

14TH ANNUAL INTERNATIONAL TAX CONFERENCE

“International Tax in a Digital Era”

March 3, 2023

Tax certainty in an uncertain environment

First, it’s an honour to be asked to provide this keynote speech. My only regret is that I am not with you today since I see many of my good Indian friends in the audience. It’s also almost three years since I last visited India and I do miss my regular trips to your country.

I had thought of focusing on the BEPS Pillar Two solutions but so much has been discussed on this that I felt I would have little new to say (although I will touch on some of these issues). So my focus will be on how to achieve greater tax certainty in an uncertain political and economic environment.

I will first try to define tax certainty, then explore the different initiatives to achieve it, make some suggestions on how to move forward with the debate on mediation and arbitration, and finish by looking at a neglected topic of cross-border VAT disputes.

I will not use any power point so you will have to focus on what I say!

A - Current political and economic uncertain environment

Over the last decade and a half the world has gone through three crisis

- in 2007/8 we had the Lehman Brothers crash which in the absence of a strong G20 response would have brought down the global financial system (the first success of the G20)
- before countries had fully emerged from this crisis we had the COVID pandemic which disrupted both domestic markets and global supply chains
- And this was followed by the Russian/Ukrainian war which led to the spike in energy and food prices which in turn resulted in double-digit rates of inflation that most countries had not seen since the 1970s.

The three crises disrupted world trade and FDI flows (it took almost a decade for FDI to recover to the pre-2007 levels) but also lead to the rise of populism, a call to reverse globalisation, the spread of tax transparency and the call for MNE and HNWI to pay their fair share of the tax burden.

These events saw governments' deficit increase as expenditures on health, defence, and supporting firms and workers, expanded to unprecedented levels whilst tax revenues declined.

Developing countries were badly hit especially by the increase in food prices and the cost of servicing their public debt. As the head of the IMF said at the recent G20 Finance meeting hosted by India these setbacks have reversed the gains made over 4 decades in reducing poverty.

India came through these crises better placed than most countries and is slowly- too slowly in my view - taking advantage of the move away from globalisation characterised by “ just in time” to one characterised by ‘ just in case ‘, namely attracting investment from China.

So this is the backdrop against which we must see the current G20 lead debate on the need to provide greater tax certainty.

B - What do we mean by tax certainty?

Tax certainty means that the tax administration acts in a predicable, consistent, and fair way so that taxpayers are able to know in advance of a transaction what are the tax consequences.

The taxpayers also need to know that if disputes arise they will be resolved quickly and in a principal fashion

None of this is easier to achieve in a fast-changing international tax environment.

C - The current BEPS Two Pillar solution

One can argue about the merits of these proposals- about what principles underlie pillar1, about whether we will get a consistent implementation of the new standards, about whether governments are underestimating the compliance cost for business - but there is one certainty; during what will be a long transitional period this initiative will lead to greater tax uncertainty! And the risk is that this can curtail FDI.

D - What are the Current mechanisms to minimise and resolve disputes at the international level

(1) Minimising cross-border direct tax disputes here we have some positive developments:

- The spread of APA and the gradual move to make these multilateral rather than unilateral
- The spread of rulings
- More countries signing up to ICAP
- The take up of cooperative compliance programs (what our Dutch colleagues call horizon monitoring).

This was a concept I launched when I headed up the OECD tax work and it has spread to many countries (not India unfortunately). These programs are what ex-president Trump would call “a deal”: the taxpayer provides greater transparency in return for the tax administrations providing greater certainty. It is all about changing the nature of the dialogue between taxpayers and tax administrations moving it from you-win-I-lose mentality to one of you-win-and-I-win. We at WU published in 2021 a handbook on how to implement CC programs and we are currently working with over 15 countries on how to do this. I would very much like to see India engage in this Multi-stakeholder group.

Overall we need a more open, constructive, and respectful dialogue between Tax Administrations and taxpayers which would go a long way to minimise tax disputes.

(2) Resolving cross-border direct tax disputes in the context of tax treaties

The main mechanisms used to resolve these disputes are found in Article 25 namely the MAP. After the BEPS recommendations and the creation of the FTA MAP forum MAP has improved but:

- new MAP cases are still being added at a quicker pace than old MAP cases are resolved so the inventory continues to grow
- Access to MAP is constrained in some countries
- Taxpayer participation is limited
- It can take years to resolve a case
- And there is no obligation on the competent authorities to come to a resolution.

These shortcomings have led the OECD to push forward the concept of mandatory arbitration, both as part of its multilateral convention and the pillar 1 proposals. But it’s fair to say that the

vast majority of non-OECD countries - including most LDC and India – remain sceptical. I will return to how we can unblock this situation later.

Also last year I worked with the UNCTC to produce a handbook that LDC could use to both minimise and resolve tax disputes - including by mediation - and hopefully, this will encourage LDC to have greater confidence in the MAP process.

(3) Using bilateral investments agreements

India has seen a number of high-profile tax disputes which have ended up in IIAs arbitration panels. In fact, over the last decade, more than 165 tax disputes worldwide have ended up in these panels. Some have had tax as the major issue (e.g. Yukos), others a secondary issue. Vienna, working with UNCTAD, just completed an analysis of these cases which showed that the main issues centered on national treatment, non-discrimination, and fair and equitable treatment. Roughly half the cases were resolved in favour of the taxpayer and half in favour of government.

Nevertheless, I am not keen on having tax disputes brought into IIA panels (which often don't have much tax expertise) but if we the tax community, can't improve the mechanisms we have to resolve the dispute this trend will continue.

E - What more can be done?

The short answer is that we must overcome the reluctance of non-OECD countries including India, toward mandatory arbitration. Over the years I have talked to many of these countries to understand their concerns, many of which are legitimate.

The concerns can be divided into two categories:

Procedural

- MAP is slow and costly
- it lacks transparency
- the arbitrators are a small group, mainly white males from OECD countries, who may not be familiar with the situation in LDC
- LDC do not always have the expertise to prepare for arbitration

Political

- Arbitration infringes on a country's sovereignty

- and is contrary to the constitution

Let me first deal with the two political concerns:

Sovereignty: every time you sign a treaty you give away a part of your freedom to design laws.

Arbitration is no exception

Constitution issues: when I was pushing the concept of arbitration at the OECD this was an argument that I often heard include from big countries such as Japan, U.K., and US

On closer examination, it was clear that these claims were false, and my discussion with some judges here in India suggests that the same applies here.

Procedural concerns: These are legitimate but they can be addressed.

Over 5 years ago I published a proposal for an UN-based disputes panel that would:

- Set up objective criteria for the selection of arbitrators so we get more representative samples
- Creation of a permanent roster of qualified arbitrators from which countries have to choose
- A cap on cost (Arbitrators without borders!) TIWB
- Greater transparency by publishing a redacted version of decisions
- Programs to build up the capacity of ÇA in LDC by for example, requiring any person who is appointed as an arbitrator to be shadowed by a young person from an LDC thereby building up the next generation of arbitrators.

All of these proposals would help build confidence in the integrity of the process, especially if the panel was under a UN umbrella

Yes, I know this will take time but with the resolution passed by the UN this February to create a more inclusive framework for tax cooperation there is now an opening to move forward with this proposal.

One last point: up to now I have focused on direct tax disputes, yet what I have seen as part of a study that Vienna is undertaking with the ICC tax committee is that cross-border disputes are growing in the area of VAT/GST. This should not surprise us since more than 160 countries now have these taxes and with the growth of eCommerce and digital services, there is more scope for conflict. Unresolved VAT disputes impact the liquidity position of companies and can affect location decisions.

What we are aiming to do is to analysis the causes of the disputes and come forward with new ways (e.g. mediation) to resolve them. I would very much like to have the Indian business community engaged in this work (just email me)

Let me conclude this presentation with a few suggestions on what measure India could take domestically to improve tax certainty.

India could try to minimise tax uncertainty in a number of ways:

I. at the level of tax policy, by ensuring that:

1. the legislation is unambiguous and clear, leaving no or little room for unintended misinterpretation,
2. the legislation realises the policy aims determined by the Government
3. the legislation should be as much as possible in line with international standards and best practices, both in terms of content and administrative practice
4. the legislation needs to be based upon a ‘principle’ based approach

II. at the administration level by ensuring that:

1. the administration is incentivised and capable to apply the tax legislation in accordance with the letter and spirit of the law;
2. it is supported by efficient and effective administrative and IT platforms;
3. social skills and tools to ensure compliant taxpayers are served as efficiently as possible by providing clarity on the taxation positions in as early as possible a stage;
4. guidelines, safeguards, tools, and skills ensure that non-compliant tax-payers are identified and appropriately curbed;
5. the response of the tax administration should be proportional to the behaviour of the taxpayers;
6. checks and balances should be in place to ensure that the elements above are continuously guaranteed, including through the availability of mediation processes and well-functioning administrative and judicial appeal procedures; and
7. metrics are established for evaluation measures of success in achieving high compliance that go beyond simple revenue yield measure.
8. Business also has a role in achieving greater tax certainty by being open and transparent in its dealings with tax administrations and respecting the spirit and letter of the law

Conclusion

We live in uncertain times. Our economies are held back by a reluctance of MNEs to invest in sustainable and inclusive investments. We must avoid that taxation adds to this uncertain environment. Here India with its presidency of the G20 could play a lead role.

Happy to answer questions.