SUBMISSION RELATED TO WORKSTREAM III: PROTOCOL ON PREVENTION AND RESOLUTION OF TAX DISPUTES

SUBMITTED BY

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Abstract

First, we argue that prevention must be established as a binding legal obligation grounded in the pacta sunt servanda principle under Article 26 of the Vienna Convention, structured through a three-tier architecture of mandatory information exchange, proactive cooperation mechanisms, and conditional advance resolution. Second, we propose a comparable treatment clause preventing discriminatory optionality whilst respecting sovereign choice. Third, we advance three independent grounds for rejecting mandatory arbitration. Fourth, we address the no-treaty jurisdictional lacuna through a tripartite framework illustrated by the concrete problem of digital economy disputes between states without bilateral treaties. Fifth, we argue that advance pricing agreements should be conditional upon institutional prerequisites, not positioned as a default core mechanism. Sixth, we propose inter-protocol coherence provisions and a functional definition of cross-border tax dispute.

I. Prevention as a Binding Legal Obligation

CENTRAL SUBMISSION: Prevention must be the Protocol's primary obligation, not a secondary aspiration.

The Concept Note treats prevention as secondary to resolution, suggesting states should focus on resolving disputes after they arise. This inverts proper legal architecture. The Vienna Convention on the Law of Treaties establishes that treaties must be performed in good faith. This good faith obligation under Article 26 extends beyond remedying breaches after they occur; it encompasses the prior duty to prevent disputes through proactive cooperation. The International Court of Justice has consistently held that procedural obligations requiring consultation and cooperation constitute independent legal obligations, not merely preliminary steps to substantive compliance. Prevention must therefore be framed as an operative legal obligation with enforceable content.

For developing countries with resource-constrained revenue administrations, this is not a procedural preference but a substantive protection of fiscal sovereignty. The costs of engaging in mutual agreement procedures or arbitration fall disproportionately on developing countries lacking the technical expertise, legal resources, and diplomatic capacity to pursue protracted disputes. Without effective prevention, these jurisdictions effectively forfeit their taxing rights when disputes arise because they cannot afford to defend them. Dispute resolution in such conditions functions not as a neutral procedural mechanism but as a structural advantage for well-resourced jurisdictions.

PROPOSED THREE-TIER PREVENTION ARCHITECTURE:

The first tier comprises mandatory information exchange and transparency obligations. States cannot prevent transfer pricing disputes if they lack information about comparable transactions or the taxpayer's global value chain. Automatic exchange of country-by-country reports must provide both source and residence states simultaneous access to the same information, reducing the informational asymmetry that breeds conflicting assessments. The second tier establishes proactive cooperation mechanisms: simultaneous tax examinations where both jurisdictions audit the same taxpayer concurrently rather than sequentially, joint risk assessment frameworks identifying contentious issues before they crystallise into adjustments, and advance consultation procedures requiring competent authorities to confer before making any determination likely to affect another state's tax base. This consultation obligation must be framed as mandatory good faith negotiation, not discretionary cooperation. The third tier comprises conditional advance resolution mechanisms, addressed in Section V below.

The Protocol should mandate that when a state proposes legislative changes likely to affect cross-border tax treatment, it must notify affected treaty partners and engage in consultative procedures before implementation. This transforms prevention from discretionary cooperation into a justiciable obligation, enabling affected states to invoke non-compliance where prevention procedures are ignored.

II. Safeguarding Optionality: The Comparable Treatment Clause

KEY PROPOSAL: A comparable treatment clause preventing discriminatory application of optional mechanisms.

Optionality is broadly accepted as necessary for respecting sovereignty and accommodating diverse capacities. However, optionality without safeguards enables strategic behaviour where powerful states secure benefits whilst avoiding obligations. 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. Selective application violates the good faith obligation under Article 26 of the Vienna Convention.

PROPOSED DRAFTING LANGUAGE:

> *"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. A State Party may rebut the presumption by demonstrating that: (a) material differences in treaty relationships, legal frameworks, or factual circumstances justify different treatment; (b) the other State Party lacks necessary administrative capacity 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. Any refusal shall be notified in writing with reasons provided. The requesting State Party may submit the question of justification to review by a designated body whose determination shall be binding."*

Dispute categories for which the comparable treatment obligation operates should include but not be limited to transfer pricing disputes, permanent establishment determinations, residence questions, withholding tax disputes, and disputes regarding harmful tax practices. This preserves sovereign discretion regarding which mechanisms to adopt whilst ensuring that once adopted, mechanisms are available on a non-discriminatory basis.

III. Rejection of Mandatory Arbitration

THREE INDEPENDENT GROUNDS against mandatory arbitration.

First, structural bias in arbitrator selection. International tax arbitration has drawn arbitrators predominantly from capital-exporting jurisdictions and professional practices serving multinational enterprises. Even with personal impartiality, pool composition creates systemic bias towards restrictive interpretations of source-country taxing rights, reflecting epistemic communities and professional socialisation rather than neutral application of legal principles. Second, asymmetric costs creating barriers to access. Arbitration costs including arbitrator fees, legal representation, expert witnesses, and administrative expenses create barriers when developing country revenue authorities with constrained budgets face well-resourced counterparts. Resource constraints may prevent effective case presentation or render arbitration economically irrational when potential revenue recovery is less than proceedings costs. Third, negative experiences with investor-state dispute settlement. ISDS arbitration under bilateral investment treaties has systematically curtailed developing countries' regulatory sovereignty, imposed substantial damages for legitimate public policy measures, and created chilling effects that deter fiscal policy innovation. Tax treaty arbitration risks reproducing these pathologies.

Where arbitration is available by mutual agreement on a case-by-case basis, the Protocol must specify safeguards: balanced representation ensuring arbitrators familiar with source-country taxation challenges, interpretive principles giving due weight to source-country taxing rights, progressive cost allocation based on capacity, transparency through published awards with reasoning, and preservation of domestic judicial jurisdiction as an alternative pathway. Mediation and conciliation should be established as the primary mechanisms beyond enhanced MAP, operating through a UN Tax Dispute Resolution Centre with mandated Global South majority representation on its governance board.

IV. The No-Treaty Jurisdictional Lacuna

CRITICAL GAP: The Protocol must address disputes arising where no bilateral treaty exists.

Consider this example. Kenya and China have no bilateral tax treaty addressing digital services. A Chinese technology platform serves Kenyan users, collects data on Kenyan consumers, and derives revenue from Kenyan advertisers without physical presence in Kenya. Kenya amends its domestic law to assert taxing rights. China objects, arguing Kenya lacks jurisdiction under traditional principles. This generates a genuine cross-border tax dispute arising not from differing treaty interpretations but from the absence of any agreed framework. Protocol 2 must address whether its scope encompasses such disputes and what substantive law would apply.

This submission proposes distinguishing three categories:

- Category A covers disputes falling within Protocol 1 scope where both states are Protocol 1 parties; Protocol 1 provides the substantive law and Protocol 2 provides the resolution mechanisms.
- Category B addresses disputes outside Protocol 1 where both states are Framework Convention parties but have no bilateral treaty; the Convention's Article 5 fair allocation principle provides the substantive standard, but submission requires both parties' agreement on questions to be resolved and interpretive principles to apply.
- Category C covers disputes where at least one state is not a Convention party; domestic systems govern. The Barbados and Trinidad and Tobago matter that reached the Judicial Committee of the Privy Council referred to by Co-Lead Marlene demonstrates that domestic courts can and do resolve international tax disputes absent bilateral treaties. Protocol 2 must explicitly preserve domestic judicial jurisdiction: its mechanisms shall be available as an alternative to, not replacement for, domestic legal procedures.

INTER-PROTOCOL COHERENCE: Protocols must contain interrelated provisions establishing that disputes arising under one protocol are resolved pursuant to mechanisms established in another.

Without such provisions, each protocol may require its own dispute resolution framework, fragmenting the system. The Protocol should state:

> *"Where a dispute arises between States Parties to Protocol 1 regarding interpretation or application of that Protocol's provisions, such dispute may be submitted to the dispute resolution mechanisms established in this Protocol."*

The Committee must also address whether the Framework Convention itself, through Article 20, should provide dispute resolution for no-treaty situations, with Protocol 2 providing the detailed procedural mechanisms.

V. Conditional Advance Pricing Agreements, Not Default Core Mechanism

KEY ARGUMENT: APAs must be conditioned on institutional prerequisites. Positioning them as unconditional core mechanism risks institutionalising informational asymmetry.

APAs have genuine merit where the tax administration has deep familiarity with the taxpayer's operations, has conducted sustained audits over multiple years, has access to reliable comparables, and can evaluate proposed transfer pricing methodologies on their merits. Where those conditions obtain, the APA adds formalised certainty atop an already functioning

relationship. Where they do not obtain, the APA risks becoming a mechanism through which informational asymmetry is institutionalised rather than addressed. A tax administration entering an APA without the informational base to evaluate the proposed methodology is not preventing a dispute; it is preventing scrutiny.

The prevention framework should be built from the ground up: information exchange and capacity-building first, cooperative examination mechanisms such as joint audits and simultaneous examinations second, and APAs third once institutional prerequisites are met. This sequencing reflects the reality that dispute prevention is an ecosystem of institutional capabilities. APAs are the capstone of that ecosystem, not its foundation. Digital business models present particular difficulties: how does a revenue authority evaluate an APA proposal for algorithmic advertising revenue or data monetisation when it has no comparables and no precedent? The Protocol should adopt a conditional approach, operationalised through technical annexes that elaborate preconditions, offer guidance on methodology evaluation, and address the specific challenges of digital economy transactions. Annexes can be updated by the Conference of States Parties more readily than core protocol text, allowing the prevention framework to evolve as capacity develops.

CORE MECHANISM: Joint audits and simultaneous examinations, supported by a multilateral transfer pricing database.

The core dispute prevention mechanism under Protocol 2 should be joint audits and simultaneous examinations. The case for this is structural, not merely practical. A joint audit places both revenue authorities in the same evidentiary position at the same time, examining the same taxpayer's transactions concurrently rather than sequentially. It eliminates the informational asymmetry that generates disputes in the first instance, because both jurisdictions are assessing the same facts rather than arriving at competing conclusions from incomplete, unilateral investigations conducted years apart. Simultaneous examinations serve a similar function where joint audits are not yet institutionally feasible: they do not require the same degree of operational integration, but they ensure that both administrations are examining the same tax period contemporaneously, creating the conditions for early identification of inconsistent positions before those positions harden into formal assessments.

Critically, the effectiveness of both mechanisms depends on an informational infrastructure that does not yet exist at the multilateral level. The Protocol should therefore establish the legal and institutional basis for a multilateral transfer pricing database, accessible to all States Parties, that compiles anonymised comparable data across jurisdictions. Much of the informational asymmetry that distorts both APA negotiations and unilateral transfer pricing assessments stems from developing country administrations' inability to access the comparable data they need to evaluate pricing methodologies independently. A publicly accessible, multilaterally governed database would begin to shift the structural conditions under which all prevention mechanisms operate. The Protocol need not operationalise the database immediately, but it must establish the mandate, governance framework, and phased development timeline under the Conference of States Parties.

VI. Defining Cross-Border Tax Disputes and Reforming MAP

The Protocol must include a functional definition.

Dispute settlement clauses are read restrictively under general international law. Jurisdiction is not presumed. Every ambiguity is resolved against inclusion. Without a definition, the Protocol's scope will be shaped not by what states agree here but by the states with the

resources and the incentive to advance narrow readings, shrinking quietly through accumulated practice. A functional definition should provide that a cross-border tax dispute exists when two or more states assert competing claims to tax the same income, transaction, or taxpayer, when actions by one state's tax administration create material tax consequences in another state, or when a dispute requires coordination between multiple national tax systems for resolution.

The proposal to use the UN Model Convention's MAP article as the starting point for the Protocol's MAP provision embeds a fundamental conceptual error: it imports a bilateral mechanism into a multilateral framework. The existing MAP's limitations are well documented: no obligation to reach agreement, opacity to the affected taxpayer, elastic timeframes, and a presumption of capacity parity between competent authorities that does not hold between well-resourced and developing country administrations. Starting from this article means starting from an instrument already carrying these deficiencies. The Protocol should instead establish strengthened MAP with binding timeframes, transparency obligations, and capacity support provisions, drawing lessons from the existing MAP's failures rather than codifying them.