REGULATION OF INCOME AND PROFIT SHIFTING TO TAX HAVEN COUNTRIES: A SUGGESTED APPROACH FOR NIGERIA*

Abstract
One of the major strategies usually employed by companies to avoid taxation in Nigeria is to shift their income or profit to their subsidiaries located in low or no tax countries usually referred to as 'tax haven countries' where it will be subjected to low or no tax. This is a result of globalization of international trade and economy which made it possible for companies to extend their business activities to countries other than where they are headquartered. Companies, therefore, usually set-up shell corporations in tax haven countries to shift income and profit to avoid taxation in high tax countries. The rate at which companies shift income and profit out developing countries to tax haven countries is regarded as one of the major problems undermining development of developing countries. Yet, there are no clear rules in Nigeria to prevent income and profit shifting which had resulted in substantial revenue loss. The objective of this article is to examine the international regulations developed to prevent income and profit shifting to tax haven countries. This is to assist policy makers in the country to put in place necessary legal framework to tackle tax avoidance through income and profit shifting.

Keywords: *Income, Profit Shifting, Tax Haven Countries, Regulation, Nigeria*

1. Introduction

The integration of international trade and economy from technological advancements in transportation and communication resulted in globalization of the world economy. Globalization, in turn, freed the erstwhile geographical and territorial limitations and boundaries in international trade and business activities. This allowed companies to extend their business activities and operations by establishing subsidiaries in countries other than where they are headquartered.[1] The geographical boundary between a company located in one country and its subsidiary located in another country makes it possible for cross border international transfer of goods and services to occur in transactions between the company and its subsidiary. The basic economic objectives of every company are to reduce tax payment, increase profit and the wealth of their shareholders.[2] This is a legal obligation which every company owe their shareholders.[3] Therefore, as rational economic actors, companies exploit various ways to achieve these economic objectives to promote their success as well as the interest of their shareholders. The major strategy usually employ by companies to achieve their economic objectives is to avoid tax payment by shifting their income or profit from high tax jurisdictions/countries to low or no tax jurisdictions/countries.[4] This is mostly achieved by over-invoicing/pricing of transaction for the purpose of shifting their income or profit out of high tax jurisdictions/countries to their subsidiaries located in a lower or no tax jurisdiction/country.[5] These low or no tax jurisdictions/countries known as tax haven countries[6] normally use their sovereign legislative powers to preserve secrecy of financial transactions of companies, provide light regulation and levy low or no tax on the income or profit of companies.[7] This often attracts companies seeking to set-up shell corporations for the purpose of shifting income from high tax

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[1] A. A. Lazarus, 'Multinational Corporations' in N J Smelser and P. B. Baltes (eds.) *International Encyclopedia of Social and Behavioural Science*s (New York: Elsevier 2001) 1099

[2] P. Sikka & H. Willmott, 'The Dark Side of Transfer Pricing: Its Role in Tax Avoidance and Wealth Retentiveness' (2010) Essex Business School, University of Essex 7

[3] See Section 279(3) of the Companies and Allied Matters Act CAP. C20 LFN 2004 (CAMA) which requires directors of companies to promote the success of the company and in that process, have regard for the interests of their shareholders.

[4] H. D. Ki & T. Lau, 'An Exploratory Study of Transfer Pricing Practices by Multinationals with International Affiliates' (2005) 31(4) International Tax Journal 6

[5] L. W. Maseki, Effects of Transfer Pricing on Revenue Generation by Multinational Enterprises in Kenya (M.Sc. Research Project, University of Nairobi 2015) 4, 5

[6] R. Baker, *Capitalism's Achilles Heel: Dirty Money and How to Renew the Free- Market System*, (John Wiley & Sons Inc. Hoboken, United States 2005) 53

[7] P. Sikka, 'The Role of Offshore Financial Centres in Globalization' (2003) 27(4) Accounting Forum' 365-399

jurisdiction to tax haven countries where they know that their income and profit will not be subjected to taxation.[8] It is therefore not surprising that estimate had shown that in each year, companies around the world establish more than 200,000 new subsidiaries in tax haven countries with a cumulative total of more than three million subsidiaries.[9] The implication of this is that companies nowadays avoid paying tax in countries where they earn income or profit by shifting such income and profit to tax haven countries to relieve their tax burden. It is now generally believed that capital flight arising income and profits shifting activities of companies has devastating effects on the economy of developing countries.[10] The OECD in its 2014 Report noted that illicit financial flow arising from income and profit shifting activities strip resources from developing countries that could be used to finance much-needed public and social services such as health and education and that it also weaken the financial systems and the economic potential of developing countries.[11]

In the light of the foregoing, the paper examines the fundamental features of tax haven countries and the magnitude of revenue loss arising from income and profit shifting to tax haven countries. The paper also considers the negative effects of income and profit shifting on the economy of developing countries and its international regulation. The paper makes series of recommendations to strengthen and prevent companies from shifting their income and profit out of Nigeria to tax haven countries**.**

2. What is Tax Haven?

There is no universal or standard definition of the term 'tax haven'.[12] This is a consensus among scholars. For example, the Gordon Report noted thus: 'there is no single, clear, objective test which permits the identification of a country as a tax haven'.[13] In addition, Jason Sharman held the view that the term 'tax haven' lacks a clear definition and its application is often controversial and contested.[14] Nonetheless, tax haven also known as offshore financial centre or secrecy jurisdiction is a term used to refer to countries/jurisdictions/territories that offer favourable or no tax rates on income and profits of companies, provide lax regulatory policies,[15] banking and business secrecy to foreign investors.[16] Corporate and personal tax rates can be zero, nominal or very low; while secrecy involves a lack of transparency in the implementation of a legal framework, along with lack of effective exchange of tax information with foreign tax authorities.[17]

The OECD identifies tax havens as any country/jurisdiction/territory that apply no or nominal taxes to non-residents (individuals and corporations) and whose laws or administrative practices prevent the effective exchange of relevant information with other governments on taxpayers benefiting from the low or no tax jurisdiction, lack of transparency and the absence of a requirement for substantive activity in the tax haven jurisdiction.[18] Likewise, the International Monetary Fund (IMF) identified three recurring characteristics of tax haven countries to wit: (i) the primary orientation of business toward non-residents; (ii) the favorable regulatory environment (low supervisory requirements

[8] United Nations Economic and Social Council (UNESCO), *Enhancing Social Protection and Reducing Vulnerability in a Globalized World*, (United Nations Library, Geneva 2001) 10 and Brittain-Catlin W., *Offshore: The Dark Side of the Global Economy* (Farrar, Straus & Giroux, New York, 2005) 19

[9] Ibid

[10] Organisation for Economic Co-operation and Development (OECD), Measuring OECD Responses to Illicit Financial Flows from Developing Countries (2013, Paris: OECD Publishing) 15

[11] Ibid

[12] R. Palan, R. Murphy & Chavagneux, *Tax Havens: How Globalization Really Works* (Cornell University Press New York 2010) 12

[13] Gordon Report, 'Tax Havens and Their Use by United States Taxpayers—An Overview' (1981) United States Treasury Report 13

[14] J. C. Sharman, 'Havens in a storm: the struggle for global tax regulation' (Cornell University Press New York 2006) 6

[15] J. R.Hines, 'Treasure Islands' (2010) 24(4) The Journal of Economic Perspectives 103-126

[16] N. Shaxson, 'Treasure Islands' (Palgrave Macmillan, New York 2011) 11

[17] European Commission, 'Where does the money come from?' <http://www.ec.europa.eu/budget/explained/budg_system/financing/fin_en.cfm> accessed on 15 July 2018

[18] OECD, "Harmful Tax Competition - An Emerging Global Issue", (1998) <http://www.oecd.org/daaoecd/33/1/1904184.pdf> accessed on 15 July 2018

and minimal information disclosure) and; (iii) the low-or zero-taxation schemes.[19] The European Parliament's resolution of 19 April 2012 describes tax havens as 'foreign non-cooperative jurisdictions characterized in particular by no or nominal taxes, a lack of effective exchange of information with foreign tax authorities and a lack of transparency in legislative, legal or administrative provisions, or identified as such by the Organisation for Economic Cooperation and Development or the Financial Action Task Force.'[20]

The Tax Justice Network (TJN) regard tax haven as countries that create legislations designed to assist persons whether real or legal to avoid regulatory obligations imposed upon them in the place where they undertake the substance of their economic transactions.[21] According to the TJN, Offshore Financial Centres (OFCs) are not the same as tax havens but are commercial communities hosted by tax havens countries that exploit legislation in tax haven countries for the benefit of those resident elsewhere. In other words, the offshore financial centre is made up of accountants, lawyers, bankers and their associated trust companies that sell services to those who wish to exploit the mechanisms the tax haven has created.[22] In fact, the TJN now regard both tax haven countries or OFCs as 'secrecy jurisdiction' which it defined as a place that intentionally creates regulation for the primary benefit and use of those not resident in their geographical domain that is designed to undermine the legislation or regulation of another jurisdiction and that, in addition, creates a deliberate, legally backed veil of secrecy that ensures that those from outside the jurisdiction making use of its regulation cannot be identified to be doing so.[23] This definition, according to the TJN, is a broad enough to accommodate the definitions of 'tax havens' and 'offshore financial centres' because it covers many more issues than tax by emphasizing the international nature of the problem, and highlights the fact that secrecy is the most important corrosive issue that must be addressed if the abuse that those places traditionally called tax havens promote is to be prevented in the future.[24]

From the above, it can be safely posited that a country will be regarded as a tax haven if it charges low or no taxes on the income and profit of companies in its jurisdiction. Likewise, a country that provide light or lax regulation for companies, refuse to exchange information on a taxpayer's affairs with other jurisdictions or that guarantee strong secrecy (such as banking secrecy and non-disclosure of corporate legal and financial data) will be regarded as tax haven.[25] It is important to note that there is no official list of tax haven countries. However, international institutions and organizations such as OECD and International Monetary Fund (IMF) have over the years developed their respective lists of tax haven countries. According to Fortune magazine, the twelve most popular tax havens in the world are Bermuda, Netherlands, Luxemburg, Caymans Islands, Singapore, Channel Islands, Isle of Man, Ireland, Mauritius, Monaco, Switzerland and Bahamas.[26]

3. Revenue Loss arising from Income and Profit Shifting to Tax Haven Countries

The use of tax haven subsidiaries for the purposes of shifting income and profit from high tax jurisdiction to tax haven countries is regarded as an aggressive and an abusive a form of corporate tax avoidance/evasion known as 'abuse of transfer pricing'.[27] Abuse of transfer pricing simply means the intentional over-invoicing/pricing or under-invoicing/pricing of the prices of goods and services in transaction between a company and its subsidiary for the purpose of reducing tax.[28] Income and profit shifting to tax haven countries from high tax jurisdictions is now

[19] A. Zoromé, 'Concept of Offshore Financial Centers: In Search of an Operational Definition' IMF Working Paper, April 2007 p. 4 and 7.

[20] European Parliament, 'Concrete ways to combat tax fraud and tax evasion' (2012) <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2012-0137&language=EN&ring=B7-2012-0203> accessed on 18 July 2018

[21] R. Murphy, 'Creating Turmoil, Tax Justice Network submission to the Treasury Select Committee' (2008)

[22] Ibid

[23] R. Murphy, 'Finding the Secrecy World: Rethinking the language of offshore', Tax Research LLP, 2008

[24] R. Murphy, 'Tax havens report'

[25] M. Henn, 'Tax Havens and the Taxation of Transnational Corporations' <http://www.fes-globalization.org> accessed on 18 July 2018

[26] A Depiretro 'The 12 Most Lucrative Tax Havens in the World' Fortune Magazine (United States of America 22 February 2017) <http://www.fortune.com/2017/02/22/world-best-tax-havens-countries-corporate-business/> accessed on 27 October 2017

[27] J. R. Graham & L. T. Alan, 'Tax shelters and corporate debt policy' (2006) Journal of Financial Economics 81

[28] L. Eden, 'Taxes, Transfer Pricing, and the Multinational Enterprise' in Rugman A. M., The Oxford Handbook of International Business (2nd Ed.) (Oxford: Oxford University Press, 2009) 593, Kobetsky M., *International Taxation of Permanent Establishments: Principles and Policy* (Cambridge University Press, Cambridge 2011) 71

considered as a significant threat to global revenue generation.[29] This position is corroborated by the amount of global revenue loss arising from income and profit shifting which is quite staggering for both the developed and the developing countries.[30] It is estimated that more than US$11.5 trillion in assets, income and profits resides in tax haven countries.[31] Data released by the IMF in its 2014 World Economic Outlook Database estimated that a total of US$10.35 trillion has been invested in tax havens countries by companies through the shifting of income and profit from higher tax jurisdictions to tax haven countries.[32]

Revenue loss to income and profit shifting is not peculiar to a region of the world. Rather, it is a menace negatively impacting on global revenue generation including developed countries that one would have expected to be equipped with the requisite capacity to deal with the menace. In the US for example, Apple Inc. was reported to have shifted its profits and income to Ireland (which is a low tax jurisdiction compared to the US) leading to an estimated revenue loss amounting to more than US$2.4 billion in 2014.[33] In another instance, Starbucks was reported to have paid a paltry sum of UK£8.6 million in taxes to the Her Majesty Revenue and Custom (HMRC) since it started business in the United Kingdom (UK) in 1998 despite making more than UK£3 billion in profit in the country.[34] Likewise, in 2012, it was reported that Microsoft avoided paying more than UK£1.7 billion in corporate taxes in the UK by shifting its profit and income to Luxembourg which is a low tax jurisdiction in Europe.[35] Google's income and profit shifting activities from its subsidiary located in the Netherlands to its subsidiary in Bermuda was reported to have resulted in a tax revenue loss of around 10.7 billion euros to European countries.[36]

However, the negative impact of income and profit shifting on revenue generation is more pronounced in developing countries that usually lack the ability to check the aggressive practices of companies in their jurisdictions.[37] Although, little is known about the magnitude of revenue loss in these countries which is due to lack of data to measure or quantify such revenue loss.[38] Nonetheless, some international organizations and non-governmental organizations (NGOs) have tried to quantify the amount of tax revenues lost by developing countries in this regard. For example, OXFAM estimated that US$50 billion in tax revenue is lost yearly to income shifting activities of Multinational Corporations (MNCs).[39] Another research by OXFAM revealed that developing countries lost more than US$80 billion in tax revenue to income shifting activity of the MNCs to tax havens in 2009.[40] This figure increased in 2016 when further research by OXFAM in the regard estimated that developing countries lost more than US$172 billion

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[29]Ernst and Young, 'Global Transfer Pricing Surveys' (2006) <http://www.ey.com/Global/download.nsf/International/Tax__Global_Transfer_Pricing_Survey_Part_3/$file/EY_GlobalTPSurvey3_Sep2006.pdf> accessed on 13 March 2014

[30]Ernst and Young, 'Global Transfer Pricing Surveys' (2006) <http://www.ey.com/Global/download.nsf/International/Tax__Global_Transfer_Pricing_Survey_Part_3/$file/EY_GlobalTPSurvey3_Sep2006.pdf> accessed on 13 March 2014.

[31] R. Baker, *Capitalism's Achilles Heel: Dirty Money and How to Renew the Free- Market System*, (John Wiley & Sons Inc. Hoboken, United States 2005) 53

[32] International Monetary Fund (IMF), 'World Economic Outlook Database October 2014: Legacies, Clouds, Uncertainties' (2014) <https://www.imf.org/external/pubs/ft/weo/2014/02/pdf/text.pdf> accessed on accessed on 20 October 2017

[33] R. Kitty & J. Craig, 'Offshore Corporate Profits: The Only Thing 'Trapped' Is Tax Revenue' (2014) <https://www.americanprogress.org/issues/tax-reform/report/2014/01/09/81681/offshore-corporate-profits-the-only-thing-trapped-is-tax-revenue> accessed on 15 February 2017

[34]N. Huber, 'Starbucks tax bill stirs transfer pricing spat' (2012) https://www.accountingweb.co.uk/business/finance-strategy/starbucks-tax-bill-stirs-transfer-pricing-spat accessed on 15 February 2017

[35]J. Chew '7 Corporate Giants Accused of Evading Billions in Taxes' (2016) <http://www.fortune.com/2016/03/11/apple-google-taxes-eu/> accessed on 17 January 2017

[36] Ibid ,

[37] S. C. Borkowski,, 'The transfer pricing concerns of developed and developing countries' (1997) 32(3) International Journal of Accounting 321-336

[38] C. Fuest & N. Riedel, 'Tax evasion, Tax Avoidance and Tax Expenditures in Developing Countries: A review of the literature' Report prepared for the UK Department for International Development (DFID) 2009 Oxford University Centre for Business Taxation <http://r4d.dfid.gov.uk/PDF/Outputs/EcoDev/60670_TaxEvasionReportDFIDFINAL1906.pdf> accessed 24 July 2014. See also L. Eden, 'Transfer Price Manipulation' in P. Reuter, 'Draining Development? Controlling Flows of Illicit Funds from Developing Countries' (2012) 223 <http://ww.worldbank.org> accessed on 20 October 2016

[39]OXFAM, 'Tax Havens: Releasing the Hidden Billions for Poverty Eradication' (2000) <http://www.taxjustice.net/cms/upload/pdf/oxfam_paper_-_final_version __06 _00.pdf> 11 accessed on 20 October 2016

[40]OXFAM, 'The Hidden Billions: How Tax Havens impact lives at Home and Abroad' (2016) Oxfam Research Reports <http://www.oxfam.org.au> accessed on accessed on 20 October 2017

in tax revenue.[41] OXFAM predicted that the tax revenue loss in this regard will continue to increase in developing countries in the coming years.

In Nigeria, just like other developing countries, there is minimal evidence about the magnitude of tax revenue lost to income and profit shifting due to the limitation of data.[42] However, estimates in international studies will provide an idea of the magnitude of revenue that has been lost to income and profit shifting activities of companies. Findings from a research conducted by Global Financial Integrity (GFI)[43] indicated that Nigeria's revenue loss to income and profit shifting amounted to about US$1.020 billion between 2002 and 2006.[44] In addition, another research conducted by Christian Aid specifically on companies operating in the oil and gas industry of the country estimated that the country lost more than UK£502 million between 2005 and 2007.[45] The research further indicated that this loss (that is UK£502 million) was one of the highest tax losses suffered by any developing country within the years under review.[46] According to OXFAM, more than US$327.30 million in income and profit was shifted out of the country by MNCs operating in the country in 2014 resulting in a tax loss of about US$98.19.[47]

There have been reported cases of income and profit shifting by MNCs operating in the upstream oil and gas industry of the country. For example, Shell International Petroleum Limited, Halliburton and Chevron were accused by the Federal Inland Revenue Service (FIRS) to have avoided estimated sum of US$17,857,142.86 million, US$14,285,714.20 million and US$710,506,000 in taxes for the years 2003, 2002 and 1999 respectively through over-invoicing of transfer of goods and services to shift income out of the country to low/no tax jurisdictions. In addition, an investigative report by Premium Times (an online Newspaper in Nigeria) on 26th October 2015 alleged that MTN Nigeria shifted the sum of =N= 11.398 billion out of Nigeria to its offshore subsidiaries in tax havens in Dubai and Mauritius through an abusive transfer pricing scheme in 2013. The report further alleged that MTN admitted making unauthorised payments of =N=37.6 Billion to MTN Dubai between 2010 and 2013 which was then transferred to Mauritius.[48] Similarly, on 22nd September 2016, it was alleged on the floor of the Nigerian Senate by a Senator representing Kogi West, Mr. Dino Melaye that MTN laundered billions of US dollars over several years through abusive transfer pricing scheme failing to pay necessary tax in the country. Mr. Melaye, while making the allegation, revealed that between 2006 and 2016, MTN Nigeria in collaboration with four Nigerian commercial banks with the help of a serving minister moved over US$12 billion out of the country through abusive transfer pricing.[49]

Due to the amount of revenue that had been lost to it, income and profits shifting to tax havens is now globally recognized as a major form of abusive and aggressive tax avoidance practice hurting and draining the revenue of most countries [50] It is predicted that tax revenue loss to income and profit shifting to tax haven countries will continue to rise each year.[51] The reason for this is not far-fetched bearing in mind that lax regulation and the secrecy guarantee by tax haven countries normally attracts companies to set up shell subsidiaries with little or no operational activities for the purpose of shifting income and profit away from high tax jurisdiction to reduce their tax bills. It therefore

[41] Ibid

[42] K. Zannah 'An Empirical Investigation of Transfer Pricing Regulations for Nigeria with a Particular Emphasis on the Petroleum Sector' (PhD Thesis, Aberdeen Business School, The Robert Gordon University) 39

[43] Global Financial Integrity (GFI) is a non-profit research, advisory and advocacy organization located in Washington, D.C. GFI produces research on the scale, impact and attributes of illicit financial flows- the proceeds of crime, corruption, and tax evasion with a focus on developing and emerging economies <http://www.gfinyegrity.org> accessed on 15 December 2016

[44] A. Hollingshead, 'The implied tax revenue loss from trade mispricing' (2010) <http://www.gfintegrity.org/report/the-implied-tax-revenue-loss-from-from-trade-mispricing/> accessed on 21 November 2016

[45] Christian Aid, 'False Profits: Robbing the Poor to Keep the Rich Tax-Free' (2009) <https://www.christianaid.org.uk/Images/false-profits.pdf> accessed on 13 March 2014

[46] Ibid

[47] OXFAM, 'The Hidden Billions: How Tax Havens impact lives at Home and Abroad' (2016) Oxfam Research Reports <http://www.oxfam.org.au> accessed on accessed on 20 October 2017

[48] E. Mayah 'Investigation: How MTN ships billions abroad paying less tax in Nigeria' Premium Times Newspaper (Nigeria 26 October 2015) <https://www.premiumtimesng.com/investigationspecial-report/192159-investigation-how-mtn-ships-billions-abroad-paying-less-tax-in-nigeria.html/> accessed on 26 October 2016

[49] C. Eboh 'Nigerian Senate hears how MTN allegedly laundered $12 billion' <https://www.premiumtimesng.com/news/headlines/211026-nigerian-senate-hears-mtn-allegedly-laundered-12-billion.html> accessed on 26 October 2016

[50] M. Kobetsky, *International Taxation of Permanent Establishments: Principles and Policy* (Cambridge University Press, Cambridge 2011) 71

[51] R. S. Avi-Yonah, 'The Rise and Fall of Arm's Length: A Study in the Evolution of U.S. International Taxation' (1995) 15 V Virginia Tax Review 89-90

becomes necessary for a country have in place regulation to prevent or regulate income and profit shifting to tax haven countries.

4. International Regulation of Income and Profit Shifting to Tax Haven Countries
As noted earlier, income and profit shifting to tax haven countries is regarded as a form of abuse of transfer pricing which is regarded as an aggressive and abusive form of tax avoidance. Both the OECD and the United Nations (UN) recommended the Arm's Length Principle (ALP) as the means to prevent abusive transfer pricing practices including over-invoicing or pricing of transactions for the purpose of income and profit shifting. Article 9(1) of OECD Model Tax Convention provides the general standard for the application of the ALP. In this respect, the application of the ALP is predicated on treating a company and its subsidiaries as separate and distinct entities. This is to ensure that in a transaction between a company and its subsidiary, price of such transaction must reflect the price that would have been charged were the transaction between independent entities. In other words, the price charged by independent entities in a similar transaction is the measure to benchmark or verify the price to be charged in a transaction between a company and its subsidiary and it is what determines whether or not a company has over invoiced the transaction for the purpose of shifting income and profit to its tax haven subsidiary.[52] This benchmarking process is what is as 'comparability analysis' and it is regarded as the heart of the application of the ALP.[53] It is important to note that the ALP is not an anti-tax avoidance provision; rather, the provision is meant to achieve the double purposes of ensuring an equitable inter-nation allocation of taxing rights on income and profit of companies in different tax jurisdiction and to prevent the incidence of economic double taxation.[54]

The application of the ALP is however not without its own challenges for which it has been severely criticized. A major challenge in this regard is the emergence of globalised economy which rendered geographical boundaries irrelevant for business decision making as companies were now able to conduct their business activities in different geographical jurisdictions without necessarily creating a permanent establishment in those jurisdictions.[55] With the challenges presented by globalisation, it is argued that the current ALP system is no longer suited for the global nature of international business.[56] This is because its application of treating a company and its subsidiary as separate entities has been significantly weakened.[57]
Another challenge in this regard is the difficulty on the part of both the tax authorities and the taxpayers in obtaining sufficient information on prices of transactions between independent entities to conduct this comparability analysis.[58] This is perhaps the most widely acknowledged major problem and challenge confronting the application of the ALP. In fact, by both developed and developing countries have all expressed serious concerns about the availability of data on transactions between independent parties that can be used to conduct comparability analysis.[59]

[52]United Nations, 'Practical Manual on Transfer Pricing for Developing Countries' <http://www.un.org/esa/ffd/documents/UN_Mannual_TranferPricing.pdf> accessed on 15 December 2015

[53]OECD, 'OECD/G20 Base Erosion and Profit Shifting Project: Aligning Transfer Pricing Outcomes with Value Creation' <http://dx.doi.org/10.1787/9789264241244-en> accessed on 15 August 2017

[54] OECD, Committee on Fiscal Affairs, Report of the OECD Committee on Fiscal Affairs on Transfer Pricing and Multinational Enterprises, (Paris: OECD, 1979) para. 3.

[55] R.S. Avi-Yonah, K. A. Clausing & M. C. Durst, 'Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split' (2009) 9 *Florida Tax Review* 497-500

[56] R. S. Avi-Yonah K. A. Clausing, 'Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment' <https://www.brookings.edu/research/reforming-corporate-taxation-in-a-global-economy-a-proposal-to adopt-formulary-apportionment/> accessed on 15August 2017

[57]M. Kobetsky, *International Taxation of Permanent Establishments: Principles and Policy* (Cambridge University Press, Cambridge 2011) 76

[58] OECD, 'Transfer Pricing Comparability Data and Developing Countries' <http://www.oecd.org/.../transfer-pricing-comparability-data-and-developing-countries.html> accessed on 20 December 2016

[59] Ibid

These challenges have provoked a lively debate of whether the ALP should be replaced or not.[60] It is in this respect that reputed scholars and professionals such as Avi-Yonah,[61] Clausing[62] and Durst[63] proposed a move away from the current ALP system to another system that will reflect the present international business and economic realities rather than the illusion created under the ALP system which has resulted in a continuous loss of tax revenue.[64] They, therefore, advocated for a global adoption of Formulary Apportionment (FA) also known as Unitary Taxation as an alternative to the ALP.[65] The application of the FA is predicated on treating a MNC and its permanent establishments (subsidiaries, branches and affiliates) as a single entity or as a unitary business whereby the income, expenses, profits and losses of the corporate group are allocated on a pre-determined term across the various taxing jurisdictions where the MNC groups have permanent establishments.[66] In this situation, unlike under the ALP system, a MNC and its permanent establishments are treated as a single global taxpayer and its profit is calculated by subtracting its worldwide expenses from a global income without regard to legal distinctions between the MNC and its permanent establishments.[67] The resulting profit is thereafter allocated and apportioned among various taxing jurisdictions where it does business based on a formula that takes into account the economic realities, activities and contributions of each of the permanent establishments to the global income and profit of the MNC group.[68] Each taxing jurisdiction will then apply its tax rate to the profit apportioned to its jurisdiction.[69] The major advantage of the FA over the ALP is that it does away with the illusory assumption created under the ALP system that a MNC and its permanent establishments are separate and distinct entities. The implication of this is that the need to conduct a comparability analysis which can be a very difficult task is not applicable under the FA system.[70] The application of the FA therefore ensures economic substance and realities of the integrated nature of the MNCs in the new globalised economy is reflected in its transactions because by treating a MNC group as a single worldwide taxpayer, the global income and profit of the MNC is distributed among members of the group to reflect their contributions to the global income.[71] The OECD has however criticised the idea of replacing the ALP system with the FA. It rejected the notion and it continued to view the ALP as the only appropriate means to prevent income and profit shifting to tax haven countries. Instead, the OECD recommended that the ALP should rather be reformed to overcome its challenges instead of being thrown away.[72] The reforms recommended by the OECD formed part of the 15-Action Plan developed by the OECD

[60]Avi-Yonah, Clausing & Durst, 'Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split' (2009) 9 *Florida Tax Review* 497-500; H. Grubert & R. Altshuler, 'Fixing the System: An Analysis of Alternative Proposals for the Reform of International Tax' (2013) 66 National Tax Journal 671, H. Hamaekers, 'Arm's Length-How Long?' in Kirchhoof (Ed.) *International and Comparative Taxation* (2002) 51

[61] Reuven S. Avi-Yonah is an Irwin I. Cohn Professor of Law and specializes in corporate and international taxation. See <https://www.law.umich.edu/FacultyBio/Pages/FacultyBio.aspx?FacID=aviyonah> accessed on 15 August 2017

[62] Kimberly Clausing is the Thormund A. Miller and Walter Mintz Professor of Economics at Reed College. See http://www.reed.edu/economics/clausing/ accessed on 15 August 2017

[63]M. C. Durst is a former Director of the IRS Advance Pricing Agreement Program. See http://www.ictd.ac/about-us/ictd-team> accessed on 15 August 2017

[64]Avi-Yonah & Clausing, 'Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment' (2007) <https://www.brookings.edu/research/reforming-corporate-taxation-in-a-global-economy-a-proposal-to adopt-formulary-apportionment/> accessed on 15August 2017

[65]Avi-Yonah, Clausing, & Durst, 'Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split' (2009) 9 Florida Tax Review 497-500

[66] Ibid

[67]Avi-Yonah & Clausing, 'Reforming Corporate Taxation in a Global Economy: A Proposal to Adopt Formulary Apportionment' (2007) <https://www.brookings.edu/research/reforming-corporate-taxation-in-a-global-economy-a-proposal-to adopt-formulary-apportionment/> accessed on 15August 2017

[68]J. M. Weiner, 'Formulary Apportionment and Group Taxation in the European Union: Insights from the United States and Canada' <http://europa.eu.int/comm/taxation_customs/taxation/taxation.htm> accessed on 25 July 2017

[69] Ibid

[70] L. Sheppard, 'Transfer pricing is the leading edge of what is wrong with International Tax' (2012). <http://www.taxjustice.net/cms/front_content.php?idcat=139> accessed on 15 August 2017

[71] T. J. H. Dennis, 'Unitary Formulary Apportionment as a Solution to the Conundrum of Source' (2010) <http://www.jmls.edu/academics/.../Faherty_1.pdf> 7 accessed on 17 July 2017

[72] OECD, 'Action Plan on Base Erosion and Profit Shifting' <http://dx.doi.org/10.1787/9789264202719-en> 14 accessed on 15 July 2017

and the G20[73] to address the issue of Profit Shifting under a general package known as Base Erosion and Profit Shifting (BEPS) Project.[74] The BEPS project is briefly examined below.

The OECD/G20 15-Action Plan against Base Erosion and Profit Shifting (BEPS)

Base Erosion and Profit Shifting (BEPS) is a term generally use to refer to various tax avoidance schemes/strategies usually employed by taxpayers to artificially shift profits from high tax jurisdiction to low or no-tax locations.[75] BEPS schemes enable taxpayers to move profits to where they are taxed at lower rates and expenses from where they are taxed at higher rates. The result of this is the reduction of revenue accruable to the government.[76] Addressing the issue of BEPS was therefore a key priority of governments around the globe. It was in this respect that in 2012, the OECD countries and the G20 countries,[77] working together embarked on the most significant and ambitious objective of re-writing of the international tax rules in a century.[78] This ambition was to revise the ALP rule and align it to developments in the world economy to ensure that profits are taxed where economic activities are carried out and where value is created.[79] Beyond securing revenues, the OECD/G20 BEPS Project also aim to create a single set of consensus-based international tax rules to address BEPS and to protect tax bases while offering increased certainty and predictability to taxpayers.[80] While the OECD and G20 countries recognised the need to address the issue of BEPS internationally, they did not want to unravel the existing consensus-based international framework such as the ALP which has been internationally accepted as the standard for regulating transfer pricing. Their fear is that unraveling the ALP might lead to decreased international cooperation and uncoordinated unilateral actions in the tax sphere which would multiply uncertainty and unpredictability.[81] On 12th February 2013, the OECD issued a lengthy report to address BEPS known as the BEPS Report.[82] This was followed up with the publication of a concrete 15-Action Plan on BEPS on 19th July 2013 (Action Plan).[83] The 15-Action Plan otherwise known as the BEPS Package equips the governments with the domestic and international instruments needed to tackle BEPS and was eventually endorsed by the G20 Finance Ministers during their meeting of 8th October 2015 in Lima while the G20 Leaders followed suit by endorsing the BEPS package during their summit held in Antalya, Turkey between 15 and 16 November 2015.[84] The 15-Action Plan are listed below:

i. Address the tax challenges of the digital economy;
ii. Neutralise the effects of hybrid mismatch arrangements;
iii. Strengthen Controlled Foreign Company rules;
iv. Limit base erosion via interest deductions and other financial payments;
v. Counter harmful tax practices more effectively, taking into account transparency and substance;
vi. Prevent treaty abuse;
vii. Prevent the artificial avoidance of PE status;
viii. Assure that transfer pricing outcomes are in line with value creation- Intangibles;
ix. Risk & capital;

[73] The G20 (or G-20 or Group of Twenty) is an international forum for the governments and central bank governors from 20 major economies. Currently, these are Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, United Kingdom, United States, and the European Union. See <https://www.g20.org/Webs/G20/DE/Home/home_node.html> accessed on 17 July 2017

[74] OECD, 'OECD/G20 Base Erosion and Profit Shifting Project 2015' <http://www.oecd-ilibrary.org/taxation/oecd-g20-base-erosion-and-profit-shifting-project_23132612> accessed on 17 July 2017

[75] OECD, 'Base Erosion and Profit Shifting' <http://www.oecd.org/tax/beps/> accessed on 15 July 2017

[76] Ibid

[77] The G20 (or G-20 or Group of Twenty) is an international forum for the governments and central bank governors from 20 major economies. Currently, these are Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, United Kingdom, United States, and the European Union. See <https://www.g20.org/Webs/G20/DE/Home/home_node.html> accessed on 17 July 2017

[78] OECD, 'OECD/G20 Base Erosion and Profit Shifting Project 2015 Final Reports: Information Brief' <www.oecd.org/ctp/beps-reports-2015-information-brief.pdf> accessed on 15 July 2017

[79] Ibid

[80] OECD, 'OECD/G20 Base Erosion and Profit Shifting Project 2015' <http://www.oecd-ilibrary.org/taxation/oecd-g20-base-erosion-and-profit-shifting-project_23132612> accessed on 17 July 2017

[81] Ibid

[82] OECD, 'Addressing Base Erosion and Profit Shifting 2013'< http://www.oecd.org/ctp/beps.htm> 42 accessed on 17 July 2017

[83] OECD, 'Action Plan on Base Erosion and Profit Shifting 2013' <http://www.dx.doi.org/10.1787/9789264202719-en> accessed on 17 July 2017

[84] OECD, 'Base Erosion and Profit Shifting (BEPS)' 'https://www.oecd.org/g20/topics/taxation/' accessed on 15 July 2017

x. Other high-risk transactions;
xi. Establish methodologies to collect and analyse data on BEPS and the actions to address it;
xii. Require taxpayers to disclose their aggressive tax planning arrangements;
xiii. Re-examine transfer pricing documentation;
xiv. Make dispute resolution mechanisms more effective;
xv. Develop a multilateral instrument.[85]

All of the above 15-Action Plan are meant to prevent all kind of tax avoidance schemes. To ensure international consistency on the application of the Action Plan and as required by Action Plan 15, a Multilateral Convention to implement tax treaty related measures to prevent BEPS (Multilateral Instrument) was opened for signatory on 7th June 2017.[86] This Multilateral Instrument is considered as the solution for governments to close the gaps in existing international tax rules by transposing results from the OECD/G20 BEPS Project into various bilateral tax treaties worldwide without the necessity of amend the treaties. This is because signing the Multilateral Instrument automatically modifies the bilateral tax treaties of signatory countries to include the BEPS 15-Action Plan to prevent not only tax avoidance schemes but also to prevent treaty shopping and increase greater certainty in tax treatment among the signatory countries.[87]

Thus, many countries have adopted the OECD/G20 Base Erosion and Profit Shifting (BEPS) 15-Action Plan to address the income and profit shifting strategies of companies in their respective jurisdiction by signing the Multilateral Convention to implement tax treaty related measures to prevent base erosion and profit (MLI) and the Common Reporting Standard Multilateral Competent Authority Agreement (CRS MCAA) as recommended by the OECD. It is highly commendable that Nigeria signed the Multilateral Convention on 17 August 2017. This saves the country the need to renegotiate its existing tax treaties with countries who are also signatories to the convention bearing in mind that such renegotiation can be time consuming, resource intensive and cumbersome.[88] As at 17 August 2017, 71 countries have signed the Multilateral Instrument including six African Countries which are Burkina Faso, Cameroun, Egypt, Gabon, Nigeria, Senegal and South Africa.[89] Countries around the world are expected one way or the other to implement this 15-Action Plan BEPS package by amending their various tax legislation to counteract income and profit shifting to tax haven countries.

5. Regulation of Income and Profit Shifting to Tax Haven Countries in Nigeria

The Nigerian government recently signed the Multilateral Convention to implement tax treaty related measures to prevent base erosion and profit (MLI) and the Common Reporting Standard Multilateral Competent Authority Agreement (CRS MCAA) as recommended by the OECD to prevent companies from shifting their income and profits to tax haven countries. It has however been contended that the signing of these OECD instruments is not enough to prevent income and profit shifting in Nigeria but that the country has to go a step further in ensuring that the necessary legal frameworks are put in place otherwise the instruments will not be able to achieve their objectives in the country. For example, the objective of the MLI is to transpose the OECD/G20 BEPS project into their existing bilateral Double Tax Treaties network without going through the rigours of amendment. Nigeria has ratified bilateral Double Tax Treaties with just 13 countries. This means that the MLI is only applicable in respect of 13 countries which do not even include most of the tax haven countries identified by the OECD and other international organizations. The number of bilateral Double Tax Treaties has therefore been held to be too limited to achieve the objective of the MLI. Likewise, in respect of implementing the CRS MCAA, the country is yet to have domestic legislation mandating financial institution in the country to collate the financial information of relevant taxpayers which will be forwarded

[85]OECD, 'Action Plan on Base Erosion and Profit Shifting' <http://dx.doi.org/10.1787/9789264202719-en> accessed on 15 July 2017

[86]OECD, 'Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS' <http://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm> accessed on 3 August 2017

[87]OECD, 'Opening Remarks by Angel Gurria, OECD Secretary-General on 7th June 2017 at the Signing Ceremony: Multilateral Convention to implement tax treaty related measures to prevent BEPS' http://www.oecd.org/tax/signing-ceremony-multilateral-convention-on-tax-treaty-related-measures-to-prevent-BEPS> accessed on 17 July 2017

[88] Ibid

[89] OECD, 'Signatories and Parties to the Multilateral Convention to Implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting: Status as of 17 August 2017' <http://www.oecd.org/tax/treaties/beps-mli-signatories-and-parties.pdf> accessed on 26 August 2017

to the FIRS for onward automatic exchange with other countries.[90] The implication of this is that Nigeria will not be able to exchange information of this kind with countries that do not have bilateral Double Tax Treaty with the country.[91] It is therefore important that the Nigerian government should put all necessary legal framework in place to adopt this BEPS 15-Action Plan in line with the new international best practices. A country such as the US has shown a strong interest in regulating the use of offshore tax havens by signing Tax Information Exchange Agreements (TIEAs) with the tax haven countries in order to obtain income/profit shifting activities of the MNCs.[92] It is clear from the above that Nigeria do not have adequate legal framework to prevent the shifting of income and profit by companies operating in the country to their tax haven subsidiaries. It is therefore not surprising that despite the disclosure of the huge amount of income and profits shifted by individuals and companies in Nigeria to tax haven countries in both the panama papers[93] and the paradise papers,[94] the Nigerian government is yet to take any serious action in this respect.

6. Conclusion

The article provides an in-depth understanding of how companies shift income and profit to their tax haven subsidiaries to avoid taxation. The article revealed that a tax haven is any country that levy low or no tax on the income and profit of companies and provides lax regulatory policies, banking and business secrecy to companies. The article observed that due to the amount of income that have been lost to of income and profit shifting to tax haven, it is now seen as major form of transfer pricing abuse employed by companies to avoid taxation. The article found that the international response to income and profit shifting is the Arm's Length Principle (ALP) recommended by the OECD and the UN which is not without its weaknesses which have provoked argument for and against its continuous use. The 15-Action Plan on BEPS was developed to address the weaknesses of ALP. Finding from the article revealed that even though Nigeria relied on the arm's length provision in Section 22(2)(b) and Income Tax (Transfer Pricing) Regulation to prevent income and profit shifting, the country has not implemented the 15-Action Plan on BEPS recommended by the OECD/G20 or any other legal framework to stem the tide of income and profit shifting. This has severely affected the fight against the income and profit shifting in the country.

In light of the above, the article recommends as follows: The Nigerian government should work with the IMF, the OECD and other international organisations to develop its own official list of tax haven countries. These tax haven countries should be blacklisted by the Nigerian government. The Nigerian government should endeavour to sign Tax Information Exchange Agreements (TIEAs) with these tax havens. This is in line with what is obtainable in the United State. A provision should be included in the Income Tax (Transfer Pricing) Regulations stating that transactions into these tax haven countries carry a rebuttable presumption that such transaction is meant to shift the income and profit of Nigeria to avoid taxation. This will automatically put the burden on a MNCs in the country to prove that their transaction with their subsidiaries located in tax havens country are legitimate and not an artificial means to shift income and profit out of the country. The country should provide for stricter criminal penalty in form jail sentence without option of fine for Directors of MNCs where the income and profit shifting results in tax evasion. The OECD/G20 15-Action Plan BEPS Project should be implemented in Nigeria by putting in place necessary legal frameworks to incorporate the Action Plans into CITA. Nigeria should consider the option of using Formulary Apportionment (FA) in the future instead of relying on the ALP at all times. The European Union has stated that it will consider the use of FA in the future by introducing the Common Consolidated Corporate Tax Base under which it planned to allocate income and profit of MNCs rather than the ALP.

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[90] Ibid

[91] Ibid

[92] M. A. Desai, F. C. Foley F.C. & R. H. James, The demand for tax haven operations (2006) *Journal of Public Economics* 90

[93] International Consortium of Investigative Journalists (ICIJ), 'Investigative Report on Panama Papers' <https://www.panamapapers.icij.org> accessed on 12 July 2018

[94] International Consortium of Investigative Journalists (ICIJ), 'Investigative Report on Paradise Papers' <https://www.icij.org/investigations/paradise-papers> accessed on 12 July 2018