

Co-Lead's Concept Note on Ideas for Potential Solutions [24 October 2025]

Submission on Workstream III (Protocol 2)

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ABSTRACT

This submission addresses the Co-Lead's Concept Note for Potential Solutions: Protocol 2. The analysis identifies a fundamental jurisdictional lacuna arising where no bilateral tax treaty exists between disputing states, questioning whether genuine tax disputes can exist absent agreed substantive frameworks for allocating taxing rights. Through concrete examination of digital economy taxation scenarios, the submission demonstrates that the absence of treaty relationships generates authentic cross-border conflicts where states advance competing legal claims over the same income streams, yet no shared legal instrument exists to adjudicate these claims. The submission proposes a tripartite framework distinguishing disputes falling within Protocol 1's digital economy scope, disputes outside Protocol 1 but within the Framework Convention's purview, and disputes involving non-party states, with differentiated resolution mechanisms appropriate to each category. Recognising that optionality in dispute resolution mechanisms risks reproducing asymmetric power relations wherein economically dominant states selectively apply procedures to secure advantages whilst avoiding obligations, the submission advances mandatory safeguards against discriminatory application through a comparable treatment clause establishing rebuttable presumptions of mechanism availability across similarly situated disputes. Finally, the submission advocates establishing a United Nations Tax Dispute Resolution Centre with governance structures ensuring developing country representation, capacity-building functions, and transparency mechanisms. Throughout, the analysis confronts tensions between sovereign fiscal autonomy and the necessity for international coordination, proposing legal architecture that respects domestic jurisdiction whilst providing effective frameworks for resolving genuine cross-border tax conflicts that domestic systems alone cannot adequately address. The Committee on Fiscal Studies made submission during the Third Session held in Nairobi in November, and respectfully asks the Chair and Co-Leads to also make reference to those submissions in addition to these.

I. THE NO-TREATY JURISDICTIONAL LACUNA

A. The Problem Defined

1. The Concept Note acknowledges that many countries have limited treaty networks, leaving them without mechanisms to resolve disputes that may arise. Paragraph 16 notes “broad interest was expressed in further exploring the feasibility of multilateral mechanisms to address ‘no-treaty’ situations.” However, the Concept Note fails to address the fundamental legal question: what constitutes a “dispute” absent a substantive legal framework allocating taxing rights?
2. Consider a concrete example demonstrating this lacuna. Kenya and China have no bilateral tax treaty addressing taxation of digital services, data collection, or user-generated value. A Chinese technology company operates a digital platform serving Kenyan users, collecting data on Kenyan consumers, and deriving revenue from Kenyan advertisers, but maintains no physical presence in Kenya. Kenya assesses corporate income tax on the platform’s Kenyan-source income under its domestic law, which Kenya has amended to assert taxing rights over digital services provided to Kenyan users regardless of physical presence.
3. China objects to this assessment, arguing that without a bilateral tax treaty, Kenya lacks jurisdiction to tax a Chinese resident company with no permanent establishment in Kenya under traditional international tax principles. Kenya responds that its domestic law governs taxation of income sourced within its territory and that China’s position would enable Chinese companies to extract value from Kenyan markets without contributing to Kenyan public finances.
4. This presents a genuine cross-border tax dispute: two states advance conflicting legal positions regarding taxation of the same income derived from the same economic activity. However, this dispute arises not from differing interpretations of a shared legal instrument (a tax treaty), but rather from the absence of any agreed framework allocating taxing rights between the jurisdictions.

B. Legal Questions Requiring Resolution

This scenario raises several interrelated legal questions that Protocol 2 and the Framework Convention must address:

First, does Protocol 2’s scope encompass disputes arising in no-treaty situations, or is it confined to disputes arising from interpretation and application of existing tax treaties? The Concept Note’s paragraph 17 states the protocol “could apply to the range of cross-border tax disputes” and notes “consideration could also be given to the possibility of addressing non-treaty situations.” This language suggests openness but provides no clarity regarding the legal framework that would govern such disputes.

Second, even if Protocol 2 provides dispute resolution mechanisms for no-treaty situations, what substantive law would those mechanisms apply? In treaty-based disputes, mutual agreement procedures and arbitration apply the treaty provisions that both parties have accepted. In no-treaty situations, no such shared legal framework exists. Would dispute resolution mechanisms apply: (a) the domestic law of the source state; (b) the domestic law of the residence state; (c) general principles of international tax law; (d) customary international law; or (e) some combination thereof?

Third, how does digital economy taxation under Protocol 1 interact with dispute resolution under Protocol 2 in no-treaty contexts? Protocol 1 addresses “taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy.” If

Protocol 1 establishes substantive rules for digital economy taxation that apply between States Parties, those rules provide the legal framework that dispute resolution mechanisms under Protocol 2 would apply. However, if two states are both parties to Protocol 1 but have no bilateral tax treaty, and a dispute arises regarding application of Protocol 1's provisions, does Protocol 2 provide the resolution mechanism?

Fourth, must protocols contain interrelated provisions establishing that disputes arising under one protocol are resolved pursuant to mechanisms established in another protocol? Without such provisions, each protocol might require its own dispute resolution framework, fragmenting the system and creating multiple parallel procedures.

Fifth, should the Framework Convention itself, rather than Protocol 2, provide dispute resolution for no-treaty situations? The Convention's Article 20 "Settlement of Disputes arising under the Convention" remains to be drafted. This Article could establish that disputes between States Parties regarding taxation of cross-border income, even absent a bilateral treaty, may be submitted to specified resolution procedures. This approach would locate the dispute resolution framework at the Convention level, with Protocol 2 providing detailed procedural mechanisms that Article 20 invokes.

Sixth, could no-treaty dispute resolution constitute impermissible expansion of international law into domestic tax sovereignty? If State A has chosen not to negotiate a tax treaty with State B, this represents a sovereign decision to retain complete freedom regarding taxation of income arising from transactions with State B. Establishing multilateral dispute resolution for no-treaty situations might override this sovereign choice by creating de facto tax coordination obligations between states that have deliberately avoided such obligations.

Seventh, should no-treaty disputes be handled through domestic judicial systems rather than international mechanisms? The case between Barbados and Trinidad and Tobago, which ultimately reached the Judicial Committee of the Privy Council, demonstrates that domestic and regional courts have resolved international tax disputes absent bilateral treaties. In that matter, questions of fiscal sovereignty, treaty interpretation, and constitutional limits on taxation were addressed through domestic legal frameworks rather than international dispute resolution mechanisms.

C. Proposed Legal Framework for No-Treaty Situations

These questions require careful legal architecture to avoid creating either ineffective procedures or excessive intrusion into domestic sovereignty. The submission proposes the following framework:

First, the Framework Convention should distinguish between three categories of no-treaty disputes:

Category A: Disputes regarding taxation of transactions or income that would fall within the scope of Protocol 1 (digital economy) if both states are parties to that Protocol. For these disputes, Protocol 1's substantive provisions provide the applicable legal framework, and Protocol 2's dispute resolution mechanisms apply to resolve differing interpretations or applications of Protocol 1.

Category B: Disputes regarding taxation of transactions or income falling outside Protocol 1's scope, where both states are parties to the Framework Convention but have no bilateral tax treaty. For these disputes, the Framework Convention's Article 4 (Fair Allocation of Taxing Rights) provides the substantive principle that "every jurisdiction

where a taxpayer conducts business activities, including jurisdictions where value is created, markets are located and revenues are generated, have a right to tax the income generated from such business activities.” Disputes concerning application of this principle may be submitted to Protocol 2’s resolution mechanisms on a voluntary basis, with both states required to agree to submit the specific dispute for resolution.

Category C: Disputes where at least one state is not a party to the Framework Convention. For these disputes, Protocol 2 provides no jurisdiction, and domestic legal systems or other international frameworks would govern.

Second, Protocol 2 should establish that for Category A disputes (falling within Protocol 1’s scope), the Protocol 1 provisions constitute the applicable law, interpreted in accordance with the Vienna Convention’s treaty interpretation rules. The Protocol 2 text should state:

“Where a dispute arises between States Parties to Protocol 1 regarding the interpretation or application of that Protocol’s provisions, such dispute may be submitted to the dispute resolution mechanisms established in this Protocol. The provisions of Protocol 1 shall constitute the applicable law, interpreted in accordance with Articles 31-33 of the Vienna Convention on the Law of Treaties.”

Third, for Category B disputes (outside Protocol 1 but within Framework Convention scope), Protocol 2 should provide that Article 4’s principle of fair allocation of taxing rights constitutes the applicable standard, supplemented by relevant provisions of Articles 5-9 as applicable. However, recognising that Article 4 establishes a broad principle rather than detailed allocation rules, the protocol should provide that dispute resolution in these cases proceeds only where both states agree to submit the dispute and further agree on interpretive principles to be applied. The text should state:

“Where a dispute arises between States Parties regarding taxation of cross-border income or activities, and the States Parties have no bilateral tax treaty or other legal instrument providing a framework for allocation of taxing rights, either State Party may propose submission of the dispute to the mechanisms established in this Protocol. Such submission requires the agreement of both States Parties and written agreement on: (a) the specific questions to be resolved; (b) the legal principles and interpretive standards to be applied, which shall include but need not be limited to Article 4 of the Framework Convention; and (c) the procedure to be followed, including whether the outcome shall be binding or advisory. In the absence of such agreement, each State Party retains full authority to apply its domestic law.”

Fourth, Protocol 2 should explicitly preserve domestic judicial jurisdiction whilst providing an alternative international mechanism. The text should state:

“Nothing in this Protocol shall preclude taxpayers or States Parties from pursuing resolution of disputes through domestic judicial systems or other available legal frameworks. The dispute resolution mechanisms established in this Protocol shall be available as an alternative to, not a replacement for, domestic legal procedures. Where a taxpayer has initiated judicial proceedings in the domestic courts of a State Party regarding a matter that could be submitted to this Protocol’s mechanisms, both States Parties must agree to submission of the dispute under this Protocol, and such submission shall not divest domestic courts of jurisdiction unless the domestic legal system of the State Party permits such divestment.”

Fifth, the Framework Convention's Article 10 (Prevention and Resolution of Tax Disputes) must be substantially enhanced to establish the connection between Convention-level principles and Protocol 2 mechanisms. The current Article 10 text is insufficient to support the architecture proposed above. The submission proposes amending Article 10 as follows:

“Article 10

Prevention and Resolution of Tax Disputes

1. The States Parties recognize that effective mechanisms for preventing and resolving tax disputes support cross-border investment and trade whilst safeguarding the fiscal sovereignty and domestic resource mobilization capacity of all States Parties.

2. The States Parties shall prioritise prevention of tax disputes through: (a) providing clear and accessible legislation and interpretative guidance regarding tax obligations; (b) implementing domestic dispute resolution mechanisms that are fair, independent, accessible, and effective; (c) engaging in good faith consultation with other States Parties before making tax determinations likely to affect those States Parties' tax bases; and (d) participating in information exchange and administrative cooperation frameworks established under this Convention and its Protocols.

3. Where prevention mechanisms have not averted a cross-border tax dispute, States Parties shall seek resolution through the mechanisms established in the Protocol on Prevention and Resolution of Tax Disputes, taking into account:

(a) The need to resolve disputes expeditiously to avoid prolonged uncertainty for taxpayers and tax authorities;

(b) The importance of outcomes that respect the fair allocation of taxing rights as established in Article 4;

(c) The obligation to engage in good faith negotiations;

(d) The different capacities of States Parties and the availability of technical and financial assistance; and

(e) The availability of domestic legal remedies and the relationship between international dispute resolution mechanisms and domestic judicial systems.

4. Disputes arising from the interpretation or application of this Convention or its Protocols may be resolved through the mechanisms established in the Protocol on Prevention and Resolution of Tax Disputes or through other procedures agreed between the States Parties concerned.

5. Nothing in this Article shall affect the sovereign right of States Parties to apply their domestic tax laws or limit the jurisdiction of domestic courts to resolve tax disputes in accordance with domestic legal systems.”

II. MANDATORY SAFEGUARDS AGAINST DISCRIMINATORY OPTIONALITY

The Concept Note correctly identifies optionality as essential for respecting state sovereignty and accommodating diverse capacities. However, optionality without safeguards enables strategic behaviour where powerful states secure benefits whilst avoiding obligations, reproducing asymmetries that necessitated this Convention.

The principle of reciprocity in treaty law requires that when State A agrees to apply specific mechanisms with State B, it cannot arbitrarily deny equivalent mechanisms to State C facing comparable disputes. This selective application violates the good faith obligation under Article 26 of the Vienna Convention. Most-favoured-nation treatment principles from international trade law establish that parties cannot discriminate among similarly situated partners without objective justification.

Protocol 2 should therefore include a “comparable treatment clause” providing that once a state accepts a mechanism with any party for a particular type of dispute (transfer pricing, permanent establishment, etc.), it creates a rebuttable presumption that the same mechanism is available to other parties with similar disputes. The text should state:

“Article [X]: Comparable Treatment in Optional Mechanisms

1. Where a State Party has agreed to apply a particular dispute prevention or resolution mechanism under this Protocol with respect to a specific category of dispute with one State Party, there shall be a rebuttable presumption that the same mechanism is available to other States Parties with respect to disputes in the same category.
2. For purposes of paragraph 1, dispute categories shall include but not be limited to: (a) transfer pricing disputes; (b) permanent establishment determinations; (c) residence questions; (d) withholding tax disputes; (e) disputes regarding harmful tax practices; and (f) other categories as may be defined by the Conference of States Parties.
3. A State Party may rebut the presumption in paragraph 1 by demonstrating that:
 - (a) Material differences in treaty relationships, legal frameworks, or factual circumstances justify different treatment; or
 - (b) The other State Party lacks the administrative capacity necessary to engage effectively in the particular mechanism, and has declined offers of capacity-building assistance; or
 - (c) The other State Party has previously failed to comply in good faith with obligations under the mechanism when applied in other contexts.
4. Any refusal to extend a mechanism based on grounds specified in paragraph 3 shall be notified in writing to the requesting State Party and to the Secretariat, with reasons provided. The requesting State Party may submit the question of whether the refusal is justified to review by [specified body], whose determination shall be binding.
5. This Article preserves State Parties’ sovereign discretion regarding which mechanisms to adopt, but ensures that once adopted, mechanisms are made available on a non-discriminatory basis to all States Parties facing comparable disputes, subject only to the objective justifications specified in paragraph 3.”

III. INSTITUTIONAL FRAMEWORK: UNITED NATIONS ROLE

The Concept Note raises the question of “potential role of the United Nations in supporting these resolution mechanisms” including “providing assistance to parties” and “hosting or acting as a permanent or ad hoc forum for the resolution of cross-border tax disputes.”

Protocol 2 should establish a UN Tax Dispute Resolution Centre with the following mandate:

“Article [Z]: United Nations Tax Dispute Resolution Centre

1. There is hereby established the United Nations Tax Dispute Resolution Centre (the Centre) to support implementation of this Protocol’s dispute prevention and resolution mechanisms.

2. The Centre shall:

- (a) Maintain rosters of qualified mediators, conciliators, and arbitrators as specified in this Protocol;
- (b) Provide administrative support for dispute prevention and resolution proceedings;
- (c) Develop and publish best practices for dispute prevention;
- (d) Provide technical assistance to States Parties in building capacity for effective dispute prevention and resolution;
- (e) Maintain a public database of resolved disputes (in anonymized form where appropriate) to promote transparency and consistent practice;
- (f) Prepare annual reports for the Conference of States Parties on dispute prevention and resolution activities;
- (g) Convene expert consultations on emerging issues in cross-border tax disputes.

3. The Centre shall be governed by a Board comprising [15] members elected by the Conference of States Parties, with:

- (a) At least 8 members from developing countries;
- (b) Balanced representation across regions;
- (c) Representation including tax administrators, judicial officers, academics, and civil society; and
- (d) Membership rotating to ensure fresh perspectives and prevent entrenchment.

4. The Centre shall be funded through [specified funding sources including mandatory contributions from States Parties allocated based on capacity to pay, with voluntary contributions supplementing mandatory funding].

5. The Centre shall operate independently whilst remaining accountable to the Conference of States Parties through annual reporting, periodic review, and such other accountability mechanisms as the Conference may establish.”

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