

## **Implementing the OECD Tax Base Erosion and Profit Shifting Action Items: What impacts will investment arbitration have? *Bogdanova v. Moldova, Enron v. Argentina and others***

**UNIGE-IISD Lunch Series on Investment Disputes  
October 19, 2017  
Speaker: Howard Mann  
Meeting Report: Mintewab Abebe**

As a part of the UNIGE–IISD Lunch Series on Investment Disputes on October 19, 2017, the International Institute for Sustainable Development (IISD) and the University of Geneva (UNIGE) co-organized a discussion on the topic of tax base erosion and profit shifting (BEPS) by investors. The session was moderated by Professor Makane Mbengue of UNIGE; Howard Mann, Senior International Law Advisor of IISD, was the main speaker.

Mr. Mann commenced his presentation by giving a brief background on the project he is leading that works on [countering tax BEPS by investors in the mining](#) sector for the Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development.

The presentation continued with a focus on the impact of stabilization clauses and investment treaties on BEPS mitigation. Used by corporations to exploit gaps and mismatches in the tax rules, BEPS refers to two types of tax avoidance strategies: (1) base erosion, the act of reducing taxable income; and (2) profit shifting, the act of moving profit from high-tax to low- or no-tax jurisdictions.

Unlike illegal tax evasion, allocating profits using BEPS strategies is not illegal: it is the legal use of loopholes or business practices to avoid being captured by tax laws. It is estimated that such practices have resulted in an annual loss to governments in terms of tax revenue ranging from USD 100 billion to 200 billion, mostly in the natural resource sectors in developing countries.

However, as governments start to recognize the harm and begin to explore ways to address BEPS, they have found that the current investment legal framework might impose significant limitations. One such limitation is the so-called stabilization clauses, which are found in some investment contracts and domestic laws. Some of these clauses stabilize the legal regime, for example, by freezing the law that is applicable at the time investment is made. Others force governments to compensate the costs of implementing a new measure. The scope of these stabilization clauses may cover all domestic laws or be limited to the fiscal regime. They may be in force during the entire life of the investment project or for a specified period starting from the date of commencement or production.

Research shows that these clauses are commonly found in agreements concluded by developing countries, particularly in Africa, as these governments are still being told that their markets are too volatile and require them to make specific guarantees to attract foreign capital and develop the sector.

Taking *Enron v. Argentina* and *Bogdanov v. Moldova* as two examples, Mr. Mann explained how these stabilization clauses could be read to limit a government's ability to address BEPS, especially when coupled with investment protection clauses offered by investment treaties. Although many investment arbitration tribunals have recognized the states' rights to regulate, the tribunals in these and other cases subjected the right to regulate to the caveat of stabilization clauses.

Mr. Mann discussed how states could address this issue in future investment treaty practice. There are exceptions to the limitations on states' right to regulate. Countering BEPS practices is now increasingly being recognized as a matter of international public order; hence, restricting governments' ability to address BEPS measures that may have been unforeseen when stabilization provisions were introduced could be seen as inconsistent with public policy. Implementation of international agreements and standards that are emerging in this area also helps ensure that measures are not seen as arbitrary or discriminatory.

Several options might also be proposed in contracts and treaties. One is to include precise provisions on what is covered and for how long in the stabilization clauses. The other option is to include alternative clauses on obligation against the arbitrary and discriminatory treatment of investors instead of stabilization clauses. Other suggested options include:

- Counter-balancing investor rights with express recognition of the obligation of investors not to use BEPS practices
- Recognizing that governments maintain the right to regulate in the public interest without paying compensation
- Expressing right to implement international best practice/standards provision concerning operations, taxation, accountability
- Obligations for the Extractive Industries Transparency Initiative to apply to covered projects
- Excluding taxation or limiting access to dispute settlement for tax issues (*Occidental v. Ecuador* compared to *Encana v. Ecuador*).

In conclusion, it was underlined that stabilization clauses have an impact under international law, whether they are legal under domestic law or not. However, their impacts depend on the clarity and scope of drafting in contracts, in investment treaties and a changing perception of international policy on BEPS.