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Interstate Arbitration in International Tax Disputes

Ilias Bantekas*

ABSTRACT

The proliferation of interstate alternative dispute resolution (ADR) mechanisms, such as joint tax vetoes and mutual agreement procedures, as well as investor–state tax-related arbitration, are the chief reasons for the decline of interstate arbitration (or other forms of adjudication) in tax matters. The article argues that interstate arbitration is envisaged, apart from energy pipeline agreements, as a residual dispute settlement mechanism, but the relative success of ADR has limited interstate arbitration to a limited set of contexts and cases. The following instruments typically serve as submission agreements, namely: bilateral investment treaties, bilateral tax treaties, multilateral regional economic cooperation (or free trade) agreements and pipeline treaties. Ultimately, as the article concludes, a hybrid system that combines: (i) the direct involvement of the taxpayer; (ii) the efficiency of institutional arbitration; and (iii) the transparency guarantees of interstate arbitration is perhaps the way forward.

1. INTRODUCTION

Although there is a growing literature on tax-related investor–state arbitration[1] and a rise in national legislation by which tax disputes (arising within a single state) may be brought before an arbitral body,[2] the literature on the resolution of interstate tax disputes is sparse and is very often intermingled with state–non-state actor (NSA) tax dispute settlement methods. Interstate tax-related arbitration is rare nowadays, although there are several notable spheres of regulation, particularly energy pipelines, where it is commonly provided for in treaties. As the article goes on to demonstrate, the chief reason for the relative scarcity of interstate arbitration (other than transnational energy) is the proliferation of specialized interstate alternative dispute resolution (ADR) mechanisms, such as joint tax vetoes and mutual agreement procedures (MAPs), as well as the rise of investment arbitration. Moreover, it is now well recognized that states possess a legitimate regulatory power to impose *bona fide*

* Brunel University, School of Law. Email: ilias_bantekas@yahoo.co.uk.

1 See A Lazem and I Bantekas, 'The Treatment of Tax as Expropriation in International Investor-State Arbitration' (2015) 30 Arb Intl 1.

2 See eg Portuguese Law/Decree No 10/2011 on tax arbitration, in respect of which commentators suggest that it has increased tax arbitration manifold.

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tax measures[3] and hence there are relatively few instances where, absent a treaty mechanism, it is worth pursuing interstate legal action. The underlying thesis of the article is that the drive towards international tax-related dispute settlement has been driven by powerful states and influential non-state actors, such as arbitral institutions and multinational corporations. Powerful states realized that in order to restrict the reach of foreign tax laws while at the same time retaining their sovereign power to tax as much as possible, bilateral ADR mechanisms, such as MAPs and joint tax vetoes, were the optimum solution.[4] These processes were driven by powerful states through the Organisation for Economic Co-operation and Development (OECD) (in the form of guidances, model treaties and others),[5] the United Nations[6] and bilateral treaties, the majority of which were effectively drafted by industrialized nations. The limited use of interstate arbitration in tax matters cannot be explained on the basis of a coherent schema. No doubt, powerful states believed that as a residual, at the very least, mechanism, interstate arbitration would allow their weaker counterparts to implement and adhere to obligations in particular contexts, such as pipeline agreements and bilateral investment treaties (BITs) or multilateral investment treaties (MITs). Ultimately, investment arbitration has flourished and interstate arbitration has not been of any real use. This residual character of interstate arbitration is also evident as regards the European Union (EU) Arbitration Convention, Base Erosion and Profit Shifting (BEPS) and the OECD Model Income Tax Treaty, with ADR mechanisms being the primary means of dispute settlement. Conversely, the prevalence of interstate tax arbitration in pipeline agreements is rational because these regulate and delimit the tax powers of the Member States and envisage no role of NSAs.

The article examines two particular strands of interstate tax-related arbitration. After a brief historical analysis of pertinent developments prior to World War II, which is instructive in order to fully understand the contemporary paradigm, we go on to assess the instruments under which interstate arbitration is possible. Essentially, these instruments serve as submission agreements. The following types of instruments are considered: BITs, bilateral tax treaties, multilateral regional economic cooperation (or free trade) agreements and pipeline treaties. Subsequently, and given the existence of *locus standi*, the article goes on to examine the forums or

3 *Yukos Universal Ltd (Isle of Man) v Russia*, PCA Award (18 July 2014) para 1444. In this case, however, the tribunal found that Russia's tax measures against Yukos were expropriatory; see also *Les Laboratoires Servier SAS Arts et Techniques du Progres SAS v Poland,* UNCITRAL Award (12 February 2012) paras 277–78, 569, which reiterated that a state was validly exercising its regulatory (police) powers where it was acting: in good faith, reasonably, without discrimination and in proportion to the public aim pursued. This applies *mutatis mutandis* to taxation measures.

4 This idea has been explored by G Simpson, *Great Powers and Outlaw States* (CUP 2004), who argues that powerful states do not desire to share or afford the use of exceptional rules or practices to their weaker counterparts or political foes, with humanitarian intervention being the key paradigm. This unilateralist stance explains the opposition of stronger states to the idea of an international tax tribunal, chiefly because it would render arbitral tax resolution 'unexceptional'. See RJ Jeffery, *The Impact of State Sovereignty on Global Trade and International Taxation* (Kluwer 1999); see also WW Park and DR Tillinghast, *Income Tax Treaty Arbitration* (Sdu Fiscal 2004).

5 See, implicitly, M Desax and M Veit, 'Arbitration of Tax Treaty Disputes: The OECD Proposal' (2007) 23 Arb Intl 405.

6 Chiefly, art 25 of the UN Model Taxation Convention between Developed and Developing Countries.

arbitral choices that states avail themselves in disputes with other sovereigns. Unlike private disputes or state–investor disputes that are typically brought before an institutional body or *ad hoc* proceedings, states are generally disinclined to have interstate tax disputes heard before standing bodies. The majority of disputes in the instruments analysed are to be submitted to *ad hoc* arbitration. Even so, the article traces the role of other forums as arbitral tribunals in interstate tax disputes, namely: the International Court of Justice (ICJ) and its predecessor, the Permanent Court of International Justice (PCIJ), the Court of Justice of the European Union (CJEU) and other Free Trade and Economic Union tribunals.[7] Finally, a brief mention to the prospect of an international tax tribunal (ITT) will be made. Although this article is concerned with arbitral dispute resolution, some reference to very specific tax-related ADR is made in order to provide the reader with a comprehensive picture of existing dispute resolution processes and outcomes. In this light, the article briefly examines treaty-based joint tax vetoes and MAPs, both independently and as the first tier to arbitration, where applicable. Ultimately, as the article goes on to conclude, a hybrid system that combines: (i) the direct involvement of the taxpayer; (ii) the efficiency of institutional arbitration and (iii) the transparency guarantees of interstate arbitration is the way forward.

Before we go on to explore the specialized aspects of this article, it is worth briefly recalling the general framework whereby states have retained absolute sovereignty over tax matters, while at the same time considering those developments that have somewhat limited such absolute sovereignty. After evaluating the various interstate mechanisms, the article will offer an analysis of their legitimacy and the efficacy of public interest pursuits.

2. THE LIMITED SHIFT FROM EXCLUSIVE TAX SOVEREIGNTY

States have traditionally been viewed as having absolute authority to determine and impose taxes on persons, services and assets on their territory. This territorial nature of the sovereign power to tax was never under dispute. However, such neat territorial delineations are incapable of capturing the multitude of transactions, services or the movement of persons or legal entities across two or more frontiers. Should these be taxed at source, on the basis of nationality, or both?[8] Taxpayers taxed twice for the same activity will rightly seek some remedy for the unjustness of double taxation and many states routinely enter into bilateral treaties to adjust and remove double taxation between their nationals. In equal measure, the unimpeded movement of global capital in the era of globalization means that states can (and do) compete with each other to attract businesses and investments to their territory. One notable way is by enhancing their competitive tax advantage and offer preferential tax rates, tax bases, exemptions, deductions, as well as associated advantages such as tax secrecy.[9] This process is known as interstate tax competition and although it has come under

7 The WTO's tax-related dispute resolution procedures will not be examined here, although some references are unavoidable.

8 See P Harris and D Oliver, *International Commercial Tax* (CUP 2010) 43–71.

9 See DM Ring, 'Democracy, Sovereignty and Tax Competition: The Role of Tax Sovereignty in Shaping Tax Cooperation' (2009) 9 Fla Tax Rev 555.

attack by the OECD and financially powerful states as giving rise to harmful tax practices[10] it does actually render tax as matter of transnational concern.[11] Transfer pricing has also become the subject matter of international regulation to the degree that it is used as a means of corporate tax avoidance. In general terms, transfer pricing concerns the fixing of prices for services or products between affiliated companies operating in more than one country. Where such price fixing is undertaken with the sole purpose of tax avoidance, although possibly legal in one or more jurisdictions, it ultimately produces unjust results. Transfer pricing is regulated at bilateral level and the 2010 OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, these having been adopted by several countries.[12]

This gradual, but hardly surprising, erosion of the absolute tax sovereignty paradigm could not but receive some form of regulation under international law. The subject matter of bilateral tax treaties is increasingly making its way in multilateral tax treaties at the OECD and EU level and the taxation of foreign investment is equally entertained in multilateral investment agreements, such as the Energy Charter Treaty (ECT) and under the prism of customary international law, particularly as concerns claims of creeping expropriation.[13] By necessity, this web of international agreements must be construed in accordance with international law (within their particular context), in accordance with Articles 31 and 32 of the 1969 Vienna Convention on the Law of Treaties (VCLT) and not under the domestic laws of their Member States.[14] Moreover, the power to impose taxes must be compatible with the state's other international obligations, such as EU law and human rights law. Taxation that is discriminatory, or which impedes entrenched rights may be challenged not only before local courts, but also before international courts and tribunals, such as the CJEU or the European Court of Human Rights (ECtHR).[15]

It is precisely this increasing transnational and international nature of tax that has necessitated the evolution of dispute resolution at both state–individual and interstate level and it is to the latter that we shall now turn.

10 OECD Report on Harmful Tax Practices (2004).

11 RS Avi-Yonah, *International Tax as International Law: An Analysis of the International Tax Regime* (CUP 2007) 182ff.

12 This is a complex issue and this brief exposition can hardly do justice to the topic. See generally, J Henshall, *Global Transfer Pricing: Principles and Practice* (Bloomsbury 2013); the Base Erosion and Profit Shifting (BEPS) project of the OECD is also concerned, among others, with transfer pricing and its dispute settlement provision is discussed below in another section of this article. But see M Lang and A Storck (eds), *Transfer Pricing in a Post-BEPS World* (Kluwer 2016).

13 See Lazem and Bantekas (n 1).

14 Harris and Oliver (n 8) 28–42; see C Garbarino, *Judicial Interpretation of Tax Treaties: The Use of the OECD Commentary* (Edward Elgar 2016).

15 The European Convention of Human Rights (ECHR) only makes reference to tax in the context of the right to property in art 1(2) of Protocol I to the ECHR and then merely to affirm the tax sovereignty of states. Despite its earlier reluctance to find violations arising out of tax measures, in *OAO Neftyanaya Kompaniya Yukos v Russia* (2012) 54 EHRR 19, paras 656–57, the ECtHR held that the Russian authorities lacked flexibility in their enforcement of the tax debt and 'given the pace of the enforcement proceedings, the obligation to pay the full enforcement fee and the authorities' failure to take proper account of the consequences of their actions', it also held that that the 'domestic authorities failed to strike a fair balance between the legitimate aims sought and the measures employed'.

3. INTERSTATE TAX ARBITRATION PRIOR TO WORLD WAR II

In the pre-WWII era, two tax-related cross-border observations are pertinent. First, NSAs (physical and corporations) possessed severely limited international legal personality. Secondly, tax sovereignty was undisputed, save where it amounted to a violation of an investment guarantee (ie discrimination, expropriation or other).[16] These two observations, taken together, suggest that states would naturally be unwilling to extend arbitral-type resolution to tax disputes with aliens. At the same time, the investor's home state would equally be disinclined to pursue the dispute further (for anything less than expropriation) out of respect for the host nation's fiscal and tax sovereignty. As a result, one would assume that disputes of this nature would be resolved, other than through interstate negotiation, by means of interstate adjudication or arbitration. Practice demonstrates, however, that this was hardly the case, as states were content to regulate tax matters through bilateral treaties, none of which envisaged interstate dispute resolution mechanisms.

Some exceptions to this rule did, however, emerge.[17] In 1926, the Double Income Tax Treaty between Britain and the Irish Free State envisaged the creation of a tax tribunal. The pertinent provision stipulated that:

> Any question that may arise between the parties of this Agreement as to the interpretation of this Agreement or as to any matter arising out of or incidental to the Agreement shall be determined by such tribunal as may be agreed between them and the determination of such tribunal shall, as between them, be final.

The 1928 League of Nations Model Treaty on Double Taxation and Tax Evasion set out a rather elaborate mechanism for the time. Article 5 thereof stipulated that in the event of a dispute regarding the interpretation or implementation of the treaty the parties could have recourse to a technical body appointed by the Council of the League, which could then go on to issue a non-binding advisory opinion. The parties could, if they so agreed, treat the opinion as binding between them. If the opinion was not to their liking and the dispute remained unresolved they could set up an arbitral tribunal or submit the dispute to the Permanent Court of International Justice (PCIJ).[18]

During this time only a single bilateral double tax treaty replicated the League's rather forward-thinking dispute resolution procedures. Article 6 of the 1934

16 A notable reported case is *Kugele v Polish State* (1931) AD, Case No 34, decided by the Arbitral Tribunal of Upper Silesia. The case concerned the imposition of an allegedly confiscatory levy disguised as a license fee. The arbitral tribunal was set up as part of a generalized interstate agreement for the protection of national minorities and it is only very tangentially that the applicant in question may be equated to an investor.

17 See JP Chetcuti, 'Arbitration in International Tax Dispute Resolution' (2001) <www.inter-lawyer.com/lex-e-scripta/articles/tax-arbitration.htm> accessed 10 January 2017.

18 See generally, OR Hoor, *The OECD Model Tax Convention: A Comprehensive Technical Analysis* (Legitech 2010) 19–23, for a history of tax treaties; JDB Oliver, 'The Relevance of Tax Treaty History' (2005) 33 Intertax 484; L Friedlander and S Wilkie, 'Policy Forum: The History of Tax Provisions and Why it is Important to Know about It' (2006) 54 Can Tax J 907; RS Avi-Yonah, 'All of a Piece Throughout: The Four Ages of US International Taxation' (2005) 25 Va Tax Rev 313.

Succession Duties Convention between Romania and Czechoslovakia stated that in the event the parties could not resolve their dispute amicably they could submit it to any technical committee of the League's Fiscal Committee, whose award was binding on the parties. This procedure is tantamount to arbitration given that it clearly constituted an arbitration agreement (pre-dispute) by which the parties referred a future dispute to a body entrusted with producing a final and binding award. This treaty went beyond the exhortation for an advisory opinion envisaged in the 1928 Model Treaty and is considered a landmark instrument even for contemporary standards. Sadly, it did not serve as a blueprint for subsequent developments. It was not until the 1989 USA–Germany Double Taxation and Fiscal Evasion Treaty that arbitration was explicitly provided in a bilateral tax agreement. In that treaty, arbitration is reserved for all matters except tax policy and domestic tax laws. The competent authorities of both states must agree to this arbitral process in accordance with Article 25(5) by notes to be exchanged through diplomatic channels.

One of the few cases known to this author that found its way to an international tribunal, in this instance the Permanent Court of Arbitration (PCA), is the *Japanese House Tax* case, for which an award was rendered in 1905. Japan had allowed communities of aliens to live in its territory, the rights of which were laid down in several bilateral agreements. Aliens were not allowed to own land and hence a system of perpetual leases were granted by or on behalf of Japan, all of which were free from any imposts, taxes, charges, contributions or conditions whatsoever. Japan maintained that the absence of taxes or other charges applied only to the bare land, not to buildings and other constructions later erected by the tenants. The PCA ruled against Japan.[19] The legal basis for engaging the jurisdiction of the PCA was the 1899 Convention for the Pacific Settlement of Disputes.[20] In 1902 the parties drafted a more elaborate *compromis* (ie submission agreement) through a Protocol.[21] It is illustrative of our previous comment as to the scarcity of interstate arbitration regarding internal sovereign undertakings, such as tax, that the Japanese government and its political establishment were hugely disappointed with the outcome of the case, which gave rise to the perception that international law was a machination of the West.[22]

The purpose of this brief historical survey was to demonstrate that even with the restriction of international legal personality to states, tax matters, particularly double taxation and/or discriminatory taxes, were only sparingly encompassed in international treaties and even less provision was made for recourse to interstate arbitration. This is not to say that states chose to ignore these issues, but unlike contemporary times where interstate commerce is expansive this was not the case in the pre-WWII era. As a result, the perception was that any cross-border disputes could either be resolved amicably on the basis of bilateral treaties, general principles or rules of

19 *Germany, France, UK v Japan* [*Japanese House Tax* case], Award ICGJ 407 (PCA 1905), 22 May 1905. It should, of course, be noted that the PCIJ in the *Free Zones of Upper Savoy and the District of Gex* (*France v Switzerland*), (1932) PCIJ Ser A/B No 46, was asked to decide whether art 435 of the Versailles Peace Treaty had abrogated prior customs agreements between the two nations.

20 1 Bevans 230. The 1899 Convention in fact established the PCA.

21 <http://www.pcacases.com/web/sendAttach/1253> accessed 10 January 2017.

22 See A Becker Lorca, *Mestizo International Law: A Global Intellectual History 1842-1933* (CUP 2014) 172–73.

international law (eg minimum treatment afforded to aliens)[23] or by recourse to local courts.

A. The Arbitration Agreement in InterState Tax Disputes

The most fundamental characteristic of arbitration is party autonomy, which is expressed through a *compromis* or arbitration (submission) agreement. The agreement itself may take several forms other than contracts, such as wills, trust deeds, corporate articles of agreement and others.[24] In interstate arbitration, the parties' consent may be expressed in a variety of instruments, given that international law imposes no limitation on states' contractual capacity, so long as consent is manifest and undoubted. Hence, while most instances of interstate tax arbitration have been effected through bilateral or multilateral treaties, there is no reason why the same result may not be derived by an exchange of letters, memoranda of understanding (MoU) or by means of a private agreement (ie a contract governed by the law of a third state).[25]

Unlike other forms of arbitration, the parties are naturally not restricted by arbitrability or public policy limitations, unless they have expressly said so in their agreement. There is of course an issue regarding the applicable governing law of their agreement to arbitrate. In international arbitration, the law of any nation, *lex mercatoria*,[26] general international law or even equitable determination would suffice as the parties' governing law. All of these sources contain enough substantive rules for the merits of a dispute to be decided. In interstate tax arbitration, however, the situation is rather different. Domestic tax laws largely concern income generated on the

23 Several ILC instruments are illustrative of customary international law in this regard. The articles on State Responsibility and those on the Expulsion of Aliens are certainly indicative.

24 I Bantekas, *Introduction to International Arbitration* (CUP 2015) 79–84.

25 In a recent spate of interstate loan agreements, particularly those to Greece, such as the 2012 European Financial Stability Facility (EFSF)–Greece Master Financial Assistance Facility Agreement, which is a private contract governed by English law, a series of MoUs were envisaged as integral to the original contract, which suggested that despite their designation that they were binding, these MoUs set out several conditions for the borrower in order for the loan to be disbursed. Among these were reforms to the borrower's tax system. If a dispute were to arise regarding an interpretation as to what was actually demanded or accepted, or what part of the demand was not adequately addressed by the borrower this would constitute a *sui generis* interstate tax dispute (given that the bulk of EFSF funds are derived by state entities). Although the loan agreements in question designated Luxembourg courts and the CJEU (the latter only concerns the Greek loan agreement of August 2015) as forums for hearing disputes, given the restrictions imposed on such courts (eg EFSF is not an EU institution and hence not subject to EU law. See particularly, *Pringle v Ireland*, Case C-370/12 [2012] ECR I-756; equally, the loan agreement/MoU which function as submission agreements designate English law as their choice of law) their function is akin to an arbitral tribunal.

26 Although it is far beyond the purview of this article, it should be stated that there does exist a sustained practice in several industries with respect to the allocation of taxes between host states and foreign investors. As will be demonstrated in a subsequent section dealing with oil and gas pipeline construction and transit, the host state (investor–state) host agreements are very elaborate regarding taxation. Although these are private agreements (essentially contracts), their tax-related provisions are similar in other projects around the world, thus suggesting some form of *lex mercatoria* (involving a state). Such projects are structured around an initial treaty between the states concerned, further elaborated through a series of host government agreements with the private contractors. In case of a dispute between the State Parties as to the meaning of the tax-related provisions, they could in theory (although unlikely in practice) request the tribunal to take into consideration also the dictates of *lex mercatoria* in the field in question.

territory of the taxing state or income otherwise generated abroad, but which is connected to the country in question. In the absence of a treaty, domestic tax laws are thus in conflict, except if the dispute in question concerns whether a tax should have been imposed in the first place or is otherwise discriminatory, or the entity for which diplomatic protection is sought has engaged in tax evasion (eg through illegal transfer pricing).

B. Bilateral Investment Treaties

The vast majority of BITs or free-trade agreements (FTAs) (with investment provisions, eg NAFTA) do not exclude the application of expropriation provisions in respect of tax-related claims, save for the competence of the tax authorities of the BIT parties to jointly veto the application of expropriation provisions in respect of tax claims on a case-by-case basis[27] (joint tax veto). They do, however, widely exclude the application of national treatment and most-favoured-nation (MFN) treatment in tax matters. The rationale underlying such tax exclusions is to avoid conflicts with existing bilateral tax regimes[28] and in order that states can retain maximum fiscal sovereignty, such as avoiding regulatory chill from the threat of investor–state arbitration in respect of tax matters relating to national treatment (and MFN treatment). In addition, tax exclusions ensure the granting of favourable tax treatment to one's nationals or nationals of select third states (which would breach national treatment and MFN, respectively, but for the tax exclusions).[29] This explains why investment tribunals have found a violation of applicable standards of treatment and indirect expropriation (in the form of *measures with an equivalent* effect)[30] only in BITs that are either silent on such matters or otherwise contain tax exclusions.[31] In fact, the draft Multilateral Agreement on Investment (MAI) contained a definition of 'taxation measures' which includes 'any provision relating to taxes of the law of the contracting party or of a political subdivision thereof or a local authority therein, or any administrative practices of the contracting party relating to taxes' and taxes are taken to include 'direct taxes, indirect taxes and social security contributions'.[32] The MAI Interpretive Notes recognized that some taxation measures are capable of constituting an expropriation, although the general presumption was that if they are 'within the bounds of internationally recognised tax policies and practices' they would not.[33]

27 See eg art 2103(6) NAFTA; art 21.3(6) DR-CAFTA; art 21(5) ECT; art XII(4) Canada–Ecuador BIT; art 170(4)(b) Japan–Mexico BIT; art 21(2) US Model BIT; art 16 Canada Model BIT; art 28 Norwegian Model BIT. See generally, Lazem and Bantekas (n 1).

28 This is explicit in art 16(1) of the 2004 Canadian Model BIT and art 3(4) of the 2008 German Model BIT, which excludes the application of national and MFN treatment to advantages provided in other bilateral tax treaties; equally, art 28(2) Norwegian Model BIT and art 196(3) EC-Chile FTA.

29 UNCTAD, 'Taxation' (2000), Series on Issues in International Investment Agreements, Doc No UNCTAD/ITE/IIT/16, 36 <http://unctad.org/en/docs/iteiit16_en.pdf>.

30 Eg art 13(1), 2004 Canadian Model BIT; art 1110(1) NAFTA; art 9 EC-RSA FTA.

31 *El Paso Energy International Company v Argentine Republic*, ICSID Case No ARB/03/15 (Merits) 31 October 2011, para 292.

32 art VIII(5)(b), Draft MAI.

33 OECD Negotiating Group on the Multilateral Agreement on Investment, 'The Multilateral Agreement on Investment- Draft Consolidated Text' Doc No DAFFE/MAI(98)7/REV1 (22 April 1998) 86; see also art 6(2) of the Norwegian Model BIT.

Although most of the new generation of BITs and MITs contain explicit references to tax exclusions, joint tax vetoes prescribe the ambit of this authority in the field of foreign investment (as well as other fields in the context of all-embracing FTAs, such as competition and customs), very few specifically spell out that tax measures may be expropriatory or in violation of other investor guarantees. Article 21(5)(a) of the ECT is therefore a rarity. It states that the ECT expropriation provision (Article 13) applies to taxes and hence relevant disputes may be submitted to IIA under condition that the joint veto procedure is first exhausted. Subparagraph (b) then goes on to say that a tax may indeed be expropriatory or discriminatory, in which case the full impact of Article 13 is applicable (subject to the joint veto procedure). Some BITs list tax measures among those that may give rise to expropriation. Exceptionally, the US–Egypt BIT does so indicatively, stipulating that:

> No investment or any part of an investment of a national or a company of either Party shall be expropriated or nationalized by the other Party or a political or administrative subdivision thereof or subjected to any other measure, direct or indirect (including, for example, *the levying of taxation,* the compulsory sale of all or part of such an investment, or impairment or *deprivation* of management, control or economic value of such an investment by the national or company concerned), if the effect of such other measure, or a series of such other measures, would be tantamount to expropriation or nationalization.[34] (emphasis added)

Most international investment treaties (IITs), whether bilateral or multilateral, subject their expropriation provisions to the host state's regulatory measures in the field of tax.[35] As a result, investors may validly claim under the treaty that their assets were taken, directly or indirectly, under a particular tax law or measure. While most IITs, as already explained, contain tax exclusions to the privileges otherwise offered under the national treatment principle, some exceptionally restrict the application of tax measures to expropriation by including tax exclusions to the entire IIT and therefore encompass expropriation within such exclusion.[36] In equal measure, although this is pretty much the norm, the majority of IITs attempt to block the deliberation of tax in expropriation claims through joint tax vetoes, which will be explored in a subsequent subsection.

Unlike bilateral tax treaties, BITs and IITs contain interstate dispute resolution provisions.[37] However, because violations of investment guarantees (granted under BITs or contract) are susceptible to investment arbitration, there is no practical need

34 art III, US–Egypt BIT.

35 UNCTAD, *Expropriation* (UNCTAD Series on Issues in International Investment Agreements II (2011), Doc UNCTAD/DIAE/IA/2011/7) 133.

36 art 5, 1999 Argentina–New Zealand BIT; art 8, 1999 New Zealand-Chile BIT; art 5, 1988 New Zealand–China BIT (with exchange of notes).

37 NAFTA, ch 20; art IX of the 1987 ASEAN Agreement (as modified in 1996); arts 28(2) and 37 US Model BIT; art 21 Australia-US FTA; art 19 UK-France 1986 Treaty on the Construction and Operation by Private Concessionaires of a Fixed Channel Link [Treaty of Canterbury]. art 9 of the Canterbury Treaty refers specifically to taxes on gains and profits imposed by both nations and any disputes over the application of this provision falls within the jurisdiction of the interstate tribunal under art 19 thereof.

for states to engage in any type of dispute resolution, other than ADR in the eventuality of a breach by the host state. Other than cases of expropriation by means of domestic taxation, pertinent states will engage with one another through specialized mechanisms, such as joint tax vetoes or MAPs, given that the intention of states is to use bilateral tax treaties to resolve outstanding tax disputes.

C. Bilateral Tax Treaties

Typical interstate tax disputes (covered in bilateral tax treaties) concern transfer pricing, division of revenues from value-added taxes, double taxation, source-based withholding tax on royalties for intellectual property (such as trademarks and copyright) used in one country and paid to enterprises or persons resident in another,[38] and others. Unlike the vast majority of all bilateral and multilateral treaties, which contain an interstate dispute resolution clause, bilateral tax treaties prior to the latest revision of Article 25(5) of the OECD Model Tax Treaty usually contained no such clause. This is unusual because in the event of dispute over the interpretation of the treaty the parties will have to consider post-conflict measures on the basis of a new agreement. The US Model Tax Treaty[39] and recent bilateral double taxation treaties to which the United States is a party are silent on this matter. However, several bilateral tax treaties adopted in the 1990s provide for a *sui generis* form of interstate arbitration.[40]

Recent bilateral tax treaties seem to disfavour interstate arbitration, instead promoting taxpayers to make use of MAPs. However, as will be shown in a subsequent section, with the amendment of Article 25 of the OECD Model Tax Treaty on Income and Capital, which allows tax authority to arbitrate a dispute not settled by a MAP 2 years after the procedure commenced, interstate tax arbitration predicated on the revised Article 25 model may indeed be reinvigorated. There is some evidence of this particularly in Asia, where Japan, Singapore, Hong Kong and South Korea have entered into new bilateral tax treaties.[41]

Overall, practice suggests that bilateral tax treaties are treated as *lex specialis* as compared to other spheres of international regulation, such as investment or

38 See AD Christians, 'Tax Treaties for Investment and Aid to Sub-Saharan Africa' (2005) 71 Brook L Rev 639.

39 2006 US Model Income Tax Convention; equally, other similar treaties, such as the 1985 US-Canada Income Tax Convention.

40 As a result, art 25(5) of the 1989 USA-Germany Double Taxation and Fiscal Evasion Treaty, which explicitly provides for interstate arbitration as exceptional, although it may give rise to a particular genre. art 29(5) of the 1992 US-Netherlands Treaty on Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, states that if the MAP fails to yield any results: 'the case may, if both competent authorities and the taxpayer(s) agree, be submitted for arbitration, provided the taxpayer agrees in writing to be bound by the decision of the arbitration board. The decision of the arbitration board in a particular case shall be binding on both states with respect to that case. The provisions of this paragraph shall have effect after the states have so agreed through the exchange of diplomatic notes'.

That tax arbitration of this nature is exceptional is reinforced by the MoU to the US-Netherlands Treaty, which stipulated that arbitration under art 29(5) will not be used until both countries agree that experience with such a procedure in other contexts has proven satisfactory. See M Markham, *The Transfer Pricing of Intangibles* (Kluwer 2005) 217.

41 H Vollebregt, R Thomas and W Pieschel, 'Arbitration under the new Japan-Netherlands Tax Treaty' (2011) 65 BFIT 223.

international trade. As a result, these other treaties are mindful of avoiding any kind of conflict with bilateral tax treaties as regards general tax policy.[42] In respect of specialized tax regimes, such as those relating to cross-border energy pipelines (explored in a subsequent section), bilateral tax treaties are not treated as *lex specialis* and are routinely ignored, which explains the existence of interstate arbitration in the pertinent agreements.

D. Multilateral Regional Economic Cooperation Treaties

It is very rare for such agreements to envisage an interstate tax arbitration procedure. Tax-related national policies are usually outside their purview, as is the case with EU treaties, unless a particular tax violates a freedom or prohibited practice (such as state aid) set out by these treaties. Exceptionally, the Brasilia Protocol of 1991 (to the MERCOSUR Convention[43]) for the Settlement of Disputes sets out an interstate dispute resolution process involving a series of fast-track ADR methods. If these prove to be unsuccessful and fail to satisfy the parties, recourse to *ad hoc* arbitration is ultimately available.[44] The Protocol itself suffices as a valid agreement to arbitrate and does not require that the parties enter into a post-dispute agreement in the eventuality of future conflict. Given that the MERCOSUR Convention establishes a free trade area, it is evident that tax issues, broadly understood, constitute a crucial dimension of its operation.

Disputes have been entertained under this procedure. In the case *Concerning Specific Internal Taxes (IMESI) on Cigarettes* (*Paraguay v Uruguay*),[45] Paraguay questioned Uruguay's collection of specific internal taxes on cigarettes imported from non-neighbouring countries. One of the key issues in the case concerned the alleged discriminatory character of the calculation of taxes for Paraguayan exports. The tribunal found that in conformity with the MERCOSUR Convention there was no reason to discriminate by way of internal taxes against cigarettes imported from Paraguay solely because it is a non-coboundary state. On 21 May 2002, the tribunal unanimously ordered Uruguay to stop the denounced discrimination and also ordered by a majority vote that it abstain provoking collateral negative effects on cigarettes imported from Paraguay. Uruguay finally enforced the award by eliminating discriminatory measures against cigarettes produced in Paraguay.

The MERCOSUR interstate arbitration system exemplifies that where an FTA lacks a robust dispute settlement mechanism, as is the case with the 1972 Swiss–EU FTA, the disputing parties will ultimately have recourse to negotiation. In the tax dispute between the EU and Switzerland, the former alleged that several corporate tax regimes established by Switzerland were effectively state aids, which were prohibited under the FTA. The EU Commission issued a decision identifying the

42 art 22(3) GATS, for example, prevents the application of the dispute settlement mechanism to encompass matters that fall within the remit of tax treaties. To counter this situation, it sets up a binding arbitration mechanism where there is doubt about the applicability of this provision on a specific subject matter.

43 1991 Treaty of Asuncion, Establishing a Common Market between Argentina, Brazil, Paraguay and Uruguay (as subsequently amended).

44 arts 29–30 Brasilia Protocol.

45 22 BO del Mercosur 209, 210 (Tribunal *Ad Hoc* del Mercosur 2002).

incompatibility with the FTA.[46] After years of negotiation, the two entities finally resolved their dispute in 2014 through the adoption of a mutual understanding and a lifting of the harmful tax measures by Switzerland.[47] This is not to say that the existence of robust interstate arbitration would have been speedier or produced a better outcome; rather, it would have provided an additional tool to the parties.

E. Pipeline Treaties

Pipeline (construction, operation and transit) agreements must be viewed as a distinct species of agreement as far as tax and dispute resolution is concerned.[48] This is not because they are somehow *lex specialis*, but rather because of the State Parties' contribution to the pertinent phases of said agreements (usually through the form of state enterprises) as well as sovereignty considerations as will be shortly demonstrated. Structurally speaking, because pipeline construction and operation concern the territorial sovereignty of states, it is natural that states regulate such matters on the basis of interstate treaties, even if some or all of the participating states contribute few, if any, resources to the project under consideration. A typical agreement of this nature is the 2003 Treaty on the West African Gas Pipeline Project (WAGP Treaty) between Benin, Ghana, Nigeria and Togo. Given that the pipeline will ultimately be mostly financed, constructed and operated by private investors (with the participation of the pertinent states as partners or in other capacities, such as auditors), subsequent private agreements must be concluded between the participating states and the investors. These are mostly known as host government agreements. These constitute an integral part of the interstate treaties. Taxation, including tax stabilization obligations, may be regulated in either the treaty or the host government agreement.[49] Article V of the WAGP Treaty regulates fully the fiscal (tax) regime of the project, as does Article V of the Baku–Tbilisi–Ceyhan Main Export Pipeline [Turkey–Georgia–Azerbaijan]. Article 10, on the other hand, of the 2012 Baku–Tbilisi–Ceyhan Main Export Pipeline (Trans-Anatolian Natural Gas Pipeline Project - TANAP) Treaty stipulates that taxes are to be regulated under the pertinent host government agreements.

While the host government agreements oblige the host state and the foreign investor to settle disputes through arbitration (typically the International Convention for Settlement of Investment Disputes (ICSID) or the ECT), it is clear that disputes concerning domestic tax measures can only be resolved through the limited expropriation lens offered by international foreign investment law, as explained above. If the pipeline treaties offered no further interstate recourse, then host states would be free

46 Commission Decision of 13 February 2007 on the incompatibility of certain Swiss company tax regimes with the Agreement between the European Economic Community and the Swiss Confederation of 22 July 1972.

47 See AR Ziegler and JK Baumgartner, 'The Tax Controversy between Switzerland the European Union Relating to the 1972 Free Trade Agreement' in R Danon (ed), *Rethinking Corporate Tax* (forthcoming, 2017).

48 See D Azaria, *Treaties on Transit of Energy via Pipelines and Countermeasures* (OUP 2014) 183.

49 Some stipulate a combination of both. For example, para 31 of the Turkmenistan–Afghanistan–Pakistan–India (TAPI) Gas Pipeline Framework Agreement provides that matters of tax are to be regulated by each state's national laws, bilateral agreements or distinct host government agreements.

to engage in any tax action or policy, short of expropriation. Prior to the proliferation of investment arbitration, interstate arbitration was not uncommon. Article 21 of the 1975 Turkey–Iraq Crude Oil Pipeline Agreement envisages *ad hoc* arbitration between the two countries, further stipulating that following the selection of party-appointed arbitrators they in turn shall select an umpire. With the gradual proliferation of investment arbitration, such clauses were conceived as serving no real purpose. However, because tax-related investment arbitration is limited in scope and also because pipelines encompass a number of enduring sovereignty considerations, pipeline treaties have revived many of the features of interstate dispute resolution; as has already been explained, this is not the case in other fields of interstate tax regulation and this is chiefly the reason why this author believes that pipeline agreements are distinct from other tax-related treaties.

Pipeline treaties set forth a tiered interstate dispute resolution system. At the first level, they make provision for an inter-governmental body that possesses, among others, the function of mediator and/or conciliator. The WAGP Treaty establishes the WAGP Authority, which is effectively a distinct intergovernmental organization (IGO) that is entrusted with setting out various policies on behalf of the State Parties. The fiscal regime (essentially tax regime) provided by the WAGP Treaty, and any alleged violations thereof may be brought before a WAGP Fiscal Review Board.[50] Its decisions are appealable before the WAGP Tribunal.[51] The WAGP Authority, which is an IGO, operates a WAGP Company and hence any disputes between the WAGP Company and the participating states would not qualify as investment disputes. In equal measure, Article 13(1) of the 2009 Nabucco Agreement between Austria–Bulgaria–Hungary–Romania–Turkey provides that any interstate disputes brought before the Nabucco Committee, shall seek an amicable solution within a period of 90 days, following which the dispute may be submitted to *ad hoc* arbitration under the terms of Article 27(3) of the ECT.[52]

Just like Article 13(1) and (5) of the Nabucco Agreement, most pipeline treaties stipulate that in the event that the mediating body has failed to reach a compromise that is acceptable to both parties, either one may have recourse to some form of *ad hoc* or institutional (ECT) arbitration. Article 27(3) of the ECT provides for *ad hoc* interstate arbitration in the event of dispute, including tax-related disputes, despite the availability of joint tax vetoes and mediation. Hence, it is natural that specialized/regional pipeline treaties are influenced by the ECT in this regard which serves as a benchmark for contemporary energy agreements. *Ad hoc* interstate arbitration can take several forms, however. Besides the possibility of *ad hoc* arbitration under the UNCITRAL Rules, for example, the treaty may provide for recourse to an existing entity. Article XI of the WAGP Treaty obliges parties to submit disputes to the ECOWAS Court of Justice, which shall serve as an arbitral tribunal. While some agreements rely on the format laid out in Article 27(3) ECT, others produce an elaborate set of rules relating to *ad hoc* arbitral proceedings. By way of illustration, Article

50 art VI WAGP Treaty.

51 art VI(4) WAGP Treaty.

52 Equally, art VII of the Baku–Tbilisi–Ceyhan Main Export Pipeline Treaty; art X(2)(d) of the WAGP Treaty, which confers mediatory functions to the WAGP Committee of Ministers.

12 of the TANAP Agreement provides for arbitration under UNCITRAL Rules in Geneva. Paragraph 5 of Article 12 goes on to make an elaborate plan for the allocation of arbitral costs, which is not encountered in any other specialized pipeline agreement.[53]

4. INTERSTATE ADR IN INTERNATIONAL TAX MATTERS

Interstate ADR is beyond the narrow purview of this article, which deals exclusively with interstate arbitration, but a brief exposition is essential in order for the reader to receive a fuller picture of the processes by which states have agreed to resolve tax conflicts. ADR processes are typically triggered by taxpayers. Here, we shall refer to the so-called MAP and joint tax vetoes. In between, a section on interstate arbitration, as a supplement to MAPs, is explored in some depth, as envisaged in the EU Arbitration Convention and the recent amendments to the OECD Model Tax Treaty. Although this would ordinarily have been encompassed in other sections dealing specifically with interstate tax arbitration, it is intentionally included here for reasons of coherency with a view to the reader understanding its overall rationale and context.

It should be noted that although this article deals with interstate tax arbitration it does not necessarily attempt to promote this method over others. In fact, states find it compelling to avoid binding awards in matters that affect their broader fiscal policy and this is why tax is generally perceived as *lex specialis* even in the context of international foreign investment law.

A. Mutual Agreement Procedure

The MAP is by now a standardized ADR procedure whose legal basis is prescribed in bilateral tax treaties.[54] It is triggered by a formal application of an aggrieved natural or legal person (usually as a result of disputed double taxation measures) to the authorities of one Member State. Such an application subsequently obliges the tax authorities of both states to engage in discussions over the disputed taxes with a view to arriving at a just, fair and lawful assessment for the taxpayer in question. Article 25 of the OECD's Model Tax Convention[55] is instructive of this procedure.

> 1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of the Contracting State of which he is a resident or, if his case comes under paragraph 1 of Article 24, to that of the Contracting State of which he is a national. The case must be presented within 3 years from

53 But see art 27(3)(j) ECT.

54 P Harris and D Oliver, *International Commercial Tax* (CUP 2010) 458–62; UN, Guide to the Mutual Agreement Procedure under Tax Treaties <http://www.un.org/esa/ffd/wp-content/uploads/2014/10/ta-Guide_MAP.pdf> accessed 10 January 2017.

55 Upon which art 25 of the UN Model Tax Convention has been modelled.

the first notification of the action resulting in taxation that is not in accordance with the provisions of the Convention.

2. The competent authority shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States.
3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention.
4. The competent authorities of the Contracting States may communicate with each other directly, including through a joint commission consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs.

The legal nature of the MAP procedure under Article 25 does not seem to reflect the traditional notion of diplomatic protection, particularly because the latter seldom arose as a result of contract or treaty, whereas the MAP can only arise out of a treaty obligation.[56] Equally, diplomatic protection generally arises because the private claimant does not possess sufficient international legal personality in a particular sphere and hence lacks *locus standi*. The MAP, on the other hand, is prescribed in treaties and while the aggrieved (private) entity is not a party to the proceedings, it may initiate other judicial proceedings—although where a mutual agreement has been adopted and the taxpayer has accepted it, he may not subsequently pursue the settled points before a judicial *forum*.[57] In this sense, the MAP is a *sui generis* form of arbitration applicable to tax disputes.[58]

Despite the absence of a *locus standi* for private entities, the OECD Commentary on the Model Tax Treaty is adamant that where the procedure is brought before the joint commissions,[59] taxpayers must be afforded certain essential guarantees, namely: (i) the right to make representations in writing or orally, either in person or through

56 Diplomatic protection is not an entitlement, but is in the discretion of the state. See *Barcelona Traction, Light and Power Co Ltd (Belgium v Spain)*, Merits [1970] ICJ Rep 44, para 79.

57 Under art 27(1) ICSID Convention the triggering of investment arbitration terminates diplomatic protection. Hence, if indeed the MAP is not a form of diplomatic protection, it may coexist alongside investment arbitration.

58 The OECD Commentary to the Double Tax Treaty <www.oecd.org/berlin/publikationen/43324465.pdf> accessed 10 January 2017, notes that on account of para 4 of art 25, the competent authorities may communicate with each other directly without the need to establish in each case diplomatic channels. This will be achieved by joint commissions through an oral exchange of opinions. 'OECD Commentary', ibid 300, para 4.

59 A joint commission is that which is established in accordance with art 25(4) of the OECD Model Tax Treaty.

a representative, and; (ii) the right to be assisted by counsel.[60] It is also evident that the application of the MAP encompasses situations in which the private entity is not necessarily a national of the two states involved in the double taxation dispute. This is possible where enterprise X is incorporated in country A, but is currently resident in country B and its income generated from activities in country B are also taxed in country C, which is where it conducts associated business. In this case, the dispute may arise on account of income taxation imposed in both B and C, but not country A.[61] Such an eventuality further justifies the conclusion that the MAP is not a form of diplomatic protection because the claim of the taxpayer may be assumed by the country of residence rather than the country of nationality.

B. Interstate Arbitration as a Complement to Failed MAPs

Although the MAP is a significant improvement to the unilateral powers typically granted to domestic tax authorities under international law, it is not always certain that the authorities in question will resolve the dispute. It is for this reason that several Model and bilateral tax treaties have gone a step further, establishing a *sui generis* arbitral process. Article 25(5) of the OECD Model Tax Treaty (2014 version)[62] provides a mechanism that allows a taxpayer to request the arbitration of unresolved issues that have prevented competent authorities from reaching a mutual agreement within 2 years. While the mutual agreement procedure provides a generally effective and efficient method of resolving disputes arising under the Convention, there may be cases where the competent authorities are unable to agree that the taxation imposed by both states is in accordance with the Convention. The arbitration process provided for under paragraph 5 allows such cases to be resolved by allowing an independent decision of the unresolved issues, thereby allowing a mutual agreement to be reached. This process is an integral part of the mutual agreement procedure and does not constitute an alternative route to solving disputes concerning the application of the Convention. Article 25(5) reads as follows:

> Where,
> *a)* under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and
> *b)* the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within two years from the presentation of the case to the competent authority of the other Contracting State, any unresolved issues arising from the case shall be submitted to arbitration if the person so requests. These unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or

60 OECD Commentary (n 58) 309, paras 42–43. There is no requirement, however, of disclosure to the taxpayer, which confirms the lack of effective *locus standi* of the taxpayer in the procedure.

61 See generally, I Bantekas, 'The Mutual Agreement Procedure and Arbitration of Double Taxation Disputes' (2008) 1 Colom Yb Intl L 182, 187.

62 As does also art 25(5) [Alternative B] of the UN Model Tax Convention.

> administrative tribunal of either State. Unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.

The forerunner and innovator in this respect, however, was the EC Convention on the Elimination of Double Taxation in Connection with the Adjustment of Profits of Associated Enterprises, adopted in 1990 (EU Arbitration Convention).[63] Article 7(1) of the EU Arbitration Convention goes on to say that if the competent authorities fail to reach an appropriate agreement within 2 years of the date on which the case was first submitted to one of them, they shall set up an advisory commission charged with delivering its opinion on the elimination of the double taxation in question. The competent authorities of the states concerned contractually agree to submit double taxation claims to arbitration on the basis of Article 7(1) of the EU Convention itself, which in this sense serves the same purpose as an arbitration clause in a private contract. The parties to this arbitration clause are the concerned states and no further post-dispute submission agreement is required before the Advisory Commission assumes responsibility.

The Commission resembles the function and attributes of arbitral tribunals, albeit given its mandate, scope and sovereign sensitivities the process should not be strictly compared to that of commercial arbitration. The Commission's jurisdiction would have been seriously compromised were the Convention to contain a provision to the effect that contracting states were under no obligation to recognize or enforce the tribunal's award, or where a state's domestic laws forbade it to arbitrate tax disputes before an international body. With a minor exception this is not the case and hence the tribunal's competence is not compromised. A further criterion is that of the independence of the arbitrators[64] and the ability of the parties to choose said persons. There is no doubt that under Article 9 of the Arbitration Convention, some members of the Advisory Commission must be independent, but not all. In addition to the Chairman, Article 9(1) states that the Commission shall consist of one or two (following agreement to reduce the number) representatives of each competent authority concerned, as well as 'an even number of independent persons of standing to be appointed by mutual agreement from the list of persons referred to in paragraph 4[65] or, in the absence of agreement, by the drawing of lots by the competent authorities concerned'. Hence, unlike international arbitration, there is no requirement that

63 EC Convention on the Elimination of Double Taxation in Connection with the Adjustment of Profits of Associated Enterprises 90/436/EEC [1990] OJ L225.

64 art 10, UNCITRAL Arbitration Rules provide for a challenge where justifiable doubts as to the arbitrator's impartiality and independence arise. Equally, art 11(1) of the International Chamber of Commerce's (ICC) Rules provide for a challenge in cases of lack of impartiality or otherwise.

65 art 9 states that the list of independent persons of standing shall consist of all the independent persons nominated by the contracting states. For this purpose, each contracting state shall nominate five persons, which must be nationals of a contracting state and resident within the territory where the Convention applies. Such persons must be competent and independent.

representatives of state authorities be independent and impartial. Article 11(2) of the Convention makes it clear that the Advisory Commission shall adopt its opinion by a simple majority of its members, including its non-independent members.

Because of the treaty-based nature of this arbitral process, many, if not all, of the discovery hurdles encountered in commercial arbitration, have been resolved through express mandatory terms in the EU Arbitration Convention. The enterprises and the competent authorities of the contracting states concerned *shall* give effect 'to any request made by the Advisory Commission to provide information, evidence or documents'.[66] This obligation is not incumbent on the competent authorities where: (i) this would be at variance with their domestic law or normal administrative practices; (ii) the requested information is not obtainable under its domestic law or administrative practices; or (iii) to supply such information which would disclose any trade, business, industrial or professional secret or trade process or information would be contrary to public policy.[67] Equally, the associated enterprises are obliged to appear before the commission if it so requests them.[68] Although aggrieved private entities are third parties to the arbitral process and their claim is assumed by a competent authority they constitute an integral part of the arbitration process, albeit with no independent right of *locus standi*. Their direct participation in the arbitral proceedings encompasses also the right to 'provide any information, evidence or documents which seem to them likely to be of use' to the Advisory Commission in reaching a decision. Equally, each of the associated enterprises may, at their request, appear or be represented before the Commission.[69] In 2006, the EU Council adopted a Code of Conduct for the Effective Implementation of the Convention.[70] This lays down important principles for the efficient, effective and just submission and determination of cases, such as the introduction of the arm's length principle.

Given that the 'arbitration' procedure in the EU Arbitration Convention constitutes an integral part of the MAP, the onus is on the concerned states to reach a mutual solution. Hence, although the opinion of the Commission is not initially binding on the parties, they must, 'acting by common consent', take a decision that will eliminate double taxation within 6 months from the date on which the Advisory Commission delivered its opinion.[71] In doing so, the competent authorities are free to adopt a common decision, which deviates from the Commission's advisory opinion. However, if they fail to reach agreement, 'they shall be obliged to act in accordance with that opinion'.[72] Hence, the Commission's opinion shares the same legal effects, *mutatis mutandis*, with an arbitral award, save that the parties are not typically estopped from enforcing an arbitral award if they have subsequently deviated from the dispositive parts of the award. As regards enforcement of the Commission's

66 art 10(1), EU Arbitration Convention.

67 ibid.

68 art 10(2), ibid.

69 art 10(1) and (2).

70 OJ C176/8 (2006).

71 art 12(1), EU Arbitration Convention.

72 ibid.

opinion, given that its binding character is premised on a treaty undertaking, there is no question that it is enforceable between the contracting states.[73]

C. BEPS Action 14

The OECD's Base Erosion and Profit Shifting Project (BEPS) is a relative newcomer to the international tax scene. Although a lengthy analysis is beyond the purview of this article, a short section is, nonetheless, useful at this juncture in order to understand the OECD's viewpoint on the future of the MAP process in conjunction with a future arbitral trend in respect of double tax disputes. Action 14 does not depart from the MAP process in Article 25 of the Model Tax Treaty, but calls on states to strengthen it through political commitments and enforcement action (eg by making it effective and speedy) and further suggests a residual arbitral phase in situations where the disputes have not been resolved. It is clear that the OECD and its Member States are not yet at the stage where they envisage the creation of institutional or *ad hoc* interstate or taxpayer-state tax arbitration. Nonetheless, the model of paragraph 5 of Article 25 of the Model Tax Treaty is perceived as an adequate residual mechanism. In fact, following the launch of the 5 October 2015 final paper on the BEPS Action 14,[74] New Zealand and Australia committed themselves to adopt mandatory binding arbitration as part of their MAP process in their double tax agreements. Just as elsewhere, the purpose of interstate arbitration in the BEPS should be viewed as having a residual character and not destined as a primary form of dispute settlement.

5. JOINT TAX VETOES

Contemporary BITs and FTAs routinely incorporate the practice of *joint tax vetoes*. Here, the parties to BITs and FTAs agree that where a tax measure may affect the guarantees ordinarily promised towards investors, the determination as to whether such measures constitute a violation of the relevant instruments will be decided by the authorities of the two states at a political level.[75] Any decision must of course be taken through mutual consent, but in any event it is evident that there is general reluctance to subject national tax measures to investment arbitration without first exhausting all alternative remedies. There is nothing equivalent to joint tax vetoes for other matters in investment treaties which suggests that tax policies are viewed more from a political lens rather than a legal one and in case a mutual decision to approve a particular tax measure is adopted (and hence the investor has no recourse to investment arbitration) the relevant states may off-set a tax measure for a future political favour. What this means for the investor in question is unknown, but no doubt it is in the investor's interest to put political pressure on its government to uphold its rights in one way or another. BITs and FTAs envisaging joint tax veto procedures do not expressly exclude recourse to investment or other arbitration and of course there

73 See Panayi (n 89) 70–75; J Henshall, *Global Transfer Pricing: Principles and Practice* (Bloomsbury 2013) 151ff.

74 <http://www.oecd-ilibrary.org/docserver/download/2315391e.pdf?expires=1450076090&id=id&accname=guest&checksum=4EA2C0338287242F788E4AFA82F40B3F> accessed 10 January 2017.

75 See A Kolo, 'Tax Veto as a Special Jurisdictional and Substantive Issue in Investor-State Arbitration: Need for Reassessment?' (2008–2009) 32 Suffolk Transnatl L Rev 475.

is no reason why the State Parties to these treaties may not substitute joint tax veto decision-making for ad hoc arbitration where the treaty in question allows a state party (not the investor) to bypass this ADR procedure. Although this author is not aware of any such deviation, particularly given its transactional cost and the animosity it raises, it may in fact be beneficial in cases where the dispute in question raises broader tax (of fiscal) policy issues.

A. Arbitral Forums for Interstate Tax Disputes

There are several tested and non-tested forums for settling interstate tax disputes. To the degree that standardized procedures are emerging as a result of BITs and bilateral tax treaties (eg joint tax vetoes and MAPs), it is unlikely that states will consider new procedures and dispute resolution bodies. However, given that tax is a complex phenomenon that engages states and domestic policies at several levels, challenges against taxation is often multidimensional. A particular tax measure may adversely impact a foreign investor while at the same time enhance the socio-economic rights of a large under-privileged class. In equal measure, it may increase or decrease the creditworthiness of the state in question and in this regard it constitutes a foreign (fiscal) policy measure. Taxes, however, are seldom divorced from the state's foreign relations and obligations under general international law. A complex maze of free trade, trade liberalization and human rights agreements necessarily curtails the ability of the state to impose taxes without consideration of said obligations. What this means in terms of dispute resolution is that disputes over a particular tax measure are likely to engage various treaty regimes and by implication a variety of dispute resolution mechanisms. In the World Trade Organisation (WTO) context, for example, though the restrictions on tariffs (taxes on foreign goods upon entry) and internal taxes[76] in the context of trade liberalization treaties are meant to inhibit any undue advantages to similar domestic products (essentially by making the imported goods more expensive), the purpose in foreign investment law is to decrease the economic value of the investment in such a manner that its operation is no longer profitable to the investor. These two restrictions on the imposition of (arbitrary) taxes are over-arching and it is not unusual for concerned states to initiate proceedings under the WTO, subsequently followed by submission to investment arbitration.[77]

The dispute resolution bodies analysed in the following sections have dealt with interstate tax disputes, but as will become evident such occurrences are by no means frequent. Nonetheless, the post-2008 economic crisis and the reluctance of many developing nations to partake in the existing global financial architecture (eg through the creation of BRICS institutions) demonstrates that the unilateral imposition and collection of taxes, especially against private entities that have traditionally resisted

76 Trade liberalization encompasses tariff and non-tariff barriers. As far as the former is concerned, the term tariff is broad and includes practices such as duties, surcharges and export subsidies. Non-tariff barriers include licensing requirements, quotas and arbitrary standards, among others.

77 WTO, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, adopted on 24 March 2006; the same tax measures were subject to investment arbitration between *Cargill Incorporated v United Mexican States*, ICSID Case No ARB(AF)/05/2, Award of 18 September 2009 and *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas Inc v United Mexican States* (ICSID Case No ARB(AF)/05/05), Final Award of 21 November 2007.

them, such as MNCs, will become highly contentious and lead to the formation of distinct international legal regimes, even if resisted by most developed nations.[78] In this climate, states will view their tax policies as not merely an integral aspect of their self-determination, but more importantly as the single most important tool for their survival. It is evident that such disputes cannot satisfactorily be dealt by the regime of international foreign investment, or by the dispute resolution mechanisms encountered in BITs and bilateral tax treaties. At the first level, they require a holistic re-assessment of the existing global financial (and trade) architecture, followed by highly effective, persuasive and mutually agreed dispute resolution processes. This can only be achieved at the interstate level, perhaps through an international tax tribunal, or through existing mechanisms, enhanced by an expert tax chamber, such as the ICJ or the PCA. Consistency and uniformity is key to such a regime, which *ad hoc* arbitration is unable to satisfactorily deliver. No doubt, an appropriate body of substantive law must first be set out in clear and unequivocal terms before a robust procedural and enforcement corpus can be established. A consensus on such an international substantive law does not at present exist.

B. The International Court of Justice

The ICJ as a forum for litigating interstate tax disputes is not envisaged in bilateral tax treaties or treaties with a significant tax dimension. By way of illustration, in the event of interstate disputes arising from the ECT, Article 27 thereof provides for *ad hoc* arbitration. The ICJ could certainly play a distinct role in settling tax disputes with a strong policy dimension (eg abusive transfer pricing), but perhaps it is felt that it is a 'strict' mechanism with little expertise in international tax law, or that its processes are far too slow. These arguments are not without merit. It would perhaps go too far to argue that unlike the ICJ whose procedures are transparent a distinct advantage of *ad hoc* arbitration is its preservation of confidentiality. This is because constitutional guarantees demand that all actions of the state (other than military affairs) are transparent and known to the public.[79]

In practice, although no tax dispute has been directly submitted to the jurisdiction of the Court, the legality of certain taxes or charges has indirectly been called into

78 MNCs will demand investment in exchange for lower taxes, while home states will enforce lower tax agreements between host states and MNCs. At the same, the peoples of host states will demand fairer systems of taxation that allow the highest attainable standards of living. The two demands clearly conflict and the states involved cater to distinct stakeholders and interests. Where states cater to the demands of investors alone we have what is known as a 'race to the bottom'.

79 In *BCB Holdings Ltd and Belize Bank Ltd v Attorney-General of Belize*, [2013] CCJ 5 (AJ), a newly elected Belize government repudiated a tax concession granted to a group of companies by means of a settlement deed negotiated by its predecessor. The concession had not been approved by the Belize legislature, was confidential (hence non-transparent) and was manifestly contrary to the country's tax laws. The successor government repudiated the concession and the private parties achieved an arbitral award for damages they subsequently sought to enforce in Belize. The Caribbean Court of Justice upheld the argument that government's claim that the violation of fundamental constitutional rules and the interests of the people of Belize dictate that the award in question violates Caribbean and international public policy. Public policy should be assessed by reference to 'the values, aspirations, mores, institutions and conception of cardinal principles of law of the people of Belize' as well as international public policy. The tax concession could only be considered illegal if it was found to breach 'fundamental principles of justice or the rule of law and represented an unacceptable violation of those principles'.

question. Hence, unlike other forms of interstate arbitration which have predominantly concerned double taxation, the ICJ has been employed, albeit sparingly, with a view to assessing discriminatory or unlawful taxes. The legal basis for submitting such disputes has been treaties of friendship and navigation (TFN), the forerunners to modern BITs. In *Costa Rica v Nicaragua* [*Dispute regarding navigational and related rights*][80] the dispute concerned the parties' right of navigation on the San Juan river based on a 1858 Freedom of Navigation Treaty. Article VI of the Treaty stated that the parties were not allowed to unilaterally impose any taxes on the vessels of either nation. The ICJ held that Nicaragua could curtail certain navigational rights of Costa Rican citizens, but this must not violate Article VI of the Treaty.[81] Costa Rica requested the Court to declare that Nicaragua has an obligation not to impose any charges or fees on Costa Rican vessels and their passengers for navigating on the river.[82] The Costa Rican claim related to payments required in respect of departure clearance certificates for vessels and visas and tourist cards for passengers. According to Nicaragua, these were not payments for navigating on the river, but for the service involved in the issuance of the various documents. In 1982, Costa Rica protested against the imposition of a charge for the issuing of a departure clearance certificate as a tax that is excluded by Article VI of the Treaty. In a later exchange, in 2001, Nicaragua contended that the sum being charged was:not for navigating the San Juan River, nor does it constitute any type of tax, but is, rather, the amount charged for providing the departure clearance certificate service that both Nicaraguan and foreign vessels in any Nicaraguan port, including those located in the said river, are charged when travelling to another State.

The ICJ concurred with the Costa Rican position as follows:

> 122. In the Court's view, the final sentence of Article VI has two elements. It first confers a right on the vessels of each Party to land on the bank of the other. Second, that sentence provides that the exercise of that particular right is not to be the subject of an impost or tax. Just as the exercise of the right of navigation on the river is to be free and not the subject of any payment, so is stopping on the other bank. The Court does not read the provision as extending beyond that particular situation and as prohibiting charges for services lawfully and properly required by Nicaragua and rendered to vessels navigating on the river.
> 123. The Court now turns to the issue raised by Costa Rica in its correspondence with Nicaragua in 2001 (see paragraph 120 above): what is the service being rendered for the certificate and the charge. As the Court understands the situation, Costa Rica does not challenge the right of Nicaragua to inspect vessels on the river for safety, environmental and law enforcement reasons; as noted, it accepted it in respect of drug trafficking in 1997. In the Court's opinion, that right would in any event be an aspect of Nicaraguan sovereignty over the river. But those actions of policing by the sovereign do not include the

80 (2009) ICJ Rep 213.

81 ibid, paras 87 and 93.

82 ibid, para 120.

> provision of any service to boat operators. In respect of Costa Rican vessels exercising freedom of navigation on the river, the payment must be seen as unlawful.

In the only other case where tax measures were discussed by the Court, the *Electronica Sicula* [ELSI] case,[83] a very minor tax issue arose, but to which the ICJ paid almost no attention. Essentially, the disputing parties' TFN treaty provided for national treatment (including in tax matters) and the USA argued that Italy had breached that obligation. The Court did not consider that less favourable treatment had been offered to the US company in Italy, given that at the crucial time the contested tax practices were routinely imposed against Italian companies.

These two cases by no means circumscribe the potential of the ICJ in dealing with interstate tax disputes. The *lex specialis* nature of international tax law seems to suggest that general international law will not, or cannot, apply in most tax disputes. However, this suggestion is rather theoretical and has not been tested in practice. By way of illustration, would a Nyerere-style doctrine of unilateral tax repudiation, or the invocation of defences such as necessity, fundamental change of circumstances, right to development (or similar human rights arguments) be antithetical to the *lex specialis* character of international tax law? If not, which is this author's contention, then the ICJ, rather than an investment tribunal would constitute the ideal forum. This argument is further enhanced by the fact that unlike the alleged fragmented nature of investment arbitration there is no compelling argument that international tax policy (that impacts on the core attributes that bind a state to its people and the state to the international community) is equally fragmented from general international law. Such a proposal would certainly be enhanced by a holistic attempt by the ILC to draft a multilateral treaty on unilateral tax competences, clearly circumscribing the place of such competences within the general framework of general international law.

C. The Court of Justice of the European Union

Direct taxes fall outside the competence of the Union and the CJEU does not, as a result, possess jurisdiction over the interpretation of bilateral tax treaties because these are not part of EU law.[84] Matters relating to the regulation and elimination of double taxation fall within the exclusive competence of the EU member states which are free to enter into bilateral and multilateral tax agreements.[85] Be that as it may, the CJEU has demanded that double taxation treaties and their corresponding implementing laws be amended to conform to EU law (where pertinent).[86] Naturally, the

83 *USA v Italy* [*Elettronica Sicula* case] (1989) ICJ Rep 15.

84 The only exception relates to VAT because this is an EU tax measure and hence is subject to EU law and the EU Charter of Fundamental Rights. See B Terra and P Wattell, *European Tax Law* (6th edn, Kluwer 2014).

85 Case C-336 *Mr and Mrs Robert Gilly v Directeur des Services Fiscaux du Bas-Rhin* [1998] ECR I-2793, point 24; Case C-307/97 *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt* [1999] ECR I-6161, point 56.

86 See Case C-385/00 *F W L de Groot v Staatssecretaris van Financien* [2002] ECR I-11819, points 84, 94, 99ff; Case C-58/01 *Oce Van den Grinten NV v Inland Revenue Commissioner* [2003] ECR I-9809, point

CJEU can assess tax-related measures as these affect rights and freedoms stipulated in the Treaties. In three recent joined cases the CJEU addressed the compatibility of double taxation treaties with the freedom of establishment. Two of the cases before the CJEU involved the imposition of a Dutch dividend withholding tax levied on individual shareholders in Dutch companies, whereas in the third, the withholding tax was levied on a French bank.[87] The CJEU held that the parties' double tax treaty obligations could possibly justify the difference in treatment between cross-border and domestic situations in the Netherlands. However, in respect of the *X* case, it was held that since Belgium unilaterally grants a set-off for the Dutch withholding tax, the Netherlands could rely on the Netherlands-Belgium tax treaty to claim that it has neutralized the restriction in question. In respect of the *Société Générale* case, the outcome was different because the set-off under the Netherlands-France tax treaty was not granted unilaterally. In this case, the Netherlands could rely on the elimination of double taxation under the treaty, but only if the full amount of the tax on dividends paid in the Netherlands actually had been neutralized in France.[88]

EU member states may of course grant the CJEU jurisdiction over tax treaties by mutual agreement. Article 273 (former 239) of the Consolidated Version of the Treaty on the Functioning of the EU gives this right to states who can use the CJEU as an arbitral tribunal (solely interstate). This is to be achieved by mutual agreement between two or more disputing states. The 2000 Double Tax Treaty between Germany and Austria conferred such jurisdiction on the CJEU.

However, the empowerment of the CJEU as an arbitral tribunal is problematic where its subject-matter jurisdiction is constricted by a submission agreement that prevents it from having recourse to general international law and fundamental rights. In such an eventuality the Court would be reduced to an *ad hoc* arbitral institution,[89] and its bench would be forced to dismiss the application of otherwise fundamental principles of EU law and justice.

D. Free Trade Agreement Tribunals

The CJEU is a very particular FTA tribunal and was examined in isolation of others because of the all-embracing nature of EU law. In a previous section, we examined how the MERCOSUR tribunal possesses jurisdiction to examine interstate tax disputes between its Member States. This jurisdiction arises from the founding MERCOSUR treaty.[90]

However, as we have already seen, the jurisdiction of FTA tribunals may arise not only by their founding treaties but also by reference to a treaty establishing some

54; Joint Cases C-397/98 and C-410/98 *Metallgesellschaft Ltd and Others, Hoechst AG and Hoechst (UK) Ltd v Commissioners of Inland Revenue and HM Attorney-General* [2001] ECR I-1727, point 71ff.

87 Joined Cases C-10/14, C-14/14 and C-17/14 *J B G T Miljoen, X and Société Générale v Staatssecretaris van Financiën* OJ C 371 (2015) 6-7.

88 See Deloitte, CJEU Rules on Dutch Dividend Withholding Tax Cases <http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-europeanunion-18-september-2015.pdf> accessed 10 January 2017.

89 It should be pointed out that proposals have been made for the CJEU to assume jurisdiction over the interpretation of the EU Arbitration Convention. This has never materialized. See CHJI Panayi, *European Union Corporate Tax Law* (CUP 2013) 73.

90 See nn 43–45.

type of economic activity, such as the WAGP Agreement, which concerned the construction and operation of oil and gas pipelines. Specifically, in accordance with Article XI of the WAGP Agreement interstate disputes are to be resolved by reference to the ECOWAS Court of Justice and alternatively by the WAGP Committee of Ministers (Article X(2)(d)). In this case, the ECOWAS Court acts like an arbitral tribunal because it is mandated to apply the governing law of the contract (namely, that which is stipulated in the Agreement and the subsequent private contracts between the implementing states and the private contractors). The choice of FTA tribunals in such cases, although certainly not the rule, is viewed as an intermediate solution between domestic courts (the states' choice) and investment tribunals (the private parties' choice). This means that that proliferation of FTA referral clauses in treaties, as supplemented by private implementing agreements, will depend on whether regional FTAs are perceived as fair, unbiased and speedy by investors and home governments.

E. The Prospect of an ITT

The establishment of a permanent ITT has been debated manifold in the past and governments and scholars are still deliberating on how best it may be employed, despite the practical issues involved. Altman, for example, suggests that the creation of an ITT would give non-binding opinions to domestic courts and in the process provide some degree of coordination to the interpretation of tax treaties.[91] He goes on to say that almost 60% of cross-border tax disputes concern transfer pricing and hence because such disputes require extensive fact-finding and neutrality, arbitration is the best method. For double tax disputes a permanent ITT more than suffices.[92]

Indeed, an ITT with jurisdiction over interstate tax disputes would require some degree of compulsory jurisdiction and given the problems of competing jurisdiction which many international courts and tribunals face nowadays,[93] any submission agreement thereto should specifically exclude the jurisdiction of other international tribunals, unless the dispute in question encompass also non-tax-related matters. Even so, there is no reason why an ITT would not be able to provide adequate responses to non-tax-related disputes, especially if these stem from taxation measures. However, it is not at all clear that international tax disputes will be resolved in the same way by an ITT and investment tribunals or the ICJ. The likelihood of incoherency and non-uniformity is significant, particularly since each tribunal (and its individual members) view tax from a wholly different lens.

Moreover, it is not totally clear whether such an ITT should operate on the basis of referrals by domestic courts, in which case the local court's decision will be greatly influenced by the demands of the private party to the dispute, or whether its jurisdiction should be triggered by state entities only. If one looks up to the CJEU referral paradigm it is obvious that had it not been for this system EU law would have been far less advanced than it is now and national institutions would lack uniformity in their application of EU law. States are less likely to initiate recourse to a dispute

91 ZD Altman, *Dispute Resolution under Tax Treaties* (IBFD 2006) 431ff.

92 ibid 432.

93 See generally, Y Shany, *The Competing Jurisdictions of International Courts and Tribunals* (OUP 2004).

settlement mechanism and hence national court-based referrals seem to be the most prudent option.

6. LEGITIMACY AND PUBLIC INTEREST IN INTERSTATE INTERNATIONAL TAX ADJUDICATION

It has been argued that international adjudication is a 'law-based way of reaching a final decision' and that the 'law-based nature of adjudicative decision-making distinguishes adjudication from other processes, such as political decision-making and mediation'.[94] Two legitimacy-based approaches have been advanced in the literature and these have been adapted in turn to explain the concept of judicial legitimacy from the perspective of international law, namely: sociological (or descriptive) and normative legitimacy.[95] The sociological approach is chiefly concerned with the perception of legitimacy ascribed to a particular judicial institution, whereas the normative approach investigates whether such institution deserves to be regarded as authoritative (or whether its authority is justified). It is evident that both approaches are predicated on external perceptions by relevant constituencies. A court that makes a claim for normative legitimacy is effectively arguing for the 'right to rule', whereas a claim of sociological legitimacy is perceived as already having that right.[96] Normative legitimacy is prescriptive, whereas sociological legitimacy is agent-relative and subjective.[97] Judicial legitimacy, particularly in the sphere of international law, is inextricably woven around the concept of authority, which ultimately dictates adherence, obedience or even disobedience. Because of the horizontal nature of international law and the juridical equality of states, which itself is based on consent, the legitimacy of domestic courts is different to (as is also its origin) their international counterparts. The source of authority, for example, is directly affected by perceptions as to the legitimacy of the source itself (eg the UNSC as creator of tribunals in countries where the UN has allowed grand massacres to take place). In contrast, acts of parliament (or the constitution itself) from which regular courts derive their creation are not under dispute. The same is true of the processes employed by an international tribunal in exercising its powers, as well as the overall outcomes such processes produce.

This article takes the view that irrespective of the source of authority of an interstate tax-related adjudicatory mechanism, chiefly arbitration, its legitimacy is guaranteed only where its outcomes and processes are in the public interest. Public interest in the field of transnational tax encompasses a variety of affected stakeholders and ultimately affects the capacity of the state to generate revenue for the

94 CPR Romano, KJ Alter and Y Shany (eds), 'Mapping International Adjudicative Bodies, the Issues, and Players' in *The Oxford Handbook of International Adjudication* (OUP 2014) 4–5.

95 See eg C Thornhill and S Ashenden, 'Introduction: Legality and Legitimacy – Between Political Theory and Theoretical Sociology in *Legality and Legitimacy: Normative and Sociological Approaches* (Baden-Baden 2010) 7–12.

96 D Bodansky, 'The Concept of Legitimacy in International Law' in R Wolfrum and V Roben (eds), *Legitimacy in International Law* (Springer-Verlag 2008) 313; A Buchanan and R Keohane, 'The Legitimacy of Global Governance Institutions' in LH Meyer (ed), *Legitimacy, Justice and Public International Law* (CUP 2009) 29.

97 Bodansky, ibid 313.

benefit of its people as well as the objectives of fiscal self-determination.[98] However, one cannot artificially divorce source from processes and outcomes, because the source dictates the subject matter of such tribunals, which ultimately may restrict or expand their decision-making autonomy. States can no longer view tax solely from a domestic (sovereign) lens. Many activities are transnational and this in and of itself requires some degree of regulation and coordination at international level and a restriction to absolute tax sovereignty. The agreements explained in this article not only set out the substantive law in respect of conflicting tax regimes, but also the procedural framework for resolving tax disputes. The sole authority of national courts and tax authorities has come under intense legitimacy concerns, thus necessarily paving the way for alternative mechanisms of an international nature, namely investor–state tax-related arbitration, interstate ADR (particularly in respect of double taxation) and some forms of interstate arbitration, albeit in limited spheres of tax regulation. This process was clearly driven from pertinent stakeholders because of the absence of fair outcomes from the exclusive sovereignty paradigm.[99] Even so, the overall process is not necessarily in the public interest nor wholly legitimate. It should be emphasized that a significant degree of confidentiality is embedded in the MAP process and hence it is almost impossible to discern its effectiveness both for states as well as taxpayers.[100] The arbitration provisions to the OECD Model Tax Treaty were added after vociferous lobbying by the International Fiscal Association and the International Chamber of Commerce, both clearly serving the interests of businesses. Moreover, the arbitration process in both the OECD Model Tax Treaty and the EU Arbitration Convention allow for very limited publication of the final outcome and even the publication of a summary may be blocked by the taxpayers, thus bypassing the general requirement of transparency in the allocation and determination of tax. Such an outcome, although outwardly consistent with the otherwise confidential nature of the arbitral process and awards, is wholly antithetical with the transparency underpinning public finances and the public interest dimension of taxation.[101] If tax arbitration initiated by taxpayers is to be secretive and wholly outside the public domain, this cannot be in the public interest and the possibility of abuse is significant. Interstate arbitration can, or at least should, guarantee such transparency, if for no other reason as a matter of constitutional obligation.

98 Unlike the infusion of 'public interest' in other areas of interstate concern, such as foreign investment, this is generally unknown in international tax debates. See A Kulick, *Global Public Interest in International Investment Law* (CUP 2014).

99 Peters argues that the legitimacy of tax law (in the international sphere) varies with our changing perceptions of justice and society and will oscillate along 'the intricate balance between the authority of states to impose taxes in the international society and the moral, legal, political and economic limits to that authority'. C Peters, *The Faltering Legitimacy of International Tax Law* (2013) 7 <https://pure.uvt.nl/portal/files/1532460/Cees_Peters_-_The_faltering_legitimacy_of_international_tax_law_-_MANUSCRIPT_-_FINAL.pdf>.

100 AD Christians, 'Your Own Personal Tax Law: Dispute Resolution Under the OECD Model Tax Convention' (2009) 17 Willamette J Intl L & Dispute Res 172, 180.

101 The CJEU, for example, has long held that the protection of a taxpayer's secrecy versus the public' interest in tax matters may be counterbalanced by anonymized transcripts of the case. Case C-200/98 *X and Y AB* [1999] CJEU I-8261. For a critical outlook, see A Rovine, *Contemporary Issues in International Arbitration and Mediation* (Brill 2016) 449–50.

7. CONCLUSION

The emergence of investor–state and taxpayer–state dispute settlement mechanisms in the past 40 or so years has sidelined, and for good reason, the need for diplomatic protection in the field of transnational tax law. While this is welcome, in many cases it is cumbersome, slow and does not exhibit those qualities of arbitration as one generally expects from a dispute settlement mechanism desirous of arbitral processes and outcomes. The range of interstate tax arbitration analysed in this article is relatively sparse compared to MAPs and other forms of dispute settlement, but its underlying rationale seems to be as a reserve, residual mechanism that is to be made available in the event that all other mechanisms fail the pertinent stakeholders. In areas where taxpayers are not directly involved, as is the case with energy pipeline agreements, states naturally find it expedient to designate interstate arbitration in tax matters as their primary dispute settlement mechanisms, alongside ADR. Perhaps, the much awaited BEPS Action 14 will bring about a new era of tax arbitration that will improve the inefficiencies of the existing MAP system, unless tax arbitration, save for its true regulatory dimension,[102] assumes the qualities of ordinary arbitration (ie speed, independence), the MAP system will continue to be problematic. The tension whereby states seek to retain their right to adopt taxes and the right of citizens to be fairly taxed is always going to give rise to disputes. Besides the functions analysed in this article, interstate tax arbitration can counterbalance the cumbersome characteristics of the MAP and other mechanisms. If the key actors in interstate arbitration produce attractive outcomes to the liking of relevant stakeholders, then a move away from cumbersome procedures should not be discounted. But apart from interstate arbitration and its potential, if any, there is now significant competition from private arbitral institutions that see tax as a new and profitable expansion to their business portfolio. Ultimately, a hybrid system that combines: (i) the direct involvement of the taxpayer; (ii) the efficiency of institutional arbitration; and (iii) the transparency guarantees of interstate arbitration is the way forward.

102 See L Wandahl Mouya, *International Investment Law and the Right to Regulate* (Routledge 2016), who provide a survey of the trends of investment tribunals whereby the exercise of regulatory powers of the state is afforded significant primacy over other considerations.