International Journal of Law
ISSN: 2455-2194; Impact Factor: RJIF 5.12
Received: 29-04-2020; Accepted: 19-05-2020; Published: 29-05-2020
www.lawjournals.org
Volume 6; Issue 3; 2020; Page No. 146-151

The legal regime for arbitration in international tax disputes in the emerging global market: The Nigerian experience

Kwaghkehe Ierkwagh
Associate Professor, Tax Law Department of Commercial Law, Faculty of Law, Benue State University, Makurdi, Nigeria

Abstract
Arbitration as a mechanism for resolving international tax disputes as an alternative to litigation is gaining prominence globally. Most trading partners of Nigeria have now adopted the mandatory international tax arbitration in their double taxation agreements as required by OECD Action Plan 15. However, Nigeria as a signatory to the Multinational Convention to Implement Tax Treaty Related Measure to Prevent Base Erosion and Profit Shifting ("Multilateral Treaty" or "MLT") has refused to introduce mandatory binding arbitration to resolve international tax disputes. Through the doctrinal research method, the paper has found that the tax system plays a vital role in foreign investment destinations, and features of a good tax system include certainty and predictability in quick and timely resolution of tax disputes. Arbitrability of international tax disputes presents itself as the surest mechanism for resolution of tax disputes as against the regular courts. Consequently, the absence of mechanism for arbitration of international tax disputes in Nigeria has the potentials to increase uncertainties and result in a decline of foreign investment in Nigeria. The paper therefore recommends that Nigeria adopt the international regime for arbitration of international tax disputes in order to give the desired assurances and confidence to her trading partners and foreign investors that tax disputes will be resolved amicably, and speedily too.

Keywords: mechanism, prominence, arbitration, global

1. Introduction
Arbitration as a mechanism for amicable dispute resolution in commercial transaction without recourse to the regular judicial system is fast assuming relevance and prominence globally. With globalization of trade and investment, the entire world has become a global market place. This has been achieved through advancements in technology and facilitated by the global wave towards a perfect market driven economy.

The prominence of arbitration over the court system has been largely due to its perceived advantages like the fact that it is faster, ensures privacy of hearing, it's less expensive and enables technical matters to be referred to persons with technical expertise, particularly in view of the complexities of modern capitalism termed globalisation. Most importantly, Orojo and Ajomo [1] have argued that the uniqueness of arbitration in particular is the enhancement of relationships between conflicting parties. Arbitration is therefore a more preferred mechanism of Alternative Dispute Resolution (ADR).

Taxation in any economy is indispensable as a catalyst for attainment of economic and social goals. It is an armoury which can be used to stimulate investment, development and growth, and indeed a potent weapon for restructuring an ailing economy like Nigeria. Ayua [2] captured the scenario when he stated that there is hardly any government today that does not rely on tax for development. This is true even for an economy like Nigeria that is blessed with abundant petroleum resources. In fact, taxation is an important armoury in the hands of governments worldwide to reshape the economies of nations. Consequently, it has been stated *in Nicholas V. Arnes* [3] by the United States Supreme Court that taxation is the:

One great power upon which the whole national fabric is based. It is as necessary of a nation as it is the air he breathes to the natural man. It is not only the power to destroy, but it is also the power to keep alive.

Globalisation of trade has taken the issue of taxation beyond national boundaries to an international realm. Businesses can now be conducted internationally without physical contact and funds moved electronically. This has increased the volume of trade and opened up more avenues for conflicts between local or national tax authorities and international business concerns. Despite the potentialities of arbitration in commercial relationships, arguments suggest that both within and without Nigeria, tax matters are non-arbitrable.

This paper therefore examines fundamental issue of whether international tax disputes are arbitrable. The article begins with an introduction which basically lays a background to the understanding of the subject under discourse. The article then undertakes a conceptual framework for the appreciation of terms which form the building blocks for this discourse. The article proceeds to appraise the main theme of this discourse. In doing this, the discourse shall also be drawn from the Nigerian experience since the paperis situate within the Nigerian context. Finally, recommendations for the way forward are proffered sequel to findings.

2. Conceptual Framework
2.1 Arbitration
Arbitration has been judicially defined as where two or more persons agree that a dispute or potential dispute between them shall be resolved and decided in a legally binding way by one or more impartial persons in a judicial manner upon evidence put before him or them [4]. Similarly, Bernstein [5] has explained that when two or more persons agree that a dispute or potential dispute between them shall

be decided in a legally binding way, by one or more impartial persons in a judicial manner which is upon evidence before them, the agreement is called an arbitration agreement or submission to arbitration.

Arbitration has features which include the following:

a. Arbitrable Subject Matters

For parties to submit their dispute to arbitrators, the subject matter must be arbitrable for the arbitrators to have jurisdiction. In *Federal Inland Revenue Service V. Nigerian National Petroleum Corporation* [6], the issue was whether tax disputes are arbitrable. The trial court held that tax law being statutory, tax disputes are within the exclusive jurisdiction of the Federal High Court and therefore not arbitrable.

The Supreme Court has established non-arbitrable disputes in *Kano State Urban Development Board V. Fanz Construction Co* [7]. to include:

1. An indictment for an offence of a public nature;
2. Disputes arising out of an illegal contract;
3. Disputes arising under agreements void as being by way of gaming or wagering;
4. Disputes leading to a change of status, such as a divorce; and
5. Any agreement purporting to give an arbitrator the right to give judgment in rem.

In all, for a dispute to be referred to an arbitration panel, the subject matter must be arbitrable.

b. Consent as to Choice of Arbitrator

Consent as to choice of arbitrators is an essential feature of arbitration. Since parties are at liberty to choose their arbitrators, there must be mutual agreement or consent among the parties as to choice of arbitrators. Only then can each of the parties have confidence in the process and awards of the arbitration. In *Taylor Woodrow of Nigerian Ltd. V. Suddeutsche Week Gmba* [8], the Supreme Court of Nigeria held that "the general rule regarding arbitration is that parties to a transaction choose their arbitrator for better for worse to be the judge both as to decision of law and decision of fact in the dispute between them. Thus, none of them can, when the award is prima facie good on the face of it, object to his decision either upon law or the fact simply because the award is not in his favour".

c. Seat of Arbitration

The seat of arbitration in international tax disputes presents a unique problem. This is in view of the position of law the rules of procedure of arbitration are adopted from the seat of arbitration. The parties must therefore be free to choose the seat of arbitration since "strictly the legal concept is dependent on the will of the parties" [9].

The International Centre for Settlement of Investment Disputes (ICSID) considered to be a leading international arbitration institution devoted to resolving disputes between States and Nationals of other states through provision of facilities, rules and procedures for arbitration of international investment disputes resolution [10] with the headquarters in Washington DC (United States of America) has provided other venues in which parties may agree to hold arbitrations. These locations include the following:

a. World Bank Facilities in Paris;
b. Permanent Court of Arbitration at the Hague;
c. Regional Arbitration Centres of the Asian-African Legal Consultative Committee at Cairo, at Kuala Lumpur and Lagos;
d. Australian Commercial Dispute Centre at Sydney;
e. Arbitration Centre for International Commercial Arbitration in Melbourne;
f. Singapore International Arbitration Centre;
g. Gulf Cooperation Council Commercial Arbitration Centre at Bahrain;
h. German Institution of Arbitration; and
i. Maxwell Chambers, Singapore.

d. Substantive Law

One important consideration in international arbitration is the substantive law. That is, the law that guides the process or conduct of arbitration. In terms of arbitration of international tax disputes, the choice of substantive law is also important in view of the position of law that the local tax laws of a country are not enforceable in the forum [11]. This problem has however been solved by Lord McNair's argument that in investment contracts, where the parties do not specify any particular legal system, then their contract should be governed by the general principles of law recognised by civilised nations [12]. According to Lord McNair' [13], this principle is possible to implement because;

a. Many host countries have a system of law which has not yet developed to deal with a particular type of transaction; and
b. The parties do not specify the applicable law but agree to submit their dispute to arbitration.

2.2 Taxation

Taxation may be defined as a compulsory levy imposed by government on a person, his income, property or goods purchased pursuant to legislative authority for support of government, or social and economic development. Inherent in this definition are four principal elements. The first is that the levy must be compulsory and non-voluntary. The element of compulsion is true even in respect of certain taxes like sales tax and value-added tax if and when the subjects decides to purchase the taxable commodity. Secondly, it is an imposition by government. A third element is that a tax must have an objective. Also, for a tax to be valid, it must be imposed pursuant to legislative authority.

It is instructive to note that the power of imposition of taxes is essentially an exercise of sovereign power of the state. It is an important attribute of sovereignty. An important consideration here therefore is whether the submission of the sovereign power of the state to arbitration would amount to undermining same. Consequently, arguments have been advanced to the effect that fiscal measures should remain beyond the reach of private adjudicators [14].

2.3 International

The word, international has been defined severally. The Mariam Webster Dictionary has defined the word international as "Between or among nations, pertaining to the intercourse of nations, participated in by two or more nations, common to or affecting two or more nations [15]. The word, international has also been defined to "mostly mean something involving more than a single country; the term international as a word means involvement of interaction between or encompassing more than one nation" [16]. For the present purposes, international would therefore mean any transaction involving more than one country.

2.4 Dispute

The Black's Law Dictionary defines dispute as "a conflict or controversy, especially one that has given rise to a particular lawsuit". This definition is rather too anticipatory of the consequences of a dispute. A more realistic picture of the nature of a dispute was offered in the case of *Halki Shipping Corp. V. Sopex Oil Ltd* [17]. in the following words:

Dispute in respect of a matter which under an arbitration agreement had to be referred to arbitration was to be given its ordinary meaning and included any claim which the other party refused to admit or did not pay whether or not there was an answer to the claim in fact or in law [18].

A dispute may therefore be defined as a controversy as to the rights and claims between two or more persons. In international tax dispute would therefore imply a tax dispute that has transcended national boundaries. According to Hanotiau [19]:

The issues of arbitrability can arise at three stages in arbitration; first on an application to stay the arbitration, when the opposing party claims that the tribunal lacks the authority to determine a dispute because it is not arbitrable; second, in the course of the arbitral proceedings on hearing of an objection that the tribunal lacks substantive jurisdiction and third on an application to challenge the award or to oppose its agreement.

3. International Arbitration of Tax Disputes

According to Carbonneau and Sheidrick [20], the resolution of statutory claims involving tax issues is unsuitable for arbitration. In other words, tax disputes should remain beyond the reach of private arbitrators. However, in reality, tax disputes have been institutionalised.

There are basically three categories of fiscal disputes available for international arbitration as suggested by Park [21]. These are:

a. Tax controversies arising from business relationships;
b. Overlapping tax on the same transaction by two or more countries;
c. Disputes implicating tax issues between a foreign investor and the host state.

a. Tax Controversies arising from Business Relationships

With mergers and acquisitions which are part of the ongoing process of globalisation, the question of whether the buyer or the seller should bear taxes due for previously accrued tax liabilities may arise. This is a classically opportunity for tax disputes arbitration in international commercial transactions. Other cases available for international tax arbitrators include situations where the seller is alleged to have misrepresented corporate tax liabilities, which party gets the benefits and/or burdens of credits and liabilities under a "tax allocation agreement" concluded pursuant to a corporate spin-off [22]. Carbonneau and Sheidrick also argue that international tax disputes may arise between taxpayers and their advisers when advice about a tax shelter proves unfounded and leads to liability [23]. In *Reddan V. KPMG* [24], a tax shelter sponsor was held bound to arbitrate on the basis of an arbitration clause in brokerage contract related to tax the shelter transaction, while in *Vassahuzzo V. Ernst & Young and Sadley Austin* [25], an arbitration clause in engagement letter was found to exist and the adviser found liable on a malpractice action for advice on an unsuccessful tax shelter.

b. Income Tax Treaties

Controversy over Income Tax Treaties presents another fertile ground for international fiscal arbitration. Where the same income is subject to two tax jurisdictions, Double Taxation Agreements may be entered into between the two countries subjecting the income to tax in either of the jurisdictions and exempting same from tax in the other. Carbonneau and Sheidrick [26] have shown that double taxation agreements have been endorsed by international organisations such as the Organisation for Economic Cooperation and Development (OECD) and International Chamber of Commerce (ICC), as well as several national fiscal authorities, including Austria, Belgium, Canada, Germany and the United States of America [27]. The advantage of tax treaty arbitration is that it provides one hope for fiscal symmetry, thereby reducing the fiscal barriers to cross-border trade and investment [28]. In other words, one of the greatest barriers to international trade and foreign investment is that of double taxation since incomes derived therefrom are subject to tax in both the home and host countries. Bilateral Double Taxation Agreement treaties therefore, provide for the avoidance of double taxation and promote free trade and investments.

c. Investment Tax Disputes

Under investment tax dispute, the controversy that arises is whether the tax in question is legitimate. A tax on foreign investment may simply be seen as expropriation. It is therefore necessary to incorporate the arbitration clause in an investment agreement that permits arbitration of disputes over the quantum of a foreign investor's tax liability.

3.1 Developments in International Tax Arbitration

Therehas been major developments in tax arbitration which have impacted on the global practice of tax arbitration. Here, these developments in some regions have been examined below.

a. The European Union (EU) Convention

By 1990, the states of then European community concluded a convention providing for the use of arbitration in certain international tax disputes. This convention is called the [29] "EU Convention". This convention has provided guidelines for framing the appropriate terms for international arbitration in general [30]. On 10th October 2017, the European Council approved a directive for resolving double tax disputes within the European Union. This directive includes arbitration procedure for member states to resolve tax disputes [31]. The characteristics of the EU convention have been given as follows [32]:

1. It is multilateral agreement;
2. Arbitration is compulsory;
3. The result of the arbitration is not binding;
4. The applies to permanent establishments as well as compounds;
5. It applies to both judicial and economic double taxation;
6. The taxpayer has the right to initiate arbitration;
7. The convention establishes a timetable;
8. No rules of procedure are prescribed but are determined by competent authorities;
9. No judicial review is permitted;
10. Arbitration is not applicable in cases of "serious penalty";
11. Arbitration decisions must be implemented regardless

of any domestic time limits.

b. United States Treaty Practice

For many years, the United States resisted including arbitration clauses in double taxation conventions [33]. However, by 1993 the United States had firmly accepted arbitration clauses in taxation conventions [34].

In recent years, the United States has signed more Investment Treaties with tax arbitration clauses which exhibit the following features [35]:

1. Arbitration is not compulsory but occurs only with the consent of both competent authorities and taxpayers;
2. The arbitration is binding on all parties (including the taxpayer);
3. An exception is provided so that the competent authorities will not generally accede to arbitration concerning matters of tax policy or domestic law;
4. Taxpayers are provided with the right to present their views.

c. The Organisation for Economic Cooperation and Development (OECD)

A 1984 report concluded that for the time being was not contemplated. However, by 2015 the OECD issued fifteen Action Plans under the Base Erosion and Profit Shifting (BEPS) initiative to update obsolete international tax ruleswith the aim of curbing harmful tax practices [36]. Action Plan 14 recommended that countries update their existing Double Tax Treaties (DTTs) to include mandatory binding arbitration to complement the Mutual Agreement Procedure (MAP) while Action 15 requires countries to adopt a multilateral treaty incorporating all 15 Action Plans in one full swoop to update all their existing Double Taxation Treaties (DTTs) [37].

From the foregoing, it is evident that international tax arbitration dispute has been given much attention is double taxation treaty aspect. The concept of relief from double taxation can be traced as far back as the later part of the nineteenth century when the first treaties for the avoidance of double taxation were concluded among the various states of Germany and of the Austro-Hungarian Empire [38]. Double taxation treaties have since evolved into an essential feature of international trade and investment, and today, the total number of treaties worldwide is in excess of 1,500 [39]. In some cases, double taxation treaties require that tax be paid in the country of residence and exempt in the country in which it arises. In order cases, the country where the gain arises deducts tax at source (i.e. "withholding tax") and the taxpayer receives a compensating tax credit in the country of residence to reflect the fact that tax has already been paid. Most existing double taxation treaties follow the (OECD) Double Taxation Convention [40]. According to this treaty model, countries are allowed to tax the income from foreign investment of their multinational firms either according to the credit system or the exemption system. Under the credit system, countries may tax international investment income through which both domestic and foreign profits are subject to domestic taxation, but tax on foreign profits paid abroad are credited against domestic taxes on foreign profits. Under the exemption system, foreign profits are exempt from domestic taxation. As a result, capital income is effectively taxed according to the source principle.

The advantage inherent in double taxation treaty is that it encourages and stimulates foreign investment and trade between the treaty countries. Through the avoidance of double taxation regime, a friendly environment is created for investment and trade. One can therefore agree with the submission that:

Adopting mandatory binding arbitration to deal with double taxation disputes represents best practice in an era of increasing complexities in global trade and sophisticated business models such as digital economy [41].

4. The Nigerian Experience

A major development in the global economy in the 21st century, do suggest that Nigeria is a fertile ground for international tax arbitration. That is, the emergence and spread of economic globalisation which simply means the breaking down of national economic barriers through regulatory regimes, the international spread of trade, financial and other services, production activities, the growing spread and power of transnational corporations and international financial institutions across the entire globe. Globalisation has as its major components; commercialization, liberalisation, public companies of public companies. Under commercialisation, public companies so designated are expected to operate profitably on commercial basis and be able to raise funds from the capital market without government guarantee. Liberalisation on the other hand means opening up to competition based on laws, regulations, licensing rules and obligations already established under company law and investment initiatives. Privatisation means complete divestment or reduction in government ownership of means of production [42]. The whole essence is to create conducive environment to stimulate investment being local or foreign. In other words, creating a favourable or friendly tax regime is part of this globalisation agenda aimed at breaking down of all national boundaries for the free flow of labour and capital.

In Nigeria, the globalisation agenda was heralded by the setting up of a Technical Committee on the Privatisation and Commercialisation Decree [43] to regulate the privatisation agenda. Unfortunately, no attention has been given to tax dispute arbitration which Akinla says represents best practice in an era of increasing complexities in global trade and sophisticated business models such as digital economy [44].

On 17th August 2017, in line with Action Plan 15 of the OECD which requires countries to adopt a multinational treaty incorporating all 15 plans and update all existing Double Taxation Treaties, Nigeria became a signatory to the Multinational Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Treaty" or "MLT") [45]. However, when signing the MLT, Nigeria indicated that she will not adopt Action 14, that is, she will not introduce mandatory binding arbitration to resolve international tax disputes [46]. This position was arrived at because tax disputes are not arbitrable so Nigeria will not subject her taxes to arbitration [47].

In the last few years, Nigeria has entered into double taxation agreements with about nineteen (19) countries [48]. These countries have either adopted or indicate their intention to adopt the mandatory arbitration for tax disputes. Akinla has rightly argued that because Nigeria has not adopted arbitration, mismatch in the tax regime regarding dispute resolution between Nigeria and these trading partners can increase uncertainties and potentially result in a

decline in foreign investment into Nigeria [49]. This submission finds support in the fact that the tax regime plays a vital role in foreign investment destinations, and the features of a good tax system include certainly and predictability. Investors will be prepared to invest only where the tax system can assure them of a quick tax dispute resolution mechanism. For as the old saying goes; "time is of the essence" for businesses. Unfortunately, the regular court system in Nigeria does not guarantee this desire for quick dispute resolution. For instance, it took about twenty-five (25) years for the case of *Shell Petroleum Development Company of Nigeria Limited V. Federal Board of Inland Revenue* [50] to be disposed off from the High Court to the Supreme Court. This may make nonsense of the whole essence and benefits of litigation even for the victorious party since with the current inflationary rate, the amount involve may depreciate to an insignificant value. This tendency is definitely unsuitable for trade and investment to prosper.

Another form of international tax dispute relevant for the present purposes is the dispute implicating tax issues between a foreign investor and the host state. Since Nigeria is not disposed to submission of tax disputes to arbitration, there is no available record that disputes implicating tax issues between tax authorities and a foreign investor have been contemplated under any enactment or ever attempted. The dispute in *Reiss & Company (Nig) Ltd. V. Federal Board of Inland Revenue* [51] is a typical tax dispute suitable for international tax arbitration. In this case, Reiss & Co. (Nig) Ltd., a subsidiary of Reiss & Co. (Amsterdam), introduced Nigerian customers to the Amsterdam Company that in turn sold certain goods to the Nigerian buyers. The consideration was a buying commission varying from 10-14 percent that was said to be shared equally between the two companies. The dispute then aroused as to assessment of tax in respect of profits made by the principal on all business introduced to them by the subsidiary. The dispute was then resolved by the court and went to the Supreme Court, losing the benefits associated with arbitration.

5. Conclusion

Arbitrability of international tax disputes presents itself as a viable armoury for amicable resolution of international tax disputes in the emerging global market. This is in view of the perceived advantages of arbitration over the regular court system which include the fact that arbitration is faster, cheaper, ensures privacy and affords the parties the opportunity of the services of persons with technical expertise to resolve their dispute.

Globally, the International Centre for settlement of Investment Disputes (ICSID) has provided parties with convenient venues and facilities for commercial arbitration. Tax being commercial in nature parties to a tax dispute can effectively take advantage of these venues for the purpose of resolving their disputes.

Three categories of fiscal disputes have been identified and discussed at the international level where the legal frameworks for international tax arbitration have been put in place. However, it has been shown that Nigeria has refused to introduce arbitration to resolve tax disputes, the reason being that tax matters are not arbitrable, so, Nigeria will not subject its taxes to arbitration. This stand is even against the fact that most of her trading partners have either already adopted mandatory arbitration over their tax disputes or indicated the intention to adopt same.

This stand by Nigeria not to subject her taxes to arbitration is bound to create uncertainty and lack of confidence in the minds of her trading partners. The undesirable effect is the consequential decline in trade and investment to the detriment of Nigeria. Foreign investment and trade are both crucial to the economic recovery, development and growth of an ailing economy like Nigeria.

It is therefore, in the interest of the government of Nigeria to cue into the global legal framework for arbitration of tax disputes in order to give the desired assurance and confidence to her trading partners and foreign investors that tax disputes between them will be amicable resolved, and speedily too. Amicable resolution of tax disputes is also capable of maintaining a harmonious relationship between Nigeria and her trading partners, and foreign investors.

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