, Commission Recommendation of 6th December 2 012 on aggressive tax planning, C(2012)8806 final.

682 Morgan, supra note 570 at 463–481.

683 EU CCCTB, supra, note 579.

functioning of the internal market) has proven difficult for member states. In light of this, the EU's CCCTB is being proposed to member states of the European Union as a collective effort to ensure income is attributed where the economic activities occur value is created.[684] This, it is believed, will promote sustainable growth and investment within a fair and better integrated market.[685] Thus, the EU CCCTB has two main functions: an anti-tax avoidance function; and a facilitator of cross-border trade and investment in the internal market.[686] These functions present valuable lessons for the AfCFTA.

Furthermore, the EU CCCTB proposes mandatory compliance for parent companies established under the laws of a Member State, including the permanent establishments of the parent companies in other Member States.[687] Compliance with the proposed CCCTB is mandatory for companies with a total consolidated group revenue of more than 750 million euros during the financial year preceding the relevant financial year.[688] For companies below the monetary threshold, compliance with the EU CCCTB is optional though encouraged.[689] The proposed CCCTB extends to a company established under the laws of a non-Member State where the company has permanent establishments situated in one or more Member States and meets the monetary threshold.[690] This covers companies not headquartered in the EU but have significant economic presence in the EU to be caught by the CCCTB proposal.

To sum up, under the proposed EU CCCTB, a consolidated group consists of a resident taxpayer with all its subsidiaries resident in a Member State for tax

---

684 The BEPS Monitoring Group, "Comments on the European Commission's Proposals for a CCTB and for a CCCTB" (May 2017), Publication of The BEPS Monitoring Group, online: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4dcc60e2e72299b765c2b/1525996746863/ccctb-2017-final.pdf>.
685 Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) (SWD (2016) 341 Final) (SWD (2016) 342 Final), at 2.
686 Ibid.
687 EU CCCTB, supra note 578, at 17.
688 Ibid. There are suggestions to reduce this threshold to 40 million Euros or completely remove the requirement for a monetary threshold, making it compulsory for all eligible taxpayers.
689 EU CCCTB, supra note 578 at 13.
690EU CCCTB, supra note 578 at 18.

purposes and their permanent establishments situated in a Member State; all permanent establishments of the parent company situated in a Member State; all permanent establishments situated in a Member State belonging to subsidiaries of the parent company, resident in a third country for tax purposes; and Member State subsidiaries and permanent establishments of a non-taxpayer resident in a third country for tax purposes.[691]

The proposed CCCTB by the European Union adopts a three-factor formula[692] for apportioning cross-border income within the EU.[693] These factors are assets, labour and sales. The factors are weighted equally.[694] The EU believes these factors reflect a balanced approach to distributing taxable profits amongst eligible Member States and ensure that profits are taxed where they are actually earned.[695] The labour factor will be divided into payroll and the number of employees (weighted equally) to account for the levels of wages across the EU and ensure a fair distribution.[696] Assets will consist of only fixed tangible assets.[697] Intangibles and financial assets are excluded from the formula due to their mobile nature and vulnerability to manipulation. Sales is based on destination.[698]

This multilateral approach harmonizes the corporate tax base for member states and provides a common apportionment formula for the allocation of cross-border income within the EU. The proposed EU CCCTB has valuable lessons for the African continent as it seeks to adopt a single market. It is recommended that discussion on the tax implications of the AfCFTA should be part of the larger trade discussions, in line with the events in the EU.

---

691 EU CCCTB, supra note 578.
692 There are suggestions to add a fourth factor- "use of data" in the formula. See the European Parliament position on the CCCTB proposal, available online: <http://www.europarl.europa.eu/RegData/etudes/ATAG/2018/614731/EPRS_ATA(2018)614731_EN.pdf>.
693 EU CCCTB, supra note 578 at 14.
694 Ibid.
695 Ibid.
696 EU CCCTB, supra note 578 at 15.
697 Ibid.
698 EU CCCTB, supra note 578 at 14.

4.2. Theoretical Soundness of the Unitary Approach

Another support for the shift to the unitary approach comes from its theoretical soundness. Here, I shall discuss two theories, which support the adoption of the unitary approach by Nigeria and under the AfCFTA framework.

4.2.1. Theory of FDI and MNE

Tax systems represent multi-disciplinary disciplines, incorporating the legal, political, socio, and economic aspects of a state. In the earlier theories of taxation-economic allegiance, power to tax, and exchange theory, I considered the influences of legal, political and social studies on the international tax law system. However, the field of economics has always influenced tax systems of states. It has been argued that the current international tax system may have been influenced by economic principles and theories of the organizational structure of firms. Tavares posits that "legal scholars in the field of international tax often resort to "firm theory" to critically address policy considerations concerning the international allocation of taxing rights…"[699] The theory of the firm is relevant to this discussion to the extent that it attempts to explain the influences on the League of Nations in arriving at the current system of international tax system. However, I shall rely on the theory of FDI[700] and MNE[701] to advocate a shift from the existing system of international tax to the unitary approach.

Ronald Coase, in a 1937 article, "The Nature of the Firm" justified the growth of the firm structure on the reduction of transactional cost, such as cost of gathering

[699] Romero Tavares, "Multinational Firm Theory and International Tax Law: Seeking Coherence" (2016) World Tax Journal, Vol 8, No 2.
[700] Dunning and Rugman define FDI as "primarily about the transfer of nonfinancial and ownership- specific intangible assets by the MNE, which needs to appropriate and control the rate of use of its internalized advantage(s)". see: John Dunning and Alan Rugman, "The Influence of Hymer's Dissertation on the Theory of Foreign Direct Investment" (1985) The American Economic Review, Vol 75, No 2.
[701] Rugman defines the MNE as "a firm engaged in international production and distribution, in at least one foreign nation." See: Alan Rugman, "Internalization is Still a General Theory of Foreign Direct Investment" (1985) Weltwirtschaftliches Archiv, Bd 121, H 3 at 570–575

information on the price and quality of the product or the trustworthiness of the supplier or the legal costs of stipulating contracts.[702] Tavares states in his paper, that Coase's firm theory is commonly used to debate the international allocation of the right to tax residual income from synergistic multinational firms and to address the subject of transfer pricing. According to Tavares, "The functionally separate legal entity approach (FSLE), which is instrumental to the arm's length principle (ALP), embedded in article 9 of the OECD and UN Models, is heavily influenced by, or perhaps derived from, views of the firm in which ownership and property rights, as well as contractual law, are primarily value drivers (supported by the vast literature developed primarily in the 1980s, particularly on asset specificity)."[703] Tavares opines that critics of the inherent flaws of the ALP often use the same transactional cost theory of the firm to defend the unitary taxation of multinational firms and the abandonment of the ALP in favour of global formulary apportionment (GFA), or an equivalent formulary application of the profit split methods. In his paper, he advocates the adoption of the unitary taxation of MNEs and the use of ALP in apportioning income, based on the theory of the firm.

The limitations of Coase's theory of the firm (transactional cost theory) reflect in Tavares's conclusion and election of the ALP approach to income allocation, though he advocates the unitary treatment of MNEs. Coase's theory of the firm depicts the nature of international trade, which existed in the 1920s and 1930s when the current system of international taxation was established- an era of trade dominated by portfolio investment- mere movement of capital- and export of raw materials. Firms in this era were established to essentially reduce cost of export of raw materials and ensure the security of portfolio investments. Ownership of assets and organizational control were not at the heart of the firm structure in Coase's theory. Stephen Hymer's theory of FDI and MNE provides a refreshing

[702] Grazia Letto-Gillies, "Transnational Corporations and the Globalization Process" (2002) in "Transnational Corporations. Fragmentation amidst Integration" London: Routledge.
[703] Tavares, supra note 694.

perspective on the nature of MNEs and the choice of FDI, as against portfolio investment. I examine Hymer's theory of FDI and MNE next.

Hymer's contributions to the appreciation of MNEs and FDI can be divided into two eras[704]- his Capitalist leanings and his Marxist leanings.[705] Notwithstanding his later conversion to Marxist views, his works on MNE and FDI are relevant in both capitalist and Marxist societies. Unlike Coase who based his theory of why firms went abroad on transactional costs, Hymer extended the reason to structural market imperfections.[706] Hymer believed that the MNE was a creature of market imperfections and had the ability to use its international operations to separate markets and remove competition or exploit an advantage.[707]

In his doctoral dissertation written in 1960[708] but later published in 1976, posthumously, Stephen Hymer developed the theory of the transnational corporation (TNC[709]) and its defining activity- foreign direct investment (FDI).[710] In Hymer's FDI, capital movements merged with international operations of firms

---

[704] Peter Buckley, on his part, suggests three phases of Hymer's work: first phase being his PhD thesis; the second phase is his neoclassical phase and the third phase is his radical phase. See: Peter Buckley, "Stephen Hymer: Three Phases, one approach?" (2006) International Business Review, Vol 15, 140; See: Grazia Letto-Gillies, "Hymer, the Nation-State and the Determinants of MNCs' Activities" (2002) Contribution to Political Economy, Vol 21, No 1 at 43−54.

[705] Robert Cohen, "The Multinational Corporation: a radical approach- papers by Stephen Herbert Hymer" (1980) Cambridge University Press; Stephen Hymer, "The Internationalization of Capital" (1972) Journal of Economic Issues, Vol 6, No 1 at 91−111.

[706] Some scholars (Dunning and Rugman) have accused Hymer of not recognizing the Coasian transactional cost theory of MNE, and that Hymer failed to distinguish between the Bain-type structural market imperfections and transaction cost market imperfections. However, Horaguchi and Toyne have argued that Hymer incorporated a Coasian theory of firms and markets in his theory as early as 1968 and that the genesis of transactions as applied to the MNE could be traced to Hymer. Though in a 2008 paper, John Dunning would come to agree that Hymer had considered the Coasian transactional cost theory in his analysis. See: Haruo Horaguchi & Brian Toyne, "Setting the Record Straight: Stephen Hymer, "Internalization Theory and Transactions Cost Economics" (1990) Journal of International Business Studies, Vol 21, No 3 at 487—494. John Dunning and Christos Pitelis, "Stephen Hymer's Contribution to International Business Scholarship: An Assessment and Extension" (2008) Journal of International Business Studies, Vol 39, No 1 at 167−176.

[707] Dunning, supra note 695.

[708] Hymer, supra note 575.

[709] TNCs and MNEs are used interchangeably in this section of the chapter to represent institutions with transnational business activities.

[710] Grazia Letto-Gillies, "The Theory of the Transnational Corporation at 50+" (2014) Economic Thought, Vol 3, No 2.

to gain and keep control of production. This, he distinguished from portfolio investments, which focus on differences in interest rates or profit differentials, for decision-making.[711] He identified the major determinants of FDI to be the removal of competition and the advantages firm possessed in particular activities.[712] Letto-Gilles summarizes Hymer's work as a variety of theories dealing with different aspects of the TNC, focused on issues such as: why firms become transnational; to the modalities of their activities; to FDI as their main activity;[713] to why some countries become host or home (or both) for TNCs and FDI.[714]

Hymer held the view that multinational firms were better institutions than international markets for stimulating business, transmitting information and fixing prices. He saw MNEs as having three related sides: international capital movements; international capitalist production; and international government.[715] These related sides are expanded below.

First, Hymer saw international capital movements as the direct investment of corporations in their overseas branches and subsidiaries.[716] MNEs[717] are distinct from other firms because of their direct production and direct business activities

[711] Dunning, supra note 695.
[712]In the paper, "The Internalization of Capital", Hymer gave three motives for expansion of American MNEs: (1) rapid growth in the markets for goods in which they specialized; (2) cheaper labour (productivity divided by wage) which made it profitable to produce abroad; and (3) faster growth of foreign competitors than themselves who were gaining an increased share of the world market. See: Hymer, supra note 700 at 91−111.
[713] Dunning and Rugman argue that prior to Hymer, there was no separate theory of FDI, nor the question of "why is there FDI?"; there was no focused attention on the study of the MNE. They state that Hymer's great insight was in focusing attention upon the MNE as the institution for international production, rather than international exchange. See: Dunning, supra note 695.
[714] Other scholars considered the "why, where and when" firms become transnational and go abroad. John Dunning developed the "eclectic framework" where he established that firms become transnational because of the advantage of ownership, location and internalization (Dunning's OLI advantages).
[715] Hymer, supra note 700 at 91−111.
[716] Ibid at 91−111.
[717] Letto-Gilles argues that the growth of TNCs may be attributed to the following: (a) the developments in transportation and in the communications technologies and costs; (b) the organizational innovation within large companies and institutions; (c) the favorable political environment after the Second World War; (d) the liberalization and privatization programmes of many developed and developing countries in the last 30 years. In addition, the rise and influence of supranational bodies such as the WTO, IMF, World Bank, with far-reaching policies, has led to the growth of TNCs.

abroad. To achieve direct production and direct business activities, Hymer identified key attributes that must be present- ownership of assets, central control[718], and internalization.[719] These attributes ensure that MNEs acquire long-term strategic and management control of the entities, while at the same time determining the use or non-use of the assets of the MNE. Thus, integral to the MNE structure is the need for control. Control of the entities in the MNE becomes the reason firms engage in foreign direct investment.[720]. Grazia Letto-Gillies argues that for operations abroad to be seen as part and parcel of a company's operations and for the company to be seen as an MNE the same company must be able to exercise control over its foreign assets and businesses.[721] To Hymer, control of foreign subsidiaries was desired in order to remove competition between that foreign enterprise and enterprises in other countries and or to appropriate fully the returns on certain skills and abilities.[722] This "control" is the basis upon which I argue that treating subsidiaries of an MNE as separate entities reflects the failure of law to actively capture economic developments.

Internalization of its market is another relevant factor in the election of the MNE structure and engagement in FDI. Hymer, in his dissertation, argued that the distinctive elements of the MNE is its control of the value-added activities of its subsidiaries.[723] Dunning and Rugman state that "the great advantage of being an MNE is the ability to use internal markets across nations. The MNE can use

[718] Control may arise from the ownership of assets, which may be direct ownership or indirect ownership of the assets; or mere managerial control. Thus, there is a link between ownership of assets and control and could be used interchangeably in certain instances. Control provides one of the means the unitary taxation of MNEs could be manipulated to erode bases or shift profit to low or no tax havens, and as such, must be uniquely considered.

[719] Buckley and Casson expanding the internalization theory in 1976 wrote that: "There is a special reason for believing that internalization of the knowledge market will generate a high degree of multinationality among firms. Because knowledge is a public good which is easily transmitted across national boundaries, its exploitation is logically an international operation." See: Peter Buckley and Mark Casson, "The Future of the Multinational Enterprise" (1976) London: MacMillan.

[720] Letto-Gilles opined that Hymer's demarcation criterion between foreign direct investment and portfolio investment is control and that by directly investing abroad, firms gained control over the business abroad, removing conflicts with local competitors, thereby, gaining market power.

[721] Grazia Letto-Gillies, "The Integration and Fragmentation Role of Transnational Companies" (2002) London: Routledge.

[722] Hymer, supra note 575.

[723] Dunning & Pitelis, supra note 701 at 167–176.

transfer prices, maneuver liquid assets, move around production facilities, and so on".[724] Internalization of market grants greater flexibility and autonomy to the MNE than it does firms confined to a country. It reduces production and transaction costs for the MNE by exterminating knowledge-acquisition costs and other external costs. Rugman, on his part, highlights vertical integration, transfer pricing and quality control as examples of market imperfections which lead to internalization of the market by MNEs.[725] Thus, alongside control of the subsidiaries in the MNE structure, internalization of the operations and management of the firm market are gains of the MNE structure and why firms directly invest abroad.

Third, Hymer's international capitalist production refers to the incorporation of labour from many countries into an integrated worldwide corporate productive structure.[726] An effect of the MNE structure is the intra-firm trade that occurs among its subsidiaries and branches. Intra-firm trade necessitates the setting up of vertically-integrated production and sale system within the MNE for the transfer of good and services to different countries across the globe. This internalization of trade takes advantage of different skills availability, labour costs, central management and economies of scale, to bring down transaction costs and eliminate competition. An integrated management or organizational structure is desirable for optimum maximization of the resources and opportunities at the disposal of the MNE. This ensures that the MNE is equipped to distribute and re-allocate wealth to places where it is likely to have the maximum returns.[727] This desire to maximize returns means that as part of the

[724] Dunning, supra note 695.
[725] Rugman, supra note 696 at 570−575.
[726] Hymer, supra note 605 at 91−111.
[727] Kant argues that one of the truly distinguishing characteristics of multinational firms is the intra-firm transactions among units in different countries and the absence of constraint by marketing forces in setting the terms, in particular, the transfer price, at which such transactions take place. See: Chander Kant, "Foreign subsidiary, Transfer Pricing and Tariffs" (1988) Southern Economic Journal, Vol 55, No 1 at 162−170.

intra-firm trade, the MNE can fix prices for the goods and services transferred among its subsidiaries in a profit-maximization driven manner.[728]

The transfer pricing of goods among related entities is not bad. What is bad, however, with far-reaching economic implications for all countries is the manipulation of the transfer price[729], to shift profit to low or no tax jurisdictions or erode the base in high-tax jurisdictions.[730] This effectively minimizes the tax liabilities of the MNE as a whole,[731] lending credence to the claim that, maximizing its global profits[732] is at the heart of the operations of the MNE.[733] Given that the ultimate goal of an MNE is to maximize its global profit and the activities of its entities are contributory to that global profit, justifying the need for control and internalization of the activities of the entities under the MNE, the tax law treatment of entities under the MNE as separate entities flies in the face of reason.

---

[728] Eden defines transfer pricing as "the prices set by a multinational enterprise for the sale of goods and services between two entities controlled by the multinational" and attributes its increased attention over the past quarter century to the increase in the volume of intra-firm trade. See: Barbara Rollinson, "Reviewed Work(s): Taxing Multinationals: Transfer Pricing and Corporate Income Taxation in North America by Lorraine Eden" (2001) Journal of Economic Literature, Vol 39, No 1 at 150−151: Jacob, supra note 243. In his article, Jacob argues that firms with substantial international intrafirm sales pay lower global taxes than otherwise similar firms, consistent with the global tax minimization through transfer prices objective of multinational enterprises.

[729] Roger Wesley defines transfer mispricing as "the method of price manipulation between the MNE and its affiliates (referred to as intracompany pricing to achieve tax or other fiscal advantages) as well as with other suppliers or customers. See: Roger, supra note 1, at 613−622

[730] Mansori and Weichenrieder argue that, a large share of international trade occurs within multinationals, and manipulation of the transfer prices that they use for such internal transactions can shift a huge amount of taxable profits between countries. See: Kashif Mansori & Alfons Weichenrieder, "Tax Competition and Transfer Pricing Disputes" (2001) Public Finance Analysis, Vol 58, No 1 at 1−11.

[731] William Petty II & Ernest Walker reiterate this point by arguing in their paper, that the earnings of a multinational concern can be altered to varying degrees by its internal pricing policies. See: William Petty II & Ernest Walker, "Optimal Transfer Pricing for the Multinational Firm" (1972) Financial Management, Vol. 1, No 3 at 4−87.

[732] Petty II and Walker argue that the demands made on a company's transfer pricing network generally relate to improving the after-tax profitability of the worldwide organization and the effective movement of funds among sub-entities, accompanied by recognition of earnings in the most favorable tax jurisdiction; Ibid at 74−87.

[733] Other reasons for the manipulation of transfer prices to include: circumventing restrictions to the transfer of profits from those host country(ies) which pose strict ceilings and constraints to such transfers; allocating markets of affiliates subject to high government royalty requirements and such external factors as varying rates of tax assessment among countries; taking advantage of expected appreciation or depreciation of currencies; recording low costs of components in a country/market that the company wants to penetrate through low prices; and recording relatively low profits in countries where it is feared labour and its trade unions might demand wage increases if high profits were discussed. See: Roger, supra note 2 at 613-622. Ibid at 74−87.

In addition, Hymer deemed international government as the erosion of the traditional powers of nation-states and the emergence of internal economic policy instruments in line with the tendency of the multinational corporation to internationalize capital and labour.[734] The cross-border activities of the MNE cause direct and indirect effects on the economies of countries involved in the value chain and the countries affected by the activities and decisions of the MNE. These effects could be at the macro-economic level, such as trade and balance of payments, innovation and capacity creation, or could be at the micro level, such as effects on labour and employment in general[735]

Discussing the inequality orchestrated by the activities of the MNEs, especially in developing countries, Hymer saw a conflict between the MNE and the state, and criticized "the bourgeois belief that capitalism and the 'free market' are the direct forces in the development of the human species."[736] Hymer held the view that MNEs created hierarchy rather than equality and spread the benefits unequally.[737] The dominance of MNEs in world trade, aided by the absence of learning by nation-states in developing countries meant that developing countries become rental states for MNEs.[738] He saw international trade as a division between superior and subordinate states rather than a division between equals. This, he argued, reduces the independence of nation-states and requires the

---

[734] Hymer, supra note 700 at 91−111; Letto-Gillies, supra note 716.

[735] Ibid.

[736] Cohen, supra note 700. Dunning and Christos in their paper, "The Political Economy of Globalization (Revisiting Stephen Hymer 50 years on) reported Hymer as holding the view that the need of MNEs both to access new markets and natural resources products would lead them to consider investing in less developed countries (LDCs). Acknowledging the benefit to the recipient economies, Hymer argued more that such internalization of capital would lead to dependant and uneven development and the erosion of the power of the host countries.

[737] In Hymer's words, "…markets come out of the barrel of a gun, and to establish an integrated world economy on capitalist lines requires the international mobilization of political power." Hymer, supra note 700 at 91−111.

[738] Hymer described it thus: "The government may have apparent political sovereignty, but it too has limited real power and is forever looking to international corporations for technology and capital."; Hymer, supra note 700 at 91−111; Letto-Gillies, supra note 699. Letto-Gillies summarises the issues as the gradual loss of sovereignty and the loss of effectiveness of traditional policy instruments.

formation of supranational institutions to handle the increased interdependence.[739]

Addressing the question of income distribution, Hymer held the opinion that the institutional structure through which MNEs were conducted and governed led to unequal share of the benefits being realized by high-income countries and disproportionate share of the costs being realized by low-income ones.[740] This, MNEs achieve by the use of transfer mispricing on the transfers of goods, services, capital and technology in intrafirm transactions thereby, reducing the profit that accrues to the host countries.[741] Hymer called for a world system in which the separate interests, laws, governments, and systems of taxation and regulation are lumped together into a unified code of laws on the rights and limits of international private property. He feared a world economy in which the leading sectors are dominated by a few, giant world corporations, competing through advertising and innovation.

While the world has seen the rise and increase of supranational institutions regulating trade and taxation, the system of taxation has not changed since its establishment, prior to Hymer's theory of FDI and MNE. Thus, Hymer's plea has gone unattended to and the world is still governed by a tax system unfit for the economies of today, thereby perpetrating and perpetuating uneven development of smaller countries. Hymer's works are relevant in this thesis. One, it helps us understand the nature, purpose and attributes of MNEs and the drive for direct investment by MNEs. Second, it helps us appreciate the consequences, especially for African countries, of non-regulation of MNEs and treatment of MNEs, devoid of their unique attributes. Third, it affirms the argument for a revisit to the international tax system and a shift to the unitary approach.

---

[739] Hymer, supra note 700 at 91–111.
[740] Donald Lecraw, "Hymer and Public Policy in LDCs" (1985) The American Economic Review, Vol 75, No 2, Papers and Proceedings of the Ninety-seventh Annual Meeting of the American Economic Association at 239–244.
[741] Ibid.

4.2.2. The Global Economy perspective[742]

In the 1920s, when the current international tax system was formulated, productions were local and value contributions were limited to single territories. What this means is that the allocating system was essentially meant to capture sales of goods by an MNE to its distributing entities, and the prices attributed to the transfer of the goods. However, with the advent of global production networks (GPN) and global value chains (GVCs), attributable to the rise and activities of MNEs, a finished product, represents inputs from multiple jurisdictions. There is increased reliance on inputs from other countries and MNEs today are structured to actively capture such inputs. Djelic and Sahlin-Anderson, in their paper, hold that, "transnational pressures- the multiplication of multinational companies, the progress of Europeanization, the intensification of transnational competition, the increasing number of international organizations and institutions, and the explosion of transnational regulation- challenge national business systems and their systemic complementarities.[743] Thus, the current international system that treats actions of MNEs as expressions of national interests becomes too restrictive and unfit for the new world order.

Levitt-Polanyi articulates the failure of the present system, claiming that "the modern transactional enterprise is a much more powerful and sophisticated

[742] Some scholars argue against the use of "globalization" to describe the new world order, and prefer the use of the term, "transnational". Djelic and Sahlin-Anderson quote Hanners (1996) as saying, "I am also somewhat uncomfortable with the rather prodigious use of the term globalization to describe just about any process or relationship that somehow crosses state boundaries. In themselves, many such processes and relationships obviously do not at all extend across the world. The term "transnational" is in a way humbler and offers a more adequate label for phenomena which can be quite variable scale and distribution, even when they do share the characteristic of not being contained within the state." See: Marie-Laure Djelic and Kerstin Sahlin-Anderson, "Introduction: A World of Governance: The Rise of Transnational Regulation" (2006), in Transnational Governance: Institutional Dynamics of Regulation, (New York: Cambridge University Press, 2006) at 1−28. Gereffi, on his part, distinguishes between internationalization- the mere extension or geographic spread of economic activities across national boundaries- and globalization- the functional integration of internationally dispersed activities. See: Gary Gereffi, "The Global Economy: Organization, Governance, and Development" in Neil J. Smelser & Richard Swedberg, eds., The Handbook of Economic Sociology, at 160−182, 2nd ed. (Princeton, NJ: Princeton University Press and Russell Sage Foundation). I have elected to stick with the term, "global" and its many derivatives to keep faith with the majority of audience and to distinguish economic integration from the rise and influence of transnational companies.

[743] Djelic & Sahlin-Anderson, supra note 737 at 1−28.

business organization than the national corporation. It appears to be capable of integrating world production and exchange to an ever-greater extent. Commodity trade and portfolio capital movements of the nineteenth century are being displaced by the international transfer of organizational capacity (foreign direct investment) which integrates world production within the private horizons of global corporate entities."[744] She goes ahead to argue that "the traditional policy instruments- fiscal, monetary, anti-trust, wage and income policies- are eroded when the commanding heights of the economic and financial system are controlled by very large and multinational corporations."[745] The rise of the MNE has meant the diminution of the powers of state, especially those of developing countries.[746] The economies of many developing countries are now controlled by MNEs, who go beyond economic interests to affect the political, social and cultural values of the states.

This new global economy supports the argument for the unitary taxation of MNEs. Today's world is one characterized by deep integration, with MNEs at the centre of it, who engage in production of goods and services in cross-border value-adding activities that redefine the kind of production processes contained within national boundaries. Gereffi distinguishes the global economy from its predecessors[747] by the way MNEs are able to link the production of goods and services in cross-border value-adding networks.[748]

In Gereffi's global economy, MNEs have become the primary movers and shakers of the global economy because they have the power to coordinate and control

[744] Kari Levitt-Polanyi, "A Memoir: Stephen Hymer on the Multinational Corporation" (1982) Review (Fernand Braudel Center) Vol 6, No 2 at 253–279.
[745] Ibid at 253–279.
[746] Erika Siu et al., argue that to reap the benefits of economic integration, tax sovereignty of states needs to be coordinated. The converse would be a race to the bottom from market competition and the desire to safeguard revenue. They conclude by stating that to balance national/state sovereignty with market integration, unitary taxation offers a middle ground solution. See: Siu, supra note 531.; Tracy Kaye and Michael Mahoney, "Various Approaches to Sourcing Multijurisdictional Values: Sourcing Options Available to Tax Policy Makers" (2009) St. & Loc. Tax Law Symp. ed., 2013.
[747] Characterized by the search for raw materials, new markets and relatively low-cost of labour.
[748] Gereffi, supra note 737.

supply chain operations in more than one country, even if they do not own them. Gereffi's works in analyzing the growth of global value chains and the shift to a global economy, put the MNE at the centre of it. He attributes the emergence of the MNE in shaping the new global economic system to the period after World War II, in consonance with Hymer's development of the theory of FDI and MNE. He narrows the centrality of MNEs in the global economy discourse as: the rise of intra-industry and intra-product trade in intermediate inputs; the ability of producers to "slice up the value chain" by breaking a production process into many geographically separated steps;[749] and the emergence of a global production networks framework that highlights how these shifts have altered governance structures and the distribution of gains in the global economy. [750] Therefore, one cannot exclude discussion of the relevance and nature of the MNE from the discussion of the global economy. Their activities have wide-ranging implications and as such a globally-uniform approach is needed in addressing the tax law treatment of MNEs.

To sum it up. Today's global economy, characterized by economic integration and vertical integration of entities under the MNE defeat the treatment of companies, as separate entities, given that for MNEs to optimally function, integration of entities, management and activities, is a key factor. The continuous tax law treatment of entities under an MNE as separate entities in a global economy, is to facilitate global GWCs. As stated in chapter 1 of the thesis, global wealth chains hide, obscure and relocate wealth to the extent that they break loose from the location of value creation and heighten inequality.[751] The OECD's BEPS Project is essentially geared towards addressing global wealth chains, within the existing system which created it. However, the BEPS Project is a sentimental approach to addressing an issue, which demands a complete overhaul. In the words of Lindsay Celestin "…the perennial questions of international taxation can no longer be addressed within the constraints of the separate entity theory and a narrow

[749] Ibid.
[750] Ibid.
[751] Leonard Seabrooke & Duncan Wigan, "Global Wealth Chains in the International Political Economy" (2014) Review of the International Political Economy, Vol 12, No 1 at 257–263.

definition of national sovereignty."[752] In the absence of a globally-uniform approach to the taxation of MNEs, tax competition among countries will remain rife, and MNEs will continue to shift profit to low or no tax jurisdictions and erode the tax bases of countries, with developing countries getting the hardest hit. A new approach is urgently needed, and unitary approach is a viable alternative.

Conclusion

I have set out in this chapter to argue for a shift from the current global tax system, premised on the separate entity treatment of MNEs and the arm's length standard of income allocation, to a system which ensures that profits are taxed where the economic activities occur. This system is the unitary approach. To effectively capture today's world economy and the reality of businesses, a paradigm shift from a national claim to taxation to an international outlook must be adopted. A large percentage of world trade occurs through MNEs who are structured to take advantage of the economies of scale from integration, and as such taxation of companies must reflect an understanding of this form of trade, a necessary departure from the old order. As argued in the chapter, relying on Hymer's theory of MNE and FDI and Gereffi's global economy perspectives, the unitary approach is theoretically sound and reconciles tax law and practice with economic realities.

In the next chapter, I shall discuss the practical steps towards achieving this by Nigeria and within the AfCFTA framework.

[752] Celestin, supra note 67.

Chapter 5: Reforming the Tax Law Treatment of Multinational Enterprises in Nigeria

Table of Content

1. Introduction

1.1 Executive Summary of the Chapter

The discussion here reviews the constitutional and legal provisions on taxation of persons, their relationship with the current tax system and the entrenchment of the arm's length principle in the domestic laws. The chapter analyses the textual wording of the unitary approach. I propose the exclusion of the phrase, "value creation"' from the wording of the unitary approach in the domestic laws of Nigeria and international treaties entered into by Nigeria. This is to avoid the controversies around the statement "aligning the taxation of profit with where value is created".

Beyond the legal steps required to achieve a shift to the unitary approach, I discuss the political support needed to achieve a global effort. This, I approach, by recommending an expansive definition of IFFs to include tax avoidance. The reason for this is to benefit from ongoing global efforts to curb IFFs, especially in African countries. A global consensus adopting tax avoidance as one of the ways IFFs are perpetrated will accelerate global and national efforts at arresting the erosion of tax bases and shifting of taxable profits by multinational entities. These global efforts led by the UN, the African Union and individual countries, are important in the fight against IFFs.

Finally, I discuss the challenges of adopting the unitary approach within trading blocs, such as the Economic Community of West African States (ECOWAS) and the recently signed African Continental Free Trade Agreement (AfCFTA).

1.2 Objectives of the Chapter

One criticism of the unitary approach is that it will be difficult to gather the political will needed to effect legal changes in the tax law treatment of MNEs. In this chapter, I discuss both the legal changes needed for a shift to the unitary approach and steps to gather the political will. My argument here is that these challenges are surmountable in the present circumstances. Nigeria is committed to curtailing IFFs in the country. This is true for other African countries, and the world at large. This commitment to curtail IFFs can be utilized to achieve a change.

1.3 Outline of the Chapter

The rest of the chapter proceeds as follows. In section 2, I discuss the existing legal instruments for the taxation of MNEs in Nigeria. I discuss ongoing reforms of the FIRS to optimize tax collection. In section 3, I discuss the legal changes that have to be effected by Nigeria where it seeks to adopt the unitary approach. In section 4, I discuss how the relevant political will to influence a change from the current global tax system to the unitary approach can be gathered both at the national level and at the global level.

2 Tax Law Treatment of Multinational Entities in Nigeria

2.1 The Constitutional Framework for Tax in Nigeria

Nigeria operates a constitutional democracy. This implies that the system of government is one representative of the wishes of majority of the people. It means that the people are guided by a constitution, which is supreme and has binding force. This last claim is contained in the first section of the 1999 Constitution of the Federal Republic of Nigeria (as amended) (hereinafter described as, the Nigerian Constitution). Section 1 of that constitution prescribes expressly that, "this Constitution is supreme, and its provisions shall have binding force on the authorities and persons throughout the Federal Republic of Nigeria.[753] Subsection 3 of section 1 of the Nigerian constitution provides that any other law inconsistent

[753] The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 1(1).

with the provisions of the constitution, shall to the extent of the inconsistency, be void.

On the political structure of the country, Nigeria is a federal state. This is as prescribed by section 2, subsection 2 of the Nigerian Constitution, to wit: "Nigeria shall be a Federation consisting of States and a Federal Capital Territory." As at 2019, the Federation consists of 36 states and the Federal Capital Territory, Abuja.

The legislative powers of Nigeria are vested in the National Assembly of Nigeria, which consists of the Senate and the House of Representatives.[754] The National Assembly has powers to make laws for the peace, order and good government of Nigeria, with respect to any matter included in the Exclusive Legislative List as set out in Part I of the Second Schedule to the Constitution.[755] In addition to its exclusive powers to make laws with respect to any matters included in the Exclusive Legislative List, the National Assembly has powers to make laws with respect to any matter in the Concurrent Legislative List as set out in Part II of the Second Schedule to the Nigerian Constitution and to the extent prescribed therein.[756]

Legislative matters in Nigeria are divided into Exclusive Legislative List, Concurrent Legislative List and the Residual Legislative List. The Exclusive Legislative List contains matters exclusively reserved to the National assembly. The Concurrent Legislative List contains matters both the National Assembly and the State House of Assembly can legislate upon. As prescribed in the Exclusive Legislative List, the National Assembly has exclusive powers to make laws on the taxation of incomes, profits and capital gains.[757] This constitutional provision grants the power to make laws for the taxation of companies exclusively to the National Assembly.

[754] The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 4(1).
[755] The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 4(2).
[756] The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 4(4).
[757] Item 59 of Part I of the Second Schedule to the Constitution.

Nigeria is signatory to double taxation agreements (DTAs) with other countries, especially its trading partners. DTAs are bilateral tax treaties, which aim at preventing double taxation and fiscal evasion. Recently, they have been considered as tools to prevent double non-taxation. As at December 2018, Nigeria has 13 effective DTAs with trading partners.[758] For a treaty to have the force of law in Nigeria, such treaty must be enacted into law by the National Assembly. This is a constitutional provision,[759] which empowers the National Assembly to make laws for the country or any part thereof, with respect to matters not included in the Exclusive Legislative List for the purpose of implementing a treaty.[760]

On the duty to pay tax, it is a constitutional provision that every citizen shall declare his income honestly to appropriate and lawful agencies and pay his tax promptly.[761] This ensures that the country is able to: "harness the resources of the nation and promote national prosperity and an efficient, dynamic and self-reliant economy";[762] "control the national economy in such manner as to secure the maximum welfare, freedom and happiness of every citizen on the basis of social justice and equality of status and opportunity".[763]

In the exercise of its constitutional powers to make laws for the Federation, the National Assembly has enacted laws of relevance to the discussion here. I shall briefly highlight these laws and show their relevance to the thesis.

2.1.1. Federal Inland Revenue Service (Establishment) Act, 2007.

758 The countries are: Canada, Pakistan, Belgium, France, Romania, Netherlands, United Kingdom, China, South Africa, Italy, Philippines, Czech Republic and Slovakia. Data obtained from the website of the Federal Inland Revenue Service of Nigeria (FIRS), online: <https://www.firs.gov.ng/tax-treaties.html>.
759 The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 12(1).
760 The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 12(2). Item 31 of the Exclusive Legislative List, which provides exclusive powers to the National Assembly to make laws for the implementation of treaties relating to matters contained on the Exclusive Legislative List.
761 The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 24(f).
762 The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 16(1).
763 The Constitution of the Federal Republic of Nigeria, C-23, 2004, s 16(1)(b).

The Federal Inland Revenue Services (Establishment) Act (FIRS Act) establishes the Federal Inland Revenue Service (the FIRS) as a body corporate with perpetual succession, able to sue and be sued in its corporate name, and able to acquire and hold property.[764] Section 2 of the FIRS Act states the object of the FIRS as "to control and administer the different taxes and laws specified in the First Schedule or other laws made or to be made, from time to time, by the National Assembly or other regulations made thereunder by the Government of the Federation and to account for all taxes collected."[765] Corporate income tax is one of the taxes listed in the First Schedule.

The functions of the FIRS include to: assess persons including companies, enterprises chargeable with tax;[766] assess, collect, account and enforce payment of taxes as may be due to the Government or any of its agencies;[767] in collaboration with the relevant ministries and agencies, review the tax regime and promote the application of tax revenues to stimulate economic activities and development;[768] make, from time to time, a determination of the extent of financial loss and such other loss by government arising from tax fraud or evasion and such other losses (or revenue forgone) arising from tax waivers and other related matters;[769] adopt measures to identify, trace, freeze, confiscate or seize proceeds derived from tax fraud or evasion;[770] adopt measures which include compliance and regulatory actions, introduction and maintenance or investigative and control techniques on the detection and prevention of non-compliance;[771] collaborate and facilitate rapid exchange of information with relevant national or international agencies or bodies on tax matters;[772] establish and maintain a system for monitoring international dynamics of taxation in order to identify suspicious transactions and perpetrators and other persons involved;[773] undertake and support research on similar

[764] The Federal Inland Revenue Service (Establishment) Act, 2007, s 1.
[765] The Federal Inland Revenue Service (Establishment) Act, 2007, s 2.
[766] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (a).
[767] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (b).
[768] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (d).
[769] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (f).
[770] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (g).
[771] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (h).
[772] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (j).
[773] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (k).

measures with a view to stimulating economic development and determine the manifestation, extent, magnitude and effects of tax fraud, evasion and other matters that affect effective tax administration and make recommendations to the government on appropriate intervention and preventive measures;[774] and collate and continually review all policies of the Federal Government relating to taxation and revenue generation and undertake a systematic and progressive implementation of such policies.[775]

The FIRS has the power to make regulations, with the approval of the minister, as are necessary or expedient to give full effect to the provisions of the FIRS Act and for the effective administration of tax in the country.[776] In exercise of this power, the FIRS in 2018 revised its transfer pricing regulations,[777] which were first published in 2012. In enforcing the BEPS Action Plans, the FIRS has issued Country-by-Country Reporting (CBCR) regulations and guidelines. I shall return to the analysis and relevance of these regulations and their roles in making a shift to unitary approach of income allocation.

2.1.2. The Companies Income Tax Act of Nigeria

The Companies Income Tax Act (CITA) regulates the taxation of companies in Nigeria. The basis for corporate taxation in Nigeria is income derived from, accruing from, brought into or received in Nigeria.[778] The rate of corporate tax in Nigeria is 30 percent.[779] Income liable to tax in Nigeria includes chargeable profits in respect of any trade or business;[780] rent or any premium arising from the use or occupation of any property;[781] and income from dividends, interests, royalties, discounts, charges or annuities.[782] Furthermore, the profits of a Nigerian company

[774] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (n).
[775] The Federal Inland Revenue Service (Establishment) Act, 2007, s 3 (o).
[776] The Federal Inland Revenue Service (Establishment) Act, 2007, s 61.
[777] Income Tax (Transfer Pricing) Regulations, 2018.
[778] The Corporate Income Tax Act, C-21, 2004, s 9 (1)
[779] The Corporate Income Tax Act, C-21, 2004, s 40.
[780] The Corporate Income Tax Act, C-21, 2004, s 9(1)(a).
[781] The Corporate Income Tax Act, C-21, 2004, s 9(1)(b).
[782] The Corporate Income Tax Act, C-21, 2004, s 9(1)(c).

are deemed to accrue in Nigeria, notwithstanding where they may have arisen and whether they have been brought into or received in Nigeria.[783] A Nigerian company is defined as a company which has been incorporated in Nigeria.

Profits of a non-Nigerian company from trade or business are deemed to be derived from Nigeria where that company: has a fixed place of business;[784] habitually operates a trade or business in Nigeria through an agent;[785] engages in a single contract for surveys, deliveries, installations or construction;[786] or has a subsidiary or branch in Nigeria and conditions are imposed between the company and such branch or subsidiary in their commercial or financial relations which the Board of the FIRS deems to be artificial or fictitious[787]. The profit of the company will be adjusted to reflect arm's length pricing and taxed subsequently.[788] The arm's length principle is enshrined under the domestic law of Nigeria and profits arising from transfer mispricing is taxable as chargeable profits. This applies, notwithstanding the presence or absence of tax treaties. This is buttressed by section 22 of the CITA, which empowers the Board of the FIRS to disregard any transaction which in its opinion, it considers fictitious or artificial.[789]

By virtue of section 55 of CITA every company is duty-bound to, at least once a year file its tax returns with the Board of the FIRS, without notice or demand. The return must include, the audited accounts, tax and capital allowances

[783] The Corporate Income Tax Act, C-21, 2004, s 13.
[784] The Corporate Income Tax Act, C-21, 2004, s 13 (2)(a).
[785] The Corporate Income Tax Act, C-21, 2004, s 13(2)(b).
[786] The Corporate Income Tax Act, C-21, 2004, s 13(2)(c).
[787] Artificial or fictitious transactions are defined as transactions that, "have not been made on terms which might fairly have been expected to have been made by persons engaged in the same or similar activities dealing with one another at arm's length" as a result of the control of one over the other. See, section 22(2)(b) of the Companies Income Tax Act.
[788] The Corporate Income Tax Act, C-21, 2004, s 13(2)(d).
[789] Section 22(1)- "where the Board is of opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments shall be made as respects liability to tax as it considers appropriate so as to counteract the reduction of liability to tax affected, or reduction which would otherwise be affected, by the transaction and any company concerned shall be assessable accordingly."

computations and a profit statement.[790] There are no provisions for group accounts under the CITA.

2.1.3. Companies and Allied Matters Act

The administration of companies in Nigeria is one of the items on the Exclusive Legislative List. This implies that the National Assembly has the powers to make laws, exclusively, for the due administration of companies in the country. To this end, the National Assembly enacted, in 1990, the Companies and Allied Matters Act (CAMA), with proposed amendments in 2018. The executive arm of the government at the federal level has responsibilities for the implementation of the provisions of CAMA.

The CAMA was enacted to regulate the establishment and operation of companies in Nigeria. Any two or more persons may form and incorporate a company.[791] Foreign companies intending to carry on business in Nigeria must incorporate a local subsidiary in Nigeria, before commencing business.[792] This provision to incorporate a local subsidiary may not apply where the foreign company has obtained exemption from the President of the Federal Republic of Nigeria.[793]

On reporting, every company is mandated to keep accounting records, at its registered office or such place determined by its directors,[794] showing the financial position of the company.[795] The accounting records must show all sums of money

[790] The Corporate Income Tax Act, C-21, 2004, s 55
[791] The Companies and Allied Matters Act, C-20, 2004, s 18.
[792] The Companies and Allied Matters Act, C-20, 2004, s 54.
[793] The Companies and Allied Matters Act, C-20, 2004, s 56. This section highlights the basis upon which exemption may be granted by the President. They are: (a). foreign companies invited to Nigeria by or with the approval of the Federal Government to execute any specified individual project; (b) foreign companies which are in Nigeria to execute loan projects on behalf of a donor country or international organization; foreign government-owned companies engaged solely in export promotion activities; and engineering consultants and technical experts invited by any government of Nigeria to execute individual specialised projects, where such contract has been approved by the Federal Government.
[794] The Companies and Allied Matters Act, C-20, 2004, s 332.
[795] The Companies and Allied Matters Act, C-20, 2004, s 331.

received and expended by the company, and the matters in respect of which the receipt and expenditure took place.[796] Where the company engages in trading of goods, the accounting records must show stock of goods, goods sold and purchased, the buyers and sellers in sufficient detail to enable them to be identified, save for goods sold by way of retail trade. Furthermore, the directors of the company have the duty to prepare annual accounts of the company.[797] The annual accounts of the company include: statement of the accounting policies of the company;[798] balance sheet as at the last day of the year;[799] a profit and loss account, or an income and expenditure account, for non-profit trading companies;[800] notes on the accounts;[801] auditors' reports;[802] directors' report;[803] statement of the source and application of fund;[804] value-added statement for the year;[805] five-year financial summary;[806] and group financial statements, in the case of a holding company.[807] It must be noted that the CAMA does not make it mandatory for private companies to prepare statement of the accounting policies, statement of the source and application of fund, value-added statement for the year, and five-year financial summary.

On group financial statements, the CAMA provides that where a company has subsidiaries[808], the directors of the company shall prepare group financial statements, showing the state of affairs and profit and loss of the company and its subsidiaries.[809] However, this provision does not apply where the Nigerian company is a wholly owned subsidiary of another body corporate incorporated in

[796] The Companies and Allied Matters Act, C-20, 2004, s 331(3)(a).
[797] The Companies and Allied Matters Act, C-20, 2004, s 334.
[798] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(a).
[799] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(b).
[800] The Companies and Allied Matters Act, C-20, 2004, s 334(c).
[801] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(d).
[802] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(e).
[803] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(f).
[804] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(g)
[805] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(h)
[806] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(i).
[807] The Companies and Allied Matters Act, C-20, 2004, s 334(2)(i).
[808] A subsidiary is deemed to be a subsidiary of another company if: (a) the company is a member of it and controls the composition of its board of directors; (b) or the company holds more than half in nominal value of its equity share capital; (c) or the first-mentioned company is subsidiary of any company which is that other's subsidiary.
[809] The Companies and Allied Matters Act, C-20, 2004, s 336(1).

Nigeria.[810] The implication of this provision for intra-firm transactions is to limit the acknowledgment of transfer pricing practice and record-keeping to Nigerian companies with foreign subsidiaries or parent companies. This is in contrast to the tax laws, which extend transfer pricing rules to Nigerian entities that transact with local subsidiaries and are required to prepare transfer pricing documentation to that effect. The group financial statements shall consist of a consolidated balance sheet, consolidated profit and loss account.

2.1.4. National Tax Policy[811]

Nigeria's tax laws are influenced by principles contained in the country's tax policy. Though policies are not legislative instruments and are, in most cases, documents prepared by the executive arm of government, they (policies) guide law-makers when making laws. Specifically, the national tax policy of Nigeria is to: guide the operation and review of the tax system; provide the basis for future tax legislation and administration; serve as a point of reference for all stakeholders on taxation; provide benchmark on which stakeholders shall be held accountable; and provide clarity on the roles and responsibilities of stakeholders in the tax system."[812]

The National Tax Policy of Nigeria was first published in 2012, which provided guidance for the country's direction in its tax space. However, four years later, acknowledging the changing commercial environment, the country's low tax to GDP ratio, the federal government's economic diversification drive and the urgent need to ease tax compliance and administration, a committee was set up to review the country's tax policy. In 2016, the committee completed its assignment and published a document, which was adopted by the Federal Ministry of Finance of Nigeria. In February 2017, the Ministry of Finance published the new National Tax Policy, with the hope that the revised policy "will eventually give a new lease

---

[810] The Companies and Allied Matters Act, C-20, 2004, s 336(2).
[811] National Tax Policy of the Federal Ministry of Finance, accessible online: <https://pwcnigeria.typepad.com/files/fec-approved-ntp---feb-1-2017.pdf>.
[812] Paragraph 1.5 of the National Tax Policy of the Federal Ministry of Finance.

of life to and inspire far-reaching reform of the Nigerian tax system in terms of structure, number of taxes, and administration of taxes, within the context of our peculiar environment."[813]

The National Tax Policy Document defines tax as "any compulsory payment to government imposed by law without direct benefit or return of value or a service whether it is called a tax or not."[814] This helps clarify the lingering dispute in some quarters whether levies and rates imposed by other tiers of government, which are not expressly termed tax in the tax laws of Nigeria, are taxes in the narrow sense.

Of relevance to this chapter, are the policy statements to advance the administration and collection of taxes, especially, as it relates to MNEs and cross-border transactions.[815] The National Tax Policy provides that the country's tax laws and practice must ensure the attainment of the following: ability of all taxable persons to declare their income honestly to appropriate and lawful agencies and pay their tax promptly;[816] promoting fiscal responsibility and accountability that reflects the principle of fiscal federalism;[817] eradicating corrupt practices and abuse of authority in the tax system;[818] ensuring that the resources of the nation promote national prosperity and self-reliant economy;[819] ensuring that the resources of the nation are harnessed and distributed to serve the common good;[820] promoting and protecting Nigeria's national interest;[821] promoting African integration, international co-operation and eliminating discrimination;[822] and respecting international law and treaty obligations.[823] These policy statements are to guide the arms of government (executive, legislative, judicial) in their

[813] See the Foreword to the National Tax Policy of the Federal Ministry of Finance.
[814] Paragraph 1.2 of the National Tax Policy of the Federal Ministry of Finance.
[815] Paragraph 1.3 of the National Tax Policy of the Federal Ministry of Finance.
[816] Paragraph 1.3(a) of the National Tax Policy of the Federal Ministry of Finance.
[817] Paragraph 1.3(c) of the National Tax Policy of the Federal Ministry of Finance.
[818] Paragraph 1.3(e) of the National Tax Policy of the Federal Ministry of Finance.
[819] Paragraph 1.3(f) of the National Tax Policy of the Federal Ministry of Finance.
[820] Paragraph 1.3(f) of the National Tax Policy of the Federal Ministry of Finance.
[821] Paragraph 1.3(i) of the National Tax Policy of the Federal Ministry of Finance.
[822] Paragraph 1.3(j) of the National Tax Policy of the Federal Ministry of Finance.
[823] Paragraph 1.3(j) of the National Tax Policy of the Federal Ministry of Finance.

administration, legislation and interpretation of tax laws and practice in the country.

Concluding this section, the above discussion was to highlight the constitutional and legal frameworks for taxation of MNEs in Nigeria. In the next section, I shall discuss the existing tax practice in Nigeria, as it relates to MNEs, related entities, cross-border economic activities and transfer pricing issues arising therefrom.

2.2 The Treatment of Multinational Entities under the Companies Act and the Companies Income Tax Act of Nigeria

The first point to note is the conflict between the CAMA and the CITA. Recall that section 54 of the CAMA provides that no foreign company is to carry out business in Nigeria without incorporating a subsidiary, except in limited circumstances where the foreign company is exempted from incorporation, as provided in section 56 of CAMA. This presupposes that a foreign company that does not have a local subsidiary here in Nigeria should not be liable to tax, as it is not recognised as an entity under the CAMA. However, the tax laws and practice of Nigeria subject branches of foreign entities to taxation here in Nigeria, notwithstanding that they are not incorporated in Nigeria and are in breach of the laws of Nigeria. This is contained in the CITA and the transfer pricing rules, established pursuant to the CITA, which provides that a permanent establishment and its head office are treated as separate entities and transactions between them are treated as controlled transaction.

This is clarified in the Circular issued by the FIRS, entitled, "The Taxation of Non-Residents in Nigeria" (the Circular).[824] The Circular clearly states that every company, resident and non-resident, is liable to tax under the CITA. It states that

[824] Federal Inland Revenue Service Information No: 9302: Subject- The Taxation of Non-Residents in Nigeria, issued 22nd March 1993, accessible online: <https://www.firs.gov.ng/sites/Authoring/contentLibrary/3b8f359e-d0ec-4a2e-d63d-1e7db187a6f92.TAXATION%20OF%20NON-RESIDENTS%20IN%20NIGERIA-9302.pdf>.

the "Nigerian tax laws do not exempt the income of a branch from tax".[825] The Circular notes that the Nigeria branch of a foreign company is treated as a corporate entity under the law of Nigeria and income or profit derived from the branch is taxable in Nigeria.[826] The only exemptions are where the branch is used solely for storage or display of goods or merchandise or for the collection of information. Thus, the discussion here covers both the subsidiaries and branches of companies doing business in Nigeria.

The treatment of related or connected entities[827] engaged in intra-firm transactions is contained in the transfer pricing rules.[828] The objectives of the transfer pricing rules are spelt out in regulation 2 of the Regulations. In summary, they aim to: ensure that Nigeria can tax appropriate persons and income, corresponding to their economic activities in Nigeria, when they transact and deal with related persons;[829] provide the tax authorities with the tools to fight tax evasion, which arises as a result of over or under pricing of transactions between related persons;[830] reduce the risk of double taxation;[831] create a level playing field for both multinational and independent entities to carry on business in Nigeria;[832] and provide certainty of transfer pricing treatment to taxable persons.[833]

Nigeria's transfer pricing rules are based on the arm's length principle.[834] The arm's length principle is to be applied in a manner consistent with the: arm's length principle in Article 9 of the UN and OECD Model Tax Conventions on Income and Capital; OECD Transfer Pricing Guidelines for Multi-national

[825] Paragraph 2.32 of the Circular.
[826] Paragraph 2.4 of the Circular.
[827] Connected persons "are deemed connected where one person has the ability to control or influence the other person in making financial, commercial or operational decisions, or there is a third person who has the ability to control or influence both persons. In making financial, commercial, or operational decisions". See, Regulation 12 of the Income Tax (Transfer Pricing) Regulations, 2018.
[828] The Income Tax (Transfer Pricing) Regulations, 2018 of Nigeria.
[829] The Income Tax (Transfer Pricing) Regulations, 2018, r 2(a).
[830] The Income Tax (Transfer Pricing) Regulations, 2018, r 2 (b).
[831] The Income Tax (Transfer Pricing) Regulations, 2018, r 2(c).
[832] The Income Tax (Transfer Pricing) Regulations, 2018, r 2 (d).
[833] The Income Tax (Transfer Pricing) Regulations, 2018, s 2 (e).
[834] The Income Tax (Transfer Pricing) Regulations, 2018, r 4.

Enterprises and Tax Administrations, 2017 and the UN Practical Manual on Transfer Pricing for Developing Countries, 2017, as may be supplemented and updated from time to time.[835] However, where inconsistency exists between Nigeria's domestic laws and both the UN and OECD's tax conventions and guidelines or manual, the provisions of the domestic laws shall prevail. The provisions of the transfer pricing rules contained in the Regulations shall prevail over other regulatory authorities' approvals.

The transfer pricing rules apply to the sale of goods and services, sales, purchase or lease of tangible assets, transfer, purchase, licence or use of intangible assets, provision of services, lending or borrowing of money, manufacturing arrangements, and any transaction, which may affect the profit or loss of a company.[836] The rules recommend the application of one of the transfer pricing methods: the Comparable Uncontrolled Price (CUP) method; the Resale Price method; the Cost Plus method; the Transactional Net Margin method; the Transactional Profit Split method; or any other method prescribed by Regulations by the FIRS.[837] The rules recommend the application of the most appropriate transfer pricing method, taking into consideration the: respective strengths and weaknesses of the transfer pricing method in the circumstances of the case; appropriateness of the transfer pricing method having regard to the nature of the controlled transaction; availability of reliable information needed for comparability analysis; and the degree of comparability between the controlled and uncontrolled transactions, including the reliability, where needed to eliminate differences between the comparable transactions.[838]

Furthermore, a taxable person may apply a transfer pricing method, other than those expressly listed in Regulation 5(1) of the transfer pricing rules. This is the case where the taxable person can establish that none of the other transfer pricing methods can be reasonably applied to determine whether the controlled

[835] The Income Tax (Transfer Pricing) Regulations, 2018, r 18.
[836] The Income Tax (Transfer Pricing) Regulations, 2018, r 3.
[837] The Income Tax (Transfer Pricing) Regulations, 2018, r 5(1).
[838] The Income Tax (Transfer Pricing) Regulations, 2018, r 5(2).

transaction is at arm's length; and that the method chosen gives rise to a result, consistent with that between independent persons who transact with each other at arm's length; and the reliable information needed to apply the chosen transfer pricing method exists. It is note-worthy that the rules mandate the FIRS to base its review of controlled transaction on the transfer pricing method used by the taxpayer and may only use another method for review of the controlled transaction, where it considers that other method most appropriate in the given circumstances.[839] The rules provide for corresponding adjustment, where adjustment is made to the taxable profits or income in the other country, of a taxable person, taxable in Nigeria on same income or profit. This is specifically applicable where a double taxation agreement exists between Nigeria and the other country.

Nigeria's transfer pricing rules have been overhauled from their 2012 version, in line with the OECD's BEPS Project and the BEPS Action Plans. The transfer pricing documentation requirement has been expanded to comply with the recommendations of the BEPS Action Plan 13 on transparency. Eligible taxpayers are now required to prepare and maintain a master file and a local file. The master file provides an overview of the global business operations of the MNE. The master file shall include information on the: organisational structure of the business; description of the MNE's business; intangibles transactions; MNE's intercompany financial activities; financial and tax provisions of the MNE. The local file, on the other hand, discloses related party transactions within the MNE, in a detailed manner. Information contained in the local file shall include: overview of the enterprise, such as management structure, business strategies, financial data; related party relationship, such as name of related parties, legal representatives, composition of senior management, tax information, mergers and acquisitions; controlled transactions, such as value chain analysis, related party equity transfers, comparability analysis, selection and application of transfer pricing method and financial information.[840]

[839] The Income Tax (Transfer Pricing) Regulations, 2018, r 5(3).
[840] Schedule to Regulation 17 of the Income Tax (Transfer Pricing) Regulations, 2018.

For bigger companies with an annual revenue of 160 billion Naira[841] and above, a third layer of compliance has been introduced. These companies are to complete and file Country-by-Country (CBC) Reports.[842] The introduction of CBC Reports is in compliance with the OECD's "Guidance on Transfer Pricing Documentation and Country-by-Country Reporting", published on 16 September 2014.[843] To this end, the FIRS has produced the Income Tax (Country-by-Country Reporting) Regulations 2018, alongside guidance document for the implementation of CBC reporting in Nigeria.[844] The objectives of the CBCR, as enumerated in the CBCR Regulations are to: make available information on the global activities, profits and taxes of MNEs to tax authorities;[845] make available to tax authorities, information on assessing international tax avoidance risks;[846] improve transparency of tax practice of MNEs;[847] and address tax evasion and avoidance through base erosion and profit shifting.[848] The CBC Report, using aggregated data, presents clear indicators of the location of economic activities and value creation, among the tax jurisdictions where the MNE group operates.

The CBCR Regulations mandate the filing of consolidated financial statements by the Nigerian subsidiary, where the Nigerian subsidiary is the ultimate parent company or the surrogate company. The CBCR Regulations define the consolidated financial statements as, "the financial statements of an MNE group

---

841 Equivalent of 750 million Euros, using 2015 exchange rates.
842 Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018.
843 OECD (2017), Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment, OECD, Paris, online: <www.oecd.org/tax/beps/country-by-country-reporting-handbook-on-effective-tax-risk-assessment.pdf>.
844 Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, online: <https://www.firs.gov.ng/sites/Authoring/contentLibrary/d6f75a74-2a5e-4b8f-a9db-3f2fe3b183a9The%20Income%20Tax%20(Country-by-Country%20Reporting).pdf>
845 The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 2(a).
846 The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 2(b).
847 The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 2 (c).
848 The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 2 (d).

in which the assets, liabilities, income, expenses and cash flows of the Ultimate Parent Entity and the Constituent Entities are presented as those of a single economic entity". The CBCR Regulations recommend that the consolidated financial statements be prepared in line with the requirements of the International Financial Reporting Standard (IFRS), or any other accounting standard approved by the Financial Reporting Council of Nigeria.

To ensure compliance with the CBCR Regulations, a constituent entity of an MNE group, resident in Nigeria for tax purposes, shall notify the FIRS whether it is the Ultimate Parent Entity or the Surrogate Parent Entity, in which case, it shall have the responsibility to complete and file the CBC Report. Where the Nigerian entity is neither the Ultimate Parent Entity, nor the Surrogate Parent Entity, it shall inform the FIRS, of the identity and tax residence of the reporting entity, not later than the last day of the reporting accounting year of such MNE group.[849]

Information required to be contained in the CBC Report include: aggregated information on the amount of revenue, profit or loss pre-tax, income tax paid, income tax accrued, stated capital, accumulated earnings, number of employees, tangible assets other than cash or cash equivalents, belonging to each jurisdiction within the MNE group;[850] identification of each constituent entity of the MNE group, the jurisdiction of tax residence of the constituent entity, and the nature of the business of the constituent entity.[851] The CBCR Regulations require eligible taxpayers to file the CBC Report not later than 12 months after the last day of the reporting accounting year of the group.[852]

The CBCR Regulations provide for the use of the CBC Report by the relevant tax authority. The CBC Report filed by companies may be used for transfer pricing

[849] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 6.
[850] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 7(a).
[851] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 7(b).
[852] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 9.

risks high-level assessment, assessing the risks of non-compliance with the transfer pricing rules by members of the MNE group, and/or economic and statistical analysis.[853] However, the CBC Report shall not be used as a basis for transfer pricing adjustment by the tax authority.[854]

This limitation of the use of the CBC Report is frustrating for tax authorities and government, who in the light of known tax avoidance and evasion practices, will be unable to act. Limiting the use of the CBC Report to the policy space is unhelpful for countries, especially African countries. This is where the unitary approach may be highly relevant and practical today. Given that the CBC Report shows where the economic activities occur and value is created in an MNE group, such information makes it easy to apportion the global profits or income based on pre-selected formula. For a long time, one of the arguments against the adoption of the unitary approach has been the absence of consolidated financial accounts of MNE groups for tax purposes. With the CBC Report, in addition to the requirement to maintain and file master file and local file, tax authorities are better equipped with information to appropriately apportion global profits or income.

Furthermore, the tax authority must guarantee the confidentiality of the CBC Report filed by eligible taxpayers.[855] The Regulations provide for monetary penalty for failure to complete and file the CBC Report, or failure to notify the tax authority of the ultimate parent entity or the reporting entity for the MNE group.[856]

2.3 Treatment of Multinational Entities under the Nigerian Model Tax Treaty

[853] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 10 (1).
[854] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 10 (1)(b).
[855] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 10(2).
[856] The Federal Inland Revenue Service (Establishment) Act, 2007 Income Tax (Country-by-Country Reporting) Regulations, 2018, r 11, 12 & 13.

Nigeria has enacted a model treaty convention[857] with respect to taxes on income and on capital (Nigeria MTC). The Nigeria MTC borrows largely from the OECD MTC. Both articles 7 (branches) and 9 (subsidiaries) of the model convention adopt the separate entity treatment and arm's length principle. Article 7 of the Nigeria MTC provides that the profits attributable to a branch are the profits it might be expected to make if it were a separate and independent enterprise, engaged in the same activities under similar conditions.[858] Article 7(3) provides for the power to adjust the amount of tax charged on an entity, to avoid double taxation. This is relevant where a Contracting State has made an adjustment to the profits of the branch of an enterprise in its Contracting State, and double taxation may arise if the other Contracting State does not corresponding adjust the tax levied on the branch.

Article 9 of Nigeria MTC, similar to the OECD's model convention, provides for the independent entity treatment of related entities in an MNE group. It provides for corresponding adjustment of tax charged to avoid double taxation. The challenges of this provision and that of Article 7 have been discussed in previous chapters of this thesis and shall be adopted here.

2.4 Proposed Reforms

The international tax practice in Nigeria has witnessed significant reforms in the last 5 years, corresponding with the OECD's BEPS Project. In 2016, the country joined the BEPS Inclusive Framework and attended the inaugural meeting held in Japan.[859] Since joining the BEPS Inclusive Framework, Nigeria has adopted the BEPS Action Plans and recommendations, in some cases, being signatory to multilateral conventions, and in others, amending its domestic tax regulations and practices to correspond with the global tax reforms.

---

[857] Model Convention with Respect to Taxes on Income and on Capital, Nigeria.
[858] Article 7(2) of the Model Convention with Respect to Taxes on Income and on Capital, Nigeria.
[859] The head of the International Tax Department, FIRS, Mr. Matthew Gbonjubola, was in 2018, elected Vice-Chairman of the BEPS Inclusive Framework, strengthening Nigeria's involvement in the BEPS Project.

Specifically, in 2017, Nigeria signed both the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the MLI) and Country Reporting Standard Multilateral Competent Authority Agreement (the CRS MCAA).[860] The MLI presents a bold move by countries to amend existing tax treaties without carrying out individual bilateral negotiations with treaty partners, thus achieving a quick and efficient manner of preventing base erosion and profit shifting by MNEs.[861]

The CRS MCAA, on its part, promotes the automatic exchange of tax and financial information among countries, by implementing the OECD/G20 Common Reporting Standard (CRS), based on Article 6 of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. The recommendations of the MLI and the CRS MCAA have been reflected in the 2018 transfer pricing rules, the new national tax policy and recent guidance document issued by the FIRS.

At a continental level, Nigeria remains an active member of the African Tax Administration Forum (ATAF). Mr. Tunde Fowler, Chairman of FIRS, was in 2018, re-elected chairperson of ATAF, for another 2-year term.[862] Nigeria's involvement in ATAF has seen the country participate in regional discussions, development of practical tools and south-south cooperation. In 2017, ATAF launched its Transfer Pricing Toolkit, with the aim of assisting African tax authorities determine "whether particular high-risk related party transactions

---

[860] OECD, "Nigeria Signs Both the Multilateral BEPS Convention and the CRS Multilateral Competent Authority Agreement to Tackle International Tax Avoidance and Evasion" (17 August 201 7) OECD Publication, online: <http://www.oecd.org/tax/nigeria-signs-multilateral-beps-convention-and-crs-multilateral-competent-authority-agreement-to-tackle-international-tax-avoidance-and-evasion.htm>.

[861] The BEPS Monitoring Group, "Explanation and Analysis of Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MC-BEPS)" online publication of The BEPS Monitoring Group: <https://static1.squarespace.com/static/5a64c4f39f8dceb7a9159745/t/5af4dc10f950b78091d69b0d/1525996565723/explanation-and-analysis-of-mc-beps-final-rev.pdf>.

[862] The Sun, "ATAF Re-elects Fowler as African Tax Chief" (26 October 2018) The Sun Newspaper, online: <https://www.sunnewsonline.com/ataf-re-elects-fowler-as-african-tax-chief/>.

should be selected for transfer pricing risk".[863] The 2018 transfer pricing rules of Nigeria contains provisions from the ATAF Transfer Pricing Toolkit, which Nigeria was actively involved in the negotiation and drafting.

These tax reforms by Nigeria are welcome and timely. If the country is to significantly improve on its current tax to GDP ratio, which averages 5-6%, then the country must take bolder moves, especially as it relates to cross-border transactions by related entities.

3 Application of the Unitary Taxation of Multinational Entities in Nigeria

Multinational entities operate in Nigeria either as local subsidiaries or branches. The country has more than 2,900 taxpayers who are subject to transfer pricing rules. In this section, I consider the regulatory steps towards achieving a shift to unitary approach at a country level and regional level.

3.1 Nigeria's Federal Structure and Implication for Unitary Taxation

As stated above, Nigeria is a federal state, divided into 36 semi-autonomous units and a federal capital territory. Its fiscal federalism has always been a subject of controversy. This is as a result of the power, constituent units exercise over their resources and revenue. On resources, the constitution of Nigeria grants ownership of all resources, on, above and below the earth, to the federal government. On revenue, the constitution grants the power to make laws on taxation of income, profits, and capital gains to the National Assembly. It is the practice that the federal government collects, to the exclusion of all others, taxes from income and profits from companies. State governments are empowered to collect taxes from income and profits from individuals.

[863] Gauge- A Quarterly Publication of the Federal Inland Revenue Service (July-September 2017), at 5.

Achieving a shift to the unitary approach from the present tax structure may demand legislative amendments, depending on one's interpretation of the legal texts. However, there will be no requirement to amend the constitutional provision on taxation. This is because the constitution only admonishes citizens to declare their income honestly to appropriate and lawful agencies and pay their taxes promptly. It leaves to the National Assembly the responsibility of determining how, what, where and to whom, taxes will be paid. This is relevant consideration, given the elaborate and rigorous process of amending a provision of the constitution.

In the same vein, nothing in the FIRS Act suggests that a textual amendment is necessary to achieve a shift to the unitary approach. Even so, the functions[864] and powers[865] of the FIRS are broadly described to empower it, through its power to make regulations, to establish a tax regime based on the unitary approach. This is to the primary duty of the FIRS to control and administer the different taxes and laws specified in the enabling act or as may be prescribed by the National Assembly.[866]

On its part, the CITA may be viewed as requiring textual amendments to achieve a shift to the unitary approach. This is because the term "arm's length" is mentioned in the Act. Specifically, section 13(2)(d) of the CITA empowers the FIRS to adjust the profit of a corporate taxpayer to reflect arm's length transaction, where the commercial or financial relations between controlled entities is deemed to be artificial or fictitious. This is buttressed in section 22(2)(b) of the CITA, which establishes the comparability analysis needed to establish that transactions between related or controlled entities are artificial or fictitious. Even so, the Income Tax (Transfer Pricing) Regulations give effect to the provisions of the CITA on related party transactions, providing transfer pricing methods and documentation needed to establish the arm's length principle.

[864] Federal Inland Revenue Service Act, s 3.
[865] Federal Inland Revenue Service Act, s 61.
[866] Federal Inland Revenue Service Act, s 2.

It is thus clear that both the CITA and the transfer pricing rules adopt the separate entity treatment of companies and the arm's length principle. A shift to the unitary approach of taxing multinational entities will require textual amendment of both the provisions of the CITA and the transfer pricing regulations. The amendment of the CITA will be carried out by the National Assembly, while the amendment of the transfer pricing regulations will be carried out by the Board of the FIRS, under the supervision of the Minister of Finance.

The CAMA already provides for group financial statements and no amendments may be required. Even so, given the introduction of the filing of master file, local file and CBC Reports by MNEs in Nigeria, the provisions of the CAMA are superfluous for tax purpose.

3.2 Trading Blocs as Testing Grounds for Unitary Taxation and Nigeria's Role as a Key Stakeholder in ECOWAS and the AU

Though the unitary approach has, so far, only been practised at the national level, the calls for the shift to the unitary approach are largely for its adoption at a regional, continental or world-wide basis. For African countries engaged in cross-border economic activities, regional cooperation on income allocation may go a long way in attracting FDI, reducing tax competition and ensuring administrative efficiency. Multilateral tax regime, in the form of a regional or continental unitary approach may reduce the risks of double taxation and double non-taxation by establishing an agreement between countries within a trade bloc, on sensitive issues for which the tax administrations may differ, such as the pricing of intragroup transactions.

At a regional level, the shift to the unitary approach by ECOWAS countries presents a realistic case for the adoption of the unitary approach. First, the proximity of the countries actually means that there are MNEs who have subsidiaries in other ECOWAS countries. The sectors which witness the presence of most MNEs in the region include telecommunications, banking, transport, agriculture, manufacturing, and the extractive industries.[867] Second, Nigeria dominates the economy of the ECOWAS region, in terms of the volume and value of trade. Given Nigeria's economic dominance, it is able to wield political power in influencing the adoption of the unitary approach. Third, the transfer pricing legal regime in ECOWAS Countries is still growing, creating the potential to experiment with a new income allocation system, without disrupting the order. Of the 16 member-countries of the ECOWAS, only 4 (Nigeria, Ghana, Liberia and Senegal) have transfer pricing regulations.[868] This presents great opportunity to adopt the unitary approach at the regional level since the transition cost and process will be bearable.

Implementing a unitary approach to income allocation at the ECOWAS trading bloc comes with its challenges. While the fact that many ECOWAS countries are yet to establish transfer pricing rules and practices in their tax regime has been stated in a positive light above, it may present an obstacle towards a regional adoption of the unitary approach. It must be appreciated that discussion on the adoption of a unitary approach is predicated on certain factors: presence of MNEs in the country; legislation on corporate income taxation; and allocation method for income arising from cross-border economic activities among related entities. At present, the widely-practised allocation method is the OECD's separate entity treatment of entities in an MNE and the arm's length principle. While many African countries have legislation on the taxation of corporate income, a handful of them are yet to establish allocation methods for income from cross-border economic activities among related entities. This may be attributed to the presence of few MNEs in many of these countries and the prioritisation of cross-border economic activities. As a result, negotiating a regional tax system may not receive the political support needed for such a regional agreement, since many countries within the ECOWAS region may not easily appreciate the benefits of such an

[867] Charlet, Silberztein & Pointe, supra note 400.
[868] Picciotto, supra note 29.

agreement. There may be the temptation to focus discussions of a regional unitary approach on countries who are home and host to MNEs, have allocation systems in their tax regimes and experience the challenges of applying the arm's length standard. This will be non-inclusive and may be disadvantageous in the long term, as the economies of countries open and they adopt allocation methods.

There is the challenge of fear of capture of the unitary approach process and terms and conditions by the larger economies. As stated earlier, Nigeria dominates the ECOWAS region economically, politically and military-wise. About 80% of the GDP, FDI inflow and trade volumes taking place in the ECOWAS region are situated in Nigeria. Without checks, it is positioned to dominate the negotiating process, while cornering to itself favourable terms and conditions.

This fear of capture may discourage other countries from agreeing to a regional agreement. One way to address this is by appointing an unbiased mediator to oversee the negotiations. A second approach may be to have negotiators appointed for all parties (or weaker parties, as the case may be) by supranational or donor bodies such as the World Bank, IMF, OECD, etc. The oft-touted breach of tax sovereignty claim may not be relevant here, since from observations many countries have acceded their tax sovereignty to supranational bodies, in exchange for improved revenue generation.[869] Without the involvement of external parties, adjudged to be unbiased, achieving a consensus regional agreement will be difficult in the circumstances, given the imbalance in economic powers.

There are other challenges worth mentioning, however, they are easily surmountable today, given the progress achieved globally through the BEPS

---

869 See, the activities and report of the Tax Inspectors Without Boarders (TIWB), online: <http://www.tiwb.org/resources/publications/tax-inspectors-without-borders-annual-report-2017-2018-web.pdf> the OECD's Automatic of Exchange of Information Agreement- OECD (2017), Standard for Automatic Exchange of Financial Account Information in Tax Matters, Second Edition, OECD Publishing, Paris, online: <https://www.oecd-ilibrary.org/docserver/9789264267992-en.pdf?expires=1554082816&id=id&accname=guest&checksum=B42C2E84DA96467E3736E8942161E135>.

Project. The administrative burden involved in arriving at such agreement, whether through the enactment of a Protocol or Regulation or Directive of the whole is quite immense. Surmounting the language and technical barriers for example in the ECOWAS region will be demanding.

The discussion here on the challenges of adopting the unitary approach at a regional level is relevant to its adoption at a continental level. Similar recommendations apply. However, given the recent establishment of the AfCFTA, the continent is poised to adopt the unitary approach to income allocation. This is because the AfCFTA recognises non-trade barriers to doing business on the continent, of which taxation of income from cross-border economic activities is one. Given the attention directed towards IFFs on the continent by African governments and the consensus that transfer mispricing is a significant cause of the IFFs out of the continent, one would expect African governments to be vested in seeking a solution to the threat of transfer mispricing.

3.3 Suggesting a New Tax Law Treatment of MNEs Model

This section attempts a textual suggestion of the relevant section of the domestic tax laws of Nigeria on income allocation arising from cross border economic activities among related entities. By extension, it provides wording for the relevant article of Nigeria's model tax treaty and other bilateral treaties Nigeria is signatory to or intends to sign.

For the sake of efficiency, I shall reproduce the relevant wording of article 9 of the model tax treaties, acclaimed to have established the arm's length principle. I shall demonstrate departures from part of the wording and addition, where necessary, to establish a unitary approach.

Article 9 of the model tax treaties:

1. Where

a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or
b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State,

and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

I suggest wording for a provision on unitary approach in the tax laws, thus:

> "Where it is established that entities in a group are managed, controlled or owned directly or indirectly by the same persons and they engage in commercial or financial relations, then the consolidated profit of the group will be apportioned among the related entities on the basis of their economic activities and contribution to the group profit, using pre-agreed factors and formula."

Consonance between both provisions:

Administering both provisions hinges on the presence of a relationship between the entities. Such relationship may be via management of the entities by same persons, control of the entities or ownership of the entities by same persons. Before a tax authority can adjust the taxable profits under the current global tax regime, or apportion the profit based on a formula, the tax authority must establish relationship between the entities.

Secondly, beyond the existence of the relationship between the parties, the related parties must engage in commercial or financial relations. This excludes companies, which though part of the corporate group, are not involved in the commercial or financial activities of the group. This may be applicable to entities in tax havens, with no economic activities occurring there, or shell companies incorporated to meet regulatory requirement or act as place holders.

Third, they both (at the minimum, theoretically) focus on the profit of the company, and not on the expenses or price of transactions. This has been a criticism of the OECD's interpretation of article 9 by its enshrinement of the arm's length principle and emphasis on prices of transactions. The OECD's interpretation of article 9 has led to the ineffective search for comparables. Focusing on profits of the group and discounting the value of intra-firm transactions reduces opportunities for aggressive tax planning and profit shift to low tax jurisdictions.

Dissonance between both provisions:

An obvious distinction between article 9 provision and the suggested provision for the unitary approach is the relevance of independent entities in the discussion. Under the current tax regime, there is a requirement to benchmark the relationship between related entities with that of independent entities. This benchmarking requirement is the progenitor of the comparability analysis. In the place of independent entities or comparability analysis, as it may, the suggested provision adopts the threshold of "economic activities and contribution to the group profit". This is a more scientific approach, which is represented by relevant factors such as assets, sales, labour, data, etc.

Another distinction is the presence of pre-determined formula in the unitary approach, distinct from its article 9 counterpart, which relies on individual fact and circumstances analysis of transactions. From an administration perspective, pre-determined formula, factors and terms promote tax predictability and certainty, which eases doing business in a jurisdiction, thereby encouraging investment. This is an improvement from the current tax system, often accused of not being predictable and taxpayers and tax authorities are unaware of the outcome of the transfer pricing process. This is compounded by the recognition that a taxpayer may choose a transfer pricing method it deems fit, arriving at its conclusions, while the tax authority is empowered to apply a completely different transfer pricing method. The uncertainty and unpredictability of the current system makes the entire process expensive, resource-intensive and complex to manage.

Excluding "Value Creation" in the Wording of the Unitary Approach

At inception of the BEPS Project, the OECD stated one of the primary goals of the project as ensuring "that profits are taxed where economic activities generating the profits are performed and value is created."[870] Critics of the arm's length principle argued that the current tax system could not achieve the stated primary goal as it is designed to encourage the erosion of tax bases and shift of profits from one deserving jurisdiction to a low tax jurisdiction.[871] They posited that only a system based on factors of production and sale could ensure that income is taxed where the economic activities occur, and value is created.[872]

Given its insistence on the validity and viability of the current tax system, it may be observed that the OECD has adjusted the stated primary goal of the BEPS Project by carefully excluding "…where economic activities occur" in the allocation of income,[873] and emphasizing more the relationship between where income is taxed, and value is created. This may be an acknowledgment of the claim by tax

[870] OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing, online: <https://www.oecd.org/ctp/BEPSActionPlan.pdf>.
[871] IMF Policy Paper, "Corporate Taxation in the Global Economy" (2019), IMF, Washington, D.C, online: <https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/08/Corporate-Taxation-in-the-Global-Economy-46650>.
[872] ICRICT, "The Fight Against Tax Avoidance. BEPS 2.0: What the OECD BEPS Process has Achieved and what Real Reform Should Look Like" (2019) ICRICT Publication: online: <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5c409495f950b7e303b71a45/1547736215689/thefightagainsttaxavoidance_FINAL.pdf>
[873] BEPS Action Plans 8-10 seek to align transfer pricing outcomes with value creation.

expert that intending to align where income is taxed with where the economic activities occur calls for a complete abandonment of the current tax system and a shift to a unitary approach of taxation of income.[874] Value creation would appear to have become the primary directive of the OECD in achieving a fair allocation of income.[875] However, this directive of aligning where income is taxed with value creation has not gone without criticism.

Experts criticize the use of "value creation" as justification for new international tax rules.[876] One reason they give is that taxation of income achieves the taxation of value capture and not value creation. Taxation of value creation is already captured in countries who possess value added tax regimes in their tax structures. As such, aligning taxation of income with value creation does not effectively address the right to tax debate.[877]

Another criticism of the value creation mantra is its deceptively misleading claim of achieving a neutral, apolitical distribution of income among countries. Christians demonstrates, relying on the Smile Curve, that reliance on the logic of value creation "will always assign virtually all of the credit for international cooperation to wealthy countries".[878] Christians argues that it is a wrong assumption that a dollar of income arising from a seamlessly "symbiotic global economic order can somehow be re-fragmented and correctly assigned to one or another jurisdiction as a technical or economic matter."[879] Issues such as inaccuracy of fragmentation of income and the integrated and symbiotic nature of MNE business make the claim to taxing income based on value creation a difficult task to achieve.

---

874 ICRICT, "The Fight Against Tax Avoidance. BEPS 2.0: What the OECD BEPS Process has Achieved and what Real Reform Should Look Like" (2019) ICRICT Publication: online: <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5c409495f950b7e303b71a45/1547736215689/thefightagainsttaxavoidance_FINAL.pdf>
875 Kash Mansori & Guy Sanschagrin, "Assessing Value Creation for Transfer Pricing" (2016) Tax Notes International, Vol 81, No 13.
876 Ibid.
877 Ibid.
878 Allison Christians, "Taxing According to Value Creation" (2018) Tax Notes International, Vol 90.
879 Ibid at 3.

As a result of the vulnerability of the logic of value creation, my suggested wording for the unitary approach has carefully omitted the phrase, "…where value is created" as seen in the stated primary objective of the OECD's BEPS Project. What this achieves is twofold: one, to accept "value creation" as present in "economic activities"; or two to conclude that the logic of value creation is not important in the apportionment of income under the unitary approach.

It is arguable that jurisdictions where the economic activities occur- be they through ownership of the assets, the provision of labour or the marketing and sale of the goods and services— create value and are adequately rewarded in the factors and pre-determined formula. As such, the wording above may be expansive enough to capture the creation of value, as the case may be. However, where it is disputed that economic activities encompass value creation and that value creation be separately provided for in the wording of the unitary approach, I have inserted the phrase, "contribution to the group profit", which arguably, captures value creation. Thus, "contribution to the group profit" is superfluous or necessary, depending on one's interpretation and appreciation of the wording. Whatever the preference, I have set out to avoid controversy which may fundamentally affect the administration of the unitary approach to income allocation by tax jurisdictions.

4 Political Support Needed to Reform the Tax Law Treatment of Multinational Enterprises

In the previous section, I discussed the legal framework for achieving a shift to the unitary approach to income allocation. I offered wording for what a provision on unitary approach will look like, discussing this within the Nigerian context. In this section, I offer suggestions on achieving the political will, globally and nationally, to achieve the adoption of the unitary approach.

Beyond the legal steps to achieving reforms, the political will to push for reforms is as just as important as pushing for legal enactments. One such current political effort is the global effort to address IFFs. Countries have, at the national level, set out measures to combat IFFs out of their jurisdictions.

IFFs out of countries have amassed global attention due to their global reach and impact. To key into the global discussion and efforts at addressing IFFs, the first step is to determine if the scope of IFFs is broad enough to include tax avoidance. This is where the conflict is and will be addressed below. The intention here is to bring the discussion of transfer mispricing under the United Nation's Sustainable Development Goals (SDGs).[880] This accords the treatment of transfer mispricing the same attention accorded to goals such as poverty, hunger, security, education, etc. To achieve this (i.e. including the discussion of transfer mispricing within the discussion of the SDGs), one must attempt an expansive definition of IFFs, which encompasses tax avoidance. These, I shall attempt to achieve in the subsequent sub-sections.

4.1. Bringing Tax Avoidance under the Scope of Illicit Financial Flows

Indications show that the African continent may be unable to achieve the 2030 SDGs, leading to a new Agenda 2063 set for itself by African leaders to achieve some of the goals listed in the SDGs.[881] The sustainable development goals aim at developing states in a sustainable manner for future generations and improving the quality of life of all. However, this cannot be achieved without the abundance of public revenue. The public revenue of any state is affected by the illicit flow of funds out of its territory. IFFs contribute to the resource curse commonly used to describe the African continent. This paradox of plenty has meant that the

[880] United Nations, "Transforming Our World: The 2030 Agenda for Sustainable Development" UN, New York.
[881] African Union Commission, "Agenda 2063: The Africa We Want" (2015), African Union Commission Secretariat, Addis Ababa: Ethiopia.

continent contains the least developing countries, under-developed countries and developing countries.

Tax-motivated IFFs are manifested in tax evasion and avoidance practices of multinational entities. While it is accepted that tax evasion constitutes part of IFFs, the acceptance of tax avoidance as part of IFFs is a matter for debate. Nevertheless, an increasing number of literatures includes in their calculations of IFFs losses from tax avoidance practices by multinational entities. This is in acknowledgment of the fact that tax avoidance contributes significantly to the under-development of the African continent,[882] and as such should be accorded similar importance as accorded drug trafficking, tax evasion and crime.

The lack of consensus on whether tax avoidance constitutes IFFs may be attributed to the question whether "illicit" means "illegal" or whether it has a broader meaning of being "unacceptable". Illegal connotes a criminal violation of the law. The attribute of being "unacceptable" depicts a broader meaning of violation of legal provisions, or norms, customs, practices, moral standards, ethics, etc. of a community. I shall discuss this.

Adopting an Expansive Definition of Illicit Financial Flows

Why Definition Matters?

Why does the definition of IFFs matter, especially for African countries? Because failing to explore other definitions and narratives perpetuates a single story. There is the danger of a single story here.[883] Western literature is quick to highlight leadership failures, corruption and political crisis as causes of Africa's under-development, without accepting the significant contribution of MNEs

[882] James Boyce & Leonce Ndikumana, "Capital Flight from Sub-Saharan African Countries: Updated Estimates, 1970–2010" (2012) PERI Research Report.

[883] Chimamanda Ngozi Adichie, "The Danger of a Single Story" (2009) YouTube video, online: <https://www.google.ca/url?sa=t&rct=j&q=&esrc=s&source=web&cd=3&cad=rja&uact=8&ved=2ahUKEwiQyK2hkrrhAhVST98KHSscDYgQwqsBMAJ6BAgIEAo&url=https%3A%2F%2Fwww.youtube.com%2Fwatch%3Fv%3DD9Ihs241zeg&usg=AOvVaw1jhYo8eZPB3Dka2oYsQPVJ>.

headquartered in the Global North. Though MNEs do not actively participate in tax evasion, unlike their local counterparts, they are actively involved in tax avoidance on the African continent. Removing tax avoidance from the scope and definition of IFFs perpetuates the popular view that Africans are their own worst enemies, without acknowledging the contributions of outsiders. That is the danger of a single story.

Further, if tax avoidance practices of MNEs are to get the global attention and international cooperation needed to address their root cause, electing an expansive definition becomes important. For example, target 16.4 of the Sustainable Development Goals (SDGs) seeks to "significantly reduce illicit financial and arms flows, strengthen the recovery and return of stolen assets and combat all forms of organized crime".[884] Target 17.1 of the SDGs seeks to "strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection."[885]

The SDGs are global goals set by the United Nations to guide member states in forming their policies and agendas. Thus, they hold great political weight, global acceptance and concerted effort towards achieving them. Similarly, the Mbeki Report since its publication has attracted global attention and concerted efforts at addressing IFFs. The Report situates tax avoidance as a significant cause of IFFs out of Africa. Adopting a narrow definition, limits the work of the panel, creating a setback in addressing tax avoidance practices of MNEs.

Attempting a Definition of Illicit Financial Flows

There is yet to be consensus in the literature on the definition of IFFs.[886] This lack of consensus may be attributed to the question whether "illicit" means "illegal" or

---

[884] United Nations, "Transforming Our World: The 2030 Agenda for Sustainable Development" UN, New York, at 30.

[885] United Nations, "Transforming Our World: The 2030 Agenda for Sustainable Development" UN, New York, at 30.

[886] Annet Oguttu, "Tax Base Erosion and Profit Shifting in Africa- Part 1: Africa's Response to the OECD BEPS Action Plan" (2015) ICTD Working Paper 54.

whether it has a broader meaning of being "unacceptable". Illegal connotes a criminal violation of the law. The attribute of being "unacceptable" depicts a broader meaning of violation of legal provisions, or norms, customs, practices, moral standards, ethics, etc. of a community. A second debate, tied to the first, is whether tax avoidance constitutes IFFs. The determination of this rests on the definition of "illicit".

Where illicit is given a strict and narrow meaning of "illegal" then it would appear that tax avoidance falls outside the scope of IFFs. This is because, over the decades, prevailing literature[887] and court decisions have deemed tax avoidance to be in the realm of questionable morality and not illegality.[888] However, recent judgments by African courts show a departure.[889]

Where illicit is given a broader definition of being unacceptable, then tax avoidance rightly falls within the scope of illicit financial flows. The significance of this distinction will be shown later in the discussion. In the meantime, we reproduce definitions of IFFs, showing the differing views and why consensus is important.

Organisational definitions adopting the narrow, illegality-focused definition include definitions from the World Bank, GFI and the African Tax Administration Forum (ATAF). According to the World Bank, IFFs represent 'cross-border movement of capital associated with illegal activity or more explicitly, money that is illegally earned, transferred or used that cross borders."[890] The Global Financial integrity (GFI), on its part, defines IFFs as "illegal movements of money or capital from one country to another."[891] The ATAF considers IFFs to be "money that is

[887] Allison Christians, "Avoidance, Evasion and Taxpayer Morality" (2014) WASH. U. J.L. & POL'Y, VOL 44, ISSUE 39.
[888] Inland Revenue Commissioners ("IRC") v Duke of Westminster (1935) All ER 259 (HL).
[889] African Barrick Gold vs Commissioner-General, Tanzania Revenue Authority [2013] Tax Appeal No 16 of 2015.
[890] World Bank, "Illicit Financial Flows" (2017) World Bank Brief, Washington D.C. World Bank, online: <http://www.worldbank.org/en/topic/financialsector/brief/illicit-financial-flows-iffs>
[891] Global Financial Integrity, "Illicit Financial Flows" Global Financial Integrity, online: <https://www.gfintegrity.org/issue/illicit-financial-flows/>.

illegally earned, transferred or utilised".[892] The Mbeki Report defines IFFs as "money illegally earned, transferred or used."[893] These definitions put illegality of the actions at the centre of the definition of IFFs, though not in its analysis. I shall return to this.

Organisations adopting the broader definition of IFFs, whether advertently or inadvertently, include the OECD, the UN, and the European Parliament. According to the OECD, IFFs are "generated by methods, practices and crimes aiming to transfer financial capital out of a country in contravention of national or international laws."[894] This definition would appear to recognise the illegal and criminal aspects of IFFs, while at the same time, extending the scope to acts and practices which are not necessarily considered illegal, thereby including tax avoidance in the definition. Some jurisdictions include anti-avoidance provisions in their national laws, thus, making tax avoidance practices contravention of national laws.

The European Parliament considers IFFs to "typically originate from tax evasion and avoidance activities, such as abusive transfer pricing, against the principle that taxes should be paid where profits have been generated".[895] The United Nations Human Rights Council refers to IFFs as, "funds that, through legal loopholes and other artificial arrangements, circumvent the spirit of the law, including, for example, tax avoidance schemes used by transactional corporations".[896]

---

892 African Tax Administrators Forum. "Illicit Financial Flows and Trade Misinvoicing: the challenges for Africa" (2015) ATAF: Pretoria.

893 United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf>

894 OECD, "Illicit Financial Flows from Developing Countries: Measuring OECD Responses" (2013) Paris: OECD.

895 European Parliament, "Report on Tax Avoidance and Tax Evasion as Challenges for Governance, Social Protection and Development in Developing Countries" (2015) (2015/2058(INI)), online: <http://www.europarl.europa.eu/doceo/document/A-8-2015-0184_EN.html#title1>

896 United Nations Human Right Council, "Final Study on Illicit Financial Flows, Human Rights and the 2030 Agenda for Sustainable Development of the Independent Expert on the Effects of Foreign Debt and other Related International Financial Obligations of States on the Full Enjoyment of all Human Rights, particularly Economic, Social and Cultural Rights" (2016) A/HRC/31/61, para 7, online: <https://www.undocs.org/A/HRC/31/61>.

Amongst academics and experts, opinions are divided on the definition of IFFs. Oguttu[897] for instance, argues that equating BEPS and illicit financial flows fosters confusion in understanding international tax principles and in solving the problem of capital flight. She opines that, "…BEPS is as a result of a perceived weakness in the international tax laws, as well as the lack of administrative capacity fully to assess and audit international tax risks which are exploited by MNEs".[898] She holds that IFFs 'arise from a wide range of illegal flows of money including organised crime, money laundering, terrorist financing, bribery, and customs fraud." Charles Goredema[899] wants us to see IFFs as "the movement of illegally transferred assets or value, funds earned through illegal activity (i.e., corruption), or proceeds of tax evasion."[900] These views are corroborated by the work of Maya Forstater in this field. Forstater's views in this discourse are that, "combining legal and illegal activities into a vaguely defined composite category is not something to do lightly, if the overall goal is to strengthen the rule of law, democratic accountability, and the effectiveness of states".[901] She posits that, "…bracketing questions of how to allocate international taxing rights along complex international value chains into the same category as prosecuting theft of public assets, or money laundering of criminal proceeds, implies guilt-by-association which is not helpful for public-private dialogue, development of effective fiscal regimes and accountability, or cooperative compliance."[902]

Lindelwa Ngwenya, on his part, favours a broader discussion, by arguing that in its broadest sense, illicit capital flows should be understood as flows with adverse

[897] Oguttu, supra note 881.
[898] Ibid.
[899] Charles Goredema, "Combating Illicit Financial Flows and Related Corruption in Africa: Towards a More Integrated and Effective Approach" (2011) U4 Issue, No 12, Chr Michelsen Institute.
[900] Ibid at 9.
[901] Maya Forstater, "Illicit Financial Flows, Trade Mis invoicing, and Multinational Tax Avoidance: The Same or Different?" (2018) CGD Policy Paper. Washington DC: Centre for Global Development, online: <https://www.cgdev.org/sites/default/files/illicit-financial-flows-trade-misinvoicing-and-multinational-tax-avoidance.pdf>
[902] Ibid at 30.

economic impact on society.[903] This position is corroborated by Martin Hearson who views tax-motivated IFFs to include tax evasion, tax avoidance and aggressive tax planning.[904]

While definitions appear to be split between the illegal or unacceptable nature of IFFs, one prevailing item in a number of the analyses of IFFs, is the tacit acceptance of tax avoidance as within the scope of IFFs. For example, notwithstanding its narrow definition, the Mbeki Report believes that IFFs "while not strictly illegal in all cases, go against established rules and norms, including avoiding legal obligations to pay tax."[905] It expressly mentions the methods of IFFs in Africa to include "abusive transfer pricing, trade mispricing, misinvoicing of services and intangibles and using unequal contracts, all for purposes of tax evasion, aggressive tax avoidance and illegal export of foreign exchange."[906]

In my opinion and given the above discussion on the definition of IFFs, any definition of IFFs should conclusively establish tax avoidance as part of IFFs. This aligns with the views of those who believe that taxation must be recognised in terms of not only the law and society movement but the racial, ethnic, historical, economic, political, ideological, and belief systems in which it exists.

It must be accepted that the word "illicit" connotes a broader meaning than the word, "illegal". This distinction is recognised in the domestic laws of taxing jurisdictions, which contain provisions against tax avoidance practices without necessarily illegalizing or criminalizing them. On the contrary, these provisions

---

903 Lindelwa Ngwenya, "The Spillovers of Illicit Financial Flows", being paper delivered at the High-level Conference on Illicit Financial Flows: Inter-Agency Cooperation and Good Tax Governance in Africa in Pretoria, 14–15 July 2016, available online: <https://www.wu.ac.at/fileadmin/wu/d/i/taxlaw/institute/WU_Global_Tax_Policy_Center/Siemens/Oct_2015/Annex_6_T_GG_Spillovers_of_IFFs.pdf>.

904 Martin Hearson, "Tax-motivated Illicit Financial Flows: A Guide for Development practitioners" (2014) U4 Issue, No 2, Chr Michelsen Institute.

905 United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf, p. 23>.

906 United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf, p. 24>.

grant the taxing authority the arbitrary power to adjust such returns and tax accordingly, without criminalizing the acts. For instance, section 22 (1) of the Companies Income Tax Act of Nigeria (CITA), provides that, "where the Board is of opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments shall be made as respects liability to tax as it considers appropriate so as to counteract the reduction of liability to tax affected, or reduction which would otherwise be affected, by the transaction and any company concerned shall be assessable accordingly."[907] Section 22 (2)(b) expressly provides that, "transactions between persons one of whom either has control over the other or, in the case of individuals, who are related to each other or between persons both of whom are controlled by some other person, shall be deemed to be artificial or fictitious if in the opinion of the Board, those transactions have been made on terms which might fairly have been expected to have been made by persons engaged in the same or similar activities dealing with one another at arm's length."[908]

The essence of section 22 of the CITA is to make tax avoidance practices of related entities unacceptable, without necessarily criminalizing it. Contrast the provisions of section 22 of CITA with section 55 of the CITA, which makes it an offence not to file returns by a taxpayer and makes provisions for penalties for contravening the provisions of the section. Similar provisions can be found in sections 82, 92, 93, 96 of the CITA.

Even so, the etymology of the word, "illicit" suggests a broader meaning than illegal. The word "illicit" derives from the French word, "illicite" meaning "unlawful, forbidden"; from the Latin word, "illicitus", meaning "not allowed", "unlawful", "illegal". The Oxford Dictionary defines "illicit" as "forbidden by law, rules or custom".[909] This definition, while covering illegal activities such as tax

---

[907] The Corporate Income Tax Act, C-21, 2004, s 22 (1).
[908] The Corporate Income Tax Act, C-21, 2004, s 22(2)(b).
[909] Oxford Dictionary of English, Third Edition, Oxford University Press.

evasion, extends to immoral/unethical activities such as tax avoidance. Black's Law Dictionary, 10th ed., defines "illicit" as "illegal or improper". The word "improper" is defined in the same Black's Law Dictionary, 10th ed., as "incorrect; unsuitable or irregular; fraudulent or otherwise wrongful."[910] These dictionary meanings adopt a broader approach to the meaning of the word, "illicit".

Relying on dictionary meaning of words in judicial interpretation, is part of the legal jurisprudence of African countries who were former British colonies. For instance, in the Tanzanian case of African Barrick Gold Plc v Commissioner-General, Tanzania Revenue Authority (2015), the resolution of the case depended on the dictionary meanings of the words, "incorporated" and "formed". The appellant, relying on the Oxford Advanced Learners Dictionary (8th edition) and the Black's Law Dictionary (9th ed.) had urged the appeal tribunal to interpret both words (incorporate and form) as synonymous- "to create a company or to bring a company into existence". In same case, the appeal tribunal relied on Wharton's Concise Law Dictionary (2012 reprint) and the Black's Law Dictionary (9th ed.) for the meaning of the word, dividend, in deciding that the claim of the appellant that dividends distributed to its shareholders were from the company's distributable reserves and IPO proceeds, were far from being plausible. Similar reliance on dictionary meaning of words can be found in Nigerian legal jurisprudence. See the case of Osafile & Anor v. Odi & Anor[911] where the court relied on the dictionary meaning of words.

In common law and Nigerian legal jurisprudence, it is a canon of interpretation that where words are plain and unambiguous, the court is bound to give the word, its literal interpretation- the "literal rule" of interpretation.[912] The literal rule presupposes that words are intended to have their ordinary and natural meanings, where they are unambiguous and do not lead to absurdity. In this instance, illicit

[910] Black's Law Dictionary, Tenth Edition.
[911] [1985] 1 NWLR, part 1 at 17.
[912] Africa Newspaper v Federal Republic of Nigeria [1985] NWLR, part 6, 137; Akintola v Adegbenro [1963] 3 All ER 544.

represents acts that are not only illegal, but forbidden, immoral, improper, against rules or custom. There appears to be no ambiguity here.

Concluding, in line with the broader analysis of the Mbeki Report, IFFs must be defined as financial flows that contravene established rules and norms, including avoiding legal obligations to pay tax. This should be the African position.

4.2. Leveraging International Efforts at Addressing Illicit Financial Flows

As mentioned above, the fight against IFFs has garnered efforts at the national, continental and global levels. The fight against IFFs in Nigeria is led by the country's president.[913] In an October 2018 report published on the website of the United Nations Commission for Africa (UNECA), the President was quoted saying that, "fighting corruption and illicit financial flows (IFFs) in Nigeria is non-negotiable".[914] This statement was made in an address to former President of the Republic of South Africa and Chair of the AU/ECA High-Level Panel on Illicit Financial Flows from Africa, who visited President Buhari of Nigeria, along with his team.

Practical steps taken by the government to address IFFs include signing of bilateral agreements with the governments of the United States, United Kingdom, United Arab Emirates and Switzerland for the return of stolen assets hidden in those countries.[915] The country introduced a whistle blower policy to incentivize people to expose stolen funds hidden in Nigeria and abroad. Improved inter-agency relationship has led to recovery of funds for the government. For instance, the

[913] As at the time of writing: 2015—2019. Important to note that the African Union declared 2018 as the African year of combatting corruption, under the theme, "Winning the Fight Against Corruption: A Sustainable Path to Africa's Transformation" online: <http://aga-platform.org/node/152>

[914] UNECA, "Fighting Corruption and Illicit Financial Flows (IFFs) in Nigeria is non-negotiable-President Buhari", online: <https://www.uneca.org/stories/%E2%80%9Cfighting-corruption-and-illicit-financial-flows-iffs-nigeria-non-negotiable%E2%80%9D-president>

[915] Ibrahim Magu, "Combatting Corruption and Illicit Financial Flows in Nigeria" (November 2018) Leadership Newspaper, online: <https://leadership.ng/2018/11/20/combatting-corruption-and-illicit-financial-flows-in-nigeria/>.

Economic and Financial Crimes Commission (EFCC) established a dedicated special tax investigation team to work with the FIRS and the Revenue Mobilisation and Fiscal Commission in identifying and prosecuting tax evaders. It is reported that the joint efforts have led to the recovery of N27,712,334,455.64 between January and December 2017.[916]

Other initiatives of the government to address IFFs include: the introduction of the Voluntary Assets and Income Declaration Scheme,[917] the Bank Verification Number;[918] passing the law granting independence to the National Financial Intelligence Unit,[919]. In the tax space, the government of Nigeria signed the Multi-lateral Convention to Implement Treaty-Related Measures to Prevent Base Erosion and Profit Shifting, and the Common Reporting Standard Multilateral Competent Authority Agreement.

These actions and instruments of the government of Nigeria are described as efforts to tackle the IFFs out of the country. As such, an expansive definition of IFFs, which includes tax avoidance will automatically receive the attention of the government and demand actions from the relevant government agencies responsible for addressing base erosion and profit shifting.

At the continental level, the AU leads efforts to tackle IFFs. In 2011, the African Union Commission, jointly with UNECA, held jointly a Conference of African Ministers of Finance, Planning and Economic Development. The Conference, at the end of its deliberations, mandated the establishment of the High-Level Panel on Illicit Financial Flows from Africa (HLP on IFFS).[920] In 2015, the HLP on IFFS

---

[916] Ibid.

[917] A form of amnesty programme for tax defaulters.

[918] Unique bank identity number to each account holder in Nigeria, which traces the inflow and outflow of funds out of their accounts.

[919] The agency responsible for tacking money laundering activities and related crimes.

[920] TRALAC, "Report of the High Level Panel on illicit Financial Flows" (2015) online report: <https://www.tralac.org/news/article/6951-report-of-the-high-level-panel-on-illicit-financial-flows-from-africa.html>.

published its report on IFFs.[921] The report is the foremost account on IFFs out of Africa and recommends ways of addressing the menace. One encouraging attribute of the report is its inclusion of tax avoidance within the scope of the IFFs.

Other continental efforts at addressing IFFs are found in the activities of: civil societies, such as Tax Justice Network Africa who champion calls for governments and supranational bodies to address IFFs; other international organisations such as the ATAF, who through their tools, manual, guidelines, model conventions, policies and recommendations, set out to address IFFs; and academics and technical experts, whose writings contribute to the discussion on IFFs. It is noteworthy that a good number of civil societies on the continent, academics and technical experts support the inclusion of tax avoidance within the scope of IFFs.

Finally, at the global level, there is increased attention paid to IFFs and ways of tackling them, by developed countries and supranational bodies. The OECD is committed to addressing IFFs as evident in its reports and activities. In 2018, it published a report on the economy of illicit trade in West Africa.[922] The report makes a case for a comprehensive view of the linkages between development, governance and the negative externalities of globalization. In a similar sense, where the definition of IFFs is given an expansive definition incorporating tax avoidance, it is arguable that the BEPS Project is a global effort of the OECD and its partners to address IFFs. Other regional institutions such as the European Union have in place, programmes or policies to address illicit financial flows.[923]

---

[921] United Nations Economic Commission for Africa, "Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa" (2015), online: <https://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf>

[922] OECD (2018), Illicit Financial Flows: The Economy of Illicit Trade in West Africa, OECD Publishing, online: <https://read.oecd-ilibrary.org/development/illicit-financial-flows_9789264268418-en#page3>

[923] Luckystar Miyandazi & Martin Ronceray, "Understanding Illicit Financial Flows and Efforts to Combat them in Europe and Africa" (2008) ECDPM Discussion Paper, No 227, online: <https://ecdpm.org/wp-content/uploads/DP-227-Understanding-illicit-financial-flows-efforts-combat-Europe-Africa-June-2018-1.pdf>. European Parliament, "Corruption and Human Rights in Third Countries: European Parliament Resolution of 13 September 2017 on Corruption and Human Rights in Third Countries)2017/2028(INI))" (2017), European Parliament: Brussels, online: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+TA+P8-TA-2017-0346+0+DOC+PDF+V0//EN>; Aitor Perez & Iliana Olivie, "Europe Beyond Aid: Illicit Financial Flows. Policy Responses in Europe and Implications for Developing Countries" (2015)

In conclusion, at present, the world is committed to addressing and stemming the threat of IFFs. While countries and regional bodies are able to unilaterally and collectively with others, engage in reforms that seek to arrest the prevalence of tax avoidance practices, bringing tax avoidance under the framework of IFFs is a more effective approach at addressing these tax avoidance activities especially transfer mispricing, which shifts profit out of countries. Including tax avoidance in the IFFs framework is logical, legal, right and acceptable to most, especially on the African continent.

Conclusion

In this chapter, I have attempted to reveal and review the legal process required to attain the adoption of the unitary approach by Nigeria in its domestic laws and interactions with other countries, through bilateral or multilateral agreements. Beyond the legal processes, a strong political will is needed to achieve the adoption of the unitary approach. A way to achieve the political support needed is to include tax avoidance practices of multinational entities in the IFFs. A first step towards achieving this is to adopt an expansive definition of IFFs to include tax avoidance, especially through transfer mispricing. I have provided justification for such a claim in the chapter.

CGD Background Paper, online: <http://www.cgdev.org/sites/default/files/Europe-Beyond-Aid-Illicit-Financial-Flows-background-paper.pdf>.

Chapter 6: Conclusion

The enablers of transfer mispricing are two century-old principles which influence the allocation of income between related entities when they transact with each other. These principles are the separate entity principle and the arm's length principle. They are contained in article 9 of most model tax conventions, which influence the global tax system. As such, they are enshrined in bilateral tax treaties and national laws of states.

The separate entity principle treats members of an MNE group as independent from each other though it recognises that relationships exist between them and the potential for conditions to be imposed or made between them which would not be made between independent entities. The arm's length principle proceeds to demand from these related entities that they act as independent entities would in their dealings with each other, fixing prices independent entities would. To achieve the arm's length standards, a set of transfer pricing methods contained in the TPGs have been introduced by the OECD and adopted by other supranational bodies and tax jurisdictions.

The limitations of these principles have been extensively discussed in chapter 2 of the thesis. They are that, conceptually, the principles suffer from fundamental flaws. Procedurally, they are difficult to apply and are impractical and inadequate. The belief that related entities of an MNE group can act as independent entities is deceptive. As I have argued, using Hymer's theory of FDI and MNE, MNEs are established for the purpose of internalizing market, centralizing ownership and control and reducing transaction costs. Furthermore, the common law treatment of companies as separate and independent from their shareholders, applicable to MNE groups, is impeachable on the ground of single enterprise. The theory of single enterprise, observed in recent judicial decisions, supposes that a parent company and its subsidiaries should be treated as a single firm.

The arm's length principle focuses on the pricing of transactions, contrary to the power to adjust profits, stipulated in article 9 of the OECD MTC and other model conventions. The TPGs require an individual facts and circumstances examination of individual taxpayers and adjustment of prices of transactions between related entities by comparing with transactions independent entities negotiate. The individual facts and circumstances analysis demands expert knowledge of the industry of the taxpayer. It is resource-demanding for countries, especially for African countries. it is complex to implement and highly technical for the average tax authority staffer. Thus, there is a mismatch in capacities of taxpayers and tax authorities.

The comparability analysis relies on the presence of comparables and accessible database where the comparables are housed. The available databases are expensive and unaffordable for African governments. In addition, there are no African-generated databases making data obtained from the foreign databases mostly inapplicable to African countries. Furthermore, due to the integrated nature of MNEs as discussed in this thesis, comparables are hard to come by.

The cumulative outcome of the limitations of the separate entity principle and the arm's length principle is the creation of a global tax system that is uncertain, unpredictable and leads to conflict between taxpayers and tax authorities. A system that is vulnerable to manipulation and corporate capture by MNEs. In addition, a system that allows MNEs to erode the tax bases of tax jurisdictions and shift profits out of jurisdictions where economic activities occur and income is accrued, to low or no tax jurisdictions. The greater effect of this global tax system is the unjust allocation of income system it has created. The system fails to achieve inter-nation equity and inter-taxpayer equity. It is discriminatory towards independent business owners and shifts the tax burden to individuals, in most cases being regressive. The greatest effect of the global tax system is the depletion of limited revenue needed by African countries to meet the SDGs.

Responses to the inadequate global tax system have arisen in reforms of the application of the two principles. With support and backing from the governments and supranational bodies, these reforms take place under the OECD BEPS Project— a set of 15 action plans believed to have the cumulative effect of ensuring that profits are taxed where the economic activities occur, and value is created. However, these reforms are patchy and partial. For instance, the CFC rules allow countries to tax deemed income in the hands of resident taxpayers though undistributed by the offshore subsidiaries, effectively piercing the corporate veil. However, the reforms refuse to treat entities in an MNE group as single firms for the purpose of taxation. The recent Guidance on TPSM recognises the use of formula to allocate residual profits but insists on comparability analysis and denies the use of pre-determined formula, insisting on individual facts and circumstances analysis.

Responses have come in the observation of alternatives to transfer pricing adopted by tax jurisdictions. These alternatives discussed in this thesis are Safe Harbours, Fixed Margin System, Sixth Method, Use of Secret Comparables and Advance Pricing Agreements. Radical departures have been observed. Durst's ACMT calls for the abandonment of taxation of profits to taxing companies on their turnover. The pros and cons of this suggested approach are discussed in chapter 3 of the thesis.

Notwithstanding the patchy reform efforts of the OECD and the alternatives to the transfer pricing practice which fail at their foundation and are at best short-term measures, there is growing consensus that an overhaul of the global tax system is needed. The OECD seems to have finally come to terms with this. In its Policy Note on the Digitalization of the Economy, it avers that solutions outside the arm's length principle may have to be adopted for the allocation of income. As observed in the literature, radical alternatives are being put forward by experts. This thesis has made a case for the adoption of the unitary approach.

The unitary approach is not fool-proof. Its adoption and implementation in Africa will be difficult to sell and practice. No prior study has taken place on its application to African countries. No empirical evidence of the revenue gains has been carried out. However, from a conceptual analysis of its attributes, it represents the best alternative in the long term for African countries.

The unitary approach corrects the two flaws of the current tax system: the separate entity treatment of related entities in an MNE group and the arm's length principle. First, it treats related entities in an MNE group as a single firm for tax purpose. This approach recognises the true intent of MNEs and their business model. Second, it focuses on the apportionment and adjustment of profits of companies, contrary to the adjustment of prices as practised under the current global tax system. This focus on profit is a true interpretation of article 9 of model tax treaties.

To avert ambiguity, I suggested a new article 9(1) in chapter 5 of the thesis. This new article 9(1) apportions the global profits of an MNE group among tax jurisdictions where the related entities are tax liable, on the basis of the economic activities in their jurisdictions and the contribution of the related entities to the global profit. The global profit is apportioned using pre-determined factors and formula. I have adopted the Massachusetts formula, which splits the global profit among the factors of asset, labour and sales. My conviction is that this formula will lead to significant increase in tax revenue for African countries while curtailing base erosion and profit shifting. The legal and political hurdles to jump to achieve the shift to the unitary approach are surmountable as argued in chapter 5 of the thesis.

This thesis does not claim to have provided all the answers needed, nor does it claim to have found the fool-proof solution to the allocation of income. What I have set out to achieve in this dissertation is to contribute to ongoing discussion on the reform of the global tax system with new insights and perspectives. I have provided a voice often neglected in the global discourse— the African voice. This has been a doctrinal research, meaning that no empirical work has been undertaken to verify the claims made here, especially, the contribution of the unitary approach to revenue increase and curtailing IFFs. This limitation of the dissertation presents opportunities for future and studies. What this thesis offers is the theoretical support for such future empirical work.

Finally, any alternative to the current global tax system will present difficulties in acceptance and implementation. What is relevant is that countries push the alternative that best suit their economies and development stages. The discussion on the next global tax system must be inclusive and expansive. African countries must be involved in the discussions at the global level and at home here on the continent. This thesis presents a narrative, peculiar to Africa. It presents an alternative to the existing tax system, which African countries can unilaterally and collectively support.

Appendix I (a)

DATA REQUEST ON TRANSFER PRICING FROM NIGERIA

ALEXANDER EZENAGU

+1514-623-2125; alexander.ezenagu@mail.mcgill.ca

January 15, 2018.

The Executive Chairman,
Federal Inland Revenue Service,
20, Sokode Crescent.
Revenue House, Wuse Zone 5,
Abuja, Nigeria.

Attention: Deputy Director,
Research and Development Unit,
FIRS.

Dear Executive Chairman,

REQUEST FOR DATA ON TRANSFER PRICING AUDIT OUTCOMES

I am Alexander Ezenagu, a PhD Candidate at McGill University, Canada. I am also an international tax researcher with the International Centre for Tax and Development (ICTD). My doctoral research seeks to understand the correlation between the contemporary international tax system (separate entity and arm's length standard treatment of multinational entities) and tax avoidance.

To this end, I am seeking to obtain and use data on transfer pricing outcomes from the Federal Inland Revenue Service (FIRS). This data ordinarily should show the following: audit period; audit start date; initial tax returns of the multinational entity in terms of value; the period and reason for investigation; the progress to a full audit of the multinational entity; amount subsequently collected; reason for the new amount; and general remarks. The information may be limited to five (5) multinational entities and from the period 2010-2015. The findings from my research will help answer the lingering question of the suitability of the existing income allocation approach currently practised. For the FIRS, it presents relevant knowledge, analysis and options for policy formulation.

This information shall be anonymised, respecting privacy of taxpayers. Summaries of the audit process will suffice. I commit to the confidentiality of details and will only use this information for analytical purposes in the research I am conducting. Issues of tax avoidance are of great importance to African countries and I hope to contribute to the body of knowledge on addressing tax avoidance on the continent through my research. Your support would go a long way in achieving this.

I look forward to your favourable response.

Yours faithfully,

Alexander Ezenagu

Appendix I (b)

DATA REQUEST ON TRANSFER PRICING FROM UGANDA

Request for Data
on Transfer Pricing A

Appendix I (c)

TRANSFER PRICING DATA REQUEST TEMPLATE

TRANSFER PRICING AUDIT REQUEST TEMPLATE

S/N	INDUSTRY	AUDIT PERIOD	MULTINATIONAL COMPANY? YES/NO?	INITIAL RETURNS				AUDIT START DATE	VALUE AT STAKE/ASSESSED RETURNS BY FIR				AUDIT END DATE	AMOUNT ULTIMATELY COLLECTED BY FIRS				LITIGATION DETAILS (IF ANY)	REMARK
		FY		(₦)	($)	(£)	(€)		(₦)	($)	(£)	(€)		(₦)	($)	(£)	(€)		
1																			
2																			
3																			
4																			
5																			
6																			
7																			
8																			
9																			

Appendix II (a)

FEDERAL INLAND REVENUE SERVICE TRANSFER PRICING DATA

TP Audit Request
for Alex 12.03.18 cop

Appendix II (b)

UGANDA REVENUE AUTHORITY TRANSFER PRICING DATA

Copy of Copy of
TRANSFER PRICING /

Bibliography

Articles

ActionAid, ''Calling Time: Why SABMiller Should Stop Dodging Taxes in Africa'' (2010; updated 2012) ActionAid UK.

Rosanne Altshuler & Harry Grubert, ''The Three Parties in the Race to the Bottom: Host Governments, Home Governments and Multinational Companies'' (2005) CESifo, Working Paper No 1613.

Mohammed Amin Almfraji & Mahmoud Khalid Almsafir, ''Foreign Direct Investment and Economic Growth Literature Review from 1994 to 2012'' (2014) Procedia – Social and Behavioral Sciences. 129: 206-213.

Brian Arnold, ''The Role of a General Anti-Avoidance Rule in Protecting the Tax Base of Developing Countries'' in A Trepelkov, H Tonino & D Halka, eds., ''United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries'' 2nd ed, (2017) New York: United Nations.

Hugh Ault & Brian Arnold, ''Protecting the Tax Base of Developing Countries: An Overview'' in A Trepelkov, H Tonino & D Halka, eds., United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries 2nd ed, (2017) New York: United Nations.

Reuven Avi-Yonah, ''The Rise and Fall of Arm's Length: A Study in the Evolution of US International Taxation'' (2007) Law and Economics Working Paper, University of Michigan Law School.

Reuven Avi-Yonah, ''Corporations, Society and the State: A Defence of the Corporate Tax" (2004) University of Virginia Law Review 90(5): 1193-255.

Reuven Avi-Yonah, "Between Formulary Apportionment and the OECD Guidelines: A Proposal for Reconciliation" (2009) Law & Economics Working Papers Archive: 2003-2009 Paper 102

Reuven Avi-Yonah, ''Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State" (2000) Harvard Law Review 113(7): 1573-676.

Reuven Avi-Yonah, "The Three Goals of Taxation" (2006) Tax Law Review 60, 1-28.

Reuven Avi-Yonah & Kimberly Clausing, "Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment" (2007) The Brookings Institution.

Reuven Avi-Yonah, Kimberly Clausing, & Michael C Durst, ''Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split" (2008) Public Law and Legal Theory Working Paper No 138, University of Michigan Law School.

Reuven Avi-Yonah, & Pouga Tinhaga, Z, ''Unitary Taxation and International Tax Rules" (2014) ICTD Working Paper 26, Brighton, UK: Institute of Development Studies.

Eduador Baistrocchi, ''The Transfer Pricing Problem: A Global Proposal for Simplification" (2006) Tax Lawyer 59: 941-979.

Eduador Baistrocchi & Ian Roxan, eds. ''Transfer Pricing Disputes in India" in ''Resolving Transfer Pricing Disputes" (2012) Cambridge: Cambridge University Press: 584-633.

Edward Barlow & Ira Wender, ''Foreign Investment and Taxation'' (1955) Cambridge MA: Harvard Law School International Program in Taxation.

Peter Barnes, ''Limiting Interest Deductions'' in A Trepelkov, H Tonino & D. Halka, eds., United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries 2nd ed, (2017) New York: United Nations.

Sebastian Beer & Jan Loeprick, ''The Costs and Benefits of Tax Treaties with Investment Hubs – Findings from Sub-Saharan Africa'' (2018) Working Paper, World Bank Group Governance Practice.

Timothy Besley & Torsten Persson ''Why Do Developing Countries Tax So Little'' (2014) Journal of Economic Perspectives 28(4): 99-120.

Richard Bird, ''Tax and Development: What Have We Learned from Fifty Years of Research'' (2012) ICTD Working Paper No. 1, Brighton: Institute of Development Studies

Ken Blanchard, ''How Not to Engage with CFC Rules'' (2015) Bloomberg BNA International Tax Monitor.

James Boyce & Leonce Ndikumana, "Capital Flight From sub-Saharan African Countries: Updated Estimates, 1970 – 2010" (2012) PERI Research Report.

Yariv Brauner ''Treaties in the Aftermath of BEPS'' (2016) Brooklyn Journal of International Law 41(3): 973-1041.

Margaret Burow, ''Lux Rulings Reveal 'Industrial Scale' Tax Avoidance''(2014a) Tax Notes International.

Isabel Calich & Joao Rolim, 'Transfer Pricing Disputes in Brazil in E Baistrocchi & I Roxan, eds., "Resolving Transfer Pricing Disputes" (2012) Cambridge: Cambridge University Press: 519-554.

Carroll Report, "League of Nations Document No. C. 425. M. 217(b). IIA. (1933).

Mitchell Carroll "Allocation of Business Income: The Draft Convention of the League of Nations" (1934) Columbia Law Review 34: 473-498.

Mitchell Carroll, "Prevention of international Double Taxation and Tax Evasion: Two Decades of Progress Under the League of Nations." Geneva, League of Nations.

Mitchell Carroll, "Income Tax Conventions as an Aid to International Trade and Investment" (1962) Section of International and Comparative Law Bulletin, 6(3), 16-30.

Mitchell Carroll, "Taxation of Foreign and National Enterprises, Volume IV—Methods of Allocating Taxable Income."

Eric Chaffee & Karie Davis-Nozemack "Corporate Tax Avoidance and Honoring the Fiduciary Duties Owed to the Corporation and Its Stockholders" (2017) Boston College Law Review 58(5): 1425-1481.

Alex Cobham & Petr Jansky "Global distribution of revenue loss from tax avoidance: Re-estimation and country results" (2017) WIDER Working Paper 2017/55, Helsinki: UNU-WIDER.

Alex Cobham & Simon Loretz, "International Distribution of the Corporate Tax Base: Implications of Different Apportionment Factors under Unitary Taxation" (2014) ICTD Working Paper 27.

Richard Collier & Joseph Andrus ''Transfer Pricing and the Arm's Length Principle after BEPS" (2017) Oxford: Oxford University Press.

Ernesto Crivelli, Ruud A. de Mooij & Michael Keen, ''Base Erosion, Profit Shifting and Developing Countries" (2015) IMF Working Paper 15/118, International Monetary Fund.

Tsilly Dagan, ''International Tax Policy: Beyond Competition and Cooperation" (2018) Cambridge Tax Law Series, Cambridge University Press.

Derek Devgun, "Worldwide Combined Reporting in the United States after Barclays" (1995) The Modern Law Review, Vol. 58, Issue 2.

Ruud A. de Mooij, & Li Liu, ''At a Cost: The Real Effects of Transfer Pricing Regulations" (2018) Working Paper 18/69, Washington DC: IMF.

Michael Durst, ''Improving Natural Resource Taxation in Developing Countries"(2017b) Tax Notes International.

Michael Durst, "Beyond BEPS: A Tax Policy Agenda for Developing Countries" (2014) ICTD Working Paper 18.

Michael Durst, ''Self-Help & Altruism: Protecting Developing Countries' Tax Revenues" in T. Pogge and K. Mehta, eds., ''Global Tax Fairness", (2016b) Oxford and NY: Oxford University Press.

Michael Durst, ''Limitations of the BEPs Reforms: Looking Beyond Corporate Taxation for Revenue Gains" (2015) ICTD Working Paper No. 40, Brighton: Institute of Development Studies.

Michael Durst, ''The Tax Policy Outlook for Developing Countries: Reflections on International Formulary Apportionment" (2015b) ICTD Working Paper 32, Brighton: International Centre for Tax and Development.

Michael Durst, ''Analysis of a Formulary System, Part VIII: Suggested Statutory, Regulatory Language for Implementing Formulary Apportionment" (2014a) Bloomberg BNA Tax Management Transfer Pricing Report 23: 70.

Michael Durst, ''Analysis of a Formulary System, Part VII: The Sales Factor" (2014b) Bloomberg BNA Tax Management Transfer Pricing Report 22(22): 1414.

Michael Durst, ''Analysis of a Formulary System, Part VI: Building the Formula" (2014c) Bloomberg BNA Tax Management Transfer Pricing Report 22(18): 1180.

Michael Durst, ''Analysis of a Formulary System, Part V: Apportionment Using a Combined Tax Base" (2013a) Bloomberg BNA Tax Management Transfer Pricing Report 22(15): 972.

Michael Durst, ''Analysis of a Formulary System, Part IV: Choosing a Tax Base" (2013b) Bloomberg BNA Tax Management Transfer Pricing Report 22(12): 771-775.

Michael Durst, ''Analysis of a Formulary System for Dividing Income, Part III: Comparative Assessment of Formulary, Arm's Length Regimes" (2013c) Bloomberg BNA Tax Management Transfer Pricing Report 22: 653.

Michael Durst, ''Analysis of a Formulary System for Dividing Income, Part II: Examining Current Formulary and Arm's Length Approaches" (2013d) Bloomberg BNA Tax Management Transfer Pricing Report 22(5): 270.

Michael Durst, ''Starting the Conversation: A Formulary System for Dividing Income Among Taxing Jurisdictions" (2013e) Bloomberg BNA Tax Management Transfer Pricing Report, 22(2): 98.

Michael Durst, ''Pragmatic Transfer Pricing for Developing Countries" (2012) Tax Notes International.

Michael Durst, ''Making Transfer Pricing Work for Developing Countries" (2010) Tax Notes International.

Michael Durst & Robert Culbertson, ''Clearing Away the Sand: Retrospective Methods and Prospective Documentation in Transfer Pricing Today" (2003) Tax Law Review 57: 37-84.

Wolfgang Eggert & Andreas Haufler, "Fiscal Policy in Action- Coordination cum Tax Rate Competition in the European Union" (2006) FinanzArchiv/Public Finance Analysis, 62(4), 579-601.

James Eustice, ''Tax Problems Arising from Transactions Between Affiliated or Controlled Corporations" (1968) Tax Law Review 23: 451.

Maya Forstater, ''Can Stopping 'Tax Dodging' by Multinational Enterprises Close the Gap in Development Finance?" (2015) Center for Global Development.

Clemens Fuest & Nadine Riedel, ''Tax evasion, tax avoidance and tax expenditures in developing countries: A review of the literature" (2009) Oxford University Centre for Business Taxation.

Gary Gereffi, "The Global Economy: Organization, Governance, and Development" (2005) The Handbook of Economic Sociology 2, 160-182.

Martin Hearson, ”Tax Treaties in Sub-Saharan Africa A Critical Review, Technical Report” (2015) Tax Justice Network – Africa.

Eli Heckscher, ‘The effect of foreign trade on the distribution of income” in H. Ellis and L.A. (1919).

Walter Hellerstein, “Designing the Limits of Formulary Income Attribution Regimes: Lessons from the US States and the Proposed EU CCCTB” (2014) State Tax Notes 72: 45.

IMF, ‘‘Spillovers in International Corporate Taxation” (2014) IMF Policy Paper, International Monetary Fund

IMF, ‘’Revenue Mobilization in Developing Countries” (2011) Fiscal Affairs Department, International Monetary Fund

IMF, OECD, UN and World Bank, ‘’Options for Low Income Countries’ Effective and Efficient Use of Tax Incentives for Investment” Report to the G-20 Development Working Group, (2005), Washington: International Monetary Fund

Tracy Kaye & Michael Mahoney, “Various Approaches to Sourcing Multijurisdictional Values: Sourcing Options Available to Tax Policy Makers” (2009) St. & Loc. Tax Law Symp. Ed. 2013.

Michael Keen & Peter Mullins, ‘’International Corporate Taxation and the Extractive Industries” in P Daniel et al., eds., ‘’International Taxation and the Extractive Industries” (2017) Routledge.

Edward Kleinbard. ‘’Stateless Income” (2011a) Florida Tax Review 11(9): 699- 774.

KPMG India, ''CBDT notifies the much-awaited revised Safe Harbour Rules'' (2017) KPMG Tax Flash News.

Stanley Langbein, ''The Unitary Method and the Myth of Arm's Length'' (1986) Tax Notes 30:625-681.

Michael Lennard, 'The UN Model Tax Convention as Compared with the OECD Model Tax Convention – Current Points of Difference and Recent Developments'' (2009) International Bureau of Fiscal Documentation Asia-Pacific Tax Bulletin.

Patricia Lewis, ''Where Have All the Safe Harbors Gone? A Plea for Reinvigoration'' (2017) Bloomberg BNA Transfer Pricing Report.

Celestin Lindsay, "The Formulary Approach to the Taxation of Transnational Corporations: A Realistic Alternative?" (2000) Dissertation, University of Sydney: Sydney.

Jonathan Macey & Joshua Mitts, ''Finding Order in the Morass: The Three Real Justifications for Piercing the Corporate Veil''. (2014) Cornell Law Review 100(1): 99-155.

Thierry Madies & Jean-Jacques Dethier, ''Fiscal Competition in Developing Countries: A Survey of the Theoretical and Empirical Literature'' (2012) Journal of International Commerce, Economics and Policy 3(2).

John Matheson, 'The Modern Law of Corporate Groups: An Empirical Study of Piercing the Corporate Veil in the Parent-Subsidiary Context'' (2009) North Carolina Law Review 87: 1091-1155.

Thornton Matheson & Patrick Petit, ''Taxing Telecommunications in Developing Countries'' (2017) IMF Working Paper No17/247, International Monetary Fund.

Michael McIntyre, "Developing Countries and International Cooperation on Income Tax Matters" (2005) An Historical Review.

Jack Mintz, "Globalisation of the Corporate Income Tax: The Role of Allocation" (1999) FinanzArchiv/Public Finance Analysis 56, no. ¾, 389-423.

Jeremy Moon, Andrew Crane & Dirk Matten, 'Can Corporations Be Citizens? Corporate Citizenship as a Metaphor for Business Participation in Society" (2005) Business Ethics Quarterly 15(3): 427-453.

Mick Moore & Wilson Prichard, "How Can Governments of Low-Income Countries Collect More Tax Revenues" (2017) ICTD Working Paper No. 70, Brighton: Institute of Development Studies.

Theodore Moran, Edward Graham, & Magnus Blomström "Does Foreign Direct Investment Promote Development?" (2005) Peterson Institute for International Economics, Center for Global Development.

Richard Murphy, "Country-by-Country Reporting. Accounting for globalization locally" (2012) Tax Justice Network.

Peggy Musgrave, "International Tax Base Division and the Multinational Corporation," (1972) 27 Public Finance 39.

Peggy Musgrave, "Inter-jurisdictional Equity in Company Taxation: Principles and Applications to the European Union" in Cnossen, at 46-78.

Alexander Readhead, "Toolkit for Transfer Pricing Risk Assessment in the African Mining Industry, Bonn: GIZ, (2017a). online: <www.bmz.de/rue/includes/downloads/2017_GIZ_Transfer_Pricing_Risk_Tool_EN.pdf >

Alex Readhead, ''What Mining Can Learn from Oil – A Study of Special Transfer Pricing Practices in the Oil Sector, and their Potential Application to Hard Rock Minerals" (2018) Center for Global Development Policy Paper 128.

Kimberley Reeder, Sarah McGahan, & Jon Sedon, "The Unitary Group's Identity Crisis: Is There Really an "I" in Unitary? (2008) The State and Local Tax Lawyer, Symposium Edition, 83-114.

Thomas Rixen, ''From double tax avoidance to tax competition: Explaining the institutional trajectory of international tax governance" (2010) Review of International Political Economy 18(2): 197-227.

Julie Roin, "Competition and Evasion: Another Perspective on International Tax Competition" (2000) Georgetown Law Journal 89: 543-604.

Julie Roin, "Can the Income Tax be Saved? The Promise and Pitfalls of Adopting Worldwide Formulary Apportionment'" (2008) Tax Law Review, Volume 61, No. 3, 169.

Marco Runkel & Guttorm Schjelderup, "The Choice of Appointment Factors under Formula Apportionment" (2011) International Economic Review 52, 913-934.

Kerrie Sadiq, "Unitary Taxation of the Finance Sector" (2014) ICTD Working Paper 25.

Prem Sikka & Richard Murphy, "Unitary Taxation and the Role of Accounting" (2015) ICTD Working Paper 34.

Eriks Siu, et al., "Unitary Taxation in the Extractive Industry Sector" (2015) ICTD Working Paper 35.

Andrew Snyder, "Taxation of Global Trading Operations: Use of Advance Pricing Agreements and Profit-Split Methodology" (1995) Tax Lawyer Bd. 48, S. 1057.

Sol Picciotto, "Illicit Financial Flows and the Tax Haven and Offshore Secrecy System" (2018a) Tax Justice Network. www.taxjustice.net/2018/02/08/illicit-financial-flows-tax-haven-offshore-secrecy-system/

Sol Picciotto, "International Tax, Regulatory Arbitrage and the Growth of Transnational Corporations, (2018b) Transnational Corporations Volume 25(2).

Sol Picciotto, "Taxing Multinational Enterprises as Unitary Firms" (2017) Brighton, UK: Institute of Development Studies.

Sol Picciotto, "Is the International Tax System Fit for Purpose, Especially for Developing Countries?" (2013) ICTD Working Paper 13, Brighton, UK: Institute of Development Studies.

Jefferson VanderWolk "A Look Ahead: A Multinational Prescription for Global Tax Policy" (2018) Tax Notes.

Klaus Vogel, "Worldwide vs. Source Taxation of Income-A Review and Re-evaluation of Arguments" (Part I) [1988/8-9] Intertax 216, at 218-19. (Part II [1988/10] Intertax 310, Part III [1988/11] Intertax 393.).

Attiya Waris, "How Kenya has Implemented and Adjusted to the Changes in International Transfer Pricing Regulations: 1920-2016" (2017) ICTD Working Paper 69, Brighton, UK: Institute of Development Studies.

Bret Wells & Cym Lowell, "Income Tax Treaty Policy in the 21st Century: Residence vs. Source" 5 Colum. J. Tx. L. 1.

Jens Wittendorff, "Transfer Pricing and the Arm's Length Principle in International Tax Law" in the Netherlands: Alphen aan den Rijn; Wolters Kluwer Law & Business.

Books

Daron Acemoglu & James A Robinson, Why Nations Fail: The Origins of Power, Prosperity, and Poverty (New York: Crown, 2012). Print.

Charlet Alain, Silberztein Caroline and Pointe Gerard, Transfer Pricing: Study on the Feasibility of Introducing Safe Harbour Provisions in ECOWAS Countries (European Commission, 2017). Online: <https://ec.europa.eu/europeaid/transfer-pricing-study-feasibility-introducing-safe-harbour-provisions-ecowas-countries_en>

Reuven Avi-Yonah, Advanced Introduction to International Tax Law (Cheltenham: Edward Elgar Publishing Limited, 2015). Print.

Peter Buckley, and Mark Casson, The Future of the Multinational Enterprise (London: Macmillan,1976) at 32-65. Print.

Mark Casson, Multinational Corporations, Aldershot, UK and Brookfield (USA: Edward Elgar, 1990) at 6–31. Print.

RE Caves, Multinational Enterprise and Economic Analysis (Cambridge: Cambridge University Press,1982). Print.

Evans Chris, Containing Tax Avoidance in JG Head and KRE Alphen aan den Rijn, eds., Tax reform in the 21st century (The Netherlands: Kluwer Law International,2009). Print.

Robert B Cohen et al., The Multinational Corporations: A Radical Approach. Papers by Stephen Herbert Hymer, (Cambridge: Cambridge University Press,1979). at 41–53. Print.

Peter Dietsch, Catching Capital: The Ethics of Tax Competition (Oxford: Oxford University Press, 2015). Print.

Marie-Laure Djelic and Kerstin Sahlin-Anderson, Introduction: A World of Governance: The Rise of Transnational Regulation, Transnational Governance: Institutional Dynamics of Regulation, (Cambridge: Cambridge Univ. Press, 2008) at 1-28. Print.

John Dunning, Multinational Enterprises and the Global Economy (Wokingham: Addison Wesley,1993a). Print.

John Dunning, The Globalization of Business (London: Routledge,1993b). Print.

John Dunning, Trade, Location of Economic Activity and the MNE: A Search for an Eclectic Approach in Ohlin B, Hesselborn, PO and Wijkman, PM, eds., The International Allocation of Economic Activity (London: Macmillan,1977) at 395-431. Print.

John Dunning and R Narula, The investment development path revisited: some emerging issues in JH Dunning and R. Narula, eds., Foreign Direct Investment and Governments, Catalysts for Economic Restructuring, (London: Routledge,1996). Print.

Ronald Dworkin, Taking Rights Seriously (Cambridge, Mass: Harvard University Press, 1977). Print.

Lorraine Eden, Taxes, Transfer Pricing, and the Multinational Enterprise in AM Rugman and TL Brewer, eds., The Oxford Handbook of International Business, (Oxford: Oxford University Press, 2001) at. 591-619. Print.

Mats Forsgren , Ulf Holm and Jan Johanson, Managing the Embedded Multinational. A Business Network View (Cheltenham, UK and Northampton, US: Edward Elgar,2005). Print.

Gary Gereffi, The Global Economy: Organization, Governance, and Development in NJ Smelser, & R Swedberg, eds., The Handbook of Economic Sociology (Princeton, NJ: Princeton University Press and Russell Sage Foundation,2005) at 160-182. Print.

Sumantra Ghoshal and Nitin Nohria, The differentiated MNC: Organizing Multinational Corporations for Value Creation (San Francisco, CA: Jossey-Bass,1997). Print.

Peter Harris, International Commercial Tax (Cambridge: Cambridge University Press, 2010). Print.

Peter Harris, Corporate/shareholder income taxation and allocating taxing rights between countries: a comparison of imputation systems (Amsterdam: IBFD Publications,1996). Print.

Peter Harris & Dominic de Cogan, Studies in the History of Tax Law, Volume 7 (Oxford: Hart Publishing, 2015). Print.

Wesley Newcomb Hohfield, Fundamental Legal Conceptions, 3rd reprint 1964 (New Haven: Yale University Press, 1919). Print.

Hugh Ault and David Bradley, US Taxation of International Income in A Razin and J Slemrod, eds., Taxation in the global economy, A National Bureau of Economic Research project report (Chicago: University of Chicago Press,1990). Print.

Stephen Hymer, The International Operations of National Firms: a Study of Direct Foreign Investment, (Cambridge, MA: MIT Press,1976). Print.

Stephen Hymer, Direct foreign investment and the national economic interest in P. Russell, eds., Nationalism in Canada, (Toronto: McGraw-Hill, 1966) at 191–202. Print.

Stephen Hymer, The multinational corporation and the law of uneven development in JW Bhagwati eds., Economics and World Order, (London: Macmillan,1971) at 113–40. Print.

Calestous Juma, Innovation and its Enemies: Why People Resist New Technologies (Oxford: Oxford University Press, 2016). Print.

Kim Brooks, Inter-Nation Equity in JG Head and KRE Alphen aan den Rijn, eds., Tax reform in the 21st century (The Netherlands: Kluwer Law International, 2009). Print.

Cooper Joel Lachian et al., Transfer Pricing and Developing Economies: A Handbook for Policy Makers and Practitioners, (Washington DC: World Bank, 2016).

Michael Lang, et al., Multilateral Tax Treaties; New Developments in International Tax Law (Kluwer: Law International, 1997). Print.

John McManus, The theory of the international firm in Gilles Paquet, eds., The Multinational Firm and the Nation State (Don Mills, Ontario: Collier-Macmillan, 1972) at 66–93. Print.

Richard Murphy, The Joy of Tax: How a Fair Tax System Can Create a Better Society (London: Bantam Press, 2015). Print

Giorgio Navaretti and Anthony Venables, Multinational Firms in the World Economy (Princeton and Oxford: Princeton University Press, 2004). Print.

Kees Wan Raad, Materials on International, TP & EU Tax Law (Leiden: International Tax Centre, 2016). Print.

Hugo Radice, International Firms and Modern Imperialism (Harmondsworth: Penguin,1975) at 113–35. Print.

Metzler Readings in the Theory of International Trade (London: Allen and Unwin,1950) at 272–300. Print.

John Rawls, A Theory of Justice (Cambridge, Mass: Belknap Press, 2005). Print.

Dworkin Ronald, Sovereign Virtue (Cambridge, Mass: Harvard University Press,2000). Print.

Malcolm Shaw, International Law, 6th ed (Cambridge: Cambridge University Press, 2008). Print.

Caney Simon, Justice beyond borders: a global political theory (Oxford: Oxford University Press, 2006). Print.

Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations (1776) in Edwin Cannan, eds., (Methuen & Co., 1925), at 310. Print.

Picciotto, Sol, International Business Taxation (London: Weidenfeld & Nicolson, 1992).

George Stigler and Kenneth E Boulding, Readings in Price Theory (London: Allen and Unwin,1953) at. 331–51. Print.

Alan White, "Rights", (1984), Oxford: The Claredon Press.

Cases

Adams v Cape Industries [1990] CH 433

Adeyemi v Lan & Baker (Nigeria) Ltd (2002) 7 NWLR (pt 663) 33.

African Barrick Gold Plc v Commissioner General, Tanzania Revenue Authority [2013] Tax Appeal No 16 of 2015.

African Continental Bank Plc v Emostrade Limited [2002] 8 NWLR pt 770 at 501.

Africa Newspaper v Federal Republic of Nigeria [1985] NWLR, pt 6.

Akintola v Adegbenro [1963] 3 All ER 544.

Albacruz (Cargo Owners) v Albazero 'The Albazero' [1977] AC 774.

Apthorpe v Peter Schoenhofen Brewery Co Ltd [1899] 80 LT 395

Aron Salomon (Pauper) Appellant; v A Salomon and Company Limited, Respondents [1897] AC 22.

Bolton (Engineering) Co Ltd v Graham [1957] 1 QB 159.

Bluecorp Pty Ltd (in liquidation) v ANZ Executors and Trustee Co Ltd [1995] QCA 487

Butler Bros v McColgan [1942] 315 US 501.

DHN Food Distributors Ltd v London Borough of Tower Hamlets [1976] 1 WLR 852

FDB Financial Services Ltd v Adesoza [2002] 8 NWLR (pt 668) 170

Harold Holdsworth& Co (Wakefield) Ltd v Caddies [1955] 1 WLR 352

Industrial Equity Ltd v Blackburn [1977] HCA 59

Inland Revenue Commissioners ("IRC") v Duke of Westminster (1935) All ER 259 (H.L).

Jones v Lipman [1962] 1 WLR 832.

Le v Lee's Air Farming Ltd [1961] AC 12.

Lennard's Carrying Co v Asiatic Petroleum Ltd [1915] AC 705.

Littlewoods Stores Ltd v IBC [1969] 1 WLR, 1241.

Mezu v CB (Nig) Limited [2013] 3 NWLR (pt 1340) 188.

Mobil Oil Corporation v Commissioner of Taxes of Vermont (1980) 445 US

Osafile & Anor v Odi & Anor [1985] 1 NWLR Pt 1, 17.

Prest v Petrodel Resources Ltd [2013] UKSC 34.

Qintex Australia Finance Ltd v Schroders Australia Ltd [1990] 3 ACSR 267.

State v Commissioner General of Malawi Revenue Authority, ex parte: Eastern Produce Malawi Ltd, [2018] MWHC 800. Online: <https://malawilii.org/mw/judgment/high-court-general-division/2018/800>

Underwood Typewriter Co v Chamberlain (1920) 254 US 113.

Unilever (Kenya) Ltd v The Commissioner of Income Tax, High Court of Kenya, [2005] eKLR, http://kenyalaw.org/caselaw/cases/view/12804

Viho Europe BV v Commissioner of the European Communities (1996) ECJ Case C-73/95

Vodafone International Holdings v Union of India & Anor [2012] 6 SCC 613

Woolfson v Strathclyde Regional Council [1978] UKHL 5

WT Ramsay Ltd v Inland Revenue Commissioners (1981) All ER 865 (H.L).

Conventions/Guidelines/Primary Reports

ATAF (2018) 'Resolving African Challenges in Transfer Pricing. ATAF makes Critical Contribution to Affect Global Tax Standards', Medium, 6 April, Online: <https://medium.com/african-tax-administration-forum/resolving-african-challenges-in-transfer-pricing-44868cfacb64>

ATAF (2017) Suggested Approach to Transfer Pricing Legislation, Pretoria: ATAF, Online: <https://irp-cdn.multiscreensite.com/a521d626/files/uploaded/ATAF%20Suggested%20Approach_revise_green_HR.pdf>

European Commission, "Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)" European Commission COM (2016)

Organization for Economic Co-operation and Development (OECD), "Model Tax Convention on Income and on Capital: Condensed Version 2014/

Organization for Economic Co-operation and Development (OECD), “OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration 2017.

OECD (1995) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, Paris: Organisation for Economic Cooperation and Development.

OECD (2018), Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online: <https://doi.org/10.1787/9789264293083-en>

OECD (2017a) BEPS Action 7: Additional Guidance on the Attribution of Profits to Permanent Establishments (BEPS Public Discussion Draft), OECD

OECD (2017b) OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017, OECD Publishing, Paris. Online: <https://doi.org/10.1787/tpg-2017-en>

(2017c) ‘BEPS Action 13: OECD releases CbC reporting implementation status and exchange relationships between tax administrations’, OECD, 11 October 2017

OECD (2015) Aligning Transfer Pricing Outcomes with Value Creation, Paris: Organisation for Economic Cooperation and Development

OECD (2015) Designing Effective Controlled Foreign Company Rules, Action 3 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, Paris: OECD Publishing. Online: <https://doi.org/10.1787/9789264241152-en>

OECD (2015) Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online: <https://doi.org/10.1787/9789264241176-en>

OECD (2015) Measuring and Monitoring BEPS, Action 11 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, Paris: OECD Publishing. Online: <https://doi.org/10.1787/9789264241343-en>

OECD (2015) Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, Paris: OECD Publishing. Online: <https://doi.org/10.1787/9789264241480-en>

OECD (2015) Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online: <https://doi.org/10.1787/9789264241688-en>

OECD (2015) Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online: <https://doi.org/10.1787/9789264241220-en>

OECD (2014) Transfer Pricing Comparability Data and Developing Countries, Paris: Organisation for Economic Cooperation and Development

OECD (2014) Guidance on Transfer Pricing Documentation and Country-by-Country Reporting, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Online:<https://doi.org/10.1787/9789264219236-en>

OECD (2013) Addressing Base Erosion and Profit Shifting, OECD Publishing, Paris, Online: <https://doi.org/10.1787/9789264192744-en>

OECD (2013) Action Plan on Base Erosion and Profit Shifting, Paris: Organisation for Economic Cooperation and Development.

OECD (2013) Revised Section E on Safe Harbours in Chapter IV of the Transfer Pricing Guidelines, 16 May 2013, OECD.

OECD (2012) Multi-Country Analysis of Existing Transfer Pricing Simplification Measures – 2012 Update, Paris: Organisation for Economic Cooperation and Development

OECD (2012) Revision of the Special Considerations for Intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and Related Provisions, Discussion Draft, Discussion Draft, June 2012, OECD Centre for Tax Policy and Administration.

OECD (2011) Transfer Pricing Legislation, Paris: Organisation for Economic Cooperation and Development

OECD (2010) Revision of the Recommendation of the Council on the Determination of Transfer Pricing between Associated Enterprises, Paris: Organisation for Economic Cooperation and Development

Platform for Collaboration on Tax (2017) A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses. Including a Supplementary Report on Addressing the Information Gaps on Prices of Minerals Sold in an Intermediate Form, Platform for Collaboration on Tax

Platform for Collaboration on Tax (2016) Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries, July 2016, Platform for Collaboration on Tax

Tax Inspectors without Borders (n.d.) (2018), Annual Report 2017/18, Tax Inspectors without Borders

UN (2017a) United Nations Model Double Taxation Convention between Developed and Developing Countries, New York: United Nations.

UN (2017b) Practical Manual on Transfer Pricing for Developing Countries, New York: United Nations.

JOURNALS and PERIODICALS

Reuven Avi-Yonah, "Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State" (2000) Harvard Law Review 113 (7):1573-1676.

Ronald Coase, 'The nature of the firm" (1973) Economica, 4 at 386–405; reprinted in G.J. Stigler and K.E.

Michael C Durst & Culbertson RE, 'Clearing Away the Sand: Retrospective Methods and Prospective Documentation in Transfer Pricing Today" (2003) NYU Tax Law Review 57: 37-136.

Thomas Eichner & Marco Runkel, "Why the European Union Should Adopt Formulary Apportionment with a Sales Factor" (2007) Scandinavia Journal of Economics 110, 567-589.

Tommaso Faccio, et al. ''Alternatives to the Separate Entity/Arm's Length Principle for Taxation of Multinational Enterprises" (2018) Independent Commission for the Reform of International Corporate Taxation. Online: <https://static1.squarespace.com/static/5a0c602bf43b5594845abb81/t/5a792c6b9140b70aade4b83f/1517890668637/ICRICT+Alternatives+Eng+Sept+2017+%281%29.pdf >

Joseph Fleming et al. “Fairness in International Taxation: The Ability-to-Pay Case for Taxing Worldwide Income” (2001) Florida Tax Review 5 (4):299-356.

Elhanan Helpman, ‘‘A simple theory of international trade with multinational corporations” (1984), Journal of Political Economy, 92 (3), 451–71.

Stephen Hymer, ‘‘The internationalisation of capital” (1972) The Journal of Economic Issues, 6 (1), 91–111.

Stephen Hymer. ‘La grande “corporation” multinationale: analyse de certaines raisons qui poussent à l’integration internationale des affaires’ (1968) Revue Economique, 14 (6), 949–73; English version (‘The large multinational “corporation”: an analysis of some motives for the international integration of business’)

Stephen Hymer, ‘The efficiency (contradictions) of multinational corporations” (1970) American Economic Review, 60 (2), 411–18;

Marcelo Ilarraz, ‘‘Does One Size Really Fit All? A Comparative Study of the Transfer-pricing Frameworks of Brazil, India and South Africa” (2016) Sixth Annual Doctoral Meeting, Oxford University Centre for Business Taxation.

Nancy Kaufman, “Fairness and the Taxation of International Income.” (1998) Law & Policy International Business 29 (2):145-204.

Li Jinyan, “Global Profit Split: An Evolutionary Approach to International Income Allocation” (2002) Canadian Tax Journal, Volume 50, No. 3.

James Markusen, ‘‘The boundaries of multinational enterprises, and the theory of international trade” (1995) Journal of Economic Perspectives, 9 (2), 169–89.

Edith Penrose, ‟Foreign Investment and the Growth of the Firm” (1956) The Economic Journal, 66, 262: 220-35.

Mark Segal, "The Unitary Tax Reconsidered" (1994) Journal of Applied Business Research Vol. 10, No. 3.

Tax Inspectors without Borders (n.d.) Tax Inspectors Without Borders: Frequently Asked Questions, OECD/UNDP, Online: <http://www.tiwb.org/about/faq/>

Klaus Vogel, "Worldwide vs. Source taxation of income- a review and re-evaluation of arguments" (Part 1), Intertax, 216, 1988/8-9

Georg Von Schanz as stated by Prof. Eric CCM Kemmeren in "Source of Income in globalised economies, overtire of the issues and the plea for an Origin-based approach", (2006) International Bulletin for Fiscal Documentation at 430.

Oliver Williamson, 'The modern corporation: origins, evolution, attributes" (1981) Journal of Economic Literature, 19, 1537–68.