

**BEPS Action 14 – The Effectiveness of the Dispute Resolution Proposals,  
with Specific Reference to South Africa**

A minor dissertation submitted in partial fulfilment for the requirements for the Master's degree in laws (international tax).

By

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Minor research dissertation presented for the approval of Senate in fulfilment of part of the requirements for the Master of Laws (LLM) specialising in International taxation and a minor dissertation paper. The other part of the requirement for this qualification was the completion of a programme of courses.

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# ***BEPS ACTION 14 –THE EFFECTIVENESS OF THE DISPUTE RESOLUTION PROPOSALS, WITH SPECIFIC REFERENCE TO SOUTH AFRICA***

## **1. INTRODUCTION**

### **A. Background**

The focus of this minor dissertation is on the dispute resolution methods proposed by Action 14 of the Base Erosion Profit Shifting (BEPS) Project. The BEPS Project<sup>1</sup> was introduced in 2013 by the OECD<sup>2</sup> working together with the G20<sup>3</sup> and other states to reform the international tax framework. The reform was necessary to deal with the challenges posed by globalisation. The existing international tax framework had not changed for many years and was unable to deal with these new challenges.

As stated by the OECD in its Explanatory Statement in 2013, there was a need to build an international tax system to support economic growth and a resilient global economy.<sup>4</sup> The report highlighted that the loss to international corporate income tax caused by these challenges was between 4% and 10% of global corporate income revenues<sup>5</sup>.

As part of the proposed reforms, the report highlighted the need for new measures to address the problem of BEPS as well as provide a structure to support these newly introduced measures. Improving the international dispute resolution mechanisms was identified as an essential structural reform to support the new BEPS measures, as it was anticipated these measures would give rise to more inter-State disputes.

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<sup>1</sup>OECD(2015)/, Making Dispute Resolution Mechanisms More Effective, Action 14 -2015 Final Report,OECD/ G20 Base Erosion and Profit Shifting Project , OECD Publishing Paris.  
<http://dx.doi.org/10.1787/9789264241633-en> accessed 10 June 2019.

<sup>2</sup> OECD Organisation of Economic Co-operation and Development, an international organisation of 37 member countries formed after world war two as part of the Marshall plan to rebuild Europe. Its aim is to promote economic prosperity.

<sup>3</sup> G20 An international forum of 19 governments and central bank governors and the European Union who meet annually to discuss important issues in the global economy.

<sup>4</sup> OECD (2015), Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project, OECD.  
[www.oecd.org/tax/beps-explanatory-statement-2015.pdf](http://www.oecd.org/tax/beps-explanatory-statement-2015.pdf) (accessed 10 June 2019).

<sup>5</sup> Ibid at 4 para 2.

Dispute resolution is covered in Article 25 of the OECD model tax treaty network and provides for a mutual agreement procedure (“MAP”) to resolve disputes between states. The treaty network is a combination of international agreements which follow either the OECD or United Nations model treaty, aimed at the avoidance of double taxation. The OECD model is the most popular treaty, favoured by developed countries, followed by the UN Model (based to a large extent on the OECD model), which tends to be favoured by developing countries. All of these treaties include a dispute resolution clause, generally based on Article 25 of the OECD model.

There are approximately three thousand double tax treaties in operation internationally, each with dispute resolution clauses. Despite the proliferation of tax treaties, it is interesting to note that Article 25 is the only dispute mechanism available.

Brian J Altman in the introduction to his book, *Dispute Resolution under Tax Treaties*, (2006)<sup>6</sup> notes that the original intention behind trade and tax treaties was to reduce trade barriers. He goes on to note that the dispute resolution mechanisms under trade treaties evolved a lot more rapidly than those under tax treaties, as the former provide compulsory binding resolutions and use trade sanctions as an enforcement aid.

Dispute resolution mechanisms under tax treaties, on the other hand, have not developed at the same rate and in the same manner. Whilst it would make for an interesting study to delve further into the different types of dispute resolution, that is not the purpose of this research; suffice it to note that there are other mechanisms in international law than those under tax treaties to resolve inter-State disputes.

One of the major criticisms of dispute resolution in international tax is the lack of a central institution to deal with disputes collectively. Comparisons are made with the European Union (“EU”<sup>7</sup>) and its European Court of Justice<sup>8</sup> (“ECJ”), as well as the International Court of Justice<sup>9</sup> (“ICJ”). Proposals have been made to utilise the ICJ to settle international tax disputes. In 1949, the Netherlands suggested to the UN that the ICJ should be used to settle international tax disputes<sup>10</sup>. This was rejected at the time, as the view was that resolution was best left to contracting parties and further that it would not be fitting to permit taxpayers access to the ICJ.

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<sup>6</sup> Brian J Arnold, *An introduction to Tax Treaties* (United Kingdom 2015) 1.

<sup>7</sup> European Union is a group of 28 countries based in Europe working towards common goals.

<sup>8</sup> Court of Justice of the European Union, its mandate being to ensure that EU laws are applied consistently by all member states.

<sup>9</sup> International Court of Justice is the principal legal organ of the United Nations, mandated to settle international disputes referred by States and provide opinions.

<sup>10</sup> Altman op cit 6 at Chapter 1, para 1.3.1.3, p 28.

In 2013, the OECD and G20 appear not to have considered this as an option, given their Action 14 measures.

### **B. Research question**

This dissertation seeks to answer the following question –

‘How effective are the measures proposed in Action 14 of the BEPS Project and adopted by the OECD and G20, specifically from a South African perspective?’

This question raises the following subsidiary questions:

- Does Action 14 improve existing international dispute resolution measures?
- How effective has South Africa been in resolving disputes after introducing Action 14 measures in the international tax sphere?
- What, if any, changes need to be implemented to improve the effectiveness of international dispute resolution?

### **C. Research method**

The research method used to answer the questions posed above involves obtaining a clear understanding of the nature and extent of the measures contained in Action 14. Thereafter identifying a suitable benchmark which can be used to evaluate these measures, which in this instance has been identified as the rule of law. The benchmark will then be applied in the abstract to the measures, followed by an evaluation of South Africa’s implementation of the measures. It is hoped that this will then result in a finding of the effectiveness of the BEPS Action 14 measures.

### **D. Benefit**

It is hoped that the findings will reveal where and how the dispute resolution measures adopted in Action 14 assist in resolving international tax disputes. It is one thing to have an extensive network of treaties, the aim of which is to prevent double taxation, if there is no adequate or effective dispute resolution method to resolve instances of double taxation.

It is anticipated that the adoption of BEPS will result in an increase in international disputes. It is important that the dispute resolution process can effectively deal with an increase in disputes.

It is hoped that the findings can highlight where Action 14 needs to be modified, which would benefit both taxpayers and States who are tasked with resolving these disputes.

### **E. Chapter outline**

As a starting point, Action 14 will be reviewed in detail in Chapter 1 from an objective standpoint. Chapter 2 will focus on establishing an adequate measure of effectiveness. Measuring effectiveness is not a simple binary exercise; it involves both objective and subjective criteria.

Chapter 3 will apply the methodology identified in Chapter 2 to the action 14 measures from a theoretical standpoint. Thereafter Chapter 4 will assess how South Africa has interpreted and applied Action 14. This will involve analysing how South Africa has adopted and incorporated the dispute resolution provisions into its treaty network, and whether these provisions measure up to the standard identified in Chapter 2. South Africa has been duly subjected to its peer review in this regard; the peer review report was released in May 2019 and will be referred to as an indicator of South Africa's performance.

It is hoped that the assessment in Chapter 4 will serve to highlight the efficiencies of Action 14 as well as any inherent inefficiencies.

In conclusion, the efficiencies of Action 14 can be seen as a useful indicator of whether the international dispute resolution framework meets the needs of the global community in dealing with the challenges posed by BEPS. Ultimately the importance of an effective dispute resolution framework is vital to ensure that the spirit and intention of the international tax treaty network is maintained.

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## 11. CHAPTER 1 ACTION 14 MEASURES

### A. Action 14 –General observations

BEPS Action 14 is designed to improve the dispute resolution procedures contained in tax treaties. Dispute resolution is included in most tax treaties in Article 25. The model Article 25 provides a remedy to both taxpayers and contracting States in the form of a mutual assistance programme (“MAP”, an abbreviation which can also stand for ‘mutual assistance procedure’). The remedial action provided for, aims to address disputes arising from the application of a treaty as well as cases where there are interpretative issues arising from the treaty itself. The overriding aim of the article is to prevent the imposition of any tax which is not in accordance with the particular treaty.<sup>11</sup> In essence, Action 14 attempts to improve the application of such remedial action.

MAP provisions have formed part of the OECD Model Convention since its inception, i.e. 1963. The most significant change (prior to Action 14), occurred in 2008, when the OECD consented to add a paragraph 5 to Article 25.

This addition provided for the option of arbitration as an additional tool to resolve disputes. It is suggested that this move to include arbitration as a further remedial action in tax disputes, was to reflect the increasing reliance internationally on arbitration as an alternative remedy to resolve disputes in general

Article 25, prior to the amendments introduced by Action 14, was couched in general terms. It is suggested that this was due to the consideration that treaties, being part of international law, and acknowledged as “soft” law, cannot be prescriptive as to how States deal domestically with disputes. It also acknowledged the sovereignty of an individual State’s remedial provisions within its domestic law.

Remedies contained in domestic tax law do not automatically apply to resolving disputes arising from the application of tax treaties. MAP operates independently of domestic remedies and applies to a dispute that is between States, but initiated by a taxpayer. The aim of MAP is to ensure the proper application of a treaty, both in interpretation and application. The outcome

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<sup>11</sup> OECD Income and Capital Model Convention and Commentary (2008), commentary on art 25 paragraph 1 and 2, at para 7. <https://research-ibfd-org.ezproxy.uct.ac.za> accessed July 2019.

of a successful MAP should result in the taxpayer being taxed in accordance with the relevant treaty.

Action 14 recognized that there were weaknesses in the MAP and therefore aimed at strengthening these weaknesses, hoping to make MAP more effective. The focus is on providing certainty, arising from the proposals adopted in the other actions as well as providing a framework for the speedy resolution of disputes.

The final report identified two main obstacles, namely that access to MAP may be denied and the lack of arbitration clauses in most treaties. Specific measures have been identified as a means to address these obstacles in the MAP provisions of a tax treaty and emphasise the commitment by the contracting States to implement a minimum standard to prevent these obstacles from arising.

Action 14 has a two-pronged approach, namely amending Article 25 along with providing for actions that will enhance the effectiveness of the amended Article 25. These actions will be provided for by amending, where necessary, the commentaries on Article 7<sup>12</sup>, 9<sup>13</sup> and 25. In addition to these two reforming aspects, a third is proposed in the form of a peer review system, to ensure the continued improvement and enhancement of the MAP system.

The BEPS action plan proposed amendments to the existing treaty network. As mentioned earlier, there are over three thousand double tax treaties in existence. To amend these mainly bilateral treaties is a lengthy process, requiring negotiations between contracting States. In order to ensure that the measures proposed in the BEPS action plan were swiftly incorporated into the existing treaty network, Article 15 of the plan proposed that the amendments be incorporated through a multi-lateral instrument (“MLI”)<sup>14</sup>.

The MLI allows contracting States to swiftly amend their treaties in line with the BEPS action plan. The MLI was signed by seventy States in June 2017, committing them to implement the changes proposed in the BEPS action plan. Article 15 sets out the fourteen actions, by reference to specific articles, and how these actions will be incorporated into the existing treaty network.

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<sup>12</sup> Article 7 of the model treaty deals with the taxation of business profits arising from a permanent establishment.

<sup>13</sup> Article 9 of the model treaty deals with the arm’s length principle in relation to associated enterprises.

<sup>14</sup> Multi-Lateral Instrument, which means a multilateral treaty which enables jurisdictions to swiftly modify their existing bilateral treaties to incorporate the BEPS Action Plan. ....  
<https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm> accessed on 9 July 2019.

In addition, Article 15 specifically lists which items States can elect to be bound by, which articles are not negotiable and how the changes are to be ratified. South Africa is one of the seventy States that signed the MLI. It is hoped that government will ratify the MLI early in 2020.

It is important to note that a State has the right to elect how it incorporates the changes to the model Article 25 (1) and Article 25(5) into its treaties and which treaties will be affected. Prior to signing the MLI, each State was required to indicate which of its treaties were to be “covered” by the MLI, meaning the treaties to which the MLI was to apply, and what reservations and options it was making or electing to adopt (where the article was capable of reservation or election). The MLI has therefore given legal effect<sup>15</sup> to the changes that the BEPS action plan identified as essential to prevent base erosion and profit shifting.

The actions provided for, on the other hand, will not have the force of law, as they are merely included in the Commentaries to the OECD Model Convention.

The actions contained in the report are threefold, namely:

1. Minimum standard on dispute resolution;
2. Best practices; and
3. Effective monitoring mechanism.

## **B. Article 14 -Minimum Standard**

Agreement was reached between all OECD Countries, G20 Countries and countries on the minimum standards contained in Action 14, which collectively constitute one Minimum Standard.

These standards are guided by three objectives. Minimum standards are contained within each stated objective, the detail of which is set out below. The implementation of some of the standards requires amendments to the existing model convention. This will be indicated where appropriate.

The minimum standards are objective in nature in order to ensure that they are capable of peer review. The report takes the view that the minimum standards will only be fully effective where

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<sup>15</sup> The MLI must be ratified domestically, before it can be said to have legal effect.

States adopt mandatory binding arbitration. States have the option of electing to include mandatory arbitration in their treaties.

The three objectives are set out below; within each objective, the specific actions are addressed.

**i). Objective: States to ensure that treaty obligations in relation to article 25 are fully enacted in good faith, and in a timely manner.**

*Action 1*

*States should include paragraphs (1) to (3) of Article 25 in all their treaties. In applying these articles, States should refer to the Commentaries, to ensure consistency in application and that effect is given to the correct interpretation.*

Applying the objectives to the standard, it is submitted that the meaning of “fully enacted in good faith“, is, firstly, that States should not exclude parts of paragraphs 1 to 3 when enacting Article 25 in their treaties. This would ensure that when States are attempting to resolve a dispute, they will be governed by the same minimum standard in the MAP process. Access to MAP should be consistently applied.

In addition, the reference to good faith implies that States should be guided by the overarching goal of the treaty, being the avoidance of double taxation. There could be a tendency for States to attempt to protect their own tax base when engaged in MAP, at the expense of the obligation to avoid double taxation.

The report<sup>16</sup> in its reference to the Commentaries makes specific reference to the Commentary<sup>17</sup> on Article 25 in paragraph (55), which deals with paragraph (3) of Article 25. It confirms that para (3) entitles a State to use MAP to deal with double taxation which doesn't come within the scope of the treaty. For example, on transfer pricing adjustments, where the taxpayer is resident in a third State, and profit allocations are made to two permanent establishments, MAP should be used to relieve the incidence of double taxation, thereby ensuring the effective utilisation of MAP to resolve double taxation. To deny access to MAP in this instance, which has resulted in economic double taxation, would be contrary to the aims of the treaty. The Commentaries acknowledge that in certain instances, a State's domestic law will prevent it from applying the MAP. They suggest Protocols are used to

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<sup>16</sup> Op cit 1 at 13 para 10.

<sup>17</sup> Op cit 11

resolve this sort of impasse. The report<sup>18</sup> further recommends that States should provide access to MAP in all transfer pricing cases.

The reference in the objective to resolution in a timely manner, takes cognisance of the reference in para 5 of Article 25 of the need resolve disputes within two years from date of receipt of the case. This is to ensure that disputes are resolved speedily, in line with the maxim that ‘justice delayed is justice denied’.

#### *Action 2*

*States should grant access to MAP in cases where the State and the Taxpayer disagree over whether the anti-abuse provisions of the treaty apply; or whether the domestic anti-abuse provisions are in conflict with the treaty*

This is premised on the basis that there should not be a blanket refusal to deny access to MAP in anti-abuse cases. The report<sup>19</sup> makes the comment that by granting access to MAP, a State is not agreeing to resolve the issue per se, but is simply giving taxpayers the opportunity to present their case. Provided the threshold for MAP in paragraph (1) of Article 25 has been met, the State should grant access to MAP.

It is submitted that the ‘good faith’ part of the objective requires the State to objectively apply the threshold test and not to prejudge a taxpayer’s case. If it is the intention of a State to deny MAP access in cases of anti-abuse, it should expressly state its position to its treaty partners and further, the contracting States should agree to notify each other in such instances.

#### *Action 3*

*States should commit to a timely resolution of MAP cases.*

The average time taken should be two years. However, this may vary, depending on the complexity of the case.

#### *Action 4*

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<sup>18</sup> Op cit 1 at 14, para 11.

<sup>19</sup> Op cit 1 at 14 para 14.

*States should develop their competent authority relationships, and work together to improve the effectiveness of MAP by joining the Forum on Tax Administration MAP Forum (FTA MAP Forum).*

The FTA MAP Forum is a multilateral strategic plan to improve the MAP process on an ongoing basis and to meet the needs of both taxpayers and States. The FTA MAP Forum monitors the implementation of the minimum standards provided for.

*Action 5*

*Timely reporting in accordance with an agreed timeframe as required by the FTA MAP Forum.*

The OECD has been collecting data on MAP statistics since 2006. These reports provide a comprehensive view of MAP status internationally. With the introduction of these minimum standards, it is anticipated that the reports will be able to reflect on the efficiency of these standards and where they need to be improved upon.

*Action 6*

*States to be subjected to peer review of their compliance with the minimum standards.*

States should agree to peer review, as part of their objective to implement and apply MAP in good faith.

*Action 7*

*States to be transparent in respect of their positions on MAP arbitration.*

It is submitted that this is an additional ‘good faith’ aspect of the objective, aimed at ensuring that States are up front about why they either agree to arbitration or choose not to adopt arbitration. In the Commentaries<sup>20</sup> and a footnote to para (5) of article 25 in the 2008 version, it was recognised that arbitration may be disallowed by a State’s domestic law or policy considerations. As such it was not required for States to note their positions on arbitration.

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<sup>20</sup> Op cit 11 para 65.

However, it is now regarded as a minimum standard for a State to be transparent with regard to its position taken on arbitration, given the context of mutual agreement procedures and the requirement of good faith, which should underpin all negotiating. The report<sup>21</sup> proposes that paragraph (5) of Article 25 be amended in accordance with this minimum standard and further that paragraph (65) of the Commentary on Article 25 also be amended to reflect this change.

**ii). Objective: States to ensure that administrative processes are in place domestically that promote the prevention of disputes and their timely resolution where disputes occur.**

*Action 1*

*States should publish rules and guidelines on MAP for Taxpayers.*

States should endeavor to make access to and the use of MAP as simple as possible for taxpayers. Guidelines should be placed on a public platform which Taxpayers can easily access.

*Action 2*

*States should publish MAP profiles on a shared public platform.*

A MAP profile would typically provide contact details of the Competent Authority and other useful information relating to MAP. It is proposed in the report that a specific MAP template be developed in conjunction with the FTA MAP Forum. What is intended is to provide transparency with regard to an individual State's MAP profile.

This standard is intended to practically address the objective of timely resolution and prevention of disputes by ensuring that taxpayers pursue only legitimate MAPs and direct them to the correct person, thereby reducing delays for both States and taxpayers.

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<sup>21</sup> Op cit 2 at 17 para 23.

*Action 3*

*States should assign dedicated personnel to the MAP process with the specific task of resolving disputed objectively.*

States are required to ensure that their internal governance procedures do not limit MAP staff in terms of their authority to objectively evaluate MAP applications. This would entail delegating to staff the authority to independently consider MAP cases, without having to defer to other personnel within the administration who would have been exposed to the case at a domestic level. In other words, the review and decision-making process on MAP matters must be done objectively and not tainted by staff who may have previously been exposed to the case, for example audit staff. In addition, MAP personnel should not be subjected to influence from policy-makers within the administration.

This insistence on objectivity ensures that disputes are evaluated fairly and consistently, without undue influence from other role-players who may have agendas other than compliance with the objectives of the treaty.

*Action 4*

*Evaluation of MAP personnel should reflect the objectives of Action 14.*

The report<sup>22</sup> emphasises the need for MAP personnel's performance to be reviewed on a basis that reflects and promotes the objectives of Action 14. It warns against using domestic criteria that advance the agenda of the administration, like increased revenue and the number of audit adjustments.

It is proposed that objective factors like the number of MAP cases resolved, consistency in dealing with them and time taken to resolve MAP cases, should rather be used to evaluate MAP personnel. These objectives are in line with the objectives of Action 14 as set out above.

*Action 5*

*States should allocate sufficient resources to MAP functions.*

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<sup>22</sup> Op cit 2 at 19 para 28.

This is relatively self-explanatory and makes sense, if the objectives of MAP are to be achieved.

*Action 6*

*States should clarify access to MAP where their domestic legislation provides for settlement of tax issues.*

The minimum standard requires each State to clarify for taxpayers and treaty partners its position on MAP where settlements are involved. It is submitted that audit settlements between taxpayers and administrations should not preclude access to MAP.

Where, however, domestic legislation allows taxpayers to request settlement independently of the audit process, the report<sup>23</sup> acknowledges that States may limit access to MAP where matters are settled through this process. However, States should notify their treaty partners and further clarify their position in their MAP guide. This would ensure that both treaty partners and taxpayers are aware of a State's position prior to making a decision on which remedy to utilize.

In cases where matters are settled independently (as in South Africa), it is submitted that the personnel evaluating the settlement should as a matter of course consider the issue of whether that settlement is in accordance with the relevant treaty. There are policy issues at stake in this minimum standard; whichever way a State elects to proceed, it should be governed by the overriding treaty objective, which is the avoidance of double taxation.

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<sup>23</sup> Op cit 2 at 19 para 27.

*Action 7*

*States with Advanced Pricing Arrangements (“APA”) should provide for “roll back” of APAs where appropriate.*

It is envisaged that where APAs are agreed that are relevant to prior tax years, States should attempt to apply the APAs to the prior years, in an attempt to prevent transfer pricing disputes.

This minimum standard acknowledges that domestic legislation may have prescription clauses that prevent roll back in certain cases. In addition, where MAP is requested in respect of prior years, the time frame for MAP access in Article 25 would apply. It is submitted that as an anti-abuse method where downward adjustments are made, the State should notify its treaty partner to avoid double non-taxation.

**iii). Objective: States to ensure that taxpayers who meet the minimum threshold of Article 25(1) can access MAP.**

*Action 1*

*Both competent authorities should be made aware of MAP requests and be given the opportunity to allow interested parties to express views on the request. This would entail giving the taxpayer the option of approaching either State.*

The aim of this proposal is make MAP as widely accessible as possible and to provide flexibility to the taxpayer.

*Action 2*

*The MAP guidelines should specify what information the taxpayer is required to include in a MAP request.*

States should not deny access to MAP simply because the taxpayer has failed to submit all the information required. The FTA MAP Forum will provide guidance on what information is required.

*Action 3*

*States should agree to implement MAP agreements, irrespective of any time prescripts in domestic legislation. This entails an amendment to para (2) of Article 25.*

It is suggested that where States cannot agree to the above amendment, they rather amend their bilateral treaties, specifically Article 9 (1)<sup>24</sup> and Article 7(2)<sup>25</sup> limiting the time frame within which a State can make adjustments. These proposed amendments would provide some certainty and transparency to taxpayers and States on statutory limitations.

**C Article 14- Best Practices**

The best practices are aligned to the three stated objectives of the Minimum Standard and will be dealt with accordingly. As these are best practices, no changes to the model convention have been envisaged. However, amendments to the commentaries are proposed in an attempt to obtain consensus on the practices.

**i) Objective: States to ensure that treaty obligations relating to MAP are fully implemented in good faith and resolved in a timely manner.**

*Minimum Standard*

*States should include Article 9 paragraph (2) in their treaties.*

Article 9(2) relates to transfer pricing adjustments made to associated enterprises. It is an anti-double taxation provision, as it requires unilateral adjustments to be made in order to alleviate economic double taxation. Some States take the view that absent a specific para (2) clause in their treaty, they are not obliged to make unilateral adjustments. This attitude reflects bad faith in implementation of the treaty, and is contrary to the stated objective.

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<sup>24</sup> Article 9 relates to associated enterprises.

<sup>25</sup> Article 7 relates to business profits

**ii). Objective: States to ensure that administrative processes promote the prevention of disputes and timely resolution of disputes.**

*Minimum Standard*

*It is proposed that States should be encouraged to publish inter-State agreements.*

These would be MAP agreements reached according to para (3) of Article 25, relating to resolving issues of interpretation or application of the treaty.

The publication would provide clarity and direction to the State's personnel and thus ensure consistency in the interpretation and application of the treaty provisions. This would go some way to preventing disputes and promoting timely resolution of matters. The publication should be on a public platform, on an anonymous basis to ensure secrecy provisions are not breached

*Minimum Standard*

*States should develop global awareness on international matters amongst their personnel.*

Audit personnel should be trained on international matters and to this end, FTA MAP Forum has developed a number of training modules. Member states are encouraged to utilise these initiatives to expose their personnel to global training on specific issues. In this way it is hoped that audit personnel will be better equipped to deal with international issues and application of treaty provisions, thereby preventing the potential for disputes. Audit staff need to be made aware of the following issues:

- Potential for double taxation
- Impact of proposed adjustments on the tax base of one or more jurisdictions
- How competent authorities reconcile competing jurisdictions claims.

*Minimum Standard*

*States should implement bilateral APAs.*

Bilateral APAs would create certainty between competing jurisdictions, reduce the potential for double taxation and may even reduce transfer duty disputes.

*Minimum Standard*

*States should permit multiyear resolution of MAP disputes.*

It is submitted that this would only be practical where the facts and issues are the same in multiple years. This practice would be subject to the time frame given in para (1) of Article 25.

**iii). Objective States should ensure that taxpayers that meet the threshold of Article 25(1) are given access to MAP.**

*Minimum Standard*

*States should ensure a suspension of collection pending resolution of MAP.*

The suspension of collection should be on the same basis as that provided for under domestic legislation. This measure is intended to assist the taxpayer who may be required to pay the tax in order to gain access to MAP and may thus be severely prejudiced by having to pay tax twice before relief is available.

In addition, the report<sup>26</sup> points out that States that enter into negotiations on MAP in cases where tax has already been paid, may be influenced by having to refund the tax paid. This best practice would level the playing fields and enable the treaty partners to negotiate in good faith, ensuring the taxpayer will not suffer financial prejudice.

It is proposed that this best practice be included in the Commentary on Article 25.

*Minimum Standard*

*States should recognise that taxpayers are entitled to choose their remedial action.*

It is proposed that where administrative measures are needed to facilitate this principle, they be introduced domestically.

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<sup>26</sup> Op cit 2 at 31 para 50

MAP is available to taxpayers as a remedy over and above any domestic remedy that may exist. It is for taxpayers to choose which remedy they will rely on, and they should have the opportunity to pursue both the MAP and domestic options. Administrators should recognize that agreement under MAP can potentially resolve a bilateral issue, as opposed to a domestic remedy which is unilateral in the relief it provides.

*Minimum Standard*

*States should highlight in their MAP guidelines, the relationship between MAP and domestic law remedies, including a reference to each State's position on judicial decisions.*

The interaction between the MAP remedy and domestic law remedies is reflective of the overlap between domestic law and international law – ‘hard’ law versus ‘soft’ law. As this is a complex and often confusing topic, it is highlighted as something that should be clarified in the guidelines.

It is suggested that the following issues be dealt with in the guidelines:

- The order in which a remedy is dealt with domestically and at the bilateral level;
- whether a State is bound by judicial decisions of its courts when resolving MAP; and
- the *locus standi* of the relevant parties,

It is proposed to make changes to the Commentary on article 25 in order to give effect to this best practice.

*Minimum Standard*

*States should give MAP access to Taxpayers who have made bona fide foreign tax adjustments.*

These instances would arise where the Taxpayer makes amendments to previously filed returns. It is important to distinguish between domestic remedies which rely on an action by the Administrator to trigger remedial action, as against MAP remedies which don't require the tax to have been charged. Provided there is a possibility that taxation was not in accordance with the treaty, the Taxpayer is entitled to request MAP access under Article 25(1).

Permitting access to MAP would be in line with the objective of giving access to MAP where the provisions of Article 25(1) have been met. If MAP is denied, the taxpayer could suffer double tax, which would represent an application of the treaty not in accordance with its objective. *Bona fide* (good faith) in this context can refer to a situation where the Taxpayer has made a concerted effort to correctly reflect an arm's length price in a controlled transaction. In order to ensure that this best practice is effected, it will be necessary to make changes to the Commentaries on Articles 7, 9 and 25.

*Minimum Standard*

*Each State should provide guidance in its MAP guidelines on how it treats interest and penalties in the MAP process.*

Interest and penalties can be a significant factor to consider when accessing relief measures. For this reason, Taxpayers should be informed about them before electing whether to pursue a remedy. It would also be useful for treaty partners to be aware in advance of how these aspects are to be treated.

*Minimum Standard*

*States should provide guidance on multilateral MAPS and APAs.*

This best practice has been proposed in order to reflect the modern reality of doing business in a global environment.

#### **D. Effective Monitoring Mechanism**

Members of the Inclusive Framework<sup>27</sup> have agreed to implementation of Action 14, whilst OECD and G20 members<sup>28</sup> agreed on the minimum standards and what constitutes best practices. This agreement includes an undertaking to be subjected to a review mechanism. The review mechanism takes the form of a peer review on the effective implementation of the minimum standards. The review is carried out in two phases – Stage One assesses a country on the minimum standards and Stage Two focuses on a follow-up of recommendations made in stage one.

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<sup>27</sup> Consisting of approximately 140 countries.

<sup>28</sup> Approximately 40 countries.

The review entails an assessment of a State's legal framework, including a review of its tax treaties, domestic law and regulations as well as its MAP guidelines. As mentioned in 1 above, the minimum standards are objective criteria which can be more effectively evaluated than subjective criteria. As such, the minimum standards form the basis of the terms of reference for the review. This will ensure consistency in the review process. The terms of reference and accompanying methodology of review have been developed by the FTA MAP Forum.

Annexure A<sup>29</sup> to Action 14 sets out the mandate for the development of the terms of reference and the assessment methodology. The OECD Committee on Fiscal Affairs and the FTA MAP Forum have been mandated to develop the core documents for monitoring of the implementation of the minimum standards.

The desired outcome of the review is a report on each State's strengths and weaknesses in implementing the minimum standards as well as recommendations on how to address the weaknesses. The first Reports were issued in 2017 and the process is ongoing.

### **E. Conclusion**

In summary, the above are the actions contained in Action 14, designed to improve the dispute resolution process arising out of the incorrect application of tax treaties. The amendments to Article 25 are meant to align the dispute resolution process with all the BEPS Action Plans. The introduction of the minimum standards and best practices are designed to provide effective mechanisms to resolve disputes in international tax law. The actions have been designed from a rule of law perspective, acknowledging a taxpayer's right to access remedial action, speedy resolution of disputes, certainty and transparency in the hope of achieving the objective of relief from double taxation (or double non-taxation).

In the following chapter, the choice of the rule of law as a tool to measure Action 14 will be substantiated and summarised into a measurable framework in the context of international law. The focus will shift to South Africa in Chapter 4, where its response to Action 14 will be reviewed. This will include an analysis of the effectiveness of Action 14 using the Rule of Law framework identified in Chapter 2, as well as commentary on South Africa's first peer review report.

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<sup>29</sup> Op cit 2 Annexure A to Action 14 -Making Dispute Resolution Mechanism More Effective OECD 2015.

### III. CHAPTER 2 ESTABLISHING A BENCHMARK FOR ACTION 14

#### A. Introduction

The aim of this chapter is to identify an appropriate measure to evaluate Action 14. There is no readily accessible formula or guideline for measuring the effectiveness of Action 14. The starting point is establishing the meaning of “effective”; thereafter it will be necessary to contextualise the meaning, as it is a subjective concept. “Effective” is defined as ‘the degree to which something is successful in achieving the desired result’<sup>30</sup>. It follows that success is a measure of effectiveness. Success, however, is also subjective, which means that success has to be defined in the context of Action 14.

The purpose of Action 14 as stated in the OECD BEPS, Action 14<sup>31</sup> is to improve the dispute resolution process between States in order to make the dispute process more effective and for disputes to be resolved timeously. Effectiveness is a subjective criterion that cannot be evaluated in a vacuum. In order to evaluate whether the purpose of the Action 14 measures have been achieved, the measures need to be measured against specific parameters. The specifics in turn need to be relevant to international dispute resolution and based on universally accepted parameters.

#### B. The Rule of Law

It is submitted that given the objective and the context within which Action 14 is to be evaluated, the rule of law is the most appropriate standard. The rule of law has been defined by Professor Hattingh<sup>32</sup> as the most fundamental right governing the relationship between a citizen and the State. It protects the rights of the individuals against the state in its various forms. He identifies three common properties of the rule of law, namely:

1. protecting people from anarchy;
2. allowing people to plan their affairs with confidence, certainty and knowledge of what the law requires of them; and

<sup>30</sup> Oxford English Dictionary (United Kingdom 2019) <https://www.lexico.com/en/definition/effectiveness> (accessed on 30th October 2019).

<sup>31</sup> Op cit 2 at 9.

<sup>32</sup> Professor J Hattingh *Fundamentals of Taxation: An Introduction to Tax Policy, Tax Law and Tax Administration* (P Pistone et al. eds, IBFD 2019) Ch 2 at para 2:3:1 p 17.

3. protecting people from arbitrary exercise of power by the State.

In an attempt to define the concept of the rule of law, Lord Bingham<sup>33</sup> describes it as having at its core that the law is applicable equally to the State and its citizens. Lord Bingham admits that it is difficult to confine the concept as it is subject to qualification and exceptions, depending on the context in which it is applied.

The concept has been in existence for centuries, and has been debated and discussed by many scholars, from Aristotle to modern-day philosophers and jurists. Professor A.V. Dicey<sup>34</sup> has been credited with introducing the term “the rule of law” in the nineteenth century. However as Lord Bingham points out<sup>35</sup>, Professor Dicey did not create the idea behind the phrase “the rule of law”. He does acknowledge Dicey’s influence<sup>36</sup> on the use and application of the rule of law, especially in the modern democratic order. Dicey’s view of the rule of law was that everybody, including the State, is equal before the law

It is a concept that has universal application and has been acknowledged as a guiding principle in all legal systems operating in a constitutional democracy.

The OECD adheres to the rule of law, by requiring as a minimum for admission that States adhere to the rule of law. The OECD<sup>37</sup> stated that States wishing to apply for membership to the OECD must display commitment to two basic requirements, namely:

1. Democratic societies committed to the rule of law and protection of human rights;  
and
2. Open, transparent and free market economies.

In addition, on the occasion of the OECD’s fiftieth anniversary<sup>38</sup>, the Ministerial Committee confirmed the organisation’s commitment to the values of democracy based on the rule of law.

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<sup>33</sup> Tom Bingham *The Rule of Law* (England 2011).

<sup>34</sup> Vinerian Professor of English Law at Oxford University, in his book “An Introduction to the Study of the Law of the Constitution, published in 1885, and quoted in Tom Bingham’s book *ibid*.

<sup>35</sup> *Op cit* 33 at 3.

<sup>36</sup> *Ibid*.

<sup>37</sup> Trade Union Advisory Committee to the OECD Commission [https://tuac.org/wp-content/uploads/2018/06/140PS\\_E\\_8\\_membership.pdf](https://tuac.org/wp-content/uploads/2018/06/140PS_E_8_membership.pdf) accessed on 9 January 2020.

<sup>38</sup> *Ibid* at 3.

South Africa adheres to the rule of law: Section 1 (c) of the Constitution<sup>39</sup> lists supremacy of the constitution and the rule of law as the founding values of the State of South Africa.

The above confirms that the use of the rule of law as a measure of the effectiveness of Action 14 is apposite in this case, both internationally and in the South African context. Professor Hattingh<sup>40</sup> acknowledges the impact of the rule of law in taxation and recognises it as an important universal benchmark in tax law.

### **C. Definition of the Rule of Law**

There is no codification of the rule of law, along the lines of laws as we know them, nor is there a list of requirements that make up the rule of law. In common law countries like South Africa, the concept of the rule of law is built into legislation and also applied in the application and administration of the law. In countries with civil law, the rule of law has been codified.

It is submitted that because of its universal application in various guises and forms, it is difficult to create an objective universal measuring tool or benchmark for the rule of law, as it incorporates both objective and subjective factors. It is fact- specific and the context in which it is applied in each case needs to be taken into account.

In essence the rule of law has been described by The United Nations<sup>41</sup> as:

*'a principle of governance in which all persons, institutions and entities, public and private, including the state itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards. It requires measures to ensure adherence to the principles of supremacy of law, equality before the law, accountability to the law, fairness in the application of the law, separation of powers, participation in decision making, legal certainty, avoidance of arbitrariness and procedural and legal transparency'.*

Dr Pim Albers<sup>42</sup>, in discussing how to measure the rule of law, notes that it has many different definitions. He characterises the issue by differentiating between a “thick” and a “thin” notion

<sup>39</sup> Constitution of the Republic of South Africa, 1996.

<sup>40</sup> Op cit 32 at 29 para 2.3.4.

<sup>41</sup> <https://www.un.org/ruleoflaw/what-is-the-rule-of-law/> accessed on 1 November 2019.

<sup>42</sup> Dr Pim Albers Special Advisor of the Council of Europe CEPEJ *How to measure the rule of law: a comparison of three studies* 1. <https://rm.coe.int/how-to-measure-the-rule-of-law-a-comparison-of-three-studies-dr-pim-al/16807907b2> accessed on 15 August 2019.

of the rule of law. The “thick” notion confines itself to the legitimacy of the law itself and does not delve into whether the law is just or any other considerations pertaining to the rule of law. The “thin” notion looks at the law more substantively and takes into account basic rights which are fundamental to the rule of law. The different approaches can also be seen as a type of substance-over-form approach. Albers is of the view that a “thinner” concept of the rule of law enables one to measure the rule of law effectively.

The authors of another paper on measuring the rule of law<sup>43</sup>, when discussing the principle of access to justice as one of its elements, take the view that this is part of both the “thin” and “thick” notions, as it includes access to dispute resolution mechanisms and access to more formalistic mechanisms like the judiciary.

For our purposes (discussing international dispute resolution), the rule of law must be viewed substantively by evaluating it in the context of international law. Lord Bingham<sup>44</sup>, in a relevant discussion, takes the view that the rule of law in international law is simply the domestic rule of law on a larger scale. In support of his view, he quotes Professor Chesterman, who defines the international rule of law as the application of rule of law principles to relations between States and other subjects of international law. He suggests that the rule of law should be analogous in both international and domestic law in order to achieve strict compliance with the law. He does not consider that the lack of an international legislature detracts from the legitimacy of international law. For example, he believes that by signing treaties, States formally commit themselves to be bound by the terms of the treaty.

Lord Bingham’s view of the rule of law as analogous in domestic and international law has merit in the right context. While his views were expressed in the context of discussing the concept of the rule of law, the focus in this chapter goes beyond simply discussing it. The intention is to develop a measure or benchmark of the effectiveness of the rule of law in the context of international dispute resolution. The distinction between international law and domestic law needs to be taken into account here.

Claasens<sup>45</sup> defines international law as:

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<sup>43</sup> Measuring the Rule of law, Juan C Botero Alejandro Ponce, The World Justice Project –working paper series, WPS No.001, at page 13.

<sup>44</sup> Op cit 33 at 111.

<sup>45</sup> RD Claassen *Dictionary of Legal Words and Phrases* 2 ed(1997).

*'Butterworths Words and Phrases Judicially Defined 2ed records the following under this heading: International law may be defined as that body of law which is composed for its greater part of the principles and rules of conduct which States feel themselves bound to observe, and therefore, do commonly observe in their relations with each other and which includes also: (a) the rules of law relating to the functioning of international institutions or organisations, their relations with each other, and their relations with States and individuals; and (b) certain rules relating to individuals and non-State entities so far as the rights or duties of such individuals and non-State entities are the concern of the international community.'*

International law is defined by John Dugard<sup>46</sup> in his book *Dugard's International Law: A South African Perspective* as a normative body of rules binding upon States in their relations with one another.

One of the differences between domestic law and "international law" is the lack of an underlying obligation. In the context of international dispute resolution, a study on effectiveness must take into account the enforceability of the resolution. International law relies on adherence to the rule of law as a method of enforceability. This is somewhat aligned to Bingham's views described above, that States obey international law in much the same way that citizens obey domestic law<sup>47</sup>.

This distinction between international and domestic law has been described as that between "soft" and "hard" law respectively. In the above definition, international law is seen as "soft" law relying on the rule of law and the good faith of states. Domestic law is seen as "hard" law in that it creates rights and obligations for citizens which are enforceable by the State.

The ability to enact "hard" law is seen as the State's sovereign right. There is no sovereignty in the international context; the idea is an anathema. Altman<sup>48</sup> is of the view that sovereignty of nations prevents hierarchical enforcement of international law, and further that enforcement of international law is only effective when introduced into domestic law.

It is not the subject of this thesis to further debate the concept of international law; it is sufficient for our purposes to draw attention to the inherent differences between "soft" and

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<sup>46</sup> John Dugard, *Dugard's International Law A South African Perspective* 5 ed ch 1 at 1.

<sup>47</sup> Op cit 33 at 113.

<sup>48</sup> ZD Altman *Dispute Resolution under Tax Treaties* vol 11 (IBFD Doctoral Series 2006) ch 7 p1.

“hard” law, (as well as the similarities according to Bingham) and how this affects the effectiveness of “soft” law.

#### **D. Establishing the Benchmark**

Now that the rule of law has been defined in broad terms as a measuring tool in the present context, those aspects of it which are applicable for our purposes, need to be identified.

The OECD relies on a formula, based on rule of law principles, used by an international initiative, the World Justice Project or WJP. To explain: the OECD has designed a framework for consideration of prospective members, which includes a list of indicators compiled by the WJP and others to measure commitment to the rule of law. This is part of a framework to evaluate a state’s commitment to the OECD’s values. The WJP’s list of rule of law indicators will now be discussed along with its background.

The WJP<sup>49</sup> evaluates annually the rule of law compliance by 126 countries. The Project defines the rule of law as a framework of laws and institutions which embody four universal principles:

1. Accountability;
2. Just laws;
3. Open government; and
4. Accessible and impartial dispute resolution

The principles identified by Lord Bingham<sup>50</sup> also need to be taken into account in formulating the measure, namely:

- Accessibility, meaning that laws must be accessible to the people they apply to. Laws must be intelligible, clear and predictable;
- Law must limit discretionary power. Where discretion is granted, it must be exercised legally, rationally and fairly;
- Equality before the law;
- Exercise of power must be done in good faith, fairly, purposefully and lawfully;
- Dispute resolution options to enforce rights and obligations;

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<sup>49</sup> World Justice 2019 Rule of Law Report, <https://worldjusticeproject.org/sites/default/files/documents/WJP-ROLI-2019-Single%20Page%20View> accessed on 23 May 2019.

<sup>50</sup> Op cit 33.

- Right to a fair trial, including “equality of arms” (all parties to a case having the same rights in court), fairness and an independent judiciary.

Whilst the focus is on dispute resolution, the other principles identified above should be taken into consideration in an evaluation of a dispute resolution mechanism. In developing the rule of law as a measuring tool for dispute resolution, some of the principles identified above need to be included. Whilst timely resolution of disputes has not been specifically identified, Lord Bingham <sup>51</sup> in discussing dispute resolution as a principle of the rule of law, highlights two factors that detract from the principle, namely cost of litigation and delays in resolving disputes. Dispute resolution must be conducted in a timely manner if it is to conform to the rule of law. The saying “justice delayed is justice denied” <sup>52</sup> is a well-established and often applied principle of the rule of law.

The dispute process must be conducted by suitable and competent officials, who must be ethical and independent as well as knowledgeable and able to perform the required processes.

In addition, the process must be accessible to all those who may have a right to be admitted to the process. This means that the laws or procedures must be clear, unambiguous and accessible to all. The process must also be adequately resourced to ensure that it can function. Lastly, it must be representative of all those whose rights have been affected.

The characteristics as set out above are ideals to which all dispute resolution processes should aspire. In order to apply the above to the dispute resolution mechanisms contained in Action 14, it is perhaps necessary to refine the characteristics into a more useable format. A report by the Vera Institute of Justice <sup>53</sup> highlights the different approaches to measuring the rule of law, with one approach referring to *de jure* measures, which would focus on legislative reviews. The focus here will take the form of a *de jure* type measure, analysing the objectives contained in Action 14. It is acknowledged that the BEPS project does not have the force of law on its own. However, to the extent that the BEPS recommendations are intended to be included in a State’s treaty network and incorporated into its domestic law, they have the characteristics of legislation.

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<sup>51</sup> Op cit 33 at 88.

<sup>52</sup> See *Carneiro v State* (425/18)[2019]ZASCA 45 where the court applied the maxim in a criminal matter.

<sup>53</sup> Developing Indicators to Measure the Rule of Law: A Global Approach, A report to the World Justice Project July 2008 4-16. [https://www.vera.org/downloads/Publications/developing-indicators-to-measure-the-rule-of-law-a-global\\_Online\\_version2.pdf](https://www.vera.org/downloads/Publications/developing-indicators-to-measure-the-rule-of-law-a-global_Online_version2.pdf) accessed September 2019.

### **E. The Measure.**

The proposed format to measure the effectiveness of Action 14 is to test the following three of its components:

1. Minimum standards;
2. Best practices; and
3. Effective monitoring

The various actions proposed under each of these components will be discussed individually in the next chapter.

The following rule of law measures will be applied to the Action 14 components:

1. Timeous resolution of disputes;
2. Accessibility to the process;
3. Adequately resourced process;
4. Competency and suitability of officials; and
5. Independence of officials.

To reiterate, the objective of this research is to determine the effectiveness of Action 14. As explained in Chapter 1, Action 14 is designed to supplement and improve the existing dispute resolution provisions in the model tax treaty. The scope of this research is not to focus only on the MAP provisions contained in Article 25 of the model treaty, but also to refer to and discuss some of the actions designed to underpin Article 25.

Chapter 3 will focus on the inputs, defined as the objectives and actions contained in Action 14, and how these measure up to the rule of law indicators. Chapter 4 will focus on the local outputs, referring to how South Africa has applied Action 14, with specific reference to the peer review report. The intention is that discussion of the South African review will identify both the efficiencies and any inherent inefficiencies occurring in this country, which will in turn result in a finding on the effectiveness of Action 14 for South Africa.

## **IV. CHAPTER 3 REVIEW OF THE EFFECTIVENESS OF BEPS ACTION 14 MEASURES**

### **A. Context**

The opening paragraph of the introduction to Action 14, states under the heading “Aim of Action 14”, “Make dispute resolution more effective”. The report then proceeds to list how it intends to achieve this, namely by removing obstacles to an effective MAP procedure, introducing minimum standards and best practices, and instituting peer reviews. These are indicative of attempts to improve the dispute resolution process. Whilst the aim of this research is to test the effectiveness of the Action 14 measures, there will also be brief references to provisions of Article 25, which deals specifically with dispute resolution and which Action 14 attempts to improve via proposed amendments. This chapter will focus on inputs, these being the measures of Action 14, with an emphasis on objective elements.

The review of the Action 14 measures will be approached initially from a broad perspective, and then narrowing to a review of the specific actions. This approach is necessitated by the form in which Action 14 is presented.

### **B. Article 25**

Before Action 14 measures are reviewed, it is necessary to refer to Article 25 of the model tax treaty.

Article 25 consists of five sub-provisions, as follows:

1. Article 25(1) entitles a person, who is of the view that the actions of one or both of the contracting states will result in that person being subjected to tax not in accordance with the provisions of the particular treaty, to present his or her case to either of the States. There is a time limit of three years from when a State receives notification of the contention that the action giving rise to the taxation is not in conformity with the treaty, to the deadline for resolving the dispute.
2. Article 25(2) compels the competent authority<sup>54</sup> to consider the case, and if it appears to be justified, to attempt to settle the matter. If the competent authority is unable to settle the matter unilaterally, it has to resolve the case by MAP with the other

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<sup>54</sup> Competent authority being a duly delegated person from the contracting state’s tax office.

contracting State, with a view to avoiding taxation not in accordance with the treaty. If agreement is reached, it will not be affected by any time limits in domestic law.

3. Article 25(3) compels the contracting States to resolve by MAP any interpretative issues arising from the treaty, or any issues with applying the treaty provisions. The States are also entitled to consult on eliminating any double taxation not provided for in the treaty.
4. Article 25(4) permits States to engage with each other directly without having to observe any diplomatic protocol, for purposes of reaching an agreement.
5. Article 25(5) provides for arbitration where the states are unable to reach agreement within two years from the initiation of a MAP. The initiation of arbitration is at the request of the person affected by taxation not in accordance with the treaty.

#### **i).Observations on article 25**

By way of an overall observation on Article 25, the provisions are couched in broad terms which are problematic. Article 25 deals with remedial action and should clarify with certainty the conditions under which the remedies are available. In addition, it should provide for a more objective determination at the initiation stage. The gatekeeper to the process is the State, once it is approached by the affected party. It is for the gatekeeper, who has either a direct or indirect interest in the case, to determine whether the person qualifies for relief. If access is denied, the affected party has no right to demand access.

The Commentaries to Article 25<sup>55</sup> at paragraph (17), state that access to MAP should be as widely accessible as possible and provide flexibility. On the question of impartiality, the paragraph states further that access to MAP should be considered by both States.

Article 25 presupposes that domestic tax law does not change. Domestic tax law is a moving target which could potentially affect a successful resolution of a MAP. This could arise where a MAP is agreed upon and subsequent changes to domestic law prevent its implementation, as the terms of the agreement are contrary to the amended domestic tax provisions. The

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<sup>55</sup> Op cit 11 Model Tax Convention –Commentary on Article 25 concerning the mutual agreement procedure – OECD 2109.

Commentaries at paragraph 29<sup>56</sup> suggest that in this situation, States should act in good faith and attempt to amend or revise the agreement to the extent possible.

In addition, in paragraph (38.1) of the Commentaries, it is recommended that where a State is precluded from reaching settlement with a taxpayer on a strict interpretation of domestic provisions, the State should, for the sake of equity, take other considerations into account, for example the avoidance of double taxation, in order to resolve the taxpayer's case. This approach is in accordance with international arbitration.

A criticism of Article 25 is that it doesn't permit taxpayer participation. Dr Katerina Perrou<sup>57</sup> states that international tax dispute resolution is based on the doctrine of diplomatic protection and naturally excludes taxpayer participation, from what is essentially a taxpayer problem. She advocates for direct taxpayer participation in the proceedings in order to protect a person's right to a fair trial. The study was done before the introduction of Action 14. In the concluding findings on the effectiveness of Action 14, I will revisit this issue, to determine whether Action 14 has adequately addressed the issue of taxpayer access.

The Commentaries, at paragraph (40), recognise the importance of taxpayer participation in the process, in relation to transfer pricing adjustments. They propose that in a MAP relating to transfer pricing, the taxpayers should be given an opportunity to address the respective contracting States, before agreement is reached.

There are no enforcement measures for failure to comply with Article 25. It is acknowledged that Action 25 is remedial action arising in international law, which is "soft" law and lacks inherent enforceability. Sir Frederick Pollock<sup>58</sup>, in response to the question "does international law qualify as law", states that a legal system simply requires the existence of a political community, and the recognition that there are settled laws binding on them.

The apparent "defect" in international law lying in its lack of enforceability, can be overcome through various methods adopted by the international community acting together. If Article 25 is viewed from this perspective, this inherent defect of the lack of enforceability can be addressed, but with limited options. The question that should then be posed is: does Action 14 effectively address the lack of enforceability.

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<sup>56</sup> Op cit 11.

<sup>57</sup> Katerina Perrou *Taxpayer participation in tax treaty dispute resolution*, vol 28,( IBFD Doctoral Series 2014).

<sup>58</sup> Op cit 46; cited in Dugard's International Law at 9.

The question of enforceability affects Article 25 in a number of instances. For example, Article 25(1) provides that it is for the State to assess the Taxpayer's case and determine if the complaint is justified. If it appears that the complaint arises through an action of the other contracting State, the originating State is obligated to contact the other State so that the bilateral process can start. There is no sanction available to the Taxpayer should the originating State fail to engage the other State. The Taxpayer is entitled to approach the other State for assistance, but it is submitted, this is not ideal, as the process would start afresh, and delay the ultimate conclusion of the case. It is debateable whether a taxpayer would have any domestic remedies available to address the failure on the part of the State to engage with its counterpart. In South Africa, judicial review could be instituted, but it is questionable whether the court would have **locus standi** to engage in what is essentially an international law issue.

The Commentaries at paragraph (36) deal with the legal nature of para (2) of the process, and express the view that para (2) simply places a duty on the contracting States to negotiate. It does not place a duty on the States to try to reach an agreement.

In a similar vein, paragraph (3) provides an opportunity for States to resolve interpretative or general difficulties relating to a treaty.

Similarly, there is no judicial remedy available if a State does not observe the terms of the MAP or fails to reach agreement on a MAP.

Paragraph (4) does not prescribe the procedures or formalities for MAP, leaving it up to contracting States to determine their own processes.

The lack of a prescriptive structure could result in a multitude of different processes and procedures arising. It is submitted that it would be more beneficial to have a minimum prescribed standard which contracting States are obliged to adopt. This would ensure a certain degree of uniformity, which will assist taxpayers, especially Multinational Entities that operate across a multitude of countries.

Paragraph (5) provides for arbitration as a last resort, where MAP has been unsuccessful.

Where States elect not to adopt arbitration, the failure of MAP leaves the Taxpayer with no alternative remedy to pursue, other than domestic remedies if they are available. If the Taxpayer is not in agreement with the outcome of arbitration, it is the end of the road for any resolution under international law. In addition, the provisions of Article 25 require that the

Taxpayer first adopt MAP as a remedy, with arbitration only available post the MAP process. This can cause significant delay in finalisation of a case, as the Taxpayer first has to go through the motions of MAP, even where MAP is not suitable as a means of resolution, before the case can be referred to arbitration. Thus the structure of Article 25 can cause significant delays in finalising cases, to the detriment of taxpayers.

Where a matter is referred to arbitration, the taxpayer is not bound to accept the agreement reached through arbitration. The article recognises that a taxpayer also has domestic remedies available. The principle of “**lis pendente**”<sup>59</sup> is acknowledged in Article 25, requiring taxpayers to choose between arbitration and domestic remedies. The international remedies as contained in Article 25 cannot be pursued simultaneously with domestic remedies.

### **C. Action 14**

The aim of Action 14 is to improve the effectiveness and efficiency of the MAP process. Action 14 introduced a three-point minimum standard that needs to be met in resolving treaty related disputes, namely:

- Implement treaty obligations in good faith with a view to resolving MAP cases timeously;
- Implement administrative processes aimed at reducing treaty-related disputes and timely resolution of disputes; and
- Ensure access to MAP.

These items on their own cannot be evaluated for effectiveness; they are simply minimum standards which States are advised to comply with in resolving treaty related disputes. The true extent of their effectiveness from a rule of law perspective cannot be determined in isolation. The only comment that can be made is that it appears that the rule of law has been taken into account in identifying the above as minimum standards. It remains to be seen whether these minimum standards, in the implementation phase, translate into something more measurable.

In addition to these minimum standards, Action 14 provides for best practices to be incorporated into the Commentaries to ensure adherence to the minimum standards. The best practices are aligned to the standards, and under each item, specific further standards are identified to entrench them. The minimum standards were designed to be objective. The need

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<sup>59</sup> Meaning –pending litigation -Dr Theo B Rood *Glossarium* ed(2003)at 45.

for objective standards is to ensure that a State's actions in relation to dispute resolution can be evaluated by its peers. The effective monitoring is the third aspect of Action 14.

**i). Minimum Standards**

The minimum standards to ensure treaty obligations are implemented in good faith and in a timely manner, involve the following actions:

1. States to include paragraphs (1) to (3) of Article 25 in all their treaties. The good faith principle requires that all aspects of these paragraphs are included in the treaty; there cannot be selective inclusion.

**Observation.**

This will ensure uniformity in the MAP process. In addition, States, in applying the provisions of these paragraphs, should be guided by the aim of the double tax treaty, being the avoidance of double tax. States will achieve this if they can objectively apply the provisions and not be guided by their own sovereign interests. Aligned to this is the issue of access to MAP in cases of double tax that do not fall within the scope of the treaty. This could arise where profits are allocated to two permanent establishments in two States, while the Taxpayer resides in a third state. Despite the fact that a treaty would not necessarily provide relief, the State should consider access to MAP in such cases to relieve double taxation.

The effectiveness of this action can be measured against the rule of law measure of "independence of officials". It is submitted that where States are required to be guided by an objective factor like the avoidance of double taxation in resolving disputes, this helps to meet the independence requirement. The requirement for States to step away from their own sovereign tax requirements and consider the broader issue of relieving double taxation goes some way towards ensuring independence, both in allowing access to MAP and in attempting to resolve the dispute. However, while the goal of independence is admirable from a rule of law perspective, in practice it is difficult to ensure that this independence is achieved. It would entail prescribing to in allowing access to MAP Tax Administrations (which is the aim of Action 14), and then close monitoring of all MAP applications and how they are dealt with. This aspect will be dealt with below when the peer review section is evaluated.

It is also recommended that access to MAP be permitted in all transfer pricing cases to avoid economic double taxation. It is not clear whether this should be included in Article 25 or in domestic legislation.

2. Access to MAP should not be denied, specifically in anti-abuse cases. If the parties disagree over the application of either the treaty's anti-abuse provisions or domestic anti-abuse provisions, States should not, as a matter of course, simply deny access to MAP. By allowing access to MAP, a State is not agreeing to resolve the issue; it is simply providing the forum for the issues to be ventilated.

**Observation**

This action is an attempt to meet the independence requirement of the rule of law. However, it is submitted that for the independence requirement to be fully met, the State must objectively assess a case on the facts and not be subjectively influenced by perceptions of abuse in allowing access to MAP. The State should not summarily deny rights to remedial action because of perceptions of abuse.

3. States to resolve MAP cases within twenty-four months of receipt.

**Observation**

Placing a time restriction on the resolution of disputes complies with the requirement for timeous resolution. However, it is submitted that this needs to be tempered, as there may be instances where a dispute could be resolved well before the expiry of two years, but because there is a maximum time allowed, there is no incentive to speedily resolve the dispute. To fully meet the requirement of timeous resolution of disputes, the wording should be amended to promote a speedier resolution where possible.

4. States should aim to improve competent authority relationships and become members of the Forum on Tax Administration MAP Forum (FTA MAP Forum).

**Observation**

This would ensure a level of competency amongst officials as well as uniformity in addressing issues and provide an international platform to discuss issues arising from MAP.

It is submitted that this action helps to meet the requirement of officials being competent. It is presumed that if competent authorities strengthen relationships

with their counterparts and interact on an international level, their officials will be exposed to new problems and issues as well as new ways to resolve them. This can only improve the officials' level of competence and skill.

5. States should compile complete and MAP reports timeously to the FTA MAP Forum.

**Observation**

Comprehensive reporting will assist in evaluating and assessing the effectiveness of Action 14 measures and of Article 25 on a continuous basis. It should also promote accountability amongst states, which is important in the international context, given the lack of enforceability in international law.

6. States need to agree to peer reviews of their adherence to the minimum standards under the FTA MAP Forum.

**Observation**

As stated above on the action of reporting, the review function is one way of ensuring compliance with the standards, especially in the absence of legislative enforcement provisions. This minimum standard will go some way in ensuring over all compliance with Action 14.

7. States should state clearly their positions on MAP arbitration.

**Observation**

This standard addresses a general rule of law requirement that laws should provide certainty. As highlighted in the Action 14 report, it is not always possible for States to publicly state their position on mandatory arbitration (possibly from a strategic perspective). To overcome this obstacle, it is suggested that alternate provisions for resolving disputes be proposed, for example a list of defined cases that can be resolved via MAP. This requirement on transparency is in line with the general principles of the rule of law, providing certainty to taxpayers as to what their remedies are before they elect which remedy to follow. It also addresses the requirement of accessibility to the process.

ii). **Best Practices within Minimum Standard**

1. States institute administrative processes that promote the prevention of disputes and the timely resolution of disputes.

The following actions have been proposed to achieve this:

- MAP guidelines to be published for taxpayer use.

**Observation**

This action promotes accessibility to MAP, as it informs taxpayers of the remedial action that is available to them and how to access it.

- MAP profiles to be developed and placed on a public platform.

**Observation**

This action also promotes accessibility to the MAP process, as it assists taxpayers in applying for MAP. It addresses the timely resolution requirement as it attempts to inform taxpayers first-hand how and where to direct their cases, which could go some way to reducing delays in delivery of requests.

- Dedicated staff must be allocated to deal with MAP requests. This includes delegating the staff the necessary authority to resolve MAP cases.

**Observation**

This action ensures that the MAP process is adequately resourced. It also ensures that staff are vested with the necessary authority to independently resolve the dispute, without having to defer to other administrative staff who may lack objectivity. This action goes some way towards addressing the independence of the process. However, it is only in the implementation of this action (and most of the other actions) that its effectiveness can be truly measured.

- Staff in charge of the MAP process should be independent of the Administration and should not be subjected to performance indicators that could affect their independence.

**Observation**

It is submitted that MAP staff should rather be evaluated on their achieving the actions of Action 14, focusing on speedy resolution of MAP cases, the number of MAP cases they resolve and their consistency in applying the treaty provisions.

This action addresses the issue of independence and overall commitment to the principles of Action 14.

- States should ensure that the MAP function is adequately resourced.

### **Observation**

This action clearly addresses the resource criteria of our rule of law indicator, but as noted above, with most of these actions, the proof of the pudding will be in the eating.

- States need to clarify their positions on MAP, especially in relation to settlement of tax disputes domestically. Where a State's domestic provisions permit it to settle domestic tax issues independently of the audit process, this should not automatically preclude access to MAP. In addition, where a State has domestic settlement provisions which could in some instances preclude access to MAP, that State should by right consider the treaty consequences of a settlement.

### **Observation**

This action is important in ensuring that a taxpayer is aware of the possible remedies upfront before electing which route to follow, to prevent a denial of access to the process down the line. This action meets the accessibility measure and if adopted by states, will be effective in protecting and promoting access to justice.

- States should provide for roll-back relief in relation to advanced pricing arrangement programmes (APA) for prior years, provided the facts in the prior years are the same. The intention of this action is to prevent potential transfer pricing disputes from arising.

### **Observation**

This action can be said to address a fundamental principle, that of certainty. Certainty on how laws are applied or will be applied, goes a long way towards reducing disputes and brings an aspect of objectivity to a potential dispute.

2. States to ensure that taxpayers who meet the requirements of Article 25(1) on dispute resolution, can access MAP.

The actions aimed at giving effect to this standard are:

- Both states should be made aware of MAP requests and be able to provide their views on whether access should be permitted. The action proposes that either the wording of Article 25(1) be amended to give effect to this intention, or a bilateral notification system be introduced under which, where a State is of the view that the case does not qualify for MAP, it can inform the other State.

### **Observation**

The aim of this action is to make access to MAP as wide as possible, and to prevent a taxpayer from being denied access, simply because one State is of the view that the case doesn't qualify. The aim of opening up access to what is essentially a remedy is in line with the rule of law requirement of access to justice. By opening up access to both states, it also enables the taxpayer to have a fresh set of eyes evaluating the case, which can be expected to promote objectivity and independence.

- States' MAP guidelines must specify what documents are required to be submitted with a MAP request. However, MAP should not be denied simply because of failure to comply with the documentary requirements.

### **Observations**

This action positively addresses the access to justice requirement, as it ensures that the Taxpayer has sufficient knowledge of what is required before submitting a request.

- States should undertake to implement MAP agreements irrespective of whether time limitations imposed in terms of domestic legislation have prescribed. Where States are unable to comply with this action, the time limits imposed in articles 7(2)<sup>60</sup> and 9(1)<sup>61</sup> of the treaty should be limited accordingly.

### **Observations**

This action is designed to ensure that both taxpayers and States are transparent in their dealings with each other and also further incentivises timely resolution of disputes.

### iii). **Best Practices**

Action 14 has also proposed a list of best practices which are aligned to the three facets of minimum standards discussed above. The best practices are simply practices and are not meant to be incorporated into the treaty. In an attempt to codify these practices, they have been incorporated into the Commentaries.

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<sup>60</sup> Article 7 of the model treaty deals with the taxation of business profits.

<sup>61</sup> Article 9 deals with associated enterprises.

1. States to ensure that treaty obligations are implemented in good faith and resolved in a timely manner
  - The best practice to achieve this objective is to incorporate Article 9(2) in the treaty. Article 9(2) is a transfer duty provision which directs States to make unilateral transfer pricing adjustments to prevent economic double taxation.

#### **Observation**

This accords with the objective of implementing treaty obligations in good faith and also helps to prevent disputes. Absent Article 9(2), States may be reluctant to make unilateral adjustments, as they may feel they are acting outside their legislative mandate. However, Article 25(3) does provide for adjustments not provided for in the treaty in order to prevent double taxation. This practice measures up to the rule of law principle of fairness and could be said to meet the requirement of officials being independent, in that it requires States, through their officials, to act in accordance with the aims of the double tax treaty.

2. States to ensure administrative processes promote the prevention of disputes and timely resolution

The recommended best practices are:

- States should publish MAP agreements. These would be agreements under Article 25(3) relating to interpretation or application of the treaty.

#### **Observation**

This is designed to achieve consistency in approach and clarity on how matters will be treated. It also addresses the competence of officials, as the published agreements would provide a reference source for officials, to guide and inform their actions.

- States should develop global awareness amongst their dedicated MAP personnel. The FTA MAP Forum provides training to member states in an attempt to better equip personnel on international matters.

#### **Observation**

This practice (in theory) complies with the competency requirement as well as contributing to the adequate resourcing of the MAP process.

- States should implement bilateral APAs.

**Observation**

This practice could go a long way towards creating certainty on treatment of transfer pricing and also reducing disputes between States on transfer duty. This practice is compliant with the rule of law in that it ensures certainty. To the extent that it reduces potential for conflict, it also accords with the rule of law.

- States should allow multiyear resolution of disputes.

**Observation**

This practice has limited application, as the facts would have to be identical to allow for multiyear resolution. It could in fact be counter to the rule of law in that it could potentially deny a taxpayer a right to access, where agreement excludes access. Whilst it would be an efficient practice from the point of view of States in that it reduces disputes, it is a risky option as it could be open to abuse and may be difficult to monitor.

## 3. States to provide access to MAP

The best practices to ensure access are:

- Suspension of collection of tax debt pending resolution of MAP.

**Observation**

This practice is to alleviate any prejudice the taxpayer may suffer through having to pay tax in two jurisdictions. It also addresses the aspect of independence, as a State may be negatively influenced by having to refund tax already accounted for when considering a MAP request.

- States need to recognise that taxpayers are entitled to choose their remedial action, either domestically and/or through treaty relief. Domestic provisions need to be amended to reflect this practice.

**Observation**

A taxpayer should not be prejudiced by being denied a remedy in one forum; the difference between treaty relief (bilateral relief) and domestic relief (unilateral relief) should be highlighted. This meets the access to justice requirement.

- The MAP guidelines should highlight the MAP and domestic law remedies. States should also state their position on judicial decisions. This practice is to provide certainty and clarity to taxpayers on their available remedies, with emphasis on how the States deal with them on a domestic and international level.

**Observation**

This can assist taxpayers when electing which remedial action to pursue. It also addresses the access to justice principle, as it ensures that taxpayers can make informed decisions about how to pursue their remedial action.

- States should give access to taxpayers who have made *bona fide* foreign tax adjustments. These would not entitle a taxpayer to domestic relief and MAP access would be the only way in which double tax relief can be obtained.

**Observation**

This practice does address the access to justice requirement, as it provides a mechanism which would possibly not otherwise be available to taxpayers.

- Each State should provide clarity in its guidelines on how it treats interest and penalties.

**Observation**

This information would assist taxpayers when considering how to pursue their remedy. Access to justice is confirmed if this practice is adopted.

- States should provide guidance on multilateral MAPs and APAs.

**Observation**

This would assist taxpayers operating in a global environment and could potentially alleviate the potential for treaty disputes. This practice also encourages transparency from states and supports the access to justice requirement. It could also potentially prevent requests for MAPs on matters which don't qualify for access.

**iv). Peer Review**

The third component of Action 14 is the implementation of a peer review system. The aim of the peer review is to monitor the implementation of the minimum standards by States in an attempt to ensure commitment to the implementation of Action 14. Member states of the OECD, G20 countries and the Committee on Fiscal Affairs (“CFA”) agreed to be subjected to peer reviews.

The working group of the CFA developed terms of reference and an assessment monitor prior to the commencement of peer reviews<sup>62</sup>. The peer reviews started in 2016 and to date,

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<sup>62</sup> <https://www.oecd.org/tax/beps/beps-action-14-on-more-effective-dispute-resolution-peer-review-documents.pdf> accessed on 14 November 2019.

approximately 45<sup>63</sup> states have been reviewed. The review is a two-stage process: Stage One highlights compliance with the minimum standards, while the Stage Two report is a follow-up on recommendations arising from the Stage One report.

The terms of reference incorporate the minimum standards. The review is split into four components, namely:

1. Prevention of disputes
2. Availability and access to MAP
3. Resolution of MAP cases
4. Implementation of MAP agreements.

Questions are formulated for each component, which form the basis of the review. States are requested to complete the questionnaire, and then input is obtained from treaty partners (peers) as well as from taxpayers. Once feedback is received by the CFA, reports are drafted, submitted to the State being reviewed for comment and then finalised. The report sets out the shortcomings and proposals on how to address these.

The State is then obligated to address the CFA on how it is addressing its identified shortcomings. This then forms the basis of the second report.

In addition to the two reports, States are required to complete MAP statistics, which attempt to measure accessibility to the process, timeous resolution and implementation of agreements. The Guide to MAP reporting in the Action 14 report<sup>64</sup> defines the various reporting elements to ensure consistency and accuracy in reporting on MAP.

The CFA has provided comprehensive procedures and guides on how the peer review is to be conducted, to ensure effective monitoring of the implementation of the Action 14 minimum standards.

### **Observation**

The procedures and guidelines for peer reviews appear to comply with rule of law indicators like speedy completion of dispute resolutions, access to the process, competency of officials

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<sup>63</sup> <http://www.oecd.org/tax/beps/beps-actions/action14/> accessed 18 November 2019.

<sup>64</sup> OECD(2016), BEPS Action 14 on More Effective Dispute Resolution Mechanisms –Peer Review Documents, OECD G20 Base Erosion and Profit Shifting Project, OECD Paris. [www.oecd.org/tax/beps/bepsaction-14-on-more-effective-dispute-resolution-mechanisms-peer-review-documents.pdf](http://www.oecd.org/tax/beps/bepsaction-14-on-more-effective-dispute-resolution-mechanisms-peer-review-documents.pdf) accessed August 2019.

and adequate resourcing of the process. These are all covered in the peer review terms of reference. It is submitted that the peer review, to the extent that it is conducted by an independent body and obtains information /comment from third parties (other States and Taxpayers), contributes to the independence of the process. Whilst the peer review appears to be informed by rule of law indicators, it is submitted that the real rationale behind the peer review is to ensure enforceability of the Action 14 measures. This is an attempt to address the inherent unenforceability of international law measures, which are at best “soft” law.

The peer review component cannot stand on its own; it is a function of the other two components of Action 14. It is submitted that the other two components, minimum standards and best practices, are capable of being stand-alone measures. As mentioned above, my view is that the peer review is an attempt to make the other two components enforceable. The OECD uses peer review extensively for a number of purposes, one of them being to encourage mutual accountability amongst States.

An OECD publication by Fabrizio Pagani<sup>65</sup> titled *Peer Review: An OECD Tool for Co Operation and Change* states at page 10 that a peer review can impose peer pressure on a State to observe the aims and objectives of international organisations. It is a means of soft persuasion and most impactful when made public. Absent other enforcement measures, it is submitted that the system of peer review as provided in Action 14 can be effective in ensuring compliance by States with the minimum standards.

#### **D. Findings**

In summary, the Action 14 measures seem to have been designed in accordance with the rule of law. It does appear, though, that the major stumbling block in delivery of these ideals through Action 14 is the lack of enforceability in relation to dispute resolution. These points have been discussed above. Given the international context in which Action 14 operates, this will always be an issue, as enforceability of “soft” law can never equate to enforceability of “hard” law. However, it is submitted that the actions in Action14 go a long way towards achieving this objective. In addition, the incorporation of the BEPS measures through the MLI into the existing treaty network does add another element of enforceability. Where a domestic state incorporates its treaties into its domestic framework, compliance with treaty obligations can be said to be enforceable under domestic law. In this way the BEPS measures, to the extent a State

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<sup>65</sup>[https://www.oecd-ilibrary.org/economics/peer-review\\_9789264099210-en-fr](https://www.oecd-ilibrary.org/economics/peer-review_9789264099210-en-fr), accessed on 14 November 2019.

elects to incorporate them into existing treaties which form part of its domestic law, can be said to be enforceable.

Mario Zuger in his book *Arbitration under Tax Treaties*<sup>66</sup>, acknowledges that tax treaties on their own don't create rights and obligations for taxpayers. It is incumbent on States to comply with their own obligations arising from a treaty that may offer protection to the Taxpayer from double taxation. Neither does international law compel a State to pursue its citizen's claims. The rule of law is in stark contrast to international law<sup>67</sup>. The rule of law protects the fundamental rights of individuals, whereas international law is concerned with relations between States. Whilst international law may ultimately concern itself with individuals, its main focus and interaction is at a State level. Dennis Davis writing in the *South African Journal on Human Rights*<sup>68</sup> is of the view that there is an inextricable link between international and domestic law. This view has been informed by Constitutional Court judgment<sup>69</sup> in South Africa, relating to the status of international agreements, which bind the South African government once ratified. The question that could then be posed is to what extent the government, bound by a double tax treaty, feels compelled to take up the fight on behalf of its citizens who have not been taxed in accordance with a treaty.

As mentioned earlier on the issue of taxpayer participation, Katerina Perrou<sup>70</sup> concludes that the diplomatic protection which forms the basis of the MAP, does not work in resolving international tax disputes. The nature of international tax disputes needs to be taken into account; it does not necessarily require the protection of a State's nationals. International tax disputes are usually concerned with alleviating the effects of double taxation involving three parties, namely the Taxpayer's state of residence, state of source and the Taxpayer in person. It is for this reason that Perrou advocates that the participation of taxpayers in the international dispute resolution process is necessary. Action 14 has not directly addressed the issue of taxpayer participation in allowing access to MAP, instead focusing on the State's actions to accommodate taxpayer involvement. It also focuses attention on addressing taxpayers' rights to be relieved from double taxation, but stops short of insisting on direct taxpayer participation in the MAP process. It is submitted that this detracts from the effectiveness of Action 14, but

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<sup>66</sup> M Zuger *Arbitration under Tax Treaties* vol 5 (IBFD Doctoral series December 2001).

<sup>67</sup> Op cit 33 -This in contrast to Lord Bingham's view expressed in Chapter 2 at page 30.

<sup>68</sup> Dennis Davis, 'Introduction to International Law' 2015 SAJHR 667.

<sup>69</sup> *Glenister v President of the Republic of South Africa* 2011(3) SA 347 (CC).

<sup>70</sup> Op cit 57 ch 2 at 10.

possibly as mentioned below, the problem lies more in the structural problems in Article 25 and in the context of international law.

The well-known international tax case of *National Westminster Bank plc v United States*<sup>71</sup> is a good example of how the UK tax authority was unable to successfully alleviate the double taxation suffered by Natwest. The Taxpayer, Natwest, had to litigate for thirteen years in the USA to ensure that the tax treaty between the USA and the UK was correctly applied.

The 1981 report by the Congress of the International Fiscal Association<sup>72</sup>, stated that in its observation, MAP did not protect taxpayers' rights. It listed the following examples in support of its view:

- Taxpayer has no right to initiate MAP;
- Taxpayer has no legal remedy, other than under domestic law, to enforce treaty provisions;
- Taxpayer has no right to access the MAP process; and
- The Authorities are under no obligation to resolve the dispute

Whilst these shortcomings were recognised in 1981, it appears that this situation persists, despite the best attempts by Action 14 to address them.

In concluding this aspect of the evaluation, it has been observed that whilst the actions contained in Action 14 accord in the main with rule of law principles, the dispute resolution process contained in Article 25 and on which Action 14 is based, appears to suffer from inherent problems. These problems have been highlighted in this Chapter, but as a general observation, it appears that the main defects in Article 25 are structural in nature. Tax treaties form part of international law, yet their true impact is felt in domestic law. International tax law segues between international and domestic law.

It appears from the above observations that the dispute resolution process as provided for in Article 25 of the model treaty, straddles international law norms and domestic law remedies. Whilst the Action 14 measures appear to address and improve Article 25, the article's effectiveness as a dispute resolution mechanism is still constrained by its inherent defects.

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<sup>71</sup> *National Westminster Bank plc v United States* USA Court of Appeal, Federal Circuit no. 2007-5028.

<sup>72</sup> International Fiscal Association, *Cahiers de Droit Fiscal International*, vol 66 (1981) Dr Karl Koch "General Report" at 93,99 and 100.

The remaining chapter will address Action 14 from an outputs perspective by focusing on South Africa's response and the specific actions that South Africa has adopted. This will be followed by a review of the peer review report on South Africa, which was released in October 2019, and the chapter will conclude with a finding on how effective Action 14 has been from a South African perspective. My conclusion will then focus on an evaluation of the full effect of Action 14.

## V. CHAPTER 4 SOUTH AFRICA'S RESPONSE TO ACTION 14.

### A. Introduction

The measures contained in Action 14 attempt to provide an effective international dispute resolution process. Whilst Action 14 does not have the force of law, it contains input from a group of approximately 50 sovereign States, with a common purpose to develop effective dispute resolution mechanisms. This alone does not give the actions the status of law. Within the broader BEPS Action plan, measures have been introduced to give the actions the force of law through the use of the Multi-Lateral Instrument ("MLI")<sup>73</sup>. The MLI is a comprehensive instrument containing all of the BEPS actions and has the effect of incorporating all the proposed treaty amendments into the existing international treaty network, simultaneously. South Africa, as a member of the Committee on Fiscal Affairs at BEPS, has adopted Action 14 measures into its treaty network via the Multi-Lateral Instrument ("MLI"). The MLI was signed by South Africa in June 2017, along with about seventy other States in a joint signing ceremony in Paris. The MLI must still be ratified in South Africa<sup>74</sup>; it is anticipated that this will happen in 2020.

The aim of the MLI is to enable States to implement the BEPS measures swiftly, thereby strengthening their treaties against tax abuse.<sup>75</sup> States are able to elect which treaties they wish to modify through the MLI by denoting them as "covered" tax treaties<sup>76</sup>. In addition, the MLI identifies which articles a State may "reserve"<sup>77</sup>, and which optional provisions it may opt out of at any time. This allows States that have adopted the MLI a certain amount of flexibility in amending their treaty network. This, it is submitted, is an acknowledgment that ultimately tax is a sovereign issue and that it is for the sovereign State to elect how it wishes to interact with

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<sup>73</sup> Op cit 14.

<sup>74</sup> See s231 of The Constitution of the Republic of South Africa, and confirmed in *Glenister v President of the Republic of South Africa* 2011 (3) SA 347 (CC).

<sup>75</sup> Multilateral Convention to implement tax treaty related measures to prevent BEPS, Information brochure published 22 March 2018, at unnumbered page 3 - <https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm> (accessed 3 December 2019).

<sup>76</sup> Article 2 of MLI, which defines "Covered Tax Agreement" "as an agreement for the avoidance of double taxation with respect to taxes on income that is in force between two or more parties and each party has made a notification to the Depositary listing agreement as an agreement which is covered by the MLI convention. <https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm> accessed on 3 December 2019.

<sup>77</sup> "Reserved" – meaning that the State was reserving the right not to adopt the article/provision in the form set out in the MLI.

other sovereign States. As mentioned previously, tax treaties do not impose tax; their stated aim is to relieve the incidence of double taxation arising from cross-border transactions by allocating taxing rights to contracting States.

Prior to the signing of the MLI, the South African treaty network, which consists of 80 tax treaties, provided for MAP as a dispute resolution mechanism in seventy-seven of its treaties. South Africa has 40 “covered” tax treaties, meaning that the MLI has only amended<sup>78</sup> half of its treaties. South Africa has indicated that it will endeavour to renegotiate these treaties that have not been “covered” on a bilateral basis to ensure that they fall within the parameters of the Action 14 minimum standards.<sup>79</sup>

## **B. Article 25**

### **i) Access to MAP**

The majority of South African treaties provided for MAP as a dispute resolution mechanism prior to the adoption of BEPS Action 14. However, it has been deemed necessary to incorporate the MLI and specifically the articles dealing with dispute resolution. This will ensure that South Africa achieves a certain amount of uniformity in the manner in which it deals with dispute resolution, as well as complying with the country’s obligations as a signatory to the MLI. It also ensures that South Africa’s position on how it will deal with dispute resolution, will be transparent, and further that the country will be bound to follow these procedures as a contracting party to a binding treaty.

Article 16 of the MLI deals with amendments to Article 25 of the model treaty, being the dispute resolution provision. South Africa has reserved the right under Article 16 (5)(a) to restrict access to MAP, as contained in Article 25(1) of its treaties, to South African residents. This reservation is in line with provisions in the rest of Article 16, as well as the minimum standard in Action 14. This is not much of a shift from the country’s prior position, as it previously (in 64 of its 80 treaties) restricted access to MAP to residents of South Africa. One treaty allowed taxpayers to approach either contracting State. There is also one treaty that requires a taxpayer to resort to domestic remedies simultaneously with MAP requests. On the

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<sup>78</sup> Subject to the ratification of the MLI by the South African government.

<sup>79</sup> OECD (2019), Making Dispute Resolution More Effective –MAP Peer Review Report, South Africa(Stage 1): Inclusive framework on BEPS: Action 14 , at 13 OECD/G20 Base Erosion and Profit Shifting Project , (OECD) Publishing Paris, <https://doi.org/10.17873f820b8e-en> accessed December 2019.

access to MAP requirement, South Africa's position in the majority of its treaties is that it permits its own residents access to MAP.

In addition, South Africa has introduced a bilateral consultation process which enables the other contracting State to provide its views on a case where South Africa considers the objection to be without merit.

In relation to the time limitation on lodging MAP requests contained in Article 25(1), which requires that MAP requests must be made within three years from the date of the action giving rise to taxation not in accordance with the treaty, the majority of the South African treaties (67 out of 80) are subject to this three-year limitation. South Africa also has seven treaties where the time limit for lodging MAP requests is restricted to two years, in line with domestic law. However it is noted that of these seven treaties, five are "covered" treaties where the treaty partners have also listed Article 25(1). This means that once South Africa ratifies the MLI, there will be only two treaties with a two-year time frame.

Access to MAP in transfer pricing cases is an essential requirement for alleviating economic double tax. Article 9(2) of the model treaty provides for States to make a corrective adjustment where a transfer pricing adjustment is made by a treaty partner. Before the MLI, South Africa had an Article 9(2) provision in 36 of its treaties. The balance of its treaties did provide for some sort of adjustment, but not in a mandatory manner. South Africa has now indicated through the MLI and specifically in the Action 14 measures that it will apply Article 9(2) and further that it will provide access to MAP in transfer pricing cases, provided the relevant treaty has MAP provisions.<sup>80</sup>

South Africa's treaties do not deny access to MAP in cases of anti-abuse or perceived anti-abuse cases. Neither does its domestic law prohibit access to MAP in anti-abuse cases.

On the issue of settlements, South Africa provides for administrative settlements. It has indicated that once settlements have been reached, access to MAP will be denied. Similarly MAP cannot override judicial decisions. However, the domestic appeals process can run simultaneously with a MAP application, but once a judicial decision has been reached, the MAP must be resolved in line with the decision.

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<sup>80</sup> South Africa's MAP Guidelines published by SARS, Legal Counsel Division *Guide on Mutual Agreement Procedures* (issue2) issued on 10<sup>th</sup> October 2018 at page 10. <https://www.sars.gov.za/Legal/International-Treaties-Agreements/Pages/default.aspx?country> accessed on 4 December 2019.

South Africa has indicated that it will not deny access to MAP for submitting an incomplete MAP request. It will endeavour to engage the Taxpayer to add the missing details.

Action 14 doesn't deal specifically with Article 4(3) of the model treaty. However, to the extent that the MLI has amended Article 4(3) and made MAP the tie-breaker for determining residence, it needs to be mentioned. The MLI provides that in cases of dual residence, the tie breaker is to lie in the MAP process. States are given the opportunity to opt out of applying Article 4(3). South Africa, however, has adopted Article 4(3). This is designed as an anti-abuse provision as it suspends treaty benefits until the MAP has resolved the residence of the taxpayer. The MLI is silent on whether the provisions relating to MAP in Article 25 automatically apply to dual residence MAPs; it is submitted that absent anything to the contrary, Article 25 applies. It has been confirmed by the Competent Authority for South Africa, SARS, that this is how South Africa interprets the application of Article 4(3) MAP requests.

South Africa has restricted access to MAP under Article 25(1) to its own residents. For purposes of Article 4T(3) MAPs where residence is the key issue in a dispute, South Africa requires that the Taxpayer obtain a certificate of residency from South Africa as well as the other contracting State before being allowed to apply for MAP. In its MAP guide<sup>81</sup>, South Africa has set out the factors it takes into account to determine place of effective management, which is the determinant of residence in these cases. This approach is in line with the OECD commentary on Article 4(3).

## **ii). Preventing disputes**

Article 25(3) directs contracting States to contain MAP provisions in their treaties to resolve any difficulties arising from the interpretation and/or application of the treaty. This article enables States to resolve any difficulties they may encounter in relation to the treaty via MAP. MAP in this instance is available as a remedy for States to resolve their difficulties with other States. MAP is not limited to issues affecting taxpayers.

South Africa has this provision in 76 of its treaties. It has also listed a notification in terms of Article 16(4)(c)(i), which provides that in the absence of Article 25(3) in its treaties, then by virtue of the MLI, Article 25(3) will apply to those "covered" tax treaties. Of the remaining four treaties that do not contain Article 25(3), only one is a "covered" tax treaty; but even in

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<sup>81</sup> Op cit 77 at 9.

this case, South Africa did not list a notification in terms of Article 16(4)(c)(i) of the MLI, which means that Article 25(3) will still not apply. In terms of the other three treaties, South Africa indicated in its input to the peer review<sup>82</sup>, that it would engage in bilateral negotiations to include Article 25(3), and in respect of future treaties it would endeavour to include Article 25(3).

The second part of Article 25(3) provides for States to resolve issues of double taxation in cases not covered by other provisions of the treaty, through MAP. South Africa has 71 treaties that contain this provision. Four of the remaining treaties are “covered” treaties and South Africa has noted that article 16(6)(c)(ii) of the MLI will apply. This means that these four treaties do not contain this Article 25(3) provision. As such, they will be amended by the MLI and from date of ratification, Article 25(3) will apply to them. This will mean that South Africa, post ratification, will have access to MAP in a broad sense to resolve incidents of double taxation not covered by a treaty, in 74 of its treaties. For the remainder of its treaties that do not provide for MAP, South Africa has endeavoured to negotiate bilaterally with the relevant State to ensure it conforms to Action 14 measures.

### **iii).Making MAP accessible**

South Africa has complied with the best practice and minimum standards in Action 14 in making MAP more accessible to taxpayers. It has done this by adopting the following measures:

1. It has published a MAP guide<sup>83</sup>, which sets out clearly what MAP is, when it can be applied for, the documentation required to be submitted, applicable time periods, other remedies available and how MAP functions, amongst other matters.
2. It has created a MAP profile which has been published on the OECD website<sup>84</sup>
3. It has made its treaty partners aware of its domestic dispute resolution measures by publishing them in its guide and on its OECD profile.

### **iv).Arbitration**

Action 14 proposed that Article 25(5) be amended to include mandatory arbitration in the event that a dispute could not be resolved via MAP. In terms of Article 18 of the MLI which deals

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<sup>82</sup> Op cit 76 at 18, para 6.

<sup>83</sup> Op cit 77 at 8.

<sup>84</sup> [www.oecd.org/ctp/dispute/country-map-profiles.htm](http://www.oecd.org/ctp/dispute/country-map-profiles.htm) accessed December 2019.

with arbitration, States can elect to adopt the arbitration article. South Africa noted a reservation against Article 25(5), as it does not favour mandatory arbitration.

Arbitration is generally not favoured by developing countries as it is seen as giving up taxing rights<sup>85</sup>. They tend to favour the voluntary arbitration procedure adopted in the United Nations treaties. Despite its position, South Africa has mandatory arbitration clauses in three of its treaties.

### **C. Peer Review Report**

I have focused on the theoretical processes that South Africa has adopted in relation to Action 14. To complete this review, the peer review report<sup>86</sup> on South Africa's implementation needs to be considered. South Africa has only been subject to a Stage One review. The report was approved by the Inclusive Framework on the 8<sup>th</sup> May 2019. It covered the period from 1 January 2016 to 31 December 2017.

It has been divided into four parts, namely:

1. Preventing disputes;
2. Availability and access to MAP
3. Resolution of MAP cases
4. Implementation of MAP agreements

I have elected to focus mainly on the report's findings on MAP cases and implementation of MAP agreements, as I am of the view that these findings will ultimately determine the effectiveness of Action 14 from a South African perspective.

#### **i). Preventing disputes**

On the prevention of disputes, it was noted that the majority<sup>87</sup> of South Africa's treaties contain MAP provisions, which is indicative of an intention to prevent disputes. However, it was noted that 10 percent of its treaties did not contain an Article 25(3) equivalent, meaning that in these cases, where there is no relief for double taxation in a treaty, there is no other way to resolve a dispute. Absent MAP provisions, it is submitted that there appears to be no other way to resolve a dispute arising out of these treaties at an international level. Whilst in the majority of cases

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<sup>85</sup> [https://www.un.org/esa/ffd/wp-content/uploads/2017/03/14STM\\_CRP4\\_map-dar.pdf](https://www.un.org/esa/ffd/wp-content/uploads/2017/03/14STM_CRP4_map-dar.pdf) at 27, accessed December 2019.

<sup>86</sup> Op cit 76.

<sup>87</sup> 77 treaties out of 80 contain MAP provisions.

the Taxpayer will have domestic remedies available; there are no other international methods to resolve the dispute.

The recent Tax Court judgment, *ITC 14287*<sup>88</sup>, dealt with the interpretation of the Netherlands/South Africa double tax treaty, as well as South Africa's tax treaties with Sweden and Kuwait. The taxpayer, a South African resident, relied on the most favoured nation clause in paragraph 10(10) of the treaty with the Netherlands. This provides that the rate of dividends tax to be withheld by South Africa, is limited to the lowest dividend rate applicable in South Africa's treaties. The Kuwait treaty granted a sole taxing right to Kuwait in respect of South African-sourced dividends. This amounts in effect to a zero rate to be applied on the payment of dividends out of South Africa. The Kuwait treaty has been renegotiated to provide for a dual taxing right to both source and residence States. South Africa has ratified the treaty, but Kuwait has not ratified it yet, so the treaty is not in force. Until it has been ratified, the old Kuwait treaty applies.

Under the current regime that South Africa finds itself in, the country has limited remedies to rectify this untenable situation. This judgement opens the door for taxpayers resident in States whose treaties with South Africa contain most favoured nation clauses to request that these be applied, effectively giving them a zero rate of tax on dividends tax.

South Africa could possibly approach Kuwait via the MAP process to see if this situation could be rectified. Article 25(3) could apply (which provides for MAP in cases not covered by the treaty), but is this a "MAP-able" dispute? The desired outcome for South Africa would be an agreement by Kuwait to ratify the new treaty. The current treaty with Kuwait contains a MAP provision in Article 25(3). The treaty, as noted, allocates a sole taxing right to Kuwait; South Africa could argue that this in effect results in double non-taxation – which the BEPS action plan seeks to prevent, along with double taxation, as among its underlying purposes. However, the provisions of Article 21, which is a catchall for other income (limiting taxing right to the State of residence), could negate this argument around non-taxation.

A better remedy for South Africa would be to exercise its rights under Article 30 of the treaty. This provides for termination of the treaty by way of notice. In justification, South Africa could argue that Kuwait's inaction in failing to ratify the new treaty could be classified as acting in bad faith, and a breach of its international law obligations.

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<sup>88</sup> Case no14287 Tax Court Cape Town 12 June 2019 ITC 14287 81 SATC

The case raises more questions than it answers, but it does illustrate the potential of the MAP process as to resolve or prevent disputes on a wider scale. It is submitted that the ultimate resolution to the current impasse (for South Africa) would be for Kuwait to ratify the treaty. In this regard, it is submitted that attempts to resolve the impasse belong not at the Competent Authority level, but with the executive sphere of government, so this is where the engagement with Kuwait needs to take place. It appears that the South African government does not have the appetite to put any pressure on Kuwait to ratify, nor to take further decisive action like termination. This could be for strategic reasons, given Kuwait's strategic importance as an oil-producing country.

The peer review report's overall finding on South Africa's performance in preventing disputes is that South Africa should engage in bilateral negotiations with its treaty partners to introduce MAP into its existing treaty network and to include MAP in all future treaties.

#### **ii). Availability and access to MAP**

On the availability and access to MAP review, South Africa has adhered to Action 14 in that it includes Article 25(1) in the majority of its treaties<sup>89</sup>. In one treaty, South Africa requires that domestic remedies are pursued simultaneously with MAP, whilst its treaty with the United States grants MAP access to either State of residence or source State. The MLI will not amend the treaties that fall outside Article 25(1).

A bilateral notification process is in place in South Africa that permits the other contracting State to provide its views on matters where South Africa takes the view that the objection is not justified. In these instances, South Africa has undertaken to provide the other State with its legal opinions and views. The review of the peer review report found that South Africa has not considered any objection in a MAP request not to be justified. The report did make a finding that South Africa needs to formally document the process involved in the bilateral notification process as part of its internal operating procedures.

On the requirement to provide access to MAP in transfer pricing cases, South Africa has adopted Article 9(2) in 36 of its treaties. This requires one contracting State to make a corresponding adjustment for transfer pricing adjustments in the other State. The review found that 34 of the remaining treaties did not contain a mandatory adjustment, simply stating that adjustments "may" be made. South Africa has indicated that it will apply Article 9(2) in all its

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<sup>89</sup> In 64/80 treaties.

treaties that provide for MAP (this would mean that only three of its treaties would not provide access to MAP). To date, South Africa has not denied access to MAP on transfer pricing cases. South Africa has noted in the MLI that it will apply Article 9(2) in its treaties in the absence of a clause in its treaties, provided both parties have listed the treaty as a “covered” tax treaty under the MLI. South Africa has classified 40 of its treaties as MLI-covered.

South Africa has a number of treaties that do not comply with the Action 14 requirement that MAP requests must be made within three years of the occurrence of the event that amounted to taxation not in accordance with the treaty. The majority<sup>90</sup> do provide for a three-year time period in which to submit a MAP request. Three treaties have not limited the time period for requesting MAP. In two treaties, the MAP request period is linked to the domestic dispute resolution time periods, which is usually two years. Five of the treaties that do not comply with the Action 14-time period will be amended by the MLI to provide for a three-year time period, once ratified.

South Africa’s policy in regard to allowing access to MAP in anti-abuse cases is to permit access. Similarly, South Africa permits access to MAP where a matter is still under its domestic resolution process, but will deny access where a matter has been settled through its domestic process. In cases where an incomplete MAP application is submitted, South Africa would not deny access.

South Africa was found to be compliant with the requirements in respect of its reporting and making MAP accessible. The only negative finding was that it should include a timetable on the time taken to resolve each step in the MAP process. In addition, it was noted that South Africa should provide clarity on the effects on MAP where a matter is settled via the dispute resolution process.

### **iii).Resolution of MAP cases**

In line with Article 25(2) of the model treaty, contracting States are obligated to endeavour to resolve disputes by mutual agreement. In an attempt to ensure that this obligation is adhered to, and absent any other method of coercion, States are subject to peer review on their performance in resolving disputes via the MAP. This in my view is a form of “peer pressure”.

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<sup>90</sup> 67/80 treaties

As part of Action 14, States are required to maintain accurate MAP statistics, which are then reported to the OECD and published for all to see. The FTA MAP Forum<sup>91</sup> has developed regulations for the reporting of MAP statistics. South Africa has complied with this reporting requirement<sup>92</sup> and has put systems in place to liaise with its counterparts (treaty partners) for purposes of monitoring and communicating on the MAP caseload.

For the review period from 1 January 2016 to 31 December 2017, South Africa's caseload of MAP cases increased from 19 cases to 28 cases, which represents a 47 percent increase over two years. The MAP cases are split between attribution/allocation cases (12 cases) and other cases (16). The attribution cases include transfer-pricing cases.

In terms of the Action 14 objective of resolving disputes timeously, Action 3 set a time limit of two years for resolving MAP cases. South Africa's reporting complies with this time frame, as shown by the review and evaluated in the peer review. The average time taken to resolve disputes is 19,72 months.<sup>93</sup>

South Africa has denied MAP in 37 percent of its cases, a figure seemingly exacerbated by a further 11% of cases where it did not agree with the Taxpayer's submission claiming to have been subjected to taxation contrary to the treaty. The rest of the world has a six percent average rating for denying access to MAP. On the face of it, South Africa's denial of access to MAP is way out of kilter with the rest of the world. On further analysis of three other countries' caseloads, France has 972 cases<sup>94</sup>, Australia 31 and India 831 to South Africa's 28 cases. France denied access to MAP in 5,3 percent of its cases; Australia did not deny access but decided in 20 percent of its cases that the objection was not justified; while in India, only two cases were denied access, but the country's average time taken to resolve disputes is 60 months.

South Africa's Competent Authority (SARS) revealed on enquiry that the cases that were denied access to MAP were all outside the three-year time period for lodging a MAP case. As such, access had to be denied. The peer review report does not highlight this and in fact does not address this point directly. The criticism seems to be directed at SARS' lack of resources, leaving the Service not fully resourced to deal with MAP. The report concluded that despite

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<sup>91</sup> Forum on Tax Administration, formed in 2002 and consisting of 53 OECD and non OECD member States, the aim of the forum being to enhance tax administration globally [https://www.oecd.org/tax/forum-on-tax-administration/Forum\\_on\\_Tax\\_Administration](https://www.oecd.org/tax/forum-on-tax-administration/Forum_on_Tax_Administration) accessed December 2019.

<sup>92</sup> Op cit 76 at 47 para 105.

<sup>93</sup> Op cit 76 at 51 para 120.

<sup>94</sup> <http://www.oecd.org/tax/dispute/2018-map-statistics-france.pdf> accessed December 2019.

the significant increase in SARS' caseload in 2016, it may not be adequately resourced, and further that no specific actions have been taken so far to address this shortcoming.

The review on the measure to which SARS staff have the necessary authority to resolve MAP cases, independently of the operational side of SARS who would have made the adjustments, was favourable. It found that the staff do not appear to have any impediments stopping them from resolving MAP cases. The recommendation was that SARS should ensure that the MAP personnel are permitted to resolve MAP cases without interference, which already appears to be the case.

On the requirement of independent officials, the peer review found that the MAP staff at SARS were not motivated by the outcome of MAP cases in their performance contracts. As such, these officials were held to be sufficiently distanced from the outcome of any MAP case.

The final aspect the review dealt with was on South Africa's level of transparency in relation to MAP arbitration. South Africa reserved the right not to include Article 25(5) in its treaties. South Africa has opted for arbitration in three of its treaties. South Africa has no domestic law preventing arbitration in its treaties, so the country could make use of the United Nations model, which provides for voluntary arbitration. Developing countries in general do not seem to be in favour of mandatory arbitration. As far as South Africa has stated its position on arbitration, it has been transparent. What would have been more useful would be for the country to explain why it is not in favour of arbitration, and whether it intends to revisit this issue in the future.

#### **iv). Implementation of MAP agreements**

Article 25(2) provides for the implementation of MAP agreements, notwithstanding domestic law prescription provisions. South Africa has included this provision in 60 of its 80 treaties. This means that the treaties falling outside of this provision will restrict the implementation of MAP agreements, where the implementation would fall foul of domestic law prescription. Ten treaties will be remedied by ratification of the MLI by South Africa, and the balance of its treaties by bilateral negotiations.

In the review period it was noted that South Africa has not had to implement any agreement arising from the MAP.

With regard to the timely implementation of MAP agreements, South Africa in its guide mentioned that the domestic law provides for a three-year window from date of assessment. This would apply in the case of MAP adjustments, unless the treaty overrode this provision. South Africa indicated in the guide that once a MAP is agreed upon, its tax authority would grant the Taxpayer concerned 21 days to communicate acceptance of MAP. This is prior to giving effect to the agreement.

#### **D. Application of the Benchmark**

In the introductory part of this chapter, the legal status of the dispute resolution measures was highlighted. The process of ensuring that these measures were incorporated into a State's treaty network does not automatically mean that they now represent an effective dispute resolution mechanism. The measures themselves have been identified and discussed, and their practical application in South Africa has been reviewed. The rule of law has been identified as the measure against which the associated actions are to be measured; what remains is to determine whether these measures comply with the rule of law.

In Chapter 2 we identified the rule of law measures to be used, namely:

1. Timely resolution of disputes;
2. Accessibility to the process;
3. Adequate resources;
4. Competency of officials; and
5. Independence of officials.

Applying these measures to the South African response in enacting Action 14 measures, the following has been observed:

##### **i). Timely Resolution of disputes**

South Africa has complied with the time periods set out in Action 14, and has resolved MAP cases within the two-year time period. However, it has been observed that in relation to transfer pricing cases, the time period may in future not be adhered to, given the complexities of these cases and the lack of a dedicated MAP resource.

## **ii). Accessibility to the Process**

South Africa denied access to MAP in 37 percent of its cases. In all these cases the taxpayers' applications fell outside the three year time period for applying for MAP relief. It is submitted that absent any further explanation on this finding, the conclusion can be made that a simple objective time factor is applied to applications without any subjective evaluation of the factors involved. Given that the Action 14 measures are a relatively new concept, one would expect a level of leniency with regard to applying time limits. This even more so, given that this is the only remedy the taxpayer has. A domestic remedy may exist; but a denial of access to MAP, which is possibly a cheaper and quicker process than resolution through the domestic justice system, with no right of redress to the decision by the Competent Authority, appears to be heavy-handed. In the South African domestic appeal system, where there are time limits for lodging appeals, there is a provision allowing objections to a denial on the timing aspect, provided exceptional circumstances can justify relaxing the time periods. It is submitted that a similar provision in the MAP timelines would make MAP more accessible in instances where exceptional circumstances exist for failure to comply with the three-year time period. Such a change would also indicate a less formulaic application of the provisions, and more of a substantive application, giving effect to the intention to provide access to the process in justifiable circumstances – what Dr Pim Albers<sup>95</sup> calls a “thin” notion of the rule of law.

In addition, on the accessibility aspect, South Africa has elected to adopt Article 25(1) option which permits access to MAP only to resident taxpayers. This can be seen as an unnecessary restriction to access. Apparently, the reasoning for South Africa adopting this stance is that it is under-resourced and could not cope with MAP requests from non-resident taxpayers. It is submitted that the taxpayer may be a resident of the other contracting State and as such would have access to MAP through that State's Article 25(1).

## **iii). Adequate Resources**

In a number of areas, South Africa was evaluated as being under-resourced. South Africa does not have a dedicated MAP team. However, if one notes that despite this finding, SARS still manages to comply with the turnaround time in respect of resolution of MAP cases and the fact that currently its caseload is not excessive, this problem is not impacting negatively on its

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<sup>95</sup> Op cit at 42.

ability to function. However, in the long term this could prove problematic and affect SARS' ability to provide an effective MAP function.

#### **iv.) Competency of Officials**

The peer review report indicated that the level of competency of South African officials was of a standard to resolve MAP cases. Without any further information on the merits of the cases resolved and the issues at stake, one is unable to make any further comment on this aspect.

#### **v). Independence of Officials**

The independence of the process was evaluated and found to meet the required standard, in that the SARS officials handling MAP are given the necessary authority to conclude MAP settlements independently of the audit process that may have been involved in creating the dispute. The officials were also found not to have a personal or vested interest in the outcome of the process.

### **E. Findings**

Whilst these findings appear to comply with the rule of law standard, the review is performed in a tick-the-box format. The peer review, whilst serving a function of assessing how compliant States are in resolving MAP disputes, cannot assess the effectiveness of the process as a whole. This is not a function of a peer review – a consideration which, it is submitted, indicates that the review fulfils more of a peer pressure function to obtain universal buy-in to the process. It is accepted that the peer review was never intended to be indicative of the effectiveness of Action 14.

A review of the effectiveness of Action 14 needs to look at the system as a whole, as well as the context in which Action 14 has been developed. For example, if one drills deeper into the access to process requirement, it is found that the Taxpayer, who is generally the aggrieved party is not directly involved in the process. Up to now, the focus has been on the specific measures and actions contained in Action 14. What remains is to assess the effectiveness of the system as a whole.

As mentioned above, Action 14 needs to be contextualised. It arose out of a need to address a system that was not working effectively as well as to address the increased caseload arising out

of the other BEPS measures<sup>96</sup>. As has been seen in our review in Chapter 1, the actions proposed included making adjustments to the existing MAP provisions in Article 25 of the model treaty. It is unclear whether any analysis of the pre-existing MAP provisions was undertaken first, but it is submitted that this approach of tinkering with the pre-existing system may have been short-sighted. If the aim of the exercise was to make dispute resolution more effective, surely the existing system should have been thoroughly analysed to see if it was fit for purpose.

An analysis of the criticisms levelled against the pre-existing system indicates that there were some inherent structural issues with MAP. For example, Katerina Perrou<sup>97</sup>, in her doctoral thesis *Taxpayer Participation in Tax Treaty Dispute Resolution*, is of the view that the exclusion of direct taxpayer participation in MAP is a failing. The writing predated BEPS Action 14; however, the points she makes are still relevant as taxpayer involvement has not been addressed and point to the structural defects inherent in the current MAP system.

Perrou makes the point that the MAP, being embedded in a treaty, becomes a State-controlled process. A double tax treaty is an international agreement between States. As an international agreement, the State is obligated to ensure that its rights and obligations in terms of the treaty are protected, including the rights of its nationals to be taxed in accordance with the treaty. The State in this instance provides diplomatic protection to its nationals. Diplomatic protection, which can only be provided by a State, naturally excludes direct involvement by the taxpayer. Perrou points out that when treaties were initially drafted, taxation was levied on nationals of a State. With the advent of time and globalisation, this notion has changed and taxation is now to a large extent residence-based. This does not equate to nationality. She submits that the crafting of MAP onto this system was the wrong foundation from the start<sup>98</sup>. Her argument is that whilst MAP as a system based on diplomatic protection may be fit for dealing with general disputes between States (excluding specific taxpayer disputes), it is not fit for the purpose of resolving taxpayer disputes.

It is acknowledged that dispute resolution in the context of international law is difficult, as it straddles domestic and international law regimes. This is reflected in the difficulty in providing just remedial action to resolve disputes arising out of this dichotomous situation. In an attempt

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<sup>96</sup> <http://www.oecd.org/ctp/BEPSActionPlan.pdf> at 4 para 3 accessed December 2019.

<sup>97</sup> Op cit at 57.

<sup>98</sup> Op cit 57 at 13.

to address this hybrid situation, Perrou suggests that direct involvement in the MAP process by taxpayers could address some of the inherent difficulties. This could go some way towards addressing the issue of fair trial rights, which are embedded in our Constitution and in fact in most legal systems. Where a party is directly aggrieved by the actions of a State, it should be entitled to a remedial system that at the very least permits direct access to the aggrieved party, despite the fact that the dispute may involve the actions of another State. In the current MAP process, the State has a stake in the outcome of the case (collecting taxes) and its actions may have given rise to the dispute, yet it is the one meant to protect the taxpayer. This situation potentially goes against fair trial rights, access to justice and basic administrative law principles.

J Croner, in an article entitled '*A new Approach to International Taxation Dispute Resolution Process*'<sup>99</sup> is also of the view that taxpayers' lack of standing is the main reason why taxpayers mistrust MAP and are sceptical of its effectiveness. This article was written post the release of Action 14.

The shortcomings of the MAP system have been acknowledged in Action 14 in the minimum standards and best practices that have been proposed. However, these have not been able to cure the inherent structural defect in MAP. The introduction of mandatory arbitration in Article 25(5) goes some way to address the fundamental flaws in MAP, both in terms of the lack of direct taxpayer involvement and introducing objectivity into the process by interposing an independent arbitrator into the decision-making process. Arbitration also provides another avenue to obtain redress if MAP fails. When agreement cannot be reached in the MAP, and the relevant treaty does not provide for arbitration, the taxpayer is left with no other remedy to pursue at international level.

Article 25(3) has been criticised for failing to make it obligatory for States to reach agreement under MAP. This also applies in the case of Article 4(3) where MAP is the tie breaker instrument. In an IBFD publication titled '*International –Dual Residence of Companies under Tax Treaties*'<sup>100</sup>, the point is made that the new Article 4(3) of the model treaty as proposed under BEPS Action Plan does not impose an obligation on States to reach agreement on

<sup>99</sup> [https://library.croneri.co.uk/iectr-wkus\\_tal\\_15926-2017045005-klitaxi450503](https://library.croneri.co.uk/iectr-wkus_tal_15926-2017045005-klitaxi450503), at page 11, accessed on 24 January 2019.

<sup>100</sup> Maisto et al *Dual Residence under Tax Treaties* International Tax Studies (IBFD)2018 vol 1 no 1 at para 5:3:2:2 [https://research-ibfd-/collections/itaxs/html/itaxs\\_2018\\_01\\_int\\_1.html#itaxs\\_2018\\_01\\_int\\_1\\_s\\_5](https://research-ibfd-/collections/itaxs/html/itaxs_2018_01_int_1.html#itaxs_2018_01_int_1_s_5) accessed on 19<sup>th</sup> November 2019.

residency. This leaves taxpayers in limbo, as they are excluded from the deliberations; they are not able to access information about the decision-making process (or lack thereof), and if no decision is reached they have no further remedy under MAP, unless the treaty provides for arbitration.

This does leaves them with a limited remedy under domestic law, in the form of a judicial review of the decision. In footnote 329 to the article, this point is made in relation to South Africa. Taxpayers are entitled to just administrative action which should be accompanied by a reasoned explanation for the action by the Administrator. Where these reasons are insufficient, then taxpayers are entitled to apply for a domestic court to review the decision on administrative justice grounds.

Article 25(5), which provides for mandatory arbitration, has not been universally adopted. South Africa, as mentioned earlier, has entered a reservation on Article 25(5), but does have arbitration in 3 of its treaties. Generally, as noted earlier, developing countries do not favour mandatory arbitration as it is seen as giving up the sovereign right to impose tax. The United Nations voluntary method seems more favourable to developing nations. It is submitted that South Africa would do well to consider use of the UN model of voluntary arbitration.

Ana Paula Dourado and Pasquale Pistone, in an editorial for *Intertax*<sup>101</sup> titled 'Some Critical Thoughts on the Introduction of Arbitration in Tax Treaties', state that arbitration has been seen as incompatible with the rule of law principle on the separation of powers, where the courts are seen as the interpreters of the law. They submit that in tax law, specifically in international tax matters, it is only issues of fact that can be subjected to arbitration<sup>102</sup> under Article 25(5). They argue that arbitration when used as a tie-breaker instrument is compatible with the rule of law. Reference is also made in the editorial to the obstacles in developing countries with regard to arbitration and the need for a mentoring-type role by international organisations. They conclude by acknowledging that whilst arbitration may not be the best solution, especially in building a body of international case law, it is the best solution available.

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<sup>101</sup> AP Dourado and P Pistone 'Some critical thoughts on the Introduction of Arbitration in Tax Treaties' (2014) volume 42 Issue 3 *Intertax*.

<sup>102</sup> Only matters falling into article 25(1) can proceed to arbitration.

## **F. Conclusion**

In summary, the implementation of BEPS Action 14 measures by South Africa and the peer review of its actions to date in this regard, have raised some issues about the effectiveness of Action 14. The implementation has been to a large extent compliant with Action 14 measures, which indicates South Africa's willingness to adopt these dispute resolution measures into its treaty network. The peer review has also shown that South Africa has been relatively successful in implementing the measures. The review finds that where problems have been identified in some of its treaties, South Africa's response has been to address these problems through bilateral negotiations, in order to bring its treaty network in line with Action 14. The main problem facing South Africa's effective implementation of Action 14 is the ratification of the MLI, but this will hopefully be addressed in 2020. The other main area that was highlighted in the peer review was the shortage of resources in dealing with MAP. South Africa's MAP caseload is relatively small at this stage and is not expected to increase dramatically in the short term.

## **VI CONCLUSION: THE EFFECTIVENESS OF BEPS ACTION 14**

The focus of this minor dissertation has been on the effectiveness of the Action 14 measures flowing from the BEPS Project. From the start of the BEPS Project in 2013, substantial milestones have been achieved in the international tax arena. The Project's final report was released in 2015, followed by the incorporation of these measures through the MLI in 2017. This has resulted in the measures being incorporated into a substantial number of double tax treaties internationally. In my view, the fact that consensus could be achieved by a significant number of countries on what are typically highly litigious and contentious topics in international tax, is testimony to the acknowledgement that traditional tax rules could not deal with the realities of globalisation.

The intention behind Action 14 was to provide an effective dispute resolution system for the increase in disputes arising from the new "world order" under BEPS. It was ambitious in its aim to provide a speedy and efficient universal system to resolve disputes between states. Whilst there was an existing dispute resolution system in the form of MAP, it was felt that the system needed to be improved to support the BEPS measures. The improvement has not resulted in a new dispute resolution system. Rather, new design elements based on rule of law principles have been introduced. This in itself cannot be faulted, as the rule of law has stood the test of time and is universally accepted and incorporated into modern democratic states.

In attempting to debate the effectiveness of Action 14, the following questions were raised in the introduction:

1. Has Action 14 improved the international dispute resolution measures, and
2. How effective are South Africa's international dispute resolution processes?

These questions have been discussed and dealt with in preceding chapters. The findings on these questions can be summarised as:

1. Objectively, the measures in Action 14 comply with the rule of law measures, which is commendable. It has resulted in a more uniform, universal and transparent dispute resolution system, subject to peer reviews to promote compliance amongst States. It is

accessible in the sense that the provisions have been clarified and made publicly available. This is an improvement on what had existed prior to Action 14;

2. South Africa's adoption and application of the Action 14 measures has to a large extent conformed to Action 14. Its peer review report indicated that it has complied to a large degree with its obligations.

In addition, my evaluation shows that whilst the principles of Action 14 are admirable, the system onto which they have been crafted is not fit for purpose. MAP is inherently contrary to the rule of law, in that it does not permit the aggrieved party, namely the taxpayer, access to the process. It permits parties who have vested interests in the dispute, i.e. the State, to be gatekeeper and decision-maker, with no right of appearance for the taxpayer. We have seen that international tax law, being part of international law, is subject to the diplomatic perspective that governs a State engaging with another State, requiring it to protect its citizens' rights. The problem is that in most international tax cases, the very rights which the State is ostensibly protecting when it engages with other States, are the citizens' rights which the State itself is not honouring. In particular, this is so of the right of the citizen to be taxed in accordance with domestic laws and not to be subjected to double taxation. Added to this is the fact that MAP does not compel States to resolve the dispute. The final remedy is mandatory arbitration, but not all states have adopted this provision.

What is the solution to these problems, which it appears Action 14 has not resolved and which detracts from its effectiveness?

As a starting point, permitting a taxpayer access to the MAP system as an affected party would address part of the shortcomings. It is submitted that there are sufficient technological means of communication to enable taxpayers to present their issues or potential issues without incurring substantial travelling costs.

There is no simple remedy to compel States to resolve disputes.

The lack of enforcement measures in international law has been highlighted. The use of regional forums like ATAF<sup>103</sup> could be used to as an additional measure to compel resolution, where states fail to adhere to their own laws. For example, there is a current issue around granting credit relief under domestic law where source States do not strictly apply their own

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<sup>103</sup> ATAF- African Tax Administration Forum consisting of members from African States.

domestic tax legislation. Taxpayers are left with no remedy to pursue, as the State of residence cannot grant relief where tax was not legally deducted (i.e. in terms of tax legislation). Often the source State is not prepared to engage on the issue. This appears to be a regional problem and could be addressed through regional forums, absent any other remedy available to the taxpayer. The region could bring pressure to bear on the State concerned in order to achieve compliance.

The establishment or utilisation of existing international tribunals or courts, like the European Court of Justice or the International Court of Justice, has been mooted as a solution to resolving international tax disputes. It is submitted that a more appropriate solution would be to apply the current trend in litigation to move away from litigious processes towards mediation and arbitration, given the benefit of flexibility and the cost factor.

The case for arbitration has been made in Action 14 by including mandatory arbitration, however as mentioned previously, not all States have adopted this option. The two arbitration methods that have been adopted to date by States are not viable options for all States it seems. The baseball arbitration method, where the Arbitration Panel is called on to make a binary decision, is favoured by some developed countries, like America and Canada. This format does not require the Panel to debate the opinions presented and provide a reasoned based decision. This in itself flies in the face of the rule of law. Developing countries who lack the resources and necessary skill and expertise do not favour this binary option.

The other arbitration method, the independent approach which is favoured by the EU, is possibly in line with the rule of law as it requires the Panel to debate the opinions of each State and come to a reasoned based decision.

Perhaps States need to take heed of the advice offered by Abraham Lincoln

*'Discourage litigation. Persuade your neighbours to compromise where you can. Point out to them how the nominal winner is often a real loser-in fees, expenses, and waste of time. As a peacemaker, the lawyer has a superior opportunity of being a good man. There will still be business enough'.*

The main finding arising from this research is that whilst the measures contained in Action 14 on their own appear to meet the rule of law criteria, the system of MAP does not meet rule of law measures. Structural reform of the MAP system needs to be undertaken to address these

rule of law failings. It is my view that Action 14, as the only dispute resolution mechanism for international tax issues, cannot be classified as effective until these reforms are undertaken.

Mindy Herzfeld, in a 2019 article in *European Taxation*<sup>104</sup>, is critical of attempts to find solutions to resolve cross border tax disputes. She is of the view that attempts to adopt a one size fits all approach to dealing with anti-avoidance will create uncertainty and could result in dispute resolution becoming politicised. She advocates a more plurilateral approach as opposed to a multilateral approach to resolving international disputes, and sees the EU approach to cross border dispute resolution as a more viable solution than the OECD proposals under BEPS.

The approach adopted by the European Union, as part of its attempts to reform its tax dispute resolution framework, is contained in a Directive<sup>105</sup> issued in 2017 and effective from July 2019. The Directive attempts to resolve some of the structural defects of its own dispute resolution mechanisms as well as incorporate and improve upon Action 14 measures. Jonathan Schwartz<sup>106</sup> is of the view that the EU tax dispute resolution approach should be extended to countries outside the EU, which would ‘revolutionise the area’. The enforceability of decisions<sup>107</sup> reached does make the EU approach attractive in one sense.

Some of the measures adopted in the Directive include speedy resolution of disputes within 18 months, publication of decisions reached, and importantly gives taxpayers the ability to intervene in the process.

K Perrou<sup>108</sup> has advocated that an Ombudsman should be created for the MAP procedure, to ensure that taxpayer rights are protected.

It is submitted that the suggestions and proposals made to Action 14 and specifically dispute resolution in the international tax arena are worthy of consideration. The problem however is how to achieve consensus. The issues will not go away and there will be a lot more debate

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<sup>104</sup> Mindy Herzfeld ‘European Union/International –Resolving Disputes in a Lawless World’ *European Taxation* vol 59(2019).

<sup>105</sup> EU Directive on dispute resolution (2017/1852).

<sup>106</sup> Jonathan Schwartz *The EU Sets the Standard for International Tax Dispute Resolution* (Temple Chambers Kings College London); <http://arbitrationblog.kluwerarbitrationblog.kluwerarbitration.co> accessed on 24<sup>th</sup> January 2019.

<sup>107</sup> EU member States are subject to the jurisdiction of the EU Court of Justice.

<sup>108</sup> K Perrou *The Ombudsman and the Process of Resolution of International Tax Disputes –Protecting the “invisible party” to the MAP* 10 *World Tax Journal* (2018) *IBFD Journals* (accessed on 25 January 2019).

before consensus is reached, if ever. Debate and discussion is positive provided it ultimately leads to a viable solution.

IBEPS Action 14 has put dispute resolution processes on the agenda in international tax. It has attempted to achieve a greater level of consistency and uniformity in the way in which dispute resolution is handled. What still needs to be addressed are the needs of taxpayers. Until there is a realignment of dispute resolution mechanisms which directly address the concerns of the taxpayer, Action 14 will not be fully effective.

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