

Have the OECD Transfer Pricing Guidelines influenced  
the development of domestic legislation for transfer  
pricing and the outcome of court decisions in selected  
African states?

By

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## ABSTRACT

The Organisation for Economic Cooperation and Development (OECD) Transfer Pricing Guidelines (TPG) is a soft law instrument that acts as a guide to many multinational entities (MNE) in applying the arm's length principle (ALP). Amongst OECD member states, the OECD TPG is a relevant instrument to provide guidance to MNEs and Tax Administrations on how to apply the ALP. In transfer pricing legal disputes, international court judgments discussing the ALP touch on the influence of the OECD TPG. Every case may vary depending on the circumstances in each case and the time the ALP was enacted as part of hard law.

This paper aims to answer the question, *“Have the OECD TPG influenced the development of domestic legislation for transfer pricing and the outcome of court decisions in selected African states?”* A sample of literature was reviewed to understand the use of the OECD TPG as a soft law instrument within the international law landscape. Thereafter, a sample of international TP case law that references the OECD TPG was inspected to understand and analyse the stance of the OECD TPG. A systematic review was conducted on a sample of international transfer pricing court judgments to determine the weighting that the OECD TPG acts as a soft law instrument in the international tax community. A sample of African TP disputes in Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe was inspected to understand the status of the OECD TPG by the courts and the subsequent developments within the domestic tax legislation since the court judgment to determine whether the OECD TPG had any influence in shaping its domestic tax legislation.

Through this analysis, the author attempted to understand the influential status of the OECD TPG within an African regional context despite many African countries not holding a member status with the OECD and some African countries holding observer status or act as key partners with the OECD. Where the domestic TP tax legislation lacks guidance on the application of the ALP, the OECD TPG does hold a higher status in most OECD member countries. The status of the OECD TPG varies across different jurisdictions in the sample of countries selected. It should be noted that the case law inspected is not exhaustive of the court decisions discussing the ALP for all African countries. The OECD TPG status within Africa started as a soft law instrument, but over time, it has proven to be a focal area in developing TP regulations and the domestic TP tax legislative frameworks in Africa.

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## Table of abbreviations and terms

<b>Abbreviation</b>	<b>Meaning</b>
AE	Associated Enterprises
ALP	Arm's Length Principle
ATAF	African Tax Administration Forum
BGR	Binding General Ruling
CJEU	The Court of Justice of the European Union
CUP	Comparable Uncontrolled Price
DTC	Double Tax Convention
FIRS	Federal Inland Revenue Service
GPM	Gross Profit Margin
IFA	International Fiscal Association
ITA	Income Tax Act
IBFD	International Bureau of Fiscal Documentation
ITLR	International Tax Law Reports
KRA	Kenya Revenue Authority
MTC	Model Tax Convention
MLI	Multilateral instrument
MRA	Malawi Revenue Authority
NT	National Treasury
OECD	Organisation for Economic Co-operation and Development
PLI	Profit Level Indicator
SA	South Africa
SARS	South African Revenue Service
SCoF	Standing Committee on Finance
TC	Tax Court
TNMM	Transactional Net Margin Method
TPG	Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, Paris (2022)
TRA	Tanzania Revenue Authority
UK	United Kingdom
UKL	Unilever Kenya Limited
UUL	Unilever Uganda Limited
UN	United Nations
VCLT	Vienna Convention on the Law of Treaties (1969)
ZATC	South African Tax Court

## Chapter 1: Introduction

### 1.1. Background

The African Tax Administration Forum (ATAF) has acknowledged that transfer pricing (TP) within African countries is complex.<sup>1</sup> African countries have made great strides to bring TP legislation into their domestic tax systems; however, this gain can be offset by the lack of enforceability by the tax administrations.<sup>2</sup> Where a multinational entity (MNE) has determined an arm's length TP approach and the application thereof is challenged by the tax authorities, an adjustment may be triggered if its enforceability is allowed by the domestic tax legislation.<sup>3</sup> The Organisation for Economic Co-operation and Development (OECD) provides guidance to taxpayers on how to apply the arm's length principle (ALP) within the relevant Model Tax Convention (MTC) through supplemental aids such as the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, Paris (2022) (herein referred to as the OECD TPG).

The World Bank has characterised tax reform within developing countries as a means of improving economic and social infrastructures in a way that protects the tax base of a state.<sup>4</sup> Tax administrations in developing countries face problems of limited resources to deal with complex tax legislation.<sup>5</sup> The European courts are better resourced to deal with unique and complex financial transactions of a particular industry.<sup>6</sup> The number of TP cases available in the African continent is limited, which is

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<sup>1</sup> A.W. Oguttu, *Base Erosion and Profit Shifting: A Blueprint for Africa's Response* (IBFD 2021), Books IBFD.

<sup>2</sup> A.W. Oguttu, 'Factors That Exacerbate BEPS in Africa', in *Base Erosion and Profit Shifting: A Blueprint for Africa's Response* (Books IBFD, 2021). Refer to section in chapter 2.2. stating, "The development of the international tax jurisprudence in Africa will require not only relevant laws to be enacted but also having court judges that understand international tax laws and rightly rule on international tax cases. This will require African countries to train their judges on international tax law matters."

<sup>3</sup> E Baistrocchi, *Article 9: Associated Enterprises - Global Tax Treaty Commentaries*, Global Topics (IBFD, 2020).

<sup>4</sup> M.H.J. Alink & V. van Kommer, Chapter 4: Organizational Structures – Features of Tax Administration Design in Handbook on Tax Administration (Second Revised Edition) (IBFD 2016), Books IBFD. Refer to section, "4.13. Trends in developing countries".

<sup>5</sup> T Diniz Magalhães, 'What Is Really Wrong with Global Tax Governance and How to Properly Fix It', Vol. 10 World Tax Journal, No.4 (2018). Refer to section 2.1. of the article "Expertise as a source of misrepresentation, or the problem of technocracy."

<sup>6</sup> M.H.J. Alink & V. van Kommer, Chapter 4: Organizational Structures – Features of Tax Administration Design in Handbook on Tax Administration (Second Revised Edition) (IBFD 2016), Books IBFD.

driven by the political history unique to each country.<sup>7</sup> Also, TP cases are often settled before they even reach the court, further limiting the number of TP cases available within Africa.<sup>8</sup>

Tax administrations in different states could interpret the commercial substance and arm's length nature of a transaction differently to that of the taxpayer in the Base Erosion and Profit Shifting (BEPS) project. Complex TP disputes involving the tax administrations in different states creates a risk where a tax administration in one state could tax the cross border TP income whilst the tax administration in the other state impose a non-deductible TP cost on the same transaction. This arises if the tax administrations in the TP dispute hold differing views on the commercial substance and arm's length nature of the transaction leading to double taxation for the taxpayer.<sup>9</sup> The Commentaries to Article 9 of the 2017 OECD Model Tax Convention (MTC) refer to the use of the OECD TPG as an "authoritative statement" (see 2.1. and 2.2.) as to the interpretation and application of the ALP between associated enterprises (AE).<sup>10</sup> It is of particular interest to see how the sample of African countries court rulings have used the OECD TPG at a time when little to no actual TP legislation existed within the country's domestic tax legislation (see results in Chapter 3 and the analysis in Chapter 4). The African Tax Administration Forum (ATAF) MTC is a hybridized version of the OECD and United Nations (UN) MTC.<sup>11</sup> It is expected that courts in Africa will be influenced, to some degree, by the international developments of the OECD when applying the ALP as contained in Article 9 of the OECD MTC and UN MTC.

With only a limited number of court cases addressing the implementation of the ALP in cross border transaction within the African continent, it is useful for tax administrators and MNE taxpayers to

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<sup>7</sup> For instance, in South Africa, political sanctions on economic trade were imposed on South Africa during the Apartheid regime shunning South Africa from participating in the international sphere contributing to the limited number of transfer pricing cases available. See literature from R Carvalho et al, 'Is There Evidence of Increasing Harmonization in the Interpretation of Tax Treaties by Courts in Their Reference to Foreign Court Decisions? A Study of South African Case Law', Vol. 71 *Bulletin for International Taxation*, No. 10 (2017). Also C West, 'From Colonialism to Apartheid: International Influence on Tax Treaties in South Africa (1932-1990)', in *Income Tax in South Africa: The First 100 Years (1914-2014)*, eds. J Roeleveld, J Hattingh, and C West (Juta and Company, 2016).

<sup>8</sup> J Kotze and W Horak, 'Chapter 14: South Africa', section 3: "Appeals and Litigation" in *Transfer Pricing and Dispute Resolution: Aligning Strategy and Execution*, ed. A Bakker and MM Levey (IBFD, 2011). As an example, in South Africa Kotze and Horak acknowledges that many TP cases in South Africa are settled by negotiation. Similar mechanisms are available in other African countries to facilitate a settlement of a complex TP case by negotiation before the court judgment.

<sup>9</sup> S Rocha & L Schoueri, in *General Report: Future of Transfer Pricing (IFA) Cahiers* vol. 102B, 2017), Online Books IBFD. It is reported on p.34, "The Swedish branch report voiced a different concern: that "[t]he BEPS project is likely to result in complex disputes given the focus on substance and important functions performed, as tax administrations in different jurisdictions could interpret the commercial reality underpinning TP policies differently. This could end up being a cause of double taxation."

<sup>10</sup> OECD Model Tax Convention on Income and on Capital art. 9 (1963 to 2017). Refer to Appendix 1 for an OECD comparison of the Commentary to Article 9 of the OECD MTC for the periods 1963 to 2017.

<sup>11</sup> C West, 'Emerging Treaty Policies in Africa – Evidence from the African Tax Administration Forum Models', *Bulletin for International Taxation* 75, no. 1 (2021). See p.11.

understand the influence that the OECD TPG has as a soft law instrument amongst non-OECD member countries.

## 1.2. Objective of research / Research question

The aim of this study is to assess the extent to which the OECD TPG have influenced the development of domestic rules for transfer pricing and the outcome of court decisions in selected African states.

To perform this assessment, the study begins with a systematic review of a sample of international TP cases addressing the OECD TPG. This first analysis seeks to identify any common trends that could explain the transfer pricing legislative landscape amongst OECD member and non-OECD member countries and is covered in chapters 2 and 3. Chapter 2 discusses a sample of international opinions from various scholars dealing with the status of the OECD TPG as a soft law instrument. The global literature inspected provides a balanced opinion of the use of the OECD TPG as a soft law instrument within the international TP legislative environment within OECD and non-OECD member countries. The review provides a useful understanding of the complexities involved where the court judgments relied on the OECD TPG or where they did not. The findings of Chapter 2 are further explored in Chapter 3 through the observation of trends in a sample of international court judgments amongst OECD and non-OECD member countries.

The trends found in Chapter 3 are compared against a sample of those African countries analysed as part of Chapter 4. The assessment of the legislation and case law of the African countries also take into account the TP legislation in effect at the point in time when the case was decided. The developments in the domestic tax legislation for periods after the relevant case was decided is also observed in this dissertation to test whether the OECD TPG later shaped the domestic tax legislation of the country during TP reform and whether greater or less reliance was placed on the OECD TPG. This analysis is addressed in Chapter 4.

Understanding the influence of the OECD TPGs will help to gather insights into how the domestic TP legislative framework amongst African countries has been developed and infer how it could be developed in countries that have a young TP legislative environment within Africa. This paper will focus on a sample of case law within the African continent that addresses the ALP to determine the influence of the OECD TPG in shaping domestic tax legislation dealing with the ALP in selected African countries.

This study gains insight to how Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe are applying the ALP as part of their domestic tax legislation and analysing the court interpretation of the ALP and, where applicable, the use of the OECD TPG as a soft law instrument to aid the decisions. The study further analyses how the OECD TPG have shaped the domestic TP tax law when determining the ALP, especially after any court cases.

### 1.3. Research method and sample creation

#### 1.3.1. Introduction

This study obtained a sample of transfer pricing court cases, addressing the OECD TPG as a soft law instrument, from the International Bureau of Fiscal Documentation (IBFD) and the International Tax Law Reports (ITLR) databases to understand the weighting of the OECD TPG in the courts of various countries.

The sample of international tax cases was used to determine whether the OECD TPG, as a soft law instrument, have shaped the domestic tax legislation or whether the domestic legislation has, by direct reference, sought to elevate the OECD TPG to that of a hard law (black letter) instrument when applying the ALP.

By analysing the African tax cases at the time of the judgment and based on the domestic tax law governing the ALP, any mention of the OECD TPG in the courts' judgments and the developments after the court judgments are analysed for the sample of court cases to determine the influence and status of the OECD TPG, despite these African countries not being members of the OECD.

#### 1.3.2. Case law selection

To select the sample of cases, databases from the IBFD, ITLR and TPCases.com<sup>12</sup> were used to search for case law dealing with the OECD TPG when applying the ALP using a specific search criteria and filtering exercise.<sup>13</sup> The results provided case law from both OECD and non-OECD member countries addressing the ALP. The sample selection from the IBFD and ITLR databases were used to analyse the trends observed internationally for Chapter 3, and the TPCases.com database was used to widen the selection of TP cases within Africa for the analysis in Chapter 4 (and ensure the robustness of the selection of cases for Africa). Chapter 3 discusses the trends observed from the sample of international TP cases obtained from the case law in the IBFD and ITLR databases. Chapter 4 discusses in more detail the trends observed within a sample of case law from African countries and the influence that the OECD TPG have had on the domestic tax law within the same sample of African countries. Chapter 4 also addresses the current TP legislation for this sample of African states.

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<sup>12</sup> 'TPcases.Com', accessed 20 November 2022, <https://www.tpcases.com>. "TPcases.com provides a free and fully searchable database of international transfer pricing and tax avoidance case laws, news, guidelines, investigations and country profiles."

<sup>13</sup> Refer to section 1.3.3 and 1.3.4. of Chapter 1 below.

1.3.3. Sample selection for Chapter 3: Trends observed from a sample of international transfer pricing cases.

The data obtained for the trend analysis in chapter three was obtained by filtering the case law from the IBFD and ITLR databases with the search phrases described in the table below.

Results from database search criteria		
Database	Search phrase	Number of cases from the search
IBFD	transfer pricing guideline	672
IBFD	“OECD Transfer Pricing Guidelines”	186
IBFD	Practical Manual on Transfer Pricing	39
ITLR	“OECD Transfer Pricing Guidelines”	27
ITLR	Transfer Pricing Guidelines	33
Total number of cases		957

The output generated from the search criteria above gave a comprehensive (but non-exhaustive) listing of case law within the OECD Member and non-OECD member countries containing reference to the OECD TPG in its application of the ALP. A further filtering exercise was conducted to obtain a final sample of 166 cases. This sample of 166 cases was used to understand the international use and weighting that the OECD TPG has in court judgments.

The initial total sample of 957 cases obtained from these databases, spanning over 37 countries and covering tax years from 1983 to 2021 was subject to the following filtering exercise (Figure 1) to reduce the cases to a final case law sample of 166 international cases over 34 countries used for the analysis in Chapter 3.

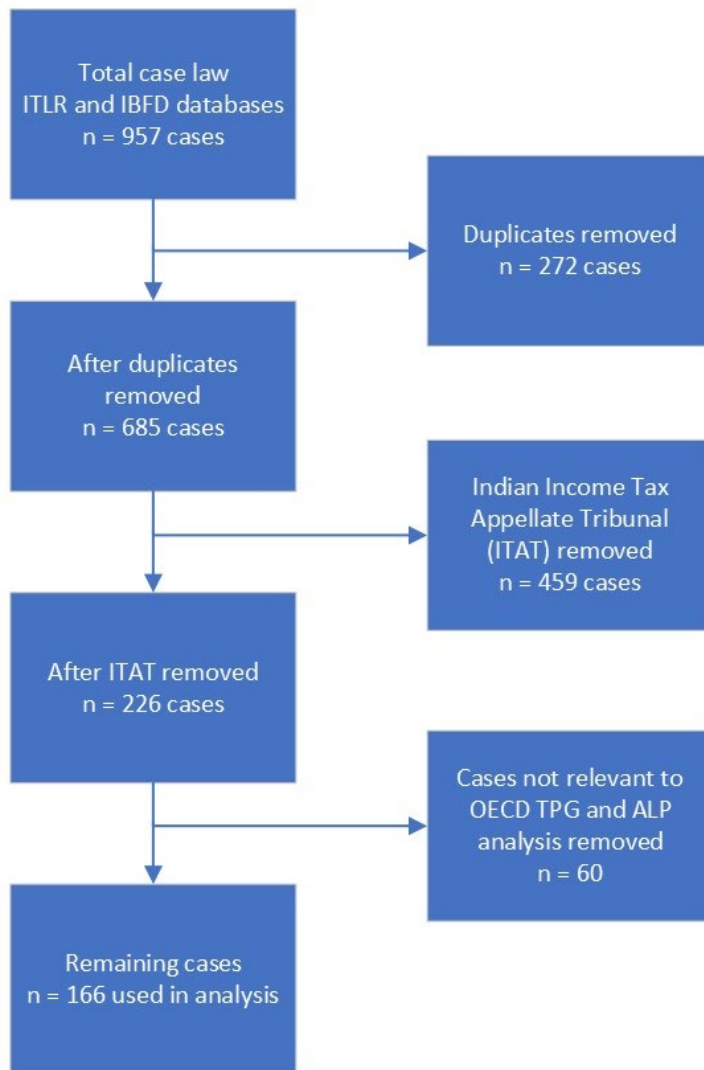


Figure 1: IBFD and ICLR TP case law filtering

The filtering exercise illustrated in Figure 1 is explained as follows:

- 272 duplicate cases were identified and removed from the sample resulting in 685 cases remaining.
- Of these 685 cases, 512 cases were from courts located in India. The 459 of the 512 cases reflected a sample of decisions from the Income Tax Appellate Tribunal (ITAT). The Authority for Advanced Ruling of India, India High Court and the India Supreme Court, were not removed from the sample because of the higher precedential value in decisions issued by the High Court and the Supreme Court.
- 19 of the remaining Indian court cases were identified as not relevant for purposes of determining the weighting that the OECD TPG had in the Indian domestic tax law. These 19 cases represented a duplication of cases heard in the lower courts and the higher courts. Where such duplication occurred, decision of the higher court was retained in the sample. Some cases did not address transfer pricing principles and were removed from the sample.

- A further 41,<sup>14</sup> non-Indian, cases were removed from the analysis that were not relevant to the analysis of this paper. These cases considered issues outside of the use of the ALP in reference to the OECD TPG application. For example, some cases addressed the profit attribution rules and permanent establishment concept instead of the ALP, other cases addressed Value Added Tax domestic tax legislation (not relevant for this analysis), whilst others examined the ALP within the ambit of its own local TP legislation with little or no reference to the OECD TPG.
- The remaining 166 cases were used in the analysis.

#### 1.3.4. Sample selection for Chapter 4: Trends observed within a sample of African countries case law on the influence of the OECD TPG in domestic tax law.

The sample from the IBFD and ITLR databases using the search criteria for the sample in Chapter 3 provided a population of only six cases within Africa.<sup>15</sup> These cases were fewer than those produced by the IBFD and ITLR concerning transfer pricing case law from OECD member countries. An additional database from TPCases.com<sup>16</sup> was utilised to obtain a wider sample size within Africa and gain a better understanding of the influence the OECD had on shaping domestic tax legislation within a sample of case law within Africa. Six cases found through the IBFD and ITLR database search were also found in the TPCases.com database. These six cases were analysed in both Chapters 3 and 4, but with a different focus. The African cases used in Chapter 3 form part of the sample selected from the IBFD and ITLR databases to understand the OECD TPG weighting across OECD and non-OECD countries. The sample of countries within Africa used in Chapter 4 is solely from the TPCases.com database, dealing with cases within Africa dealing with the ALP and is required to understand the impact the OECD TPG may have had on the domestic TP tax legislative development within that sample of African countries. The African countries selected for this dissertation are a function of those for which case law concerning the use of the ALP where the OECD TPGs are mentioned. The case law found was the natural limitation to the sample.

From TPCases.com, all transfer pricing cases within African states were selected. This produced a wider list of 38 TP cases across African countries in Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe than the other databases had provided. One case was removed because

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<sup>14</sup> Judgments excluded came from courts in Australia (3 cases excluded from 11), Canada (4 cases of 14), Denmark (1 case of 17), France (3 cases of 5), Germany (3 cases of 4), Hong Kong (1 case of 1), Indonesia (1 case of 1), Latvia (1 case of 1), Netherlands (3 cases of 6), Norway (3 cases of 21), Spain (2 cases of 3), Sweden (1 case of 9), Switzerland (1 case of 2), United Kingdom (7 cases of 9) and the United States of America (7 cases of 21).

<sup>15</sup> Referring to the results in section 1.3.1. *Sample selection for Chapter 3: Trends observed from a sample of international transfer pricing cases*, of the 166 cases analysed in Chapter 3, only 6 cases spanning across Kenya, Malawi, Nigeria, South Africa and Zambia were included in the sample size for African countries using the search criteria for the IBFD and ITLR databases.

<sup>16</sup> Ibid.

the decision pre-dated the use of the OECD TPG.<sup>17</sup> 25 cases were further removed because, on deeper analysis, it was not related to the use of the OECD TPG and/or ALP. Also excluded was the Ghanaian case of *Ghana vs Beiersdorf Gh. Ltd.*<sup>18</sup> The case did not provide any insight to the application of the ALP nor the influence that the OECD TPG. Despite the case in Ghana excluded, Ghana still maintains their own TP legislation, and has been included in the analysis to better understand how (if any) the domestic TP legislation, when applying the ALP, has been influenced by the OECD TPG. A total sample of 12 cases within Africa were thus analysed in Chapter 4.

Figure 2 below illustrates the filtering exercise conducted to get to total of 12 TP cases within Africa from the TPCases.com database.

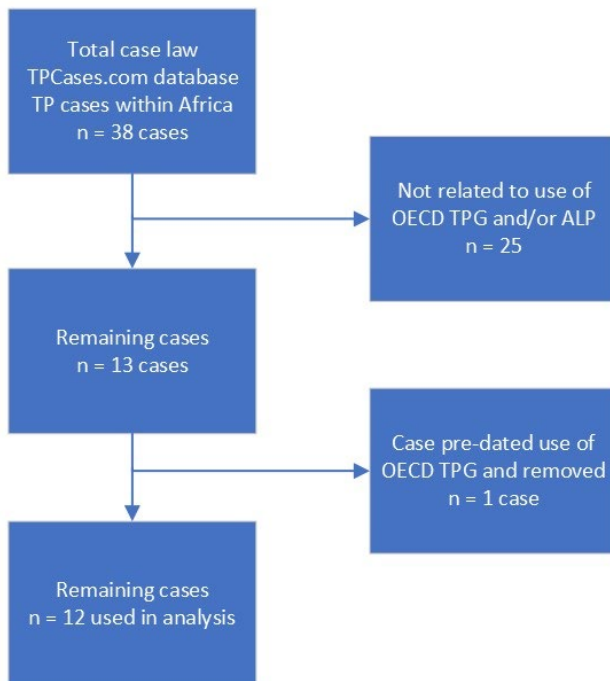


Figure 2: TPCases.com TP case law filtering

#### 1.4. Limitation of scope

Only the databases from the IBFD, ITLR and TPCases.com were used to select a sample of TP cases within the African region. The databases selected provided a listing of international TP cases. This cannot be guaranteed as an exhaustive listing of all international TP cases dealing with the OECD TPG as a soft law instrument and its influence in a court’s judgment and influence to shape domestic tax

<sup>17</sup> South Africa: ZATC, 30 March 1946, *Commissioner for Inland Revenue v Lever Brothers and Unilever Ltd* (14 SATC 1), LexisNexis. This case does not refer to OECD TPG and rejected as part of this sample. The case is not considered in the analysis.

<sup>18</sup> Ghana: HC, 1 August 2018, *Beiersdorf Ghana Limited vs The Commissioner General Ghana Revenue Authority* Accra, Laws Ghana.com, <https://lawsghana.com/judgement/Ghana/High-Court/237>

legislation. However, the sample obtained is an adequate representation to better understand the trends and developments within domestic transfer pricing tax legislation within Africa and to help to infer whether the OECD TPG, as a soft law instrument, has had an influence within this sample of African countries.

### 1.5. Dissertation outline

A selected sample of TP case law on judgments covering the ALP amongst African countries is analysed in this paper in respect of Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe to understand the impact of the OECD TPG as a soft law instrument and its influence over time in domestic tax legislation within these countries. This question is analysed in Chapters 2 to 4 with concluding statements in Chapter 5. The outline of each chapter is as follows:

*Chapter 2: A comparative analysis of a sample of international literature dealing with the OECD TPG Arm's length Principle in Article 9 as a soft law instrument* discusses Article 9, Associated Enterprises, from the OECD, UN and ATAF MTCs when dealing with the ALP. Chapter 2 further details the history and development of the Commentary to Article 9 in the OECD MTC for periods 1963 to 2017 (see sections 2.2. and 2.3.). Literature considering opinions from a sample of various scholars providing an understanding of the OECD TPG's influence in international court judgments is further analysed (see section 2.4).

*Chapter 3: Trends observed from the sample of international TP cases* analyses the results of a sample of cases from the IBFD and ITLR databases to determine the status that the OECD TPG holds in international courts. This is achieved through analysis of the sample of international tax cases selected (as discussed in 1.3.3. above). The analysis further considers the influence that the OECD TPG has had on developing countries within Africa (as a soft law instrument) in so far as the sample of African cases found in the IBFD and ITLR databases.

*Chapter 4: Trends observed within a sample of African countries on the status of the OECD TPG* discusses the impact of the OECD TPG in the domestic TP tax legislative environment in Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe. Where the OECD TPG are mentioned in African tax court judgments, the reference is usually favourable and demonstrates the influence that the OECD TPG could have when introduced to the court during the proceedings. The wider sample of cases within the African state is due to additional cases from the TPCases.com database. For many cases analysed in this chapter, the OECD TPG is either not introduced in domestic tax legislation or referenced by the judge, resulting in no inference as to its influence can be drawn in such circumstances. The analysis in this chapter looks at the reference in legislation or tax administration practices that forces reference to the OECD TPG, especially where such reference was included after the TP case judgment, or the judge excluded the OECD TPG as irrelevant.

Chapter 5: *Conclusion* concludes the research topic to determine if the OECD TPG influenced the development of domestic TP legislation, to some extent (if at all) across the sample of African countries. The conclusion takes into consideration the court judgments within this sample of African states. The results obtained from Chapters 2, 3 and 4 highlight important considerations from the various opinions in the court judgments to understand the impact these judgments had in the development of the domestic TP legislative framework.

## Chapter 2: A comparative analysis of a sample of international literature dealing with the OECD TPG Arm's length Principle in Article 9 as a soft law instrument.

### 2.1. Introduction

This chapter covers four sections to help understand the influence that the OECD TPG, as a soft law instrument, have on the international tax landscape in practice. The meaning of Article 9 of the OECD MTC *Associated Enterprises* is analysed from the perspective of OECD member countries and non-OECD member countries by inspecting the relevant OECD, UN and ATAF MTC to understand the differences. Understanding the differences of Article 9 under each MTC may give insight into understanding the case law in OECD and non-OECD member countries, depending on which model the relevant country follows. Section 2.3. briefly explains the history of the OECD MTC Commentary of Article 9 from 1963 to 2017, which is relevant because each court judgment may be with reference to a treaty based on an earlier version of the OECD (or other) MTC. Section 2.4. provides context on how the OECD TPG acts as an “authoritative statement” in practice in the international tax environment. Section 2.5. summarises some of the main findings in the sample of international literature in 2.4. as a way of identifying characteristics that will help to understand the weighting of the OECD TPG as a soft law instrument analysed in Chapter 3 amongst OECD and non-OECD member countries.

### 2.2. A comparison of Article 9 of the OECD, UN Model Tax Convention and ATAF Model Tax Convention

Article 9 of the OECD MTC and Article 9 of the UN MTC relate to transactions between AE and both make reference to the application of the ALP. Where the transactions between AEs are not in line with the ALP, article 9(2) of the relevant OECD/UN MTC allows the tax authority to adjust the transaction between the AEs such that it is measured on an arm's length basis.<sup>19</sup> The purpose of Article 9 is to facilitate transactions with the AE such that they are at arm's length. Guidance is sought from the OECD TPG to ensure that AEs are transacting at arm's length.<sup>20</sup> Article 9 dealing with the ALP deals with economic double taxation where more than one person is taxed on the same income.<sup>21</sup> The type of income covered is related to profits generated from the transaction between AEs in each of the contracting states. The objective of this article is to ensure that the transactions between such AEs are at arm's length. Therefore, any transactions that are not at arm's length between the contracting states will trigger an adjustment to the profits generated from this transaction between the two states.

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<sup>19</sup> E Baistrocchi, *Article 9: Associated Enterprises - Global Tax Treaty Commentaries*, Global Topics (IBFD, 2020).

<sup>20</sup> OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD 2022), International Organizations' Documentation IBFD.

<sup>21</sup> E Baistrocchi, *Article 9: Associated Enterprises - Global Tax Treaty Commentaries*, Global Topics (IBFD, 2020).

Determining an arm's length price is not covered in this treaty article; however, guidance has been provided by the OECD TPG to ascertain a methodology to determine the arm's length price between two parties.<sup>22</sup> Rather than a division of taxing rights, this article serves to reallocate profits based on adjustments to the arm's length price, resulting in the profits generated in transactions between AE being taxed in the state where the value is created.

Article 9 in the 2017 OECD MTC is consistent with the UN 2017 MTC (no changes have been noted in the wording of Article 9 of the UN 2021 MTC) and the most common deviation is in relation to a limitation by the other contracting state allowing a corresponding adjustment as envisaged in paragraph 2 of this article. Appendix 1 illustrates the difference in wording between the OECD 2017, UN 2017 and ATAF 2019 MTC. Under the UN MTC, paragraph 3 is included to deter the other contracting state from initiating a corresponding adjustment raised in paragraph 2 if it is proven through a final decision by the courts on a dispute that, "...*fraud, gross negligence or wilful default*"<sup>23</sup> has been identified.<sup>24</sup> If no corresponding adjustment is made, double taxation can exist which is in contravention of the intention of the Convention.<sup>25</sup> The ATAF (2019) MTC agrees with the wording in the OECD and UN MTC for paragraphs 1 and 2. The ATAF MTC in paragraph 4 agrees with the UN MTC in paragraph 3 limiting the corresponding adjustments if it is found that the taxpayer was acting, "...*fraud, gross negligence or wilful default*",<sup>26</sup> because of the adjustment. The ATAF MTC includes an additional paragraph that is not found in either the OECD MTC or the UN MTC. Paragraph 3 of the ATAF MTC is a timing provision regarding when the relevant article is applicable between the states as part of the bilateral treaty negotiations. According to the reservations noted in the ATAF (2019) MTC, Nigeria has reserved their right to include this paragraph when negotiating bilateral treaties.<sup>27</sup> An example of a tax treaty where such a paragraph is applied can be found in the 2016 Australia-Germany bilateral tax treaty where a 10-year limit is imposed on any open audits where no defined time period is applied.<sup>28</sup>

South Africa has not listed positions in relation to Article 9 in the OECD 2017 MTC; however, the domestic tax legislation has recently enacted the definition of associated enterprises in line with the

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<sup>22</sup> OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD 2022), International Organizations' Documentation IBFD.

<sup>23</sup> Article 9, para.3 of the United Nations (UN), United Nations Model Double Taxation Convention between Developed and Developing Countries (UN 2017).

<sup>24</sup> Article 9, UN Model (2017).

<sup>25</sup> Article 9, UN Model (2017). Refer to the "Commentary on Article 9" para.2 where it states, "*However, paragraph 2 is an essential aspect of Article 9 and failure to provide a correlative adjustment will result in double taxation, which is contrary to the purpose of the Convention.*"

<sup>26</sup> Article 9, UN Model (2017). Refer to para.3

<sup>27</sup> Article 9 of the ATAF (2019) model. 'ATAF Model Agreement for the Elimination of Double Taxation with Respect to Taxes on Income and the Prevention of Tax Avoidance and Evasion' (ATAF 2019).

<sup>28</sup> 'Agreement between Australia and the Federal Republic of Germany for the Elimination of Double Taxation with respect to taxes on Income and on Capital and the prevention of Fiscal Evasion and Avoidance. [hereinafter: Australia-Germany bilateral tax treaty], promulgated in the Australia "International Tax Agreements Amendment Bill 2016" (n.d.); <https://treasury.gov.au/tax-treaties/income-tax-treaties>. Refer to Article 7: Business Profits, para 8 of the treaty.

OECD 2017 MTC.<sup>29</sup> The amendment to the definition of domestic tax legislation in South Africa to include the definition of AE was effective from 1 January 2023.<sup>30</sup>

### 2.3. The progression of Article 9 Commentary in the OECD MTC with respect to the OECD Transfer Pricing Guidelines

The first reference to the TPG is found in the 1979 transfer pricing report by the OECD. The 1979 transfer pricing report;<sup>31</sup> is one of the initial guidelines to apply the ALP. The transfer pricing report could be viewed as a soft law instrument to interpret the meaning of Article 9 of the OECD for treaties concluded in this period. The OECD MTC commentaries as a basis to aid in the interpretation of court judgments is recognised in the 2017 OECD MTC.<sup>32</sup>

Appendix 2 shows extracts from the Commentary of Article 9 OECD MTC from 1963 to 2017. The OECD TPG was introduced to aid tax authorities and taxpayers to apply the ALP in terms of Article 9 in the relevant OECD MTC. The purpose of the guidelines was to ensure that no artificial TP was taking place for non-commercial reasons. This is supported in the OECD MTC commentary on article 9 of the OECD MTC as it reads from 1963 to 2017. The progression from the OECD 1963 and OECD 1992 MTC commentary on article 9 mentions the term “open market commercial terms” where the OECD 1992 commentary first mentions “arm’s length basis”. For commentary on article 9 of the OECD MTC for the periods 1998 to 2017 the term “commercial terms” is removed, and the term “arm’s length” is predominantly used. Another finding when comparing the commentary to article 9 of the OECD MTCs for periods 1998 to 2017 is that the OECD TPG is considered as the “authoritative statement” when applying the ALP. Section 2.4. below references the article, “*The status of the OECD Transfer Pricing Guidelines in the Post-BEPS Dynamic*”, where it is supported that the OECD TPG can be used as an “authoritative statement” in the interpretation of Article 9.

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<sup>29</sup> OECD 2017. Also refer to amendment in ZA: South African Tax Administration Act (2011), National Legislation, SARS Legal, refer to Section 31(2)- Affected Transactions’ (n.d.), <https://www.sars.gov.za/wp-content/uploads/Legal/AABC/LAPD-LPrim-Act-2012-01-Tax-Administration-Act-2011.pdf>.

<sup>30</sup> M. Badenhorst, ‘New Guidance in South Africa on the Definition of “Associated Enterprises” in Connection with the Transfer Pricing Rules’, *International Transfer Pricing Journal* 2023, no. 2 (2023): 100–103.

<sup>31</sup> M. Kobetsky, ‘2.1. History of the Transfer Pricing Reports’, in *The Status of the OECD Transfer Pricing Guidelines in the Post-BEPS Dynamic*, ed. Pasquale Pistone et al. (2020).

<sup>32</sup> OECD (2017), Model Tax Convention on Income and on Capital. Refer to para. 29.3. where it states, “*Bilateral tax treaties are receiving more and more judicial attention as well. The courts are increasingly using the Commentaries in reaching their decisions. Information collected by the Committee on Fiscal Affairs shows that the Commentaries have been cited in the published decisions of the courts of the great majority of member countries. In many decisions, the Commentaries have been extensively quoted and analysed, and have frequently played a key role in the judge’s deliberations. The Committee expects this trend to continue as the worldwide network of tax treaties continues to grow and as the Commentaries gain even more widespread acceptance as an important interpretative reference.*”

From the history of the OECD MTC commentaries on Article 9 of the relevant MTC for periods 1963 to 2017, it is surmised that the purpose of Article 9 is to apply the ALP (or commercial substance) to a transaction. It is also evident from the relevant OECD MTC for the period 1998 to 2017 that the OECD TPG may act as an “authoritative statement” and important instrument when applying the ALP.

#### 2.4. A sample of opinions from international literature on the interpretation of the influence of the OECD TPG as a soft law instrument

The interpretation of the relevant treaties stems from the general rule of interpretation in accordance with Article 31 of the Vienna Convention on the Law of Treaties (VCLT).<sup>33</sup> The Vienna Convention represents customary international law.<sup>34</sup> The question remains whether the OECD TPG has any bearing in treaty interpretation in courts or any bearing as a supplemental soft law instrument for purposes of treaty interpretation, hence guiding its influence in legal jurisprudence.

In an article titled, “*OECD Transfer Pricing Guidelines as a Quasi Source of Law in a Post-BEPS World – Legislative and Judicial Developments from a Polish Perspective*”, Brezinski et al<sup>35</sup> discuss the OECD TPG’s status as a soft law instrument in the context of Poland’s legal taxing structure. The OECD TPG status in courts is also discussed from the perspective of whether it meets the requirements of Article 31 of the VCLT. Poland is a member of the OECD. It is argued by the authors that the OECD TPG should not have any impact in the context of the treaty interpretation.<sup>36</sup> When a treaty is concluded between two countries, the principles in Article 31(2) of the VCLT is not fulfilled in respect of the OECD TPG because there is insufficient evidence to conclude that the OECD TPG act as an instrument between both countries (even if they are both OECD member countries) at the time of concluding the treaty and accepting the treaty into law by both parties. The authors further argue that the OECD TPG are not supported as an interpretive aid in terms of Article 31(3) of the VCLT because consensus by both parties on the whole application may not be achieved in a general sense. Article 32 of the VCLT

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<sup>33</sup> Article 31: United Nations, 1969 Vienna Convention on the Law of Treaties, 1155 § (1969), <https://doi.org/10.1007/978-3-642-19291-3>.

<sup>34</sup> Kobetsky, ‘4.2.2., “Contrary argument that the OECD Guidelines are not part of the Commentary”. Further articulated by Linda Brosens and Jasper Bossuyt, ‘Legitimacy in International Tax Law-Making: Can the OECD Remain the Guardian of Open Tax Norms?’, *World Tax Journal* 12, no. No. 2 (2020), section 2, ““The Role of the OECD in Developing International Tax Norms: Hard Law, Soft Law or No Law?””, where the authors note, “There is an abundant amount of literature on this topic, but most authors focus on the legal status of the OECD Commentaries on the basis of articles 31 and 32 of the Vienna Convention on the Law of Treaties (VCLT), which are widely considered to provide for the general rules on treaty interpretation.” and 2.3, “Do the OECD Commentaries and TP Guidelines constitute (authentic) interpretative means for tax treaty interpretation purposes?”, noting, “The applicable rules on treaty interpretation are enshrined in articles 31 and 32 of the VCLT. They are considered to be customary international law and hence also apply to tax treaties. As stated above, the legal status of the OECD Commentaries and TP Guidelines has been debated for a while in the literature, and there still is no consensus.”.

<sup>35</sup> B Brzeziński, K Lasiński-Sulecki, and W Morawski, ‘OECD Transfer Pricing Guidelines as a Quasi Source of Law in a Post BEPS World – Legislative and Judicial Developments from a Polish Perspective’, *International Transfer Pricing Journal* 27, no. 3 (2020).

<sup>36</sup> *Ibid.* See section 4.

will reject the use of the OECD TPG or the latest version of the OECD TPG as supplementary means of interpretation because the OECD TPG may have only been published after the conclusion of the treaty.

A further problem identified by Brezinski et al is whether the OECD TPG should be interpreted statically at the time of ratification of the treaty with the closest version of the TPG available or rather dynamically as new developments in the OECD TPG are revealed.<sup>37</sup> In the article, “*The influence of the OECD Commentaries on Treaty Interpretation*”,<sup>38</sup> Vogel argues that when an article in a bilateral treaty is concluded, it can be asserted that the meaning of the article and its Commentary can be understood at the time of enactment. This results in a static approach to the application of the relevant Commentary at the time. Vogel further opines that despite the Commentaries not acting as a binding legal instrument they are still expert opinion, which hold a great weight in the court proceedings.<sup>39</sup> This dissertation does not delve into whether common law countries or civil law countries place more or less reliance on expert opinions contained within the Commentary.

The author Kobetsky in the article, “*The status of the OECD Transfer Pricing Guidelines in the Post-BEPS Dynamic*” discusses how the “*authoritative statement*” connecting the OECD TPG to Article 9, as referenced in the OECD MTC Commentary<sup>40</sup> may be used as part of the treaty interpretation of Article 9 in terms of the general rules of interpretation in Articles 31 and 32 of the VCLT.<sup>41</sup> Kobetsky

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<sup>37</sup> Ibid.

<sup>38</sup> K. Vogel, ‘The Influence of the OECD Commentaries on Treaty Interpretation’, *Bulletin for International Taxation*, vol. 54, no.12 December (2000).

<sup>39</sup> Ibid. Where Vogel was citing the case *Sun Life Assurance v Pearson* where the high-ranking expert is regarded stating, “*Even where their interpretation is not binding on taxpayers and on courts, they are still the opinion of high-ranking experts which, as Mr Justice Vinelott put it in Sun Life Assurance v. Pearson, in all questions of treaty interpretation is “clearly entitled to very great weight”.*”

<sup>40</sup> Also refer to appendix 2 for a summary of the treaty Commentary in Article 9 of the OECD MTC for periods 1963 to 2017. OECD MTCs for periods 1998 to 2017 considers the OECD TPG at the time as the “authoritative statement” when determining the ALP.

<sup>41</sup> Kobetsky, ‘4.2. OECD Commentary on Article 9’.

supports this assertion by citing various literature in support of reliance on the OECD MTC Commentary as an interpretative aid in applying domestic TP legislation.<sup>42 43 44 45</sup>

In a contrasting view, the *SNF* case<sup>46</sup> is an Australian case where the court decided that the OECD TPG do not form part of the OECD MTC Commentary to Article 9.<sup>47</sup> The court considered that the OECD TPG is not an agreement between the parties to the bilateral treaty at the time of conclusion. The guidelines and supplementary information was not viewed as a subsequent agreement to aid in the interpretation of the treaty, as envisaged in section 31(3) of the VCLT.<sup>48</sup> Kobetsky's opinion is that the decision was a "legal error" where the decision by the court was an incorrect focus on the label, "guidelines".<sup>49</sup> Subsequent to the ruling, Australia's domestic tax legislation was amended to align to the principles in the OECD Guidelines.<sup>50</sup>

The OECD ALP in Article 9(1) of the OECD MTC ensures that the ALP in cross border intragroup transactions is adhered to; however, the German view is that the article is a hindrance on the application of German domestic tax law.<sup>51</sup> Whilst Germany was developing its own TP legislative framework, confusion was created on how the domestic tax legislation in Germany will interact with the already existing Article 9 in the OECD MTC as agreed with its existing treaties.<sup>52</sup> German domestic tax law on TP is constantly being developed and takes precedence over Article 9 of the relevant OECD MTC.<sup>53</sup> A situation may arise where future treaty negotiations will need to be carefully considered so as to not

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<sup>42</sup> This point can be argued in, "*Klaus Vogel on Double Taxation Conventions*" where it is commented that the OECD TPG and OECD MTC hold the same weight; in "*Transfer Pricing and the Arm's Length Principle in International Tax Law*", where J. Wittendorff asserts that the OECD TPG are an important part of the Commentary amongst OECD member countries and in the article "*International Governance through Soft Law: The Case of the OECD Transfer Pricing Guidelines*", where the author A. Vega states that the OECD Commentary explains that the OECD TPG is used to understand the principles are internationally agreed upon to determine the Arm's Length Principle in terms of Article 9 in the OECD TPG.

<sup>43</sup> Cited in *Ibid.*, "*The Status of the OECD Transfer Pricing Guidelines in the Post-BEPS Dynamic*", reference to E. Reimer & A. Rust eds., *Klaus Vogel on Double Taxation Conventions* para. 24 (4th ed., Kluwer Law International 2015). This publication claims that the OECD TPG are considered to have "*virtually the same weight as the OECD*".

<sup>44</sup> Cited in *Ibid.*, "*The Status of the OECD Transfer Pricing Guidelines in the Post-BEPS Dynamic*", See J. Wittendorff, *Transfer Pricing and the Arm's Length Principle in International Tax Law* p. 246 (Kluwer Law International 2010).

<sup>45</sup> Alberto Vega, 'International Governance through Soft Law: The Case of the OECD Transfer Pricing Guidelines', Working Paper 2012-05, 2012, <http://www.tax.mpg.de>.

<sup>46</sup> Australia, Federal Court of Australia, 1 June 2011, *SNF (Australia) Pty Ltd v. Commissioner of Taxation of the Commonwealth of Australia* (2011), Australian Government: Australian Taxation Office, <https://www.ato.gov.au/law>.

<sup>47</sup> Kobetsky, '4.2. OECD Commentary on Article 9'.

<sup>48</sup> *Ibid.*, '4.2.2. Contrary argument that the OECD Guidelines are not part of the Commentary'.

<sup>49</sup> *Ibid.*, '4.2.2. Contrary argument that the OECD Guidelines are not part of the Commentary'.

<sup>50</sup> *Ibid.*, '4.4. Status of the OECD Guidelines in Australian and UK domestic transfer pricing rules.'

<sup>51</sup> Martin Weiss, 'Germany: The Impact of Article 9 of the OECD Model on German Taxation', *European Taxation* February/M (2016): p. 57.

<sup>52</sup> *Ibid.*

<sup>53</sup> *Ibid.*

imply a treaty override in conflict with the domestic TP legislation in Germany in comparison to the existing OECD TPG as an “authoritative statement” at the time of treaty enactment.<sup>54</sup>

Despite the OECD TPG stating that OECD member countries are “*encouraged to follow these Guidelines in their domestic transfer pricing practices*”<sup>55</sup> the practice observed by Pichhadze<sup>56</sup> is that the treatment of the OECD TPG differs in and amongst OECD member countries in their domestic tax law practices. In the OECD Annual Report in 2004, it is clearly acknowledged that the OECD TPG are non-binding “*soft law*” instruments whose reinforcement in tax treaty practices and implementation stems from members within the OECD unifying on the consensus to implement these guidelines within their treaty practices.<sup>57</sup> In the Canadian case involving the pharmaceutical company, *GlaxoSmithKline*,<sup>58</sup> the judge notes that Canadian domestic tax legislation takes precedence over the OECD TPG. However, it is acknowledged that the domestic tax legislation in terms of section 69(2) of the Canadian Income Tax Act (ITA) at the time did not have sufficient guidance to determine whether the transaction was at arm’s length.<sup>59</sup> In the same case, it is noted that the court still relied on part of the OECD TPG to conclude on the analysis.<sup>60</sup> Pichhadze further states that, just like there are countries that solely rely on the domestic tax legislation without any legal binding status of the OECD TPG, countries such as the United Kingdom (UK) require the use of the OECD TPG as part of the ALP analysis.<sup>61</sup> Section 164(1) of the Taxation (International and Other Provisions) Act 2010 of the UK ITA requires the TP analysis to be carried out in a manner that that is consistent with the OECD TPG.<sup>62</sup> The current

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<sup>54</sup> Ibid. where the author notes, “*It also emphasized that the German transfer pricing rule in section 1 of the FTTA was to be interpreted within the framework of the applicable tax treaty, not the other way around. Hence, the tax treaty sets the standard for a permissible transfer pricing adjustment in article 9(1), and the domestic law must help execute the rule since it cannot self-execute. Section 1 of the FTTA did not constitute a treaty override, which might have displaced the rules of the tax treaty in favour of a rule under national tax law.*”

<sup>55</sup> OECD 2017. Preface, para. 16.

<sup>56</sup> A Pichhadze, ‘Exposing Unaddressed Issues in the OECD’s BEPS Project: What About the Roles and Implications of Contract Interpretation Law and Private International Law in the Transfer Pricing Arm’s Length Comparability Analysis?’, *World Tax Journal*, no. 7 (2015).

<sup>57</sup> Although not specific to the OECD TPG, it is still relevant to understand the status of OECD Guidelines being nonbinding instruments. OECD, ‘OECD Annual Report’, 2004. It is noted on p.9, “The Organisation provides a setting where governments can compare policy experiences, seek answers to common problems such as population ageing, identify good practice and work to co-ordinate domestic and international policies. It is a forum where peer pressure can act as a powerful incentive to improve policy and implement “soft law” – nonbinding instruments such as the OECD Guidelines for Multinational Enterprises – and can on occasion lead to formal agreements or treaties.” Access: <https://www.oecd.org/newsroom/31621929.pdf>.

<sup>58</sup> Her Majesty The Queen (Appellant/Respondent on cross-appeal) v. *GlaxoSmithKline Inc.* (Respondent/Appellant on cross-appeal) (2012). Refer to para. 20 and para 40-41.

<sup>59</sup> Ibid. Noted in para. 21, “section 69(2) of the ITA “does not, itself, offer guidance as to how to determine the ‘reasonable amount’ that would have been payable had the parties been dealing at arm’s length”.

<sup>60</sup> Pichhadze, ‘Exposing Unaddressed Issues in the OECD’s BEPS Project: What About the Roles and Implications of Contract Interpretation Law and Private International Law in the Transfer Pricing Arm’s Length Comparability Analysis?’

<sup>61</sup> Ibid.

<sup>62</sup> ‘Taxation (International and Other Provisions) Act 2010 - Section 164, “Part to Be Interpreted in Accordance with OECD Principles” (2010).

trend is that even amongst OECD member countries, despite their OECD member status, each country's courts may differ in their reliance on the OECD TPG as a soft law instrument.

Brosens and Bossuyt undertake a wider analysis of OECD and non-OECD member countries to understand the influence of the OECD TPG as a soft law instrument in legally binding practice. The authors highlighted areas where it is not automatically presumed that the OECD MTC nor its commentaries are applied as a legal obligation in a court of law simply because a treaty was concluded based on the wording of the OECD MTC. Brosen and Bossuyt further explain the difficulty to determine the status of the Commentary of the relevant MTC and OECD TPG. Even if the tax administrators disclose an authoritative statement to clarify its meaning, it is not automatic that its meaning will be accepted in domestic tax law.<sup>63</sup> Double tax agreements agreed by different jurisdictions do not always include an explanatory memo by the relevant jurisdiction on the treaty concluded. This gap creates an inference by the courts to interpret the treaty within the ambit of their domestic legislative framework for treaty interpretation. Brosen and Bossuyt argue that failure to comply with the recommendations and the Commentary of the relevant OECD MTC (when the treaty is concluded) is in contravention of the good faith principle by the OECD member country. The authors' argument stems from an opinion by Judge Lauterpacht on the good faith obligation where a Separate Opinion in the UN General Assembly indicates that this obligation is also an international law recommendation,<sup>64</sup> where any disregard for the recommendation amounts to a violation of the good faith obligation especially when the stance is clearly noted by relevant international organisation.<sup>65</sup> The OECD Legal instruments 0424, "*Recommendation of the Council on OECD Legal Instruments Base Erosion and Profit Shifting Measures Related to Transfer Pricing*"<sup>66</sup> provides a recommendation where members and non-members of the OECD adhere to the 2015 BEPS Reports on Actions 8-10 and Action 13. Therefore,

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<sup>63</sup> L Brosens and J Bossuyt, 'Legitimacy in International Tax Law-Making: Can the OECD Remain the Guardian of Open Tax Norms?', p. 313-376. See section, "2.1. Legal basis of the OECD Commentaries and TP Guidelines", where a recommendation by an international organisation such as the OECD is described as, "*A recommendation in international law is generally defined by referring to its legally non-binding character, i.e. the addressees of the recommendations are not legally bound to follow its guidelines unless the contrary is provided for in the constitutive treaty or charter, or the parties agreed otherwise.*"

The author further explains that this is not a complete rejection of any recommendations from an international organisation holding any weight to determine the meaning when applying a treaty and continues to explain that its influence varies where the author states, "*As a result, a recommendation in itself does not have any direct law-making effect, but it may result in legal effects in terms of contributing to the development of international law insofar as the member countries consider the recommended measures to be appropriate and subsequently accepted.*"

<sup>64</sup> Cited in Ibid., "Legitimacy in International Tax Law-Making: Can the OECD Remain the Guardian of Open Tax Norms?" is the Separate Opinion by Judge Lauterpacht, Admissibility of Hearings of Petitioners by the Committee on South West Africa (Request for Advisory Opinion), ICJ Reports 1955, pp. 117-120. Also see section "2.1. Legal basis of the OECD Commentaries and TP Guidelines".

<sup>65</sup> Ibid.

<sup>66</sup> OECD, 'Recommendation of the Council on Base Erosion and Profit Shifting Measures Related to Transfer Pricing, OECD LEGAL/0424', n.d.

the merits of each case cannot simply deny the acceptance of the OECD MTC recommendations and its Commentary given this custom in international law.

Hattingh provides a perspective of the value of BEPS materials in treaty interpretation that depend on the interpretive community addressing its relevance.<sup>67</sup> Two spectrums of communities are illustrated by Hattingh where one is from the view of a tax advisor that may view all BEPS material as relevant, and the other is that of judicial officers that hold a higher status to the legal norms of treaty interpretation to bring about its relevance.

Brosens and Bossuyt comment on the interpretation of soft law eligibility as a basis of law in respect to the interpretation of the OECD Commentary and TPG stating:<sup>68</sup>

*“Irrespective of the different views in the literature, scholars agree that “law” – whether it be considered “hard” or “soft” – encompasses social norms or rules steering the behaviour of states in international relations. Indeed, the pertinent normative standards create mutually shared behavioural expectations vis-à-vis other members within the international legal order; the hard/soft or legal/non-legal discussion solely pertains to the extent of enforceability of those expectations. It should thus be assessed to what extent the Commentaries and the TP Guidelines effectively govern international relations by steering the conduct of states.”*

The OECD TPG is an interpretative aid to the model addressed for the benefit of tax administrators and taxpayers. Brosens and Bossuyt state that it is not conclusive that the Commentary and the relevant guidelines was used as a basis to steer the decision to sign the agreed upon bilateral treaty between the states involved and is void of a legal basis.<sup>69</sup>

The courts have been found to recognise the OECD MTC Commentaries where the treaty or protocol directly refers to the commentaries allowing its classification as hard law.<sup>70</sup> In circumstances where the protocol requires the application of the Commentary, it should require the judge to consider OECD TPG insofar that the commentaries reference these guidelines.

There is a general consensus that bilateral treaties should be interpreted more widely by the courts because of the lack of precision when the treaties are created. This creates a wider scope of interpretation; however, a key aspect is that a bilateral treaty can only be effective if it is interpreted in

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<sup>67</sup> Johann Hattingh, ‘The Relevance of Beps Materials for Tax Treaty Interpretation’, *Bulletin for International Taxation* 74, no. 4–5 (2020): 179–96.

<sup>68</sup> Brosens and Bossuyt, ‘Legitimacy in International Tax Law-Making: Can the OECD Remain the Guardian of Open Tax Norms?’ See section 2.2, “Do the OECD Commentaries and TP Guidelines constitute soft law?”

<sup>69</sup> Ibid. See section 2.2, “Do the OECD Commentaries and TP Guidelines constitute soft law?”, “In sum, contrary to the BEPS Action Reports, the OECD Commentaries and the TP Guidelines do not qualify as soft law, as they do not prescribe normative standards with a view to steering the behaviour of states in the international order and, hence, they do not create behavioural expectations essential for a legal system.”

<sup>70</sup> C West, ‘References to the OECD Commentaries in Tax Treaties: A Steady March from “Soft” Law to “Hard” Law?’, *World Tax Journal*, Vol. 9(1) February (2017).

a uniform manner between the contracting states.<sup>71</sup> Where the courts recognise the OECD MTC Commentary its weighting should be considered by the courts when delivering judgments.<sup>72</sup>

## 2.5. Summary of findings observed on the status of the OECD Commentary and their status in court proceedings and application in research amongst African countries.

Section 2.4. above outlines instances where the courts have examined at the OECD MTC Commentaries and OECD TPG as a form of guidance in their court judgments. Despite the OECD MTC Commentaries and OECD TPG acting as soft law instruments, they have influenced the court judgments and provided a basis to confirm the ALP, especially in periods of time when the local domestic tax legislation was not fully developed to tackle the determination of the ALP. It was also found that certain countries have included the OECD MTC Commentaries as part of the treaty interpretation either through an agreement noted within the bilateral treaty or an agreement to add the Commentary as part of a protocol for the interpretation of the treaty. Attempting to reduce its ambiguity shows the importance of the Commentary in the bilateral treaty interpretation.<sup>73</sup> In cases where there is a lack of domestic TP tax legislation, the courts may be required to seek guidance from the OECD MTC Commentary in its application. A dichotomy is created between decisions where certain courts only follow a strict hard law interpretation whilst others consider these soft law instruments in the treaty interpretation. The areas where a soft law instrument has been enacted in the protocol (or within the treaty itself) could be compared to where countries include aspects of soft law in their domestic TP legislation similar to that of the wording of the OECD TPG to avoid the ambiguity of its meaning in application and interpretation within cross-border transactions.

Chapter 3 analyses a sample of cases from the IBFD and ITLR to test the status of the OECD TPGs as a soft law instrument in a sample of international tax court judgments.

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<sup>71</sup> K Vogel and Rainer G Prokisch, 'General Report: Interpretation of Double Taxation', in *International Fiscal Association*, 78a ed., 1993.

<sup>72</sup> B. J. Arnold, 'The Interpretation of Tax Treaties: Myth and Reality', *Bulletin for International Taxation*, vol. 64, no.1 January (2010). See section, 4.7. "Most tax treaties follow the pattern of the OECD Model.": *Therefore, under all interpretive approaches, it is always a question of the weight to be given to the OECD Model and Commentaries.*

<sup>73</sup> C. West, References to the OECD Commentaries in Tax Treaties: A Steady March from "Soft" Law to "Hard" Law?, Vol. 9 World Tax J. No. 1 (2017), Journal Articles & Opinion Pieces IBFD. Refer to section 3, "Increasing Reference to the OECD Commentaries in Treaties and Protocols and the Issues Arising".

## Chapter 3: Trends observed from the sample of international Transfer Pricing cases.

This chapter documents the results from the sample of cases from the IBFD and ITLR databases. The purpose of the systematic review of international court judgments from a sample of OECD and non-OECD member countries TP cases from the IBFD and ITLR databases is to determine the weighting (if any) that the courts rely on the OECD TPG as a soft law instrument in their decision.

### 3.1. Data collection

The following attributes were inspected to aid in the data gathering component of this research paper:

- Whether the OECD TPG were considered in the court's decision,
- Where it was found that the OECD TPG were considered, the actual weighting of the OECD TPG in the court's decision was determined. The measurement of the weighting is subdivided into four categories, namely "None", "Low", "Medium" and "High". The meaning of each is further discussed below; and
- Whether the OECD TPG were rejected by the court.

Other data gathered for completeness was as follows:

- The tax years in question;
- The date of the decision; and
- Whether the courts favoured the taxpayer or tax authorities.

### 3.2. The weighting of the OECD TPG

The author has attributed the following characteristics when determining the OECD TPG weighting in the court's decision:

- None: No OECD TPG consideration noted in the judgment. Local domestic TP tax legislation was the sole basis of the court's decision.
- Low: The OECD TPG is considered for completeness by the court, but it is not a focal part of its decision.
- Medium: The OECD TPG are considered by the court and links the OECD TPG to the local domestic TP tax legislation.
- High: The latest OECD TPG are relied on for completeness and a key consideration in the court's decision when using the OECD TPG as part of the country's local tax legislation.

### 3.3. Results

Appendix 3 illustrates a detailed report by country of all cases used in this study across the IBFD, ITLR and TPCases.com databases. Appendix 3, table 1.1. below summarises the sample of cases in relation to OECD and non-OECD member countries in each category.

	OECD Status	a. Domestic TP legislation				b. OECD TPG considered				c. OECD TPG weighting					d. OECD TPG rejected			
		Yes	No	N/A	Total	Yes	No	N/A	Total	1. Low	2. Medium	3. High	4. None	Total	Yes	No	N/A	Total
<b>Total</b> No. of cases	OECD Member	111	0	1	<b>112</b>	93	18	1	<b>112</b>	22	60	11	19	<b>112</b>	2	97	13	<b>112</b>
	Non-OECD Member	52	0	1	<b>53</b>	39	14	0	<b>53</b>	14	22	4	13	<b>53</b>	4	44	5	<b>53</b>
	Varied	1	0	0	<b>1</b>	1	0	0	<b>1</b>	1	0	0	0	<b>1</b>	0	1	0	<b>1</b>
	Total	164	0	2	<b>166</b>	133	32	1	<b>166</b>	37	82	15	32	<b>166</b>	6	142	18	<b>166</b>
<b>Total</b> %	OECD Member	99.11%	0.00%	0.89%	<b>100%</b>	83.04%	16.07%	0.89%	<b>100%</b>	19.64%	53.57%	9.82%	16.96%	<b>100%</b>	1.79%	86.61%	11.61%	<b>100%</b>
	Non-OECD Member	98.11%	0.00%	1.89%	<b>100%</b>	73.58%	26.42%	0.00%	<b>100%</b>	26.42%	41.51%	7.55%	24.53%	<b>100%</b>	7.55%	83.02%	9.43%	<b>100%</b>
	Varied	100.00%	0.00%	0.00%	<b>100%</b>	100.00%	0.00%	0.00%	<b>100%</b>	100.00%	0.00%	0.00%	0.00%	<b>100%</b>	0.00%	100.00%	0.00%	<b>100%</b>
	Total	98.80%	0.00%	1.20%	<b>100%</b>	80.12%	19.28%	0.60%	<b>100%</b>	22.29%	49.40%	9.04%	19.28%	<b>100%</b>	3.61%	85.54%	10.84%	<b>100%</b>

The results in table 1.1. indicates that 80.12% of the sample of cases confirm that the courts considered the use of the OECD TPG in their decision. There is a degree of influence of the OECD TPG found in the court rulings, which varies across jurisdictions. In 22% of overall cases, the OECD TPG carry a “Low” measurement of influence, i.e., 22% of the court’s decisions only consider the OECD TPG for completeness.

49% of overall cases are weighted in the “Medium” bucket, indicating that where the OECD TPG were relied upon, it is also closely linked to domestic TP tax legislation to justify its use. Therefore, the OECD TPG interacts with domestic tax law. The OECD TPG were not solely relied upon in the court’s decision, but it is a contributing factor in the court’s analysis and conclusion.

Only 9% of the overall cases indicated a “High” weighting on the use of the OECD TPG in the courts’ decision. 11 cases weighted in the “High” bucket are found in OECD member countries namely, Denmark, Finland, Hungary, Norway and Spain. Although it was observed that the court ruling was made with reference to the domestic tax legislation by the relevant court, the cases weighted in the “High” bucket reveal a heavier reliance of the OECD TPG by the court’s through their direct referencing

to specific OECD TPG.<sup>74 75 76 77 78 79</sup> For the non-OECD member countries, where a "High" status of the OECD TPG appears (that is where there is a higher reliance on the OECD TPGs), it occurred in jurisdictions such as Kenya, South Africa, Venezuela and Zambia, during tax periods when the domestic tax legislation was ambiguous about TP rules in their domestic tax legislation or there lacked clarity on how to apply the ALP. Court judgments in Kenya<sup>80, 81</sup> and Venezuela relied on the OECD TPG despite these countries not being members of the OECD. In the Venezuelan case, the OECD TPG was used as guidance for the interquartile range because the domestic tax legislation at the time was ambiguous.<sup>82</sup> In South Africa, the court found it necessary to rely on the OECD TPG to apply the ALP in an attempt to overcome the global BEPS challenges (refer to section 4.7.2. for further findings).<sup>83</sup> In Zambia, domestic TP legislation was in place for the periods under scrutiny by the tax authorities and the court relied on the guidance by the OECD TPG to aid in its application (refer to section 4.8.1. for further findings).<sup>84</sup>

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<sup>74</sup> In Denmark Case: Denmark, Landsskatteretten (National Tax Tribunal), 3 October 2016, Case 17-0989902, IBFD Case Law, direct reference to Chapter VI of the OECD TP Guidelines 2017.

<sup>75</sup> In Denmark case: Denmark, Østre Landsret (High Court of Eastern Denmark), 13 January 2020, Case B-1253-17, IBFD Case Law; the court noted, "*The Court noted that the discretion of the tax authorities must be exercised in accordance with the OECD TP Guidelines*".

<sup>76</sup> In Denmark Case: Denmark, Landsskatteretten (National Tax Tribunal), 8 October 2018, Case SKM2018.510.LSR, IBFD Case Law; the court noted that Chapter 9, part II, Section E of the OECD TPG must be relied upon by the Tribunal.

<sup>77</sup> In Finland: Finland, Supreme Administrative Court (Korkein hallinto-oikeus, KHO), 18 December 2018, Case KHO: 2018:173, IBFD Case Law; the court emphasised that the OECD TPG must be used.

<sup>78</sup> In Hungary: Hungary, Fvárosi Közigazgatási és Munkaügyi Bíróság (Budapest-Capital Administration and Labour Court), 17 May 2018, Case 14.K.32.030/2016/30, IBFD Case Law; it has been clearly identified by the courts that the OECD TPG, "*In any case, what the decision of the Court demonstrates is that the OECD TPG have a de facto binding force in Hungary, as they take precedence over domestic legislation when the latter deviates from the TPG...* ".

<sup>79</sup> In Spain: Spain, Central Economic-Administrative Court (TEAC), 3 October 2013, Case R.G. 2296/2012, IBFD Case Law; the court used para. 6.17 of the OECD TPG in its decision.

<sup>80</sup> Kenya: High Court of Kenya, 5 October 2005, Unilever Kenya Limited v Commissioner of Income Tax, IBFD Case Law. The results identified in the Unilever Kenya case (2003) stemmed from an era where there was limited guidance in domestic tax legislation governing the ALP in transfer pricing transactions. Due to the limited guidance available in the domestic tax law the OECD TPG was used by the courts to determine the ALP. In the Kenyan case, Judge Alnashir Visram made a powerful statement about how the current economic landscape is operating as a "global village". Judge Visram states, "*We live in what is now referred to as a "global village". We cannot overlook or side line what has come out of the wisdom of taxpayers and tax collectors in other countries. And especially because of the absence of any such guidelines in Kenya, we must look elsewhere...it would be foolhardy for any court to disregard internationally accepted principles of business as long as these do not conflict with our own laws. To do otherwise would be highly short-sighted*".

<sup>81</sup> Kenya: High Court of Kenya, 5 October 2005, Unilever Kenya Limited v Commissioner of Income Tax, IBFD.

<sup>82</sup> In Venezuela: Juzgado Superior Noveno de lo Contencioso Tributario de la Circunscripción Judicial del Área Metro-politana de Caracas (Tax Court of the Greater Caracas Area), 5 May 2015, Case 018-2015, Diageo Venezuela, C.A. v Servicio Integrado de Administración Aduanera y Tributaria (SENIAT), IBFD.

<sup>83</sup> South Africa: Tax Court, 7 January 2021, ABC (Pty) Ltd v. Commissioner for the South African Revenue Service, Case Law, IBFD. The court noted, "*As a final remark, the Court observed that it was necessary for countries to align with the OECD TP Guidelines to overcome the challenges brought about by BEPS.*"

<sup>84</sup> Zambia: Tax Appeals Tribunal, 28 March 2019, Nestlé Zambia Trading Limited v. Zambia Revenue Authority, IBFD.

Only 3.6% of judgments rejected the OECD TPG. Two cases were from OECD member countries in Australia and the United States, and four cases were from non-OECD member countries in Argentina, India and Malawi. The rejection of the OECD TPGs in the Argentina courts was due to a view that clarity in those cases could be obtained from the domestic legislation without reference to external sources. It is noted that in Argentina case 24.921-1, which involved a similar tax year, the courts did consider the use of the OECD TPG in supporting TP adjustments.<sup>85</sup> In addition, Argentinian *case 20.972-I* also considered the OECD TPG despite the court decision appearing two years earlier.<sup>86</sup> This inconsistency indicates that there is an avenue for external sources such as the OECD TPG to be warranted in the court judgment when interpreting domestic legislation. Malawi took a strict stance against the application of the OECD TPG as an interpretative aid when applying the ALP.<sup>87</sup> The courts explicitly expressed that because the OECD TPG was not law in Malawi, it could not be used. The Indian courts considered the tax periods in the case occurred before the inception of the 2001 India TP regulations.<sup>88</sup>

In the Australian case, *SNF (Australia) Pty Ltd v. Commissioner of Taxation of the Commonwealth of Australia*<sup>89</sup> the court considered whether the arm's length consideration in the local Australian ITA could be interpreted with the OECD TPG. The court rejected the use of the OECD TPG on the basis that the treaties enforced between France, China and Australia were ratified before the OECD TPGs were drafted and therefore were, based on a static approach, inadmissible for use in interpretation by the courts. The court therefore did not rely on the OECD TPG. As the OECD TPG were not referenced as an authoritative statement in domestic statutory provisions, the ALP could only be applied under the domestic tax legislation in the view of the court. Similarly in the United States case, *National Westminster Bank plc v United States of America*,<sup>90</sup> although the OECD TPG are generally considered by the United States courts, in this case the treaty was signed before the 2003 OECD TPG. As such, the court did not apply the OECD TPG in its judgment.

Even in TP disputes amongst OECD member countries, the results indicate that the OECD TPG are not always considered in the court judgments as an interpretative aid.

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<sup>85</sup> In Argentina: Tribunal Fiscal de la Nación (Federal Tax Court), 11 December 2009, Case 24.921-1: Volkswagen Argentina S.A. v Administración Federal de Ingresos Públicos (Federal Administration of Public Resources), IBFD.

<sup>86</sup> Argentina: Tribunal Fiscal de la Nación (Federal Tax Court), 15 August 2007, Case 20.972-I: Compañía Ericsson SACI v Administración Federal de Ingresos Públicos (Federal Administration of Public Resources), IBFD.

<sup>87</sup> J. Roeleveld & T. (Tracy) Johnson, OECD Transfer Pricing Guidelines are not law in Malawi in Tax Treaty Case Law around the Globe 2019 (M. Lang et al. eds., IBFD 2020), Books IBFD.

<sup>88</sup> India: High Court of India, 30 September 2011, *BBC Worldwide Ltd. v. DIT* (2011), IBFD Case Law.

<sup>89</sup> In Australia: Federal Court of Australia, 1 June 2011, *SNF (Australia) Pty Ltd v. Commissioner of Taxation of the Commonwealth of Australia* (2011), Australian Government: Australian Taxation Office, <https://www.ato.gov.au/law>.

<sup>90</sup> In United States of America: United States Court of Federal Claims, 14 November 2003, Case No. 95-758T: *National Westminster Bank, PLC v The United States*, IBFD.

Chapter 4 analyses the domestic TP tax legislative environment in Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe, further inspecting relevant TP case law to examine how the OECD TPG have been applied in each country's domestic law (if at all) and to determine whether the OECD TPG have influenced shaping the domestic TP legislative framework in these African countries.

## Chapter 4: Trends observed within a sample of African countries case law on the influence of the OECD TPG in domestic tax law.

Chapter 3 discussed the summary of results of the OECD TPG weighting in the court's judgments using a sample of OECD and non-OECD countries.

The purpose of this chapter is to analyse the domestic TP tax legislative environment using a sample of TP cases within the African courts to determine if the OECD TPG as a soft law instrument have shaped the domestic tax law since the court judgments and aids in the interpretation of the ALP. The number of cross-border tax disputes within the African context is limited. This chapter further discusses how the consideration of the OECD TPG in these cases has subsequently shaped the domestic tax legislative environments in these countries, especially where there is a lack of guidance in the application of the ALP, even though these countries are not members of the OECD. The development of the TP legislative landscape for a sample of African countries in Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe is analysed in this chapter to determine if it is influenced by the OECD TPG.

### 4.1. Ghana

An analysis is conducted to understand the current domestic TP tax legislative environment and its developments. As at the date of this paper, the author has not identified any domestic case law dealing with transfer pricing in the Ghanaian courts. The closest case within Ghana is the *Beiersdorf Ghana Limited vs The Commissioner General Ghana Revenue Authority*; however, this case does not consider the OECD TPG nor does it provide insight into the domestic legislation on transfer pricing and the influence that the OECD has on its TP legislation.

#### 4.1.1. Ghana case law: *Beiersdorf Ghana Limited vs The Commissioner General Ghana Revenue Authority*

There is no decided transfer pricing case in Ghana.<sup>91</sup> This case addresses the application in law of royalties and any WHT implications thereon.<sup>92</sup> The only close connection with the ALP in the ambit of TP, is that the royalties were paid in terms of a cross border transaction. The case did not reference the OECD TPG nor was it brought into question. This case was therefore excluded from the analysis of this paper.

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<sup>91</sup> A. Ali-Nakyeya, *Ghana - Transfer Pricing - Country Tax Guides IBFD (Accessed 30 November 2022)*, 2023. Refer to chapter 15: Litigation.

<sup>92</sup> Ghana: HC, 1 August 2018, *Beiersdorf Ghana Limited vs The Commissioner General Ghana Revenue Authority Accra*, Laws Ghana.com, <https://lawsghana.com/judgement/Ghana/High-Court/237>.

#### 4.1.2. Ghana transfer pricing domestic tax legislation and TP Regulations

Section 31(1) of the Ghana Income Tax Act, 2015 (Act 896, as amended), covers the ALP.<sup>93</sup> TP Regulations 2012, L.I. 2188 was the first set of TP regulations in Ghana and subsequently revised in 2020 by the TP Regulations, 2020 (L.I. 2412).<sup>94</sup> The revision was necessary with the aim of aligning itself with the action plans of the OECD to tackle Base Erosion and Profit Shifting (BEPS) and provide further clarity on the technical aspects on the application of the ALP.<sup>95</sup> Further guidance on the application of the ALP was further provided in a Practice Note to the Transfer Pricing Regulations, 2020 (L.I. 2412) issued late in 2022.

#### 4.1.3. Ghana: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

In an effort to align the action plan of the OECD on BEPS, the Ghana Revenue Authority published a practice note to the TP Regulations, 2020 (L.I. 2412) where in paragraph 2 it states, “*The Regulations shall be applicable, commentaries in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration (OECD Guidelines) and United Nations Manual on Transfer Pricing for Developing Countries (UN Manual) may provide guidance where the Regulations do not provide the same.*”<sup>96</sup> Ghana has indicated through this practice note that when applying the TP regulations, the use of the OECD TPG can be used as an interpretative aid in domestic legislation if the current regulations are unable to provide guidance in the application of the ALP. It is further noted that in practice, the latest OECD TPG are followed by the Ghana Revenue Authorities as an international best practice. In addition, Ghana is also a signatory to the VCLT.<sup>97</sup>

## 4.2. Tanzania

To better understand the TP legislative environment at the time in Tanzania and whether there is reference to the OECD TPGs, the case *Alliance One Tobacco Tanzania Limited v Commissioner General, Tanzania Revenue Authority* (2018) and *Atlas Copco Tanzania Limited v Commissioner General, Tanzania Revenue Authority* (2019) are first considered in this section. The analysis in these

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<sup>93</sup> Ghana: Income Tax Act, 2015 (Abridged Version) ( Act 896 ), National Legislation. Refer to section 31 of the ITA requiring, a person within the ambit of this section ALP to “*quantify, characterise, apportion and allocate amounts to be included in or deducted from income to reflect an arrangement that would have been made between independent persons*”.

<sup>94</sup> Ghana Revenue Authority (GRA): ‘Ghana: Practice Note on Transfer Pricing Regulations 2012 (L.I. 2188)(Methodologies and Related Issues)’, Pub. L. No. L.I.2188, 2012 (2017).

<sup>95</sup> C Fuest and F Neumeier, Ghana - Corporate Taxation - Country Analyses (IBFD), *Annual Review of Economics*, vol. 15, 2023, <https://doi.org/10.1146/annurev-economics-082322-014747>. Also refer to, ‘PwC: (Ghana) The Dawn of a New Transfer Pricing Regime in Ghana The New TP Rules in a Nutshell’, n.d., <https://www.pwc.com/gh/en/assets/pdf/tax-alert-dawn-of-new-transfer-pricing-regime-in-ghana.pdf>.

<sup>96</sup> A. Ali-Nakyea, *Ghana - Transfer Pricing - Country Tax Guides IBFD (Accessed 30 November 2022)*. Refer to *chapter 2.6 Status and impact of OECD Guidelines and UN TP Manual*.

<sup>97</sup> United Nations Treaty Collection, ‘UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties’, *United Nations*, vol. 1155, 1969, [https://treaties.un.org/pages/ViewDetailsIII.aspx?src=TREATY&mtdsg\\_no=XXIII-1&chapter=23&Temp=mtdsg3&clang=\\_en](https://treaties.un.org/pages/ViewDetailsIII.aspx?src=TREATY&mtdsg_no=XXIII-1&chapter=23&Temp=mtdsg3&clang=_en).

cases provide little to no guidance on asserting the influence of the OECD TPG; however, it does examine how TP legislation is governed in Tanzania. The analysis further explains the current domestic TP tax legislative environment and the developments thereof since these cases.

#### 4.2.1. Tanzania case law: Alliance One Tobacco Tanzania Limited v Commissioner General, Tanzania Revenue Authority

The tax years in dispute are 2003, 2004 and 2009. The case is an appeal case heard in the Tax Revenue Appeals Tribunal. In the case the Tanzania Revenue Authority (TRA) imposed a TP adjustment disallowing the cost incurred by the taxpayer to its related company within the group (i.e., Alliance One International AGA). The taxpayer argued that the cost incurred was in the production of income; however, the TRA disagreed and disallowed the deduction.

The premise of the appeal by the taxpayer is that insufficient evidence was provided by the tax authorities (in terms of section 97(c) of the ITA) to explain to the taxpayer why the TP cost was disallowed as a deductible expense. The case does not address the merits of the TP adjustment, nor does it provide any guidance on the weighting of the OECD TPG by the courts. The appeal was dismissed by the court and the court maintained the ruling in favour of the tax authorities.

#### 4.2.2. Tanzania case law: Atlas Copco Tanzania Limited v Commissioner General, Tanzania Revenue Authority

The appellant, Atlas (the taxpayer), is a company part of an MNE headquartered in Sweden for the sale of generators to sister companies within the MNE. The accounting periods in question were the tax years of assessment of 2007 and 2008. The respondent (tax authorities) did not agree that the intercompany sales commission was at an arm's length price and triggered a dispute.

The case does not deal with the weighting of the OECD TPG as a soft law instrument when applying the ALP. The issues presented in the case were triggered by a retrospective transfer pricing adjustment that the taxpayer applied to the prior period tax returns to correct the historical margins on the transaction as per their internal TP policy. The adjustment, initiated by the taxpayer, was in accordance with their internal TP policy that they retrospectively adjusted creating a lower tax liability in the prior period tax return. The court was required to rule on whether this adjustment can be applied to the prior period tax returns that resulted in a lower tax liability. The court found that there was insufficient evidence produced by the taxpayer to conclude that the adjustment was applied consistently with the taxpayer's internal TP policy and the adjustment was denied. The court noted, *"If it failed to comply with its transfer pricing policy at the material time, it could not invoke it retrospectively to effectively*

*reduce its tax liability.*”<sup>98</sup> It is understood, from this judgment, that Tanzanian domestic tax law is strict on the timing of the TP adjustments.

#### 4.2.3. Tanzania transfer pricing domestic tax legislation and TP Regulations

The application of the ALP and TP principles in Tanzania are governed in the local Tanzanian Income Tax legislation in section 33 of the Income Tax Act of 2004 (as amended) and the revised Tax Administration (Transfer Pricing) Regulations 2018 (TP Regulations) issued in 27 April 2018.<sup>99</sup> Section 33 of the ITA gives the Commissioner the authority to adjust transactions between associated parties to an arm’s length price if the Commissioner is of the opinion that the transaction is not conducted on an arm’s length basis. The regulations further clarify the appropriate method to be used to apply the ALP and provide guidance on other reportable documentation to have in place in support of the arm’s length transaction. These cases were not relevant to understand the basis on which the OECD TPG can be relied upon when applying the ALP. It is also noted that Tanzania is a signatory to the VCLT.<sup>100</sup>

#### 4.2.4. Tanzania: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

On 1 July 2020, the Commissioner General of the Tanzania Revenue Authority, issued transfer pricing guidelines in relation to the 2018 TP Regulations.<sup>101</sup> Paragraph 11 references the recognition of the latest OECD and/or UN TP guidelines as an interpretative aid when applying the ALP.<sup>102</sup> The guidance illustrates that the Commissioner has the final authority to decide on the most appropriate interpretation of the ALP when referencing the OECD TPG or UN Practical Manual on Transfer Pricing;<sup>103</sup> however, when the OECD TPG contradict or are inconsistent with the 2018 domestic TP Regulations, the regulation will prevail.<sup>104</sup>

Therefore, as the OECD TPG are updated, in terms of this regulation, the latest OECD TPG should be used when applying the ALP if it is deemed appropriate by the Commissioner of the TRA as a means of applying the ALP (to the extent that it does not contradict the (current) 2018 TP Regulation rules). This is an example where the influence of the OECD TPG has permeated its way into Tanzania’s local TP regulations requiring (at least) some consideration.

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<sup>98</sup> Tanzania: Court of Appeal, 6 August 2020, Case No 167 of 2019 (TZCA 317) Tanzania vs Atlas Copco Tanzania Ltd., TPCases.com.

<sup>99</sup> E Mkaru, ‘Tanzania - Corporate Taxation - Country Tax Guides, Country Analyses IBFD (2023).

<sup>100</sup> United Nations Treaty Collection, ‘UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties’.

<sup>101</sup> ‘Tanzania Revenue Authority (TRA): Transfer Pricing Guidelines, 2020’, Pub. L. No. ISO 9001: 2015 Certified (2020), URL: [https://www.tra.go.tz/Images/headers/TPR-01072020-TRANSFER\\_PRICING\\_GUIDELINE.pdf](https://www.tra.go.tz/Images/headers/TPR-01072020-TRANSFER_PRICING_GUIDELINE.pdf).

<sup>102</sup> TRA: Tanzania Transfer Pricing Guidelines (2020). Refer to paragraphs 11.1. and 11.2.

<sup>103</sup> TRA: Tanzania Transfer Pricing Guidelines (2020). Refer to paragraph 11.4.

<sup>104</sup> TRA: Tanzania Transfer Pricing Guidelines (2020). Refer to paragraph 11.3.

### 4.3. Uganda

To better understand the TP legislative environment at the time in Uganda and whether there is reference to the OECD TPGs, the cases *East African Breweries International Limited v Uganda Revenue Authority* (decision 2020) and *Bondo Tea Estates Ltd v Uganda Revenue Authority* (decision 29 March 2021) are first considered in this section. In the case, *East African Breweries International Limited v Uganda Revenue Authority*, there is an indirect reference to the Kenya Unilever case of 2003 where a reference was made to the use of the OECD TPG under Kenya's domestic tax rules; however, the Uganda court noted that using the OECD TPG rules was not relevant in this case. The case *Bondo Tea Estates Ltd v Uganda Revenue Authority* did not directly refer to the OECD TPG. Uganda is not a signatory to the VCLT<sup>105</sup> and the court did not hear an argument as to how Article 31 of the VCLT is applied to conclude the use of the OECD TPG as an interpretative tool when applying the ALP. Although there is no weighting given to understand the status of the OECD TPG to infer their importance as a soft law instrument in the court judgment, the analysis in these cases still reveal an understanding of how the TP legislation is applied in Uganda. Lastly, the current domestic TP tax legislative environment and the developments since these cases are respectively addressed in sections 4.3.3. and 4.3.4.

#### 4.3.1. Uganda case law: *East African Breweries International Limited v Uganda Revenue Authority*

*Eastern African Breweries International Limited*, the appellant (taxpayer), is a company resident in Uganda. The tax periods in question are the years 2009 to 2015. The taxpayer explained that *Uganda Breweries Limited* was viewed as a dispatch entity with a marketing role to distribute products and does not hold commercial presence in Uganda. The main issue argued before the court is whether there was a sufficient presence in Uganda to justify income attributable to Uganda. The tax authorities noted that the markup on the sale of goods by *Uganda Breweries Limited* to the taxpayer was not at arm's length when compared to the sales between the taxpayer and the consumers residing in Sudan, Congo and Rwanda. Due to a lack of TP documentation and an office in Uganda to testify the substance of the transaction, the commissioner exercised its rights in terms of section 90 in the Uganda ITA which gives the Commissioner General the right to, "...*distribute, apportion or allocate income, deductions between the associates as is necessary to reflect the income realized by the taxpayer in an arm's length transaction*".<sup>106</sup> In the view of the Commissioner, the TP arrangement originated in Uganda and raised an arm's length adjustment for the sales made from Uganda to the taxpayer in terms of section 90.

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<sup>105</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

<sup>106</sup> Uganda: Tax Appeals Tribunal, 7 July 2020, Case no.14 of 2017: *Uganda vs East African Breweries International Ltd*. July 2020, [TPcases.com](http://TPcases.com).

The case has less to do with which TP rules to apply and rather notes that in Uganda domestic tax legislation, the Commissioner has the power to apply an arm's length price where it is found that the related party transaction is not at arm's length. This is explained in the Tribunal ruling where reference is made to the Kenya Unilever case (2003).<sup>107</sup> It is noted by the Kenyan court judgment that Unilever Kenya Limited was entitled to use the OECD TPG in the absence of guidance on the application of the ALP in Kenya's domestic tax legislation. In this Uganda case, the court notes that the issue was not about whether the OECD TPG rules can or should apply. Together with other facts and circumstances, the tribunal ruled in favour of the assessments raised by the Uganda tax authorities and regarded the tax authorities as acting within their discretion to raise the adjustment.

#### 4.3.2. Uganda case law: Bondo Tea Estates Ltd v Uganda Revenue Authority

The case covers the topic of whether the TP charged between the related parties of the applicant, Bondo Tea Estates Ltd (the taxpayer), was at arm's length. The tax period in question was the 2017 year of assessment.

The case provides insight into the application of the domestic TP tax legislation in Uganda. There is a difference in the Uganda ITA between "fair market value" and "Arm's length price".<sup>108</sup> In the opinion of the taxpayer, the ALP sections should have been applied by the taxpayer. The difference of opinion between the taxpayer and the tax authorities arose when the tax authorities based their adjustment on the "average market price" rather than the arm's length price as defined in the ITA. The arm's length price in terms of the ITA is determined by understanding what an independent third party would pay for the goods, whereas the fair market value relies on the "average market price".

The taxpayer states that within the ITA, the "Fair Market Value" is viewed as an objective market-based valuation whereas the arm's length price is a subjective valuation by comparing uncontrolled transactions. The arm's length price uses the prices charged between independent persons in terms of the Uganda domestic tax law. The taxpayer proved that the price charged was the same as that between independent persons. In contrast, the tax authorities relied on an internal field report.<sup>109</sup> This report was concluded by the court as unreliable because of the retrospective adjustment by the tax authorities using

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<sup>107</sup> Kenya: High Court of Kenya, 5 October 2005, Case no. 753 of 2003: Unilever Kenya Ltd v Commissioner of Income Tax, IBFD Case Law.

<sup>108</sup> Uganda: Tax Appeals Tribunal, 29 March 2021, Case no. 65 of 2018: Uganda vs Bondo Tea Estates Ltd., TPCases.com. Refer to reference in this case where the difference is explained, "*The applicant submitted that while the Income Tax Act provides for the application of both a "fair market value" and an "arm's length value" for the purpose of determining the price between independent parties under the concept of "a willing buyer-willing seller" considerable differences existed between these two methods. The "arm's length principle called for a subjective valuation by establishing comparing uncontrolled transactions the fair market value principle requires an objective, market-based valuation."*

<sup>109</sup> Uganda: Tax Appeals Tribunal, 29 March 2021, Case no. 65 of 2018: Uganda vs Bondo Tea Estates Ltd., TPCases.com. A field report conducted on 12 September 2018 to determine the average market price to evaluate the price as of April 2016- March 2017.

a report generated with information that arose after the tax year end in question and where there was a possibility that the prices could have been higher.

For the above reasons, the court ruled in favour of the taxpayer on the matter since the TP was at an arm's length price and the basis of adjustment from the tax authorities was unlawful.

A common thread between the two cases is that in Uganda the Commissioner has the power to apply an arm's length price in terms of s90(1) where it is found that the related party transaction is not at arm's length. In this case, the commissioner failed to provide sufficient evidence as to why the price suggested by the commissioner was at arm's length and that the price determined by the applicant was not. There is no reference to the OECD TPG in the court's judgment because the argument was about whether the arm's length price applies rather than the "Fair market value" in terms of the domestic tax legislation.

#### 4.3.3. Uganda transfer pricing domestic tax legislation and TP Regulations

The application of the arm's length price and TP principles in Uganda is governed through the Income Tax Act, Chapter 340 of the Laws of Uganda: "arm's length price" in s52(3), s53(2) and s90(1). Section 90(1) of the ITA acts as an anti-avoidance provision giving the Commissioner-General the authority to adjust a transaction that does not hold economic substance for the purpose of tax avoidance and deemed not to be at arm's length. Section 3 of the ITA defines an "associate" of another person if there is direct or indirect control over the voting power in a company of more than 50%.<sup>110</sup> The Income Tax (Transfer Pricing) Regulations, 2011 issued on 1 July 2011 is also important in providing guidance when applying the ALP. The TP Regulations is a statutory instrument brought into hard law through section 164 of the Income Tax Act Chapter 340.<sup>111</sup> The OECD TPG is mentioned only in the TP regulations and not in the black ink hard law of section 164, which enacts the TP regulations. As evident in the Bondo Tea Estates case, the Uganda ITA retains references relating to the "market value"<sup>112</sup>; however, where the "arm's length price" is referenced in the ITA, the TP regulations still hold as interpretative guidance in its application.

#### 4.3.4. Uganda: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

The OECD TPG is applied in the Uganda ITA when applying the ALP as provided in paragraph 6 of The Income Tax (Transfer Pricing) Regulations 2011. The regulations are enforced in the Uganda ITA

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<sup>110</sup> Uganda Gazette: Statutory Instruments and Statutory Instruments Supplement, 'The Uganda Gazette No.2: The Income Tax (Transfer Pricing) Regulations 2011', CIV § (2011), <https://www.drtp.ca/wp-content/uploads/2015/02/Uganda-Transfer-Pricing-Regulations-2011.pdf>. Refer to paragraph 6, "*Application of OECD documents*".

<sup>111</sup> Uganda Gazette on Transfer Pricing Regulations (2011).

<sup>112</sup> Uganda: Income Tax Act, Chapter 340 of the Laws of Uganda (1997), Pub. L. No. 1 July 1997, 157 (n.d.), National Legislation. Refer to sections 51-69 where various subsections refer to "market value".

in section 164 of the ITA allowing for the OECD TPG to be applied.<sup>113</sup> The Uganda TP regulations states that the OECD TPG and OECD MTC application of Article 9 shall be applied in determining the arm's length price when consistent with the Uganda TP regulation and the OECD TPG should be considered when applying the ALP.<sup>114</sup> As expected, if there is an inconsistency between the OECD TPG, TP Regulations and the ITA, the ITA will take precedence. Through the regulations referencing the OECD TPG as a guideline in interpretation of the ALP in terms of the Uganda ITA, the OECD TPGs are now established as an important tool when applying the ALP.

#### 4.4. Kenya

To better understand the application of the TP legislative environment at the time in Kenya and whether there is reference to the OECD TPGs, the *Unilever Kenya Ltd v The Commissioner of Income Tax* case is first considered in this section. This case is paramount in understanding the importance of the OECD TPG in the Kenya tax legislative environment because the OECD TPG is referred by the court as an “*international*” best practice. The analysis below then explains the current domestic TP tax legislative environment and the developments thereof since this case.

##### 4.4.1. Kenya case law: *Unilever Kenya Ltd v The Commissioner of Income Tax*

The *Unilever* case in Kenya is the first case to consider the application of section 18(3) of the ITA with regards to its TP regime.<sup>115</sup> *Unilever Plc* owns a majority shareholding in *Unilever Kenya Ltd (UKL)*. *Unilever Uganda limited (UUL)* is a related party to UKL. UKL is the manufacturer to UUL. UKL services both internally to UUL and external customers. UKL sold to UUL at a lower price than that of the domestic external market, which led to the tax authorities concluding that the transactions are not at an arm's length price. The basis of contention between the taxpayer and tax authorities is that the tax authorities put forward a further argument to the effect that the prices charged by UKL to UUL are nothing but “discounted prices” and not at arm's length. The court ruled on 17 September 2003 for the 1995 and 1996 tax years in question.

At the time of this case, there was no clear guidance from the Kenya domestic tax legislation on how to apply the ALP even though the concept was mentioned in the local tax legislation in section 18(3).<sup>116</sup>

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<sup>113</sup> Uganda: Income Tax Act. c.f. section 164(1), “*Regulations*”, where it states, “*The Minister may, by statutory instrument, make regulations for better carrying into effect of the purposes of this Act.*”

<sup>114</sup> Uganda Gazette on Transfer Pricing Regulations (2011). Instruments and Supplement, The Uganda Gazette No.2: The Income Tax (Transfer Pricing) Regulations 2011. Paragraph 6(b), “*...and updated from time to time.*” This paragraph references the use of the latest OECD TPG when determining the ALP.

<sup>115</sup> B Nyamori, ‘An Analysis of Kenya’s Transfer Pricing Regime’, no. September 2003 (2023): 153–60.

<sup>116</sup> Kenya: Income Tax Act, Cap. 470 Laws of Kenya (The Act) (1973), National Legislation. Refer to section 18 of the Act where it is stated that: *Related parties’ definition*. Commissioner of Income Tax quoted section 18: “*18(3) where a non-resident person carries on business with a related resident person and the course of that business is so arranged that it produces to the resident person either no profits or less than ordinary profits which might be expected to accrue from that business if there had been no such relationship, then the gains or*

Part of the ruling in the court's decision was whether the OECD TPG is an acceptable guide when applying the ALP since the TP rules were only gazetted later in 2006.<sup>117</sup> The contracting party to this transaction was the related party company in Uganda.

The tax authorities used the Comparable Uncontrolled Price method (CUP) (as envisaged in the OECD TPG at the time) but did not consider that there might be pricing differences which could alter the arm's length price. Each mix of sales was different and an exact like-for-like external CUP comparable without any adjustments to the price was an incorrect approach from the perspective of the taxpayer. No material affects were adjusted between UUL sales and domestic sales by the tax authorities in their assessment.

In the absence of clear guidance on the application of section 18(3) of the domestic Kenyan Tax act, the OECD was sought after by the taxpayer as the most appropriate "*international best practice*" in dealing with arm's length TP between associated enterprises. The tax authorities disagreed with the use of OECD international principles when applying the ALP for domestic tax law cases. The tax authorities adopted the static approach to the treaty interpretation where the OECD TPG cannot be used to interpret the ALP unless the country to the treaty has adopted the recommendations in a tax treaty.

In this case, limited guidance in the local tax legislation resulted in a higher reliance on the interpretation of the ALP using the OECD TPG. The OECD TPG was a relevant source of interpretation of the ALP by the courts because domestic TP local legislation at the time of this court case showed that the Kenyan Income Tax Act was silent on which TP methods to use when determining the arm's length price. Due to the outcome of the decision by the high court, section 18(3) was amended with the intent of reducing the level of proof required by the tax authorities to make a profit adjustment.

Kenya is not a member of the OECD and has not formally enacted the OECD principles in law. The taxpayer then sought out international best practice through the OECD TPG to defend its use of the ALP. The court does not view the use of the OECD TPG as a conflict in the application of the domestic tax legislation article 18(3), but instead relies on the OECD TPG as a necessary interpretative tool where the local legislation does not have sufficient guidance on the application of the ALP.

#### 4.4.2. Kenya transfer pricing domestic tax legislation and TP Regulations

The ALP in Kenya domestic tax legislation is governed through the Income Tax Act (Chapter 470), Laws of Kenya, as amended by Income Tax Rule, 2012 and Income Tax Rule, 2014, in section 18(3). Since the *Unilever Kenya Ltd v, The Commissioner of Income tax (No. 753 of 2003)* judgment, clarity

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*profits of that resident person shall be deemed to be the amount that might have been expected to accrue if the course of that business had been conducted by independent persons dealing at arm's length."*

<sup>117</sup> C Mutava, 'Kenya - Corporate Taxation, Country Tax Guides', sec.10.2 "Transfer Pricing", Country Surveys, IBFD.

on s18(3) of the ITA occurred and the TP regulations developed resembling that of the OECD Guidelines (despite not directly mentioned in the regulation and ITA).<sup>118</sup>

Kenya's TP legislation is governed through section 18(3) of the ITA, section 18A of the ITA (effective 3 April 2017) and the Income Tax (Transfer Pricing) Rules of 2006 (amended 2012), effective 1 July 2006,<sup>119</sup> empowers the commissioner to adjust a TP transaction if it is found that it is not in accordance with the ALP in domestic tax legislation.<sup>120</sup> Tax Procedures Act, No. 29 of 2015, is an anti-avoidance tax provision giving the authority to the Kenyan Tax Authorities to investigate pricing arrangements between local units of multinationals with their parent companies and overturn any that it deems to have been structured with the intention of avoiding tax. Kenya's Cabinet Secretary for National Treasury, on 4 September 2023, issued Draft Income Tax (Transfer Pricing) Rules, 2023 which will replace the current Kenya Transfer Pricing Rules of 2006.<sup>121</sup> Despite the replacement of the current Kenya TP rules of 2006, the TP legislation model in Kenya will still be modelled around the OECD and ATAF TP legislative suggestions.

#### 4.4.3. Kenya: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

Kenya is not a member of the OECD. The Unilever case was instrumental in urging the Ministry of Finance in Kenya to issue TP Guidelines to help taxpayers apply the ALP. The ministry took heed of the court judgment urging the Kenyan Tax Authorities to align the local legislation with international development and practices.<sup>122</sup> The Kenya Transfer Pricing Rules of 2006 were issued shortly after the Unilever Kenya Ltd case judgment and the TP rules largely embodied the guidance in the OECD TPG.<sup>123</sup>

The OECD TPG are not a legally binding instrument;<sup>124</sup> however, in the Kenya Unilever case (2003), the court relied on the OECD TPG as an interpretative aid when applying the ALP. In the absence of guidance in local legislation on the administration and application of a transaction in an international landscape, the best evidence on "*international thinking*" on the issue was reference to the OECD TPG

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<sup>118</sup> Editors notes on Commentary to this case, Bob Michel, IBFD, Kenya - Case 753 of 2003, 5 October 2005 (Summary)

<sup>119</sup> G Maina, 'Kenya - Transfer Pricing, Country Tax Guides', sec.2.1., "Systems applied", IBFD; MUTAVA, 'Kenya - Corporate Taxation, Country Tax Guides'.

<sup>120</sup> EY, 'EY Worldwide Transfer Pricing Reference Guide', n.d., [https://www.ey.com/en\\_gl/tax-guides/worldwide-transfer-pricing-reference-guide-2020](https://www.ey.com/en_gl/tax-guides/worldwide-transfer-pricing-reference-guide-2020). Refer also to, C Mutava, 'Kenya - Corporate Taxation, Country Tax Guides', sec.10.2 "Transfer Pricing", Country Surveys, IBFD.

<sup>121</sup> 'KPMG Kenya: Tax Alert - The Draft Income Tax (Transfer Pricing) Rules', KPMG, 2023, [https://assets.kpmg.com/content/dam/kpmg/ke/pdf/tax/2023/Tax Alert on Draft Transfer Pricing Rules 2023.pdf](https://assets.kpmg.com/content/dam/kpmg/ke/pdf/tax/2023/Tax%20Alert%20on%20Draft%20Transfer%20Pricing%20Rules%202023.pdf).

<sup>122</sup> B Nyamori, 'An Analysis of Kenya's Transfer Pricing Regime', Bosire Nyamori, 'An Analysis of Kenya's Transfer Pricing Regime', 19 Intl. Transfer Pricing J. 2 (2012), Journal Articles & Opinion Pieces IBFD.

<sup>123</sup> B Nyamori, 'An Analysis of Kenya's Transfer Pricing Regime', 19 Intl. Transfer Pricing J. 2 (2012), Journal Articles & Opinion Pieces IBFD.

<sup>124</sup> OECD: OECD Transfer Pricing Country Profile, 'Transfer Pricing Country Profile: Kenya (OECD)', accessed 30 November 2022, <https://www.oecd.org/ctp/transfer-pricing/transfer-pricing-country-profile-kenya.pdf>.

in the Kenya Unilever case. Kenya is a signatory to the VCLT.<sup>125</sup> In the taxpayer's argument, there was no mention of the use of the VCLT as a basis of international customary law to allow the use of the OECD TPG to defend its use of the ALP. The court judgment accepted the use of international tax practices from the OECD TPG despite the absence of a justification by the taxpayer as to why it is allowed as an interpretive aid to apply the ALP.

Kenya has adopted a different implementation of its TP rules compared to Tanzania and Uganda. As noted in chapters 4.2 and 4.3, Tanzania and Uganda include a clause in the documentation of their TP regulation to consider the latest OECD TPG when applying the ALP. Therefore, any changes that may arise in the OECD TPG, will be prescriptive as part of their domestic law, in so far as it does not contradict its domestic law. Kenya has not adopted this approach and instead tailored the Kenyan TP Rules to be specific to their own domestic tax legislative landscape predicated upon the model of the OECD TPG.

The Kenya Revenue Authority (KRA) has further shown their commitment to aligning their local legislation with the guidance of the OECD TPG in Kenya's TP regime.<sup>126</sup> A specific reference to the OECD TPG is not explicitly mentioned in the local tax legislation. The scope of the Kenya TP Rules is not as detailed as that of the OECD TPG.<sup>127</sup> It is the best practice to use the guidelines set forth by the OECD TPG as an interpretive aid. The Kenya TP rules aid in the application of the ALP in local legislation and are prescriptive in terms of local legislation. The revision to the 2006 TP rules is noted to help align with international developments reflected in the OECD TPG.<sup>128</sup>

#### 4.5. Malawi

To better understand the TP legislative landscape in Malawi and whether there is reference and importance given to the OECD TPGs, the case Eastern Produce Malawi Limited is first considered in this section. This case provides clear insight into the weight in the Malawi courts of the status of the OECD TPG at the time of the court judgment. The analysis below then explains the current domestic TP tax legislative environment and developments thereof since this case.

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<sup>125</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

<sup>126</sup> Kenya: Kenya Revenue Authorities (International Tax Office): G Njuguna, 'Transfer Pricing Developments - Kenya's Experience', International Tax Office, Kenya Revenue Authorities, n.d., <https://www.kra.go.ke/news-center/blog/1425-transfer-pricing-developments---kenya-s-experience>. 31 August 2021. Mr G Njuguna of the KRA International Tax Office has stated, "*Kenya has embraced internationally recognized guidelines namely United Nations (UN) and OECD Transfer pricing guidelines and the OECD Base Erosion and Profit Shifting (BEPS) project outcomes.*"

<sup>127</sup> See Report in Bowmans: Alex; Fredrick Ogutu Mathini, 'KENYA: THE CABINET SECRETARY FOR THE NATIONAL TREASURY AND ECONOMIC PLANNING PUBLISHES NEW DRAFT TRANSFER PRICING RULES', Bowmans, n.d., URL: <https://bowmanslaw.com/insights/tax/kenya-the-cabinet-secretary-for-the-national-treasury-and-economic-planning-publishes-new-draft-transfer-pricing-rules/>.

<sup>128</sup> See Bowmans report, Kenya: 'KPMG Kenya: Tax Alert - The Draft Income Tax (Transfer Pricing) Rules'.

#### 4.5.1. Malawi case law: Eastern Produce Malawi Limited v Commissioner General of Malawi Revenue Authority

Eastern Produce Malawi Limited (EPML) is a company that produces and processes tea in Malawi. The Malawi tax authority audited and imposed additional tax for the years 2009 to 2013. The tax authorities disputed the pricing method that the taxpayer used as not being in compliance with the ALP, which resulted in additional taxes imposed on the taxpayer. The taxpayer noted that the tax authority based the additional assessment on a calculation of the arm's length price using the guidance in the OECD TPG.

EPML argued that the Malawi Revenue Authority (MRA) was acting unlawfully to enforce the OECD TPG over the local TP legislation. At the time of this case, Section 127A of the Taxation Act and Taxation (Transfer Pricing) Regulations, 2009 were the rules in force as far as TP issues are concerned. It was agreed by both the taxpayer and tax authority that the OECD TPG at the time of the court case were not law and that the only law in force was section 127A in conjunction with the 2009 TP regulations. At the time the TP regulations did not make any specific reference to the OECD TPG as an interpretative tool to apply the ALP. The legislation at the time places the onus on the taxpayer to choose an appropriate TP method to determine the arm's length price. The court had to decide if the taxpayer's application of the ALP was in accordance with section 127A and the 2009 TP regulation or if its basis was derived from the OECD TPG when applying the ALP. It was resolved by the court that the OECD TPG was the main source of guidance used for the tax authorities assessment when applying the ALP at a time when the OECD TPG had no bearing on local Malawian tax law. Reliance on the OECD TPG by the tax authorities as a soft law instrument caused the courts to rule in favour of the taxpayer because the OECD TPG method had no legal basis.<sup>129</sup>

This case reveals that the prerequisite condition of the OECD TPG must be prescriptive in the regulations, and further, in the domestic tax legislation for reliance to be placed when applying the ALP. As a result of the omission of the OECD TPG in the prescriptive text of the local ITA or regulations, the court ruled against the tax authority's method of applying the ALP.

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<sup>129</sup> Malawi: High Court of Malawi, 27 July 2018, Case 43 of 2016: Eastern Produce Malawi Limited v Commissioner General of Malawi Revenue Authority, IBFD. Refer to judgement, 'Malawi - Case 43 of 2016, 27 July 2018 (Decision)' 2018, no. 43 (2020), where the following is noted: *"I am of the humble view that where local legislation provides for the law, it is always imperative to apply that law and use any international instruments in interpreting that local law. I do not think that using the international instruments while side lining local legislation is allowed. Doing that, in my considered view, will defeat the intention of the framers of the local legislation. Section 127A of the Taxation Act and Transfer Pricing Regulations 2009 provided for the law in as far as transfer pricing issues are concerned in Malawi. It does not matter that these local pieces of legislation are modelled on OECD Guidelines as to warrant use of the OECD Guidelines at the expense of the Taxation Act and the Transfer Pricing Regulations, 2009. The respondent was at liberty to cite and use these OECD Guidelines only as an interpretation aid. As a tax administrator, the respondent is to strictly follow the dictates of the law as enacted by the Legislature. Any slight departure from the law is not allowed. Having said that, it is my finding that the respondent used the OECD Guidelines and not the Transfer Pricing Regulations 2009. The use of these Guidelines at the expense of the Transfer Pricing Regulations, 2009 is illegal."*

One of the concerns presented to the court was whether the tax authority had the ability to determine an arm's length price that they deem fit; however, it was proven in the case that the tax authorities did not have full discretionary powers to decide an arm's length price.<sup>130</sup> The court ruled that the OECD TPG was inappropriately used by the tax authorities; however, if the tax authorities were able to show that the domestic tax legislation was used to determine the arm's length price and referred to the OECD TPGs to confirm their view, a different outcome may have been ruled by the court. Malawi is a signatory and has ratified the VCLT.<sup>131</sup> An explanation by the tax authorities to indicate the use of the VCLT to justify the use of the OECD TPG as an interpretative tool to apply the ALP may have persuaded the court to rely on the use of the OECD TPG.

#### 4.5.2. Malawi transfer pricing domestic tax legislation and TP Regulations

The latest Taxation (Transfer Pricing) Regulations was issued from 1 July 2017, and section 127A of the Malawi Tax Act is the primary TP legislation in Malawi which was enacted in 2009 and amended in 2017.<sup>132</sup> The amendment of section 127A replaces the previous version in terms of the Tax Amendments No. 24 of 2017 effective from 1 July 2017.<sup>133</sup> The tax amendment to section 127A of the ITA is the substantive law to apply the ALP.<sup>134</sup> Section 127A does not refer to the OECD Guidelines directly; however, the 2017 TP Regulations references the OECD TPG pursuant to the application of section 127A.<sup>135</sup> Section 146 of the Malawi ITA also has a clause for "Regulations by Minister" where the purpose of the regulations is to apply the purpose of the provisions of the Act.<sup>136</sup> As such, the TP regulations are considered as prescriptive to the implementation of the ITA.

#### 4.5.3. Malawi: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

Given that section 127A of the Malawi ITA does not directly reference the OECD TPG, the development of the Malawi TP regulations are further discussed in this section. The OECD TPG is explicitly mentioned in the 2017 Malawi TP regulations subsequent to the case Eastern Produce Malawi

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<sup>130</sup> J. Roeleveld & T. Johnson, OECD Transfer Pricing Guidelines are not law in Malawi in Tax Treaty Case Law around the Globe 2019 (M. Lang et al. eds., IBFD 2020), Books IBFD (accessed 6 Nov. 2022).

<sup>131</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

<sup>132</sup> EY, 'EY Worldwide Transfer Pricing Reference Guide'.

<sup>133</sup> Prof. A P Mutharika, 'The Malawi Gazette Supplement No. 24 of 2017 - An Act to Amend the Taxation Act' (n.d.), [https://www.mra.mw/assets/upload/downloads/Customs\\_VAT\\_and\\_Taxation\\_Amendments\\_2017.pdf](https://www.mra.mw/assets/upload/downloads/Customs_VAT_and_Taxation_Amendments_2017.pdf).

<sup>134</sup> Malawi: Taxation Act, Chapter 41:01 (1964), National Legislation, Malawi LII. Refer to section 10: Replacement of section 127A of the principal Act.

<sup>135</sup> Refer to, Malawi: Taxation Act, Chapter 41:01 (1964); Refer further to, V Moyo, 'Malawi - Corporate Taxation, Country Tax Guides', Country Surveys, IBFD. Refer to, 'Malawi - Transfer Pricing Regulations 2017 - Issued (27 July 2017), News IBFD', n.d.; 'Malawi Government Gazette Notice, No.36, dated on 3 July 2017, p.396; Taxation Act, (Chapter, 41:01): Taxation (Transfer Pricing) Regulations 2017, by the Minister of Finance, Economic Planning and Development' (n.d.), <https://www.mra.mw/>.

<sup>136</sup> Malawi: Income Tax Act, 'Malawi - Taxation Act - Chapter 41:01', Pub. L. No. Section 146, 'Regulations by Minister' (2014), <https://malawilii.org/akn/mw/act/1963/46/eng@2014-12-31/source.pdf>.

Limited in the analysis above.<sup>137</sup> The reference to the OECD TPG in the regulations was done to try and protect the tax base of Malawi. The 2009 Taxation (Transfer Pricing) Regulations were repealed subsequent to the recent 2017 TP regulations. Malawi is not a member of the OECD; however, the 2017 TP Regulations refers specifically to the OECD TPG as a guideline for interpretation.<sup>138</sup> These regulations now support the use of the OECD TPGs by the Malawi tax authorities since the OECD TPG is linked to the regulations with the likely result that the court will at least have to refer to the OECD TPG as an interpretative aid in future. Of course, where the domestic tax legislation and the OECD TPG differ, the domestic tax legislation takes precedence.<sup>139</sup> This was evident in the 2019 *Nestlé Zambia Trading Limited v Zambia Revenue Authority* (2019)<sup>140</sup> case, involving the Nestlé company that operates in Zambia and Malawi making the case relevant to the local laws and regulations in Malawi as well. The use of the OECD TPG as an interpretative aid to apply the ALP was accepted by the Zambian courts. The application of using the OECD TPG is consistent with the Malawi 2017 TP regulations allowing the OECD TPG as an interpretative aid when applying the ALP. The 2017 TP Regulations have been developed to allow use of the OECD TPG even in respect of transactions with neighbouring African countries such as Zambia.

#### 4.6. Nigeria

To better understand the application of the domestic TP legislative environment at the time in Nigeria and whether there is reference to the OECD TPGs, the first TP case in Nigeria is the case *Prime Plastichem Nigeria Limited v Federal Inland Revenue Services* is first considered in this section. The case provides useful insight into the status of the OECD TPG as a soft law instrument. The analysis below then explains the current domestic TP tax legislative environment and the development thereof since this case.

##### 4.6.1. Nigeria case law: *Prime Plastichem Nigeria Limited v Federal Inland Revenue Services*

This case is the first TP case in Nigeria.<sup>141</sup> The trigger in the case was the change in TP methodology by the taxpayer from CUP to Transactional Net Margin Method (TNMM) from 2013 to 2014 that caused the tax authorities to investigate further.

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<sup>137</sup> Malawi Gazette: Refer to Malawi Gazette, Malawi Government Gazette notice, No.36, dated on 3 July 2017, p.396; Taxation Act, (Chapter, 41:01): Taxation (Transfer Pricing) Regulations 2017, by the Minister of Finance, Economic Planning and Development. issued on 3 July 2017, explicitly mentioning guidance in accordance with the OECD TPG in note 14(1) and 14(2).

<sup>138</sup> Ibid.; IBFD, ‘Malawi - Transfer Pricing Regulations 2017 – Issued (27 July 2017), News IBFD’.

<sup>139</sup> Moyo, ‘Malawi - Corporate Taxation, Country Tax Guides’.

<sup>140</sup> Zambia: Tax Appeals Tribunal, 28 March 2019, *Nestlé Zambia Trading Limited v. Zambia Revenue Authority*, IBFD.

<sup>141</sup> Nigeria: T Oyedele, ‘Nigeria - Transfer Pricing, Country Tax Guides, Country Surveys, IBFD’, n.d.

The mechanism allowing the tribunal to adjust the transaction is through TP regulation No. 1 2012, para 4(2) in their local legislation.<sup>142</sup> Para 4(2) of the TP regulations No. 1 2012 states that, “*where a connected taxable person fails to comply with the provisions of this regulation, the Service shall make adjustments where necessary if it considers that the condition imposed by connected taxable persons in a controlled transaction are not in accordance with the arm’s length principle*”.<sup>143</sup> It is on the basis of the contravention of the 2012 TP regulation that the tax authorities claimed the taxpayer failed to comply.<sup>144</sup> The tax authorities argued further that the taxpayer’s use of a different TP method between the two years is in contradiction to the consistency principle as envisaged in the OECD TPG for similar transactions. The consistency principle explained in this case is noted as “*Transfer Pricing Analysis, methods must be consistently applied where the facts are not materially difference as in this instant case.*”<sup>145</sup> The functional analysis was proven to be the same in 2013 and 2014 and therefore inappropriate to have different methods testing the arm’s length price.

The Federal Inland Revenue Service (FIRS) is able to disregard the TP approach of the taxpayer through paragraph 5(2) of the TP regulation. The tribunal ruled in favour of the tax authority.

It is apparent from this case that Nigeria’s tax authority’s inspection was driven by the inconsistencies noted in the taxpayer’s tax return submission. Taxpayers should caution on ensuring that the TP policy is accurately completed by the individuals with the right level of expertise.<sup>146 147</sup>

The TAT ruled in favour of the tax authorities due to a lack of supporting explanation and documentation on the functional analysis performed by the taxpayer in relation to the TP method used. The taxpayer further lacked the ability to justify the use of TNMM and the reason for the change in method from CUP to TNMM when the functional analysis was consistent between the two years. Although it was not the case, the taxpayer was accused of cherry picking comparables that was suitable for their business as opposed to appropriately documenting the commercial reasoning substantiating the TP approach. The taxpayer lacked supporting documentation to justify an operating margin Profit level Indicator (PLI) for the type of transaction with its related party. The tax authorities presented a case that justified the use of the Gross Profit Margin (GPM) as a PLI that was considered a best practice<sup>148</sup> for this type of transaction and functional analysis of the taxpayer to determine the arm’s length profit.

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<sup>142</sup> Nigeria: The Tribunal, 19 February 2020, Case TAT/LZ/CIT/015/2017: Prime Plastichem Nigeria Limited v Federal Inland Revenue Services, IBFD.

<sup>143</sup> Ibid.

<sup>144</sup> Ibid.

<sup>145</sup> Ibid.

<sup>146</sup> ‘Nigeria’s Tax Appeal Tribunal Rules in Favour of FIRS in a Landmark TP Case - PwC Tax Alert (PwC Nigeria)’, n.d., [https://pwc-nigeria.typepad.com/tax\\_matters\\_nigeria/2020/02/nigerias-tax-appeal-tribunal-rules-in-favour-of-firs-in-a-landmark-tp-case-.html](https://pwc-nigeria.typepad.com/tax_matters_nigeria/2020/02/nigerias-tax-appeal-tribunal-rules-in-favour-of-firs-in-a-landmark-tp-case-.html) - PwC analysis of the court decision, 22 February 2020.

<sup>147</sup> Ibid. PwC tax alert where it is further noted by PwC Nigeria asserting that, “*For example it is not correct that the GPM is a recognised PLI for the application of the TNMM. It is also not correct that the FIRS’ application of the TNMM is in line with global best practice.*”

<sup>148</sup> Although contended by PwC Nigeria as not correct.

#### 4.6.2. Nigeria domestic TP tax legislation and TP Regulations

The current Taxation (Transfer Pricing) Regulations were brought into effect from 12 March 2018.<sup>149</sup> This is the primary source of TP regulations within domestic law of Nigeria. The 2012 TP Regulations (being the first year that the TP regulations were introduced in Nigeria) was repealed subsequent to the enactment of the 2018 TP regulation (2012).<sup>150 151</sup>

#### 4.6.3. Nigeria: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

The Nigerian TP regulations are based on both the OECD TPG and UN Practical Manual on Transfer Pricing. The TP guidelines ensure that an arm's length price is charged between connected persons and is defined in regulation 12 of the 2018 TP regulation.<sup>152</sup> Nigeria is not a member of the OECD; however, the TP regulations should be interpreted in accordance with the OECD TPG and ALP in terms of Article 9 of the UN and OECD MTC. Nigeria's Income Tax (Transfer Pricing) Regulations No 1, 2012 (2012 TP Regulations) were used as a basis of judgment related to the 2013 and 2014 tax years in the *Plastichem* cases. The judgment was delivered on the 19 February 2020, well after the latest implementation of the TP regulations in 2018; however, the 2012 TP regulations were pertinent to the case as it related to the 2013 and 2014 tax years. Subsequently, the 2012 TP regulations were revoked and replaced with the Income Tax (Transfer Pricing) Regulations 2018 (2018 TP Regulations). Both the 2012<sup>153</sup> and 2018 TP Regulations<sup>154</sup> included a clause that explicitly mentions the use of the OECD TPG to determine the arm's length price so long as there is no contravention and inconsistency with domestic law. It should further be noted that Nigeria is a signatory to the VCLT.<sup>155</sup>

#### 4.7. South Africa

To better understand the TP legislative environment at the time in South Africa (SA) and whether there is reference to the OECD TPGs, the cases *Crookes Brothers Limited v CSARS* (2018) and *ABC (Pty) Ltd v SARS* (2021) are referred to in this section. The *Crookes Brothers Limited* case did not provide insight into the status of the OECD TPG; however, it does examine how the ALP is implemented in the

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<sup>149</sup> EY, 'EY Worldwide Transfer Pricing Reference Guide'.

<sup>150</sup> Ibid.; S Odinna, 'Nigeria - Corporate Tax Guides, IBFD', n.d.; T OYEDELE, 'Nigeria - Transfer Pricing, Country Tax Guides IBFD.

<sup>151</sup> T Oyedele, Nigeria - Transfer Pricing, Country Tax Guides, Country Surveys, IBFD.

<sup>152</sup> J N Isaac, Nigeria - Corporate Tax Guides, Country Surveys, IBFD.

<sup>153</sup> 'Federal Republic of Nigeria, Official Gazette (No.77, Vol.99), The Income Tax (Transfer Pricing) Regulations, No. 1, 2012', Pub. L. No. No. 1, 2012, B815 (2012), <https://www.sac.com.ng/wp-content/uploads/2019/11/Nigeria-Transfer-Pricing-Regulations-2012.pdf>. Refer to regulation paragraph 11, "*Application of UN and OECD documents*".

<sup>154</sup> 'Federal Republic of Nigeria, Official Gazette (No. 38, Vol.105), The Income Tax (Transfer Pricing) Regulations, 2018', Pub. L. No. 19 March 2018, B113 (2018), <https://firs.gov.ng/wp-content/uploads/2021/06/Official-Gazette-of-TP-Regulations-2018.pdf>. Refer to regulation paragraph 18, "*Application of UN and OECD documents*".

<sup>155</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

SA domestic tax legislative environment. Although the ABC (Pty) Ltd case was heard in a special court known as the Tax court, a reference was directly made to the OECD TPG to infer their status in the domestic TP tax legislative environment in South Africa. It must be noted that any decision made in the Tax court is a non-binding decision on any court in South Africa and does not hold any precedent. The analysis below explains the current domestic TP tax legislative environment and the developments thereof since these cases.

#### 4.7.1. South Africa case law: Crookes Brothers v Commissioner for South African Revenue Services

This judgment was delivered at the High Court on 8 May 2018.<sup>156</sup> The decision of the High Court holds precedent and is a binding decision on High Courts and the lower courts (although its decision is not binding on the Supreme Court or Constitutional Court).<sup>157</sup> In the case, *Crookes Brothers Limited v. CSARS*, an interest free loan between associated enterprises was not classified at an arm's length price that resulted in a primary adjustment initiated by the taxpayer.<sup>158</sup> The primary adjustment initiated by the taxpayer resulted in a reduced assessment triggering the tax authority to investigate further.

Section 31 deals with two types of adjustments, namely primary and secondary adjustments. Primary adjustments are made where there is a difference in the arm's length transfer price such that the taxable income of the taxpayer is required to be adjusted. The secondary adjustments are defined in section 31 of the ITA as a deemed loan and remain until such time that the arm's length price is rectified; such deemed loan was also classified as an affected transaction.<sup>159</sup> The deemed loan secondary adjustment was considered impractical and removed again with retrospective effect in 2015. Secondary adjustments are levied in the form of a "deemed distribution" of an "asset in specie".<sup>160</sup>

In this case, a primary adjustment was applied through section 31 of the South African ITA where it requires that a primary adjustment be made if the taxpayer is not transacting at arm's length. This section allows the Commissioner of SARS to make an appropriate adjustment to the taxable income of the relevant taxpayer.

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<sup>156</sup> South Africa: High Court, 8 May 2018, Case No. 14179/2017: Crookes Brothers Limited and The Commissioner of the South African Revenue Services (2017), Case Law, TPcases.com.

<sup>157</sup> Johann Hattingh, 'An Overview of the Court System of South Africa with Emphasis on the Resolution', *Bulletin for International Taxation*, no. March (2011): 127–46.

<sup>158</sup> South Africa: High Court, 8 May 2018, Case No. 14179/2017: Crookes Brothers Limited and The Commissioner of the South African Revenue Services (2017), Case Law, TPcases.com.

<sup>159</sup> M. van Blerck, Chapter 14 South Africa in *Transfer Pricing and Intra-Group Financing: The entangled worlds of financial markets and transfer pricing* (A.J. Bakker & M.M. Levey eds., IBFD 2012), Books IBFD.

<sup>160</sup> South Africa: 'South African Income Tax Act No. 58 of 1962, Section 31; South Africa - Taxation Laws Amendment Act, 23 of 2020 (Promulgated - (20 Jan. 2021)', National Legislation, IBFD.

This case did not deal with the relevance of the OECD TPG as a soft law instrument, but it does illustrate the domestic tax legislative landscape of how the ALP is applied in South African domestic tax legislation and the powers given to the Commissioner of SARS to raise a TP adjustment.

#### 4.7.2. South Africa case law: ABC (Pty) Ltd v Commissioner for South African Revenue Services

The judgment in this case took place in the South African Tax court. The weighting of the decisions made in the Tax Court are not binding and is considered as a special court in South Africa.<sup>161</sup> An emphasis should also be noted that the decisions of the Tax Court do not establish precedent but rather provide persuasive evidence.<sup>162</sup>

The taxpayer is a company that imports and sells chemical products and bought inventory from a related party in Switzerland. The 2011 tax year of assessment was the relevant tax period for the court's consideration.

A matter addressed in this case was the insufficient documentation presented by the taxpayer to prove to the Commissioner of SARS that a CUP method is the arm's length price for this type of intercompany transaction. The second matter addressed by the taxpayer was the issue of the Commissioner of SARS using the OECD TPG as binding guidance instead of the literal meaning of section 31(2) in legislation. The meaning of section 31(2) of the ITA during the 2011 tax year of assessment led the taxpayer to use the CUP method to determine the arm's length price as the most appropriate.

The use of OECD TPG by the Commissioner of SARS was also challenged by the taxpayer because South Africa is not a member of the OECD. This claim was rejected by the court because recognising South Africa's involvement with the OECD cannot be disregarded. As noted by the Davis Tax Committee, South Africa is the only African country part of the G20, a member of the OECD/G20 Inclusive Framework on BEPS and a participant of the OECD Working Party No. 6 on the *Taxation of Multinational Enterprises* even though South Africa is not a member of the OECD and only holds an observer status.<sup>163</sup>

The court ruled in favour of the tax authorities. In this Tax Court judgment, the court placed a high reliance on the OECD TPG to apply the ALP in conjunction with domestic tax legislation in its ruling in section 31(2) of the South African ITA.<sup>164</sup> Although the judgment in this case may act as persuasive evidence and not binding in future disputes when applying the ALP in TP transactions, it is evident that

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<sup>161</sup> J Hattingh, 'South Africa - An Overview of the Court System of South Africa with Emphasis on the Resolution of Tax Disputes', *Bulletin for International Taxation* 65, no. No. 3 (2011).

<sup>162</sup> Ibid.

<sup>163</sup> Further supported in, 'The Davis Tax Committee: Base Erosion and Profit Shifting for the Minister of Finance (2016)', 2016, [https://www.taxcom.org.za/docs/New\\_Folder3/10 BEPS Final Report - Actions 8, 9, 10 and 13.pdf](https://www.taxcom.org.za/docs/New_Folder3/10%20BEPS%20Final%20Report%20-%20Actions%208,%209,%2010%20and%2013.pdf). Chapter 1.6, "Acknowledging South Africa's position in Africa".

<sup>164</sup> South Africa: 'South African Income Tax Act No. 58 of 1962, Section 31; South Africa - Taxation Laws Amendment Act, 23 of 2020 (Promulgated - (20 Jan. 2021)', National Legislation, IBFD.

the changing TP domestic tax legislative framework is in the process of aligning with the OECD TPG. This case assists in understanding the South African domestic TP legislation and the role that the OECD TPG has in influencing the application of the ALP.

#### 4.7.3. South Africa domestic TP legislation

South Africa's tax system is a residence-based tax system.<sup>165</sup> Section 2 of the South African Constitution states that it is the “*supreme law of the Republic*” and any inconsistencies with the laws in the Constitution are considered invalid.<sup>166</sup> The bilateral comprehensive tax treaties entered by South Africa and the respective developing nations are binding international agreements in terms of section 231 of the South African Constitution.<sup>167</sup> Therefore, these bilateral treaties are part of South African domestic law through the application of section 231 of the Constitution.<sup>168</sup>

It should be noted that whilst the bilateral treaty is regarded as an international agreement in terms of section 231 and section 232 of the South African Constitution; the OECD model tax convention and related Commentary is not binding in terms of South African domestic law.<sup>169</sup> South Africa is seen merely as an observer of the OECD model tax convention and does not hold member status.

The use of Commentary from the model tax conventions as a means of interpretative aid is not binding law in South African courts. South Africa is not a signatory to the VCLT;<sup>170</sup> however, the VCLT can be viewed as customary international law in South Africa.<sup>171</sup> The model tax conventions and related Commentary do, however, provide useful tools to interpret the context and meaning behind the bilateral treaty in accordance with Article 31 of the VCLT.<sup>172</sup> A comparison between the treaty and the most relevant OECD MTC and UN MTC closest to the conclusion date of the treaty used to identify deviations between the articles in the respective bilateral treaties. The relevant MTC is identified as the model with the release date closest to the date on which the specific bilateral treaty was concluded, as the ratification date can be delayed after conclusion of the treaty negotiation for long periods.

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<sup>165</sup> ZA: South African Revenue Service (SARS), ‘Tax-and-Non-Residents’, available at: <https://www.sars.gov.za/ClientSegments/Individuals/Tax-Stages/Tax-and-Non-Residents/Pages/default.aspx> (last accessed 2 June 2020).

<sup>166</sup> South Africa: The Constitution of the Republic of South Africa (1996), National Legislation, IBFD, refer to section 2.

<sup>167</sup> L. Steenkamp, *The use of the OECD Model Tax Convention as an interpretative aid: The static vs ambulatory approach debate considered from a South African perspective*, Journal of Economic and Financial Sciences, 10(2) (2017), 195-205. doi:<https://doi.org/10.4102/jef.v10i2.13>.

<sup>168</sup> Ibid.

<sup>169</sup> E. Mazansky, *South African Tax Court Departs from Commentary on Article 5 of the OECD Model in Finding a Permanent Establishment*, 69 Bull. Intl. Taxn. 9 (2015), Journal Articles & Papers IBFD.

<sup>170</sup> United Nations Treaty Collection, ‘UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties’.

<sup>171</sup> R. Carvalho et al., *Is There Evidence of Increasing Harmonization in the Interpretation of Tax Treaties by Courts in Their Reference to Foreign Court Decisions? A Study of South African Case Law*, 71 Bull. Intl. Taxn. 10 (2017), Journal Articles & Opinion Pieces IBFD (accessed 13 Jan. 2024).

<sup>172</sup> United Nations, 1969 Vienna Convention on the Law of Treaties.

The domestic tax law in section 31 of the ITA allows SARS to adjust the TP between the SA taxpayer and the other party if it is not deemed to be at arm's length.<sup>173</sup> This adjustment must be made for the South African taxpayer to reflect the arm's length nature of the transaction. Section 31 is crucial to the implementation of TP in South Africa where the principles of the arm's length TP are aligned with that of the OECD as at 1 April 2012.<sup>174</sup> South Africa has recently added a definition of "*affected transactions*" in the ITA which includes the term "Associated Enterprises" in line with the meaning from the OECD which will be effective for tax years on or after 1 January 2023.<sup>175</sup> Before the enactment of this term in section 31 of the ITA, the only other reference where the term "Associated Enterprise" was relevant was found in double tax treaties.<sup>176</sup> The meaning of the term "Associated Enterprises" is not found in the South African domestic tax legislation; however its closest meaning can be found in the Commentary of the 2017 OECD MTC, where the term is indicative of "*parent and subsidiary companies and companies under common control*".<sup>177</sup> The term "*control*" is not defined in the South African domestic tax legislation and require reference to case law for its interpretive meaning.

Practice Note (PN) 7<sup>178</sup> is not a prescriptive text of all transfer pricing issues that might arise in South Africa but is meant to act as practical guide for the taxpayer to apply the ALP. In section 3.2.1. of PN 7, the status of the OECD TPG is discussed explaining that PN 7 is created based on the guidelines set forth in the OECD TPG. The Commissioner of SARS endorses the OECD Guidelines, elevating its importance and recognising it a global standard when applying the ALP.<sup>179</sup>

#### 4.7.4. South Africa: Observations of OECD TPG in domestic tax legislation

The Crookes Brothers v CSAR (2018) case does highlight a similarity between section 31 and article 9(2). The wording of article 9(2) allows for costs to be adjusted if it is not at market related prices. The transaction appears to be isolated to financial transactions in this case; however, it must be determined whether this is actionable to other transactions that are not under arm's length. This case is an example

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<sup>173</sup> W. Horak & J. Kotze, Chapter 14 South Africa in *Transfer Pricing and Dispute Resolution: Aligning strategy and execution* (A.J. Bakker & M.M. Levey eds., IBFD 2011), Books IBFD (accessed 02 June 2020).

<sup>174</sup> M van Blerck, 'Chapter 14 South Africa'.

<sup>175</sup> M Badenhorst, 'New Guidance in South Africa on the Definition of "Associated Enterprises" in Connection with the Transfer Pricing Rules', *International Transfer Pricing Journal* 2023, no. 2 (2023): 100–103.

<sup>176</sup> Ibid.

<sup>177</sup> Article 9: OECD (2017). Refer to the commentary of Article 9, p.226; paragraph 1.

<sup>178</sup> SARS, 'Republic of South Africa section 31 of the Income Tax Act, 1962 (the Act): Determination of the taxable income of certain person from international transactions: Transfer Pricing', *SARS: Practice Note No. 7*, no. 7 (1999).

<sup>179</sup> Refer to section 3.2.1. of Practice Note 7 where it is stated, "*Because of the international importance of the OECD Guidelines, this Practice Note is based on, inter alia, those guidelines. Although South Africa is not a member country of the OECD, the OECD Guidelines are acknowledged as an important, influential document that reflects unanimous agreement amongst the member countries, reached after an extensive process of consultation with industry and tax practitioners in many countries. The OECD Guidelines are also followed by many countries which are not OECD members and are therefore becoming a globally accepted standard.*"

of how TP adjustments is enacted through domestic law and highlighting less the impact of the OECD TPG as a soft law instrument in the court's judgment.

The ability for SARS to enforce an adjustment to the transaction to achieve an arm's length price is in line with section 31 of the ITA.<sup>180</sup> In the the tax court case, ABC Ltd v SARS, it is noted from the Davis Committee 2016 Report that the status of South Africa as the investment gateway to Africa<sup>181</sup> is tied to the development of tax policy in line with international standards and acknowledging the OECD TPGs status into the domestic tax legislation. The case further highlights the importance that the court relies on the OECD TPG as an interpretative aid in its judgment. The status is further solidified by the Davis Committee BEPS-subcommittee acknowledging in the 2016 report that despite South Africa holding an OECD observer status, it is a member of the OECD BEPS Committee.<sup>182</sup>

The recently enacted legislation for the inclusion of the term, "*Associated Enterprises*" in section 31's definition of "*Affected transactions*" of the ITA, a similar term to that of Article 9 of the OECD MTC,<sup>183</sup> is indicative of the OECD's influence permeating in the domestic tax legislative framework in South Africa.

#### 4.8. Zambia

To better understand the TP legislative environment at the time in Zambia and whether there is reference to the OECD TPGs, two cases are first considered in this section, namely Nestlé Zambia Trading Limited v Zambia Revenue Authority (2019) and Mopani Copper Mines PLC v. Zambia Revenue Authority (2020). In the Nestlé Zambia case domestic TP tax legislation was in place for the periods under scrutiny by the tax authorities and the court considered the guidance by the OECD TPG. In the Mopani Copper Mines PLC case the court considered the OECD TPG; however, the purpose of the case was whether an anti-tax avoidance scheme existed in the TP arrangement and little weighting was granted to the OECD TPG. The analysis below explains the current domestic TP tax legislative environment and the developments thereof since these cases.

##### 4.8.1. Zambia case law: Nestlé Zambia Trading Limited v Zambia Revenue Authority

In the case Nestlé Zambia Trading Limited v Zambia Revenue Authority, a TP audit was conducted for the relevant tax years of 2010 to 2014. The decision by the Tax Appeals Tribunal was concluded on 28 March 2019.

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<sup>180</sup> 'The Davis Tax Committee: Base Erosion and Profit Shifting for the Minister of Finance (2016)'.

<sup>181</sup> South Africa: Tax Court, 7 January 2021, ABC (Pty) Ltd v. Commissioner for the South African Revenue Service, Case Law, IBFD.

<sup>182</sup> 'The Davis Tax Committee: Base Erosion and Profit Shifting for the Minister of Finance (2016)'.

<sup>183</sup> Article 9, OECD (2017). Refer to article 9, "*Associated Enterprises*".

The tax authorities audited Nestlé Zambia TP transactions because it saw the taxable losses generated in each year as a signal that the transactions were not at arm's length. The other area of contention was the method the Zambian Revenue Authority (ZRA) used to determine the arm's length price on an aggregate basis compared to that of the taxpayer using a transaction basis resulting in a proposed adjustment through the local tax legislation and regulations because the transaction, according to the tax authorities, was not at arm's length.

There was no dispute in the case to use the OECD TPG as a means of applying the ALP. The relevant local legislation at the time of the assessment did not have clear TP application of the ALP in the Income Tax (Transfer Pricing) Regulation No. 20 of 2000 and the dispute was around the method used. It is noted that in this case, the TP regulations did not make a direct reference to the OECD TPG causing a question of contention presented to the courts on the ability to use the OECD TPG. Zambia is a signatory to the VCLT.<sup>184</sup> Although an argument discussing the use of the VCLT was not heard by the court, it is assumed, in signing the VCLT, the principles of meaning envisaged in Article 31 of the VCLT was used when considering the OECD TPG as an interpretive aid to the ALP in Zambia's domestic tax legislation. The OECD TPG was used as an interpretive aid to apply the meaning of the ALP as envisaged in the local laws and regulations.

#### 4.8.2. Zambia case law: Mopani Copper Mines PLC v. Zambia Revenue Authority

In the case Mopani Copper Mines PLC v Zambia Revenue Authority, a TP audit was conducted for the relevant tax years 2006 to 2010. The decision by the Supreme Court of Zambia was concluded on 20 May 2020. This case involving the mining sector notes a common trend of a lack of comparable data available<sup>185</sup> in Africa when dealing with TP in this industry. This issue is further exacerbated by the complexity of the transaction and the lack of experts with industry-specific knowledge by the courts to opine on its merits.

The taxpayer is a large mining company conducting business in Zambia. The taxpayer sold copper internationally to its Switzerland shareholder as well as the domestic market in Zambia. It was identified that the taxpayer transacted with the related party parent company on the export of copper at lower than market related prices compared to the local Zambian market. As such the tax authorities claimed that the transactions between the taxpayer and its foreign shareholder was not at arm's length triggering the application of an adjustment in terms of the local Zambian tax legislation.

This CUP analysis revealed that profits were minimized in Zambia when exporting to the Switzerland parent company. On this basis the court ruled in favour of applying section 95 of the ITA as there was

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<sup>184</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

<sup>185</sup> A.W. Oguttu, *Base Erosion and Profit Shifting: A Blueprint for Africa's Response* (IBFD 2021), Books IBFD.

reasonable grounds for the tax authorities to believe, from the audit, that the sale of copper at lower than market related prices (or not at arm's length) was sufficient grounds to conclude that the transaction was disguised as the main purpose of tax avoidance. The Supreme court held in favour of the ZRA for applying section 95 where it was found that taxable revenue was shifted out of Zambia to the lower taxing jurisdiction.<sup>186</sup> A contention over a Deloitte report addressed to the parent company, highlighted that the commodity prices were at arm's length; however, the ZRA rejected this report on the grounds that there were inconsistencies.

A weakness in this case is the lack of application of whether the commodity prices were correctly at arm's length under Zambia domestic tax legislation.<sup>187</sup>

#### 4.8.3. Zambia transfer pricing domestic tax legislation and TP Regulations

Since the Nestlé case in Zambia, there were further developments to the TP legislative framework. The Nestlé case highlighted that the OECD TPG as a soft law instrument was relied upon to apply the ALP even though it was not explicitly mentioned in the regulation in the Zambian TP regulations of 2000. This resulted in the TP regulations being developed further to include amendments with a direct reference to the 2017 OECD TPG in a guide to the application of the ALP.<sup>188</sup> An amendment to the regulations was issued through the Government gazette on the 6 April 2018 where Zambia adopted the 2017 OECD TPG recommendations to provide further clarity on the ALP.<sup>189</sup> Zambia's TP is governed through section 97A to 97D of the ITA and local TP regulations.<sup>190</sup>

#### 4.8.4. Zambia: Observations of OECD TPG in domestic tax legislation and/or TP Regulations

Zambia is not a member of the OECD but enjoys observer status and follows the guidelines of the OECD TPG as referenced in its practice notes as a guideline when applying the their domestic tax legislation.<sup>191</sup> Where any inconsistency arises between the OECD TPG and that of the domestic tax law, the domestic tax law takes precedence.<sup>192</sup> The Zambian Transfer Pricing (Amendment) Regulations

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<sup>186</sup> Ibid.

<sup>187</sup> Ibid.

<sup>188</sup> Zambia: ZRA, 'Zambia Revenue Authority: Domestic Tax Division - Practice Note No. 2/2018' (2018), <http://www.zra.org.zm/>, Tax Authorities Documentat, ZRA.

<sup>189</sup> EY, 'EY Worldwide Transfer Pricing Reference Guide'.

<sup>190</sup> I Kawaza Mvula, 'Zambia - Corporate Taxation, Country Tax Guides', Country Survey, IBFD. Also refer to, EY, 'EY Worldwide Transfer Pricing Reference Guide'.

<sup>191</sup> Zambia Revenue Authority: Domestic Tax Division - Practice Note No. 2/2018. Refer to the foreword referencing, "*The Transfer Pricing Rules broadly adopt the internationally accepted "Arm's Length Principle" for the purposes of determining the income and associated expenditure for transactions between connected persons. Accordingly, this Practice Note has been drafted in a manner broadly consistent with the Arm's Length Principle as laid out in Article 9 of the OECD and UN Model Tax Conventions on Income and Capital; and the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.*"

<sup>192</sup> Zambia: Regulations, 'Government of Zambia, The Income Tax (Transfer Pricing) (Amendment) Regulations, 2018, The Income Tax Act (Laws, Volume 25, Cap 453)', Pub. L. No. Statutory Instrument No. 24 of 2018 (n.d.), [https://www.zambialaws.com/Zambia2018Pdfsi/SI 24 of 2018.pdf](https://www.zambialaws.com/Zambia2018Pdfsi/SI%2024%20of%202018.pdf). Refer to regulation 20(2), "*Where there is any inconsistency between the Act, these Regulations and the OECD Guidelines or the UN*

2018 (the 2018 regulations) were published in the Government Gazette on 6 April 2018, under Statutory Instrument No. 24 of 2018 and further issued Practice Note No. 2/2018 which includes direct references to the OECD TPG;<sup>193</sup> however the practice note is not intended to be prescriptive in Zambia domestic tax law for all possible TP situations.<sup>194</sup> The initial TP Regulations 2000 did not contain a reference to the OECD TPG. The TP Rules in Zambia have been amended since the initial TP Regulations of 2000.<sup>195</sup> This indicates that the amendments to the Zambian TP rules are predicated upon the position of the OECD TPG as noted in regulation 20 of the Transfer Pricing (Amendment) Regulations 2018<sup>196</sup> where the use of the OECD TPG to determine the arm's length price is deemed appropriate. The use of the OECD TPG in the amended Zambian TP Rules, and further noted historically in the Nestlé case as persuasive interpretative guidance in court judgments, are indicative of its influence in domestic TP regulations in Zambia.

#### 4.9. Zimbabwe

To better understand the TP legislative environment at the time in Zimbabwe and whether there is reference to the OECD TPGs, the case *C F (PVT) Ltd v Zimbabwe Revenue Authority (2018)* is first considered. This case provides useful insight into the status of the OECD TPG as a soft law instrument at the time of the court judgment. The analysis below explains the current domestic TP tax legislative environment and the developments thereof since this case.

##### 4.9.1. C F (PVT) LTD (the taxpayer) v. Zimbabwe Revenue Authority (the tax authorities)

In the case of *C F (PVT) LTD (the taxpayer) v. Zimbabwe Revenue Authority (the tax authorities)*;<sup>197</sup> the main issue presented to the court was whether the tax authorities correctly enforced section 24 of the Zimbabwe ITA. Section 24 of the Zimbabwe ITA gives the tax authorities the right to enforce an adjustment of notional income/cost if the transaction was not at arm's length. The years under assessment were 2009 to 2012. The taxpayer is in the business of importation, distribution and

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*manual referred to in this regulation, the Act and these Regulations shall prevail to the extent of the inconsistency.”*

<sup>193</sup> Zambia Revenue Authority (Zambia): Domestic Tax Division - Practice Note No. 2/2018, Tax Authorities Documentation (ZRA).

<sup>194</sup> Ibid.

<sup>195</sup> Zambia: Government of Zambia, The Income Tax (Transfer Pricing) Regulations, 2000, The Income Tax Act (Laws, Volume 19, Cap 323), Pub. L. No. Statutory Instrument No. 20 of 2000 (n.d.), Zambia Regulation, URL: <https://zambia.ii.org/akn/zm/act/si/2000/20/eng@2000-02-18/source.pdf>.

<sup>196</sup> Zambia: Government of Zambia, The Income Tax (Transfer Pricing) (Amendment) Regulations, 2018, The Income Tax Act (Laws, Volume 25, Cap 453). Regulation 20(1) reads, “*These Regulations shall be construed in a manner consistent with – (a) the Organisation for Economic Cooperation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations as supplemented and updated from time to time, and...*”

<sup>197</sup> Zimbabwe: High Court, 26 January 2018, Income Tax Appeal, Case No HH 99-18, *C F (PVT) LTD v. Zimbabwe Revenue Authority*, Case Law, TPCases.com.

marketing of motor vehicles and spare parts. The transactions involved a Mauritius financier company importing vehicles into Zimbabwe within this Multinational Enterprise.

The argument presented by the taxpayer was whether the use of the OECD TPG to apply the ALP was appropriate given that it was not part of law<sup>198</sup> and should not be considered on the merits of this case. The onus was on the taxpayer to prove that the tax authorities were unjustified in this approach. The tax authorities provided a functional analysis which indicated that the profits attributable to the Zimbabwean associated enterprise was understated putting the Zimbabwean fiscus in a detrimental position thereby indicating that the transaction was not at arm's length. Despite the taxpayer actually paying the amount, this was disregarded by the tax authorities. The functional analysis was presented by the tax authorities to prove that the transaction was not at arm's length in terms of the Zimbabwe ITA.

The tax authorities attempted to use the functional analysis envisaged in the OECD TPG as an international best practice to determine the arm's length price through section 24 of the ITA at the time; however, there was insufficient grounds to conclude that this analysis was considered as part of the domestic tax legislation. The tax authorities argued the use of the functional analysis, as envisaged in the OECD TPG, was on the basis of an international best practice to determine the arm's length price. Even if the functional analysis could have been used to determine the arm's length price, the functional analysis concluded by the tax authorities was agreed to be "*arbitrary, unscientific and an opinion based on value judgment and not on a formula*"<sup>199</sup> by the courts.

A gap in the argument of the tax authorities was the justification of using the OECD TPG as an interpretative aid from the Zimbabwean domestic tax legislation. An argument presented by the tax authorities describing a potential erosion of the tax base on the fiscus of Zimbabwe to justify concluding that the transaction was not at arm's length was also an insufficient argument to place reliance on the OECD TPG. It is clear from the court's decision that "*international best practice*" (a term referred to by the tax authorities in the case) did not hold any hard law relevance in Zimbabwean local tax legislation at the time of the tax years of assessment since there was no way this practice could be used in domestic tax law. In terms of section 24 of the ITA at the time of the case, the OECD TPG had no legal basis to be used and the courts could not rule in favour of its use. The court considered that the OECD TPG should be disregarded regardless of the "*international best practice*". Zimbabwe is not a signatory to the VCLT<sup>200</sup> and could therefore offer an explanation to their stance to disregard the

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<sup>198</sup> Zimbabwe: High Court, 26 January 2018, Income Tax Appeal, Case No HH 99-18, C F (PVT) LTD v. Zimbabwe Revenue Authority, Case Law, TPcases.com. Refer to section, "Is it part of law?"

<sup>199</sup> C F ( PVT ) LTD v . Zimbabwe Revenue Authority, 2018.

<sup>200</sup> United Nations Treaty Collection, 'UN: Signatories to the Vienna Convention on the Law of Treaties, 23 May 1969 - Chapter XXIII: Law of Treaties'.

international customary legal practices to apply the OECD TPG as an interpretive aid to the ALP at the time. The court thus concluded that the tax authorities erred in the use of section 24 of the ITA.

#### 4.9.2. Zimbabwe transfer pricing domestic tax legislation

Zimbabwe's first TP legislation was introduced from 1 January 2014 where there was only an introduction to the term "arm's length principle" found in sections 23, 24 and 98 of the ITA.<sup>201</sup> Guidance to determine whether transactions are consistent with the ALP was later implemented from 1 January 2016 through schedule 35 of the Zimbabwean ITA.<sup>202</sup> Zimbabwe is not an OECD member country; however, in the introduction section of the 2020 "Zimbabwe Revenue Authority Transfer Pricing Practice Notes", it is noted that reliance can be found in the OECD TPG and UN Practice Manual on TP as a source of interpretation of the Zimbabwean TP rules in its domestic legislation.<sup>203</sup> The OECD TPG is explicitly mentioned in the Zimbabwean TP practice notes, regulations and in paragraph 13 of Schedule 35 of the ITA.<sup>204</sup> Since the CF (PVT) Ltd case, it can be inferred that including the OECD TPG in domestic tax regulations was done to protect the tax base of Zimbabwe so as to not preclude the use of the OECD TPG when applying the ALP.

#### 4.9.3. Zimbabwe: Observations of the OECD TPG in domestic tax legislation

The C F (PVT) Ltd case highlights the importance of providing guidance on the use of the OECD TPG as an interpretative aid when applying the ALP. It is evident, through the domestic tax legislation and relevant guidance issued by the Zimbabwean tax authorities, that both the OECD TPG and the UN Practical Manual on Transfer Pricing for Developing Countries are relevant sources of interpretation for the Zimbabwean TP rules. Section 98B and paragraph 13 of the 35<sup>th</sup> Schedule<sup>205</sup> of the Zimbabwean

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<sup>201</sup> Zimbabwe: R Manjowe, 'Zimbabwe - Corporate Taxation, Country Tax Guides', Country Tax Survey, IBFD. Refer to section 7.2, "Transfer Pricing".

<sup>202</sup> Zimbabwe: Income Tax Act, Chapter 23:06 (1 April 1967), National Legislation, Laws.Africa. Refer to section 98B and para. 13 of the 35<sup>th</sup> Schedule to the ITA.

<sup>203</sup> EY, 'EY Worldwide Transfer Pricing Reference Guide'; R Manjowe, 'Zimbabwe - Corporate Taxation, Country Tax Guides'; ZRA, 'Zimbabwe Revenue Authority: Transfer Pricing Notes', Country Surveys, IBFD. URL: <https://www.zimra.co.zw/downloads/category/44-transfer-pricing-documentation?download=613:zimra-transfer-pricing-practice-notes-05-03-2020>. Refer to para. 3 of the Zimbabwe Revenue Authority: Transfer Pricing notes, "Introduction", paragraph 3 where it is noted that section 98B as read with the 35<sup>th</sup> Schedule to the ITA (Chapter 23:06).

<sup>204</sup> Zimbabwe: Zimbabwe Revenue Authority, 'Zimbabwe Revenue Authority: Transfer Pricing Notes' (2020), Tax Authority's Documentation, Zimbabwe Revenue Authority, URL: <https://www.zimra.co.zw/downloads/category/44-transfer-pricing-documentation?download=613:zimra-transfer-pricing-practice-notes-05-03-2020>.

<sup>205</sup> Zimbabwe: Income Tax Act, 'Zimbabwe Income Tax Act - Chapter 23:06' (n.d.), para 13 of the 35<sup>th</sup> Schedule of the ITA, "Relevance of OECD Transfer Pricing Guidelines: The Organization for Economic Cooperation and Development (OECD) "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" and the UN Manual on the interpretation of transfer pricing are relevant sources of interpretation for this Schedule. There may also be other relevant sources such as the United Nations Practical Manual on Transfer Pricing for developing countries."

ITA, include a direct reference to the OECD TPG and UN Practice Manual on Transfer Pricing.<sup>206</sup> This stance is further reiterated in the Zimbabwe Revenue Authority: Transfer Pricing notes issued on 23 March 2020.<sup>207</sup>

The tax assessments in the C F (PVT) Ltd case, were for the period 2009 to 2012 which was well before the inclusion of the OECD TPG in the TP legislation in Zimbabwe domestic tax law and before the first TP legislation was effective. TP legislation in Zimbabwe only became effective in its domestic tax legislation from 1 January 2014. In the C F (PVT) Ltd case the influence of the OECD TPG had no bearing on the Zimbabwean court decision. The OECD TPG was unable to be used as an interpretive aid when applying the ALP to its domestic laws and regulations nor could it be used as an interpretative aid as persuasive evidence.

#### 4.10. Observations of the OECD TPG shaping domestic tax legislation within the sample of African countries

Countries such as Kenya, Nigeria, Zimbabwe and Zambia have enhanced their TP local laws and regulations to align them with that of the OECD TPG; however, in areas where the OECD TPG differ from domestic TP tax law, it is clearly mentioned that the local laws and regulations take precedence over the guidelines. The ambiguity expressed in the court rulings of these African jurisdictions created the need for more concise language in their domestic tax legislation to address an international meaning of the OECD TPG and is shown in their domestic TP legislation development over time.

The court cases revealed that the right for the tax authorities to trigger an adjustment is driven either through specific TP legislation in domestic law<sup>208</sup> or on the grounds of an alternative tax anti-avoidance provision indicating that there is reasonable belief by the tax authorities that the main purpose of the transaction was to reduce the tax liability and harm the tax base of the relevant jurisdiction<sup>209</sup>. Where reasonable grounds were established to trigger an adjustment to the TP cross border transaction, the decision presented to the courts was whether the transaction is recorded at arm's length in accordance with the local TP laws and regulations of the jurisdiction.

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<sup>206</sup> Zimbabwe: Zimbabwe Income Tax Act Chapter 23:06, 35<sup>th</sup> Schedule (para 3) (amended 2019), National Legislation, Laws.Africa, <https://zimlii.org/>

<sup>207</sup> Zimbabwe: Zimbabwe Revenue Authority, 'Zimbabwe Revenue Authority: Transfer Pricing Notes'. Refer to paragraph 3 of the introductory notes stating, "*Section 98B as read with the 35th Schedule to the Income Tax Act (Chapter 23:06) (The Act) broadly adopts the internationally accepted "Arm's Length Principle" for the purposes of determining the income and associated expenditure for transactions between associated persons. Accordingly, these Practice Notes have been drafted in a manner broadly consistent with the Arm's Length Principle as laid out in Article 9 of the ATAF, OECD and UN Model Tax Conventions on Income and Capital; and the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*".

<sup>208</sup> Zimbabwe: High Court, 26 January 2018, Income Tax Appeal, Case No HH 99-18, C F (PVT) LTD v. Zimbabwe Revenue Authority, Case Law, TPcases.com.

<sup>209</sup> Zambia: Supreme Court of Zambia, 20 May 2020, Case-24/2017: Mopani Copper Mines PLC v. Zambia Revenue Authority, Case Law, IBFD.

The Eastern Produce Malawi Limited case and the Unilever Kenya Limited case highlight two different outcomes on how the OECD TPG was used or rejected by the Malawi and Kenyan courts. In the Malawi case it was ruled that the OECD TPG should not be used to determine the arm's length price whereas in the Kenya case, the court ruled in favour of the use of the OECD TPG as an interpretative aid to apply the ALP. In the Unilever Kenya case, the taxpayer used the OECD TPG as a set of international best practices as an interpretative aid when applying the ALP to the transaction. The Malawi court ruled that the argument presented by the tax authorities applied the OECD TPG without any consideration of the domestic tax legislation. Furthermore, it is evident by the case that the Malawi tax authorities were unable to demonstrate how the use of the OECD TPG supported the application of the legislation resulting in the Malawi court to rule against the tax authorities use of the OECD TPG.

For years after the Malawi and Kenya cases, the OECD TPG has been built into its TP regulations in order for the revenue authorities and taxpayers to take heed of the OECD TPG. It is the responsibility of the court to evaluate if the OECD TPG is appropriately used by the revenue authorities in reaching their decision since there is now a clear path in the domestic TP regulations to allow such a consideration.

It is noted that there is a lack of cases that referenced the VCLT to allow the use of the OECD TPG as part of an interpretative aid in the cases observed. Instead, its use in some of the cases was merely through the court deciding that it is international best practice<sup>210</sup> to utilise the OECD TPG without any detail provided on how it presented itself as an application in domestic tax law. The exception is the IT 14305 ABC (Pty) Ltd v SARS (South African case) where a local case<sup>211</sup> was cited to explain the process of interpretation that is similar to the reasoning embodied in Article 31 of the VCLT where it is noted, "*consideration must be given to the language used in the light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production*".<sup>212</sup> This argument led to the court deciding to place reliance on the use of the OECD TPG as an interpretative aid to determine the arm's length price.

The court cases observed, identifies situations where the OECD TPG was absent from the local regulations and domestic tax legislation when determining the arm's length price. The OECD TPG status in the cases above are only used as an interpretative aid in the court proceedings where

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<sup>210</sup> Reference to the Unilever Kenya case where Judge Alnashir Viram noted, "*We live in what is now referred to as a "global village". We cannot overlook or side-line what has come out of the wisdom of taxpayers and tax collectors in other countries. And especially because of the absence of any such guidelines in Kenya, we must look elsewhere. We must be prepared to innovate, and to apply creative solutions based on lessons and best practices available to us. That is indeed how our law will develop and our jurisprudence will be enhanced.*"

<sup>211</sup> South Africa: High Court, 8 May 2018, Case No. 14179/2017: Crookes Brothers Limited and The Commissioner of the South African Revenue Services (2017), Case Law, TPcases.com.

<sup>212</sup> BAM, ZA: ABC (Pty) Ltd v. Commissioner for the South African Revenue Service, 7 January 2021 (Decision), Case No: I.

appropriately argued in conjunction with domestic tax law to justify how the ALP was applied at the time. This is a common trend observed in each of the cases. The cases where the OECD TPG were successfully considered as an interpretive aid to the ALP of the domestic ITA were the Unilever Kenya case, Nestlé Zambia case, Prime Plasticchem Nigerian case and the ABC (Pty) Ltd (IT14305) South African case.

The South African case, ABC (Pty) Ltd (IT14305), the court ruled in favour of the respondent to allow the use of the OECD TPG to apply the ALP as part of the domestic tax legislation. Despite South Africa only holding an observer status of the OECD and a member of the OECD/G20 Inclusive Framework on BEPS, the court held that South Africa's economic status as the "*...Gateway for investment into Africa*", its member status of the OECD BEPS Committee and the only African country as a member of the G20 all contributed to South Africa's need to "*...align itself with the OECD standards or regulations relating to Transfer Pricing...*".<sup>213</sup>

Apart from the court decisions observed in these cases, at the time of the court rulings allowing the use of the OECD TPG to apply the ALP (in South Africa, Nigeria, Kenya and Zambia), the development to include references to the OECD TPG as part of the domestic tax rules and regulations have become pervasive. The cases reveal that the OECD TPG are a focus of inclusion in the prescriptive text of the local TP regulations especially in years after the court judgments where the tax authorities were ruled against its use of the OECD TPG.

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<sup>213</sup> Ibid.

## Chapter 5: Conclusion

The research conducted in this dissertation addresses whether there is a discernible pattern where the OECD TPG, through Article 9 of the OECD MTC, as a soft law instrument, is significant in the international court judgments in a legislative environment that has developed or in the process of developing TP domestic tax legislation or TP regulations in the sample of countries in Africa. Where the OECD TPG was considered by the courts in their judgments, it was further determined whether the outcome of the court case in the sample of African countries, namely, Ghana, Kenya, Malawi, Nigeria, South Africa, Tanzania, Uganda, Zambia and Zimbabwe has moulded TP regulations and influenced later court decisions in relation to the ALP. The weighting of the OECD TPG in the court judgments as an authoritative statement was analysed amongst the sample of international court rulings. Based on the sample of TP cases inspected, it is found that where clarity is required to interpret the ALP, the domestic TP rules and regulations may be insufficient to interpret the ALP. On this basis an international best practice may be sought through the OECD TPG.

The results in Chapter 3 reveal that in order for the OECD TPG to be considered in a court ruling, a link to the domestic tax legislation, regulation or international customary law practices should exist in that jurisdiction. The OECD TPG cannot be considered by the courts in isolation and where the ALP cannot be applied in domestic tax legislative text, the OECD TPG can be referred to as a useful interpretative tool if applied correctly in terms of their domestic legal practices. In the cases presented in Chapter 4, instances arose in the court judgment that the OECD TPG can be relied upon when the current domestic legislative environment or local TP regulations (if any for the tax years of assessment in the court judgment) does not cater for the type of TP transaction. This is shown in the Unilever Kenya case,<sup>214</sup> Nestlé Zambia case,<sup>215</sup> Prime Plastiche Nigerian case,<sup>216</sup> and IT14305 South African case<sup>217</sup> where the OECD TPG is considered during a time when the OECD TPG was not specified in any regulation or hard law prescriptive text. In the Eastern Produce Malawi Limited Malawi case, however, the Malawi court rejected the tax authority's argument for the use of the OECD TPG to aid in the interpretation of the ALP because there was no argument that allowed its use at a time when the OECD TPG was not found in any TP regulation for the tax years of assessment.

It is observed that in instances where the court ruled against the tax authorities for its incorrect use of the OECD TPG as an interpretative aid when applying the ALP, there was an insufficient link between the use of the OECD TPG and how it is applied in the domestic legislative framework. This is especially observed in the Malawi case, where the outcome could have been different if an argument was presented to the court to indicate the use of customary international law through Article 31 of the VCLT (to which

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<sup>214</sup> Refer to chapter 4.4.1

<sup>215</sup> Refer to chapter 4.8.1

<sup>216</sup> Refer to chapter 4.6.1

<sup>217</sup> Refer to chapter 4.7.2

Malawi is a signatory) to use the OECD TPG as a soft law instrument when applying the meaning of the ALP in terms of the Malawi ITA. Even in instances where the court ruled in favour of the use of the OECD TPG (e.g. Unilever Kenya and Nestlé Zambia cases above), the arguments presented to the respective courts did not mention a consideration for the use of the Article 31 of the VCLT to justify the status of the OECD TPG as an international best practice. In the absence of the discussion of Article 31 of the VCLT in the court judgments, it is difficult to ascertain whether the use of Article 31 of VCLT was the basis of the court judgments to include the OECD TPG as part of the meaning of international best practices or if it is merely implied for countries that are signatories to the VCLT.

The cases observed in Chapter 4 either did not mention the OECD TPG, and in a limited number of cases where it was mentioned, the court ruled against its use (e.g. Eastern Produce Malawi Limited case and the Zimbabwean CF (Pvt) Ltd case). In the cases where it was favourably mentioned, there is a regulatory link through the TP regulations to facilitate the reference to the OECD TPG (e.g. the Prime Plastics Nigeria case) or use of customary international law to allow its use as an international best practice to apply the ALP noted in the respective domestic tax legislation (e.g. the Nestlé Zambia case, Unilever Kenya case and South African IT14305 case). Therefore, there is no common trend amongst these African countries to conclude that the OECD TPG holds an influential status in all cases observed in the sample selected. For years after the case judgments, however, the OECD TPG inclusion in the local TP regulations and local tax authorities practice notes is clearly prevalent. It is evident that after the court judgments influenced regulatory reform amongst these African countries to force reference to the OECD TPGs rather than a clear indication that the OECD TPG is favoured by all African countries in this sample to trigger reform.

For years after the assessment in instances where the courts did not rule in favour of the use of the OECD TPG as an interpretative aid as a soft law instrument, the tax administrators eventually included a direct reference to the OECD TPG as part of the local TP regulations to provide a way of using the OECD TPG as an interpretative aid to apply the ALP. The amendments found in the TP legislative framework in Zimbabwe is the only observation made where the actual domestic tax legislation in terms of paragraph 13 of the 35<sup>th</sup> Schedule makes a direct reference to the use of the OECD TPG (and UN Practical Manual on Transfer Pricing) as an interpretative tool when applying the ALP envisaged in section 98B of the Zimbabwean ITA.<sup>218</sup> The decision to adopt the OECD TPG is a decision that is not taken lightly because of their economic status (such as South Africa as the gateway for investment into Africa) as it requires an understanding of the unique operating environment of the individual fiscus and its unique challenges causing erosion of its tax base.

Chapter 4 reveals that the OECD TPG status amongst a sample of African countries clearly demonstrates that the OECD TPG has permeated its way into the respective domestic TP regulations

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<sup>218</sup> Refer to chapter 4.9.3.

(with the exception of Zimbabwe, where a reform to include the OECD TPG is also found in the domestic tax legislation) such that it allows a clear mechanism for use by tax authorities and the taxpayers when applying the ALP. The case decisions (particularly where these have not been in favour of the revenue authorities in the African countries) led to an update of domestic tax legislation and regulation to ensure that the OECD TPG is included in the domestic tax legislative framework. The references to the ALP in the various African TP laws and regulations, and particularly the approach in practice, suggests that the OECD TPG has influenced the African transfer pricing regimes in the sample of African countries inspected in this dissertation.

In conclusion, it is evident that the OECD TPG as a soft law instrument has influenced the reform of domestic TP regulations within this sample of African countries in this study as opposed to the hard law domestic tax legislation. Where TP regulations have been developed to include the OECD TPG, reform by the tax authorities were driven after unfavourable court judgments were issued against the tax authorities. It is inferred that this reform was done to reduce any potential arguments against the right to use the OECD TPG as an interpretive tool when applying the ALP. It is found that where the domestic TP tax legislation does not give clear guidance on how to apply the ALP, the OECD TPG does hold its status as an influential interpretive aid when applying the ALP in the sample of African countries studied; albeit mostly through TP regulations as opposed to the hard law domestic tax legislation of the relevant African state.

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## Appendices

Appendix 1: Comparison of “Associated Enterprise” Article in the 2017 OECD, 2017 UN and 2019 ATAF MTC



(Appendix 1 &2)  
Extract OECD UN and

Appendix 2: Article 9 of the OECD MTC from 1963-2017



(Appendix 1 &2)  
Extract OECD UN and

Appendix 3: Full data set of results



Appendix 3\_ Full data  
set of results.xlsx