

Base Erosion And Profit Shifting In Africa: Reforms to Facilitate Improved Taxation of Multinational Enterprises



United Nations
Economic Commission for Africa

Base erosion and profit shifting in Africa: reforms to facilitate improved taxation of multinational enterprises



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Abbreviation

AfDB	African Development Bank
ATAF	African Tax Administration Forum
BRICS	Brazil, Russian Federation, India, China and South Africa
CEMAC	Central African Economic and Monetary Community
ECA	Economic Commission for Africa
ECOSOC	Economic and Social Council
FDI	Foreign Direct Investment
FfDO	Financing for Development Office
GDP	Gross Domestic Product
GFI	Global Financial Integrity
ICT	Information and Communications Technology
IMF	International Monetary Fund
KPMG	Klynveld Peat Marwick Goerdeler
NGOs	Non-Governmental Organisations
OECD	Organization for Economic Cooperation and Development
SADC	Southern African Development Community
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nation Development Project
URT	United Republic of Tanzania
VAT	Value Added Tax

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Executive summary

Increased domestic resource mobilization is central to achieving structural transformation in Africa which is in turn essential to addressing social and economic challenges on the continent, such as poverty, inequality and unemployment. . Most African countries, however, face major challenges in mobilising domestic resources for development. Most of these challenges are a direct result of poor governance, insufficient public investment, corruption and deflationary and externally imposed monetary and fiscal policies that promote systems that have failed to transform African countries. There are also challenges regarding underdeveloped tax laws, the low enforcement of tax laws and general administrative weakness.

Although there is a paucity of research on the linkages and transmissions of illicit financial flows from Africa, there has been much discussion about the meaning of such flows. The present report takes the position that addressing base erosion and profit shifting should be considered as part of the broad agenda to curtail illicit financial flows. Owing to the lack of data and transparency in reporting by multinational enterprises, the exact scale of corporate tax avoidance in Africa remains difficult to establish. Nevertheless, studies have shown that base erosion and profit shifting practices in Africa are prevalent. This entails having multinational enterprises exploit unsynchronized tax rules that have not kept pace with modern business models to erode countries' tax bases and shift profits to low-tax jurisdictions. The result is reduced government tax revenue and a critical underfunding of public investment and infrastructure that could help to promote economic growth. Given that African countries rely heavily on corporate income tax, in particular from multinational enterprises, curtailing base erosion and profit shifting practices has the potential to increase taxes paid by these enterprises, enhancing domestic resource mobilization.

In 2013, the Organization for Economic Cooperation and Development (OECD) launched an action plan to address base erosion and profit shifting, which culminated in a package of 15 actions, which was issued in 2015. OECD is of the view that, if implemented, the measures will better align the location of taxable profits with the location of economic activities and value creation and improve the information available to tax authorities to apply their tax laws effectively. The measures are designed to be implemented domestically and through double tax agreement provisions in a coordinated manner, supported by targeted monitoring and greater transparency. The work of OECD on base erosion and profit shifting was carried out by OECD member countries and base erosion and profit shifting associate countries (eight Group of 20 countries that are non-OECD countries). The work reflects consensus among these countries on solutions to eliminate base erosion and profit shifting issues that concern primarily this group of countries. The only African country that is part of the Group of 20 countries and one of the base erosion and profit shifting associate countries is South Africa.

Although OECD indicated that it would take into account the perspectives of developing countries, the interests of developing countries (aside from the few that participated in the process) were never taken into consideration when the base erosion and profit shifting agenda was developed. The base erosion and profit shifting action plan has therefore been criticized for lacking focus on or understanding the specific needs of the vast majority of developing countries. Nevertheless, some African countries have been vocal in their consultations on base erosion and profit shifting issues that are of greatest concern to them. For decades, African countries have been victims of base erosion and profit shifting not only by multinational enterprises that have invested in the continent, but also by African country residents who have shifted money to developed countries and tax haven jurisdictions. Even though African countries are not bound to follow the OECD recommendations, all countries (including African economies) have a shared interest in strengthening the integrity of

the international corporate tax system. The base erosion and profit shifting measures pertaining to information exchange will, for example, be instrumental in curtailing illicit financial flows that are a by-product of many aggressive tax avoidance schemes, and ensure better tax collection. African countries should therefore make use of the current international political will to address base erosion and profit shifting to implement previously lacking legislation, to review the effectiveness of current tax laws and to strengthen collaboration with regional organizations with a view to adopting a common position outlining their priorities as regards to base erosion and profit shifting.

The 15 actions to curtail base erosion and profit shifting deal with different dimensions of the international tax planning practices of multinational enterprises. These dimensions could affect countries in different ways, depending on whether the country is predominantly capital-importing or capital-exporting. For predominately capital-importing countries (most African countries), the priority base erosion and profit shifting action items are those that protect the erosion of their right to tax income derived from within their geographic boundaries, given that most of them do not have the administrative ability to tax worldwide income. Given that double tax treaties, in general, restrict the rights of host countries to tax corporate income at the source, capital-importing developing countries are also systematically disadvantaged from a treaty context. Nevertheless, the priorities of any particular country will depend on its socioeconomic and geopolitical circumstances, its economic development and its administrative capacity.

The 15 actions are divided into four major implementation categories that OECD recommends. These are: (a) minimum standards; (b) common practices and best practices for domestic law; (c) international standards; and (d) analytical reports (all explained below). The study examines the base erosion and profit shifting measures in each action under the relevant category, and some insight is given regarding what the response of African countries should be regarding the same. Some African countries have begun to reflect on and to implement some of OECD's base erosion and profit shifting recommendations. Countries should first take stock of the effectiveness of their current legislation so as to determine to what base erosion and profit shifting measures need to be introduced. Countries that face funding and administrative constraints in implementing the measures may have to seek assistance to devise tailored approaches to address their specific concerns. There are, however, other countries that have chosen to remain unengaged with the base erosion and profit shifting measures, choosing either a wait-and-see approach or even working on their own independent set of reforms to best counter base erosion and profit shifting using alternative approaches. In any case, for countries that do decide to adopt measures on base erosion and profit shifting, it will be important for to consider how the country's other economic and fiscal policies may need to change alongside measures to tackle base erosion and profit shifting, so that such measures do not undermine the country's broader economic development objectives.

Three African country case studies are set out in the report (Cameroon, South Africa and United Republic of Tanzania) to gauge the impact of base erosion and profit shifting on their economies, the measures that they have in place to curtail base erosion and profit shifting and to what extent they have adopted any of the OECD base erosion and profit shifting measures that are of priority to them. The case study on the United Republic of Tanzania outlines some of the key issues faced by tax administrations in a resource-rich country, which has leveraged legal instruments to address base erosion and profit shifting, while reviewing inefficient tax exemptions. Given that the United Republic of Tanzania had limited involvement in the base erosion and profit shifting package consultations, it provides a strong case for prioritizing improvements in the overall tax administrations as a precursor to adopting base erosion and profit shifting-specific interventions. The case study on Cameroon highlights a more focused approach to tackling base erosion and profit shifting, for example, through allocating resources and capacity to the establishment of a transfer pricing unit. As a member of the Group of 20, South Africa was involved in the development of the base erosion and profit shifting

package. It, however, faces unique circumstances with regard to how it adopts the package. It has to balance preserving the competitiveness of its own multinational enterprises as they invest offshore and in the African continent, and at the same time protecting its tax base from erosion by foreign investors without hampering foreign investment.

Notwithstanding the above, the OECD approach to addressing base erosion and profit shifting has also been criticized for not addressing basic fundamental principles of the international tax system that are pivotal in addressing base erosion and profit shifting. Owing to the short time frame of the base erosion and profit shifting project (two years), there was insufficient analysis of all relevant issues. In addition, as a result of the fact that the base erosion and profit shifting project was orchestrated by developed countries, it has undermined the focus on base erosion and profit shifting issues that are of priority concern to developing countries. This report therefore considers other alternative approaches and policy recommendations that African countries can consider to comprehensively address these challenges. This includes not only the OECD base erosion and profit shifting measures, but also other alternative measures. ECA is of the view that addressing base erosion and profit shifting and related illicit financial flows in Africa should be about not only strengthening anti-tax avoidance laws, but also advancing the principle of “common but differentiated responsibility”, which recognizes that, although all States may participate in international response measures aimed at addressing international problems, there should be differing approaches and obligations on States that recognize the historical differences in developed and developing States and differences between their relevant economic and technical capacities to tackle these problems. This implies that finding solutions to base erosion and profit shifting and illicit financial flows, which are pertinent to Africa, will require customized African solutions to African problems.

Addressing base erosion and profit shifting in Africa will require that countries consider some “low hanging fruit” that can be reaped in the short term and that can ensure a relatively swift and positive

impact on domestic resource mobilization. This will require political will from Governments to set aside funds to build administrative capacity, close domestic tax loopholes, build knowledge capacity in international tax matters, build tax treaty negotiating capacity, coordinate ministries and agencies dealing with tax treaty issues, improve access to data, address harmful tax practices emanating from non-strategic tax incentives and strengthen regional tax coordination and cooperation of African tax authorities.

Alternative measures to curtail base erosion and profit shifting issues and related illicit financial flows have also been suggested by other organizations. For example, the United Nations has stressed that efforts in international tax cooperation should fully take into account the various needs and capacities of all countries, in particular the least developed countries, landlocked developing countries, small island developing States and African countries. It recognizes the need for technical assistance for developing countries through multilateral, regional, bilateral and South-South cooperation, based on the different needs of countries. The 2015 United Nations handbook on selected issues in protecting the tax base of developing countries is therefore an alternative resource for African countries to consider because it addresses base erosion and profit shifting issues from a developing country perspective. It would also be in the interest of African countries to sign tax treaties that are based on the United Nations Model Tax Convention on Income and on Capital, which favours capital-importing countries over capital-exporting countries in that it, in general, imposes fewer restrictions on the tax jurisdiction of source countries through, for example, its definition of the permanent establishment concept. The United Nations new service fees article will be instrumental in curtailing base erosion and profit shifting concerns regarding service fees, a matter not addressed in the OECD base erosion and profit shifting project. Other organizations, such as the African Tax Administration Forum, have also noted that, notwithstanding the OECD base erosion and profit shifting process, Africa must devise customized solutions to protect its own tax base, with a customised approach to assist

African countries and groups of countries in similar positions to ensure domestic resource mobilization. Various academics have also suggested alternative approaches to address some base erosion and profit shifting issues. For example, whereas the OECD base erosion and profit shifting measures appear to indicate that the “arm’s-length principle” is the panacea of most base erosion and profit shifting concerns, many academics have called upon the international community to consider the use of the “unitary taxation” and “formulary apportionment”, the pros and cons of which are addressed in this report. Perhaps one of the strongest measures that came out of the base erosion and profit shifting project is the requirement for multinational enterprises to submit country-by-country reports of their global allocation of the income, economic activity and taxes paid among countries according to a common template. The OECD approach is that these reports will be availed only to tax administrations. However, non-governmental organizations (NGOs) contend that this approach will not curtail the malfeasance that it is intended to address.

Their alternative approach (the pros and cons of which are addressed in this report) is that country-by-country reports should be made public, given that doing so would enable national tax authorities to gain access to them easily and would ensure fiscal transparency and bring an end to secretive tax haven transactions. To ensure that all countries’ interests are protected, developing countries, a number of researchers and NGOs have suggested the establishment of a global tax body to drive the reform of international tax rules, instead of OECD, which does not effectively represent the interests and views of developing countries. Suggestions have been made that such a global tax authority should be established under the auspices of the United Nations and would function as a neutral and inclusive norm-setting body for international tax cooperation at the intergovernmental level, working together with regional groupings such as the African Tax Administration Forum. In the report of the high-level panel on illicit financial flows from Africa an alternative approach to curtailing illicit financial flows and related base erosion and profit shifting activities is set out,

and it is discussed in this report (African Union and Economic Commission for Africa, 2015).

In the light of the above, the key legal, political and technical recommendations that should be implemented at the national or regional levels in the short term and long term are highlighted in this report. The rationale is that, given that the economic and administrative levels of development differ between African countries, the short-term recommendations are a crucial first step for all countries on the continent. Countries that have already implemented these short-term recommendations should look into implementing the long-term recommendations. In addition, all countries should continue to strategize on the long-term recommendations by reflecting periodically on their progress in the short and medium term.

Section 1: Introduction

The success in implementing the 2030 Agenda for Sustainable Development and the African Union's Agenda 2063 depends heavily on the ability of African countries to generate and mobilize public resources for universal public service provision and , public and private investment and to provide buffers to protect their economies during global downturns. This was reaffirmed in the Addis Ababa Action Agenda of the Third International Conference on Financing for Development (United Nations, General Assembly, 2015a) and the African Union High-level Panel on Illicit Financial Flows from Africa (African Union and Economic Commission for Africa, 2015). Although African countries have witnessed an increase in government revenue since the year 2000, these have been dominated largely by resource rents that are quite volatile and influenced heavily by fluctuations in international commodity prices (African Development Bank, 2015). This highlights the urgent need for stable and reliable means of domestic revenue mobilization to fund Africa's development. With the emergence of the Sustainable Development Goals (United Nations, General Assembly, 2015b), the need to address their realization has intensified, and African Governments have acknowledged the significant shortfall in resources. In the Common African Position on the post-2015 Development Agenda and in preparation for the Addis Ababa Action Agenda, African countries placed domestic revenue mobilization at the centre of establishing an enabling framework to ensure the successful achievements of the Goals, which include ensuring financial deepening and inclusion; strengthening tax structures, coverage and administration; improving fairness, transparency, efficiency and effectiveness of tax systems; and

curtailing illicit financial flows in order to build fiscal legitimacy (Waris, 2013).

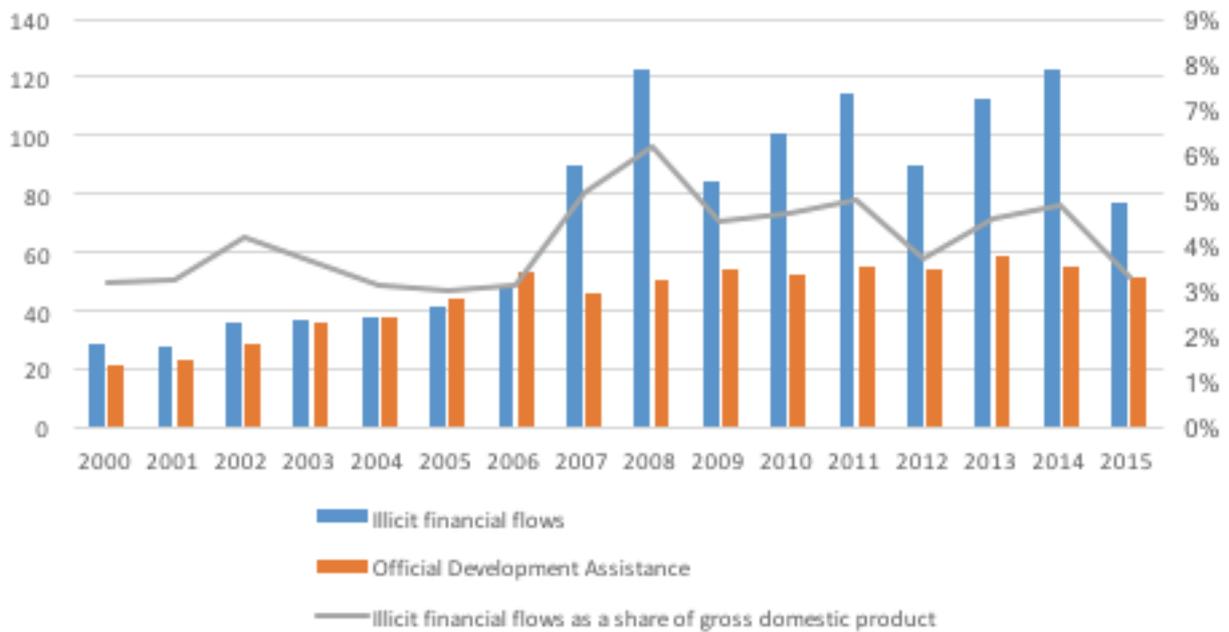
In the report of the High-Level Panel on Illicit Financial Flows from Africa (African Union and Economic Commission for Africa, 2015), it was estimated that Africa was losing more than \$50 billion annually as a result of illicit financial flows. The report presented the colossal scale on which commercial entities are hiding wealth, evading taxes, avoiding taxes by engaging in aggressive tax planning and dodging customs duties and domestic levies. In this context, figure I (based on a methodology that has been updated since the report) shows that, between 2000 and 2015, net illicit financial outflows between Africa and the rest of the world averaged \$73 billion annually (at 2016 prices), which is significantly higher than the average level annual official development assistance that Africa received during the same period.¹ These losses amount to more than 4 per cent of the continent's gross domestic product (GDP) on average during the period. The African Development Bank (2010) attributes major losses of public revenue in the extractive sector to the inefficient taxation of extractive activities and the inability to fight abuses of transfer pricing by multinational enterprises.

It is thus of little wonder that illicit financial flows out of Africa are becoming an increasing concern, given the scale and negative impact of such flows on Africa's development and governance agenda. More broadly, it is estimated that, for every dollar that goes to the developing world in aid, almost 10 dollars leave the developing world for developed countries through illicit means (Froburg and Waris, 2010). However, this is an estimate and may well be far from the

¹ These estimates are significantly higher than those included in the High-level Panel report or those recently produced by Global Financial Integrity Spanjers and Salomon, (2017). Global Financial Integrity reports on illicit financial flows on a gross basis. its estimates of the component of illicit financial flows that occurs through trade re-invoicing are estimated using the following procedure, for a given country (call it X) in a given year, Global Financial Integrity's estimates of illicit financial flows through trade re-invoicing first estimate the net illicit financial flow through this channel with each partner country. All of the instances where a net outflow occurs are then added together to produce an estimate of the gross outflow from country X; an analogous procedure is used to estimate gross illicit inflows through this channel. But it is clear that this procedure underestimates the gross flows, because of the netting that occurs in the estimates of flows between pairs of countries that are then added to form the overall estimate. . See Spanjers and Salomon (2017) for details. ECA's methodology estimates net illicit financial flows through trade re-invoicing also uses a more sophisticated procedure outlined in Mevel and others (2014) for adjusting for the costs of insurance and freight and other legitimate differences between export statistics and the corresponding "mirror" import statistics. The figures are higher than the ECA estimates reported in the High-level Panel report for the same period because revisions to the underlying databases have caused the estimates to be revised upward and because the methodology was improved to use a more sophisticated adjustment for the transit time of shipments.

Figure I: Estimates of illicit financial outflows between Africa and the rest of the world (through trade re-invoicing only) and official development assistance to Africa, 2000 to 2015

(Billions of United States dollar (2016 prices) and as percentage of GDP)



Source: ECA calculations based on Mevel (2017), OECD (2017), Illicit Financial Flows: Illicit Trade and Development Challenges in West Africa and United States of America, Bureau of Labor Statistics (2017).

reality, given that accurate data do not exist for all transactions and for all African countries. In fact, conservative estimates have shown that, without Illicit financial flows from the continent, Africa's GDP would have been at least 16 per cent higher (this is higher than the estimates of illicit financial flows presented in figure I because it takes into account multiplier effects that would result if the funds were restored) (African Union and Economic Commission for Africa, 2015).

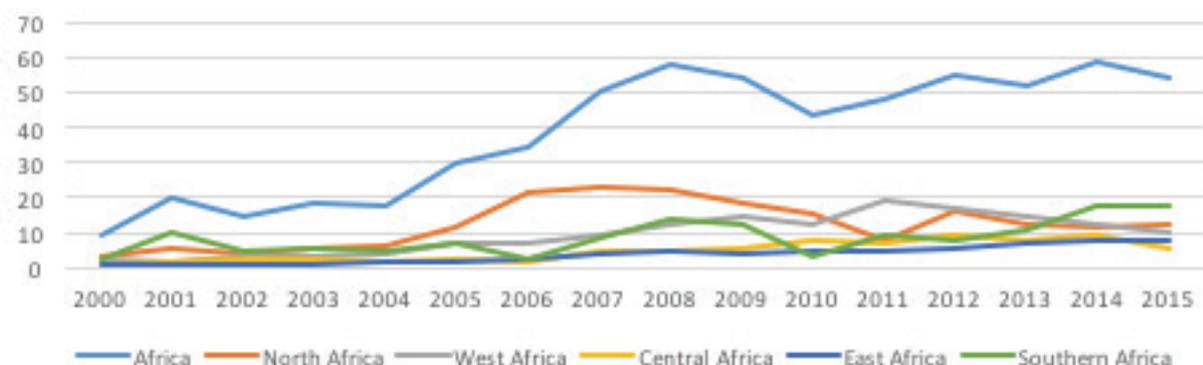
Alongside these developments, there also exists an international tax framework that undermines domestic resource mobilization by facilitating the exploitation of unsynchronized tax rules by powerful multinational enterprises that deny countries much-needed tax revenue. In the United Nations Conference on Trade and Development (UNCTAD), World Investment Report 2016, it is indicated that, with a positive trend since 2000, foreign direct investment (FDI) inflows to Africa reached \$58 billion in 2014. Although FDI flows to Africa (excluding North Africa) fell to \$54 billion in 2015, a decrease of 7 per cent compared with 2014, especially in natural-resource-based economies in West

and Central Africa (see figures II and III), North Africa's FDI flows rose by 9 per cent, to \$12.6 billion, in 2015, boosted by investment in Egypt, where FDI flows increased by 49 per cent, to \$6.9 billion, driven mainly by the expansion of foreign affiliates in the financial industry and pharmaceuticals.

Figure III indicates that even non-resource-rich countries have received increased FDI, accounting for an estimated 37 per cent of Africa's foreign direct investment in 2015, compared with 30 per cent in 2010. Several countries without significant resources are attracting investors, including Kenya, the United Republic of Tanzania and Uganda, reflecting the shift towards consumer goods. Kenya is becoming an East African business hub for manufacturing, transport, services and information and communications technology (ICT). The ability of multinational enterprises, however, to contribute to domestic resource mobilization is hampered by the fact that they often become involved in tax-avoidance schemes that erode the tax bases of the countries in which transact, while shifting

Figure II: Foreign direct investment inflows to Africa, 2000-2015

(Billions of United States dollars)



Source: United Nations Conference on Trade and Development FDI statistics database (www.unctad.org/fdistatistics).

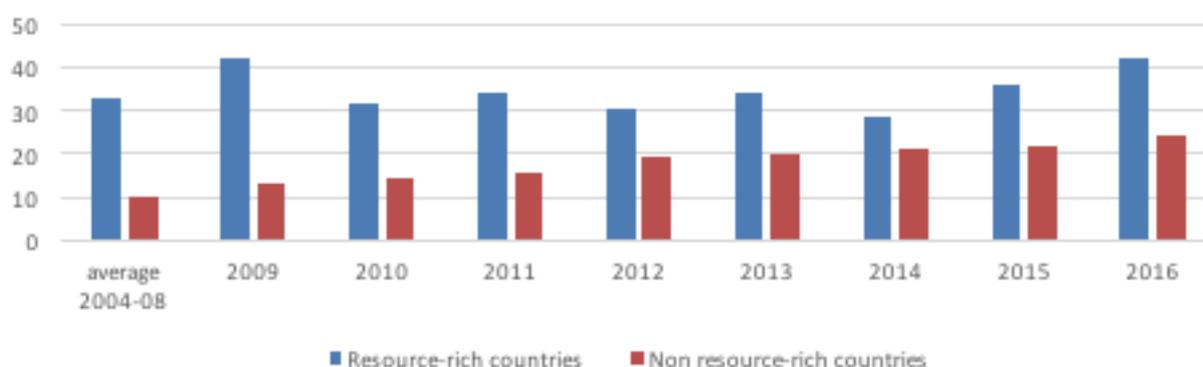
profits to low-tax jurisdictions (African Union and Economic Commission for Africa, 2015).

Given the increasingly globalized economy, ensuring that multinational enterprises honour their tax liabilities is an area that many African Governments are struggling with owing to the low capacity to monitor and address tax evasion and avoidance (African Union and Economic Commission for Africa, 2015). Given the lack of data and transparency in reporting by multinational enterprises, however, the exact scale of corporate tax avoidance in Africa remains difficult to establish. Data from 37 African countries estimate an average of 1.82 per cent

of GDP, compared with an average of 2.9 per cent for OECD countries in 2010 (Organization for Economic Cooperation and Development, African Tax Administration Forum and African Union, 2016). Limited evidence suggests that the long-run public revenue loss for developing countries is more than three times greater than in advanced economies, even though developing countries, in general, have lower levels of tax revenue and face limited alternatives to generating tax revenue (Crivelli and others, 2015). According to the most recent data from the International Monetary Fund (IMF), the tax revenue to GDP ratio in developing countries is approximately 19 per cent, compared with 26

Figure III: Foreign direct investment to Africa: resource-rich versus non-resource-rich countries, 2000-2016

(Billions of United States dollars)



Source: African Development Bank, Organization for Economic Cooperation and Development and United Nations Development Programme (2016).

per cent in advanced economies (according to the IMF country classification).²

Given that developing countries, including those in Africa, rely heavily on corporate income tax, in particular from multinational enterprises, curtailing tax avoidance is of significant importance because it erodes the already limited tax base in developing countries (Durst, 2014). This matter is of paramount importance, given that Africa's rising middle class and the unprecedented population growth that will continue to present an increasingly attractive market for multinational enterprises in the consumer goods market (KPMG, 2014). Consequently, if African countries do not curtail corporate tax avoidance, the losses of potential tax revenue that could be used for development will continue to rise. A study by Dalberg, commissioned by the Open Society Initiative for West Africa (Dalberg, 2015), estimated that West African States lost approximately \$3 billion in tax revenue in 2011 alone owing to transfer mispricing schemes by multinational enterprises. Dalberg projected that those losses would reach \$14 billion in 2018 if current trends continue. In addition to the above, UNCTAD indicated that just one tax avoidance scheme used by multinational enterprises cost developing countries around \$100 billion annually in lost revenue. UNCTAD estimates that revenue losses for developing countries due to multinational enterprises shifting profits to low-tax jurisdictions ranged from \$66 billion to \$122 billion in 2012 (United Nations Conference on Trade and Development, 2015). IMF estimated that the spill-over effects of profit-shifting resulted in an average revenue loss in developing countries included in the sample was 5 per cent of current corporate income tax revenue in all sampled developing countries, but that the corresponding figure for non-OECD countries was almost 13 per cent (International Monetary Fund, 2014b).

As African countries kick-start their efforts to achieve the Sustainable Development Goals and the goals contained in Agenda 2063, the impediments to domestic resource mobilization

need to be continuously re-examined. Huge campaign efforts by international non-governmental organisations (NGOs), such as the Tax Justice Network, Action Aid and Christian Aid, and by the United Nations have raised considerable global awareness of tax avoidance. Indeed, after the global financial crisis of 2008-2009 (McKibbin, 2010), NGOs voiced public concern about companies paying little or no corporation tax in the countries in which they do business. Consequently, at the 2012 Group of 20 Summit, national leaders explicitly referred to preventing base erosion and profit shifting, calling upon OECD to address the matter. In 2013, OECD launched an action plan on base erosion and profit shifting, which culminated in the package of 15 actions to address it, which was issued in 2015 (Organization for Economic Cooperation and Development, 2013a and 2013b).

Objectives of the study

OECD takes the view that, if implemented, the Base Erosion and Profit Shifting Actions will better align the location of taxable profits with the location of economic activities and value creation and improve the information available to tax authorities to apply their tax laws effectively. While many developing countries are now trying to implement these measures, they are faced with not only the original impediments to curtailing tax avoidance and evasion, but also additional administrative impediments, as well as policy and regulation impediments, all of which pose challenges to implementing the base erosion and profit shifting package. Only 17 of the 54 African countries were actively engaged in deliberations pertaining to the OECD base erosion and profit shifting project and only 10 were able to find funding to attend negotiations as recently as the middle of March 2017. The focus of this study on base erosion and profit shifting in Africa and reforms to facilitate the improved taxation of multinational corporations is therefore appropriate and timely for a number of reasons. First, political and public pressure has been a catalyst for intervention, which could

² ECA's calculations based on the International Monetary Fund's government finance statistics (<http://data.imf.org/?sk=E86E9088-3830-4CA3-B240-1B0EC5E15221>).

drive reform at the global level. This momentum is rare and should be leveraged by developing countries to ensure that they can pursue reforms with the support of the international community. Second, given that countries around the world are considering the actions that they need to implement in order to curtail base erosion and profit shifting, African countries that rely heavily on corporate tax as a means of domestic resource mobilization and whose tax bases are heavily affected by base erosion and profit shifting (Oguttu, 2015a) should take advantage of the initiatives and commitments from international organizations to support developing countries in funding capacity development (Organization for Economic Cooperation and Development, 2014). Lastly, given that the OECD project does not specifically focus on base erosion and profit shifting in developing countries, this report offers alternatives approach and policy recommendations that African countries can consider in curtailing base erosion and profit shifting issues that are pertinent to them.

Country case studies

This report also covers case studies on pertinent base erosion and profit shifting and related Illicit financial flows issues in Cameroon, South Africa and the United Republic of Tanzania to provide insight into how African countries are managing the taxation of multinational enterprises. The case studies are aimed at contrasting practical observations to the applicability of the proposals set forth in the base erosion and profit shifting package, in particular those pertaining to priority areas of African countries.

The case study on the United Republic of Tanzania, in East Africa, outlines some of the key issues faced by tax administrations in a resource-rich country, which has leveraged legal instruments to address base erosion and profit shifting, while reviewing inefficient tax exemptions. Information gained from fieldwork strongly suggests that it will be important to improve tax administration before adopting base erosion and profit shifting-specific interventions.

The case study on Cameroon, a bilingual (English and French speaking) country in Central Africa

highlights a more focused and well-prepared approach to tackling base erosion and profit shifting, for example, through allocating resources and capacity to the establishment of a transfer pricing unit. As a member of various forums relating to taxation, Cameroon has been proactive in identifying and filling gaps, such as preparing a manual on information exchange upon request and seeking transfer pricing advisory assistance.

The case study on South Africa portrays the most sophisticated tax administration on the continent. As a member of the Group of 20, it was involved in the development of the base erosion and profit shifting package. In contrast to other Group of 20 countries, it is an emerging economy that faces specific circumstances with regard to how it adopts the package. It has to balance preserving the competitiveness of its own multinational enterprises as they invest offshore and in the African continent, while protecting its tax base from erosion by foreign investors without hampering foreign investment. The case study offers a good example for other countries in a similar position.

These case studies highlight a variety of efforts to address base erosion and profit shifting and provide the rationale for the measures offered therein.

Structure of the study

The study comprises six sections. This introductory section provides an overview of the matters covered in the report. Section 2 discusses the impact of Illicit financial flows and related base erosion and profit shifting matters on domestic resource mobilization in Africa. Section 3 deals with the OECD approach to curtailing base erosion and profit shifting and how the measures can be implemented from an African perspective. Section 4 presents the three case studies on Cameroon, South Africa and the United Republic of Tanzania, concentrating on the efforts employed to tackle priority base erosion and profit shifting concerns in the light of the OECD base erosion and profit shifting package. Section 5 offers some policy measure that African policymakers should consider in

curtailing base erosion and profit shifting. Section 6 concludes the study by summarizing the discussion and distilling key recommendations for African countries to better facilitate the taxation of multinational enterprises in the future.

Section 2: Impact of illicit financial flows and related base erosion and profit shifting on domestic resource mobilization in Africa

Enhancing domestic resource mobilization is central to the structural transformation process in Africa in order to address social and economic challenges, such as poverty, inequality and low employment levels on the continent. Most African countries, however, face major challenges in ensuring domestic resource mobilization. Most of these challenges are a direct result of poor governance systems, poor public investment, corruption and inappropriate and externally imposed economic and fiscal policies that promote systems that have failed to transform African countries. In addition, there are challenges that pertain to underdeveloped tax laws, low enforcement of tax laws and general administrative weakness, which are essential to ensuring effective tax collection.

Addressing these challenges tends to realize gains much quicker than waiting for systemic shifts to have an impact on the level of public revenue. In this context, illicit financial flows remain one of the single greatest stumbling blocks to domestic revenue mobilization in Africa. Although there is a paucity of research on the linkages and transmissions of illicit financial flows from Africa, there has been much discussion on the definition of these flows. There is, however, no universally agreed definition of these flows, and its boundaries are still disputed (Chowla and Falcão, 2016). There are nevertheless two main interpretations of what comprises illicit financial flows: the legalistic interpretation and the broad interpretation.

2.1 Definition of illicit financial flows and the issue of tax avoidance

The legalistic interpretation of illicit financial flows suggests that the term refers to money that is earned, transferred or used in contravention to existing law. In some cases, this money is earned illegally, such as through organized

crimes, money laundering, drug trafficking, embezzlement, terrorist financing and bribery (Baker, 2005; Payne and others, 2014). In other cases, the money could have been earned legally but transferred out of the country illegally by circumventing currency controls or customs controls. An example of customs fraud is “trade mis-invoicing” that involves buyers and sellers presenting fraudulent documentation to customs officials. They falsify the value of their trade by under or over invoicing their trade documents to be less or more than the actual market value in order to circumvent the payment of customs duties” (Times Live, 2015). In addition, money could have been earned legally, but the tax on the same is evaded through illegal means by not complying with countries’ tax laws, for example, by deliberately falsifying tax returns and books of account (Meyerowitz, 2009). Prosecution is required to bring to justice the perpetrators of such illegal activities.

Under the legalistic interpretation of illicit financial flows, tax evasion, which is illegal, is part of illicit financial flows but tax avoidance is considered not to fall under these flows because tax literature defines it as involving the arranging of one’s affairs to pay less tax by utilizing loopholes in tax laws and exploiting them within legal parameters (Rapakko, 1989). This interpretation is backed up with earlier British court decisions such as *ICR v. Duke of Westminster*,³ which held the view “every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Act is less than it otherwise would be” and that no legal or moral obligation rests upon a taxpayer to pay higher taxes than he/she is legally bound to under the law (though of course it would seem that the courts of one country cannot determine what can and should be considered to be moral or legal in other countries; and determining what our moral obligations lie would seem to be in

³ See 51 TIR 467.

general to lie outside of the authority of courts) (Blankenburg and Khan, 2012).

An alternative approach used by many analysts of illicit financial flows is to define these more broadly, on the basis of the understanding that “illicit” does not refer only to the illegal. Indeed, the Oxford English Dictionary defines illicit as “not authorized or allowed; improper, irregular; esp. not sanctioned by law, rule, or custom; unlawful, forbidden”, which is much broader than only illegal. According to this view, aggressive tax avoidance practices should be seen as improper and/or not sanctioned by custom, especially given the backlash against such practices illustrated by the public outrage against illegitimate but legal commercial activities in the wake of global financial crisis of 2008-2009, when NGOs raised concern about companies paying little or no corporation tax in the countries in which they do business (Christian Aid, 2008). This prompted investigations to be carried out by the United Kingdom of Great Britain and Northern Ireland on corporations such as Google, Amazon, Starbucks, Thames Water, Vodafone and Cadbury (before a takeover by Kraft), which showed how those companies had used aggressive tax avoidance schemes to shift profits to low-tax countries (United Kingdom of Great Britain and Northern Ireland, House of Lords, 2013). This in effect makes the payment of corporation tax in a given country largely voluntary for many multinational enterprises, as exemplified by Starbucks, which volunteered an extra payment of taxes in the United Kingdom after bad publicity. Because of failure to live up to the expectations of societal norms, in line with the definition of “illicit” above, aggressive tax avoidance practices by multinational enterprises are deemed illegitimate and thus fall under the broad interpretation of illicit financial flows (Payne and others, 2014).

While the broader definition of illicit financial flows does appear to be truer to the meaning of “illicit”, an even more powerful argument for including aggressive tax avoidance in illicit financial flows is that it should be considered as harmful, and therefore illicit, owing to the negative impact that such flows have on development (African Union and economic Commission for Africa, 2015). these flows therefore needs to be measured,

tracked and stopped. From a practical point of view, given that tax avoidance and tax evasion both result from weak tax laws that are difficult to interpret and enforce in the case of tax evasion, it would appear to be important to measure tax avoidance in order to fully appreciate a country’s losses owing to weaknesses in its tax system. In addition, in many cases it is impossible for the researcher to distinguish between tax avoidance and tax evasion when estimating tax revenue losses due to the behaviour of multinational corporations, which is another argument for measuring them together.

In the report of the High-level Panel on Illicit Financial Flows from Africa, a broad definition of illicit financial flows is used, which includes examples of “abusive transfer pricing” along with tax evasion, trade mis-invoicing and criminal activities, such as the drug trade, human trafficking, illegal arms dealing and the smuggling of contraband and bribery and theft by corrupt government officials (African Union and economic Commission for Africa, 2015). The World Bank (2017) classifies the source of earnings from illicit financial flows under two main categories: flows from money earned legally and flows from money earned illegally. It notes that each type of illicit financial flow involves a different and complex network of actors, including domestic and foreign State institutions, domestic and foreign public officials and foreign financial institutions, all influenced by various factors for moving money abroad and using various channels, such as bulk cash smuggling, shell corporations, informal value transfer systems and trade-based money laundering (World Bank, 2017)

2.2 Aggressive tax avoidance and base erosion and profit shifting

Many of the aggressive tax avoidance schemes in which multinational enterprises engage are considered part of the broader illicit financial flows problem because the schemes involved are similar to those used in criminal activities, especially when they engage in schemes that route money through shell companies that are based in secretive tax haven jurisdictions (Froberg and Waris 2010). What prevents some of their activities from being exposed as criminal

tax evasion is mainly because multinational enterprises can back up what they do with opinions from tax advisers that make it difficult to prove the intent necessary for a criminal offence (Hodgson, 2006; Schlessler, 2011). Given that the base erosion and profit shifting schemes are often very complex, involving convoluted circumventions of complex tax provisions in various jurisdictions that are often shrouded secrecy in tax haven jurisdictions (African Union and economic Commission for Africa, 2015), it becomes difficult for revenue authorities to challenge their legality in a court.

OECD notes in its base erosion and profit shifting report that, although some multinational enterprises engaged in base erosion and profit shifting comply, in general, with the legal requirements of the countries in which they operate, there are cases of illegal abuse, which it claims are the exception rather than the rule (Organization for Economic Cooperation and Development, 2013a). These exceptions, in general, cover cases in which taxpayers secretly conceal their foreign investment from domestic tax authorities by investing in secret tax haven jurisdictions in which the ownership of assets, income or their business transactions is kept from the knowledge of the tax authorities. Tax haven jurisdictions often have banking secrecy laws that are used to facilitate the avoidance of taxes (United Nations, Department of Economic and Social Affairs, 1984).

Recently, many leading offshore financial centres, including those that previously provided bank secrecy, have started to share information about accounts held within their jurisdictions with the tax authorities of other countries, both on request and automatically. This can be seen as reducing the level of bank secrecy available. However, there remain loopholes in the regime for the international automatic exchange of tax information, meaning that individuals may be able to avoid having their information exchanged (Cotorceanu, 2015; Omartian, 2017). Moreover, it can be difficult for countries to access such information from certain jurisdictions, despite their agreement to provide it, for a number of reasons. First, some jurisdictions often take a long time to provide information to developing

countries. Second, African countries often do not know which taxpayers to request information about, complicating the process of requesting tax information from other jurisdictions. Third, though automatic exchange of tax information would seem to solve the problem identified in the previous sentence as it provides for jurisdictions to send tax information for all taxpayers that are residents of the counterpart country (and meet certain other requirements), in order to receive information under the relevant international agreements for automatic exchange, jurisdictions need to put in place sophisticated software and legal guarantees to ensure that the information exchanged remains secure. Very few African countries have these measures in place (as of 5 April 2018, only Mauritius, Seychelles and South Africa were benefiting from the automatic exchange of tax information) (Organization for Economic Cooperation and Development, 2018a).

In addition, a OECD introduced common reporting standards of automatic exchange of financial account information in tax matters which would ensure that tax haven jurisdictions exchange information on investment by other country residents in those jurisdictions (Organization for Economic Cooperation and Development, 2017e) the magnitude of investment still in secret jurisdictions was revealed by the International Consortium of Investigative Journalists in April 2016, which released the “Panama papers” that comprised nearly 12 million leaked documents detailing financial information on shell companies and tax havens by a single law firm in Panama. What the papers reveal is only the tip of the iceberg of tax avoidance, tax evasion and/or accumulation of illicit wealth by corrupt former or current leaders who hide their great fortune, including those in African countries who have looted their countries. The leaked documents demonstrated that tax evasion and indeed tax avoidance continues with impunity under legal cover. It is therefore argued in this report that addressing base erosion and profit shifting should be considered as part of the broad Illicit financial flows agenda. When taxpayers use secretive schemes to engage in aggressive tax avoidance provisions by purporting to keep the letter of the law but actually not following the intention

behind it, such activities need to be stopped, and can be rendered unlawful with general anti-tax avoidance provisions (though even with such laws, it remains difficult to prosecute such cases). If the base erosion and profit shifting practices by multinational enterprises are curtailed, these enterprises have the potential to contribute an enormous amount of taxes to domestic resource mobilization. The resultant base erosion and profit shifting reduces government tax revenue and leads to critical underfunding of public investment and infrastructure that could help to promote economic growth. When some enterprises pay low or no tax, they place a disproportionate tax burden on individual taxpayers and smaller domestic firms (which are typically responsible for most employment in African countries). This discourages tax morality and encourages a perception that the tax system is unfair. This, in turn, reduces voluntary compliance by all taxpayers (Oguttu, 2016a).

It is worth noting that Panama has, following the release of these papers, started to automatically exchange tax information with 28 other jurisdictions (OECD, 2018). Yet the release of the Panama papers shows the scale of abusive practices that can be hidden in just a single jurisdiction that preserves financial secrecy, and may continue to be the case until loopholes are addressed and the system is applied globally.

Conclusion

This section focusses on the impact of illicit financial flows and related base erosion and profit shifting on domestic resource mobilization in Africa. It highlights the need to adopt a broad definition of illicit financial flows, which includes aggressive tax avoidance. Even though multinational enterprises may argue that tax avoidance and the resultant base erosion and profit shifting is perfectly legal, aggressive tax avoidance practices by these enterprises have a similar development impact to other types of illicit financial flows. This report's authors take the view that, instead of emphasising merely the legality of aggressive tax avoidance schemes, the focus should be placed on their illegitimacy and development impact. Emphasizing legality implies that aggressive tax avoidance schemes

are protected unless they are forbidden by law. This approach is counterproductive, given that many African countries do not have sophisticated anti-avoidance laws to outlaw such activities. Given that aggressive tax avoidance practices and the resultant base erosion and profit shifting constitute illicit financial flows, various approaches must therefore be employed to curtail them. This includes not only the OECD action plan, but also other alternative approaches, as discussed in section 5.

Section 3: The Organization for Economic and Co-operation and Development's approach to base erosion and profit shifting

In 2013, OECD issued its action plan to address base erosion and profit shifting, noting that it posed a serious risk to tax revenue, tax sovereignty and tax fairness for member countries and non-members alike, as well as to the international corporate tax system (Organization for Economic Cooperation and Development, 2013b). In 2015, it released a package of 15 actions to curtail tax avoidance in order to better align the location of taxable profits with the location of economic activities and value creation, and improve the information available to tax authorities to apply their tax laws effectively. The measures are designed to be implemented domestically and through double tax agreement provisions in a coordinated manner, supported by targeted monitoring and strengthened transparency (Organization for Economic Cooperation and Development, 2015b).

3.1 Should African countries consider implementing OECD's base erosion and profit shifting package?

The base erosion and profit shifting agenda was developed by OECD and the Group of 20 countries. The work on base erosion and profit shifting reflects consensus among these countries on solutions to eliminate base erosion and profit shifting issues that mainly concern them. The only African country that is part of the Group of 20 and that worked together with the OECD countries on the base erosion and profit shifting project on an equal footing is South Africa. Other developing countries, including those in Africa, were invited in successive deliberations on base erosion and profit shifting issues. Although OECD indicated that it would take into account the perspectives of developing countries, and perhaps also the interests of developing countries these were never taken into consideration when the base erosion and profit shifting agenda was developed (Oguttu 2015d). The action plan has therefore been criticized for lacking focus

on or an understanding of the specific needs of developing countries. Nevertheless, some African countries (e.g., under the umbrella of the African Tax Administration Forum) have been vocal in consultations on the base erosion and profit shifting issues that are of greatest concern to them. For decades, African countries have been victims of base erosion and profit shifting not only by multinational enterprises that have invested on the continent, but also by African country residents, who have shifted money to developed countries and tax haven jurisdictions (Organization for Economic Cooperation and Development, 1987).

Even though African countries are not bound to follow the OECD recommendations, all countries, including African economies, have a shared interest in strengthening the integrity of the international corporate tax system (Group of 20 Development Working Group on Domestic Resource Mobilization, 2014). Not only would implementing measures against base erosion and profit shifting increase taxes paid by multinational enterprises engaging in base erosion and profit shifting, and as such help to fund public services, but other businesses and households would also benefit from lower taxes, including indirectly through a more level playing field (action 11). African countries should make use of the current international political will to address base erosion and profit shifting to strengthen collaboration with regional organizations such as the African Tax Administration Forum so that a united position can be taken on their base erosion and profit shifting priority concerns (Group of 20 Development Working Group on Domestic Resource Mobilization, 2014.).

3.2 Policy perspectives to consider before implementing OECD's base erosion and profit shifting measures

African countries that are considering how to implement the base erosion and profit shifting

measures should first recognize that the 15 OECD actions deal with various dimensions of the international tax planning practices of multinational enterprises. These dimensions could affect countries in various ways, depending on whether the country is predominantly capital-importing (i.e., it largely attracts FDI) or predominantly capital-exporting (i.e., country from which investment flows to other countries). For predominantly capital-importing countries (i.e., most African countries), the priority base erosion and profit shifting actions are those that protect the erosion of their right to tax income derived from within their geographic boundaries, given that most of them do not have the administrative ability to tax worldwide income (United Nations, General Assembly, 2015c). Given that tax treaties, in general, restrict the rights of host countries to tax corporate income at the source, capital-importing developing countries are also systematically disadvantaged from a treaty context (Picciotto, 2016). The priority action items for these countries are therefore the following: action 1 (address the tax challenges of the digital economy); action 4 (limit base erosion through interest deductions and other financial payments); action 6 (prevent treaty abuse); action 7 (prevent artificial avoidance of permanent establishment status); actions 8 to 10 (assure that transfer pricing outcomes are in line with value creation); and action 13 (re-examine transfer pricing documentation).

For capital-exporting countries (mainly developed countries and some African countries with relatively advanced economies that are resident States to home-grown multinational enterprises that are investing across borders), the priority base erosion and profit shifting actions are those that would encourage the competitiveness of home grown enterprises abroad and, at the same time, protect their tax bases from profit-shifting opportunities that are likely to increase with such cross-border investment. In addition to the above action items that are relevant to capital-importing countries in protecting rights to tax corporate income where it is earned, the following actions are therefore also of priority: action 2 (neutralize the effects of hybrid mismatch arrangements); action 3 (strengthen controlled foreign company rules); action 5 (counter harmful

tax practices more effectively, taking into account transparency and substance); actions 8 to 10 (assure that transfer pricing outcomes are in line with value creation); and action 13 (re-examine transfer pricing documentation).

Apart from the above, there are other action items that may be of priority to a given country depending on its administrative capacity and whether the relevant base erosion and profit shifting risk is of great concern in their specific circumstances (United Nations, General Assembly, 2015c). These are action 11 (establish methodologies to collect and analyse data on base erosion and profit shifting and the actions to address it); action 12 (require taxpayers to disclose their aggressive tax planning arrangements); action 14 (make dispute resolution mechanisms more effective); and action 15 (develop a multilateral instrument).

Even though specific action items may be considered priority for most African capital-importing countries, this does not always mean that each action item is a top priority for each African country. What is of priority to a specific country depends on its socioeconomic and geopolitical circumstances. African countries should therefore not respond to those action items by simply copying what other countries are doing. Some countries may choose not to enforce specific measures owing to a lack of resources and capacity to fully implement or enforce the regulations, or for tax competitiveness reasons (action 11). For example, some African countries, owing to their policy decisions, have signed very few double tax treaties. For such countries, some action items that pertain to tax treaties, such as actions 14 and Action 15, may not be a priority. Other African countries, owing to administrative capacity or low economic development, do not have transfer pricing rules. For such countries, the action items on transfer pricing may not be considered of top priority. They may, however, need to consider introducing transfer-pricing legislation quickly as and when their economic and administrative circumstances improve. This is especially so for natural resource-rich countries (African Union and Economic Commission for Africa, 2015).

Before adopting the base erosion and profit shifting measures, countries should also recognize the role of the country's economic and fiscal policy in ensuring economic development. Nevertheless, the approach to achieving economic development should be balanced so as not to result in negative spillover effects that have an impact on other countries' tax bases or result in double taxation or double non-taxation, which can deter international investment in the region or in the continent. Countries should also consider the base erosion and profit shifting approaches adopted by their trading partners on the continent and abroad.

Before implementing the base erosion and profit shifting measures, African countries should first take stock of the effectiveness of their current legislation in order to determine whether to buttress or introduce anti-base erosion and profit shifting measures. Ultimately, this evaluation will necessitate countries setting up a tax committee or forum to undertake such a review in the light of their specific circumstances. After such a review, a country will then determine what support it needs to address its challenges. Support can, for example, be sought from Tax Inspectors Without Borders of OECD and the United Nations Development Programme (Organization for Economic Cooperation and Development, 2015d) which can provide funding for building capacity in developing countries' tax administrations. Special approaches may be required for those countries that may be harder to reach owing to geography, capacity, size or other reasons that may affect their ability to effectively implement the base erosion and profit shifting measures (Group of 20 Development Working Group on Domestic Resource Mobilization, 2014). Such countries may have to seek assistance to devise tailored approaches to implement the outcomes of the base erosion and profit shifting action plan.

3.3 Understanding OECD's base erosion and profit shifting measures

For an African country to begin to consider how to implement the base erosion and profit shifting actions, it is important to understand what the action items are all about, the malfeasance that they are intended to curtail and the

recommendations offered by OECD. This part of the study provides a summary of the salient features in that regard and their significance from an African perspective. The analysis does not follow a chronological order of each action item; rather, they are divided into four major implementation categories that OECD recommends: minimum standards, common and best practices for domestic law, international standards and analytical reports (all explained below). For each action item listed under the relevant category, some insight is provided on what African countries' responses should be, and examples are given of steps taken by some African countries to reflect on and implement some base erosion and profit shifting recommendations. It is acknowledged that other African countries have chosen to remain unengaged with the reforms, choosing either a wait-and-see approach or even working on their own independent set of reforms to best counter base erosion and profit shifting by multinational enterprises using alternative approaches.

3.3.1 Minimum standards

The minimum standards were agreed upon by OECD and the Group of 20 countries to tackle cases in which no action by some countries would create negative spill-over effects on other countries. While OECD recommends that non-member countries, such as those in Africa, should associate themselves with the minimum standards, these are by no means binding regulations, and their implementation is of greater importance to OECD and the Group of 20 member States than to African States. The following is a brief explanation of the minimum standards in 4 of the 15 action items and some perspectives that African countries should take into consideration if they choose to implement the minimum standards.

Minimum standards in action 5: counter harmful tax practices more effectively, taking into account transparency and substance

The background to action 5 of the base erosion and profit shifting project evolves from the OECD

report on harmful tax competition (Organization for Economic Cooperation and Development, 1998, para. 75), in which it was pointed out that tax haven jurisdictions (Organization for Economic Cooperation and Development, 1987) and preferential tax regimes (Organization for Economic Cooperation and Development, 1998, para. 79) were harmful tax practices that distort financial and investment flows among countries. Over the years, however, OECD failed to address harmful tax practices in preferential tax regimes (Herzfeld, 2014). It focused only transparency and exchange of information by tax havens under its global forum (Organization for Economic Cooperation and Development, 2007). Under the base erosion and profit shifting project, OECD reiterates the underlying policy concerns expressed in the 1998 report with regard to the “race to the bottom” through preferential tax regimes, which ultimately drives applicable tax rates on specific mobile sources of income to zero for all countries, whether or not this is the tax policy that a country wishes to pursue.

The minimum standard in action 5 requires countries that have preferential regimes to ensure that substantial activity is carried on in that country (i.e., that taxpayers undertake core income-generating activities). In addition, those countries with preferential regimes that feature specific tax rulings (i.e., only a specific taxpayer may rely on it) should ensure transparency, including compulsory spontaneous exchange, about such tax rulings. Specific focus was placed on intellectual property regimes and on other non-intellectual property regimes, such as headquarter company regimes, distribution and service centre regimes, financing and leasing regimes, fund management regimes, banking and insurance regimes, shipping regimes and holding company regimes. Since 2010, OECD has reviewed 43 preferential regimes. Some of these regimes will have to be re-reviewed in light of the substantial activities requirement under action 5. African countries, such as Mauritius and South Africa, which have a headquarter company regime (Oguttu, 2011), will have to ensure that they adhere to the substance requirements and that they exchange information with other tax authorities upon request on any specific tax rulings granted to taxpayers regarding those regimes.

Although African countries such as Mauritius will have to balance these international obligations with the need to preserve the competitiveness of their economies, it is certainly important that such countries avoid harmful tax competition that attracts headquarter companies, which are used to shift profits from other African countries (ibid.). It should, however, be noted that, from an African perspective, the harmful tax practice that is of most concern in leading to the “race to the bottom” is granting “un-strategic tax incentives”. This matter was, however, not addressed in the OECD base erosion and profit shifting project. Further discussion on this issue is handled in section 5.

Minimum standard in action 6: prevent treaty abuse – a priority concern in Africa

Treaty abuse entails the use of treaty-shopping schemes to avoid taxes, whereby residents of a non-treaty country obtain tax treaty benefits that are not supposed to be available to them (van Weeghel, 1998). Such treaty benefits include reduced withholding tax rates on dividends, interest or royalties, which are normally higher than domestic withholding tax rates. Treaty shopping is done mainly by interposing a “conduit company” in one of the contracting States in order to shift profits out of that State (Oguttu, 2007; Organization for Economic Cooperation and Development, 1987). The result of such techniques is that the country of the payer of dividends, interest or royalties loses out on the domestic withholding taxes that it would otherwise have been able to collect. Treaty abuse is a priority concern for many African countries that have signed double taxation agreements with low-tax or tax haven jurisdictions. Multinational enterprises often take advantage of the low or zero withholding tax rates in many African double taxation agreements (owing to poor treaty negotiating capacity) to shift profits out of African countries. Many treaty-shopping schemes in Africa involve conduit companies registered in Mauritius under global business licences (Rohatgi, 2002), but with no or minimal active businesses in Mauritius. Mauritius’s extensive tax treaty network with many other African countries offers multinational enterprises with subsidiaries in Africa the opportunity to

route their investment through the country (Schulze, 1997). The following “minimum standards”, discussed below, are recommended in action 6 to prevent treaty shopping, which will result in changes to the OECD Model Tax Convention on Income and Capital.

Where a person circumvents domestic tax law to gain treaty benefits, it is recommended in action 6 that treaty abuse be addressed through domestic anti-abuse rules. An example is section 88 (5) of the Ugandan Income Tax Act (cap. 340, as amended in 2016), which provides that, with the exception of publicly listed companies, the benefit of an exemption from or reduction in Ugandan tax under a double taxation agreement between Uganda and another country will be available only to a non-resident person who is the beneficial owner of the income, has full and unrestricted ability to enjoy the income and determine its future use and has economic substance in the treaty country. The concern, however, is that, if the domestic law does not override a double taxation agreement, the provision may not be applicable in a treaty context if there is no such provision in the treaty itself. IMF recommends that countries should ensure that they include a similar provision in their tax treaties (International Monetary Fund, 2014).

Where a person circumvents limitations in the treaty itself, it is recommended in action 6 that country's treaties should have anti-abuse rules following a two-pronged approach. First, the title and preamble of treaties should clearly state that the treaty is not intended to create opportunities for non-taxation or reduced taxation through treaty shopping. Second, treaties should include specific limitation of benefits provisions, and/or a more general anti-abuse rule based on the principal purposes test. Regarding the decision whether to adopt the limitation of benefits and/or the principal purposes test, each rule has strengths and weaknesses and may not be appropriate for all countries. The rules may have to be adapted to the specificities of individual countries and the circumstances of the negotiation of double taxation agreements. Some countries may have constitutional or specific legal restrictions that prevent them from adopting the recommended

provisions. Other countries may have domestic anti-abuse rules or court interpretative tools that prevent some forms of treaty abuse. The administrative capacity of some countries (a major issue in African countries) may also prevent them from applying specific complex anti-abuse rules, such as complex limitation of benefits rules (Oguttu, 2016b), which have largely been adopted by countries that have signed double taxation agreements with the United States of America. Basically, the limitation of benefits provision works by restricting the entitlement to treaty benefits unless a resident passes the series of tests of the notion of “qualified person”). Although, the limitation of benefits provision may be an effective anti-abuse provision, its complexity may hamper the ability of African countries with weak and limited administrative capacity to apply it, given that it requires countries to have access to information to verify the prerequisites for qualifying for treaty benefits (International Monetary Fund, 2014). Nevertheless, OECD came up with a simplified limitation of benefits provision, which could prove feasible by some African countries. For African countries with limited administrative capacity, adopting the principal purposes test may be more feasible (Oguttu, 2016b). The test requires that treaty benefits be denied if one of the principal purposes of the transaction is to avoid taxation by taking advantage of the treaty benefits. For example, after Malawi had terminated its 1969 treaty with the Netherlands, which was prone to treaty abuse, a new treaty was re-signed in 2014 (Netherlands, 2015). This new treaty includes a limitation on accessing treaty benefits in that treaty relief is denied if the main purpose or one of the main purposes of any person is to take advantage of the treaty. This is in keeping with the new policy of the Netherlands to include such an anti-treaty abuse provision in its tax treaties with developing countries. Similar provisions have been included in the treaties that it has renegotiated with Ethiopia, Ghana, Kenya and Zambia (MNE Tax, 2015).

Apart from the above minimum standards, action 6 also sets out specific anti-abuse provisions that countries may include in their double taxation agreements to curtail specific treaty base erosion and profit shifting risks. One aspect

that should be a priority to African countries is the recommendation to include in double taxation agreements the anti-abuse provision in article 13 (4) of the Model Tax Convention, which allows the contracting State in which immovable property is situated to tax the capital gains of a resident of the other State on shares of companies that derive more than 50 per cent of their value from such immovable property. Multinational enterprises often avoid capital gains tax in African countries by incorporating conduit companies in low-tax jurisdictions, which are used to indirectly dispose of shares in assets located in African countries so that the proceeds appear to be derived from the low-tax jurisdiction (United Nations, General Assembly, 2015c; Oguttu, 2016b). This is exemplified by the Ugandan court case of *Zain International BV v. Commissioner General of Uganda Revenue Authority*,⁴ which involved the disposal of shares of a telecommunication company based in Uganda to a connected offshore company. The court ruled that the transaction was a disposal of an interest in immovable property located in the country and that the capital gains were taxable there. Adopting the OECD recommendation will be beneficial for African countries in preventing such treaty abuse.

In general, however, African countries have signed few double taxation agreements and many are sceptical about extending their treaty network owing to concerns about treaty abuse, which is exacerbated by their general lack of treaty negotiating capacity. IMF recommends that capital-importing countries should sign treaties with considerable caution in order to guard against treaty shopping (International Monetary Fund, 2014). They should first consider whether they can achieve more by signing a treaty or by instead simply using their domestic law to provide the elements of investment protection (e.g., the permanent establishment definition and withholding tax rates). Indeed, the envisaged benefits that a treaty could provide to such a country may, in fact, be of relatively little value. Other treaties, such as on the exchange of information in tax matters, could be realized through signing tax information exchange

agreements (Global Forum on Transparency and Exchange of Information for Tax Purpose, 2002; Oguttu, 2014) or by signing the Convention on Mutual Administrative Assistance in Tax Matters. African countries should also be clear about their tax policy considerations before deciding to enter into a tax treaty. A cost/benefit analysis of tax treaties that pose base erosion and profit shifting risks needs to be carried out to determine whether such treaties should be terminated (Oguttu, 2016b). For example, in 2014, Uganda announced that it had suspended all its ongoing treaty negotiations pending a review of the treaty terms that it should seek in such negotiations (Ladu, 2014). OECD has proposed adding a revised paragraph 15 to the introduction to the Model Tax Convention, which would set out the following factors that countries should take into consideration if they wish to conclude or terminate a treaty: whether there are risks of double taxation that would justify a tax treaty if the other State levies no or low income taxes; whether there are elements in the other State's tax system that could increase the risk of non-taxation; and whether the prospective treaty partner is willing and able to exchange tax information and to provide assistance in the collection of taxes. Countries should also evaluate the extent to which the risk of double taxation, in fact, exists in cross-border situations involving their residents. Many cases of residence/source juridical double taxation can be eliminated through domestic exemption or credit methods, without the need for a double taxation agreement (United Nations, Committee of Experts on International Cooperation in Tax Matters, 2011).

Minimum standard in action 13: re-examine transfer pricing documentation

Multinational enterprises are known to withhold substantial amounts of relevant information from national authorities in countries in which they operate. They often do not disclose their operations in a geographically disaggregated manner and often operate under great secrecy so that they end up reporting income in jurisdictions with very low or no taxes. Most

⁴ High court of Uganda at Kampala (Civil Division) Miscellaneous Cause No. 96 of 2011.

developing countries face significant challenges in obtaining information needed to assess the scale and impact of cross-border tax avoidance and to take effective action to counter such avoidance. If multinational enterprises are forced to report on their activities, this would improve tax collection, while tax avoidance through tax havens will be dampened (Tax Justice Network, 2015). Action 13 sets out “minimum standards” that require multinational enterprises to provide Governments with information on their global allocation of the income, economic activity and taxes paid among countries according to a common template. This must follow a three-tiered transfer pricing documentation approach consisting of a master file containing standardized information for all multinational enterprises group members, a local file with information on material transactions of the local taxpayer and a country-by-country report with information on the global allocation of the enterprise’s income and taxes paid and the location of its economic activities. Taken together, these three documents would make it easier for tax administrations to identify whether the enterprises have engaged in transfer pricing and other practices to artificially shift income into tax-advantaged environments. Enterprises with annual consolidated turnover of 750 million euros or more submit country-by-country reports annually, commencing 31 December 2017. Country-by-country reporting is intended to be an integral part of the improved transfer-pricing documentation package, which is likely to help tax administrations to better identify cases in which there is a real risk of profit diversion to low or no tax jurisdictions. It will enable developing countries to obtain the information needed to assess the risk of transfer-pricing abuse and to effectively address such risk. This has the potential to be particularly valuable for African countries if they lack good data on which to base their judgments on cross-border compliance risks.

Countries will not, however, gain access to these reports automatically. In terms of the 2015 OECD guidance note on implementing country-by-country reporting, countries must enact legislation that requires the ultimate parent entity of a multinational enterprises group to file the country-by-country report in its jurisdiction

of residence, and countries must have signed a treaty that can facilitate country-by-country reporting. Three model competent authority agreements, which can be used to facilitate the exchange of country-by-country reports, have been developed by the OECD, including the Multilateral Competent Authority Agreement on the Exchange of CbC Reports, and further agreements for exchanges under Double Tax Conventions and Tax Information Exchange Agreements (Organization for Economic Cooperation and Development, 2018b). African countries that have well-developed treaty networks can use their double taxation agreements to gain access to country-by-country reports. For countries with limited double taxation agreement networks, becoming a signatory to the Convention is probably the quickest way to secure the right to request country-by-country reports from the countries in which the parents of large multinationals are located. Statistics from the OECD website indicate that, as at 26 March 2018, the Convention had entered into force in nine African countries: Cameroon, Ghana, Mauritius, Nigeria, Senegal, Seychelles, South Africa, Tunisia and Uganda. Four countries had signed but not had the Convention enter into force: Burkina Faso, Gabon, Kenya and Morocco (Organization for Economic Cooperation and Development, 2018c). Article 6 of the Convention requires the competent authorities of the parties to the Convention to mutually agree on the scope of the automatic exchange of information and the procedure to be complied with. Accordingly, OECD developed the multilateral competent authority agreement on the exchange of country-by-country reports, which sets rules and procedures for the competent authorities to automatically exchange country-by-country reports prepared by the reporting entity of a multinational enterprise group. These requirements, however, may make the implementation of country-by-country reporting slower in non-OECD countries than in OECD ones (Ernst & Young, 2016b). Indeed, as of April 2018, Mauritius and South Africa were the only African countries receiving country-by-country reports from other jurisdictions through automatic exchange (Organization for Economic Cooperation and Development, 2018d). African countries are also concerned that signing such

treaties may not be enough to guarantee that reports will, in fact, be provided, given that multinational enterprises may raise concerns that the administrative capacity of some countries does not guarantee that they will be able to protect the sensitive business information that is exchanged with the confidentiality that it deserves. The threshold for reporting, namely, multinational enterprise groups with annual consolidated turnover of 750 million euros, is also too high for African countries. Many multinational enterprises that operate in Africa may be below that threshold but are engaged in significant base erosion and profit shifting activities. The required procedures for filing and gaining access to corporate reports are also embedded with cumbersome requirements that may impede filing in African countries that already have administrative challenges. It should, however, be noted that too much information for tax administrations with weak capacity may be overwhelming and end up being underutilized. There are also concerns that the power of host country tax authorities in country-by-country reporting is weak, given that they cannot ask for country-by-country reports from multinational enterprises operating in their jurisdiction but rather have to apply for the information from the tax authority of the enterprise's home country, provided that the latter has the information and that it has signed a treaty to exchange information and has committed itself to confidentiality (Financial Transparency Coalition, 2015). Developing countries are also concerned that some suggested criteria for country-by-country reporting in 2013 discourses on the matter were dropped. This included reporting on transactions relating to royalties, interests and service fees, which are at the centre of a number of profit-shifting scandals (Oxfam, 2014.). Under action 13, emerging economies have nevertheless insisted that country-by-country reporting should require additional transactional data (beyond that available in the master file and local files) for entities operating in their jurisdictions regarding related party interest, royalties and service fees. Such information would be needed to perform risk assessments in cases where it is challenging to obtain information on the global operations of a multinational enterprise group headquartered elsewhere. OECD will review

and consider implementing these concerns by 2020. The 2013 discussions on country-by-country reporting had also suggested that the reports be made public so that civil society can monitor whether Governments are acting on the information received. This requirement was dropped in the final reports. This matter is discussed in detail in section 4.

Minimum standard in action 14 on improving dispute resolution

When OECD issued its 2013 action plan on base erosion and profit shifting, it emphasized the need to effectively resolve treaty disputes, given that the initiatives to address base erosion and profit shifting could lead to new domestic law and treaty-based anti-abuse rules, which may be susceptible to conflicting interpretations. Action 14, which deals with making dispute resolution mechanisms effective, is aimed at strengthening the effectiveness and efficiency of the mutual agreement procedure in article 25 of the OECD Model Tax convention in order to resolve treaty disputes and ensure certainty and predictability for business (Organization for Economic Cooperation and Development, 2013b). Article 25 (5) provides for arbitration (an integral part of the mutual agreement procedure) as a means of resolving specific issues that prevent competent authorities from reaching a satisfactory resolution of the case (United Nations, 2013b). OECD notes that the business community and a number of countries consider mandatory binding arbitration to be the best way of ensuring that tax treaty disputes are effectively resolved through a mutual agreement procedure. Under action 14, minimum standards were adopted that require countries to ensure that treaty obligations relating to mutual agreement procedure are fully implemented in good faith and that mutual agreement procedure cases are resolved in a timely manner. Furthermore, administrative processes should promote the timely resolution of treaty-related disputes and taxpayers who meet the requirements of article 25 (1) can gain access to the mutual agreement procedure. The agreement to a minimum standard is complemented by a commitment by a number of countries to adopting mandatory binding arbitration. There is, however, currently

no consensus among all OECD and Group of 20 countries on the adoption of mandatory binding arbitration as a mechanism to ensure the timely resolution of mutual agreement procedure cases. Developing countries are also not keen on arbitration, and few African countries have arbitration provisions in their tax treaties (United Nations, 2012b). The matter of arbitration in mutual agreement procedure has always been of great concern to developing countries, given that many do not have actual experiences with the mutual agreement procedure. Arbitration can be very costly (United Nations, 2013b) and it is a secretive process (United Nations, Committee of Experts on International Cooperation in Tax Matters, 2015, para. 99). Developing countries with limited mutual agreement procedure experience are concerned that adding arbitration in the mutual agreement procedure (Hearson, 2015), could be unfair to them when a dispute occurs with more experienced countries. The fact that arbitral decisions under the mutual agreement procedure cannot be reviewed or appealed is also a major source of concern (United Nations, 2013b). In 2012, the United Nations came up with a guide to the mutual agreement procedure for developing countries that had signed treaties on the basis of the OECD Model Tax Convention in order to address these concerns (United Nations, 2012b). The United Nations recommends that countries consider the use of alternative dispute mechanisms, such as mediation and conciliation, which are applied in resolving commercial disputes, to resolve tax treaty disputes (United Nations, Committee of Experts on International Cooperation in Tax Matters, 2015). To encourage international investment, African countries should ensure that treaty disputes are resolved and that they support taxpayers during mutual agreement procedure processes. Until the concerns about arbitration are dealt with, however, it is recommended that African countries be cautious about adopting mandatory arbitration in their tax treaties.

Inclusive framework to implement base erosion and profit shifting minimum standards

Acknowledging that globalization requires global solutions and that a global dialogue should be

established on base erosion and profit shifting issues, OECD designed a more inclusive framework for monitoring the implementation of the minimum standards with all interested countries participating on an equal footing. As of March 2018, 21 African countries were part of the inclusive framework on base erosion and profit shifting: Angola, Benin, Botswana, Burkina Faso, Cameroon, Congo, the Democratic Republic of the Congo, Djibouti, Egypt, Gabon, Kenya, Liberia, Mauritius, Nigeria, the Republic of the Congo, Senegal, Seychelles, Sierra Leone, South Africa, Tunisia and Zambia (Organization for Economic Cooperation and Development, 2018e). African countries should, however, be circumspect, given that participation in the inclusive framework does not always imply that they will be able to influence the core decisions made by OECD on any international tax matters that could affect the revenue base of developing countries at the expense of interests of OECD countries. Historically, any changes to international tax matters, in particular to tax treaty rules under the Model Tax Convention, operate by consensus of the OECD member countries. Some changes have therefore been stalled, in which some countries have not been willing to proceed with a change that would result in their inability to attract capital, even though the change would have reduced tax avoidance in other countries (McIntyre, 2005). African countries should voice their discontent if the promise to “participate on an equal footing” is just rhetoric and not reflected in OECD policies and decisions. That being said, it may, in any case, be in African countries’ own interests to implement the base erosion and profit shifting minimum standards, given that these may help to reduce tax avoidance in their own territories.

3.3.2 Common approaches and best practices for domestic law

Under the base erosion and profit shifting project, specific best practices and common approaches for implementing base erosion and profit shifting measures under domestic laws are recommended in four action items. These are not minimum standards that have to be implemented by all countries. OECD hopes that the convergence

of the best practices will enable consideration of whether they should become minimum standards. Some African countries already have the relevant domestic legislation in place. It is important for its effectiveness to be measured against the best practices. Those that do not have the legislation should ensure that they enact laws that are in line with the best practices, given that doing so would prevent uncoordinated responses to international tax avoidance, which may result in double taxation or non-taxation. An overview of the best practices and common approaches is discussed below. Those that could be emulated by African countries that are largely capital-importing countries are pointed out.

Common approach to neutralize hybrid mismatch arrangements: action 2

Countries need to neutralize hybrid mismatch arrangements that exploit differences in the tax treatment of an entity or financial instrument under the laws of two or more tax jurisdictions to produce mismatches in tax outcomes resulting in lower aggregate tax burdens of the parties involved. The base erosion and profit shifting report deals with three types of hybrid mismatch arrangements: hybrid instruments, hybrid entities and hybrid transfers. A common approach is recommended in action 2 that entails “linking rules” that align the tax treatment of hybrid instruments with the other jurisdiction without disturbing the commercial outcomes, while minimising compliance and administrative costs for taxpayers and tax administrations. Given that many African countries do not have sophisticated administrative and banking systems, the use of hybrid mismatch arrangements is not a priority base erosion and profit shifting risk. Countries with relatively developed economies, however, such as South Africa, that consider this to be a base erosion and profit shifting risk should consider adopting the OECD recommendation in this regard. Action 2 also deals with mismatches that result when dual resident entities are used to avoid taxes. The international standard in action 6 (discussed below), which will result in revisions to article 4 (3) of the OECD Model Tax Convention, will prevent such mismatches.

Best practices to strengthen controlled foreign company rules: action 3

Base erosion and profit shifting can arise when multinational enterprises set up subsidiary companies in other jurisdictions through which they can route their income (Organization for Economic Cooperation and Development, 2013a). Given that a subsidiary is a separate legal entity, the country where the multinational enterprise is based cannot tax its income until it is distributed to the resident shareholders as dividends. This often encourages the enterprises to defer domestic taxation on their foreign income by setting up subsidiaries in low-tax jurisdictions to receive their income, instead of remitting it to the home country (Organization for Economic Cooperation and Development, 2000). With the growing use of international base companies, a number of countries have enacted controlled foreign company legislation to reduce the risk of the deferral of domestic tax revenue from international investments (Oguttu, 2015a). This legislation ensures that the undistributed income of a controlled foreign company is not deferred but taxed in the hands of its domestic shareholders on a current basis (Arnold, 1986). It is noted in the OECD base erosion and profit shifting report that, although many countries have enacted controlled foreign company and other anti-deferral rules, most countries’ rules do not always counter base erosion and profit shifting in a comprehensive manner. In action 3, OECD recommends “best practices” to strengthen controlled foreign company rules, in the form of building blocks, for designing effective rules. There are primarily two tax policy reasons why some countries have not introduced this legislation. First, some countries are not committed to the principle of “capital export neutrality”, which requires that resident taxpayers pay the same tax on their domestic and foreign source investment income. Second, and this is the case for most African countries, the amount of domestic tax avoided through the use of non-resident entities simply does not warrant the additional administrative costs and complexity associated with such legislation (Sandler, 1998). This is why, internationally, controlled foreign company legislation has been introduced by countries with advanced tax systems (Oguttu,

2015a). Such countries often have many home-grown multinational enterprises with foreign subsidiaries, so they apply the residence basis of taxation to tax their residents, given that they have the administrative ability to cast a wide tax net. African countries apply the source basis of taxation primarily because they often do not have the administrative ability to tax the worldwide income of their residents. Action 3 is therefore not a priority base erosion and profit shifting concern for many African countries. At present, South Africa is the only African country that applies controlled foreign company legislation in a comprehensive manner (Olivier and Honiball, 2011). For African countries with controlled foreign company legislation, the main policy concern is to balance the protection of their tax base without unduly hindering the competitiveness of their multinational enterprises as they invest abroad.

Best practice for limiting excessive interest deductions (action 4): a priority base erosion and profit shifting risk in Africa

The use of related party interest is one of the common and simplest profit shifting techniques used in international tax planning. Multinational enterprises often prefer to finance their subsidiaries with debt, at a commercial interest rate, which is a deductible expense that can effectively reduce source country tax, than with equity financing, in which a distribution of dividends on shares is not deductible (Arnold and McIntyre, 2002). Multinational enterprises therefore often engage in “thin capitalization” schemes, whereby a subsidiary company is financed with more debt than equity capital, compared with what it could have borrowed on its own resources, because it is borrowing either from or with the support of connected entities in the multinational enterprise group (Oguttu, 2016b). Excessive cross-border interest and similar financial flows to tax haven jurisdictions have a longer track record in Africa as a priority base erosion and profit shifting risk (Oguttu, 2012). This can be achieved by placing higher levels of third-party debt in high-tax countries, using intragroup loans to generate interest deductions in excess of the group’s actual third-

party interest expenses and using third-party of intragroup financing to fund the generation of tax exempt income. Some of the measures African countries employ to prevent the depletion of their tax bases are as follows:

- a. The use of the arm’s-length principle to determine whether the size of the loan and the interest rate would have been made in an arm’s-length transaction (article 9 of the OECD Model Tax Convention; namely, that if the loan exceeds what would have been lent in an arm’s-length situation, then the lender is deemed to have an interest in the profitability of the enterprise);
- b. The use of fixed debt/equity ratios as “safe harbours” in setting the parameters within which this arm’s-length principle applies, such that the interest relating to the debt above the fixed ratio is not tax deductible (Oguttu, 2013). African countries also apply fixed debt/equity ratios relatively easier to administer, given that they can easily link the level of the interest expense to a measure of an entity’s economic activity (Oguttu, 2016b);
- c. Withholding taxes on interest, a relatively mechanical tool that is easy to apply and administer (Oguttu, 2016a). In a treaty context, however, the rate will be reduced to 10 per cent for treaties based on article 11 of the OECD Model Tax Convention. In practice, however, the rate in most African countries’ tax treaties is often reduced below 10 per cent (sometimes to 0 per cent), which opens such treaties to abuse;
- d. The use of a debt/earnings before interest, tax and depreciation ratio to prevent excessive interest deductions. This ratio is a metric measure of a company’s ability to pay off its short-term incurred debt. The ratio is calculated as debt divided by earnings, before factors such as interest, taxes, depreciation and amortization are taken into account (Shaftoe, 2016);
- e. The use of targeted anti-avoidance rules, which disallow interest expense on specific

transactions. As new base erosion and profit shifting schemes are crafted, however, further targeted rules may be required, resulting in a complex system and increased administration and compliance costs.

Notwithstanding these measures, the excessive deduction of interest remains a major base erosion and profit shifting risk for African countries, given that the tax legislation does not clearly define the difference between what constitutes interest and equity (Africa Tax Administration Forum, 2015). OECD analysed the effectiveness of the various counteracting measures that countries apply and concluded that the use of arm's-length tests, the use of withholding taxes and the use of rules to disallow a percentage of interest, irrespective of the facts and circumstances, are ineffective rules for preventing base erosion and profit shifting as a result of excessive interest deductions. In action 4, OECD recommends that the best practice to address excessive interest deductions is the use of a debt/earnings before interest, tax and depreciation fixed ratio rule of between 10 and 30 per cent, supplementing the fixed ratio with a worldwide group ratio rule that allows an entity to exceed the limit in specific circumstances, supplementing the fixed ratio and group ratio rule with other provisions that reduce the impact of the rules on entities that pose less base erosion and profit shifting risk. Measures to reduce the impact of the rules on entities posing low base erosion and profit shifting risk could include:

Exempting firms with net interest expenses below a certain level from measures to address excessive deductions;

Excluding interest paid on loans to fund public-benefit projects from calculations of interest deductions for the purposes of identifying excessive deductions;

Permitting firms to carry forward disallowed interest expenses to future years..

African countries that wish to adopt the above base erosion and profit shifting measures should ensure a balanced approach. Where new measures are adopted, these must be

well coordinated with previous measures (if these are maintained). For example, the lack of proper interaction in the use of the arm's-length principle and tax treaty provisions may cause multinational enterprises to rely more on other forms of base erosion payments, such as payments for technology and services.

Best practice regarding mandatory disclosure of aggressive tax planning: action 12

OECD notes that comprehensive and relevant information on aggressive tax planning strategies is often unavailable to tax administrations, even though the availability of timely, targeted and comprehensive information is essential to enable Governments to quickly identify risk areas (Organization for Economic Cooperation and Development, 2013a). While audits remain a key source of relevant information, they suffer from a number of constraints as tools for the early detection of aggressive tax planning techniques (Ibid.). In action 12, OECD recommends that the best practice is for countries to have mandatory disclosure rules that require taxpayers to disclose their aggressive tax planning arrangements, taking into consideration the administrative costs for tax administrations and businesses, while drawing on experiences of countries that have such rules (Ibid.). Action 12 distinguishes between mandatory disclosure rules and other types of disclosure initiatives used by tax administrations to gather information from taxpayers in order to undertake risk assessments. These include rulings regimes, additional reporting obligations, surveys and questionnaires, voluntary disclosure rules and co-operative compliance programmes. The objectives of these initiatives are different from mandatory disclosure rules that focus exclusively on identifying revenue risks raised by aggressive tax planning through obtaining specific information about promoters, taxpayers and defined schemes. Action 12 sets out a modular framework to enable countries without mandatory disclosure rules to design a regime that fits their needs so that they can obtain early information on potentially aggressive or abusive tax planning schemes and their users. Countries with similar provisions (e.g., South Africa's reportable arrangements provisions set out in

the Tax Administration Act 28 of 2011) will have to evaluate the effectiveness of their measures with the OECD best practices.

3.3.3 Action points that reinforce international standards

Under this category of base erosion and profit shifting action items, a common understanding and interpretation of international tax standards in the OECD Model Tax Convention and in the OECD transfer-pricing guidelines have been developed. Countries are required to indicate in their domestic legislation whether they will follow these international standards. Given that double taxation agreements and transfer-pricing issues raise priority base erosion and profit shifting concerns for African countries, in the absence of constraining constitutional, economic or treaty obligations, it would be worthwhile for African countries to associate themselves with the international standards in order to ensure coordination in the international tax system. An overview of the international standards and the policy perspectives that African countries should take into consideration if they are to adopt these standards is set out below.

International standard on dual resident entities (action 6): a priority base erosion and profit shifting concern in Africa

An entity is dual resident if it is deemed tax resident in two jurisdictions. For example, it could be incorporated in one country but effectively managed in another (Oguttu, 2008). To prevent the double taxation that could arise if both jurisdictions taxed the same entity on its income, article 4 (3) of the OECD Model Tax Convention currently provides that such an entity is deemed resident where its place of effective management is based. Multinational enterprises can, however, use dual resident entities to avoid taxes by ensuring that the place of effective management is based in a low-tax jurisdiction (van den Berg and van der Gulik, 2009). This has been a concern in many African countries where companies are incorporated but effectively managed in low-tax countries, such as Mauritius and the Netherlands (HR Future, not dated). To curtail tax avoidance

emanating dual residence status, action 6 of the base erosion and profit shifting project sets out an international standard, which will result in the revision of article 4 (3). Double taxation will now be resolved through mutual agreement by the competent authorities having regard to the place of effective management, place of incorporation and other relevant factors. If no agreement is reached, treaty benefits would be denied and the dual resident entity would be subject to double taxation. This change has the potential to raise significant additional tax revenue if implemented in African countries (Davis Tax Committee, 2014b).

International standards on preventing artificial avoidance of permanent establishment status (action 7): a priority base erosion and profit shifting concern in Africa

The permanent establishment concept is a crucial element of tax treaties, most of which are based on the Model Tax Conventions and the United Nations Model Double Taxation Convention between Developed and Developing Countries (Oguttu, 2008). From a developing country perspective, the inherent flaw of the OECD Model Tax Convention is that it embodies rules proposals by developed capital exporting countries and thus favours them over capital-importing countries (Arnold and McIntyre, 2002). The definition of the permanent establishment concept in it is therefore much more limited than in the UN Model Double Taxation Convention, which favours capital-importing countries over capital-exporting countries (Singh 2011) and offers a broader definition of the permanent establishment concept, which is advantageous for source countries (United Nations, General Assembly, 2015c). The permanent establishment concept, as defined in article 5 of the OECD and United Nations Model Tax Conventions, is designed to limit source countries' tax jurisdiction over foreign businesses (Organization for Economic Cooperation and Development, 2013a), in that business profits can be taxed only by a source State if a non-resident enterprise has created a taxable presence, which is a significant and substantial economic bond between itself and that State (Vogel, 1997). The permanent

establishment concept has been under attack for years, from both multinational enterprises that abuse it by compartmentalizing it and from developing countries that want to extend its parameters to reclaim their tax jurisdiction. OECD acknowledges that the current definition of a permanent establishment is not sufficient to address base erosion and profit shifting strategies. Action 7 sets out international guidelines on permanent establishments with respect to the following:

***International standards on
commissionaire arrangements***

OECD notes that dependent agent permanent establishment status (article 5 (5) of the OECD Model Tax Convention) can be circumvented in civil law countries through commissionaire arrangements, whereby a contract concluded by an agent is not in the principal's name, so it binds only the agent even though the principal will supply the goods or services on the terms agreed to by the agent⁵ To prevent the artificial avoidance of permanent establishment status, an international standard has been developed under action 6 to the effect that, where an intermediary's activities in a country are intended to result in regular conclusion of contracts by a foreign enterprise, that enterprise is deemed to have a permanent establishment in that country unless the intermediary performs those activities in the course of an independent business. In African countries where civil law is applied, commissionaire arrangements may be a concern, but they are not a major concern for African countries with a common law background (mainly former British colonies), where the commissionaire concept is not applied. Nevertheless, there could be cases in which commissionaire proxies are employed to escape permanent establishment status, which could pose a base erosion and profit shifting risk (Oguttu, 2016b). It should be noted that, even though action 7 of the OECD base erosion and profit shifting project concentrated only on commissioner-dependent agency issues, there are other dependent agency issues that are pertinent to developing countries, which are covered in the United Nations Model Double

Taxation Convention but not in the OECD Model Tax Convention. These are discussed in section 5 under the United Nations alternative approaches.

***International standards on splitting
contracts***

Article 5 (3) of the OECD Model Tax Convention provides for a special permanent establishment rule for building sites, construction and installation projects that last for more than 12 months. Permanent establishment status can be circumvented if service contracts owned by the same group company are split into several parts that cover lesser permanent establishment time limits. Manipulating permanent establishment time limits is a major concern for Africa countries, especially for construction and assembly activities in which, as a result of modern technology, a very short time period could be spent in the source country and still result in a substantial profit for the foreign enterprise. Article 5 (3) (a) of the United Nations Model Double Taxation Convention deviates from the OECD Model Tax Convention in that it also covers "assembly projects or supervisory activities in connection therewith", and the time limit is 6 months (unlike the 12 months in the OECD Model Tax Convention). It would therefore appear to be in the interest of African countries to insist on having a provision along the lines of article 5 (3) (a) in the treaties that they sign. Some African countries have even managed to negotiate treaties with lesser time limits, arguing that even the six-month time limit is still lengthy and could be manipulated to avoid taxation in source countries (e.g., article 5 (3) (a) of Uganda's treaty with the Netherlands provides for a four-month time limit). Nevertheless, the OECD base erosion and profit shifting project does not address the inconsistency in the duration required to create a taxable presence, a matter that continues to create much uncertainty (Ernst & Young, 2012). To prevent the artificial avoidance of permanent establishment status, the principal purpose test rule recommended by OECD under action 6 will be beneficial to African to address permanent establishment abuse when contracts are split

⁵ See Zimmer Ltd., French Supreme Court, No. 3047 15, 31 March 2010.

between related enterprises. In this regard, it will be in the interest of African countries use article 5 (3) (a) of their treaties of the United Nations Model Tax Convention rather than the corresponding Article of the OECD convention or, better still, to negotiate lower time limits as the above-mentioned countries have done (United Nations, General Assembly, 2015c, ; Oguttu, 2016b).

International standard to curtail abuse of exclusions to the permanent establishment concept in articles 5 (a)-(f)

Under articles 5 (a) and (b), of the OECD Model Tax Convention, permanent establishment status does not apply if facilities are used solely for the “delivery” of merchandise belonging to the enterprise or if an enterprise maintains a stock of merchandise solely for the purpose of “delivery”. An enterprise can therefore maintain a very large warehouse from which its employees deliver goods that the enterprise sells online and still avoid permanent establishment status. Likewise, a stock of goods for prompt delivery, which can facilitate big sales, can avoid permanent establishment status. However, in the United Nations Model Double Taxation Convention, the word “delivery” is not used, and this implies that a “warehouse” used for delivery purposes can create a permanent establishment if the requirements of article 5 (1) are met (Lennard, 2009). It would be in the interest of African countries to negotiate this article on the basis of the United Nations Model Double Taxation Convention, given that it more closely reflects their interests. Article 5 (4) (c) of the OECD Model Tax Convention excludes from the permanent establishment concept the “maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose processing by another enterprise”. This implies that a stock of goods maintained and processed by a toll manufacturer for delivery to a multinational enterprise of which it is a part would not constitute a permanent establishment (Oguttu, 2016b). Article 5 (4) (d) excludes from the permanent establishment concept “the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise”. In digital business

models, however, multinational enterprises can collect information for the enterprise and disguise it by repackaging it into reports prepared for these enterprises, thereby avoiding permanent establishment status. Articles 5 (e) and 5 (f) prevent an enterprise from being taxed in the other State if it carries on activities only of a purely preparatory or auxiliary character. An example is the maintenance of a fixed place of business solely for the purpose of advertising or the supply of information or for scientific research (Holmes, 2007). In the modern world, however, real value can be created through scientific research and the development and testing of products and services in continuous processes of innovation and improvement. These processes, however, can escape permanent establishment status. Multinational enterprises can also avoid permanent establishment status by fragmenting activities and taking advantage of article 5 (4) (f), which excludes from the permanent establishment concept the maintenance of a fixed place of business for any combination of activities in articles 5 (4) (a)-(e), “provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character”. The wide application of article 5 (4) (f), however, which covers a combination of activities, often creates a nexus in the source country that is neither preparatory nor auxiliary. OECD acknowledges that business activities that were previously considered to be merely preparatory or auxiliary in nature may be core business activities of an enterprise. In action 7, an international standard has been developed that will result in the modification of article 5 (4) to ensure that each of the exceptions to the permanent establishment concept are restricted to activities that are of a preparatory or auxiliary character. An anti-fragmentation provision will also be added to article 5 (4) to deny the exceptions to the permanent establishment concept in which complementary business activities are carried on by associated enterprises at the same location, by the same enterprise or by associated enterprises at different locations. A permanent establishment would be therefore considered to exist if these activities were taken together. Such activities would constitute complementary functions that are part of a cohesive business operation. These changes are

of paramount importance to African countries that are interested in ensuring that the definition of a permanent establishment acknowledges the structure of twenty-first century business models.

International standards to ensure that transfer pricing outcomes are in line with value creation (actions 8 to 10): a priority concern for African countries

The term transfer-pricing describes the process by which related entities set prices at which they transfer goods or services between each other. The term “abusive transfer pricing” refers to the manipulation of prices in order to reduce profits or increase profits artificially or cause losses and avoid taxes in a specific country (Oguttu, 2006b). OECD recommends the use of the arm’s-length principle in article 9 (1) of the Model Tax Convention to curb transfer pricing. Many African countries, however, do not have comprehensive transfer pricing legislation and, in general, rely on general anti-avoidance rules to prevent transfer pricing schemes (PricewaterhouseCoopers, 2012). By 2016, the following African countries had enacted transfer pricing legislation: Algeria, Angola, Cameroon, Congo, Democratic Republic of the Congo, Egypt, Equatorial Guinea, Gabon, Ghana, Kenya, Malawi, Morocco, Namibia, Nigeria, Senegal, South Africa, Tunisia, Uganda, the United Republic of Tanzania and Zambia (Ernst & Young, 2016 ; PriceWaterhouseCoopers, 2017a). There is, however, a general lack of skills among tax administrations in conducting a transfer pricing analysis, which is crucial in understanding the behaviour of multinational enterprises (African Tax Administration Forum, 2014). Because most African countries do not have formal transfer pricing guidelines, they rely on the OECD transfer pricing guidelines (KPMG 2009), even though African countries are not OECD member countries. Indeed, the High Court in the Kenyan case of Unilever Kenya Limited v. Commissioner of Income Tax⁶ was prepared to refer to the guidelines. Applying these guidelines in Africa, however, is rather challenging because it is difficult to find African comparables, given

that there are very few organised companies in any given sector and there are very few African benchmarking databases (Oguttu, 2015c).

When assessing the arm’s-length criteria of related party transactions, African countries tend to accept European comparables (PricewaterhouseCoopers, 2012), which have to be adjusted to suit developing country market business. Further problems exist in gathering taxpayer information owing to the absence of documentation requirements or the inability to enforce existing requirements and the lack of capacity and technical expertise to process the data (ATAF 2015). African countries need to establish well-resourced transfer pricing units that are intended to secure access to a global comparables databases (ATAF 2016). In order to ensure that multinational enterprises do not misapply the transfer pricing rules, OECD revised its transfer pricing guidelines with respect to the transfer pricing of intangibles (action 8), risks and capital (action 9) and other high-risk transactions (action 10) to ensure that outcomes are in line with value creation (Organization for Economic Cooperation and Development, 2013a). There are however, general concerns that, although the revisions could strengthen the powers of tax authorities, they will make transfer pricing guidelines more complex and difficult to administer, in particular for developing countries. Strengthened transfer pricing enforcement based on subjective and discretionary rules will also lead to increased conflicts (Picciotto, 2016). Section 5 provides a consideration of the merits of “unitary taxation” with formulary apportionment as an alternative to the arm’s-length principle.

Action 8: transfer pricing of intangibles

Applying the arm’s-length principle to intangibles is challenging owing to their unique nature, the lack of comparables and insufficient international guidance on the definition, identification and valuation of intangibles (Organization for Economic Cooperation and Development, 2013a). Under action 8, changes were made to chapter VI of the transfer pricing guidelines, which now defines an “intangible” as an asset that is not

⁶ Income Tax Appeal No. 753 of 2003.

physical or financial, is capable of being owned or controlled for commercial purposes and the use or transfer of which between independent parties in comparable circumstances can be compensated. An intangible need not be one for accounting-, tax- or treaty-withholding purposes, nor does it need be legally protected or separately transferable. Examples of intangibles are patents, know-how and trade secrets, trademarks, trade names and brands, rights under contract or government licences, goodwill and ongoing concerns. Market conditions that are not capable of being owned or controlled, such as location savings, local market features and multinational enterprise group synergies, are not intangibles. They are comparability factors, which may affect the arm's-length price and should be taken into account in a comparability analysis. The guidelines clarify that legal ownership alone does not always entitle a right to all (or any) of the return from exploiting the intangibles. Group companies performing value-creating functions relating to the development, enhancement, maintenance, protection and exploitation of the intangibles should be entitled to an appropriate remuneration reflecting the value of their contributions. Although, internationally, most intangibles are owned by people in developed countries, there are many intangibles that have developed in Africa, but the ownership of these has been migrated to developed countries or to tax haven jurisdictions. An example is the famous SABMiller case, which asserts that many of the company's local beer brands, such as Castle, Stone and Chibuku, were invented in African countries, including South Africa, Ghana and Zambia, but that these brands were sold by the London-based beer company SABMiller to its subsidiary in the Netherlands to take advantage of the latter's favourable tax rules, which permit companies to pay low taxes on royalties by using planned licensing structures. The result was a loss of revenue for the African countries in question, given that the taxing rights of intellectual property now belong to the jurisdiction where the owner of the intellectual property resides (ActionAid, 2012). African countries that consider the transfer pricing of intangibles a base erosion and profit shifting risk should ensure that they adopt the above OECD guidance. Under action 8, OECD also developed transfer pricing guidance on cost

contribution arrangements. These are contractual arrangements among business enterprises to share the contributions and risks of the joint development of intangibles or tangible assets and services in order to create benefits for the participants. Chapter VII of the OECD transfer pricing guidelines ensures that cost contribution arrangements produce outcomes consistent with value creation. Owing to the low economic development of most African countries, these arrangements rarely arise as a base erosion and profit shifting concern.

Action 9: Contractual allocation of risk

Increased globalization, mobility of capital and technological developments have resulted in supply chain restructuring of many multinational enterprise business models and operations to ensure business efficiencies of centralized planning, procurement and the holding of intellectual property. Nevertheless, supply chain restructuring also makes it easier for these enterprises to shift profits between tax jurisdictions, in that they can enter into contractual arrangements whereby they allocate functions, assets and risks to other group members operating in a low-tax jurisdiction in a way that minimizes the overall tax burden of the enterprise but does not fully reflect the actual conduct of the parties. From a transfer pricing perspective, a party's assumption of risk can affect the arm's-length pricing of that transaction, which developing countries often find difficult to challenge (Oguttu, 2015a).

In action 9, international standards were developed to prevent the misallocation of risk between associated enterprises and to ensure that transfer pricing outcomes reflect economic realities, that they are not based on contractual arrangements, that the actual contributions of the parties and the risks actually assumed are taken into account and that transactions that make no commercial sense are not recognized. Risks contractually assumed by a party that has no control over such risks or that does not have the financial capacity to assume the risks should be allocated to the party that actually does so. If a capital-rich member of the group acts as a cash box but does not control the financial

risks associated with its funding, it should be entitled only to no more than a risk-free return. This guidance will benefit African countries that are often affected by supply chain business restructurings.⁷ In effect, if the economic realities show that the subsidiary in Africa is that one that, in fact, assumes risks, that subsidiary must be appropriately compensated for doing so.

Action 10: other high-risk transactions (clarity on applying the profit split method in global value chains)

The “transaction profit split method” is one of the methods used to determine an arm’s-length price under the OECD transfer pricing guidelines whereby the combined profit of the connected parties in a controlled transaction is identified and split between them (OECD Transfer Pricing Guidelines, 1995 para 131). Normally, the transaction profit split method is a method of last resort because it relies on gaining access to worldwide group data, which may be difficult to obtain. OECD acknowledges that, if properly applied, the method can provide transfer pricing solutions for unique intangibles and highly integrated operations, given that it is straightforward for taxpayers to apply and tax administrations to evaluate. In action 10, OECD developed guidance on appropriate application of the method. For African countries that do not have databases to determine an arm’s-length price, especially for highly integrated transactions, following the envisaged guidelines on the transaction profit split method would be helpful.

Action 10 also dealt with protection against base-eroding management fees and head office expenses

Multinational enterprises often offer intragroup management services, the cost of which may be borne by the parent or one of the group members. The enterprises, however, often claim excessive deductions for management fees and head office expenses, which poses a priority base erosion and profit shifting risk for African countries. To protect their tax bases, most African countries

levy withholding taxes on management/service fees. Accordingly, some African countries have signed treaties with a service fee article, contrary to the OECD Model Tax Convention. This matter, however, was not addressed in the base erosion and profit shifting project. Nevertheless, the United Nations came up with a technical service fee article which will be included in the next update of its Model Double Taxation Convention, which will be instrumental for African countries in curtailing base-eroding service fees (see section 5). In action 10, OECD chose to address the concern from a transfer pricing perspective. Revisions were made to chapter VII of the transfer pricing guidelines comprising a simplified elective method for determining arm’s-length charges for common low value-adding intragroup services, which require limited profit mark-ups on costs and exclude detailed benchmarking of the benefits received. Low value-adding services are those that are supportive in nature, not part of the core business of the multinational enterprise, do not require the use of unique intangibles and do not involve the assumption of significant risk. Examples are accounting and auditing, processing and management of accounts, human resources, monitoring and compilation of data, information technology, public relations support, legal and tax obligations and services of an administrative or clerical nature. Where excessive charges for intragroup management services are a major base erosion and profit shifting challenge, a threshold can be applied so that a full transfer pricing analysis is performed for services that exceed the threshold. African countries should support this simplified elective approach, given that it would reduce transfer pricing costs for taxpayers and administrative burdens for revenue authorities.

Under action 10, guidance on the transfer pricing of commodities was also provided

This matter was initially not part of the OECD base erosion and profit shifting project, but developing countries identified commodities as a critical base erosion and profit shifting concern, especially for resource-rich countries. Owing to a lack of data and the shortage of skilled capacity, many developing countries face challenges in

⁷ ECA’s analysis based on UNCTAD 2017 and UNCTAD 2017a.

ensuring that minerals are exported at a fair price, so they lose substantial amounts of revenue from transfer pricing of commodities by multinational enterprises, even though there is little attention to this problem (International Monetary Fund, 2014b). The main risks include fragmentation of the supply chain using intermediary marketing and sales entities, excessive debt deductions through thin capitalization, intragroup charges of services and royalty payments (Gosai, 2011). These are compounded by the complexity of the mining sector, which can involve hard-to-value intangibles, a lack of industry-specific knowledge and inexperience of tax administrations (International Mining for Development Centre, 2014). Developing countries, especially those in South America, therefore apply the so-called “sixth method”, an objective standard, whereby publicly quoted commodity prices are used as a guide to price commodities (Ibid.). Such quoted prices are easy to administer because they do not involve subjective judgments or a detailed examination of facts and circumstances. In Africa, the sixth method has not been applied presumably because of a lack of international guidance on its use. Under action 10, OECD devised guidance to the effect that quoted prices can be used under the “Comparable uncontrolled price” method as a reference to determine the arm’s-length price for the controlled commodity transaction and that reasonably accurate comparability adjustments should be made to ensure that the economically relevant characteristics of the controlled and uncontrolled transactions are sufficiently comparable. This guidance has been criticized, however, given that the comparable uncontrolled price method involves the complexities of the arm’s-length principle, which is challenging for developing countries to apply, as mentioned earlier. Owing to the challenges that African countries face in applying the arm’s-length method, it has been suggested that they should consider adopting the sixth method. It is, however, advisable push for international guidance on the use of this method and embark on its use in regional blocks with larger markets for multinational enterprises investing in the region.

3.3.4 Analytical reports

The base erosion and profit shifting project also devised analytical reports on some base erosion and profit shifting concerns.

Address the tax challenges of the digital economy: action 1

The digital economy is the result of a transformative process brought by ICT, which has made technologies cheaper, more powerful and widely standardized, improving business processes and bolstering innovation across all sectors of the economy. OECD notes that, because all sectors of the economy are increasingly using digital technologies (and as such are themselves becoming increasingly digital), it would be difficult, if not impossible, to separate the digital economy from the rest of the economy for tax purposes. While the digital economy and its business models do not generate unique base erosion and profit shifting issues, some of its key features exacerbate base erosion and profit shifting risks. With respect to direct taxes, the digital economy raises challenges relating to nexus, data and characterization of income. In digital economy business models, a non-resident company may interact with customers in a country remotely through a website or other digital means (e.g., an application on a mobile device) without maintaining a physical presence in the country. Given that the domestic laws of most countries require some degree of physical presence (e.g., a permanent establishment) before business profits are subject to taxation, a non-resident company may end up not being subject to tax in the country in which it has customers. Although all the base erosion and profit shifting action points may be relevant to curtailing base erosion and profit shifting in the digital economy, OECD identified specific actions as particularly relevant. Action 3, which requires enacting controlled foreign company legislation, will address taxing mobile income from digital goods and services. Action 7 on preventing artificial avoidance of permanent establishment status will ensure that digital activities that were previously considered preparatory or auxiliary (and excluded from the permanent establishment concept) are now considered core activities

of a digital enterprise and thus taxable. All the exclusions to the permanent establishment concept in article 5 (4) of the OECD Model Tax Convention will be modified to ensure that each exception is restricted to activities that are otherwise of a “preparatory or auxiliary” character. Many base erosion and profit shifting structures in the digital economy involve the transfer of intangibles or rights in intangibles to tax-advantaged locations. Actions 8 to 10 address these issues by providing guidance to ensure that transfer pricing outcomes are in line with value creation. OECD also considered some options to determine a nexus for the digital economy, namely, a new nexus in the form of a significant economic presence, a withholding tax on certain types of digital transactions and an equalization levy. It recommends that countries could introduce any of these three options in their domestic laws as additional safeguards against base erosion and profit shifting, provided they respect the obligations in their double taxation agreements.

With respect to indirect taxes, the digital economy creates challenges, especially when goods, services and intangibles are acquired by private consumers from suppliers abroad. OECD recommends that countries apply the international value added tax and goods and services tax guidelines and consider the introduction of the collection mechanisms included therein. In particular, the implementation of “business to consumer” guidelines would allow countries where customers are resident to charge a value added tax/goods and services tax on the sale of digital content from abroad, thus ensuring that consumption taxes are levied in the market country. OECD also provides guidelines on place of taxation for business-to-business supplies of services and intangibles, which can curtail base erosion and profit shifting concerns, in particular with regard to remote digital supplies to exempt businesses. African countries should amend their value-added tax legislation in line with these guidelines. They should also ensure that enterprise-rendering electronic services register as value added tax vendors locally so that the tax can be charged on the supply of those services.

The borderless nature of the digital economy also poses administrative issues regarding the identification and verification of businesses and the determination of their extent of activities. The OECD notes that the international exchange of information and assistance in the collection of taxes will help to resolve these matters, especially for countries that have signed the OECD Convention on Mutual Administrative Assistance in Tax Matters, double tax treaties (article 26 of treaties based on the OECD Model Tax Convention or the United Nations Model Double Taxation Convention) and tax information exchange agreements that are signed with countries that do not have tax treaties (typically tax haven jurisdictions) (Langer, 2005). Given that the digital economy continues to evolve and develop, OECD will continue to work on these issues and monitor digital developments over time.

Establish methodologies to collect and analyse data on base erosion and profit shifting and the actions to address it: (action 11)

Although it is accepted that multinational enterprises engage in base erosion and profit shifting activities, available data are unable to draw a clear distinction between base erosion and profit shifting-related activity and genuine economic activity. Existing empirical studies confirm, however, that, while the occurrence of profit-shifting is significant in scale, it is likely to increase and that it creates adverse economic distortions. Currently, the scale of base erosion and profit shifting in Africa and the economic impact thereof are not known owing to limitations of the available data, both in terms of quality and quantity. A better understanding of the economic effects of base erosion and profit shifting on developing countries is important for the design of tax policies. In action 11, OECD notes that it is critical that countries have the tools and data available to measure and monitor base erosion and profit shifting and to evaluate the impact of the countermeasures developed under the base erosion and profit shifting project. Accordingly, OECD developed six indicators of base erosion and profit shifting activity that highlight base erosion and profit shifting behaviours using

various sources of data, employing different metrics and examining different base erosion and profit shifting channels. When combined and presented as a dashboard of indicators, they confirm the existence of base erosion and profit shifting and its continued increase in scale in recent years. Action 11 also provides tax administrations and tax policy officers a toolkit of methodological approaches that could be used to estimate the fiscal effects of base erosion and profit shifting countermeasures and formulas for calculating base erosion and profit shifting indicators. Given developing countries' greater reliance on corporate income tax revenues and that the impact of base erosion and profit shifting on developing countries (as mentioned earlier), as a percentage of GDP, is higher than for developed countries, it is important that African countries adopt the OECD recommendations in action 11.

Develop a multilateral instrument (action 15)

Action 15 of the base erosion and profit shifting action plan provides for the development of a multilateral instrument to enable countries to implement OECD's recommendations as to how to stop base erosion and profit shifting through tax treaty abuse. OECD issued the instrument in November 2016. It believes that the instrument is feasible, given that countries can draw from the experience that they have gained through the OECD Convention on Administrative Assistance in Tax Matters. Although some African countries have signed the Convention (see discussion above on action 13), many African countries have not gained experience on how a global multilateral tax convention operates. Significant work in administrative capacity-building is still required of them if they are to reap the full benefits of the Convention. Administrative capacity will once again be a major hindrance for many African countries to be part of the instrument. On the basis of the number of double taxation agreements signed to date by each African country, its tax treaty policy and the approach being adopted by trading partners, consideration should be given as to whether signing the instrument is a priority concern. For African countries that have a wide network of

tax treaties (e.g., South Africa, which has more than 75 double taxation agreements), it may be expedient to consider signing the instrument (subject to reservations deemed necessary), given that the costs and time that it would take to renegotiate all those agreements may not be feasible. For African countries that have signed few double taxation agreements, (only 10 to date), consideration should be given to whether it would be better for them to renegotiate specific treaties that raise major base erosion and profit shifting risks, rather than rushing into signing the instrument, the ramifications of which are not yet clear. This is especially so for countries such as Uganda, which, in 2014, announced that it had suspended all its ongoing double taxation agreements negotiations pending a review of the treaty terms that it should seek in such negotiations (Ladu, 2014). It should be noted that the instrument is based on the provision in the OECD Model Tax Convention, while many African countries have instead signed treaties based on the United Nations Model Double Taxation Convention, which has some provisions favouring developing countries that are not in the OECD Model Tax Convention. It is not clear how developing country interests in treaties signed based on the United Nations Model Double Taxation Convention will be canvassed in the opt-in and opt-out provisions of the instrument. It is, however, notable that, as of 22 March 2018, the multilateral instrument had been signed by 78 jurisdictions, of which 11 are African countries: Burkina Faso, Cameroon, Côte d'Ivoire, Egypt, Gabon, Mauritius, Nigeria, Senegal, Seychelles, and South Africa and Tunisia, with Algeria having expressed intent to sign the convention (Organization for Economic Cooperation and Development, 2017c and 2018f). The signatories accepted the application of some measures of the instrument on their double taxation agreements subject to some reservations on a case-by-case basis (Organization for Economic Cooperation and Development, not dated (a)). With the uncertainties that prevail on how the instrument will apply in practice, and the fact that the United States did not sign the instrument, it is advisable for African countries to adopt a wait-and-see approach before they commit themselves to it. The convention will enter into force on 1 July 2018 in Austria, Isle of Man, Jersey, Poland,

Slovenia and any other jurisdictions that ratify the Convention (Organization for Economic Cooperation and Development, 2018g).

Conclusion

This section of the study has discussed the OECD measures to curtail base erosion and profit shifting, from an African perspective. Even though African countries are not bound to follow the OECD recommendations, and even though the primary focus of the base erosion and profit shifting project largely addresses the base erosion and profit shifting concerns of its member countries, it is in the interest of African countries to engage with the base erosion and profit shifting measures that are relevant to them. The international focus on base erosion and profit shifting and the support offered by international bodies provides an opportunity for African countries to enact up-to-date anti-avoidance laws and to improve their administrative capacity. Countries need to review their current tax laws to determine which base erosion and profit shifting measures they should implement.

Section 4: Addressing base erosion and profit shifting at the national level: country studies

This section covers three case studies of African countries (Cameroon, South Africa and the United Republic of Tanzania) to gauge the impact of base erosion and profit shifting on their economies, previous measures taken to curtail it and to what extent they have adopted any of the OECD measures that are of priority to them. Before discussing the base erosion and profit shifting matters, a brief overview is given of the economic circumstances of the country that could affect domestic resource mobilization.

4.1 United Republic of Tanzania

The United Republic of Tanzania's (also URT or Tanzania) economic strength lies in the diversity of its exploitable natural resources. Agriculture is the main contributor to its economy. Its wildlife and geography boosts its growing tourism industry. The mining and energy sectors also draw increasing amounts of global investment in gold mining, and its recent discoveries of natural gas reserves (URT, 2002, 2008, and 2014). The country's annual GDP growth rate averaged approximately 7 per cent during the period 2011-2015, making it one of the fastest-growing economies in the world.⁸ Notwithstanding the above, according to the most recent ECA estimates, the country has been identified as one of the top 10 in Africa with a high magnitude of illicit outflows through trade re-invoicing.⁹ In the Eastern African region, it was ranked second behind Ethiopia in terms of illicit financial outflows through trade re-invoicing. In 2017, Global Financial Integrity estimated cumulative illicit financial flows from the United Republic of Tanzania during 2005-2014 at \$3.5 billion, with an annual average of \$349 million (Spanjers and Salomon 2017). The most recent ECA estimates mentioned above appear to show that, at least up to 2015 (the last year for which the ECA estimates are available), trade mis-invoicing was an important channel through which illicit financial flows left the country, with estimated net

illicit outflow of \$2.5 billion through this channel in 2015 alone. . A significant proportion of ivory reaching international markets, especially in Asia, is derived from elephant poaching in the country. Similarly, many studies confirm that the smuggling of gemstones, mainly tanzanite and gold, is quite rampant. The country has nevertheless made a commitment to improving transparency through the Open Government Partnership and the Extractive Industries Transparency Initiative (Open Government Partnership, 2012). It is also a member of the Eastern and Southern Africa Anti-Money Laundering Group (2009).

Most tax revenue in the United Republic of Tanzania is derived from personal income tax and corporate income tax, which account for approximately 82 per cent of total taxes on income, followed by the value added tax on domestic services and excise taxes.

⁸ ECA's calculations based on National Bureau of Statistics (NBS) Tanzania, 2017

⁹ ECA calculations based on Mevel 2017. Member countries of the Southern African Customs Union were not included in this ranking since illicit financial flows were estimated for the bloc as a whole rather than individual member countries.

Table 1: Share of specific tax revenue as a percentage of total tax revenue in the United Republic of Tanzania (mainland and Zanzibar) (Per cent)

Share of specific tax revenue to total tax revenue (mainland)					
	2011/12	2012/13	2013/14	2014/15	2014/15
Pay-as-you-earn	16.9%	17.4%	16.5%	16.4%	17.0%
Corporation tax	11.7%	12.9%	15.0%	11.1%	10.4%
Individuals	1.0%	0.9%	0.9%	1.0%	1.1%
Domestic value added tax	14.7%	14.4%	13.3%	14.2%	13.9%
Excise duty on imports	8.8%	8.7%	7.7%	8.6%	9.7%
Value added tax on Imports	16.2%	15.1%	13.5%	14.5%	13.1%
Share of specific tax revenue to total tax revenue (Zanzibar)					
	2011/12	2012/13	2013/14	2014/15	2014/15
Pay-as-you-earn	19.2%	19.4%	20.0%	20.8%	19.7%
Corporation tax	7.2%	8.6%	6.7%	7.5%	8.6%
Import duties	24.9%	24.0%	24.7%	23.2%	20.4%
Value added tax on imports	27.1%	25.8%	28.0%	27.0%	24.3%

Source: Tanzania Revenue Authority (2016).

Most of the corporate tax revenue collection in the United Republic of Tanzania is from large taxpayers, often foreign enterprises, based in Dar es Salaam, which contribute 88 per cent of tax revenue. The extractive industries sector is central to base erosion and profit shifting and related illicit outflows of capital from the country and is a major area in need of reform. One of the main causes of the loss in revenue is the plethora of tax incentives and exemptions that complicate the tax system and leave it susceptible to corruption. The extractive industries sector is central to base erosion and profit shifting and related illicit outflows of capital from the country and is a major area in need of reform. The multinational enterprises operating in the mining sector are offered attractive tax incentives, which has resulted in a massive loss in revenue from mining. The multinational enterprises operating in the minerals sector, which are 100 per cent foreign-owned, pay royalty fees of 5 per cent (a recent increase from 3 per cent), while they are exempted from paying taxes for up to 20 years. This is compounding the practice of companies changing names and registering as a new company at the end of tax holiday so that they continue to benefit from further tax incentives. The reliance on royalties is precarious, given that the Government does not always have full control

over the operations of those companies. Some multinational enterprises in the mining sector own unregulated small ports, so the nature and quantity of exports and, subsequently, actual earnings are largely unknown. There is therefore a risk that the levels of royalties paid are only a proportion of the actual amount due. The African Development Bank (2010,) notes that the level of exemptions has contributed not only to undermining efficiency and effectiveness of gains resulting from administrative reforms, but also to the substantial loss in revenue, probably accounting for most of the country's tax gap. IMF has called upon the Government to raise taxes on the mining companies. It has also called for withholding taxes on interest paid on foreign currency loans, limits on the deductibility of debt financing for income taxes and a tightening of provisions for investment allowances for exploration and development (International Monetary Fund, 2010). It, however, remains unclear what steps the Government will take to reduce tax incentives granted to mining companies and businesses operating in its export processing zones and its special economic zones. There therefore remain further steps that the country can take towards improving tax collection. It does not also have effective systems in place for tax information exchange with other

countries (Tanzania Episcopal Conference and others, 2017; Global Financial Integrity, 2010). The Government has not signed the Convention on Mutual Administrative Assistance in Tax Matters (Organization for Economic Cooperation and Development, 2017b). The country has had limited involvement in the OECD base erosion and profit shifting consultation process and had, at the time of writing, reportedly not implemented any of the OECD's base erosion and profit shifting measures. The Government signalled that it would take a hard-line approach to reduce tax evasion and increase domestic tax revenue by 15 per cent during the period 2016–2017. It has also come up with tax reform measures to expand the tax base and raise more revenue for public expenditure.¹⁰ The discussion below highlights the tax policy reforms and legislation enacted during the past few years that can be instrumental in curtailing certain base erosion and profit shifting activities. Recommendations are also provided on how the country can enhance its current legislation in the light of the OECD base erosion and profit shifting measures.

Action 1: Address the tax challenges of the digital economy

With regard to indirect taxes, the Value Added Tax (VAT) Act, which entered into force on 1 July 2015, includes special rules for specific sectors, such as insurance and telecommunications, which can be instrumental in curtailing base erosion and profit shifting in the digital economy. The Act provides for a reduction in tax exemptions and special reliefs in order to improve government revenue collection. It also provides for widening the tax base to cover most economic activities in the market and for a platform for more scrutiny on various controversial issues (Becker, 2015). It is recommended that further reforms to be enacted in the light of recommendations in the OECD's base erosion and profit shifting action 1 to ensure that the challenges that the digital economy poses to the collection of a value added tax are addressed.

Action 2: Neutralize the effects of hybrid mismatch arrangement

This is not a priority base erosion and profit shifting concern for now.¹⁰

Action 3: Strengthen controlled foreign company rules

Residents are taxed on a worldwide basis (section 6 of the Income Tax Act 2004). The country has controlled foreign company rules (sections 73-76 of the Act, under which the attributable income less distributions from a controlled foreign trust or company is included in the income of a "controlling person."). The country should consider strengthening its controlled foreign company rules in the light of the best practice recommended in action 3.

Action 4: Limit base erosion via interest deductions and other financial payments

This is a priority base erosion and profit shifting concern. To protect its base, the country levies a withholding tax on interest paid to non-residents at a rate of 10 per cent (section 86 of the Income Tax Act). It also has thin capitalization rules, whereby interest deductions for payments made by an exempt controlled resident entity (as defined) is limited to the sum of interest income plus 70 per cent of total income, excluding interest income and interest expenses. Non-deductible amounts may be carried forward (section 12 (2) and (3) of the Act). Taxpayers are also subject to a general anti-avoidance rule (section 35 of the Act) when the main purpose of an arrangement is the avoidance or reduction of tax liability. Specific rules negate income splitting. A company registering tax losses for three consecutive years becomes liable to a minimum tax at 0.3 per cent on turnover. It is recommended that the country evaluate the effectiveness of the current provisions in the light of the OECD recommendations in action 4.

Action 5: Counter harmful tax practices more effectively, taking into account transparency and substance

The country does not appear to have a preferential tax regime that encourages harmful

¹⁰ Based on ECA interviews with individuals in the United Republic of Tanzania.

tax practices, as described in action 5 of the base erosion and profit shifting project. The granting of tax incentives can be, however, a harmful tax practice, which can lead to self-imposed base erosion and profit shifting, a race to the bottom and resultant loss in revenue for all countries in the region (Tanzania Episcopal Conference and others, 2017). The country should review the base-eroding tax incentives for its special economic zones and export processing zones, as well as the tax exemption package for mining companies.

Action 6: Prevent treaty abuse

This is a priority base erosion and profit shifting concern for the country. The main anti-treaty shopping provision used there is the “beneficial ownership” provision.¹⁰ It is recommended for the country to adopt the OECD minimum standards recommend in action 6 of the base erosion and profit shifting report. It should also enact domestic provisions to prevent treaty abuse.

Action 7: Prevent artificial avoidance of permanent establishment status

Non-residents are taxed on income sourced in the country. The Income Tax Act defines a permanent establishment as a place in which a person carries on business and includes: (a) a place in which a person is carrying on business through an agent, other than a general agent of independent status acting in the ordinary course of business; (b) a place in which a person has used or installed, or is using or installing substantial equipment or substantial machinery; and (c) a place in which a person is engaged in a construction, assembly or installation project for six months or more, including a place in which a person is conducting supervisory activities in relation to such a project. Division II of the Act (sections 70-72) deals with the taxation of permanent establishments. Branches of foreign corporations (permanent establishments) are taxed in the same way as resident companies (30 per cent corporate tax rate), with an additional tax on branch profits. Section 34 of the Act deals with income-splitting issues. It is recommended that the country adopt the tax treaty international standards regarding permanent establishments,

as set out in action 7 of the base erosion and profit shifting report. Given that some of the country's treaties are based on the United Nations Model Double Taxation Convention, efforts should be made to ensure the new United Nations “service fees article” is incorporated into future treaties (see discussion in Section V).

Actions 8-10: Assure transfer pricing outcomes are in line with value creation

This is a priority base erosion and profit shifting concern in the country. Transfer pricing provisions are set out in section 33 of the Income Tax Act. Taxpayers are required to apply the arm's length principle to transactions between associates, both resident and non-resident. On 7 February 2014, the country enacted income tax transfer pricing regulations, which apply to a controlled transaction if a person who is party to the transaction is located in and subject to tax in the country and the other party to the transaction is located in or outside it. The regulations define controlled transactions as transactions between associates and associates with direct or indirect control of 50 per cent or more of the voting power. Special rules apply for intra-group services, intangible property and intra-group financing. The regulations also stipulate the records and documents that should be included in transfer pricing documentation. Following the issuance of the regulations in 2014, the Tanzania Revenue Authority developed transfer pricing guidelines, which are based largely on the OECD guidelines and the United Nations Practical Manual on Transfer Pricing for Developing Countries. The country's transfer pricing guidelines set forth the following objectives: (a) the rationale for the adoption of the arm's-length principle; (b) the framework upon which application of the acceptable transfer pricing method is based; (c) the general principles of comparability that form the foundation of transfer pricing analysis; (d) documentation by taxpayers that should be prepared and maintained in support of their determination of the arm's-length price; and (d) the treatment of intra-group transactions (Ernst & Young, 2014a). Although its guidelines are based on the OECD guidelines and the United Nations Practical Manual, the Act prevails if there are any inconsistencies.¹⁰ It is noted that further reforms

in the light of the recommendations contained in OECD's base erosion and profit shifting actions 8-10 will go a long way in ensuring that the transfer pricing challenges that the country is facing are addressed.

Action 11: Establish methodologies to collect and analyse data on base erosion and profit shifting

Owing to capacity challenges, this is not a priority issue in the country.¹⁰

Action 12: Require taxpayers to disclose their aggressive tax planning arrangements

The country has disclosure requirements, which must be made in the return of income of an entity form. Disclosure has to be made regarding whether the entity is dormant, whether the entity is resident in the country as a result of its place of effective management, whether the entity is exclusively a tax resident of another country as a result of the application of a tax treaty, whether the entity has a participation right in a controlled foreign company and whether the return is in respect of a branch of a foreign company (South Africa Tax Guide, not dated). It is recommended that the country review its current disclosure rules in the light of the OECD recommendations contained in action 12.

Action 13: Re-examine transfer pricing documentation

This is a priority base erosion and profit shifting concern. It is recommended that domestic legislation be enacted to enable country-by-country reporting. The country needs to ensure that effective systems are in place for tax information exchange with other countries. This could include signing the Convention on Mutual Administrative Assistance in Tax Matters.¹⁰

Action 14: Make dispute resolution mechanisms more effective

The country is not committed to binding arbitration in its bilateral treaties.

Action 15: Develop a multilateral instrument

The country does not have many double taxation agreements (United Republic of Tanzania, Tanzania Revenue Authority not dated). It is however one of the Ad Hoc Group member countries that took part in the development of the OECD multilateral instrument. (Organization for Economic Cooperation and Development, 2017c). Until the uncertainties surrounding the workings of the multilateral instrument are clarified, the country should apply a wait-and-see approach and renegotiates those double taxation agreements that pose base erosion and profit shifting risks.

Other tax reform measures relevant to curtailing base erosion and profit shifting

In the United Republic of Tanzania, all taxpayers registered with the Tanzania Revenue Authority are required to verify their tax identification numbers. This measure is intended to assist in the process of installing new and modern technology to improve the taxpayer record-keeping system. The verification process requires the taxpayer to physically visit the Authority's offices to provide fingerprints. This measure could be instrumental in ensuring that all eligible taxpayers can be identified and taxed accordingly. The country also introduced a tax clearance certificate as an additional requirement for business licences in 2014 (Ernst & Young, 2016a). The Finance Act No. 16 of 2014 amended the Business Licensing Act by limiting the validity of business licences to a maximum period of 12 months from the date of issuance. The tax clearance is an additional requirement intended to ensure the proper regulation of businesses. Reforms were also introduced under the Companies Registry and the Business and Registration Licensing Agency, which required companies to file annual returns by 5 January 2015 or be subject to deregistration (Ernst & Young, 2014c). This reform could be further harnessed to develop legislation on country-by-country reporting under action 13 above. In terms of section 83 (1) (c) of the Income Tax Act, a withholding tax on service fees is levied on non-residents at a rate of 15 per cent as final tax.¹⁰ In Tanzania Revenue Authority v. Pan

African Energy,¹¹ however, the Tanzania Court of Appeal ruled that services rendered outside the country are not subject to withholding tax, regardless of the fact that payments are made by companies registered in the country. The Finance Act 2014 also brought about amendments to the capital gains tax rules in order to capture tax on disposal of shares in a Tanzanian resident entity. The amendment has the effect of widening the tax base by including in tax net gains on the sale of shares or securities held in a resident entity to counteract the tax avoidance practice of selling local companies through overseas holding companies. This domestic provision should be augmented in the country's double taxation agreements in the light of the specific treaty recommendation in base erosion and profit shifting action 6 (prevent treaty abuse), which requires countries to include in their agreement the anti-abuse provision in article 13(4) of treaties based on the OECD Model Tax Convention so as to prevent multinational enterprises from avoiding capital gains tax in the country by incorporating conduit companies in low-tax jurisdictions, which can be used to indirectly dispose of shares in assets in the country. In 2015, various laws were enacted on the oil and gas industry, which will ensure transparency in that sector. These are the Petroleum Act 2015, the Tanzania Extractive Industry (Transparency and Accountability) Act 2015 and the Oil and Gas Revenues Management Act 2015. Under the Petroleum Act 2015, the strategic oversight and management of the oil and gas economy rests with the Government, while the Ministry of Energy and Minerals has an overall supervisory mandate over policy and granting licences for oil and gas exploitation. It is also worth noting that section 44A of the Tax Administration Act 2015 introduced a requirement for entities engaged in the construction or the extractive industry to disclose to the Commissioner of Tanzanian Revenue Authority the names of all persons, the nature of work and the duration of subcontracted works in the course of the performance of their duties or business or the carrying out of any project. Sections 84, 86 and 88 of the Tax Administration Act set out penalties and fines for persons convicted of tax evasion.

4.2 Cameroon

Cameroon is the largest economy in the Central African Economic and Monetary Community (CEMAC). The country is endowed with significant natural resources, including oil and gas, high-value timber species, minerals and agricultural products such as coffee, cotton, cocoa, maize, and cassava (Cameroon, 2014). In recent years, the service sector has been the main driver of economic growth, with telecommunications, transport and financial services being particularly dynamic. Weak economic growth, low levels of investment and a worsening fiscal deficit outlook threaten the realization of the country's Vision 2035 to become an emerging economy (i.e., middle-income newly industrialized country). The country launched an emergency plan in 2015 to resuscitate its economic growth, which had been stagnant during the previous decade (African Development Bank, 2015). Domestic resource mobilization in Cameroon is significantly affected by illicit financial flows, which are encouraged by weak governance and corruption (African Development Bank, 2016). In 2015, the corruption perceptions index of Transparency International ranked Cameroon 130th of 168 countries. According to the most recent ECA estimates, Cameroon was among the top 15 countries in Africa with the highest estimated illicit financial outflows through trade re-invoicing in 2015 (with an estimated loss of \$1.4 billion) (ECA calculations based on Mevel, 2017). According to Oxfam (2016), illicit financial outflows are equivalent to 63 per cent of the country's health budget and the equivalent of its entire FDI and aid annually. A study found that the natural resources sector in Cameroon, in particular the oil and timber industry, is an important conduit of capital flight through trade misinvoicing (Ndikumana and others, 2016). The fight against corruption remains an important revenue niche on which the gains generated by the various initiatives aimed at domestic resource mobilization will be capitalized. The crackdown by the National Anti-Corruption Commission in 2013 led to the recovery of approximately \$10 million and approximately \$ 237 million for

¹¹ Civil Appeal No 146 of 2016.

Table 2: Changes in tax structure by type of tax between 2000 and 2014 (Per cent)

Taxes on income and profits (1 000)	Social Security contributions (2 000)	Taxes on payroll (3 000)	Taxes on property (4 000)	Taxes on goods and services (5 000)	Other taxes (6 000)
3.7	-1.9	1.8	-0.7	-4.2	1.3

Source: Organization for Economic Cooperation and Development, African Tax Administration Forum and African Union (2016).

2014 (Cameroon, Commission nationale anti-corruption, 2013).

Cameroon's tax-to-GDP ratio stood at 16.1 percent in 2014 (Organization for Economic Cooperation and Development, African Tax Administration Forum and African Union, 2016), higher than in previous years. In 2014, revenue from taxes on income and profits represented less than 6 per cent of GDP. The country's corporate tax rate is more than 30 per cent, and a small pool of taxpayers bear the vast majority of the tax burden, with 55 per cent of all corporate taxes in 2013 paid by only 10 companies (International Monetary Fund, 2014a). The overall tax structure has altered since 2000, showing an increase in the shares of revenue from taxes on income and profits, payroll and other taxes as a percentage of total tax revenue. The percentage shares, however, of taxes from social security contributions, goods and services and property fell (see table 2). Property income in Cameroon was related mostly to rents and royalties obtained by the Government from prospecting and extracting minerals from public lands or from harvesting government-owned farms and forests (Organization for Economic Cooperation and Development, African Tax Administration Forum and African Union, 2016).

Cameroon houses more multinational enterprises than any country in the Central and West African region. Domestic resource mobilization from these enterprises is, however, affected by the fact that those entities are often used as conduits for base erosion and profit shifting from the region (Spanjers and Foss, 2015).

Cameroon is committed to ensuring fiscal transparency and the exchange of information in tax matters. It joined the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes in 2012 and acceded to the

Convention on Mutual Administrative Assistance in Tax Matters in June 2014. Cameroon is a member of CEMAC, which ensures regional economic cooperation, and of the African Tax Administration Forum. It is also a member of the Addis Tax Initiative, a multi-stakeholder partnership of development partners and partner countries that is aimed at catalysing significant increases in domestic revenue and improving the transparency, fairness, effectiveness and efficiency of tax systems in partner countries established during the Third International Conference on Financing for Development in 2015. Cameroon's membership in these various bodies sends a strong signal that the country is among the jurisdictions directly involved in the international effort to make tax systems transparent and fair. During the period 2015-2016, the country underwent the peer review of the Global Forum, which assesses compliance with the internationally recognized standards to curb tax evasion through the exchange of information (Organization for Economic Cooperation and Development, 2015c). Cameroon received an overall rating of "largely compliant" with regard to transparency and exchange of information for tax purposes in its legal and regulatory framework, having already put in place an adequately resourced information exchange unit and drawn up the required information exchange on request manual. The peer review recognized that the country's exchange of information practice is quite new and remains to be tested (Organization for Economic Cooperation and Development, 2016b). Cameroon has also signed tax information exchange agreements with a number of jurisdictions, and several agreements are in the process of negotiation or ratification. Cameroon's tax authorities are monitoring and studying the OECD base erosion and profit shifting measures and gauging how these can be applied in the country. The large taxpayers unit is confident that country-by-country reporting

under action 13 will be of material benefit to the country. Cameroon is one of the African countries that is part of the inclusive framework that is committed to the implementation of the minimum standards in the OECD base erosion and profit shifting package (Organization for Economic Cooperation and Development, 2016a). A summary of current provisions and measures taken with respect to specific base erosion and profit shifting actions is provided below, as well as recommendations on how the Government should respond to its priority base erosion and profit shifting concerns.

Action 1: Address tax challenges of the digital economy

In order to address challenges pertaining to the digital economy, the tax administration is considering setting up a digital economy unit.

Action 2: Neutralize the effects of hybrid mismatch arrangements

This action item is not a priority concern for Cameroon. The tax administration hopes that any base erosion and profit shifting risks in this regard will be addressed by the transfer pricing unit, once operational.

Action 3: Strengthen controlled foreign company rules

Cameroon does not have controlled foreign company rules. Cameroonian companies are taxed on the territoriality principle. As a result, these companies carrying on a trade or business outside Cameroon are not taxed in Cameroon on their foreign-source profits.¹² Technical training is required before policy to adopt controlled foreign company legislation is considered. Such policy should consider best practices for the building blocks of designing effective controlled foreign company rules, as recommended in action 3.

Action 4: Limit base erosion via interest deductions and other financial payments

This is a priority base erosion and profit shifting concern in Cameroon. Cameroon's thin capitalization provisions state that local entities cannot deduct (from their income, for tax purposes) interests on debts to partners or related parties for the share of the debt above 1.5 times equity or above "25% of profit before corporate tax and before deduction of the said interests and amortisations". Partners and related parties are defined as those owning, directly or indirectly, at least 25% of the local entity in question (for the purposes of these provisions) (PriceWaterhouseCoopers, 2017).¹² In addition, the Finance Law of 2012 outlawed the deduction of payments made to countries deemed to be tax havens for corporate and income tax purposes. The Law defines a tax haven as any territory where the corporate tax or marginal tax rate is less than 11.66 per cent (a third of the comparative corporate tax rate in Cameroon). Any country qualifying as non-cooperative for fiscal transparency and exchange of information by international financial institutions also falls under this category. In addition, exchange control regulations also exist in Cameroon for financial transfers outside the franc zone, which is the monetary zone including France and its former overseas colonies. In this regard, CEMAC rule No. 0200/CEMAC/UMAC/CM of 29 April 2000 applies to all CEMAC countries (Ernst & Young, 2014b).

Action 5: Counter harmful tax practices more effectively, taking into account transparency and substance

Curtailing harmful tax practices is a priority concern in Cameroon, especially with respect to granting non-strategic tax incentives that lead to self-imposed base erosion and profit shifting and a loss in revenue. Tax competition for FDI among CEMAC countries has led to a "race to the bottom", as Governments compete with one other in devising the most attractive tax incentives to attract foreign investors.¹² Ensuring tax coordination in the region with respect to tax incentives will curtail such harmful tax practices and prevent the spillover effects that lead to the

¹² Based on ECA interviews with individuals in Cameroon.

“race to the bottom” and a loss in revenue for all countries in the region (see discussion in Section 5).

Action 6: Prevent treaty abuse

This is a priority base erosion and profit shifting concern in Cameroon. The main anti-treaty shopping provision used in the country’s tax treaties is the “beneficial ownership” provision.¹² Cameroon should adopt the OECD minimum standards recommend in action 6 of the base erosion and profit shifting report.

Action 7: Prevent the artificial avoidance of permanent establishment status

This is a priority base erosion and profit shifting concern in Cameroon. At the domestic level, the country levies a branch remittance tax set at 16.5 per cent. All the country’s double taxation agreements use United Nations Model Double Taxation Convention definition of permanent establishment.¹² Cameroon should adopt the OECD minimum standards in its double taxation agreements, as recommend in action 7 of the base erosion and profit shifting report. The article on “technical services” in the next version of the United Nations Model Double Taxation Convention should be included in future agreements and renegotiated for older ones.

Actions 8-10: Assure that transfer pricing outcomes are in line with value creation

Consultations with revenue authorities suggest that various forms of abusive transfer pricing are a significant source of base erosion and profit shifting in Cameroon. Multinational enterprises, which account for up to 90 per cent of large enterprises, are active in almost all sectors of the economy, with attendant high risks for transfer pricing.¹² The Government has adopted a strong stance against transfer pricing. Previously, transfer pricing issues were dealt with by applying anti-avoidance regulations under the Finance Law of 2007. The 2012 Finance Law specified modifications to the General Tax Law relating to transfer pricing (TPA Global, 2015). These rules were further modified and are now set out in article 18-3 of the Finance

Law 2014. Cameroon’s tax administration has a large taxpayer unit, which developed a special transfer pricing unit that was expected to be functional in 2017. Similar to other parts of the Directorate of Taxes, however, relevant skills and expertise remain the most significant challenge. The staff of the unit underwent training by OECD in 2015 and there are plans to roll out further training. The unit is also seeking to tap into transfer pricing advisory assistance of Tax Inspectors Without Borders; there is currently a Tax Inspectors Without Borders programme in place in the country (Ernst & Young 2016 ; Organization for Economic Cooperation and Development and UNDP, 2018). One of the key challenges in combatting transfer pricing abuses is the lack of comparables. The unit had sought approval for and financing from the Government to secure access to a global comparables database before the close of 2016 (Bureau van Dijk, 2016). The OECD transfer pricing guidelines may be relied upon to determine the arm’s-length nature of international transactions (Ernst & Young 2016). Transfer pricing scrutiny in Cameroon covers every business sector, aiming in particular to address loopholes in the Tax Code as a result of inadequate regulations on related parties’ business transactions, the payment of royalties and the allocation of costs and expenses (head office costs, cost-sharing agreements, disbursements, etc.) in financial transactions. At the regional level, there is close cooperation on transfer pricing among CEMAC member States. Transfer pricing rules are stipulated in the CEMAC directive relating to corporate income tax (No. 02/01/UEAC-050-CM of 6 August 2001). Further reforms in the light of recommendations in base erosion and profit shifting actions 8-10 will go a long way in ensuring that the transfer pricing challenges that Cameroon is facing are addressed.

Action 11: Establish methodologies to collect and analyse data on base erosion and profit shifting and the actions to address it

Cameroon should consider whether this is a priority base erosion and profit shifting concern. It is recommended that a tax review committee be formed to examine actions necessary in this

regard and on other base erosion and profit shifting matters.

Action 12: Require taxpayers to disclose their aggressive tax planning arrangements

The current disclosure provisions should be buttressed in the light of the recommendations in action ¹².

Action 13:- Re-examine transfer pricing documentation

This is a priority base erosion and profit shifting concern in Cameroon.¹² The Finance Law of 2007 introduced rules relating to an automatic obligation to submit documentation at the beginning of a tax audit for companies registered with the large taxpayer unit and an obligation to produce documentation on request. Tax authorities are further empowered to demand audited companies to provide detailed information on groups' transactions, including details of the operating relationship between group companies and information on any group company based outside Cameroon; methods used in determining the prices for intercompany transactions and a justification for the use thereof; activities carried out by companies, corporations or group entities party to intercompany transactions; the fiscal, legal and administrative treatment pertaining to the transactions in the group companies resident outside Cameroon, including identifying the group companies involved; the countries concerned and the total amount of the transaction in question; contractual agreements governing the repatriation of costs and any pre-established agreements, including advanced rulings if any; and an analysis of the comparative information used where applicable. In 2012, Article M19 bis in Book II of the General Tax Code on Manual of Tax Procedures was introduced to increase the regulation and control of transfer pricing. Under the new rules, if, in the course of an accounts auditing, the administration has evidence that a company has indirectly transferred profits, the administration may request that the company provide information and documents regarding its related companies and their activities, as well as the pricing method. Transfer pricing documentation

requirements were further updated through Law No. 2014/026 of December 2014. Article 18-3 thereof stipulates mandatory documentation requirements regarding shares owned in other companies in which such shares do not exceed 25 per cent of their share capital. Companies are required to attach detailed statements of transactions with the companies that control them or that are under their control, be they in Cameroon or abroad. Cameroon signed the OECD Convention on Mutual Administrative Assistance in Tax Matters on 25 June 2014 and ratified it on 1 October 2015. This will enable the automatic exchange of country-by-country reports under the base erosion and profit shifting project. Cameroon should also enact domestic legislation to enable country-by-country reporting in the light of the recommendations in base erosion and profit shifting action ¹³.

Action 14: Make dispute resolution mechanisms more effective

Dispute resolution should be improved in Cameroon's double taxation agreements.¹²

Action 15: Develop a multilateral instrument

Cameroon has a limited number of tax treaties (five) in place. The treaties with Canada and France are based on the OECD Model Tax Convention, which is perceived to carry more risk of resource leakages. The treaties with Morocco, Tunisia and a partial treaty with Switzerland are based on the United Nations Model Double Taxation Convention. Cameroon is also in the processes of finalizing a treaty with South Africa. Cameroon is one of the members of the ad hoc group that took part in the development of the multilateral instrument. and has signed it (Organization for Economic Cooperation and Development, 2018f). It is, however, advisable that, until the uncertainties regarding the workings of the instrument are clarified, Cameroon apply a wait-and-see approach and renegotiate the double taxation agreements that pose serious base erosion and profit shifting risks.

Other tax reform measures relevant in curtailing base erosion and profit shifting

Cameroon instituted wide-ranging tax reform in 1994 aimed at simplifying its tax incentives regime, in line with regional integration requirements and structural adjustment policies. Prior to 1994, the country's selective tax system had been described as one of the most complex and unfair systems of taxes and duties in Africa that encouraged tax evasion and provided considerable incentives for firms to seek special treatment from the tax authorities (Gauthier and others, 2002).

The 2015 Finance Law provided for a 5 per cent reduction in corporate taxes aimed at alleviating the tax burden on companies and improving compliance and as part of a move to shift priority to the efficiency of resource mobilization. Reforms to the organization and functioning of the tax administration resulted in the creation of separate units responsible for managing large taxpayers as well as small and medium-sized enterprises. The Government also instituted a taxpayer registration system, taxpayer education drive, pre-filled tax returns and an upgrade to the data processing capabilities to facilitate tax management. Further measures include a reduction in face-to-face contact between tax officials and the public (through the provision for electronic and mobile telephone tax declarations), the simplification of tax procedures and improved taxpayer services for small enterprises, which have enhanced the collection of various direct taxes. In 2007, Cameroon launched a reform of its customs administration, which included the installation of an automated customs clearance system, resulting in a decrease of clearance time, decreased corruption and increased tax revenue (Cantens and others, 2010). The Government noted that the lack of collaboration between inland revenue and customs resulted in losses of value added tax, a tax that represents more than 30 per cent of the national budget. Efforts were therefore made to improve coordination and cooperation between various tax collection units (Business in Cameroon, 2016). In recent years, the Government had also noted that the principal source of tax leakages was the numerous tax exemptions in various Investment

Codes. These were replaced by the much simplified and transparent Investment Charter in 2002 (Khan, 2010). Cameroon's legal environment for investment was further updated with legislation enacted on 18 April 2013 laying down private investment incentives applicable to Cameroonians and foreign natural or legal entities residing inside or outside the country (Business in Cameroon, 2016).

4.3 South Africa

South Africa is a middle-income economy with an abundant supply of natural resources, well-developed financial, legal, communications, energy and transport sectors, and a stock exchange that is Africa's largest and among the top 20 in the world. Internationally, South Africa has been recognized as one of the "emerging" economies (Holland and Vann, 1989) and is one of the so-called BRICS nations (Brazil, Russian Federation, India, China and South Africa). They are considered to be the world's five most influential economies outside the Group of 8, accounting for 22 per cent of global GDP and 40 per cent of the world's population (De Silva, 2009; authors' analysis based on UNCTAD, 2018)).

Mining is a key foundation industry, which has enabled South Africa to become the most industrialized country in Africa. The country's mineral wealth is extensive and includes rich deposits of platinum, gold, diamonds, coal antimony, chromite, cobalt, copper, iron ore, lead manganese, nickel, silver, steel, titanium, uranium, vanadium, zinc and zirconium. Many of the world's largest mining companies are South African or have their origins there, notably De Beers, Anglo American, Anglo Platinum and Anglo Gold Ashanti (Economist, 2014). The country also has an established industrial sector comprising automobile assembly, metalworking, machinery, textiles, iron and steel, chemicals, fertilizers, foodstuffs and commercial ship repair (Central Intelligence Agency, 2016). The agricultural sector is also very large, comprising the production of corn, wheat, sugarcane, fruits, vegetables, beef, poultry, mutton, wool and dairy products (South Africa, Department of Agriculture, Forestry and Fisheries, 2016).

Table 3: Details of income, profits and capital gains in South Africa, 1997-2014 (Per cent)

	1997	2000	2007	2008	2009	2010	2011	2012	2013	2014
Total taxes on income, profits and capital gains as a proportion of total tax revenue	53.3	52.7	54.6	58.0	55.8	52.4	53.1	52.1	52.2	52.6
Total tax of individuals	38.7	36.3	27.9	29.7	32.1	31.4	31.3	31.5	31.9	33.1
Total corporate tax	14.7	16.4	26.7	28.3	23.7	20.9	21.8	20.6	20.2	19.5

Source: authors' analysis based in International Monetary Fund government finance statistics.

South Africa has a fairly advanced tax system, compared with the majority of African countries.¹³ The economy relies heavily on income and profits as a proportion of its tax-to-GDP ratio. Revenue from the taxation of individuals dominates that from corporations (see table 3).

The economy relies heavily on taxes on income and profits, which represent approximately half of tax revenue (International Monetary Fund, not dated) and consumption tax (40.3 per cent). Although the country saw increased revenue collection in 2015 and 2016 (in gross terms), the potential to collect even higher revenue has been hampered by weak governance that has been marred by corruption in State-owned institutions, which have been subject to political interference (South African Revenue Service, 2017). Economic growth has also decelerated in recent years owing to strikes, power shortages and a depressed demand for commodities. While illicit financial flows from South Africa are lower than from much smaller African economies such as Cameroon, illicit flows from South Africa were the fifth highest, after Nigeria (in West Africa), and Egypt, Algeria and Morocco (in North Africa) (AfDB, OECD, UNDP, GFI, 2014). Nevertheless, there have been concerted efforts to tackle corruption and illicit financial flows, most notably through the public service anti-corruption strategy, which resulted in a number of anti-corruption measures, such as the Protected Disclosures Act, the Promotion of Access to Information Act, the Financial Intelligence Centre and the establishment of an asset register for accounting officers and the mandatory financial disclosure of assets and interests for all senior managers (Public Service Commission, 2005).

South Africa has a large presence of multinational enterprises, which leaves it vulnerable to base erosion and profit shifting practices that can reduce tax revenue (United Nations, Department of Economic and Social Affairs, 2013). Oxfam (2016) reports that only 1.6 million out of 2 million companies registered in South Africa are active and paying tax. Data from the South African Reserve Bank, which captures payments directed offshore, indicate that, just after the global financial crisis of 2008, financial outflows increased by nearly one quarter. The data also showed that financial outflows from legal, accounting and management consulting services increased by 32.6 per cent and engineering and technical services by 39.5 per cent, whereas there was low economic activity owing to the crisis. This magnitude of cross-border, non-goods transactions suggests that base erosion and profit shifting could be occurring (Davis Tax Committee 2014a). Nevertheless, over the years, South Africa has made significant progress towards identifying the avenues for base erosion and profit shifting and addressing the same. Efforts to curtail it began in 1997 when the Katz Commission was established to investigate the fiscal implications of the globalized trade on South Africa's tax structure. As a result of this investigation, South Africa introduced various specific anti-avoidance provisions in its Income Tax Act 58 of 1962 to address tax avoidance schemes. These include controlled foreign company rules in section 9D of the Income Tax Act, transfer pricing rules in section 31, rules to deal with hybrid instruments and hybrid entities and reportable arrangements rules in sections 34-39 of the Tax Administration Act 28 of 2011 and the voluntary disclosure programme in sections 225-233. South Africa's general anti-

¹³ Based on interviews with individuals in South Africa.

avoidance rules and the substance over form principle can also be applied to curtailing base erosion and profit shifting, even though they are applied mainly in the domestic arena. South Africa's tax treaties also contain anti-avoidance provisions, such as the beneficial ownership provision, which can be applied to curtail the abuse of tax treaties by third country residents (Davis Tax Committee, 2014b). The exchange control regulations, which regulate the outflow of capital, complement the anti-avoidance legislation in curtailing base erosion and profit shifting (Oguttu, 2015a). Nevertheless, due to increased globalization, modern business models and sophisticated tax planning practices, South Africa's tax system remains susceptible to base erosion and profit shifting.

As a member of the Group of 20, South Africa is the only African country that acceded to the OECD base erosion and profit shifting project. The Government sent officials from the South African Revenue Service to participate in the various working parties of OECD that shaped the outcomes of the project. By implication, South Africa has committed itself to implementing the minimum standards in the base erosion and profit shifting package, and it is a part of the OECD/Group of 20 inclusive framework. In July 2013, South Africa's Minister of Finance appointed a tax review committee, namely, the Davis Tax Committee, to review the country's tax system, taking into account the long-term objectives of the 2030 national development plan (South Africa, National Planning Commission, 2011), which requires the development of fiscal and economic policies that encourage FDI to foster economic growth. On the international front, the Committee is required to address concerns about base erosion and profit shifting, as identified by the OECD base erosion and profit shifting project. The Committee published its first interim report on base erosion and profit shifting on 30 September 2014. The final report, which was presented to the Minister of Finance in 2016, is expected to be released soon. The Committee notes that addressing base erosion and profit shifting in South Africa requires recognizing that its economy portrays aspects of both a capital-exporting and capital-importing economy. On the one hand, it is a residence State to many home-

grown multinational enterprises and a base country for many intermediary holding companies (Legwaila, 2010) for further investment in the rest of Africa (Davis Tax Committee, 2014a; Oguttu, 2011). On the other hand, it still relies heavily on FDI from developed economies for its access to technology and capital (United Nations Conference on Trade and Development, 2017b) and on the exchange control regulations that most developing countries apply to control the outflow of domestic revenue (Reserve Bank of South Africa, 2017; Deloitte, 2015a). This dual nature of the economy implies that the OECD's base erosion and profit shifting actions that pertain both to capital-exporting and capital-importing countries are of concern to the South Africa. A balanced approach is therefore required that encourages the home-grown competitiveness of multinationals when expanding abroad, while protecting against profit-shifting risks that are likely to increase with such expansion. A summary of current provisions and measures adopted by South Africa in the light of the OECD base erosion and profit shifting project and recommendations on how the Government should respond to the relevant concerns in that regard is outlined below.

Action 1: Address the tax challenges of the digital economy

Because of South Africa's advanced economy, especially with respect to financial services, the tax challenges of the digital economy are a priority base erosion and profit shifting concern. In response to the OECD base erosion and profit shifting report,¹³ the VAT Act 89 of 1991 was amended effective 1 April 2014 so that enterprises rendering specific electronic services must register as value added tax vendors in South Africa and charge the tax on the supply of such services (South Africa, not dated; interviews). South Africa should continue to monitor other OECD recommendations on the taxation of the digital economy (e.g., for direct tax) and adopt appropriate measures.

Action 2: Neutralize the effects of hybrid mismatch arrangements

The country's advanced financial sector implies that hybrid mismatches and related financial instruments are a base erosion and profit shifting risk. Current measures to counter such arrangements include section 23G of the Income Tax Act 58 of 1962, which treats sale and leaseback arrangements as a financial arrangement; sections 50A–H, which provide for the levying of a withholding tax on interest; section 23M, which limits cross-border interest deductions; section 23N, which limits excessive debt financing in reorganization transactions; sections 8F and 8FA, which deny interest deduction on a hybrid debt instrument; section 64EB, which prohibits the transfer of dividends to entities exempt from dividends tax; section 10 (1) (k) (i), which counters dividend mismatch schemes involving exempt entities; section 8E, which deems a hybrid financial instrument a hybrid equity instrument; section 8EA, which applies to equity that resembles debt; and the general anti-avoidance provisions in sections 80A–80L which can be applied to curtail impermissible tax avoidance. The Davis Tax Committee notes that the plethora of legislation may lead to mismatches if not linked to the tax treatment in the other country. It recommends that the rules be simplified to focus on legal principles rather than specific transactions or instruments, and that linking rules, as recommended in action 2 of the base erosion and profit shifting project, should be adopted (Davis Tax Committee 2014, Report on Action 2).

Action 3: Strengthen controlled foreign company rules

South Africa has controlled foreign company rules in section 9D of the Income Tax Act. The Davis Tax Committee notes that the rules are comparable to those in developed countries (Davis Tax Committee, not dated). There is no need to tighten the rules any further

Action 4: Limit base erosion via interest deductions and other financial payments

This is a priority base erosion and profit shifting concern in South Africa. Currently, measures to counter such arrangements include the exchange control regulations, which regulate

the outflow of capital; section 31 of the Income Tax Act, which requires international financial assistance to be at arm's length; section 24J, which regulates the incurrance and accrual of interest on financial instruments; section 45, which regulates debt push-down structures in intra-group transactions; section 23N, which limits the deduction of interest in reorganization and acquisition transactions; section 23M, which limits the deduction of interest for persons in a controlling relationship; section 24O, which limits the deduction of interest in share acquisitions; sections 8E and 8EA, which deem dividends declared a hybrid equity instrument as interest; sections 8F and 8FA, which deem interest on a hybrid debt instrument a dividend in specie; and the general anti-avoidance provisions in sections 80A–80L, which can be applied to curtail impermissible tax avoidance. The Davis Tax Committee has pointed out that the above rules often overlap, complicate the tax system and create uncertainty for taxpayers. It recommended that consideration be given to adopting the OECD best practices in action 4, as appropriate.

Action 5: Counter harmful tax practices more effectively, taking into account transparency and substance

South Africa's headquarter company regime could be considered potentially harmful as controlled foreign company rules, transfer pricing rules and thin capitalization rules and some capital gains tax provisions are relaxed for headquarter companies. The Davis Tax Committee recommends that a balance be made to preserve the competitiveness of the economy and to guard against harmful tax practices (Davis Tax Committee 2014, Report on Action 5). Transparency and compulsory spontaneous exchange on special rulings regarding this regime will be required in terms of the OECD minimum standards in action 5.

Action 6: Prevent treaty abuse

This is a priority base erosion and profit shifting concern. Currently, the main anti-treaty shopping provision used in South Africa's tax treaties is the "beneficial ownership" provision. It is recommended that South Africa adopt the

minimum standards, as set out in action 6 (Davis Tax Committee, 2014b).

Action 7: Prevent the artificial avoidance of permanent establishment status

Given that most of South Africa's double taxation agreements are based on the OECD Model Tax Convention, the artificial avoidance of permanent establishment status is a priority base erosion and profit shifting concern. Given that the permanent establishment concept is defined in section 1 of the Income Tax Act as defined in article 5 of the Convention, the changes to the meaning of the term as recommended in action 7 will be instrumental in addressing the relevant base erosion and profit shifting risks.

Actions 8 -10: Assure that transfer pricing outcomes are in line with value creation

Transfer pricing issues are a priority base erosion and profit shifting concern in South Africa. The transfer pricing provisions in section 31 of the Income Tax Act require that the arm's-length principle be applied in international transactions. The transfer pricing of intangibles can be curtailed by section 31 (4), which applies to the use of foreign-owned intangibles. The exchange control regulations also restrict the intra-group transfer of intangibles, given that prior approval is required. Section 23I of the Act prohibits tax deductions on intellectual property that was previously owned by a South African person or a connected person and, the exemptions to controlled foreign company rules do not apply to royalties derived from the use of intellectual property by such a company unless it directly creates, develops or substantially upgrades such intellectual property. In addition, South Africa levies a withholding tax on royalties, at a rate of 15 per cent. Given that the South African Revenue Service Practice Note 7, 1999 refers to the OECD transfer pricing guidelines, it is assumed that South Africa will follow the international standards on transfer pricing in actions 8-10 of the base erosion and profit shifting report (Davis Tax Committee 2014, Report on Action 8).

Action 11: Establish methodologies to collect and analyse data on base erosion

and profit shifting and the actions to address it

South Africa requires the tools and data to measure and monitor base erosion and profit shifting and to evaluate the impact of the measures that it is implementing under the base erosion and profit shifting project. It is therefore recommended that that recommendations in action 11 be adopted.

Action 12: Require taxpayers to disclose their aggressive tax planning arrangements

South Africa has reportable arrangements provisions in sections 34-39 of the Tax Administration Act 28 of 2011, which can ensure the disclosure of aggressive tax planning arrangements. All that is needed is to ensure that the rules are more effective in the light of the recommendations contained in action 12.

Action 13: Re-examine transfer pricing documentation

This is a priority base erosion and profit shifting concern in South Africa, to which responses have been made in the light of the base erosion and profit shifting project. In 2015, legislation on country-by-country reporting was enacted. Section 1 of the Tax Administration Act defines "international tax standard" to mean, among other things, country-by-country reporting for multinational enterprises and any other standard for the exchange of information as specified by the Minister of Finance through regulations. Section 3 (3) (a) (iii) of the Act enables service of a document from the requesting country. In 2016, regulations were issued to specify the country-by-country reporting standard for multinational enterprises for South Africa's circumstances, effective for reporting fiscal years beginning on or after 1 January 2016. Where the ultimate parent of the enterprise is a tax resident in South Africa and has an annual group consolidated turnover exceeding 10 billion rand or 750 million euros during the 2015 financial year, it will be required to prepare the country-by-country report for financial years beginning on or after 1 January 2016. The South African Revenue

Service has confirmed that the template issued by OECD should be used for the country-by-country report. A South African entity may be required to submit the report, even though it is not the ultimate parent company, if it exceeds the turnover threshold of 750 million euros. To enable international country-by-country reporting, South Africa has signed the multilateral competent authority agreement for the automatic exchange of country-by-country reports, which came into force on 27 January 2016. The country automatically receives country-by-country reports with 56 other jurisdictions, and sends them automatically to 53 other jurisdictions (Organization for Economic Cooperation and Development, 2018d).

Action 14: Make dispute resolution mechanisms more effective

South Africa is committed to ensuring that tax treaty disputes are resolved. In March 2015, the South African Revenue Service published guidance on the mutual agreement procedure (South Africa, South African Revenue Service, 2016), which is necessary to prevent disputes in a tax treaty context. The guidance includes an explanation of what a mutual agreement procedure entails and how to submit a mutual agreement procedure request. Although some of South Africa's tax treaties contain an arbitration provision, the country is not committed to binding arbitration in its bilateral treaties owing to the changes in mutual agreement procedure as discussed above. However, it has tax treaties with OECD countries that have committed themselves to binding arbitration under action 14. South Africa may need to make its position clear on this matter; especially in the light of the opt-in and opt-out provisions in the multilateral instrument, as explained below.

Action 15: Develop a multilateral instrument

Signing this multilateral instrument to deal with the tax treaty recommendations arising from the base erosion and profit shifting project is the most feasible approach for South Africa to follow instead of having to renegotiate its many tax treaties. The list of double tax treaties on the

South African Revenue Service website shows that the country has entered into 75 double tax treaties. Another 36 treaties are in the process of negotiation or have been finalized but not yet signed. When the OECD released the multilateral instrument in November 2016, the Minister of Finance announced in the budget speech of February 2017 that the country would sign a multilateral instrument (South Africa, National Treasury, 2017). Indeed, it is one of 68 countries that became signatories of the instrument at the signing ceremony on 7 June 2017 (subject to certain reservations) (Organization for Economic Cooperation and Development, 2017c).

Conclusion

This section has focused on the experiences Cameroon, South Africa and the United Republic of Tanzania in addressing base erosion and profit shifting. It has presented an outline of the measures that they have taken to protect their tax bases and to what extent they are engaging with or implementing the OECD measures. The case of the United Republic of Tanzania outlines some of the key issues faced by tax administrations in a resource-rich country, which has leveraged legal instruments to address base erosion and profit shifting, while reviewing inefficient tax exemptions. Given that the country had limited involvement in the base erosion and profit shifting consultations, it provides a good example for prioritizing improvements in the overall tax administrations as a precursor to adopting base erosion and profit shifting-specific interventions. The case study on Cameroon highlights a more focused approach to tackling base erosion and profit shifting, for example, through allocating resources and capacity to the establishment of a transfer pricing unit. As a member of the Group of 20, South Africa was involved in the development of the base erosion and profit shifting package. It faces unique circumstances with regard to how it adopts the package, given that it has to balance preserving the competitiveness of its own multinational enterprises as they invest offshore and in the African continent, and at the same time protecting its tax base from erosion by foreign investors without hampering foreign investment.

Section 5: Policy measures to curtail base erosion and profit shifting and related illicit financial flows

Although the OECD base erosion and profit shifting package has resulted in consensus regarding some international standards and minimum standards for which many countries have enacted new regulations, uncertainties remain with respect to when and how consistently countries will implement the recommendations (Nibbe, 2016). If the new international tax rules become more complex and less aligned, this will undoubtedly lead to disputes and double taxation as countries take opposing views (Kielstra, 2016). In turn, countries may pursue efforts to address such double taxation through new double taxation treaties; these may risk opening new opportunities for treaty abuse, leading to double non-taxation. It will be important for countries to be aware of this risk and seek to address it. There is also scepticism about the commitment of many OECD member countries to the implementation of the base erosion and profit shifting recommendations. The OECD approach to addressing base erosion and profit shifting has also been criticized for not addressing basic fundamental principles of the international tax system that are pivotal in addressing base erosion and profit shifting. Owing to the short time frame of the base erosion and profit shifting project (two years), there was a lack of sufficient analysis of all relevant issues. Addressing base erosion and profit shifting is not only about rewriting the global tax framework or changing the very complex laws of the international tax system; rather, fundamental behavioural change is also needed from multinational enterprises to ensure the alignment of business activities with tax outcomes. For the business community to understand and comply with the base erosion and profit shifting recommendations, base erosion and profit shifting issues needs to be placed at the top of the corporate agenda (Mealey, 2016). Addressing base erosion and profit shifting in Africa will require political will from Governments to set aside funds to build administrative capacity. The success of many of the base erosion and profit shifting measures depends heavily on information-sharing, transparency, data collection, enforcement and

strong tax administrations, in which African countries have low capacity. Faced with these challenges, African countries need to be aware of alternative strategies to address base erosion and profit shifting. This section of the study therefore proposes some policy measures and alternative approaches, which have not been addressed in the OECD's base erosion and profit shifting measures but that are pertinent to addressing base erosion and profit shifting concerns that African countries face.

5.1 Policy measures for curtailing base erosion and profit shifting in Africa

Close domestic tax loopholes

There are a number of measures that African countries can consider for having a relatively swift and positive impact on domestic resource mobilization. These include strengthening the enforcement of tax laws and removing unnecessary tax breaks, while closing the most obvious loopholes in the tax architecture. In Africa, most of the challenges of tax revenue collection are simply about the limited capacity to enforce existing laws. Governments also need to halt inefficient practices and corruption, which are counterproductive in enforcing tax collection. Legislation needs to be enacted to ensure that whistle-blowers and witnesses to corporate tax practices are protected and not subjected to reprisals. Pursuant to article 19 of the International Covenant on Civil and Political Rights, a charter on the rights of whistle-blowers should be adopted (UN 2016, See A/HRC/33/40.). Laws should be enacted to ensure that domestic accounting and legal firms and banks are more transparent about their affairs on behalf of multinational enterprises and for specific transactions, for example, by requiring domestic banks to investigate the origin of the deposits and investments that they administer.

Build administrative capacity

The base erosion and profit shifting measures are very technical and require highly sophisticated and well-resourced legislative administrations, which puts less well-resourced Governments in Africa at a disadvantage. African countries need to build the capacity of their revenue administrations. This entails employing competent tax officials in various fields, such as accountants, lawyers and economists, who can understand and administer complex international tax laws. Continuous training is required for such officials to ensure that they are up to date with current international developments. For African Governments to hire and retain specialized tax officials, they need to pay them salaries comparable to those in the private sector (Oguttu, 2015d). Measures to improve the competency of tax officials have to be combined with measures to root out corrupt tendencies, given that this is key to enhancing revenue collection. The broad discretionary powers given to tax authorities must be rooted out, given that this encourages corruption (Ibid.). There is also a need for the technological advancement of tax systems so as to handle base erosion and profit shifting measures relating to the automatic exchange of information in tax matters. Financing and technical support in building administrative capacity can be provided by organizations such as Tax Inspectors Without Borders, which makes use of tax audit experts to facilitate the transfer of knowledge and audit skills to developing countries. The organization has a toolkit available online, which is a practical guide to establishing audit assistance programmes in developing country tax administrations. A report by the European Network on Debt and Development (2016) was critical of the Tax Inspectors Without Borders initiatives in Ghana, Rwanda and Senegal because the local authorities were not allowed to own and lead the project, contrary to the format stated in the toolkit. The Network also noted that, in all the three countries, Tax Inspectors Without Borders experts originated from countries that had substantial corporate interests in the recipient country. In the case of the United Kingdom and Rwanda, PricewaterhouseCoopers, a company that provides advice to multinational enterprises on their tax planning, played a central management role in the pilot project.

Tax Inspectors Without Borders should revise its structure to avoid similar conflicts of interest in the future.

Build knowledge capacity in international tax matters

Various international organizations can support knowledge capacity in international tax matters. These include IMF, the World Bank and the United Nations (United Nations, Department of Economic and Social Affairs, 2013). Other notable institutions with international tax knowledges bases include the African Tax Institute, the African Tax Administration Forum, the African Tax Research Network, the International Centre for Tax and Development, the International Tax and Investment Centre, International Tax Dialogue, the International Bureau for Fiscal Documentation and UNCTAD (UN General Assembly Resolution 2016, A/71/150). There are also a number of NGOs that have produced reports and policy documents that should be useful in widening the knowledge base. These include the Global Alliance for Tax Justice, Tax Justice Network-Africa, Christian Aid, ActionAid, Oxfam International, Global Financial Integrity, the Extractive Industries Transparency Initiative, the Task Force on Financial Integrity and Economic Development and the Global Policy Forum Europe (German Agency for Technical Cooperation, 2010). It must also be acknowledged that, although African countries often send tax officials outside the continent for tax training, reviews often indicate that the training is based on how the tax provisions apply in the circumstances of developed countries with efficient technological development and administrative capacity, which often makes such training out of touch with the reality for African countries. Customized solutions to African issues can be enhanced if African countries with similar levels of economic development cooperate and seek guidance from fellow African countries that have made progress in resolving shared problems, given that they would appreciate the challenges faced and provide “fit for purpose” solutions to shared challenges. It is also important for African countries to enlist African researchers in tax research projects on Africa. Consultancies are often awarded to non-African nationals who may

not be conversant in the issues at stake and who have limited revenue administration access. The African Tax Administration Forum has an African tax research network that has pulled together African researchers in various tax fields who can be called upon to conduct tax research in Africa. This should be crystalized by setting up a long-term standing committee of experts, similar to the United Nations Committee of Experts on International Cooperation in Tax Matters.

Build tax treaty negotiating capacity

Many of the base erosion and profit shifting concerns that countries face relate to abuse of tax treaties. Some of the tax treaties that African countries signed, however, were entered into mainly as political gestures, with little concern for base erosion and profit shifting issues. Treaty abuse in Africa is exacerbated because countries have negotiated treaty provisions (e.g., the withholding tax rates) that are not in their favour but rather reflect the position of the other contracting State (Akunobela, 2012). The ability to negotiate favourable provisions depends a lot on the treaty negotiating power of a country. In general, developed countries are better skilled in negotiating tax treaties than developing countries (PricewaterhouseCoopers and EuropeAID, 2011). Negotiating tax treaties requires knowledge of international tax law and tax treaty principles by taxing authorities. It is important for African countries to build administrative capacity to negotiate tax treaties (Thuronyi, 1998). This matter will become even more relevant if they consider signing the multilateral instrument under action 15 of the OECD base erosion and profit shifting report.

Coordination of ministries and agencies dealing with tax treaty issues:

It is critical that ministries and agencies that have an impact on tax treaties be coordinated. In most countries, the Ministry of Finance is the arm of the Executive that is tasked with negotiating tax treaties, but revenue authorities are often responsible for the administration of tax treaties. Even though a country may have

a double tax treaty with a given country, it may also have a bilateral investment agreement with the same country. These agreements are, however, normally signed by the Ministry responsible for investment and are intended to protect investment by investors of one State in the other State (Vandeveldt, 2000). Although the application of these agreements specifically excludes tax treaties (e.g., article 4 (3) (b) of the South Africa-Kuwait bilateral investment agreement) and they normally do not cover taxation matters, they however usually contain a “most favoured nation” clause under which one contracting State is obliged to give investors from the other contracting State no less favourable treatment than it grants to investors from third countries. The most favoured nation clause allows investors to ask for the treatment in another agreement or any other agreement that may be more favourable (e.g., article 11 South Africa/United Kingdom bilateral investment agreement). This implies that investors who think that they are not favourably treated in a double tax treaty can take advantage of a most favoured nation clause in an agreement to engage in treaty shopping schemes and seek protections not offered in a double tax treaty. This is exactly what happened in the Uganda case of *Heritage & Gas Limited v. Uganda Revenue Authority*,¹⁴ in which the taxpayer who lost the case on the basis of double tax treaty issues utilized the agreement and took the matter to arbitration in London under the United Nations Commission on International Trade Law, which deals with investment disputes. This case exemplifies the importance of ensuring that the Ministry of Finance is consulted to ensure bilateral investment agreement tax treaties do not work at cross purposes.

Improve access to data

In order to resolve issues of gaining access to data for transfer pricing analyses, African countries have to purchase access to pan-European databases. For example, Kenya purchased the database on comparables in 2011 (PricewaterhouseCoopers, 2017b). South Africa has also had access to a comparable database

¹⁴ Tax Appeals Tribunal Tax Application No. 26/2010.

since 2012 (United Nations, 2012b, in para 10.4.24). The only other countries that have access in Africa are Algeria (Deloitte, 2015a) and Uganda (International Monetary Fund, 2008, in para. 12). The African Tax Administration Forum is also looking into purchasing a database for collective use. It is also recommended that multilateral agencies provide access to such data, which is fully and freely available to Governments.

Address harmful tax practices emanating from non-strategic tax incentives

Action 5 of the base erosion and profit shifting project concentrated only on harmful tax practices of preferential tax regimes. For African countries, the harmful tax practice that critically leads to the “race to the bottom” is the granting of non-strategic tax incentives to foreign investors as Governments compete with each other in devising the most attractive tax incentives that will attract foreign investors to their shores (International Monetary Fund, 2008, in para. 12). The result is that all countries ultimately end up losing revenue, with no discernible impact on the allocation of investment, which makes countries in a region collectively worse off. This is compounded by the lack of transparency in the governance of tax incentives, which undermines their efficiency. Research shows that tax incentives do not play a significant role in investment decisions; rather, investors place emphasis on fiscal policies, political stability and infrastructural development (Jones and Temouri, 2015). The OECD base erosion and profit shifting agenda does not address the matter of tax incentives, which is critical for African countries. Instead, this matter was dealt with by Group of 20 development working group, in conjunction with OECD, IMF and the World Bank, in the form of toolkits, which are essentially a side project intended to prioritize actions items that have the greatest impact for low-capacity developing economies to assist these countries in implementing base erosion and profit shifting action items. In October 2015, the development working group published a toolkit for tax incentives (Group of 20 Development Working Group on Domestic Resource Mobilization, 2014), which provides guidance on improving the design, efficiency and governance of tax

incentives, as well as recommendations on how to curtail the race to the bottom in granting tax incentives. African countries need to carry out a cost-benefit analysis of tax incentives to determine their efficiency.

Strengthen regional tax coordination and cooperation of African tax authorities

All African countries are members of at least one of the eight Regional Economic Communities that are recognised by the African Union,, which are intended to facilitate closer regional economic integration, inter alia. Commitment to the ideals of these regional bodies will go a long way in addressing the base erosion and profit shifting challenges that African countries face, in particular with regard to curtailing the race to the bottom in granting tax incentives. Regional coordination could also play a significant role in combating the financial secrecy jurisdictions that encourage base erosion and profit shifting.

5.2 Alternative approaches to curtailing base erosion and profit shifting and related illicit financial flows

Apart from the OECD approach to curtailing base erosion and profit shifting, it is important for African countries to also consider alternative approaches to address their base erosion and profit shifting concerns.

United Nations approach to curtailing base erosion and profit shifting concerns for developing countries

The United Nations participates in the tax work of OECD to provide insight regarding the concerns of developing countries. The United Nations acknowledges that, although developing countries also face base erosion and profit shifting issues that developed countries face, their base erosion and profit shifting issues may manifest themselves differently, given the specificities of their legal and administrative frameworks. The United Nations has therefore stressed that, although efforts in international tax cooperation should be universal in approach and scope, they should fully take into account the various needs and capacities of all countries, in

particular least developed countries, landlocked developing countries, small island developing States and African countries (United Nations, General Assembly, 2015a, in para. 28). The United Nations recognizes the need for technical assistance for developing countries through multilateral, regional, bilateral and South-South cooperation based on the different needs of countries. The United Nations notes that the focus of the OECD base erosion and profit shifting project is naturally on the priorities of member States of OECD and that such priorities do not always reflect issues that are of specific relevance to developing countries. In October 2013, the United Nations Committee of Experts on International Cooperation in Tax Matters established a subcommittee on base erosion and profit shifting issues for developing countries (UN Subcommittee on base erosion and profit shifting, 2014), which issued a questionnaire to developing countries to identify their priority base erosion and profit shifting concerns. Thereafter, the Committee initiated a study on the base erosion and profit shifting perspectives of developing countries, which culminated in the 2015 United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries.

It should also be noted that the United Nations Model Double Taxation Convention, which favours capital-importing countries over capital-exporting ones, in general imposes fewer restrictions on the tax jurisdiction of source countries. With respect to preventing the artificial avoidance of permanent establishment status (action 6 of the base erosion and profit shifting project), the Convention offers a broader definition of the permanent establishment concept, which is advantageous for source countries.

Article 5 (5) of the OECD Model Tax Convention provides for permanent establishment status where a person habitually acts on behalf of an enterprise in the other contracting State by exercising authority to conclude contracts in its name. This article is open to various permanent establishment dependent agency base erosion and profit shifting risks, but the OECD base erosion and profit shifting project concentrated

only on commissioner arrangements in civil law jurisdictions (see discussion in section 3). In Africa, dependent agency status is circumvented mainly by ensuring that the person who usually has the authority to conclude contracts falls under article 5 (6) as an “independent agent” who does not create a permanent establishment. This can be done by ensuring that a person does not have specific authority to conclude contracts on behalf of an enterprise but rather keeps a stock of goods or merchandise for an enterprise and delivers the same to customers in the country. The United Nations Model Double Taxation Convention covers this risk by providing in article 5 (5) (a) that a dependent agent is deemed to exist even if a person has no such authority but habitually maintains a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise (Lennard, 2009). Though both Conventions exclude agents of independent status from the permanent establishment definition, this exclusion is qualified in the United Nations Model Double Taxation Convention. In particular, when the activities of an independent agent are devoted wholly or almost wholly to an enterprise and conditions are made or imposed between that enterprise and the agent in their commercial and financial relations that differ from those that would have been made between independent enterprises, the agent will not be considered independent. under the Convention. This ensures that an enterprise represented by an independent agent does not escape tax by entering into artificial transactions to avoid permanent establishment status (*ibid.*).

The OECD base erosion and profit shifting project does not address issues pertaining to insurance permanent establishments, which are of specific concern to source countries. This matter was included in initial discussion drafts on permanent establishments, but it was dropped in the final reports, on the reasoning that insurance companies should not be treated differently from other companies but should be considered under article 5 (5) or 5 (6) of the OECD Model Tax Convention (Deloitte, 2015a). An insurance company of one State can create a permanent establishment in the other State if it has a fixed place of business in terms of article 5 (1) or if it

carries out business through a dependent agent in terms of article 5 (5). Nevertheless, agencies of foreign insurance companies may not meet either of the above requirements but can do large-scale business in a State and not be taxed on profits arising from such business. The OECD Model Tax Convention does not specifically include a permanent establishment article on insurance business but merely provides that its member countries can negotiate a provision in their tax treaties, which stipulates that insurance companies are deemed to have a permanent establishment in the other State if they collect premiums in that other State through an agent established there. The United Nations Model Double Taxation Convention, however, does not leave this matter to the whims of negotiation (United Nations, General Assembly, 2015c). Article 5 (6) of the United Nations Model Double Taxation Convention provides that an insurance enterprise of a contracting State shall, with regard to reinsurance, be deemed to have a permanent establishment in the other contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person other than an agent of an independent status. It is the interest of African countries to ensure they include this United Nations article in their tax treaties.

The OECD base erosion and profit shifting project does not address matters pertaining to the attribution of profits to permanent establishment, of which developing countries have been wary since OECD introduced its authorized approach of attributing profits to permanent establishment in 2010 (article 7 (2) of the OECD Model Tax Convention). The OECD approach recognizes the internal dealings of a permanent establishment and its head office (as if they were separate entities) without regard to the actual profits of the enterprise of which it is part. This implies that notional expenses from head office may be charged on the permanent establishment, which poses base erosion risks. In the United Nations Model Double Taxation Convention, only the actual income and expenses of the permanent establishment are allocated. It is recommended that African countries ensure that article 7 of their treaties is based on the United Nations Model Double Taxation Convention.

The OECD base erosion and profit shifting project does not fully address matters pertaining to the taxation of services that are pertinent to developing countries. Action 10 covers only protecting against base-eroding management fees and head office expenses from a transfer pricing perspective. However, for most African countries, the main counteracting measure is the use of withholding taxes on service fees. Nevertheless, the OECD Model Tax Convention does not contain a specific article on service fees nor does it have any special treatment of services. Instead, services are treated the same way as other business activities, in that a State may tax only the foreign service provider if it qualifies as a permanent establishment in terms of article 5. Under the United Nations Model Double Taxation Convention, the services of a consultant may be taxed as “independent personal services” in article 14 if the person has a “fixed base” that he or she regularly uses in the source State. Whether services are taxed under the permanent establishment article in or under article 14 in the United Nations Model Double Taxation Convention, only profits attributed to a permanent establishment or a fixed base are taxable in the source State using the arm’s-length principle (Arnold and McIntyre 2013). Applying the principle to service fees, however, is cumbersome, owing to difficulties of verifying whether the fees are appropriate (Oguttu, 2016b). Besides, article 7 (2) of the OECD Model Tax Convention, which relates to attributing profits to permanent establishment as discussed above, poses specific challenges, given that notional management expenses from head office may be charged on the permanent establishment resulting in base erosion (Deloitte, 2010). The absence of a special deemed permanent establishment rule denies source countries the right to effectively tax such businesses (Daurer and Krever, 2014). To protect their tax bases, some African countries have signed treaties with articles on management/service fees that deviate from the OECD Model Tax Convention and the United Nations Model Double Taxation Conventions (e.g., article 13 of Uganda/South Africa double taxation agreement). There is, however, no standard way of drafting these articles, which makes treaty negotiations difficult and creates uncertainties

for taxpayers. The United Nations has addressed this matter by devising a “technical service fee” article that will feature in the next update of its Model Double Taxation Convention. This article will allow developing countries to levy a tax on payments made to the overseas providers of “technical services”, even if there is no physical presence in the country. Developing countries are anticipating this service fee article. It is recommended that African countries include this article in their future tax treaties.

Action 14 of the OECD base erosion and profit shifting project is strongly in favour of using binding arbitration to resolve treaty disputes under the mutual agreement procedure. Binding arbitration, however, is of specific concern to African countries, owing in part to their lack of experience in arbitration matters. In 2012, the United Nations issued a guide to the mutual agreement procedure under tax treaties. Its primary focus is on the specific needs and concerns of developing countries and countries in transition and provides best practices and procedures to ensure effective mutual agreement procedure for these countries. The United Nations also has a capacity-building initiative to equip countries that have little or no experience with mutual agreement procedures. The guide contains a recommendation that, other than arbitration proceedings, countries can also use non-binding alternative dispute mechanisms, which are applied in resolving commercial disputes. These include the use of mediation to facilitate the negotiations between the competent authorities and the use of conciliation, in which a conciliator is more active than in mediation (United Nations, Committee of Experts on International Cooperation in Tax Matters, 2015).

African Tax Administration Forum’s approach to addressing base erosion and profit shifting in Africa

In 2014, the African Tax Administration Forum established a cross-border taxation technical committee to define the African position on base erosion and profit shifting to communicate the African response to the OECD base erosion and profit shifting project and to present an African perspective on global tax matters. In 2014, the

Forum held a consultative conference on new rules of the global tax agenda. In its outcome document (African Tax Administration Forum, 2014), the Forum noted that, notwithstanding the OECD base erosion and profit shifting process, Africa must come up with customized solutions to protect its own tax base, with a customized approach to assist African countries and groups of countries in similar positions to ensure domestic resource mobilization. It is recommended that member countries of the Forum strengthen their support and commitment to the organization, given that this will allow the Forum to have a greater impact in engaging with OECD. More African countries are called upon to join the Forum so as to take advantage of the capacity-building initiatives on base erosion and profit shifting issues that it is carrying out.

Views of academics on “unitary taxation” and formulary apportionment

Actions 8-10 of the base erosion and profit shifting project reinforce the use of the arm’s-length principle as the means for curbing transfer pricing. African countries, however, face major challenges in applying the principle (as discussed in section 3). Various commentators have pointed out the conceptual and practical difficulties that arise in applying the principle, given that it requires matching comparable transactions between non-arm’s-length entities and arm’s-length entities (Vincent, 2005; Vann, 2007; Arnold and McIntyre, 2002). Subsidiaries in modern multinational enterprises do not operate as separate enterprises but rather as a single unified enterprise managed from a central location by managers who are responsible for the enterprise as a whole (Avi-Yonah and Clausing, 2008). In applying the principle, taxpayers, their advisers and tax authorities are left to reconstruct, from largely dissimilar transactions or entities, what parties at arm’s length would have done in similar circumstances (Couzin, 2005). The principle usually challenges intra-firm arrangements because it requires recharacterizing transactions on the basis of “facts and circumstances”, analysing functions, assets and risks and searching for comparables that are shown by both theory and practice not to exist (or, where they do exist, to be

very few in number). In this manner, the principle becomes, in reality, largely a matter of negotiation between tax authorities and multinational enterprises, with no clear criteria for application. To be implemented efficiently, the principle requires significant institutional capacity and human resources at levels that are difficult for even OECD member countries, let alone for developing countries (Picciotto, 2016). Various academics have suggested that instead of using the arm's length principle, "unitary taxation" should be adopted which entails treating a multinational enterprise as a single firm for taxation purpose. Furthermore, that "formulary apportionment" should be adopted to ensure that the share of an enterprise's global income that is taxed by a country depends on the fraction of the enterprise's economic activity in that country (Cockfield, 2004; Avi-Yonah and Tinhaga, 2014). Academics argue that formulary apportionment addresses the economic reality of multinational enterprises (Cockfield, 2004) and that it provides a reasonable, administrable and conceptually satisfying compromise that suits the nature of the global economy. It is also argued that a formulary apportionment will eliminate the incentive to shift income to low-tax jurisdictions, given that business entities would be taxed on the basis of their global tax exposure (Avi-Yonah and Clausen, 2008). It has been suggested that, given the transfer pricing challenges that developing countries face, unitary taxation with a formulary apportionment would be clearer and easier to administer (Durst, 2014). It would help to minimize transfer prices for inputs, allocating overhead costs (general administration and other joint costs) and financing expenditure. A unitary approach, together with a country-by-country reporting on revenue, could assist in the development of better tax policies for the extractive sector that are sensitive to the risks and costs associated with multinational enterprises (Siu and others, 2015). Formulary apportionment has long been permitted under international tax treaty rules. Article 7 (4) of the United Nations Model Double Taxation Convention and article 7 (4) of the 2010 version of OECD Model Tax Convention permit the apportionment of total profits. The OECD transfer pricing guidelines also accept the use of profit-based methods, such as the "transaction

profit split method" and the "profit split" method (which requires the combined profit to be split among the connected parties) to determine an arm's-length price (Organization for Economic Cooperation and Development, 1995). Even the United Nations Practical Manual on Transfer Pricing for Developing Countries contains recommendations that, in a transfer pricing audit, tax authorities should (among other documents) request a group global consolidated basis profit and loss statement and a ratio of taxpayer's sales towards group global sales for five years. Many advanced pricing agreements that tax authorities enter into in order to resolve transfer pricing disputes are also based on the profit split method (Oguttu, 2006a). Different models of formulary apportionment have also long operated with relative success in federal systems with State taxation, such as in Brazil (Falcão, 2011), Canada, Switzerland and the United States of America (Picciotto, 2016). In October 2016, the European Commission relaunched the common consolidated corporate tax base, under the terms of which an apportionment formula will be used to calculate each European Union member State's tax share of a multinational enterprises profits at its own national tax rate.

Notwithstanding the perceived advantages of formulary apportionment and the examples of how it has been applied around the world, African countries should be aware of the risks associated with it. It requires countries to agree on a formula, which could prove impossible and probably create tensions (Arnold and McIntyre 2012). Such a formula could disenfranchise developing countries, given that an arbitrary predetermined formula could be difficult to apply, depending on the specific circumstances of each multinational enterprise. For example, the amount of profits attributed to each subsidiary may differ from the income shown on its books of account, even though they may be kept in good faith. Formulary apportionment would intrude on countries' tax sovereignty because countries would need to reach agreement on a set of common rules at the supranational level that would determine how much revenue each State would collect from cross-border transactions. It may, for example, require the harmonization of corporate tax bases and possibly even tax rates (McDaniel, 1994).

If coordination is weak, then this approach may lead to a shift towards formulas favouring sales by destination, which has been the case in the United States. This can create problems if a company sells in a country where it has no taxable presence (Picciotto, 2016). The OECD base erosion and profit shifting action plan rejects a radical switch to a formulary apportionment system in resolving transfer pricing problems. Rather, it advocates building on the existing arm's-length principle. Nevertheless, under action 10, OECD recommends that the "transaction profit split method", which uses some form of apportionment, can provide solutions for unique intangibles and highly integrated operations. The OECD acknowledgment of the advantages of apportionment formulas and the international trends in using the approach indicate that there is a need for the international community to seriously consider this approach as a long-term solution to transfer pricing. The current varying approaches in the use of formulas is, of course, not good for international trade. Some research has already been carried out not only on the long-term issues of design of such a system, but also on the short-term implications of moving towards a unitary approach (Ibid.). Action 13, which requires country-by-country reporting, can also be used to facilitate the application of formulary apportionment. It is advisable that regional bodies, such as Africa's Regional Economic Communities, first develop strong economic groups by harmonizing their tax systems.

Civil society's alternative approach to country-by-country reporting

Action 13 of the OECD base erosion and profit shifting project recommends that countries enact domestic legislation and sign treaties to enable country-by-country reporting of multinational enterprise income. Such reporting has the potential to be particularly valuable for African countries, given that they often lack good data on which to base their judgments on cross-border compliance risks. It should be noted, however, that the modern version of the country-by-country reporting was first suggested in 2003 by Richard Murphy, co-founder of the Tax Justice Network, as a tool to limit corporate tax abuse

by multinational enterprises, with a specific emphasis on ensuring transparency for the benefit of developing countries (Murphy, 2012). The viability of the reporting was examined by OECD when it set up an informal tax and development taskforce in 2010 (Organization for Economic Cooperation and Development, 2010), and it was ultimately included in action 13 of the OECD base erosion and profit shifting project. Country-by-country reports will only be available to tax administrations. NGOs are concerned, however, that reporting to tax administrations may not be that effective in curtailing the malfeasance that it is intended to address. The Tax Justice Network (2015) suggested that country-by-country reports should be made public, given that doing so would enable national tax authorities to gain access to them easily and would allow analysts, journalists or activists the opportunity to hold multinationals accountable. Public reporting will ensure fiscal transparency and bring an end to secretive tax haven transactions. In May 2016, more than 300 leading economists and lawyers also appealed to Governments to adopt global rules requiring companies to publicly report taxable activities in every country in which they operated and to ensure that all territories publicly disclosed information about the real owners of companies and trusts (UN General Assembly 2016). Multinational enterprises reject public reporting on the grounds that the reports may contain commercially confidential information, such as trade secrets, that they may not want to be made public. NGOs argue that concerns about confidentiality can be alleviated by providing such reports in a redacted manner, namely, by removing sensitive information about their trade (Financial Transparency Coalition, 2015).

Even though multinational enterprises lobbied against public reporting, and it was excluded from the OECD's country-by-country reporting standard, civil society still contends that the reporting standard undermines transparency, weakens accountability and is likely to worsen existing inequalities in the international distribution of corporate taxing rights. It is also likely to strengthen the relative ability of rich OECD countries to tax multinationals, at the expense of developing countries, which will exacerbate the inequality in the distribution of

taxing rights between rich and poor countries, falling short of levelling the playing field.

Calls for an alternative global tax authority instead of the Organization for Economic Cooperation and Development

To ensure that the interests of all countries are protected, developing countries, a number of researchers and NGOs have suggested the establishment of a global tax body. This call is based on concerns that OECD, which is currently at the forefront of driving the reform of international tax rules, presents the interest of rich developed countries and does not effectively represent the interests and views of developing countries (Cockfield, 2006). Suggestions have been made that the global tax authority should be established under the auspices of the United Nations, which would function as a neutral and inclusive norm-setting body for international tax cooperation at the intergovernmental level and together with regional bodies such as the African Tax Administration Forum (Tax Justice Network, 2015). Compliance with its recommendations could be achieved by establishing an international dispute forum and/or by making its benefits conditional upon a country's compliance (Oxfam, 2014). However, at the Third International Conference on Financing for Development, held in Addis Ababa in 2015, the suggestion by developing countries that the United Nations Committee of Experts on International Cooperation in Tax Matters should be transformed into a United Nations global tax body was blocked by developed countries. The debate on this matter revealed that African countries are not coordinating around a common position on this issue because domestic and possibly regional concerns continue to trump continental ones (Lei Ravelo, 2015). Nevertheless, renewed calls for a United Nations global tax body are being pushed by the Group of 77 countries, in particular by countries such as Ecuador (Edwards, 2017). African countries need to present a united front in supporting this call.

High-level Panel on Illicit Financial Flows from Africa's alternative approach to curtailing illicit financial flows and related base erosion and profit shifting activities

As indicated in section 2, ECA supports the report of the High-level Panel on Illicit Financial Flows from Africa, which adopts a broad definition of illicit financial flows and which includes specific base erosion and profit shifting activities. After the release of the report, the African Union passed a special resolution on illicit financial flows in June 2015 (African Union Assembly, 2015), in which it requested ECA, the African Development Bank and the regional economic communities to submit annual reports on the progress on the countermeasures to illicit financial flows. In its resolution, the African Union called for capacity-building for member States on matters such as tax management, regulatory and legal frameworks, money-laundering, asset recovery and repatriation and the governance of natural resources. It also called for international cooperation on illicit financial flows to be highlighted in the post-2015 development agenda.

The High-level Panel, in its report, requested the Bank for International Settlements to publish the data that it holds on international banking assets by country of origin and destination in a matrix format, along the lines of the data published by IMF for bilateral trade, FDI and portfolio investment, to inform the analysis of illicit financial flows from Africa (BIS 2016). These data are now available on the BIS website for some countries and territories (BIS, 2018). It was also recommended in the report that countries should require the public availability of disaggregated financial information on multinational enterprises, which should disclose beneficial ownership information. There are also recommendations that countries should adopt an elaborate global governance framework for asset freezing, management and the repatriations of persons involved in illicit financial flows (African Union and Economic Commission for Africa, 2015). One interesting development, by the Government of Norway, is the plan for an independent audit of all its bilateral debt owed by seven developing countries, including Egypt, Somalia, the Sudan and Zimbabwe (Deloitte, 2013). Norway has been at the forefront of efforts to address issues of odious debt (European Network on Debt and Development, 2007). The aims of the audit are to promote financial transparency and to test the

Principles on Promoting Responsible Sovereign Lending and Borrowing, which were launched by UNCTAD in 2012. It is also recommended in the report that there was a need to establish or strengthen independent institutions and agencies of Government responsible for preventing illicit financial flows, including, but not limited to, financial intelligence units, anti-fraud agencies, customs and border agencies, revenue agencies, anti-corruption agencies and financial crime agencies. As such, all such agencies should render regular reports on their activities and findings to national legislatures. In addition, the report recommends for countries to create methods for effective information-sharing and coordination among various institutions and agencies and that they should put in place robust mechanisms for the supervision of banks and financial institutions. Other recommendations include, but are not limited to, increasing the salaries of civil servants, triangulating data by updating company registries, changing procurement practices by not awarding tenders to persons related to government officials and following the Scandinavian concept of placing politicians' companies in trust for the duration of their political term and disallowing such trusts from engaging in government businesses.

Conclusion

In this section, it is contended that addressing base erosion and profit shifting and related illicit financial flows in Africa should be about more than strengthening anti-tax avoidance laws. There are “low-hanging fruit” solutions that can be reaped in the short term, for example, capacity-building issues that are pertinent to solving certain base erosion and profit shifting problems that African countries can adopt to ensure revenue mobilization. African countries should also be open to alternative approaches to solving these problems, as recommended by the United Nations, civil society, regional bodies and academics. In effect, the African approach should encompass the principle of “common but differentiated responsibility”, which recognizes that, although all States may participate in international response measures aimed at addressing international problems, there should be differing approaches and obligations

on States by recognizing differences in their priorities and perspectives as well as in their economic and technical capacity to tackle these problems (Centre for International Sustainable Development Law, 2002). This implies that finding solutions to base erosion and profit shifting and illicit financial flows in Africa will require customized African solutions to African problems, as elucidated in the African Union's New Partnership for Africa's Development and its Agenda 2063 (African Union Commission, 2015), reaffirmed in the Addis Ababa Action Agenda of the Third International Conference on Financing for Development (United Nations, General Assembly, 2015a) and in the report of the High-level Panel on Illicit Financial Flows from Africa.

Section 6: Key policy recommendations and conclusions

The purpose of this report was to take a closer look at the issue of base erosion and profit shifting from an African perspective and to present some policy measures for African policymakers to consider alongside the base erosion and profit shifting package. This report is based on the premise that aggressive tax avoidance practices that bring about base erosion and profit shifting are illicit in nature. Curtailing base erosion and profit shifting comprehensively therefore requires taking on board not only the OECD recommendations to revamp anti-avoidance provisions but also alternative measures to attack the secretive nature of these practices, which often results in illicit financial flows. The report centres on three key components: implementing the base erosion and profit shifting action plan from an African perspective, the efforts that African countries have undertaken to address base erosion and profit shifting at the national level (illustrated by case studies from Cameroon, South Africa and the United Republic of Tanzania) and a discussion of existing or emerging policy measures that African countries can consider, given that the base erosion and profit shifting package is widely expected to be adopted.

The country case studies provided some interesting insight into the various levels of progress that African countries have made towards curtailing base erosion and profit shifting. The United Republic of Tanzania is a resource-rich country that has had limited involvement in the base erosion and profit shifting consultation process. Nevertheless, it has made considerable efforts towards tackling tax evasion and corruption that contribute to base erosion and profit shifting. It has also made efforts to review its tax laws and limit the abuse of favourable tax concessions, especially in the extractive industries. Most notably, the Government has developed transfer pricing guidelines based largely on the OECD transfer pricing guidelines and the United Nations Practical Manual on Transfer Pricing for Developing Countries. Cameroon has also taken measures that can curtail some base erosion and profit shifting schemes, including plans to

establish a transfer pricing unit and, modifying the anti-avoidance regulations of the 2007 Finance Law, which also outlaws the deduction of payments made to countries considered to be tax havens for corporate and income tax purposes. Notwithstanding these proactive steps, expert capacity and skill remains a major issue. South Africa faces a unique challenge in straddling the demands posed by the base erosion and profit shifting package, given that it is the only African country that is part of the Group of 20 and took part in the development of the base erosion and profit shifting agenda. It has taken a strong regulatory oversight role on capital flows to monitor potential avenues of base erosion and profit shifting, while retaining the benefits of liberalized capital markets. It must, however, ensure that the introduction of new measures does not endanger the competitiveness of its home grown multinational enterprises.

It is shown in the report that African countries have been vocal about the base erosion and profit shifting issues that are of greatest concern to them. These include a general lack of specific anti-avoidance legislation; limited skills in conducting transfer pricing analysis; a lack of databases to conduct transfer pricing comparability analyses; unsustainable tax incentives and exemptions, especially with respect to the extractives sector; and limited reciprocity from developed countries regarding the exchange of information on tax matters owing to administrative challenges and confidentiality concerns from developed countries. In recognition of these challenges, section 5 provided alternative and complementary policy approaches that African countries could adopt, while considering the base erosion and profit shifting package. Actions such as the unitary tax approach and regional collaboration have much merit and could be further examined and developed under the auspices of a global tax body. While tax incentives are still perceived as a bargaining tool to attract FDI, African countries need to carry out a cost-benefit analysis of these tax incentives to determine their efficiency and to curtail the

harmful tax practices of tax incentives that lead to a race to bottom, given that tax avoidance is often enabled by asymmetry of tax legislation and enforcement practices. Increased collaboration with neighbouring countries and regional bodies would certainly improve the capacity to expose the base erosion and profit shifting practices of multinational enterprises. Meaningful policy reforms can be realized only by cooperative efforts between neighbouring countries. It is also essential that African countries continue efforts to strengthen tax enforcement and reduce avenues for corruption that enable base erosion and profit shifting. Lastly, the proposals put forth in this report are not exhaustive; rather, they are intended to stimulate further discussion on approaches to base erosion and profit shifting, which may be more conducive to the dynamics of African countries. There is no doubt that these discussions will continue as the global landscape for taxation evolves in the coming years.

In the light of the above, the key legal, political and technical recommendations that should be implemented at the national or regional levels in the short term and long term are highlighted in tables 4 to 7. The rationale is that, because the economic and administrative levels of development differ among African countries, the short-term recommendations are a crucial first step for all countries on the continent. Countries that have already implemented these short-term recommendations should look into implementing the long-term recommendations. In addition, all countries should continue to strategize on all the recommendations by reflecting periodically on their progress in the short term and medium term.

Table 4: Key policy recommendations that African countries should embark on at the national level in the short term

Political level	Legislative level	Administrative level
<ol style="list-style-type: none"> 1. Develop the political will to address base erosion and profit shifting 2. Address weaknesses in public financial management 3. Address harmful tax practices emanating from granting non-strategic tax incentives that lead to a race to the bottom 4. Join and support the African Tax Administration Forum 5. Identify and curtail malpractices, inefficiencies and corrupt operations within the tax structures 6. Enact legislation to protect whistle-blowers and witnesses who want to share information on corporate tax malpractice 7. Stop political interference in tax administration 8. Root out discretionary powers given to tax authorities, given that they often encourage corruption 9. Support calls for a United Nations global tax body 10. Strengthen institutional relationships between authorities charged with addressing base erosion and profit shifting, such as finance ministries, revenue authorities and ministries of trade and investment, which will enable monitoring investment flows 	<ol style="list-style-type: none"> 1. Enact relevant international tax laws to curtail base erosion and profit shifting and consider best practices and common approaches under the base erosion and profit shifting project 2. Strengthen the enforcement of tax laws, remove unnecessary tax breaks and close the most obvious loopholes in the tax architecture through annual amendments 3. Form tax commissions to review domestic tax codes and to consider how to implement priority base erosion and profit shifting actions points, including not only those under the OECD base erosion and profit shifting project, but also the alternatives discussed in section 5 4. Consider aligning domestic laws and tax treaties so that they are in line with international standards, especially the United Nations Model Double Taxation Convention approach 5. Develop a tax treaty policy 6. Develop tax treaty negotiating capacity and renegotiate abusive tax treaties 7. Enact legislation to enable the international exchange of information on tax matters and country-by-country reporting 8. Enact legislation to ensure that domestic accounting and legal firms and banks are more transparent about their affairs with multinational enterprises 9. Follow the transfer pricing recommendations in the United Nations Practical Manual on Transfer Pricing for Developing Countries 10. Enact legislation to prevent the artificial avoidance of the permanent establishment concept by adopting the OECD recommendations, with a new "significant presence" test for the digital economy 11. Ensure that renegotiated and new tax treaties include article 7 (4) of the United Nations Model Double Taxation Convention, which permits the use of apportionment formulas using data provided in country-by-country reports 	<ol style="list-style-type: none"> 1. Develop and strengthen tax administration capacity 2. Develop and strengthen the legal policy unit at the Ministry of Finance 3. Overhaul outdated tax administrative systems and automate tax systems 4. Prioritize improvements in overall tax administrations as a precursor to adopting base erosion and profit shifting-specific interventions 5. Establish well-resourced transfer pricing units and seek to secure access to a global comparables databases, while exploring alternatives to transfer pricing and anti-money laundering 6. Require robust local filing requirements, as Vietnam has done 7. Seek transfer pricing advisory assistance (e.g., through the United Nations) 8. Build knowledge capacity in international tax matters 9. Adopt a policy to hire and retain competent tax officials in various fields, such as accountants, lawyers and economists, who understand and can administer complex international tax laws, and ensure their continuous training 10. Adopt a policy to retain competent tax officials by paying them salaries that are comparable to those in private practice 11. Support the setting up of institutions of tax learning on the continent 12. Support calls by NGOs for public country-by-country reporting of the global incomes of multinational enterprises and require direct filing of global country-by-country reports by local subsidiaries of foreign multinational enterprises 13. Enlist African tax experts to conduct research on African tax issues and contact the African Tax Administration Forum/African Tax Research Network 14. Confer with other African countries to provide guidance on resolving similar challenges

Table 5: Key policy recommendations that African countries should embark on at the national level in the long term

Political level	Legislative level	Administrative level
<ol style="list-style-type: none"> 1. Support calls for a United Nations global tax body 2. Set aside funding for research on multinational enterprises by tax policy officials, national statistical offices and academics to improve the understanding of base erosion and profit shifting 	<ol style="list-style-type: none"> 1. Enact relevant international tax laws to curtail base erosion and profit shifting and consider best practices and common approaches under the base erosion and profit-shifting project 2. Review laws periodically 3. Monitor relevant international tax law developments to curtail base erosion and profit shifting and illicit financial flows 	<ol style="list-style-type: none"> 1. Invest in resources to compile data on FDI associated with resident special purpose entities, trade in services and intangible investment 2. Support institutions set up to develop tax learning on the continent

Table 6: Key policy recommendations that African countries should embark on at the regional level in the short term

Political level	Legislative level	Administrative level
<ol style="list-style-type: none"> 1. Sign up and commit to obligations relating to tax policy in regional agreements 2. Ensure the exchange of information on tax matters with countries in the region and from customs databases and beneficial ownership registries 3. Discuss a regionally coordinated way forward on the possible alternatives to transfer pricing by reflecting on unitary tax and formal apportionment 	<ol style="list-style-type: none"> 1. Commit to regional initiatives to ensure tax coordination 2. Ensure tax cooperation and the exchange of information in tax matters 3. Curtail harmful tax competition involving tax incentives and a race to the bottom 4. Set up an African Union/ECA tax committee comprising African tax experts 	<ol style="list-style-type: none"> 1. Continue to develop regional agreements on mutual assistance in tax matters 2. Develop regional model tax conventions 3. Develop a regional approach to international tax law and treaty negotiation 4. Support setting up institutions of tax learning on the continent

Table 7: Key policy recommendations that African countries should embark on at the regional level in the long term

Political level	Legislative level	Administrative level
<ol style="list-style-type: none"> 1. Develop a regional approach to cross-border tax 2. Enact regional laws on cross-border activities 3. Ensure tax coordination in matters pertaining to curtailing base erosion and profit shifting by multinational enterprises 4. Review tax treaty policy 5. Develop tax treaty negotiating capacity and continue the renegotiation of abusive tax treaties 	<ol style="list-style-type: none"> 1. Consider developing regional model tax conventions that contain article 7 (4) of the United Nations Model Double Taxation Convention and permits the use of apportionment formulas, using data provided in country-by-country reports 2. Support calls for a United Nations global tax body 3. Set up an African Union/ECA tax committee comprising African tax experts 	<ol style="list-style-type: none"> 1. Explore alternatives to arm's-length principle, such as formulary apportionment at the regional level 2. Support the setting up of institutions of tax learning on the continent 3. Have regional meetings on tax matters 4. Explore alternatives to the arm's-length principle, such as unitary taxation and formulary apportionment

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