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HANDBOOK ON DISPUTE AVOIDANCE AND RESOLUTION

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Handbook on the Avoidance and Resolution of Tax Disputes

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Preface

Taxes, which are essential for the provision of public goods and services, are a critical source of financing for the 2030 Agenda for Sustainable Development and the Sustainable Development Goals. Income taxes, in particular, contribute to reducing inequalities and ensuring greater macroeconomic stability.

Given the complexity of income tax laws, however, disputes concerning the interpretation and application of these laws are probably unavoidable in systems based on the rule of law. A main preoccupation of those responsible for designing tax systems is therefore the need to adopt measures that minimize such disputes and, where this is not possible, that ensure that disputes are resolved fairly and effectively. This is particularly important for policy makers and tax administrations of developing countries because the fair and effective resolution of tax disputes serves to balance the need to raise revenues and the need to attract and keep foreign investment. Achieving the right balance contributes to the strengthening of domestic resource mobilization.

Since the inception of the United Nations Committee of Experts on International Cooperation in Tax Matters, the avoidance and resolution of tax disputes, with a particular focus on the mutual agreement procedure, has featured prominently in the work of the Committee.

At its first session in 2005, the Committee discussed the pros and cons of international tax arbitration and some of its members were invited to prepare a report on alternative methods for avoiding or solving disputes. Following the presentation of that report at the Committee's second session in 2006, the Committee decided to set up a Subcommittee on Dispute Resolution to continue the work on this topic, paying attention "both to the ways of improving dispute settlement and of giving practical guidance to make mutual agreement procedures under existing treaties as effective as possible."[1]

At its sixth session in 2010, the Committee discussed a report on arbitration and a draft guide on the mutual agreement procedure which

1 *Report on the Second Session (30 October–3 November 2006)*, E/2006/45-E/C.18/2006/10 (accessed on 12 March 2021), p. 12, para. 60.

had been prepared by that Subcommittee. It decided that two alternative versions of Article 25 (Mutual Agreement Procedure) should appear in the *United Nations Model Double Taxation Convention between Developed and Developing Countries*[2] (United Nations Model Tax Convention): Alternative A would not provide for arbitration, while Alternative B would include a provision on mandatory arbitration.[3] Written comments were invited on the draft guide on the mutual agreement procedure, which was subsequently finalized and adopted by the Committee at its eighth session in 2012.[4]

The Committee returned to the issue of the resolution of tax disputes at its eleventh session in 2015, when a paper on arbitration was presented. The Committee then decided to set up a new *Subcommittee on the Mutual Agreement Procedure—Dispute Avoidance and Resolution*.[5] The main outcome of the work of that Subcommittee was the drafting of changes to the Commentary on Article 25 (Mutual Agreement Procedure) of the United Nations Model Tax Convention. As a result of that work, a number of changes to that Commentary, which dealt primarily with the results of the work on Action 14 of the BEPS project[6] of the Group of Twenty (G20)[7] and the Organization of Economic Cooperation and Development (OECD),[8] were adopted

2 United Nations, Department of Economic and Social Affairs, *United Nations Model Tax Convention Double Taxation Convention between Developed and Developing Countries, 2017 Update,* United Nations publication ST/ESA/PAD/SER.E/213, available at https://www.un.org/development/desa/financing/sites/www.un.org.development.desa.financing/files/2020-03/UN%20Model_2017.pdf, accessed on 12 March 2021.

3 *Report on the Sixth Session (18–22 October 2010)*, E/2010/45-E/C.18/2010/7, accessed on 12 March 2021, p. 7, para. 29. These two versions of Article 25 were included in the United Nations Model Tax Convention in 2011.

4 *Report on the Eighth Session (15–19 October 2012)*, E/2012/45-E/C.18/2012/6, accessed on 12 March 2021, p. 17, paras. 76–78.

5 *Report on the Eleventh Session (19–23 October 2015)*, E/2015/45-E/C.18/2015/6, accessed on 12 March 2021, pp. 20–23, paras. 98–100.

6 More information on Action 14 of the OECD/G20 Project is provided in chap. 1, section 1.3.

7 See www.g20.org, accessed on 12 March 2021.

8 See www.oecd.org, accessed on 12 March 2021.

at the fourteenth session of the Committee in 2017. During the same meeting, the Committee also adopted the first outline of a handbook on dispute avoidance and resolution, on which the Subcommittee had done preliminary work.

At its fifteenth session in 2017, which was the first meeting of a new membership of the Committee (2017–2021), the Committee decided that a new *Subcommittee on Dispute Avoidance and Resolution* would continue the work of the previous subcommittee with the following mandate:[9]

> The Subcommittee should consider and report back to the Committee on possible means of dispute avoidance and resolution, on both the domestic and international level. In particular, the Subcommittee will consider the Mutual Agreement Procedure, with a view to improving its effectiveness, building on the work done by the previous subcommittee. Particular attention will be paid to:
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> — Mechanisms to avoid and resolve disputes arising at the domestic level;
>
> — Ways to ensure that the Mutual Agreement Procedure under article 25 (in either of its alternatives in the United Nations Model) functions as effectively and efficiently as possible; and
>
> — Issues associated with arbitration clauses and other means as options to supplement the Mutual Agreement Procedure.
>
> Following work on these areas, the Subcommittee will produce the following outcomes:
>
> — A draft United Nations Handbook on Dispute Resolution and Avoidance;
>
> — A draft updated text of the United Nations Guide to the Mutual Agreement Procedure;
>
> — Drafts of possible changes to the United Nations Model Convention and/or Commentaries, as appropriate.
>
> The Subcommittee is to focus especially on issues affecting developing economies, possible means of addressing them in a practical manner and ways to build confidence in dealing with them. It will provide

9 *Report on the Fifteenth Session (17–20 October 2017)*, E/2018/45-E/C.18/2018/1, accessed on 12 March 2021, p. 22, para. 74. The list of participants in that Subcommittee appears in the Annex to this Handbook.

> recommendations to the Committee within its agreed mandate, on improvements, if any, for inclusion in the next version of the United Nations Model. The Subcommittee should work on the United Nations Handbook on Dispute Resolution and Avoidance and an update to the Guide to the Mutual Agreement Procedure as a priority.

At its sixteenth session in 2017, the Committee revised the outputs expected from the work of the new Subcommittee when it decided that, instead of updating the previously-adopted *Guide to the Mutual Agreement Procedure,* the Subcommittee should incorporate the contents of the Guide into the chapter of the Handbook that would deal with the mutual agreement procedure.[10]

This *Handbook on the Avoidance and Resolution of Tax Disputes* represents the final outcome of the work of the Subcommittee. The six chapters of the Handbook prepared by the Subcommittee were successively discussed and approved by the Committee at the six sessions of the Committee that took place from October 2018 to April 2021. The consolidated version of the Handbook was formally adopted by the Committee at its twenty-second session in April 2021.

As noted in Chapters 1 and 6, the provision of technical assistance to developing countries should improve their capacity to minimize and resolve tax disputes. Some of the contents of the Handbook have already been used in capacity-building workshops. Organizers of such learning events and capacity building activities are encouraged to use this complete version of the Handbook for that purpose.

We hope that this Handbook will provide a useful tool for developing countries and will contribute to the strengthening of their domestic resource mobilization for their sustainable development efforts.

We wish to acknowledge the contribution of the Secretariat of the Financing for Sustainable Development Office in preparing this Handbook, including the contribution of Irving Ojeda Alvarez, Patricia Brown, Michael Lennard, Silvia, Jacques Sasseville and Maria De Azevedo Sodre.

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10 *Report on the Sixteenth Session (14–17 May 2018)*, E/2018/45/Add.1-E/C.18/2018/7, accessed on 12 March 2021, p. 15, para. 54.

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Part 2—The dispute resolution mechanism of tax treaties: the MAP

List of Abbreviations

ALP	Arm's length principle
APA	Advance pricing arrangement
BEPS	Base erosion and profit shifting
CAP	Compliance Assistance Programme
CbC reports	Country-by-country reports
FHTP	Forum on Harmful Tax Practices
FTA	OECD Forum on Tax Administration
ICAP	International compliance assurance programme
IMF	International Monetary Fund
ICSID	International Centre for Settlement of Investment Disputes
ITAT	Income Tax Appellate Tribunal
MAP	Mutual agreement procedure
MLI	Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting
MNE	Multinational enterprise
NBDR	Non-binding dispute resolution
OECD	Organization for Economic Cooperation and Development
OECD Model Tax Convention	OECD Model Tax Convention on Income and on Capital, 2017 version
PFA	Pre-Filing Agreement
PRODECON	*Procuraduría de la Defensa del Contribuyente*

TIWB	Tax Inspectors Without Borders
United Nations Model Tax Convention	United Nations Model Double Taxation Convention between Developed and Developing Countries, 2017 version
United Nations Tax Committee	United Nations Committee of Experts on International Cooperation in Tax Matters
WBG	World Bank Group

PART 1

MEASURES TO AVOID AND RESOLVE TAX DISPUTES

Chapter 1

Introduction and Overview

1.1 Purpose of the Handbook

1. This Handbook seeks to provide guidance on the various mechanisms that may be used to avoid tax disputes and, where such disputes arise, to resolve them.

2. The Handbook has been drafted primarily for the benefit of developing countries and, in particular, least developed countries. Most of the issues that it addresses, however, present themselves to all countries, regardless of their level of development. For that reason, the guidance included in this Handbook should be relevant for all countries. The mechanisms for avoiding or resolving tax disputes that are proposed in this Handbook may not, however, be suitable for all countries. Some of these mechanisms will be more appropriate for consideration and implementation by developing countries that have more resources, including staff with the necessary experience and capability.

3. The tax disputes that are the object of this Handbook are those that may arise between tax administrations and taxpayers[1] under the provisions of domestic income tax[2] laws and tax treaties.

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1 The Handbook also covers some disputes between two tax authorities that arise in the context of a tax treaty (while references to tax authorities in this Handbook are generally synonymous to references to tax administrations, this might not always be the case, e.g. in countries where competent authority functions under tax treaties are performed by officials who do not belong to the tax administration).

2 Throughout this Handbook, references to income taxes include corporate taxes. While the focus of this Handbook is on income tax disputes, many of the mechanisms discussed in Part 1 of the Handbook could also be useful to avoid or resolve disputes regarding the application of other types of taxes, such as value-added taxes (especially since in some countries, the same or similar dispute resolution mechanisms apply to income taxes and value-added taxes). Also, because capital taxes are covered by many tax treaties, Part 2 also covers the use of the mutual agreement procedure in relation to disputes concerning the application of tax treaties with respect to such taxes.

4. The Handbook is divided into two parts, each of which is described in more detail in Section 1.4. Part 1 has a broad focus and deals with mechanisms for avoiding and resolving tax disputes that could arise in a purely domestic context as well as cross-border tax disputes, including those related to the application of tax treaties. Part 2 focuses exclusively on the mutual agreement procedure, which is the procedure included in tax treaties that enables certain tax officials of the treaty countries to resolve bilaterally cross-border issues related to the application or interpretation of the treaty provisions.

1.2 The importance of appropriate measures for the avoidance and resolution of tax disputes

5. The application and interpretation of income tax legislation raises complex issues, particularly where cross-border transactions are involved. Since it is impossible to avoid all disputes related to such issues, tax systems should ideally be designed to minimize such disputes and, when these disputes arise, to ensure that they are resolved through a fair and effective process.

6. This becomes even more important in light of the additional risks of tax disputes, in particular with respect to cross-border transactions, that arise from some features of new business models that rely on the digitalisation of the economy. Additional risks may also arise from various domestic and international measures that have been introduced or proposed to deal with difficulties that have arisen from the application to these business models of tax rules that were designed a long time ago.

7. While all countries that rely on income taxes need to strive to minimize disputes and ensure that those that arise are resolved fairly and effectively, this is particularly important for developing countries. These countries are frequently confronted with the competing needs of raising much-needed tax revenues and of attracting and keeping foreign investment, which are both essential to their sustainable development. The implementation of effective measures for avoiding and resolving tax disputes provides taxpayers with greater certainty that tax laws will be correctly applied and interpreted and therefore supports foreign cross-border investment and cross-border trade of goods and services, including employment services.

8. In their progress reports on tax certainty submitted to the G20 in 2017[3] and 2018,[4] the OECD and IMF identified the sources of uncertainty in tax matters and the various tools that taxpayers and governments could use to reduce that uncertainty from the perspective of businesses and tax administrations. The reports analyse the results of a 2016 OECD business survey on tax certainty. Figure 9 of the 2018 report shows the top 10 tools that the survey identified among different regions as most important for addressing tax certainty.[5] It reveals that improving domestic dispute regimes is seen as more important for countries of Latin America and the Caribbean, Asia and Africa than for OECD countries while mutual agreement procedure (MAP) issues appear to be relatively more important in Asia, Latin America and the Caribbean than in the OECD (and is less important in Africa, where there are relatively few MAP cases).

9. The 2018 report also gives a detailed account of the discussions at a Consultative Workshop on Tax Certainty held in Tanzania in 2017 and attended by more than 50 delegates, including officials from ministries of finance and tax administrations of 21 African countries. Improving dispute resolution was one of the possible improvements to tax policy, legislative processes as well as revenue administrations' capabilities that the participants to that workshop identified as tools that could increase tax certainty in Africa:[6]

> **Improving dispute resolution mechanisms**. Implement effective dispute resolution mechanisms as a means to enhance tax certainty for both taxpayers and tax authorities. Delegates concluded that dispute resolution mechanisms should be fair, independent from audit activities, accessible to taxpayers and effective in resolving disputes in a timely manner. This requires designing an independent, workable and

3 IMF and OECD, *Tax Certainty, IMF/OECD Report for the G20 Finance Ministers*, March 2017, available at https://www.oecd.org/tax/tax-policy/tax-certainty-report-oecd-imf-report-g20-finance-ministers-march-2017.pdf, accessed on 12 March 2021.

4 IMF and OECD, *Update on Tax Certainty, IMF/OECD Report for the G20 Finance Ministers and Central Bank Governors*, July 2018, available at http://www.oecd.org/ctp/tax-policy/tax-certainty-update-oecd-imf-report-g20-finance-ministers-july-2018.pdf, accessed on 12 March 2021.

5 Ibid., p. 46.

6 Ibid., p. 28.

graduated dispute resolution process comprising an administrative and judicial stage. The administrative stage could involve alternative dispute resolution mechanisms, while, on the judicial side, the issue of judicial capacity needs to be addressed as a matter of priority.

10. As explained in these two reports and in Chapter 2, however, tax certainty does not only require effective mechanisms to avoid tax disputes when they arise but also a general environment that minimizes the potential for such disputes. This starts with the need for clear and accessible legislation and interpretative guidance by the tax administration.

11. The increased importance of effective dispute resolution mechanisms is particularly obvious in the case of the MAP, which is the focus of Part 2 of the Handbook. The number of cases involving the use of the MAP has grown steadily over the last two decades: country statistics on the MAP show that the number of outstanding MAP cases has increased on average by more than 11 per cent each year between 2006 and 2015.[7] The statistics also show, however, that currently the vast majority of MAP cases arise under tax treaties between two developed countries and that relatively few mutual agreement cases involve developing countries other than large emerging economies.[8] As these statistics suggest, the majority of developing countries have no or limited experience with the MAP even though the number of MAP cases

7 Statistics on MAP cases have been collected by the OECD since 2006: see http://www.oecd.org/tax/dispute/map-statistics-2006-2015.htm, accessed on 12 March 2021. As explained below, these statistics were expanded in 2016 to include more details and to include the MAP cases of all countries that are members of the Inclusive Framework on BEPS: see the statistics for 2019 at http://www.oecd.org/tax/dispute/mutual-agreement-procedure-statistics.htm, accessed on 12 March 2021.

8 The 2019 MAP statistics of the Inclusive Framework on BEPS reveal that not a single outstanding MAP case was reported by countries of the Inclusive Framework that appear on the World Bank's list of low-income economies and that only 0.8 percent of the total reported outstanding MAP cases were reported by countries (other than India) that appear on the World Bank list of lower-middle-income economies (the World Bank lists are available at https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups, accessed on 12 March 2021).

involving developing countries is increasing. Regardless of a country's degree of previous experience, however, all countries that enter into tax treaties must be prepared to meet their obligations with respect to the MAP and must therefore understand that procedure and implement administrative processes to deal with MAP cases that may arise under their tax treaties.

12. The G20/OECD Project on Base Erosion and Profit Shifting (BEPS) has had a significant impact on the implementation of the MAP. The BEPS Action Plan recognized that its recommendations to counter base erosion and profit shifting had to be complemented with work aimed at improving the effectiveness of the MAP as a mechanism for resolving treaty-related disputes.[9] Work in this area was carried out under Action 14 (Making dispute resolution mechanisms more effective) of the BEPS Action Plan. The final report on Action 14[10] includes a number of best practices related to the MAP. It also sets forth a minimum standard with respect to the resolution of treaty-related disputes through the MAP which has the following objectives: [11]

- Ensure that treaty obligations related to the MAP are fully implemented in good faith and that MAP cases are resolved in a timely manner
- Ensure the implementation of administrative processes that promote the prevention and timely resolution of treaty-related disputes
- Ensure that taxpayers can access the MAP when eligible[12]

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9 OECD (2013), *Action Plan on Base Erosion and Profit Shifting*, OECD Publishing, Paris, https://doi.org/10.1787/9789264202719-en, accessed on 12 March 2021, p. 23.

10 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14—2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/9789264241633-en, accessed on 12 March 2021.

11 Ibid., p. 9.

12 On 18 November 2020, the OECD released a consultation document seeking input on proposals for a review of the Action 14 minimum standard concerning "a) Experiences with, and views on, the status of dispute resolution and suggestions for improvements […]; b) Additional elements to strengthen the Action 14 Minimum Standard;

13. The large number of countries that have joined the Inclusive Framework on BEPS[13] have committed to implement that minimum standard[14] (which is not the case for countries that are not members of the Inclusive Framework). The fact that compliance with the minimum standard is reviewed and monitored by other countries is intended to ensure a greater international scrutiny of how each country that is a member of the Inclusive Framework applies the MAP.[15] Two elements of the minimum standard will also contribute to that result. First, the minimum standard requires all countries that are members of the Inclusive Framework on BEPS to provide annual statistics on their MAP cases,[16] including their total MAP caseload, the average time required to complete MAP cases, the general outcomes of the MAP cases that were closed, the other jurisdictions involved in the cases and the proportion of the cases that dealt with issues regarding the allocation of profits between associated enterprises or the attribution of profits to a permanent establishment as opposed to other issues. Second, all these countries must become members of the FTA MAP Forum,[17] a subsidiary body of the OECD Forum on Tax Administration (FTA)[18] which meets regularly to deliberate on matters affecting the MAP and to monitor the implementation of the minimum standard.

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and c) Additional elements to strengthen the MAP Statistics Reporting Framework" (that consultation document is available at https://www.oecd.org/tax/beps/public-consultation-document-beps-action-14-2020-review-november-2020.pdf, accessed on 12 March 2021). That review process was still ongoing when this Handbook was finalized.

13 As of February 2021, 139 countries and jurisdictions were members of the Inclusive Framework on BEPS: see https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf, accessed on 12 March 2021.

14 The elements of that minimum standard and the best practices included in the final report on Action 14 are included in the Annex to Chapter 4.

15 See http://www.oecd.org/tax/dispute/beps-action-14-peer-review-and-monitoring.htm, accessed on 12 March 2021.

16 See *Action 14 - 2015 Final Report*, footnote 10, p. 15.

17 Ibid., p. 16.

18 See OECD Forum on Tax Administration, http://www.oecd.org/tax/forum-on-tax-administration, accessed on 12 March 2021.

1.3 Challenges faced by developing countries and, in particular, least developed countries

14. While the issues addressed in this Handbook present themselves to all countries regardless of their level of development, the specificities of developing countries, in particular the least developed countries, create a number of challenges with respect to the avoidance and resolution of tax disputes.

15. The limited resources of the tax authorities of these countries may be the main challenge. A lack of personnel with the capacity and expertise to deal with complex tax issues, particularly with respect to cross-border transactions, means that these issues might not be dealt with adequately. This creates risks of not assessing tax that should be payable (e.g. as a result of tax avoidance transactions) and of generating disputes that could easily have been avoided, e.g. through clear legislation or proper guidance by the tax administration or by a greater awareness, by that tax administration, of its treaty obligations.

16. Limited resources also impact these countries' capacity to effectively resolve disputes that arise. This relates to the treatment and resolution of disputes by both the tax administration and by independent parties, primarily the courts. For instance, lengthy delays in obtaining a final court decision are frequent in some countries, which undermines the usefulness of having access to domestic courts to resolve tax disputes. Also, the absence of judges specialized in tax law tend to favour a literal interpretation of tax legislation. Such a literal approach may restrict the ability to arrive at solutions that are equitable for taxpayers and for governments in need of tax revenues and may have the effect of facilitating tax avoidance.

17. There has recently been an emphasis by the international community on the provision of assistance to developing countries to help them minimize and resolve tax disputes. This assistance may help these countries overcome these and other challenges, particularly in the international context and in relation to the MAP.

18. Other challenges that arise for developing countries include, in some of these countries, the absence of tax treaties or the existence of a limited tax treaty network, which may prevent the resolution, through the mutual agreement procedure, of some cross-border issues with other tax administrations, in particular issues related to transfer

pricing and attribution of profits to permanent establishments. This may increase the potential for double taxation and may add to the pressure to provide tax incentives or to grant special tax regimes to large foreign investors. Other challenges that are specific to the MAP are discussed in paragraph 7 of Chapter 4.

19. The protection of taxpayer rights, including the right to confidentiality, may be another challenge in some countries. Without confidence that these rights will be respected, taxpayers may have little trust in available dispute avoidance and resolution measures.

20. Some countries may also have difficulties in ensuring the independence of officials involved in the resolution of tax disputes vis-à-vis those responsible for the audit or collection of taxes. This problem is often encountered with respect to officials performing the competent authority function in MAP cases.

21. Given that the income tax legislation of developing countries is typically simpler than that of developed countries, the tax administrations of developing countries are frequently more vulnerable to avoidance transactions, a problem that is likely exacerbated by the adoption of a literal interpretation approach by the courts (disputes related to avoidance transactions are typically difficult to resolve and frequently reach courts).

22. The constitutional and legal framework of some developing countries, including the views of authorities in charge of the application and interpretation of the relevant rules, may also create difficulties with respect to the adoption and implementation of some mechanisms for the avoidance or resolution of tax disputes. In some countries, for instance, the use of alternative dispute resolution mechanisms has been found to be contrary to constitutional or basic legal principles.

1.4 Contents of the Handbook

Part 1—Measures to avoid and resolve tax disputes

23. Part 1 relates to measures that may be taken by countries for the avoidance and resolution of income tax disputes that may arise both in a domestic and international context. It includes this introductory chapter as well as Chapter 2 on Approaches to avoiding disputes and Chapter 3 on Domestic dispute resolution mechanisms. It

is acknowledged that the distinction between measures that aim to avoid disputes and those that seek to resolve them is sometimes unclear; in order to distinguish the two, this Handbook considers that mechanisms for resolving disputes are those that are applicable to disagreements concerning income taxes that have been assessed or reassessed. This therefore excludes measures, such as certain forms of administrative review or mediation, that may be available to resolve disagreements that may arise at any stage up to, and during, the audit process, i.e. before the audit results in an assessment or reassessment or demand to pay tax. Some of these other measures are discussed as part of the approaches used to avoid disputes that are dealt with in Chapter 2.

Chapter 2—Approaches to avoiding disputes

24. Chapter 2 begins by explaining what types of potential disputes are addressed and the importance and benefits of effective dispute avoidance mechanisms for both tax administrations and taxpayers.

25. The chapter then discusses how the first and likely most effective way of preventing tax disputes is to ensure that taxpayers can easily determine their tax rights and obligations under the tax law. A first way to contribute to that objective is to have clear and accessible legislation and interpretative guidance; the chapter explains how setting up a public consultation process before the final adoption of tax legislation allows stakeholders to provide insights to the legislator on the effectiveness, the implementation and the compliance costs of proposed tax legislation. It will also help if governments are conscious of the interaction between proposed domestic legislation and the legislation of other countries and with the country's international obligations, for instance those arising from tax treaties. Similarly, in performing its audit function, it will be important for the tax administration to have a level of global awareness that allows it, in the course of auditing compliance with domestic tax law, to assess whether bilateral tax treaties have been interpreted and applied appropriately. Another aspect to take into account is the legal environment in which the dispute avoidance mechanisms operate: tax law is part of public law and hence, is subject to the same procedural and substantive restrictions that apply to other parts of public law; in addition, in reaching an agreement or solution with a taxpayer related to the application of tax legislation, a tax administration needs to conform

with the rule of law and the principles of good administration applicable in the relevant country. When designing, implementing and administering tax legislation, it is also important to keep in mind that taxpayers should be treated equally before the law. Finally, developing more sophisticated risk assessments will enable tax administrations to focus on high risk sectors and high risk taxpayers, which, in turn, should lead to a reduction in the number of disputes and a more effective resolution of disputes with high risk taxpayers since more resources will be available to address these disputes.

26. These general considerations are followed by a description of various specific approaches used by countries to avoid tax disputes, which constitutes the main part of the chapter.

27. This begins with a reference to the guidance and advice provided by a tax administration. Such guidance and advice can be effective in preventing disputes from arising when it is clear, accurate, consistent, and accessible to the taxpayers. A tax administration may provide guidance on how the tax law operates generally. A description of the types of guidance provided by the Australian Taxation Office illustrates different forms that such guidance can take. A tax administration may also provide advice on a taxpayer's obligations or entitlements under specific provisions of the law, such advice being generally in the form of public or private rulings. This is illustrated by a reference to the types of advice provided by the Australian Taxation Office and by the Kenya Revenue Authority.

28. The next approach discussed in the chapter is the Advance Agreement/Pre-Filing Agreement, which is a variation of the advance ruling concept. A description of the Pre-Filing Agreement Programme that the IRS offers to corporate taxpayers illustrates that approach.

29. The chapter goes on to discuss how the use of advance pricing arrangements (APAs) can also be an effective tool in avoiding disputes between tax administrations related to transfer pricing. After describing the nature of an APA and the legal basis under which unilateral, bilateral or multilateral APAs can be concluded, the chapter identifies a number of issues that should be considered by a country wishing to establish an APA programme. A brief description of Indonesia's APA programme shows how it has actually been done by a developing country.

30. Different approaches aimed at improving the relationship between the taxpayer and the tax administration, which therefore reduce the risk of disputes, are dealt with in the following section of the chapter. That section first discusses the nature and potential benefits of "cooperative compliance", which generally refers to an approach that builds on a reciprocal relationship of trust and cooperation between the tax administration and the taxpayer. A brief description of the Tax Compliance Incentive Programme (Pro-Conformity) that has been proposed by the tax administration of Brazil illustrates how cooperative compliance could be of interest not only for developed countries (where it has primarily been used so far) but also for emerging and developing countries. This is supplemented by general guidance for countries that may want to consider setting up a pilot study to see how cooperative compliance could work within their legal, political and administrative environment. The section also discusses how the appointment of a single point of contact, or "relationship manager", who would be responsible for the tax administration's overall relationship with a taxpayer (which would be particularly helpful in the case of large taxpayers and high-net-worth individuals), could help prevent disputes. This approach is illustrated by the description of the Client Relationship Manager Programme of the Tax Administration Jamaica.

31. The next approach described in Chapter 2 is "International Compliance Assurance Programme" ("ICAP"), which is a voluntary programme for a multilateral cooperative risk assessment and assurance process that was launched in January 2018 as a pilot programme. After another expanded pilot programme in 2019, ICAP is now being run as a full programme open to all OECD Forum on Tax Administration (FTA) member tax administrations. In February 2021, the FTA released a handbook on ICAP containing information on the ICAP process which reflected the experience and feedback of the tax administrations and the multinational enterprise groups (MNE groups) that participated in the two pilots.[19] ICAP provides for a

19 Forum on Tax Administration, *International Compliance Assurance Programme—Handbook for Tax Administrations and MNE Groups* (Paris, 2021), available at https://www.oecd.org/tax/forum-on-tax-administration/publications-and-products/international-compliance-assurance-programme-handbook-for-tax-administrations-and-mne-groups.pdf, accessed on 12 March 2021.

multilateral approach aimed at providing early tax certainty for eligible MNE groups which could have the effect of preventing disputes from arising between those MNE groups and the tax administrations.

32. The use of joint audits is another approach described in the chapter. That approach was introduced in 2010 by the FTA and is to be distinguished from simultaneous tax audits. The chapter explains that joint audits, where two or more countries join to form a single audit team to conduct a taxpayer examination, could result in quicker issue resolution, more streamlined fact finding and more effective compliance. For this reason, joint audits may provide tax certainty and therefore could be effective in preventing disputes from arising between tax administrations and taxpayers.

33. The "independent review of the statement of audit position" is an independent review procedure conducted during the audit stage which operates as a dispute avoidance mechanism when the outcome of that independent review has the effect of preventing a dispute from formally arising (e.g. where that review leads the tax administration to abandon the idea of issuing a reassessment for additional income tax payable in a specific case). The chapter describes how that type of procedure is provided by the Australian Taxation Office.

34. The last dispute avoidance approach referred to in Chapter 2 is that of mediation offered during a tax audit. The chapter describes two different types of mediation processes that can be conducted during the audit stage: the first, "in-house facilitation", involves an impartial official of the tax administration acting as a facilitator while the second, "independent mediation", involves mediation services provided by an independent body (the chapter describes the main features of that type of procedure as it is used in Mexico).

Chapter 3—Domestic dispute resolution mechanisms

35. Chapter 3 deals with the domestic[20] mechanisms that are generally available in countries to resolve disputes that can arise between tax administrations and taxpayers with respect to the determination

20 As opposed to international mechanisms such as those provided by treaties.

of income taxes payable.[21] It aims to provide practical guidance to countries that wish to improve certain aspects of their domestic dispute resolution process, it being understood that each country needs to determine which of the mechanisms described in the chapter are best adapted to its own situation, in particular its legal framework and the nature of the tax disputes that typically arise in it.

36. The first part of the chapter emphasizes the importance of making mechanisms available to taxpayers to resolve disputes as efficiently and quickly as possible. The chapter goes on to provide a number of typical examples of disputes resulting from findings from an audit or examination concerning the amount of tax liability, explaining that such disputes may relate to the facts of a specific case, to the interpretation of the law or to both. This is followed by a quick overview of the main categories of dispute resolution mechanisms, a distinction being made throughout the chapter between mechanisms that are provided by the tax administration, such as the administrative appeal procedure, and those that exist separately from, and outside of, the tax administration, such as the resolution of a tax issue by the courts.

37. The main part of the chapter discusses a number of issues that are common to most forms of domestic dispute resolution mechanisms. These include, for example, whether and to what extent a tax administration is able to negotiate and accept compromise solutions to tax disputes, the importance of time limits, considerations related to the collection of disputed taxes and related penalties and interest as well as the coordination between different dispute resolution mechanisms.

38. The remaining parts of the chapter describe the main types of domestic dispute resolution mechanisms. The first of these are the administrative appeal procedure and the administrative mediation, two mechanisms through which dispute resolution is provided by the tax administration. This is followed by a discussion of different mechanisms through which dispute resolution is provided by independent parties. In almost all countries, taxpayers have the right to seek resolution of tax disputes in courts. Independent mediation services are also

21 Chapter 3 does not deal with disputes concerning the exercise, by the tax administration, of its enforcement and collection powers, including disputes related to information exchanges and documentation requirements.

available in some countries. The chapter also notes the role that a tax ombudsman that operates outside the tax administration may play in resolving domestic tax disputes, while indicating that some countries have established a tax ombudsman within the tax administration. The expert determination and arbitration procedures that are available in some countries are discussed at the end of the chapter.

Part 2—The dispute resolution mechanism of tax treaties: the mutual agreement procedure

39. Part 2 of the Handbook deals exclusively with the Mutual Agreement Procedure (MAP), which is the dispute resolution mechanism provided for in bilateral tax treaties. That part is divided into three chapters.

Chapter 4—The mutual agreement procedure

40. Chapter 4, the longest chapter of the Handbook, first provides a general description of the MAP, which is separate and independent from any administrative and judicial dispute resolution mechanisms provided by domestic law. It also explains the crucial role of the MAP towards ensuring that countries respect their tax treaty obligations. Since the majority of developing countries have no or limited experience with the MAP, the main purpose of the chapter is to provide guidance to these countries even though its contents should also be relevant for a broader range of countries. The chapter, which complements the guidance on the mutual agreement procedure found in the Commentary on the United Nations Model Tax Convention and is subordinate to that guidance, makes a number of references to the minimum standard and the best practices included in the final report on BEPS Action 14,[22] which are reproduced in the Annex to that chapter.[23]

41. While Article 25 of both the United Nations and OECD models provides for three different types of MAP, the chapter focusses primarily on the first type, the so-called "MAP on request", which involves requests made to competent authorities of the treaty States

22 See section 1.2 above.

23 See footnote 10.

by persons that consider that they have not been taxed in conformity with the provisions of a tax treaty. The chapter provides a list of typical treaty issues that are dealt with under that type of MAP with emphasis on issues related to the allocation of profits between associated enterprises and the attribution of profits to permanent establishments since these issues represent the majority of outstanding MAP on request cases.

42. The chapter includes a diagram and a flowchart that show the different actions normally involved in a MAP on request case. These are regrouped under the following five steps of a typical MAP process:

1. The MAP request
2. The unilateral stage of the consideration of the MAP case
3. The bilateral stage of the consideration of the MAP case
4. The conclusion of the MAP
5. The implementation of the mutual agreement reached through the MAP

The guidance included in the chapter addresses each of these steps in detail.

43. The section on the MAP request explains who is allowed to make a MAP request, to which competent authority the request should be made, when such request should be made and how it should be filed. A description of the format and contents of a MAP request includes a detailed example of a fictitious MAP request that would satisfy the requirements of most countries that have published guidance on that issue (that example is followed throughout the chapter by other examples of documents typically produced in the course of the MAP process). The section also addresses specific issues such as whether access to MAP can be denied in certain cases, what happens if the taxpayer who requests the MAP is also pursuing domestic recourses such as a court challenge, whether a single MAP request may be made for the resolution of recurring issues where the relevant facts and circumstances are the same, whether taxes may be collected once a MAP request has been filed and whether a MAP request may be withdrawn. The role of the competent authority that receives the request is explained in the last part of that section.

44. The subsequent section addresses the unilateral stage of the consideration of the MAP request, which requires that the competent authority that received the MAP request examine the merits of the request in order to determine whether it appears to be justified and, if that is the case, whether that competent authority can unilaterally eliminate the taxation not in accordance with the treaty provisions without the need to consult the competent authority of the other treaty country involved. This is followed by the section that deals with the bilateral stage of the consideration of the MAP, which is the step of the MAP process that must take place if the competent authority that received the MAP request concludes that the objection included in the request appears to be justified but that it is not able to resolve the case unilaterally. That competent authority must then engage with the competent authority of the other treaty State with the objective of jointly arriving at a satisfactory resolution of the case. Different methods of communication may be used for that purpose but the chapter explains that the process is typically initiated by inviting the other competent authority to provide a position paper or by offering to do so. That position paper and the written response produced by the competent authority that receives it will normally constitute the basis for the subsequent discussions between the competent authorities.

45. The fourth step of the MAP process, which is the conclusion of that process, is analysed in the subsequent section. That part of the chapter discusses the different possible outcomes of a MAP case and describes the different actions that are typically undertaken when the competent authorities reach a proposed agreement in a case, which normally requires the taxpayer's acceptance of that agreement and the formal conclusion of the agreement.

46. The next section deals with the last step that takes place after such an agreement is concluded, which is the implementation of the mutual agreement reached through the MAP. That section explains the legal obligation that is imposed on the treaty States to implement such a mutual agreement regardless of any time limits that may exist under the domestic law of the States and gives a few examples of domestic measures that may be required in order to implement that mutual agreement.

47. That section is followed by a table that summarizes the different actions involved in a MAP process that were discussed in the preceding

sections and provides a tentative timetable showing reasonable deadlines for each of these different actions.

48. The next section of the chapter briefly examines the process for the two other types of MAP provided for by Article 25 of the United Nations and OECD models, namely the "interpretative or procedural MAP" envisaged by the first sentence of paragraph 3 of the article and the "MAP on double taxation not dealt with under the treaty" which is governed by the second sentence of that paragraph.

49. This is followed by a section that addresses various aspects of the communications that take place between the competent authorities in the context of any type of MAP and which are subject to the rules of Article 26 of the United Nations and OECD models concerning the exchange of information and, in particular, the confidentiality requirements imposed by that article.

50. The last part of the chapter provides guidance on the organization of the MAP functions within a tax administration and on how a competent authority should approach a MAP case. It stresses the importance for competent authorities to make every effort to resolve cases in a principled, fair and objective manner, deciding each case on its own merits and not with reference to revenue considerations or an overall balance of results.

Chapter 5—MAP arbitration

51. Chapter 5 completes the analysis of the MAP included in Chapter 4 by examining the provisions that allow for the mandatory arbitration of issues arising from a MAP request that competent authorities are unable to resolve within a certain period of time.

52. The chapter first describes the key features of the provisions of paragraph 5 of Article 25 Alternative B of the United Nations Model Tax Convention which, unlike Alternative A of the article, provides for such mandatory arbitration. In doing so, it explains how this "MAP arbitration" is fundamentally different from commercial arbitration. The chapter also describes the differences between the arbitration provisions of the United Nations Model Tax Convention and those of paragraph 5 of Article 25 of the OECD Model Tax Convention and provides a brief background for the arbitration provisions included

in Part VI of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (MLI).[24]

53. The chapter presents the different views that have been put forward concerning recourse to MAP arbitration and analyses the perceived concerns and perceived benefits that have been raised by members of the United Nations Committee of Experts on International Cooperation in Tax Matters (United Nations Tax Committee), as referred to in the Commentary on Article 25 of the United Nations Model Tax Convention.

54. The perceived concerns first relate to the view that arbitration may affect a country's sovereignty and, in some countries, could raise constitutional issues. There are also concerns with respect to the costs of arbitration and some countries' lack of resources, including as regards the availability of local experts who could act as arbitrators. Another concern that has been expressed relates to the developing countries' lack of experience and familiarity with MAP and arbitration. Similarly, it has been argued that the existing small pool of possible arbitrators who can deal with complex international tax and transfer pricing issues come from the developed world and might not be familiar with concerns of developing countries. Concerns about transparency have also been raised because, like other parts of the MAP process, MAP arbitration proceedings are generally considered confidential and opinions are not published.

55. On the other hand, the perceived benefits that have been attributed to MAP arbitration by members of the United Nations Tax Committee who supported it first include the fact that it guarantees the resolution of MAP cases. It has also been argued that the inclusion of MAP arbitration provisions in a treaty has a "prophylactic" effect by encouraging competent authorities to compromise so as to resolve MAP cases more quickly and efficiently, the purpose of arbitration not being to replace the MAP with an independent evaluation of the case by arbitration, but to supplement the current MAP process in those few cases where the competent authorities are unable to agree on a resolution in a timely manner. Other perceived benefits are that

24 http://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf, accessed on 12 March 2021.

MAP arbitration provides more certainty to taxpayers as regards the conclusion of the mutual agreement procedure and that it reduces reliance on sometimes inadequate unilateral domestic remedies.

56. The last part of Chapter 5 discusses different aspects of the procedural rules that competent authorities should consider adopting as regards the conduct of proceedings under MAP arbitration provisions. The United Nations and OECD models as well as the MLI indicate that competent authorities typically enter into a competent authority agreement as regards such procedural rules and need to do so in order to practically implement MAP arbitration. These rules should first address the process through which arbitration must be initiated, taking into account the fact that while the United Nations Model Tax Convention provides that the request for arbitration may be made by the competent authority of one of the two States involved in the MAP case, the OECD Model Tax Convention and the MLI provide that arbitration is initiated by a request by the taxpayer. The chapter then addresses how and when the "terms of reference", which are the questions to be decided by the arbitration panel, should be determined. It also discusses the process through which the arbitration panel should be selected, including possible provisions on the required qualifications and independence of arbitrators and their eventual replacement.

57. A key aspect of arbitration that should be dealt with in either the treaty itself or a competent authority agreement is what type of arbitration process should be followed. Arbitration may be done in different ways such as "independent opinion" arbitration, where the arbitrators are asked to produce a reasoned decision that includes their conclusions as regards the facts, the evidence and the legal arguments, and "last best offer" or "baseball" arbitration where each competent authority submits its most reasonable solution to the case and the arbitration panel is asked to decide which of these proposed solutions will prevail based on their views on the facts and arguments presented in each solution proposed. The chapter explains these two different processes and the specific rules that each requires; it also stresses the need for strict time limits for each step of these processes.

58. Other procedural aspects of MAP arbitration addressed in the chapter include the responsibility for logistical arrangements, in particular if physical meetings of the arbitration panel are required, how to ensure the confidentiality of taxpayer information exchanged

during the arbitration process and the payment of the costs involved in the arbitration process, including the remuneration of the arbitrators. The final aspect addressed in the chapter is how an arbitration decision should be arrived at by the arbitrators and the possibility for competent authorities to depart from that decision.

Chapter 6—Possible improvements to the MAP

59. Chapter 6, the last chapter of the Handbook, concludes the analysis of the mutual agreement procedure by discussing various measures that could possibly improve the MAP, particularly in developing countries. While there is already some limited experience with a few of the measures discussed in that chapter, other measures have not been used, at least in the context of the mutual agreement procedure.

60. The first possible improvement described in Chapter 6 is the provision of technical assistance to a country under a programme such as the UNDP-OECD Tax Inspectors Without Borders (TIWB).[25] The chapter describes that programme and explains that it can support the provision of technical assistance with respect to MAP or APA cases. The 2020 Annual Report of the TIWB[26] indicated that the programme would be expanded to cover new areas of tax assistance, including tax treaty negotiation and administration. Such an expansion could provide the competent authorities of developing countries with even greater access to the expertise of former tax officials familiar with the MAP process and with the different types of treaty disputes that are typically dealt through that process.

61. Technical training on the MAP process is another possible improvement discussed in Chapter 6. Such training would be aimed at improving the capacity of tax administrations of developing countries to deal with MAP cases; it could deal with the MAP process as well as the MAP-related commitments of the large number of countries that have joined the BEPS Inclusive Framework. The chapter refers to the example of the capacity-building workshops on MAP

25 See chap. 6, Box 1.

26 OECD/UNDP (2020), *Tax Inspectors Without Borders—Annual Report*, available at http://tiwb.org/resources/reports-case-studies/tax-inspectors-without-borders-annual-report-2020.htm, accessed on 12 March 2021, p. 10.

that have already been provided by the partners of the Platform for Collaboration on Tax.[27]

62. The chapter also explains how the conclusion of "framework agreements" could help address some of the difficulties that the competent authorities of two countries encounter in dealing with their mutual MAP caseload, especially where there is a large number of pending MAP cases between these countries. Such a framework agreement could address procedural or administrative issues related to the MAP or could deal with specific substantive treaty issues. The chapter gives the example of the framework agreement concluded in 2015 by the competent authorities of India and the United States, which facilitated the resolution of more than 100 cases in the information technology sector.

63. The use of new information technologies to facilitate the MAP process is another possible improvement discussed in Chapter 6. New technology could provide a secure environment that would facilitate contacts and the sharing of information between the taxpayers and competent authorities involved in a MAP case, facilitate record keeping, time management as well as documentation and filing requirements. In the case of treaties that provide for MAP arbitration, technology could also help the competent authorities with time and documentation management and help protect the taxpayers' privacy rights by providing a secure and protected environment for making the necessary information accessible to the arbitrators. The decision to implement any new technology would obviously require a careful cost-benefit analysis, especially for countries that have very few MAP cases.

64. Finally, the last part of Chapter 6 discusses the possible use of non-binding dispute resolution (NBDR) mechanisms in MAP cases. Some have referred to the use of NBDR in the domestic tax context to suggest that it could improve the MAP process. Others, however, have

27 The Platform for Collaboration on Tax, which is a joint effort of the IMF, the OECD, the United Nations and the WBG, was set up with a major aim "to better frame technical advice to developing countries as they seek both more capacity support and greater influence in designing international rules". See https://www.worldbank.org/en/programs/platform-for-tax-collaboration, accessed on 12 March 2021.

expressed the view that the experience of NBDR in the domestic tax context may not be easily transferred to the MAP and have observed that there are no reported cases where NBDR has been used to resolve successfully a MAP case. The chapter discusses whether expert advice and mediation could constitute an alternative or a precursory step to MAP arbitration. It presents what some consider to be benefits and disadvantages of that suggestion and explains how expert advice and mediation could be implemented in the context of MAP and possible issues that this could raise.

Chapter 2

Approaches to Avoiding Disputes

2.1 Introduction

2.1.1 Overview

1. For a country's income tax system to operate efficiently and effectively, it is essential that its government and tax administration provide dispute avoidance mechanisms. These mechanisms seek to prevent disputes between the tax administration and taxpayers, which is to the benefit of both parties.

2. This chapter explores various approaches to avoiding disputes that are generally available to prevent domestic and international income tax disputes from arising between the tax administrations and the taxpayers. The chapter discusses different aspects of creating the environment for avoiding disputes, such as by developing tax policy and legislation with a level of global awareness so that the relevant information is clear and accessible and allows taxpayers to understand their rights and obligations, which reduces the risk of disputes arising.

3. The goal of this chapter is to assist developing countries with the further development and implementation of dispute avoidance strategies by describing different approaches to avoiding disputes used around the world. Some of the dispute avoidance approaches may be more appropriate for consideration and implementation by developing countries when their tax administrations have more resources, including staff with the requisite experience and capability. The chapter also considers the potential benefits for taxpayers and tax administrations of effectively implementing such dispute avoidance mechanisms.

2.1.2 The types of disputes addressed in this chapter

4. This chapter deals with mechanisms which can prevent disputes that may arise between tax administrations and taxpayers in relation to income taxes. As previously explained, for the purposes of this Handbook, a dispute is taken to arise where an audit results in the tax administration issuing an assessment or reassessment for additional

income tax payable by the taxpayer, or a demand for payment of tax, with which the taxpayer does not agree.

5. The income tax disputes which can arise between a tax administration and a taxpayer prior to, or during the audit may be in relation to the facts, the interpretation of the tax law and/or the application of the tax law to the taxpayer's factual circumstances.

6. Illustrations of the types of disputes which can arise between a tax administration and a taxpayer at any stage up to, and including, the audit (i.e. before the audit results in the tax administration issuing an assessment or reassessment for additional income tax payable by the taxpayer or a demand of payment of tax) include disputes in relation to the following matters:

- The taxable income or tax calculated by the taxpayer
- The taxpayer's choice of transfer pricing method used to value transactions between the taxpayer and its associated enterprises
- The availability or computation of deductions, exemptions and credits, including foreign tax credits
- The availability of losses
- The characterization of items of income for tax purposes
- The existence or non-existence of a permanent establishment
- The taxpayer's country of residence

2.1.3 Benefits of avoiding disputes

7. Countries should consider adopting a range of dispute avoidance mechanisms discussed in this chapter as there are many material benefits of avoiding disputes for the tax administrations and the taxpayers.

8. From the taxpayers' perspective, an effective dispute avoidance mechanism will provide the taxpayers with transparency, certainty and a greater understanding of their rights and obligations under the tax law which, in turn, will enable them to make informed decisions about their tax affairs. Such mechanisms will also result in compliance cost savings for the taxpayers. By avoiding disputes with tax administrations, taxpayers will avoid the unnecessary costs and delays associated with disputes proceeding to litigation.

9. From the tax administrations' perspective, the development and implementation of effective dispute avoidance mechanisms will enable tax administrations to direct their resources to higher risk taxpayers and areas of the law. Such mechanisms will also provide taxpayers with transparency which will promote trust and confidence in the tax administration and the integrity of the tax system and consequently encourage voluntary compliance. Like taxpayers, tax administrations will save the costs and time associated with disputes proceeding to litigation; both the taxpayers and tax administrations will also avoid the uncertainty as to the outcome of litigation.

2.1.4 Summary of approaches to avoiding disputes

10. While there are considerable differences in the structure and legal form of the different types of dispute avoidance mechanisms that countries have adopted to deal with income tax disputes, these can be included in a few general categories. Some of the mechanisms, such as advance pricing arrangements, are binding on the tax administration. Other mechanisms, such as the provision of guidance and so-called "cooperative compliance", tend to be non-binding in nature but are instead aimed at ensuring that taxpayers have a better understanding of how a tax administration interprets and applies tax law. The common feature of such mechanisms is that they seek to provide taxpayers with a better understanding of how a tax administration will approach a taxpayer's tax affairs with the aim of avoiding disputes.

11. The first approach to dispute avoidance, which is discussed in section 2.3.1, is the provision of guidance and advice by the tax administration. Such advice may be provided directly to a taxpayer or may take the form of a publicly available explanation of how a tax administration interprets relevant tax law. Both approaches seek to ensure that taxpayers better understand how a tax administration will apply the tax law to their particular circumstances. The extent to which such guidance is binding on a tax administration will depend on its nature and the laws of the country concerned.

12. The next group of approaches to dispute avoidance concern the way in which tax administrations may work with taxpayers to arrive at a better understanding of each other's position ahead of taxpayers finalizing their tax position. These include advance agreements/pre-filing agreements (section 2.3.2), which involve a tax administration

agreeing or raising objections to the tax consequences of a transaction or arrangements in advance of a return being submitted, advance pricing arrangements (section 2.3.3), which take a similar approach for transfer pricing, and the relationship between the taxpayer and the tax administration (section 2.3.4) focusing on "cooperative compliance" and "relationship managers", which enable taxpayers to discuss their affairs with the tax administration at regular intervals or prior to a transaction or arrangement to seek certainty of their tax treatment and therefore potentially resolve any issues before a dispute arises.

13. Voluntary cooperation between multinational enterprise groups and the countries in which they operate is discussed in section 2.3.5, which presents the International Compliance Assurance Programme, and section 2.3.6, which describes the joint audit process.

14. Section 2.3.7 discusses the independent review of a statement of an audit position, a mechanism that seeks to resolve differences of view in the course of an audit.

15. The final approach to avoiding disputes, which is described in section 2.3.8, is the use of mediation during the audit stage. Mediation seeks to bring the taxpayer and tax administration together with the aim of setting out their respective positions and identifying potential solutions in an attempt to reach an agreement. The mediator may come from within the tax administration or be entirely independent.

2.2 Creating an environment for avoiding disputes

2.2.1 Clear and accessible legislation and interpretative guidance

16. The first and likely most effective way of preventing tax disputes is to ensure that taxpayers can easily determine their tax rights and obligations under the tax law as envisaged by governments and therefore can easily fulfil their obligations and understand their rights.

17. Specific attention should be given during the legislative process to the question of whether the tax laws can be reasonably understood and implemented by taxpayers. Governments normally have a standard approach to transforming policy into legislation and regulations. This approach addresses the clarity of the legislation, the ability of taxpayers

to meet the requirements, the compliance cost for affected taxpayers and the resources required by the tax administration to implement such legislation. Ideally, as part of the approach, there should be a public consultation process prior to finalizing and enacting the legislation. This would allow stakeholders to provide relevant insights to the legislator on the effectiveness, the ability to implement and the compliance costs of the proposed tax legislation. Moreover, once the legislation and supporting regulations are adopted, it is important that these are published in a way that makes them easily accessible to taxpayers.

18. In order for a public consultation process to be effective, governments may consider conducting the process as follows:

a) By releasing the text of the proposed draft tax laws and any accompanying explanatory memoranda, in preference to making an enunciation of the proposed amendments to the tax laws and/or the underlying principles of such proposed laws. In this context, it could be expected that governments will elaborate on the validity of proposed draft tax laws under multilateral initiatives (such as, recommendations of the United Nations and minimum standards under the G20-OECD BEPS Project) with the country's existing tax, legal and constitutional framework. For instance, the relationship between the anti-avoidance rules and constitutional principles has been highlighted in public consultations of countries planning to introduce tax laws in accordance with several action items of the G20-OECD BEPS Project.[1]

b) By ensuring that the relevant stakeholders have sufficient time to review, consider and provide submissions on the proposed draft tax laws and their potential impact on their interests.

c) Governments interested in broadening the scope of the participation of stakeholders in the legislative process may

1 This approach has been used, for example, by the governments of Australia, Brazil, Canada, Italy, India, the Netherlands, Poland, Singapore, South Africa and the United Kingdom, which have released drafts of proposed tax legislation for public consultation on a range of topics including anti-avoidance rules, transfer pricing documentation requirements, withholding taxes and indirect taxes.

invite experts, taxpayers, individual businesses or business associations to present their views regarding the operation of the draft tax legislation before the legislative branch.

19. Following the public consultation process by the government, but prior to the draft tax legislation becoming law, the government can decide whether to make any amendments to the proposals to take into account any of the stakeholders' views. Where such amendments are made taking into account the stakeholders' views on uncertainty, unnecessary complexity or unintended tax consequences of the proposals, the amended proposals may be released for further consultation before legislation is passed. When the new tax legislation is enacted, this will likely result in the new legislation being more certain, less complex and operating as intended with the effect of preventing, or at least, minimizing the number of disputes between the tax administration and the taxpayers.

20. Even where no amendments are made to the proposed tax legislation as a result of the stakeholders' views, the consultation process has the effect of providing taxpayers with transparency and an opportunity to prepare in advance for the entry into force of the tax legislation.

2.2.2 Putting domestic legislation and administration in an international context

21. In designing domestic legislation, governments will generally be conscious of the interaction of the domestic legislation with the legislation of other countries and with the international obligations which are in place, for example under bilateral tax treaties. Such global awareness is important to prevent double taxation and tax disputes and is relevant to all phases of introducing and administering tax legislation with cross-border implications, for instance by ensuring that the availability of tax treaty benefits is clearly communicated to the relevant taxpayers.

22. As international tax issues, such as transfer pricing, are considered priority audit areas for many tax administrations, the audit function needs to have a level of global awareness that allows it not only to effectively audit compliance with the domestic legislation, but also to assess whether bilateral tax treaties have been interpreted and applied appropriately. Without such global awareness, for example, cross-border BEPS issues might go undetected or adjustments might

be raised which result in double taxation even though relief from double taxation should be available under the relevant tax treaties.

2.2.3 Legal environment

23. Even though governments generally have the best intentions, it is difficult to anticipate all possible fact patterns and issues and therefore to draft legislation that prevents all tax disputes. For this reason, many countries have dispute avoidance mechanisms in place which provide certainty in advance on cases which come up and for which the interpretation of the tax legislation is not necessarily straightforward. Such dispute avoidance mechanisms prevent tax disputes and provide tax certainty.

24. Dispute avoidance, as referred to in this chapter, is part of public (tax) law and hence, is subject to the same procedural and substantive restrictions that apply to other parts of public law. This should be considered in the design and interpretation of tax laws as public law does not allow for the same flexibility as, for example, commercial or civil law.

25. With respect to any agreement or solution with taxpayers related to domestic law and tax treaties, the tax administration should always be compliant with the rule of law and the principles of good administration applicable in its country. Furthermore, a good system of oversight of the arrangements concluded and of checks and balances should be considered to ensure the law is followed and that unfair favouritism is avoided. Such oversight will help provide a framework within which the tax administration will be able to make decisions related to tax disputes without being overly concerned with suspicions of impropriety.

26. An important aspect to consider when designing, implementing and administering tax legislation is that taxpayers should be treated equally before the law. This applies not only to all dispute avoidance mechanisms but also to audits. It does not mean, however, that all taxpayers should be dealt with exactly the same way. Differences in the taxpayers' attributes (e.g. size, sector etc.) may require different approaches in the cooperation between them and the tax administration. Equality before the law requires that any differentiations made between taxpayers are based on the law and are well reasoned without arbitrarily favouring specific taxpayers or groups of taxpayers.

2.2.4 Risk-based approaches

27. As tax administrations get more access to information from country-by-country reports (CbC reports), master and local files and exchange of information with treaty partners, they should be able to develop more sophisticated risk assessments, in particular with the help of new technologies such as artificial intelligence. This will enable them to focus on high-risk sectors and high-risk taxpayers. That, in turn, should lead to a reduction in the number of disputes and may enable tax administrations to resolve disputes with high risk taxpayers in a more effective manner as they will be able to allocate more resources to such cases.

2.3 Approaches to dispute avoidance

2.3.1 Guidance and advice provided by the tax administration

28. An integral part of the self-assessment system is the provision of different forms of guidance and advice by the tax administration to taxpayers in order to assist them with understanding how the tax law applies to their particular circumstances. Such guidance and advice could be effective in preventing disputes from arising. This would occur where the tax administration's guidance and advice is clear, accurate, consistent and accessible to the taxpayers with the result of providing taxpayers transparency, certainty and a greater understanding of their rights and obligations under the tax law enabling them to make informed decisions about their tax affairs.

Guidance

29. A tax administration may provide guidance on how the tax law operates generally. Such guidance is general in nature and simply expressed so as to assist taxpayers and their advisors in understanding and meeting their obligations under the tax laws administered by the tax administration. Guidance can be provided in various forms as shown in Box 1 below, which describes the guidance provided by the Australian Taxation Office.

30. The extent to which guidance is binding on a tax administration depends on the laws of each country.

Box 1: Guidance—Australian Taxation Office

a) Practical compliance guidelines — provide broad administrative guidance, addressing the practical implications of tax laws and outlining the Commissioner's administrative approach.

b) Oral guidance — given by the phone or in person at a shopfront on matters of a general, straightforward or simple nature.

c) Written guidance —

i) The tax administration's website — provides extensive information, general in nature and often simply expressed, to assist taxpayers and their advisors to understand and meet their obligations under the tax laws administered by the Commissioner.

ii) Decision impact statements — set out the Commissioner's view on the implications of a particular court or tribunal decision.

iii) Media releases and speeches — brief announcements of the Commissioner's position on a newsworthy topic.

iv) Consultation — this includes matters under consultation, papers for comment, and how to get involved in consultation.

d) Audio and visual guidance — the tax administration's podcast "Tax inVoice", which enables taxpayers to listen to the latest tax information in order to meet their tax obligations.

e) Taxpayer alerts — warn taxpayers of the Commissioner's concerns about new or emerging high-risk tax arrangements or issues to assist taxpayers with making informed decisions about their tax affairs.

f) Interpretative decisions — is an edited version of a decision the Commissioner has made on an interpretative matter and gives an indication as to how the Commissioner might apply a provision of a law.

g) Law administration practice statements — provide direction to the tax administration staff on approaches to take when performing certain duties involving the tax law administered by the tax administration.

h) Tax administration's website tools and calculators — assist the taxpayer with self-assessing a tax liability or entitlement.

Advice

31. A tax administration may provide advice on a taxpayer's obligations or entitlements under a provision of a tax law, which is generally in the form of a ruling. Generally, a public ruling sets out the tax administration's interpretation of the law. It is a published statement of the tax administration's opinion of how a provision of a tax law applies, or would apply, to taxpayers in relation to a class of schemes or to a class of taxpayers generally, rather than in respect of the specific circumstances of a particular taxpayer. For examples of the different types and forms of advice which could be provided by a tax administration, see Boxes 2 and 3 below, which describe those provided by the Australian Taxation Office and the Kenya Revenue Authority, respectively.

Box 2: Different forms of advice—Australian Taxation Office

a) Public rulings — set out the Commissioner's interpretation of the law and include:
   i) Product rulings — provide certainty to participants on the tax consequences of an arrangement, provided it is carried out as described in the ruling.
   ii) Class rulings — provide certainty to a specific class of participants by explaining how a relevant provision of the tax law applies to them in relation to a particular scheme.
   iii) Law companion rulings — provide clarity and certainty on the Commissioner's interpretation of new legislation.

b) Private rulings — provide certainty on how a tax law applies to a particular taxpayer in relation to a specific scheme or circumstance.

c) Early engagement for advice — this can be requested by the taxpayer for advice on a complex transaction being considered or implemented.

d) Oral rulings — given over the phone, it is the Commissioner's opinion of how a provision of a tax law applies to an individual in their specific circumstances.

e) Administratively binding advice — provided in a limited range of circumstances in relation to certain laws which the Commissioner administers but is unable to provide legally binding advice.

Box 3: Different forms of advice—Kenya Revenue Authority

a) Binding public rulings — set out the Commissioner's interpretation of the law,

   i) A public ruling sets out the Commissioner's opinion on the application of a tax law in the circumstances specified in the ruling.

   ii) The public ruling is binding on the Commissioner until the ruling is withdrawn, it is however not binding on the taxpayer.

b) Binding private rulings — provide certainty on how a tax law applies to a particular taxpayer in relation to a specific transaction entered into or proposed to be entered into.

32. The issue of whether or not advice is binding (legally or administratively) on the tax administration will depend on the laws of each individual country. For example, in Australia, the effect of the advice or ruling being legally or administratively binding on the Commissioner of Taxation (Commissioner), who administers the tax laws, is that where a taxpayer relies on advice that is subsequently found to be incorrect or misleading and results in the taxpayer making a mistake, the law will protect the taxpayer from the imposition of a tax shortfall, interest on the tax shortfall and a false or misleading statement penalty. Where the Commissioner is unable to stand by the administrative

binding advice,[2] the taxpayer who relies on the advice will be liable for any tax that would otherwise be payable under the law (unless a time limit imposed by law precludes the liability). However, the taxpayer will be protected against a false or misleading statement penalty, and if the taxpayer has relied on the advice reasonably and in good faith, against interest on the tax shortfall.[3]

33. Since a ruling that a tax administration of a country issues with respect to cross-border issues only deals with the application of that country's domestic law and its own interpretation of its treaties, it does not address the application of the domestic tax law of other countries that may be relevant with respect to these issues nor the interpretation of the relevant treaties by these other countries. Also, countries that are members of the BEPS Inclusive Framework should be mindful of the obligation to spontaneously exchange information with respect to rulings that could potentially raise BEPS concerns.[4]

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2 This will occur in the following instances:

— there have been legislative changes since the advice was given

— a tribunal or court decision affected the tax administration's interpretation of the law since the advice was given, or

— for other reasons, the advice is no longer considered appropriate (e.g. if the advice has been exploited in an abusive and unintended way).

See Practice Statement Law Administration PS LA 2008/3, *Provision of advice and guidance by the ATO*, paragraph 199.

3 Ibid., para. 203.

4 This obligation relates to taxpayer-specific rulings which are "(i) rulings relating to preferential regimes; (ii) unilateral APAs or other cross-border unilateral rulings in respect of transfer pricing; (iii) cross-border rulings providing for a downward adjustment of taxable profits; (iv) permanent establishment (PE) rulings; (v) related party conduit rulings; and (vi) any other type of ruling agreed by the FHTP *[Forum on Harmful Tax Practices]* that in the absence of spontaneous information exchange gives rise to BEPS concerns". OECD (2015), *Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5—2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/9789264241190-en, accessed on 12 March 2021, p. 46, para. 91. That report also indicates to which countries the relevant information must be exchanged (p. 53, table 5.1).

Development and management, or enhancement of guidance and public advice

34. As the provision of guidance and public advice[5] by the tax administration to taxpayers could be effective in avoiding disputes from arising, tax administrations may wish to develop and manage such guidance and advice or enhance their existing guidance and advice. This could involve the following:

a) Assessing the risk associated with the issue
b) Working with industry and tax professionals to identity topics for future guidance and advice, and to update existing guidance and advice, as required
c) Consulting stakeholders early and frequently throughout the process to obtain their practical assistance with identifying the most important issues and developing the most effective form to address those issues
d) Ensuring that appropriately qualified officials of the tax administration produce the guidance and advice with the right tools to support them
e) Ensuring the guidance and advice is tailored, clear, current and accessible
f) Ensuring the guidance and advice is provided at the time required, in the most appropriate form and via the most effective channel

2.3.2 Advance agreements / Pre-filing agreements

35. As countries seek to provide certainty to taxpayers and reduce their compliance costs, variations on the advance ruling concept have emerged. The goal of these advance rulings is to allow a taxpayer to obtain certainty on an issue by engaging directly with the tax administration in advance of a dispute on a particular issue. This early engagement benefits both the taxpayer and the tax administration by

5 Public advice provided by the tax administration refers to advice which sets out the tax administration's interpretation of how the law applies to taxpayers in general, as opposed to how it applies to a particular taxpayer's circumstances.

allowing for up-front discussions and resolution, thereby obviating the need for protracted discussions on the issue at a later date. Box 4, which describes the Pre-Filing Agreement issued under the Pre-Filing Agreement Programme of the United States Internal Revenue Service (IRS), provides an example of such an advance ruling.

Box 4: Pre-Filing Agreement Program — IRS

In the United States, the IRS offers its corporate taxpayers the opportunity to enter into the Pre-Filing Agreement Program (Program), which oversees the issuance of a Pre-Filing Agreement (PFA). If accepted into this Program, the taxpayer will undergo an examination of a specific issue in advance of the return being filed, with the end goal of obtaining a PFA, a form of closing agreement which binds both the taxpayer and the tax administration.[6]

A critical difference between a PFA and other types of advance rulings is that the PFA will only be provided with respect to a "closed transaction" for which a position has not yet been taken on a return. The PFA does not comment on or provide guidance on a prospective or future transaction. Rather, it provides an opportunity for the taxpayer and the tax administration to discuss an issue and a position in advance of filing, in order to agree on the treatment to be reflected on the return.[7]

Pre-Filing Agreement Process

In order to obtain a PFA, a taxpayer must submit an application to the PFA Program Manager. The application must provide certain basic information including the taxpayer's name and address, as well as a statement of the relevant facts, the issue to be considered and an analysis of the relevant law. Specific guidance on the contents

6 See Revenue Procedure 2016–30.

7 The PFA is akin to the United States Compliance Assurance Programme (CAP) which provides a taxpayer with a "real-time" audit, allowing it to get agreement on its return positions in advance of filing. CAP is a form of cooperative compliance (see section 2.3.4). Where the CAP exam provides certainty on the overall return, the PFA provides certainty on one specific issue.

of the submission is provided in publicly available guidance.[8] The availability of this public guidance is a best practice, as it provides taxpayers with knowledge of the Program, the process and the expectations of the tax administration.

If accepted into the Program, an examiner is assigned to the matter, and an examination of the issue is commenced. The same procedures for gathering information which are used during an examination, apply during the PFA process.

The taxpayer and the tax administration then enter into a discussion of the technical issue and work to reach an agreement on the position to be taken on the tax return. This agreement is memorialized in a PFA.

Pre-Filing Agreement

The PFA is a form of closing document which legally binds both the taxpayer and the IRS to the terms of the agreement. Once executed, the PFA cannot be re-opened absent a showing of fraud, malfeasance or other bad faith act. Because of the binding nature of the PFA, it is important that both parties to the agreement carefully review the terms and agreement clauses.

In the United States, it is customary for the taxpayer to provide the first draft of the PFA, which is then reviewed and revised in collaboration with the tax administration. Generally, the legal division at the IRS will become involved in the drafting and revision process, as the PFA is binding.

Benefits

The PFA provides an excellent tool for taxpayers and tax administrations to achieve certainty in advance of a return being filed. The benefit of certainty to both the taxpayer and the tax administration is clear: by addressing and agreeing issues in advance of filing, the need for post-filing activity is eliminated. Thus, both the taxpayer and the tax administration conserve resources and time.

8 See Revenue Procedure 2016–30.

2.3.3 Advance pricing arrangements

Background

36. An advance pricing arrangement (APA) is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables, appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time. This could be an effective tool in avoiding disputes,[9] especially since a large part of MAP cases relate to transfer pricing.[10]

37. An APA is formally initiated by a taxpayer and requires negotiations between the taxpayer, one or more associated enterprises, and one or more tax administrations. An APA can be concluded unilaterally, bilaterally or multilaterally (a bilateral or multilateral APA may help avoid future disputes between tax administrations). Questions of transfer pricing can occur on different levels. First, they can be discussed between a taxpayer and the tax administration of the country of residence. Secondly, as they arise in cross-border transactions, they can be a matter between the tax administrations of different jurisdictions.

38. The legal basis for unilateral APAs can be found in the respective domestic tax law, either in legislation on transfer pricing, in specific legislation or in general procedural rules. The legal basis for bilateral or multilateral APAs can be found in international treaties such as bilateral tax treaties. Usually, provisions implementing Article 25 (Mutual agreement procedure) of the United Nations and OECD models serve as a basis for bilateral APAs. While some countries consider that such international treaty provisions are a sufficient basis for a bilateral or multilateral APA, other countries require more specific

9 See section C.4.4.2.2. ("Advance pricing agreements") of the *United Nations Practical Manual on Transfer Pricing for Developing Countries* (*2017)*, available at https://www.un.org/development/desa/financing/sites/www.un.org.development.desa.financing/files/2020-03/Manual-TP-2017.pdf, accessed on 12 March 2021.

10 As indicated in Chapter 4 (para. 23), transfer pricing cases and cases related to the attribution of profits to permanent establishments represented 54 per cent of outstanding MAP cases reported under the MAP statistics for 2019.

domestic legislation and international provisions for the conclusion of such an arrangement. As explained in Chapter 4, one of the elements of the BEPS Action 14 minimum standard requires that "countries with bilateral APA programmes should provide for the roll-back of APAs in appropriate cases, subject to the applicable time limits (such as statutes of limitation for assessment) where the relevant facts and circumstances in the earlier tax years are the same and subject to the verification of these facts and circumstances on audit."[11] Also, according to one of the best practices included in the final report on Action 14 "countries should implement bilateral APA programmes".[12] The explanations included in the report add that this should be done by countries "as soon as they have the capacity to do so."[13] An APA, as defined and used by the United Nations and OECD, is based on the arm's length principle (ALP).[14]

39. An APA is an individual arrangement between its signatories. Therefore, standardized templates are usually not available. Some key elements of APAs include: i) the parties to the agreement, ii) methodology, iii) comparability analysis, iv) critical assumptions;[15] and v) duration / termination of the APA.

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11 See element 2.7 of the minimum standard in the Annex to Chapter 4.

12 See best practice 4 in the Annex to Chapter 4.

13 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14–2015 Final Report*, chap. 1, footnote 10, at p. 30, para. 48.

14 The ALP is incorporated in Article 9(1) of both the United Nations and OECD models, according to which "Where … conditions are made or imposed between … two [associated] enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly."

15 Critical assumptions are a core element of an APA since they reflect the factual assumptions under which the applied method is considered to be appropriate. Generally, an APA applies only if the critical assumptions are met.

Establishing an APA programme

40. Sustainable and enduring commitments are needed to achieve the goals of an APA programme, which include avoiding future conflicts and offering an attractive governance environment.

41. The following elements should be considered by a country wishing to establish an APA programme:

a) Employees with specific skills. In particular, employees should have knowledge of, and experience in, tax law, transfer pricing and domestic procedural law. In addition, communication and organizational skills are important.

b) The personnel running an APA programme need access to certain resources, many of which are similar to those used by transfer pricing auditors. Most importantly, this will likely mean access to commercial databases to allow a comparability analysis. In addition, bilateral and multilateral APAs will necessitate face-to-face meetings between representatives of the tax administrations and this will mean travel and subsistence costs. In some countries, like Canada, the taxpayers that request an APA meet the travel expenses of the tax officials during APA negotiations.

c) The following may address obstacles to the broader use of APAs: (i) target time frames for each stage; (ii) more targeted documentation/ information; (iii) increased tax administration resources; (iv) focus on multilateral APAs, and (v) greater use of benchmarks / safe harbours.[16]

d) There should be consideration of any collateral issues, such as a roll-back of the APA result to income years prior to those covered by the proposed APA (see above), and an agreement with the taxpayer on the approach to resolve those issues.

e) As developing countries gain more experience with unilateral APAs, which provide them with tax certainty, they may

16 As suggested during a presentation on "Advance Pricing Arrangements" at the Forum on Tax Administration Tax Certainty Day held on 16 September 2019 at the OECD Conference Centre (available at https://www.oecd.org/tax/forum-on-tax-administration/events/presentations-tax-certainty-day-2019.pdf, accessed on 12 March 2021, slide 9).

wish to explore the option of bilateral APAs, and eventually multilateral APAs, to the extent that their treaty network makes it possible.

Funding of an APA programme

42. Alternative sources for funding an APA programme can be considered by tax administrations wishing to establish such a programme. Usually the expenses of an APA programme are met from that tax administration's budget. However, some countries charge a fee to taxpayers making use of the programme, which may be particularly attractive for developing countries. Such fees may be structured in different ways: they may involve fixed, hourly or graduated fees, or they may be revenue neutral.

Brief description of a developing country's APA programme

43. Box 5, which describes Indonesia's APA programme, illustrates the APA programme of a developing country.

Box 5: Indonesia's APA programme

Indonesia reported that it has introduced an APA programme in 2010, under which it is allowed to enter into unilateral and bilateral APAs. The legal basis of this programme is *[Article 18(3)a) and]*Article 32A of Law No. 7 of 1983 concerning Income Tax Law as amended by Law No. 36 of 2008 and the MAP provision of the relevant tax treaty. Article 32A stipulates that Indonesia's competent authority is authorised to enter into agreements with treaty partners to determine the transfer price between associated enterprises. The authority competent to handle APA cases is, pursuant to Article 58(1) of Regulation No. 74 (2011), the Director General of Taxes of the Ministry of Finance.

Article 58 of the Government Regulation No. 74/2011 concerning Taxation Rights and Obligations Fulfilment Procedure also includes rules relating to Indonesia's APA programme. This provision, for example, stipulates that an APA shall bind the tax administration and the taxpayer during the period the APA applies and that the tax administration cannot make adjustments on matters already agreed in the APA.

Further to the above, Indonesia issued Regulation No. 7/ PMK.03/2015 of 12 January 2015. Article 2(2) of this regulation prescribes that taxpayers may submit an APA application, provided that they have operated business activities in Indonesia for at least three years. As to the period that can be covered by an APA, Article 4 stipulates that this is for a maximum of three fiscal years in case of a unilateral APA and a maximum of four fiscal years in case of a bilateral APA. Furthermore, this regulation contains information on Indonesia's APA programme and how it runs that programme in practice. In particular this concerns information on: (i) which government authority is competent for handling APA requests, (ii) what an APA is and what the requirements for obtaining an APA are, (iii) by whom they can be requested, (iv) what steps have to be followed in the process, (v) a detailed list of information to be included in an APA request, (vi) time limits for the submission of an APA request, (vii) the implementation of an APA and (viii) the possibility to renew an APA.

Further to the above, Indonesia also includes information on its APA programme on the website of the Ministry of Finance. This website reproduces the information included in Regulation No. 7/ PMK.03/2015. It is there stated that the information contained on the website should be read in conjunction with Regulation No. 7/ PMK.03/2015.

With regard to the timing of the submission of APA requests, Articles 6 and 7 of the APA regulation requires taxpayers to submit a written pre-lodgement request to start the process, whereby such a request should be filed no later than six months before the beginning of the fiscal year covered by the APA.

Source: OECD (2019), *Making Dispute Resolution More Effective — MAP Peer Review Report, Indonesia (Stage 1): Inclusive Framework on BEPS: Action 14*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/deb42398-en, pp. 19–20 / paras. 10 – 14, accessed on 12 March 2021.

2.3.4 Relationship between the taxpayer and the tax administration

2.3.4.1 Cooperative compliance

Overview

44. Cooperative compliance is one way in which tax administrations can develop an overall compliance strategy that encourages greater transparency and voluntary compliance by MNE groups, and in the process, obtain a greater understanding of how MNE groups operate, make decisions and manage their tax exposure. This approach could have the effect of avoiding disputes from arising between the tax administrations and the taxpayers.

45. Cooperative compliance refers to a concept that builds on a reciprocal relationship of trust and cooperation between the tax administrations and the taxpayers. It is a relationship that favours collaboration over confrontation and is anchored more on mutual trust than on enforceable obligations, with both parties going beyond their statutory obligations by, for example, providing more information.

46. Cooperative compliance can also assist countries to create a tax compliance climate that provides an environment which is more conducive to business.

Relevance of cooperative compliance to developing countries

47. The cooperative compliance model has a number of characteristics that suggest it could play a positive role in the strategic response of developing countries to improve tax compliance by taxpayers and prevent or minimise tax disputes between the tax administrations and the taxpayers.

48. Under a cooperative compliance approach, the tax administration may engage early with the taxpayer to discuss the tax consequences of a proposed transaction or arrangement. Where this occurs, the parties will be able to identify if they have any differences of opinion on the tax issues and therefore potentially resolve those tax issues before the taxpayer undertakes the transaction or arrangement, or files its position. Where the tax administration and taxpayer identify and

resolve their tax issues prior to the taxpayer undertaking the transaction or arrangement, or the filing of its position, the cooperative compliance approach will have had the effect of preventing disputes from arising.

49. Cooperative compliance assists with building the capabilities of tax administrations by improving commercial awareness and familiarising MNEs with the concerns of the tax administrations. The introduction of cooperative compliance could improve the tax administrations' understanding of how business is conducted. Tax administrations that have already segmented their taxpayer population by size and economic sector may find it easier to implement the model, as they have already recognized the differentiating qualities of large taxpayers and specific industries.[17]

50. Cooperative compliance also improves tax transparency as a result of the greater openness and responsiveness expected of both the tax administration and the MNE group. In some developing countries a lack of transparency has had a corrosive effect on the relationship between government and taxpayer businesses, and in the worst case, has facilitated corruption and other dysfunctions.[18] As a result, cooperative compliance may play a role in improving the legitimacy of the whole tax system by contributing to tax compliance and assisting with eliminating corruption. The concept of cooperative compliance enshrines a set of principles that ensure that the officials of the tax administration dealing with taxpayers' affairs will adhere to the principles that underpin a transparent relationship.

51. The implementation of cooperative compliance should also result in the better management of resources by the tax administration so that it can focus on those taxpayers that engage in aggressive tax

17 IMF Policy Papers, *Current Challenges in Revenue Mobilization: Improving Tax Compliance,* 2015, p. 16, available at https://www.imf.org/-/media/Websites/IMF/imported-full-text-pdf/external/np/pp/eng/2015/_020215a.ashx, accessed on 12 March 2021.

18 Ivar Kolstad, Arne Wiig, and David Aled Williams, *Tackling Corruption in Oil Rich Countries: The Role of Transparency*, Chr. Michelsen Institute, U4 Brief 2008:3, available at https://www.cmi.no/publications/file/2938-tackling-corruption-in-oil-rich-countries.pdf, accessed on 12 March 2021.

planning facilitated by non-disclosure, which is particularly important for developing countries that struggle with limited resources and capabilities. From the perspective of taxpayers, it should result in greater proportionality of actions undertaken by the tax administration.

Tax control framework at the heart of trust

52. An essential feature of the cooperative compliance model is the tax control framework (TCF) within an MNE group. This is understood as "*the part of the system of internal control that assures the accuracy and completeness of the tax returns and disclosures made by an enterprise*."[19] It gives legitimacy to the cooperative compliance programme by providing a clear and objective basis on which the tax administration can base its decision to trust the statements made by the taxpayer. Box 6 gives an overview of the features of the TCF.

Box 6: Features of the TCF as used by MNE groups

The TCF typically includes the following features:

— **Tax strategy**: this should set out the strategic objectives of the business, the role of the tax administration, and its approach to ensuring compliance with the law. It should address all aspects of the business at all levels, from the strategic to the operational. In particular, it should set out the business' attitude to, and appetite for, tax risk. The strategy should be owned at the level of the Board of directors (Board).

— **Comprehensiveness**: the TCF should cover all policies, procedures and processes that can affect the correct assessment and reporting of tax liabilities.

— **Responsibility**: the TCF should be developed by the senior management and approved by the Chief Financial Officer or the Board. It should provide that any tax strategy is executed by a sufficient number of people with the right skills and experience.

19 OECD (2013), *Cooperative Compliance: A Framework: From Enhanced Relationship to Cooperative Compliance*, OECD Publishing, http://dx.doi.org/10.1787/9789264200852-en, p 58, accessed on 12 March 2021.

— **Governance**: the TCF should describe the mechanisms, processes and relations by which tax issues are controlled and directed. The prime responsibility for ensuring the system works according to the declaration provided in the TCF should lie with the Board.

— **Testing**: this feature of the TCF refers to its maintenance and monitoring. The system should contain feedback tools which aim at preventing, detecting and correcting errors. Regular testing of the TCF should make it possible to assess whether the system is adequate. The TCF should be dynamic, so that it responds to changes in the underlying business and issues that have arisen from the regular testing of the integrity of the control regime.

— **Assurance**: is provided when all the other features of the TCF are fully implemented. That is what provides assurance to all stakeholders, including the tax administration, that the taxpayer has an effective system which enables it to control all tax risks and issue reliable tax outputs.

53. A TCF that has all the above features delivers the justified trust that is central to the cooperative compliance model. It enables the tax administration to focus on assuring the integrity of the control processes of the MNE groups, rather than trying to routinely undertake its own verification of the way in which individual transactions have been recorded in taxpayers' accounting systems.

Developing countries have different options in designing a legal framework for cooperative compliance

54. Although the developing countries' legal systems differ, there are some fundamental principles common to most jurisdictions where the rule of law applies.[20] The rule of law requires that "all persons

20 See the Statement of the United Nations Secretary-General Ban Ki-moon, *Fundamental Principle of Rule of Law 'Our Best Hope for Building Peaceful, Prosperous Societies'*, SG/SM/13505-GA/11070-L/3171, 11 April 2011, available at http://www.un.org/press/en/2011/sgsm13505.doc.htm (accessed on 12 March 2021).

and authorities within the State, whether public or private, should be bound by and entitled to the benefits of laws publicly and prospectively promulgated and publicly administered in the courts."[21] This concept of the rule of law implies some limitations imposed on governments and their actions. Among these, two principles feature prominently: the principles of legal equality[22] and legal certainty.[23]

55. In respect of the principle of legal equality, there may be some concerns that cooperative compliance violates this principle, because the model is designed only for a select group of the largest taxpayers.[24] However, upon a closer look at the cooperative compliance model, it shows that it relates to taxpayers who are in a different circumstances than the majority of taxpayers due to the size and complexity of their tax affairs. It is often the case that larger taxpayers are subject to additional tax reporting and compliance obligations, transfer pricing documentation being a good example. Moreover, the model and its benefits are justified as an integral part of a risk-based approach to managing tax compliance. Some questions could also be raised about programmes that grant benefits above and beyond the greater tax certainty and reduced compliance costs associated with cooperative compliance. Nevertheless, even in these cases, these programmes should be justified by reference to the taxpayer's improved tax compliance and overall improvements to tax compliance risk management.

21 Lord Bingham, "The Rule of Law", *Cambridge Law Journal*, Vol. 66, No. 1, Mar. 2007, pp. 67–85, p. 69.

22 Hans Gribnau ed., "Introduction", in *Legal Protection Against Discriminatory Tax Legislation: The Struggle for Equality in European Tax Law*, Kluwer Law International, the Netherlands, 2003, p. 1.

23 Hans Gribnau, "Equality, Legal Certainty and Tax Legislation in the Netherlands — Fundamental Legal Principles as Checks on Legislative Power: A Case Study", *Utrecht Law Review*, Vol. 9, No. 2, March 2013, pp. 52–74, p. 53.

24 OECD (2013), *Cooperative Compliance: A Framework: From Enhanced Relationship to Cooperative Compliance*, OECD Publishing, http// dx.doi.org/10.1787/9789264200852-en, accessed on 12 March 2021, pp. 45 – 48.

Potential benefits of cooperative compliance programmes[25]

56. It has been argued from the perspective of governments that cooperative compliance programmes could have the following benefits:

— **Improve tax compliance:** Cooperative compliance facilitates compliance by providing timely advice on tax issues. It affects the behaviour of a broad group of taxpayers for whom avoidance of tax disputes is a tangible benefit of the programme.

— **Secure revenue base:** As a result of improved tax compliance, in the long term the revenues paid voluntarily will increase. In the short term, settlement of legacy issues, which is a first step in establishing the new relationship, may deliver an immediate yield.

— **Improve compliance risk management:** As part of a risk-based compliance strategy, cooperative compliance assists the tax administration with allocating resources to focus on high risk taxpayers.

— **Save resources by reducing the scope of audits:** As a result of transparency and full disclosure, the tax administration may get a better understanding of current issues impacting the taxpayer, and therefore may be able to reduce the scope of audits.

— **Improve capabilities:** With cooperative compliance the tax administration may improve its commercial awareness, develop a better understanding of how MNE groups manage their business including their control systems which ensure that their accounts and returns are accurate.

57. It has been argued from the perspective of taxpayer businesses that cooperative compliance programmes could have the following benefits:

— **Avoid or minimise tax disputes:** Cooperative compliance provides a platform for discussing any tax issues with the tax administration and can substantially reduce the risk of dispute.

25 See OECD (2014), *Measures of Tax Compliance Outcomes: A Practical Guide,* OECD Publishing, http//dx.doi.org/10.1787/9789264223233-en, accessed on 12 March 2021.

— **Better and easier tax risk management:** Tax issues are better integrated in the taxpayer's processes and are underpinned by a TCF.

— **Lower compliance costs:** The taxpayer is less exposed to administrative penalties, can file and settle tax returns quicker, and may require less assistance from tax intermediaries (such as lawyers, accountants and other tax professionals). Also, the number of disputes that involve extra costs should be lower.

— **Corporate social responsibility:** Taxpayers may benefit from reputational gains. The MNE group's stakeholders will perceive the enterprise as more reliable and a good corporate citizen. Shareholders and institutional investors will have greater confidence in the returns from investments.

— **Better investment climate:** An improved relationship between large taxpayers and the tax administration will encourage foreign direct investment as MNE groups can achieve certainty about the tax treatment of their investments.

Developing countries taking the first steps towards cooperative compliance programmes

58. Although to date cooperative compliance programmes have been mainly deployed in developed countries, a number of emerging and developing countries (e.g. Chile, Ghana, Malaysia, Nigeria, South Africa and Zambia) are exploring this concept.[26] Box 7 describes Brazil's experience in taking the first steps towards a cooperative compliance programme.

Box 7: Tax Compliance Incentive Programme (Pro-Conformity)—Brazil

In 2018, the Secretariat of the Brazilian Federal Revenue (RFB) initiated a public consultation on a draft ordinance establishing the Tax Compliance Incentive Programme (Pro-Conformity). The proposal was inspired by good practices adopted by other tax

26 See Global Tax Policy Center, Institute for Austrian and International Tax Law, WU (Vienna University of Economics and Business), *Cooperative Compliance Pilot Programmes*, accessed on 12 March 2021.

administrations, following a globally recognized model of favouring tax compliance practices. This draft ordinance has received several suggestions from different sectors in Brazil.

The RFB's objective is to create more favourable conditions for taxpayers who have a good relationship with the tax administration, facilitating the fulfilment of their obligations and providing them with efficient and agile service when they request it. The compliant taxpayer will have priority in his demands (for example, tax refunds) and will be previously notified of pending matters for the purpose of self-regulation.

As a previous step to the implementation of the programme, the RFB will assess the eligibility of taxpayers taking into account the following four criteria:

1. Registration status compatible with the company's activities
2. Adherence to information provided to the RFB through declarations and bookkeeping
3. Timeliness in the presentation of declarations and bookkeeping
4. Compliance in the payment of taxes due

Guidelines for setting up pilot studies in countries which wish to establish a cooperative compliance programme

59. Countries which desire to establish a cooperative compliance programme may initially consider setting up a pilot study to test how such a programme can operate within their political, legal and administrative environment. Box 8 sets out some guidance which may assist them.

Box 8: Methods to approach the implementation of a pilot study for a cooperative compliance programme

A written agreement should be a sufficient basis for the necessary cooperation between the tax administration and the taxpayer during the pilot phase although some countries may already at this stage prefer to develop a legal framework. If the pilot programme is successful, the need and case for legislative changes can be considered later.

The pilot should ideally involve taxpayers that are reasonably representative of the type of taxpayer that is likely to participate in a full-fledged programme and which have shown by their past behaviour that they are willing to be transparent.

Large business taxpayers in developing countries are often subsidiaries with the parent company located offshore. Therefore, it is important that the group as a whole is committed to participating in the pilot. Timely access to relevant data held in the foreign headquarters and to key decision makers should be an essential part of the disclosure that is expected from the taxpayer.

Both the taxpayer and the tax administration should recognize the central importance of the TCF (see Box 6).

Agreement on evaluation measures constitutes an important aspect of the pilot programme design. The pilot programme should be evaluated from the perspective of the tax administration, taxpayers and also the wider community. Possible measures of success could include: improved trust in the tax administration, greater speed of exchange of information, cordial interactions and increased collection of taxes. Agreement on a set of indicators evaluating the programme requires certain data to be in place. Indicators, quantitative and qualitative, should be based on information that is accessible to tax administrations. It will be important to establish a baseline of current performance against which progress can be measured as the pilot programme unfolds.

2.3.4.2 Relationship managers[27]

60. The appointment of a single point of contact, or relationship manager, between the tax administration and the taxpayer, who is

27 This section discusses the relationship manager whether or not that relationship manager is part of a cooperative compliance programme between the taxpayer and the tax administration, as described above in section 2.3.4.1.

responsible for the tax administration's overall relationship with the taxpayer, could have the effect of preventing disputes arising.[28] This approach may be particularly helpful to large taxpayers and high-net-worth individuals.

61. Under such an approach, there is an on-going and transparent dialogue between the tax administration and the taxpayer. This may involve structured and planned discussions, such as a formal annual risk assessment, as well as ad hoc discussions of particular issues as they arise. The taxpayer is able to discuss with its relationship manager a proposed transaction or arrangement and an analysis of the tax consequences either at the annual review or at a time when the taxpayer is seeking certainty of its tax treatment. The tax administration will then comment on those consequences. The relationship manager does not comment on those consequences independently of the tax administration. Any difference of opinion can be discussed, and therefore potentially resolved, including by a tax ruling if possible and if required, before the taxpayer goes ahead with the transaction or before the taxpayer is required to file its position for the relevant period. One of the aims of this approach is therefore to resolve any issues before a dispute arises.

62. The development of a relationship between the tax administration and the taxpayer fosters greater trust and transparency if the arrangements are approached in the right way. This relationship works to the benefit of both parties. Where the taxpayer and the tax administration reach an agreement on the tax treatment of a proposed transaction or arrangement, the taxpayer will be certain of the tax treatment of that transaction or arrangement before it reaches its filing position, which therefore prevents a dispute from arising. However, where no such agreement is reached, the taxpayer obtains an understanding of the tax administration's position, including the likelihood that its filing position will result in a dispute arising.

63. From the tax administration's perspective, the development of such a relationship with the taxpayer will result in a deeper understanding of the taxpayer's business model and operating environment and of how these, and other commercial factors, impact upon the tax position of the taxpayer. This will inform an understanding of the

28 This approach is taken, for example, in the United Kingdom, Belgium, Australia and Ireland.

particular needs of the taxpayer and how it behaves, including by reference to its approach to tax compliance. This can be an effective way of avoiding disputes based on an understanding of the motivations for particular arrangements. It also allows a tax administration to identify tax risks at an early stage and therefore, potentially, allow resolution of any issues before they result in a dispute.

64. Box 9 describes the Client Relationship Manager Programme provided by the Tax Administration Jamaica.

Box 9: Client Relationship Manager Programme - Tax Administration Jamaica

The Large Taxpayer Office

Tax Administration Jamaica (TAJ) opened the Large Taxpayer Office (LTO) in April 2009. The LTO was established in keeping with a commitment of the Government of Jamaica to provide service of the highest quality, accessibility, convenience and responsiveness to the taxpayers or clients who contributed a significant portion of the country's revenue. The LTO enables tax administrators via their Client Relationship Managers (CRMs) to interface with, and meet the needs of, the clients in a more proactive and systematic manner in order to improve service delivery and foster greater compliance, and therefore may be effective in preventing disputes from arising.

Clients

The LTO facilitates taxpayers who have total sales or turnover of over $500 million Jamaican dollars (approximately $3.7 million USD), or contribute tax revenues in excess of $50 million per annum for any of the following taxes: Corporate Income Tax, Pay-As-You-Earn, General Consumption Tax and Stamp Duty.

These taxpayers comprise 3 per cent of the tax paying population and contribute 80 per cent of tax revenue. Typically, these clients are highly sophisticated in their operations and are usually involved in complex domestic and international commercial transactions.

Client Relationship Management

Client Relationship Management involves understanding the client, understanding the objectives of the TAJ and continuously improving service quality. Where this is satisfactorily done, the outcome should be the maintenance of a nurturing environment where the clients feel that their needs are met.

The Client Relationship Management functions at the TAJ are carried out by CRMs acting under the supervision of the Director of Client Relationship Management (Director).

Role of the Director

The Director of Client Relationship Management is responsible for planning, organizing, directing, coordinating and supervising the activities of the CRMs. Among the duties of the Director are the following:

- Ensuring that all CRMs adopt and comply with the policies of the LTO
- Identifying training needs of the CRMs in tax laws and other relevant laws and practices
- Assisting the CRMs with meeting the needs of clients, in particular where there are complex tax issues involved
- Assisting the CRMs with conducting workshops and seminars targeting clients
- Establishing protocols between the CRMs and other units internal to TAJ, as well as other external stakeholders such as other government agencies and the various private sector bodies
- Conducting periodic reviews of strategies and protocols
- Ensuring that CRMs have ongoing training

Role of the CRM

The CRM is the main contact point between the client and TAJ and provides personalized service to the client. This requires that the CRM have a good understanding of the business environment and a working knowledge of the client's modus operandi.

Professionally, CRMs are required to possess at least a first degree in accounting, ACCA level 2, or other equivalent professional qualifications from a recognized university. They are also required to have at least a four-year work experience and must display a knowledge of tax laws and skills in communication of complex technical issues.

The duties and functions of the CRMs cover two broad areas: managing the interface between TAJ and the client, and research and dissemination of information.

1. Managing the interface between TAJ and the client in order to prevent or minimize disputes and avoid misunderstandings. This function includes the following activities:
   - Establishing and maintaining protocols for the relationship between TAJ and the client
   - Consulting on complex tax issues with in-house legal and technical staff in order to reach consensus on the response from TAJ to the client's concerns
   - Facilitating the flow of documents and payments between the client and TAJ
   - Facilitating the refund process as well as the timely issuance of documents such as the Tax Compliance Certificate
   - Ensuring that accounts of clients are reconciled and updated and that clients receive timely updates on accounts
   - Facilitating electronic transactions and direct bank payments
   - Ensuring timely and professional responses to complaints, questions and requests of clients by keeping them informed on the progress of queries and the timeline for resolution of issues
   - Making courtesy calls on clients
2. Conducting research and dissemination of information. This function includes the following activities:
   - Conducting ongoing research in order to appreciate the nature, characteristics and operations of the business of the assigned client

- — Consulting with industry specialists to ensure full understanding of the complexities associated with the client's industry
- — Conducting seminars and workshops aimed at informing clients about changes to domestic and international tax matters, as well as soliciting feedback from clients
- — Liaising with legal and other technical staff members who assist with presentations at the various workshops and seminars
- — Tracking, maintaining and analysing statistical data associated with the business of the assigned client

2.3.5 International Compliance Assurance Programme

65. The International Compliance Assurance Programme (ICAP)[29] provides for a multilateral approach to early tax certainty for eligible MNE groups, which could have the effect of preventing disputes from arising between those MNE groups and the tax administrations.

66. ICAP is a voluntary programme for a multilateral cooperative risk assessment and assurance process. It was launched in January 2018 as a pilot programme with only eight participating countries and five MNE groups. Based on feedback received from the initial pilot programme, ICAP 2.0 (the second iteration of the programme) was announced in March 2019 and there were 19 participating countries. Following the two pilots, ICAP is now being run as a full programme open to all FTA member tax administrations. In February 2021, the FTA released a handbook on ICAP containing information on the ICAP process reflecting the experience and feedback of the tax administrations and the MNE groups that participated in the two pilots.[30] ICAP is designed to be an efficient, effective and co-ordinated approach to provide MNE groups which are willing to engage actively, openly and

29 https://www.oecd.org/tax/forum-on-tax-administration/international-compliance-assurance-programme.htm, accessed on 12 March 2021.

30 Forum on Tax Administration, *International Compliance Assurance Programme — Handbook for Tax Administrations and MNE Groups*, chap. 1, footnote 19.

in a fully transparent manner with increased tax certainty with respect to certain of their activities and transactions. ICAP does not provide an MNE group with the legal certainty of other approaches such as, for example, an APA. It does, however, give comfort and assurance to the MNE group where the participating tax administrations undertaking the MNE group's risk assessment consider an issue covered represents no or a low tax risk. In this case, the participating tax administrations will each issue an assurance letter setting out these findings, the form of which will vary by jurisdiction. Where an area is identified as requiring further attention, work conducted in ICAP can improve the efficiency of actions taken outside the programme, if needed.

67. As ICAP is still in its infancy, there is a limited track record to provide guidance to countries considering participation in the programme. Moreover, participation in ICAP is extremely resource intensive for both the tax administrations and the MNE groups.

2.3.6 Joint audits

68. In 2010, the FTA introduced "joint audits" as a new form of coordinated action by tax administrations.[31] Joint audits are described as follows:[32]

> two or more countries joining together to form a single audit team to examine an issue(s) / transaction(s) of one or more related taxable persons (both legal entities and individuals) with cross-border business activities, perhaps including cross-border transactions involving related affiliated companies organized in the participating countries, and in which the countries have a common or complementary interest; where the taxpayer jointly makes presentations and shares information with the countries, and the team includes Competent Authority representatives from each country.

69. Joint audits can be relevant when countries have a common or complementary interest in the fiscal affairs of one or more related taxpayers. Given the overall expense associated with joint audits, this is an approach that may be more appropriate for large and complex cases

31 Forum on Tax Administration, *Joint Audit Report*, OECD, 2010, available at https://www.oecd.org/tax/administration/45988932.pdf, accessed on 12 March 2021.

32 Ibid., p. 7, para. 7.

and, from the perspective of developing countries, where they have the capacity to engage in these complex audits. They can also be most useful when a domestic audit does not allow the auditor to obtain a complete picture of a taxpayer's tax liability in relation to some portion of its operations or to a specific transaction. Transfer pricing audits are one example of audits where the information available in the jurisdiction does not always show the full picture.

70. Joint audits are distinguishable from the conduct of simultaneous tax examinations. A simultaneous tax examination is "an arrangement by two or more countries to examine simultaneously and independently, each on its territory, the tax affairs of taxpayers (or a taxpayer) in which they have a common or related interest with a view to exchanging any relevant information which they so obtain."[33] Such examinations "ensure high levels of efficiency regarding the exchange of information between tax administrations and enable a comprehensive review of all relevant business activities".[34] This may assist in averting double taxation and therefore preventing disputes from arising.

71. The term "joint audits" is not a legally defined term. From a practical perspective, most of the joint audits seen so far are audits where two or more tax administrations work together and form a highly integrated team that interacts jointly with the taxpayer. If countries want to carry out a joint audit, they need to determine the legal framework in which they will cooperate.[35] The basis for cooperation can be found in bilateral and multilateral tax treaties and other instruments which provide for varying degrees of mutual assistance. Procedural aspects of the cooperation during the audit (e.g. relating to the physical presence

33 OECD (2006), *Manual on the Implementation of Exchange of Information Provisions for Tax Purposes—Module 5 on Conducting Simultaneous Tax Examinations,* available at http://www.oecd.org/tax/exchange-of-tax-information/36648057.pdf, accessed on 12 March 2021, p. 4, para. 5.

34 Ibid., para. 6.

35 For a discussion of the legal framework for joint audits, see OECD (2019), *Joint Audit 2019—Enhancing Tax Co-operation and Improving Tax Certainty: Forum on Tax Administration*, OECD Publishing, Paris, https://doi.org/10.1787/17bfa30d-en, accessed on 12 March 2021, chap. 4.

and possible exercise of legal authority by officials of another country) are not covered in these instruments and are therefore governed by the domestic law of the participating countries. It is, however, possible for countries to conclude a working agreement that identifies legal issues and determines mitigation strategies. This could be done in the form of a Memorandum of Understanding.

72. Joint audits may provide tax certainty and could therefore be effective in preventing disputes from arising between taxpayers and the tax administrations. This is because joint audits may result in quicker issue resolution, more streamlined fact finding and more effective compliance. Joint audits may also have the potential to shorten examination processes and reduce costs, both for tax administrations and taxpayers.

73. Additional benefits of joint audits include: reducing the taxpayer's burden of having multiple countries conduct audits of similar interests or transactions, enhancing the awareness of tax officers of the opportunities available in dealing with international tax risks, assisting with gaining an understanding of the differences in legislation and procedures, and, if necessary, accelerating the MAP by having the competent authorities involved early on where double taxation is involved and, for all participating countries, by reaching a joint/mutual agreement on the audit results to avoid double taxation.

74. According to the 2019 Joint Audit report,[36] joint audits may be beneficial for developing countries as they assist with building capacity in international taxation matters, including on transfer pricing:

a) Less experienced tax administrations can gain a better understanding of the tools and approaches used in tax audits and case selection in more advanced jurisdictions, including the use of CbC reports and other risk assessment tools.

b) These administrations can also gain from the experience of seasoned auditors in issue spotting and developing the case, through to taxpayer engagement and issue resolution.

c) Joint audits also ensure that there is no information asymmetry between tax administrations as by definition the engagement is joint. This means that representatives of less

36 Ibid., chap. 6.

experienced jurisdictions will not only interface with the local tax function of the taxpayer, but could be present at the tax examination, e.g. at the MNE group's headquarters.

2.3.7 Independent review of the statement of audit position

75. An independent review of the statement of audit position (independent review) is a procedure provided by a tax administration during an audit which could operate as a dispute avoidance mechanism. This would occur where the outcome of the independent review procedure conducted during the audit stage had the effect of preventing a dispute from arising, that is, the audit would not result in the tax administration issuing an assessment or reassessment for additional income tax payable by the taxpayer to which the taxpayer would object.

76. The overall objective of the independent review procedure is to allow eligible taxpayers who disagree with the statement of audit position to request a review of the technical merits of their case by an official of the tax administration who works independently and separately from the audit function, prior to the finalization of the tax administration's audit position. Following such a review, the independent review official will make recommendations, which may or may not be binding, to the taxpayer and the audit team on what the official considers is the better position on those issues. Box 10 describes the independent review procedure provided by the Australian Taxation Office.

Box 10: Independent review of the statement of audit position—Australian Taxation Office

Independent review procedure

Under the independent review procedure, the independent review official will consider the facts, evidence and arguments that have been raised during the audit which are relevant to the issues of disagreement between the taxpayer and the tax administration as identified in the taxpayer's request and facilitate a case conference between the parties to clarify the issues in order to make recommendations on what the official considers is the better position on those issues.

A critical aspect of the independent review procedure is the case conference, which is an informal meeting attended by the taxpayer, the audit team and the independent review official. The purpose of the case conference is for the taxpayer and audit team to meet with the independent review official to discuss and clarify the factual and legal issues of disagreement raised at the audit for the benefit of the review. Although the independent review official will facilitate the case conference, the official will not provide any observations, recommendations or preliminary conclusions during the case conference.

Outcome of independent review procedure

The outcome of the independent review procedure will be in the form of recommendations containing the reasons for the conclusions made by the independent review official to the taxpayer and the audit team on what the official considers is the better position of the issues of disagreement raised in the statement of audit position. In Australia, as the independent reviewer's recommendations are binding, the audit team will complete the audit in line with the recommendations.

If the independent review official agrees with the statement of audit position, the auditors will complete the audit in line with the recommendations which will result in the tax administration issuing an assessment or reassessment for additional income tax payable by the taxpayer. Although the independent review procedure will not prevent a dispute from arising at that stage, the official's recommendations will provide the taxpayer greater clarity and understanding of the initial positions taken in the audit.

In contrast, if the independent review official does not agree with the statement of audit position, the matter will be escalated to the Chief Tax Counsel if it relates to the interpretation of a critical question of law which has broader strategic or policy implications. The Chief Tax Counsel would be the final arbiter of the best view in the circumstances. If the Chief Tax Counsel agrees with the independent reviewer's recommendations, the auditor's initial positions will be altered in line with the independent review. In these circumstances, the outcome of the independent review procedure will prevent a dispute from arising.

However, if the Chief Tax Counsel does not agree with the independent reviewer's recommendations, the outcome of the independent review procedure will not prevent a dispute from arising but it will provide the taxpayer with greater clarity and understanding of the auditor's initial positions.

77. Countries interested in establishing an independent review procedure in their tax administration should consider creating a division that works independently and separately from the audit function. Further, as such a division would be dedicated to facilitating the early resolution of factual and legal issues of disagreements between the taxpayer and the tax administration during the audit stage, it should be staffed with officials having an appropriate level of expertise in substantive tax matters, which will allow these officials to fully and competently perform a review of the initial audit positions.

78. When a tax administration desires to provide such a dispute avoidance mechanism to its taxpayers, it must take into account its financial and human resources, which are often limited. As such, a division dedicated to the resolution of factual and legal disagreements between taxpayers and the tax administration during the audit stage to prevent disputes arising by providing a service like an independent review may have a small number of employees. In such cases, the tax administration may need to limit the number and nature of cases eligible for an independent review. For example, it may be more efficient to provide access to the independent review procedure only for audits of large taxpayers, e.g. those with an annual turnover in excess of an established amount.

2.3.8 Mediation during tax audit

79. Mediation is a form of process-related assistance that involves the use of a mediator or facilitator to assist two parties with the resolution of their potential dispute. This mediation process can be conducted during the audit stage to assist the taxpayer and the tax administration case officers to identify the issues of disagreement and options for resolution and to evaluate those options in an attempt to reach an agreement.

80. This section discusses two different types of mediation processes which can be conducted during the audit stage. The difference between these two types depends primarily on who acts as a mediator. "In-house facilitation" involves an impartial official of the tax administration acting as a facilitator, while the mediator in "independent mediation" is an independent body.

In-house facilitation for individuals and small businesses

81. In-house facilitation is a voluntary mediation process generally provided by a tax administration during the audit stage to individuals or small businesses with less complex issues of disagreement with the tax administration.[37] As this mediation process is provided during the audit stage, where the outcome of the mediation results in the resolution of the issues of disagreement between the taxpayer and the tax administration, it will have the effect of preventing a dispute from arising.

82. The in-house facilitation process involves an impartial official of the tax administration who is professionally trained in facilitative mediation and has no prior knowledge or involvement in the case, acting as a facilitator to assist the taxpayer and the tax administration case officers to identify the issues of disagreement and options for resolution, and to evaluate the options in an attempt to reach a resolution.

83. The in-house facilitation process can be requested by either the taxpayer, its representatives or the tax administration case officers. In some countries (e.g. the United Kingdom), the tax administration has discretion as to whether to accept such a request. Where the request is accepted, the facilitator will contact the parties to provide them with an outline of the process, including what is expected of them. For the in-house facilitation process to be effective as a dispute avoidance mechanism, the taxpayer should prepare for the facilitation meeting, including by ensuring that all relevant persons will be participating or

37 This mediation process can be provided at any stage from the audit up to, and including, the litigation stage. Where it is provided after the conclusion of the audit which results in the tax administration issuing an assessment or reassessment for additional income tax payable by the taxpayer, it corresponds to the dispute resolution mechanism described as administrative mediation discussed in chap. 3, section 3.4.2.

be directly accessible and that these persons are authorized to discuss and resolve the issues of disagreement.

84. The facilitator will commence the facilitation meeting by outlining the meeting structure and the mutual expectations of the parties. The facilitator will invite the parties to present their view of the facts and issues of the case before assisting them to identify the issues of disagreement and the options for resolution, and to evaluate these options with a view to reaching a resolution. The role of the facilitator is not to establish facts, give advice or decide which party is right or wrong, but to guide the discussion with a view to resolving the issues of disagreement or at least make progress towards such a resolution.

85. An important aspect of this process is that any information that is shared during the process, including any admission by, or new evidence obtained from, a participant, is confidential between the participants, the facilitator and any other people specifically involved in the process, such as lawyers or expert advisors. Such information is only to be used for this process, unless disclosure is required by law or authorised by the disclosing party.

86. For the in-house facilitation process to be effective, it is imperative that the parties participate in good faith, are respectful of the other participants and the facilitator, are open and transparent in providing information relevant to the case and are willing to negotiate and attempt to resolve all aspects of their disagreement.

87. Where the outcome of the in-house facilitation process during the audit stage does not result in the resolution of the issues of disagreement between the taxpayer and the tax administration, the parties will have obtained the benefit of a greater understanding of their issues of disagreement with a clearer path of the dispute going forward. In contrast, where the outcome of the in-house facilitation process during the audit stage results in the resolution of the issues of disagreement between the taxpayer and the tax administration, it will have the effect of preventing a dispute from arising.

Independent mediation

88. Independent mediation during tax audits could be effective as a dispute avoidance mechanism as it may eliminate or minimize the

possibility of the audit resulting in the tax administration issuing an assessment or reassessment for additional income tax payable by the taxpayer.

89. The main difference between in-house facilitation (or administrative mediation) and independent mediation is that the mediator in an independent mediation is an independent body rather than an impartial official of the tax administration. Box 11 describes the main features of the independent mediation procedure in Mexico.

Box 11: Main features of independent mediation procedure in Mexico

Independent mediation

Independent mediation allows the consideration of the findings of a tax audit before that audit has been formally finalized. The mediation may cover issues of interpretation of legislation and a review of the findings of facts and associated evidence.

Independent mediator

The mediator is an independent body and has knowledge and expertise in tax matters. In Mexico, PRODECON[38] acts as an independent mediator. It is an independent public body which according to the law is recognized as an expert in tax matters with the necessary knowledge to conduct the procedure effectively, therefore creating an optimal environment for the parties to reach an agreement.

Also, if no agreement is reached, the parties understand that PRODECON will not be part of any future litigation. This promotes

38 In Mexico, the protection of the taxpayers' rights is entrusted to PRODECON, a public body created by the Federal Congress which is independent from the tax collection body even though it is part of the Federal Administration. PRODECON has an autonomous budget which allows it to act without any pressure. This body, known as the *tax ombudsman,* started operating in 2011. Since 2014, when the mediation procedure was enacted by the Federal Congress, it can act as a mediator between the tax administration and the taxpayer with respect to disagreements that arise during an audit.

trust and encourages the parties to negotiate actively during the mediation process.

Taxpayer's mediation request and tax administration's response

A taxpayer dissatisfied with the tax administration's audit position may file a mediation request with the independent mediator.[39] In the request, the taxpayer may submit some or all of the issues discussed as part of the audit. In relation to the submitted issues, the taxpayer provides reasons for its dissent including its interpretation of the facts, omissions, tax provisions and evidence involved in the audit.

Once the taxpayer's mediation request is filed, the independent mediator notifies the tax administration and asks for a response within 20 working days.

Suspension of time limits

With the filing of the mediation request, all deadlines (statutes of limitations) relating to the audit are suspended. This allows the tax administration time to carefully consider the arguments and evidence provided by the taxpayer. Despite that suspension, the mediator must ensure that the mediation procedure is agile and expeditious.

Process of mediation

The mediation procedure is effective because the officials of the tax administration who are conducting the audit are required to attend the mediation.

The mediation procedure is flexible enough to deal with a range of circumstances because it is subject to few regulations. Assuming the good faith of the parties in trying to find a consensual solution, the mediator may order any action which may contribute to the parties reaching an agreement.

The mediation procedure is confidential and does not set any precedent. The parties know that their proposals, offers and positions will

39 Only the taxpayer may file a mediation request; the tax administration is not allowed to do so.

be kept confidential by the mediator and will not become public. This encourages the parties to compromise in order to reach an agreement.

Outcome of mediation

The tax administration may accept or reject the taxpayer's proposals or make alternative proposals.

Where the tax administration agrees to the taxpayer's proposals, the mediator prepares and explains the clauses of the proposed agreement before sending these to the parties for their observations or suggestions. Where the parties accept the proposed agreement, they are asked to sign the agreement.

However, where the tax administration does not agree with the taxpayer's proposals and makes alternative proposals, the taxpayer is notified and requested to provide its approval or disapproval.

Where the taxpayer is notified of the tax administration's alternative proposals, it may modify its original proposal by presenting a counteroffer or agree with the tax administration.

The mediator may contact the tax administration and the taxpayer to clarify or further discuss any specific issue (e.g. complex transfer pricing issues). These meetings could be an opportunity for negotiations led by the mediator.

Where the tax administration and the taxpayer do not reach an agreement on some of the tax administration's conclusions, the tax administration may issue an assessment or reassessment for the tax payable related to those issues, which the taxpayer retains the right to challenge. Also, the tax administration must provide reasons for not accepting the taxpayer's proposals. Where this occurs, the mediator terminates the mediation procedure and the suspension of the deadlines is lifted, which allows the tax administration to continue the audit and issue the reassessment for tax payable by the taxpayer.

Where the tax administration and the taxpayer reach an agreement, the agreed outcome needs to be in accordance with the relevant law and in line with any guidelines dictating how the tax administration should reach settlements with taxpayers.

Legal consequences of the agreement

Once the parties sign the agreement, the agreed tax outcomes apply in relation to the stated issues. The agreement provides the parties with legal certainty and closure in relation to those issues.

Chapter 3

Domestic Dispute Resolution Mechanisms

3.1 Introduction

3.1.1 Overview

1. This chapter explores the domestic mechanisms that are generally available to resolve disputes that can arise between tax administrations and taxpayers with respect to income taxes.[1] While the primary objective of a tax administration should be to confirm that taxpayers are complying with the law and paying the correct amount of tax, tax administrations should recognize that disputes with taxpayers are inevitable. Therefore, it is of critical importance that mechanisms be available to resolve disputes in a manner that is as efficient and timely as possible and that these mechanisms be consistent with the legal framework of the country in which they are implemented.

2. These disputes can originate in a number of different ways, although they commonly arise from the results of an audit or review undertaken by the tax administration with which the affected taxpayer does not agree. While definitive statistics regarding the worldwide number of disputes between tax administrations and taxpayers are not available, the increased frequency of actions taken by tax administrations, for example to review or audit filed tax returns, likely also translate into an increase in the number of disputes with the impacted taxpayers.

3. The goal of this chapter is to provide practical guidance to countries that wish to improve certain aspects of their domestic dispute resolution process. This could be done through mechanisms that are created within, and thus as part of, the tax administration, as well as mechanisms that operate independently of the tax administration. Practice has shown that countries around the world have often chosen

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1 Including corporate taxes. As noted in Chapter 1, however, these mechanisms could also be useful to resolve disputes regarding the application of other types of taxes, such as value-added taxes.

to adopt several different dispute resolution mechanisms instead of just relying on one. Countries should therefore determine which of the mechanisms described in this chapter best suit their circumstances, the nature of the tax disputes that typically arise for their tax administration and their own legal framework (including the manner in which the taxpayer's rights to a fair and transparent process and to the rules of natural justice are protected at each level of the resolution of a tax dispute).

3.1.2 Disputes covered by this chapter

4. This chapter deals with mechanisms for resolving disputes between the tax administration and the taxpayers that relate to income taxes that have been assessed or reassessed. As explained in Chapter 1, this therefore excludes measures, such as certain forms of administrative review or mediation, that may be available in some countries to resolve disagreements that may arise at any stage up to, and during, the audit process, i.e. before the audit results in an assessment or reassessment or demand to pay tax. Some of these other mechanisms are discussed in Chapter 2.

5. Also, this chapter does not deal with disputes concerning the exercise, by the tax administration, of its enforcement and collection powers, including disputes concerning information exchanges and documentation requirements. These types of disputes do not relate to issues related to the determination of taxes payable and often involve the application of dispute resolution mechanisms generally applicable to the review of governmental actions.

3.1.3 Importance of resolving disputes

6. The main function of tax administrations around the world is to verify that their taxpayers have complied with tax laws. A tax administration's review of the accuracy of the tax paid and/or a return that was filed may conclude with a determination of an underpayment of tax, followed by the assessment and collection of the determined tax deficiency. The tax administration may also conclude that a taxpayer is not paying the taxes owed in a timely manner and may assess interest and/or penalties and enforce collection actions. Given this relationship, it is inevitable that disagreements between the tax administration and taxpayers will arise.

7. It is of critical importance for both the tax administration and taxpayers that disputes, when they arise, are addressed and resolved as quickly and efficiently as possible. Ensuring effective resolution of disputes will contribute to, and enhance, public confidence in the integrity of the tax administration as collector of tax revenues for the government.[2]

8. From the point of view of the taxpayer, access to recourse for the resolution of disputes should be available to ensure the action giving rise to the dispute, such as an assessment of additional taxes owed, is justified and does not result in an over-statement of the taxpayer's tax liability.

9. Dispute avoidance mechanisms described in Chapter 2, such as some forms of mediation, may sometimes be initiated by a taxpayer whose case is still at the examination stage. Such mechanisms, which may prevent a dispute from formally arising, do not eliminate the need for the mechanisms described in this chapter which are aimed at disputes that have formally arisen.

3.2 Overview of the main types of disputes and of domestic dispute resolution mechanisms covered by this chapter

3.2.1 Main types of disputes

10. Disputes may arise where, after an audit or the examination of a tax return, the tax administration concludes that additional taxes are payable and issues an assessment, reassessment or demand of payment of tax. Some examples of disputes resulting from findings during an audit or examination concerning the amount of tax liability include:

— Disagreements regarding the amount of taxable income calculated by the taxpayer

2 While this chapter does not deal with disputes of a general policy nature, such as concerns by taxpayers over the adoption of new audit or collection policies or the issuance of new tax forms, it is also important that tax administrations provide avenues to address such disputes with taxpayers because doing so will contribute to the public confidence in the tax administration.

— Disagreements regarding the taxpayer's choice of transfer pricing method used to value transactions between the taxpayer and its associated enterprises
— Disagreements concerning the availability or computation of foreign tax credits
— Disagreements regarding the characterization of items of income for tax purposes
— Disagreements regarding the existence or non-existence of a permanent establishment
— Disagreements regarding the taxpayer's country of residence

11. Disputes between the tax administration and taxpayers relating to the amount of tax liability may involve disagreements as to the facts on which the tax liability is based, disagreements on the interpretation of the tax law or disagreements on questions that are both factual and legal. In some countries, certain dispute resolution mechanisms are restricted to disputes concerning facts while disputes concerning the interpretation or application of the law must be dealt with by courts.[3]

3.2.2 Main types of domestic dispute resolution mechanisms

12. While there are considerable differences in the structure and legal form of the different types of dispute resolution mechanisms that countries have adopted to deal with income tax disputes, these fall within a few general categories. Some of the mechanisms, such as the administrative appeal procedure, are provided by the tax administration. Other mechanisms, such as seeking resolution of a tax issue by the courts, exist separately from, and outside of, the tax administration.

13. The first type of dispute resolution mechanism (discussed in section 3.4.1) allows a taxpayer that disputes an action or actions of the tax administration to request a review of the action in question by a

3 Throughout this chapter, a reference to a court is generally intended to include a "quasi-judicial tribunal", which is a body independent from the tax administration and set up by law which, although not technically a court of law, has the power to adjudicate disputes and does so through a process similar to the process followed in a court. See section 3.5.1.

separate appeals office within the tax administration.[4] An administrative appeal may be requested to review the conclusions of a review or audit that potentially affects the amount of tax owed. An essential aspect of the administrative appeal procedure is that although it is carried on by officials who belong to the tax administration, these officials must operate independently from the office that took the action being appealed from. Also, where the official who conducts the administrative appeal disagrees with the original decision or action of the tax administration, this official should be authorized to modify the decision or action accordingly so as to ensure the resolution of the dispute.

14. The second type of dispute resolution mechanism discussed (section 3.4.2) may be referred to as "administrative mediation". Through such procedure, officials of the tax administration trained in dispute resolution techniques facilitate the dialogue between the relevant officials in the tax administration and the taxpayer with the aim of helping to resolve the dispute. Whereas the officials who deal with administrative appeals provide their own analysis of the action or actions of the tax administration that led to the disputes, the role of the mediator is merely to enhance the communication between the disputing parties and facilitate an agreed resolution of the matter. Through such facilitation, the mediators assist the parties in clarifying and understanding each other's positions or reaching a mutually acceptable compromise.

15. The remaining dispute resolution procedures discussed in this chapter (section 3.5) involve parties that are independent from the tax administration. First, resolution of a tax dispute through the judicial system is allowed under the legal framework of almost all countries (section 3.5.1). The parties will often first attempt to resolve a dispute through other means, such as through administrative appeals, because these other means may resolve the dispute more quickly and avoid the financial costs of litigation for both the taxpayer and the tax administration. In fact, some countries require that, as a general rule, a taxpayer must first use available administrative appeals mechanisms before a case may be brought to courts. Subject to any judicial appeal rights, court decisions are binding on both parties to the dispute.

4 As indicated in footnote 15, the office in charge of such "administrative appeal procedure" will often be the office that has the initial responsibility for addressing taxpayers' objections.

16. Some countries have established, as an alternative to the civil courts of general jurisdictions, specialized courts that deal only, or almost only, with matters related to taxation (section 3.5.2). These specialized courts have a number of advantages. First, their narrower jurisdiction allows for the design of a more streamlined and time-efficient process for hearing cases. They also allow a more targeted selection of judges who have prior expertise in taxation. This facilitates a judge's ability to understand and decide tax disputes, which are often very technical in nature.

17. The dispute resolution mechanism discussed in section 3.5.3 is the establishment of a body that is commonly referred to as a "tax ombudsman". Such bodies are most commonly established outside the tax administration, but they could also be constituted within the tax administration. The functions of a tax ombudsman bear some similarity to the functions performed under other dispute resolution mechanisms described in this chapter because the tax ombudsman can serve as mediator to facilitate the resolution of taxpayer-specific disputes, but a tax ombudsman can also serve as a vehicle through which taxpayers that are concerned about general administrative issues or practices of the tax administration may express their views.

18. Section 3.5.4 briefly discusses the independent mediation mechanism, a function that is sometimes offered by a tax ombudsman service. Section 3.5.5 addresses expert determinations, a mechanism available in some countries to address purely factual questions.

19. The final type of dispute resolution mechanism discussed in this chapter is the independent arbitration of disputes between the tax administration and the taxpayer. Section 3.5.6 briefly describes the structure and operation of an arbitration procedure, including how a purely domestic arbitration procedure differs from the mutual agreement procedure arbitration provided for by some bilateral income tax treaties (a more detailed description of the latter type of arbitration is provided in Chapter 5).

3.3 Common issues for domestic dispute resolution mechanisms

20. While the various domestic dispute resolution mechanisms described in this chapter operate differently, a number of common

issues present themselves with most of these mechanisms. Countries should be aware of these issues when designing any mechanism to facilitate the resolution of disputes between taxpayers and the tax administration.

3.3.1 Ability to reach compromise solutions

21. There are significant differences in the ability of tax administrations to negotiate and accept compromise solutions to tax disputes.

22. In some countries, the tax administration has broad discretion to accept a solution that would depart from its original position in order to resolve a tax dispute at the administrative or judicial level. In the United States, for example, it is possible for taxpayers and tax authorities to reach "negotiated settlements" in order to settle a tax dispute at the administrative appeal stage or even after litigation has been undertaken. In that country, the risks inherent to the litigation process is an acceptable justification for a negotiated agreement that results in the payment of a lower amount of tax (and of interest and penalties) than what the tax administration originally claimed even if the tax administration considers that its original claim is justified.

23. Tax administrations that have the power to negotiate in this manner, however, must typically follow certain principles in reaching compromise solutions.

24. In some countries, such as Ecuador and Peru, the tax administration does not have the legal authority to depart from what it considers to be the tax payable under the law and cannot, therefore, reach a negotiated solution. In such a case, the tax administration must recognize that its original position, or part thereof, was not justified before it can agree, in the context of an administrative dispute resolution mechanism, to reduce the amount of tax initially assessed.

25. Where a tax administration has the authority to negotiate compromise solutions, this negotiation is usually not an "all or nothing" discussion and the reviewing official is normally able to settle the matter for a portion of the disputed tax in order to allow for the prompt resolution of the dispute without the need for litigation. Jurisdictions where the tax administration is allowed to negotiate compromise solutions during the administrative review or appeal process resolve a large number of cases at this level without the need for litigation.

26. The nature of negotiated compromise solutions requires that a degree of discretion be given to the official of the tax administration who negotiates with the taxpayer. This may be problematic in countries where corruption of public officials and political interference are serious risks. It is for that reason that some countries do not give their tax administrations the legal authority to negotiate compromise solutions. These risks may be partly mitigated by requiring the review of each compromise solution by a panel consisting of members of the tax administration with appropriate expertise who did not have any prior involvement in the particular dispute. It is also possible to reduce these risks through the public disclosure of the strict parameters within which compromise solutions may be reached (see, for example, the United Kingdom's *Litigation and Settlement Strategy*[5]). In many countries, the ability to reach compromise solutions on a principled basis is a normal attribute of the tax administration and its exercise does not require any specific framework.

3.3.2 Time limits

27. Countries commonly provide, in their domestic laws or administrative practices, time limitations for the tax administration and taxpayers to take certain actions, such as reviewing or amending a properly filed tax return. Once a tax return has been correctly submitted, the tax administration is typically allowed a certain period of time to review and assess additional tax regarding the taxable period covered by the return, at least as long as the taxpayer acted in good faith.[6] Similarly, a taxpayer that wishes to amend a return that has been previously submitted must typically do so within a certain period of time.

28. Time limits such as these are essential for ensuring that taxpayers acting in good faith are not exposed to a review of their tax liability many years after the relevant taxable events took place, when the information related to these events may no longer be available. Also, a tax administration should not be exposed to having to issue a tax refund for a given tax year decades after that tax year.

5 Available at https://www.gov.uk/government/publications/litigation-and-settlement-strategy-lss, accessed on 12 March 2021.

6 In many countries, no time limits are applicable in case of tax evasion or similar conduct by the taxpayer.

29. Time limits, however, may create issues when implementing a domestic dispute resolution mechanism.[7] The following basic example illustrates the main difficulty. Assume that, in 2018, the tax administration of State A audits a return for the tax year 2014 that was correctly submitted by the taxpayer in 2015. As a result of the audit, the tax administration assesses additional tax of 100 and issues a notice of assessment for that additional tax. The taxpayer disagrees with the assessment and seeks recourse through the applicable administrative appeal procedure. That procedure continues until 2019, when the amount of additional tax assessed by the tax administration is reduced from 100 to 25. The taxpayer accepts the reduced assessment.

30. Assume that, under the domestic law of State A, the tax administration may only modify a tax assessment within a period of three years following the proper filing of the return by the taxpayer. In this example, the preliminary assessment of 100 of additional tax was within that period but the reduction in the assessment to 25 that results from the administrative appeal is technically beyond the general deadline provided by domestic law.

31. This example demonstrates the importance of providing exceptions to the domestic time limits to ensure the proper implementation of a dispute resolution mechanism. A common way of addressing the issue is to suspend the time limitation for the period during which the dispute resolution mechanism is taking place. To the extent that the time limit in question is provided by domestic law, it is possible that such suspension could require legislative changes.

32. While the example above illustrates the importance of extending time limits in order to fully implement an administrative appeal resolution, the same is true for other dispute resolution mechanisms, all of which can be time consuming. Where a dispute is submitted to arbitration or review by a tax ombudsman, or if the parties litigate the dispute in court, it is equally critical for statutory time limits to be extended to allow the full implementation of the ultimate outcome of the case.

33. In some jurisdictions, tax authorities may be able to extend the deadline for assessment of additional tax with the agreement of the

7 Similar issues arise with respect to the implementation of the mutual agreement procedure of tax treaties: see chap. 4, section 4.4.6.

taxpayer. Such an extension may be requested during an examination of the taxpayer's return in a situation where the revenue authority has not yet finished its review or, where this extension is not already provided by law, during the administrative appeal or judicial process (in order to allow the outcome of that process to be implemented). In some countries, taxpayers may be able to request that an extension of the deadline be limited to certain issues, with the result that the tax administration may then assess additional tax only with respect to those issues.

34. Taxpayers who seek a refund of tax already paid are also often limited to a specific time period within which they may file a claim for refund. Depending on the jurisdiction, the time period may begin when tax is paid or when the relevant return is filed.

3.3.3 Collection considerations

35. Where tax payable, penalties or interest are assessed, the amount assessed must be collected. A number of collection tools are typically available to tax administrations for the purpose of collecting tax from taxpayers who fail to remit the appropriate amounts payable on time.[8] Collection procedures typically begin with the tax administration sending to the taxpayer a written request for payment with a stated deadline. If payment is not received by the specified deadline, imposing levies or liens on a taxpayer's bank accounts or other property may become necessary. Where the taxpayer is unable to pay the amount assessed, jurisdictions may permit a taxpayer to enter into a compromise with the tax authority to pay a lesser amount or pay the liability in instalments over a period of time.

36. Where the amount of tax owed is under dispute, the question typically arises as to whether the disputed amount should be immediately collected. A programme for administrative appeals or mediation should encourage good faith engagement and negotiation by both parties to the dispute. For example, the tax administration may find it

8 Note that a number of countries have included in their tax treaties provisions similar to those of Article 27 of the United Nations and OECD models under which they agree to assist the other treaty country in collecting finally determined taxes, as well as related interest and penalties, owed to that country.

more difficult to resolve the dispute if it considers that it may have to refund taxes already collected. To that end, it is advisable that collection actions be suspended with respect to a disputed amount of tax, interest and penalties once a case has reached the stage of administrative appeal, mediation or judicial litigation or, at least, that such a suspension be allowed in cases of hardship. Such a suspension could be associated to the requirement of providing an appropriate guarantee (e.g. to prevent the risk of a taxpayer leaving the country or disposing of all its assets before the conclusion of the dispute resolution process); it could also be subject to conditions intended to prevent procedural delays aimed at postponing collection.

3.3.4 Penalties and fines

37. To enhance voluntary compliance, countries with self-reporting tax systems often impose penalties for non-compliance.

38. There are various types of penalties which may be imposed under domestic law. Delinquency penalties may be imposed on taxpayers who fail either to pay a tax liability or to file required tax forms. Accuracy-related penalties may be asserted where a taxpayer fails to report the correct amount of tax due and underpays the correct tax liability. Penalties may also be triggered by a taxpayer's negligence or careless, reckless or intentional disregard of the tax law. Penalties may also be asserted where the taxpayer has undertaken a transaction that is specifically designed to avoid tax. Some penalties may be imposed by the tax administration subject to the taxpayers' right to challenge their application before the courts; others may require penal proceedings before a court.

39. A revenue authority may consider waiving or removing a penalty if the taxpayer can prove that it had reasonable cause for its failure to comply with the relevant obligations. For example, penalties may be inappropriate if circumstances leading to non-compliance were beyond the taxpayer's control, or where the taxpayer properly relied upon a legal precedent such as a court decision or the advice of the revenue authority or a tax professional.[9]

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9 The United States and the United Kingdom, for example, provide for this concept of "reasonable cause."

40. There are instances in which, as part of the resolution of the dispute, it is appropriate to reduce or even waive certain penalties that have been imposed on the taxpayer. In particular, penalties that are computed as a percentage of tax liability should be adjusted in a manner that is commensurate with any reduction in the tax liability that resulted from the resolution of the dispute. The same is true for any interest based on the amount of tax liability. The extent to which penalties and interest may be reduced or eliminated should be clear with respect to any dispute resolution mechanism.

3.3.5 Jurisdictional issues

41. Certain dispute resolution mechanisms do not apply to particular types of tax disputes and the question will sometimes arise as to whether a particular dispute may be dealt with under a specific domestic dispute resolution procedure. For example, in some countries, general courts are not allowed to decide issues related to the constitutionality of tax legislation, such issues being the exclusive jurisdiction of a constitutional court or similar body. There are also countries where the jurisdiction of courts that generally deal with tax matters is restricted to questions of law so that purely factual matters cannot be decided by these courts. It is also possible that quasi-judicial tribunals and arbitrators are prevented from addressing arguments related to human or procedural rights.

42. Also, in some countries, access to administrative appeals is not allowed for certain classes of tax disputes, such as cases that raise issues that are currently under consideration in the domestic court system, cases containing issues with no legal precedent or cases containing issues for which domestic courts in different regions have rendered conflicting decisions. A further example is provided by rules that provide that the availability of a particular dispute resolution mechanism depends on the amount of tax in dispute.

43. Issues may arise as to whether such restrictions are applicable in specific cases and it is often necessary to provide mechanisms through which such jurisdictional issues may be addressed. For instance, where domestic arbitration of tax cases is allowed, it will be necessary to determine whether an arbitrator has jurisdiction to determine his own jurisdiction in a specific case and whether any such decision may be subject to judicial review.

44. To the extent that it is already known, any restriction on the jurisdictional scope of a particular dispute resolution mechanism should be disclosed in publicly-available guidance so that taxpayers seeking recourse to resolve a tax dispute are aware of which mechanisms are at their disposal. Not all jurisdictional questions may be anticipated, however, and it is therefore important to provide mechanisms for the judicial resolution of jurisdictional issues that have not been addressed previously.

3.3.6 Coordination with other dispute resolution mechanisms

45. In the event that a country makes available more than one mechanism for resolving tax disputes, it is important to ensure a proper coordination between the mechanisms that are applicable. It may be the case that certain dispute resolution mechanisms are intended to apply, or could apply, simultaneously with respect to a particular dispute. In other cases, it would be more appropriate to allow certain mechanisms to apply alternatively or sequentially. Any applicable rules concerning such coordination should be made publicly available in order to avoid taxpayers pursuing the wrong dispute resolution mechanism.

46. For instance, in many countries (e.g. Belgium and India), taxpayers are generally required to first seek resolution of a tax dispute through the applicable administrative appeal procedure before being able to seek redress through the court system. Such a rule seeks to avoid the time and financial costs of pursuing judicial litigation where there is a reasonable chance that a dispute may be resolved by the tax administration. In some cases, however, it should also be possible for the taxpayer and the tax administration to agree to bypass the administrative appeal process, for instance in a case where a taxpayer intends to challenge in court a well-documented administrative practice of the tax administration.

47. Another example applicable to cross-border transactions is where a tax dispute includes a disagreement concerning the interpretation or application of a tax treaty. As is explained in detail in Chapter 4, almost all modern tax treaties provide for a mutual agreement procedure that allows a taxpayer that considers that there has been taxation not in accordance with the terms of the tax treaty to bring its case to the competent authorities designated in these treaties.

The coordination between domestic dispute resolution mechanisms and the mutual agreement procedure is an important issue. While most countries will allow the mutual agreement procedure and domestic recourses to be initiated in parallel, they will also want to ensure that both processes are not actively pursued simultaneously in order to avoid the risk of conflicting decisions.[10] Also, most countries will wish to avoid situations where the competent authorities would conclude a mutual agreement that would be binding on the tax administrations but where the taxpayer could resume or initiate judicial proceedings in order to obtain a different result in one of these countries.[11]

48. As a further example, the administrative mediation procedure described in section 3.4.2 below is intended to serve as a complement to other dispute resolution mechanisms that are provided by the tax administration. The role of a mediator is to facilitate communications between the taxpayers and the tax administration to help them reach a mutually satisfactory settlement. It follows that administrative mediation is typically available even when a case has reached the stage of administrative appeals or independent review to facilitate communications during those two processes. It also follows, however, that administrative mediation will typically not be available with respect to disputes that have been submitted to courts (such disputes, however, may then be eligible for the type of independent mediation discussed in section 3.5.4).

3.3.7 Admissibility of additional documents, evidence or arguments

49. A tax official or independent party involved in the resolution of a tax dispute needs access to information concerning that dispute. In most cases, information and arguments already communicated with respect to the dispute should be available to such person subject to the confidentiality requirements referred to in the next section. Different policy considerations, however, govern whether and to what extent these persons should be able to obtain and consider documents, evidence or arguments that were not previously presented. For instance, information that is relevant to the resolution of a dispute should be

10 See chap. 4, section 4.4.2.7.

11 See chap. 4, section 4.4.5.2.

communicated to the tax administration as soon as possible in order to prevent resources from being allocated to the processing of a dispute that could otherwise have been easily avoided or resolved. Also, where a taxpayer or the tax administration is only allowed to appeal the decision of a court on the basis that a question of law was wrongly decided, the limited scope of the appeal process would be easily circumvented if, in the course of the appeal, a party to the dispute were allowed to raise legal arguments that were not presented to the court that reached the decision that is appealed from.

50. For these and other reasons (which may reflect differences between legal systems), there are often restrictions on the ability of both taxpayers and tax administrations to refer to previously undisclosed documents or information, or to raise novel arguments, under different dispute resolution mechanisms. Tax administrations are encouraged to make publicly available guidance for taxpayers regarding not only what information needs to be included in a valid request for dispute resolution but also which restrictions, and exceptions thereto, are applicable as regards the documentation and arguments that may be raised in the context of the relevant dispute resolution process. It will not always be possible or appropriate, however, to prevent a person responsible for resolving a tax dispute from considering relevant information that was not disclosed to the tax official or officials who took the action that led to a dispute. In such cases, the best course of action may be to remand the case back to these officials for further consideration (as is done in the United States).

3.3.8 Confidentiality

51. Officials of a tax administration who are involved in processing tax disputes will generally be subject to strict legal requirements concerning the confidentiality of taxpayer data. By contrast, when individuals who are not tax officials are involved in the resolution of tax disputes, such as when a tax ombudsman is established as an organization separate from the tax administration or when an outside expert is appointed arbitrator or mediator, it is important to ensure that such an individual or organization is subject to the same or similar confidentiality requirements. This may be provided by legislation or by requiring the relevant individuals to execute legally binding confidentiality agreements.

52. In a large number of countries, however, court proceedings are public and the names of taxpayers involved in tax litigation, as well as relevant documentation, are publicly available. Thus, when a tax dispute reaches a court or tribunal, confidentiality requirements may no longer apply as regards what is disclosed to the court or tribunal. However, rules vary considerably among countries and even in countries where public disclosure of judicial proceedings is the rule, the name of the taxpayer involved may remain confidential and exceptions may be allowed with respect to sensitive information.

3.3.9 Measuring effectiveness

53. Confidentiality requirements do not prevent a country from collecting and disclosing aggregate statistics concerning the outcome of cases processed through dispute resolution mechanisms. For instance, this could be done by the tax administration as regards the tax disputes that it processes and by each court as regards the disputes that it is requested to resolve. Such statistics, which are produced by many countries, contribute to the determination of whether a particular dispute resolution is effective and to the identification of potential areas for improvement. Such statistics may include general information such as the number of cases processed, the break-down of cases based on their outcome (e.g. resolved in favour of the taxpayer or in favour of the tax administration), the average time required to process cases and the percentage of cases dealing with some topics that frequently arise in practice. A good example are the statistics on the mutual agreement procedure that are produced by countries that are members of the Inclusive Framework on BEPS.[12]

3.3.10 Tax expertise of individuals in charge of resolving tax disputes

54. It is important that the individuals who have been tasked with resolving tax disputes possess sufficient expertise in the relevant tax area. In the case of dispute resolution provided by the tax administration (e.g. the administrative appeal procedure described in section 3.4.1), this should generally not be an issue as long as sufficient budgetary resources are allocated to that function so that appeal officials are experienced and

12 See chap. 1, paras. 11 and 13.

well-trained. Involving individuals with tax expertise is equally important where dispute resolution is provided by independent parties: taxpayers and tax administrations are unlikely to be satisfied by decisions of domestic arbitration panels that would reveal that the members of the panels lack expertise in the relevant tax rules.

55. Given the broad jurisdiction of some courts, however, it may be difficult to ensure that a tax dispute submitted to such a court is heard by a judge that possesses extensive tax expertise, which may be particularly problematic with respect to complex tax cases. One solution that has been adopted by many countries is the establishment of a specialized tax court or tribunal, or a specialized tax unit within a more general court, whose jurisdiction is exclusively or primarily restricted to tax disputes. Such specialized bodies are more likely to attract and retain judges and members who have tax expertise and, through internal discussions and the sharing of decisions, further contribute to the development of the expertise of these individuals. However, countries need to weigh the potential costs and benefits associated with the establishment of such specialized bodies. For instance, if relatively few tax-related cases are typically heard in a country's civil courts, it may be difficult to justify the resources required to establish a judicial body specialized in tax matters.

3.3.11 Reliance on precedents

56. Another issue that is common to all domestic dispute resolution mechanisms is the extent to which a specific tax dispute may or should be decided based on decisions already rendered in similar cases.

57. The courts of most countries have well-developed rules and principles applicable to the question of whether and to what extent judges have to follow a decision on a similar issue that was previously rendered by a court of the same country (typically referred to as a legal precedent). In most cases, lower courts are expected to follow precedents from courts, in particular supreme courts, that hear appeals from decisions of lower courts. Decisions rendered by other judges of the same court or courts of the same level, however, are not always given the same precedential value and may simply be considered as relevant.[13]

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13 In some countries (e.g. the United States and India), some important or controversial issues may be decided (or reviewed, in the case of the

58. Accessibility to previous court decisions is sometimes an issue in developing countries. Where general access to court decisions is allowed, which is the case in a large number of countries, tax administrations and courts are encouraged to maintain a public web site through which decisions, or at least decisions that address questions of law, are publicly accessible.

59. A question that is primarily relevant in relation to disputes related to the provisions of tax treaties but which may also arise with respect to the interpretation of domestic tax provisions is whether foreign court decisions may be relied upon by domestic courts. While foreign court decisions clearly cannot be considered as legally binding, there does not seem to be any policy or legal reason that would prevent a domestic court from at least consulting the views expressed by foreign judges on the interpretation of similar legislative or treaty provisions. This is frequently done in the courts of a number of common law countries. Clearly, language issues may prevent recourse to such foreign decisions but, at least as regards tax treaties, detailed summaries and full translations of foreign decisions are often available.

60. The issue of precedents also arises with respect to dispute resolution provided by the tax administration. A tax administration will generally seek to avoid having tax officials spend their time analysing and deciding questions that other tax officials have already decided; it will also seek to provide the same treatment to taxpayers in the same circumstances. For these reasons, a tax administration should implement mechanisms that allow all tax officials involved in the resolution of tax disputes to have access to decisions rendered by their colleagues in cases similar to those that they are dealing with. While in most cases confidentiality requirements make it impossible for these decisions to be publicly disclosed, the publication by the tax administration of administrative guidance and rulings (redacted so as to remove confidential taxpayer information) may contribute to making public the positions developed by the tax administration in response to common disputes.

United States Tax Court) by larger benches that include a larger than usual number of judges. Such decisions will typically be given precedential value within that court.

3.3.12 Formalistic and purely discretionary approaches

61. Persons involved in the resolution of tax disputes are frequently required to interpret tax legislation in the light of the specific facts of a case. A question that often arises is the extent to which such persons may exercise discretion in doing so.

62. As far as judges and members of quasi-judicial tribunals are concerned, precedents will often exist as regards the approach that should be adopted when interpreting tax legislation. That approach is typically influenced by the nature and tradition of the legal system of a country (e.g. common law or civil law) and will frequently evolve over time.

63. Many countries have gradually abandoned overly formalistic approaches under which the words of a tax statute were read literally without regard to their context and the intention of the legislator. Under one such approach, any doubt as regards a tax statute had to be resolved in favour of the taxpayer. In many countries, there is now a greater recognition that the words of the tax law should be read in context and that the purpose of the provisions should be taken into account in determining how these should be interpreted. This approach is expressly mandated when interpreting the provisions of tax treaties, as recognized by Article 31(1) of the *Vienna Convention on the Law of Treaties.*[14]

64. Persons in charge of resolving tax disputes should not have complete discretion as to how they resolve these disputes. The principle of the rule of law requires that these persons, whether acting as judges, tax officials or in another capacity, perform their functions in accordance with the law. In addition, it is important that tax officials decide disputes in accordance with the applicable administrative guidance. While courts may legitimately disagree with interpretations put forward by the tax administration, taxpayers are entitled to expect a consistent treatment from the tax administration and tax officials should therefore comply with the administration's published guidance until it is decided to reverse or abandon such guidance.

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14 *Vienna Convention on the Law of Treaties*, available at https://treaties.un.org/doc/publication/unts/volume%201155/volume-1155-i-18232-english.pdf, accessed on 12 March 2021. To the extent that Article 31 is a codification of customary international law, this approach is applicable even in countries that have not signed or ratified the *Vienna Convention on the law of Treaties*.

3.4 Mechanisms through which dispute resolution is provided by the tax administration

65. This section describes in more detail a number of dispute resolution mechanisms that operate within and as part of the tax administration. These mechanisms are typically administered through an office within the administration that is separate and independent from the offices that perform audit, examination or collection functions.

3.4.1 Administrative appeal procedure

66. In many countries, taxpayers may avail themselves of a dispute resolution process that is provided by the tax administration itself and through which tax officials who are different from those who took the action that is disputed (such as an assessment for an additional amount of tax following an audit) review these actions at the request of the taxpayer affected. This is the role, for instance, of the Independent Office of Appeals in the United States and the Commissioner of Income-tax (Appeals) in India. This internal review process, which is referred to as an "administrative appeal procedure" throughout this chapter, is typically initiated by a formal objection or opposition presented by the taxpayer.[15]

67. The purpose of the administrative appeal procedure is to provide taxpayers with the ability to request a review of actions or decisions taken by tax officials with which they disagree. The most crucial aspect of a successful administrative appeal programme is that it operates independently from the exam, audit and collection functions so as to avoid a situation in which the officials who took the disputed actions or decisions influence the outcome of the review.

68. If a taxpayer disagrees with a tax adjustment resulting from the audit or examination process, the taxpayer is typically afforded the right to challenge the examiner's determination at the administrative level prior to initiating judicial proceedings. While some jurisdictions (e.g. Brazil) do not allow for an administrative review of the examiner's

15 The office in charge of such "administrative appeal procedure" will therefore be the office that has the initial responsibility of addressing taxpayers' objections. For instance, in Jamaica, this is the office to which such objections must be sent.

findings, most do. Resolution of tax disputes through administrative review without the need for litigation is typically more efficient, as regards costs and resources, for both the government and the taxpayer. In most countries, taxpayers are not required to pay the disputed tax if they file an administrative appeal. In some countries, an efficient administrative appeal procedure that resolves disputes prior to litigation not only saves taxpayers and the tax administration time and money but may also help alleviate the problem of an overloaded court system.

69. The office that deals with taxpayers' appeals should seek to resolve tax disputes in an independent, fair and impartial manner, with the goal of resolving disputes where the taxpayer is right without requiring the taxpayer to initiate judicial proceedings. As such, this office should consider all the factual information and relevant legal sources before reaching a decision.

70. As already noted,[16] when setting up an administrative appeal procedure, it is important to implement oversight measures to mitigate potential corruption risks. At the same time, however, it is important to ensure that the tax officials in charge of appeals do not feel constrained to follow the decisions reached at the audit or initial review stage.

3.4.1.1 Function of the office in charge of administrative appeals

71. As already mentioned, it is crucial that the office in charge of appeals operate separately and independently from the parts of the tax administration whose actions may lead to disputes with taxpayers, such as the exam, audit and collection functions. In order to protect this independence and to ensure an impartial and objective review of each case, the assigned appeal official should not have any prior involvement with the action (i.e. the audit, examination or assessment) that gave rise to the dispute.

72. The function of the office in charge of appeals is to provide a de novo evaluation, at the request of the taxpayer, of the disputed conclusions that have resulted from an exam, audit or from a determination of additional tax payable. In doing so, the office in charge of appeals must have the ability to arrive at its own independent conclusions concerning the tax administration's previous actions, and where

16 See para. 26 above.

appropriate, to either uphold or reduce the taxes owed as a result of the administration's original decision. For example, if after reviewing the results of the examination of a tax return that resulted in an assessment of additional tax of 100, that office determines that the appropriate amount of additional tax that should have been assessed is only 80, the office in charge of appeals will typically have the power to require that the amount of tax assessed be adjusted accordingly so that if the taxpayer accepts the revised amount, the dispute is resolved.

73. In order to resolve disputes without creating new ones and to maintain public confidence in the administrative appeal procedure, in most countries, the office in charge of appeals has the authority to maintain or reduce the amount of tax resulting from the prior decisions of the tax administration to which the taxpayer objected. It cannot, however, increase the amount of tax assessed by taking positions that are different from those initially taken by the tax administration.

74. The specifics of the administrative appeal procedure vary among jurisdictions. Some of the differences result from differences in legal systems (e.g. common law or civil law); others result from factors as diverse as a government's trust in its tax administration and the expertise of tax officials. In countries such as the United States, for example, the administrative appeal officials are authorized to negotiate and conclude binding final settlements on behalf of the government. In other countries (such as Peru), this possibility does not exist.[17]

75. In some countries, the administrative appeal process cannot result directly in an adjustment of the tax assessed: if the decision is favourable or partly favourable to the taxpayer, the case is sent back to the relevant part of the tax administration that must reassess the case (unless the taxpayer opts to pursue an additional mechanism, such as arbitration or judicial litigation procedures that may be available at that stage).

3.4.1.2 The administrative appeal request

76. The tax administration should make publicly available guidance on how to request an administrative appeal. Such guidance should emphasize any time limits for making such a request. For example, the

17 See section 3.3.1 above.

administrative appeal procedure may require that the taxpayer submit an administrative appeal request within a specified number of days of the taxpayer's receipt of the notice of the action giving rise to the dispute, such as a letter of assessment or demand of payment of additional tax after the conclusion of an audit or exam.

77. The format of such a request should be simple enough to allow unsophisticated taxpayers to initiate an administrative appeal. One would expect the request to typically include the following information:

— The taxpayer's name, address and tax identification number
— A reference to the notice or letter from the tax administration describing the action or decision that has triggered the dispute (such as a notice of assessment of additional tax, or a notice of intent to initiate collection procedures against the taxpayer), including the date of that notice or letter
— The date of the relevant event or the taxable period concerned
— A description of each decision or action to which the taxpayer objects and of the arguments supporting that objection, which may include, especially for large taxpayers, references to any relevant legal provision or authority supporting the taxpayer's position.

78. Ideally, it should be possible for taxpayers to make such a request electronically through a secure web site that would automatically link the request to the notice or letter that triggered the dispute, thereby avoiding the need to provide some of the above information.

3.4.2 Administrative mediation

79. The administrative mediation procedure described in this section, which exists in countries such as Belgium and Kenya, operates differently from, and is complementary to, the administrative appeal procedure. It is also different from the independent mediation process described in section 3.5.4 since it involves a mediator who belongs to the tax administration as opposed to one who is independent. The purpose of the administrative mediation procedure is to facilitate communications between the taxpayer and tax officials to help resolve the dispute. Mediation officials from the tax administration can attempt to facilitate dialogue between parties by helping the parties identify

the issue or issues at dispute, clarify each other's positions, and develop a range of possible options to arrive at a negotiated settlement.

80. By its nature, the administrative mediation procedure complements other dispute resolution mechanisms and may thus be invoked simultaneously. For instance, one situation in which administrative mediation might be useful is where a taxpayer has made a request under the administrative appeal procedure but finds it difficult to communicate with the tax officials in charge of appeals. In that case, the assistance of a mediator from the tax administration may facilitate the discussions. In some countries, mediation may also be requested by tax officials in charge of appeals. In many cases, however, administrative mediation may only proceed if both the taxpayer and the relevant tax officials agree to participate. It should also be noted that in some countries (e.g. Belgium and the United Kingdom), mediators may, and actually do, reject cases where their assistance has been requested, for instance because they consider that the substantive issues on which the dispute is based cannot be resolved through additional discussions.

81. Independence and impartiality are critically important to the success of the administrative mediation procedure. Therefore, as is the case with the administrative appeal procedure, countries wishing to provide mediation within the tax administration should establish an office that is independent from the rest of the tax administration, in particular the audit, examination and collection functions. If an office in charge of appeals has already been established, the administrative mediation programme could be administered from that same office and handled by appeal officials who have been specially trained in facilitation techniques.

82. The administrative mediation function does not typically involve a de novo evaluation of the dispute or a modification of the disputed decision, although it may result in a recommendation or suggestion for a different outcome. Therefore, officials performing the administrative mediation function do not require the tax authority to evaluate and possibly modify the original decision, as is the case with officials performing the administrative appeal function. Nevertheless, the mediation officials will need to have the authority to have access to confidential (e.g. taxpayer-specific) information in order to effectively

facilitate communications. To the extent that the officials who conduct the administrative mediation also work as appeal officials, they should already be legally allowed to access confidential information.

83. An administrative mediation programme should be structured in a way that allows mediation to be initiated early in the administrative appeal process. Given the potential benefits that could be gained from mediation before a decision is taken by the tax administration, mediation could even be made available while the matters in dispute are at the pre-assessment stage, such as in audit, examination or collection.[18] Moreover, it is critical that both parties to the dispute agree to submit to the administrative mediation and express a willingness to resolve the dispute. The administrative mediation may involve a mediator simply investigating a case and reporting to a taxpayer without taking further action. In many cases, however, the two parties will be convened to a meeting that is facilitated by the mediator.

84. A flexible approach should be taken regarding the form and contents of a request for administrative mediation. Given the possibility that administrative mediation could take place at any stage of a tax dispute, even before it is formalized (in the case of the mediation process described in Chapter 2), the request will not always be accompanied by a copy of the decision that affects the taxpayer (such as a notice of assessment of additional tax), as such decision may have to be taken when mediation is requested.

3.5 Mechanisms through which dispute resolution is provided by independent parties

85. This section discusses domestic dispute resolution mechanisms that generally operate outside the tax administration. In almost all countries, taxpayers have the right to seek resolution of tax disputes in courts, although practice has shown that taxpayers often seek recourse through other mechanisms before resorting to litigation so as to avoid the costs and delays associated with litigation, which can be substantial, or to avoid adverse publicity as court proceedings are generally public. Independent mediation services are also available in some countries. While this section also explores the role that a tax ombudsman

18 See chap. 2, section 2.3.8.

established outside the tax administration may play in resolving disputes, countries may equally consider establishing a tax ombudsman within the tax administration, although in that case it will be critically important that the ombudsman enjoy complete autonomy and independence from the rest of the administration. Finally, the expert determination and arbitration procedures that are available in some countries are discussed at the end of this section.

3.5.1 Resolution of disputes in courts

86. As previously indicated, taxpayers generally have the right to seek resolution of a tax dispute by the courts.[19] Such courts may be civil courts of general jurisdiction (courts that adjudicate all types of legal challenges), administrative courts, commercial courts or specific tax courts. They may also be "quasi-judicial tribunals" which, for the purposes of this chapter, correspond to separate bodies set up by law in order to decide specific types of disputes and which, although not technically courts of law, have the power to adjudicate disputes and do so through a process similar to the process followed in a court. In these quasi-judicial tribunals, disputes are adjudicated by experts who may or may not have formal legal training.[20]

87. Almost all countries also provide the possibility for both the taxpayer and the tax administration to appeal a decision of the court that first renders a decision in a tax dispute. Some appellate level courts will review only a lower court's decisions on questions of law (i.e. the appeal court will not be allowed to reverse the factual findings of the lower court), while other courts will review both questions of law and questions related to the facts of the case.

88. The benefits of the judicial resolution of tax disputes include securing a final determination of the taxpayer's tax liability, which

19 As explained in paragraph 46, in some jurisdictions, taxpayers are required to seek resolution of a tax dispute at the administrative level (i.e. through the administrative appeal procedure) before initiating court proceedings. In jurisdictions where this is not required, initiating a court proceeding may preclude an administrative appeal.

20 For this reason, persons adjudicating tax disputes in quasi-judicial tribunals are often referred to as "members of the tribunal" as opposed to "judges".

cannot be re-examined by the tax authority or another court (except to the extent the jurisdiction provides for judicial appeals). In addition, judges and members of a quasi-judicial tribunal may be perceived as more impartial and objective than the tax officials in charge of administrative appeals.

89. As already indicated, judicial proceedings and decisions rendered by courts are usually public.[21] While this transparency serves to enhance confidence in the judicial process and provides useful precedents as to how the law should be applied and interpreted, some taxpayers may be reluctant to initiate judicial proceedings because of this loss of confidentiality.

90. There are important differences between the countries' judicial processes applicable to tax disputes and it would be beyond the scope of this chapter to discuss these differences in detail. A key difference, however, is the extent to which a court will hear legal arguments and testimonies by witnesses. While this is typically the case in common law countries, it may be more exceptional in civil law countries where courts tend to rely more on a written procedure.

91. One consequence of this distinction is that countries where the hearing of witnesses is the norm tend to have "trials" and also pre-trial fact findings that may be formal or informal. Informal fact-finding, or "discovery," often means that the parties will stipulate the facts in advance of a trial, which speeds up the litigation process and assists in settling many cases prior to trial. Formal discovery, on the other hand, may involve, for example, requests for documents from the opposing party and depositions by witnesses. The parties are not required to agree on any facts; instead, the facts are determined by the fact-finder —a judge, member of tribunal or, more exceptionally, a jury.[22]

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21 See para. 52.

22 In jurisdictions that provide for jury trial, a taxpayer may prefer a jury if the taxpayer's facts are compelling but the legal basis for the taxpayer's position is not totally persuasive. In those cases, the taxpayer might want to select a forum in which it can lay out its facts in front of the jury, and not a forum in which facts must be stipulated or would be heard only by a judge. However, juries may not be able to comprehend complex tax laws, thus a case-by-case analysis must be performed.

92. Other countries, however, do not have formal pre-trial fact findings. The facts and legal arguments are presented to the court by the parties (taxpayer and tax authority) at the time the proceedings are initiated along with the information and evidence they were able to obtain.

93. In many countries, special procedures exist to allow tax cases that raise the same or similar issues to be dealt with together or to be resolved based on the results of a "test-case". This reduces the costs, duplication and risks of conflicting decisions involved in dealing with such disputes separately.

3.5.2 Specialized tax courts

94. As mentioned in the previous section, because of the complexity of tax law, many countries have established a specialized court or quasi-judicial tribunal whose jurisdiction is limited to tax issues.[23] Judges or members of these specialized courts and tribunals typically have expertise in tax matters and are thus in a better position to resolve cases dealing with these matters. Tax court judges and members are usually independent from the tax administration although, in some countries, disputes are resolved by a panel of judges and other members, some of whom are tax officials.

95. One of the benefits of having experts adjudicate tax cases is that it may ensure a quicker resolution of tax disputes and may therefore reduce delays and the caseload of a country's general court system. While it is often possible to appeal the decisions of a specialized tax court, appellate courts are typically not specialized in tax matters (even though they may have specialized tax units if the number of tax appeals justifies it).

96. Tax courts in some countries can enable and encourage settlements at an early stage of the litigation process. However, as in the case of the administrative appeal procedure, other countries do not provide taxpayers and tax authorities the possibility of reaching a settlement once litigation has commenced.

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23 The jurisdiction of these courts may be limited to a particular category of tax matters, such as disputes concerning cross-border transactions, or may extend to a wide variety of direct and indirect tax matters.

97. In many countries that offer specialized tax courts, simplified procedural rules are available in the case of judicial proceedings concerning tax disputes involving small amounts or some categories of taxpayers (e.g. individuals as opposed to legal entities). These simplified procedures may alleviate the need to be represented by a lawyer, thereby reducing the costs of tax litigation for taxpayers. This, for example, is the case in Mexico.[24]

98. The following are a few examples of specialized tax courts in developing countries.

99. In South Africa, cases heard by the Special Income Tax Court are dealt with by a judge assisted by an accountant who has at least 10 years of experience and a representative of the business community. To file a petition with the Special Income Tax Court, the dispute with the South African Revenue Service must involve an assessment exceeding R100,000. Tax disputes of less than R100,000 are heard by the Tax Board, which is chaired by an attorney, advocate, or accountant who works in the private sector.

100. India's Income Tax Appellate Tribunal (ITAT) is a quasi-judicial body that hears appeals from the decisions of India's Revenue Department. The ITAT consists of tax experts with a background in law or accounting. The ITAT's decisions with respect to legal positions are binding on the Revenue Department. Appeals from the ITAT decisions may be brought before appellate level courts but those courts may only review substantive points of law, the ITAT being the final arbiter of the facts.

101. Mexico, through its Federal Court of Administrative and Tax Justice, offers a "traditional" tax trial, an "on-line" tax trial, a "summary" tax trial and a "substance over form" tax trial. The alternative pursued by the taxpayer before the court depends on the amount of the tax liability at stake, the reasons for the tax assessment or the physical proximity of the court. For example, if a tax assessment is based only on formalities, the taxpayer may choose to pursue the "substance over form" trial, which allows magistrates to overlook formalities and nullify tax debts if there is substance in the taxpayer's position.

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24 See para. 101 below.

3.5.3 Tax ombudsman

102. The dispute resolution mechanism described in this section, often referred to as a "tax ombudsman," shares certain similarities with the administrative mediation procedure discussed in section 3.4.2 above but may also serve certain functions of a more general nature, such as the safeguarding of taxpayer rights and ensuring that the administration is providing fair and adequate services to taxpayers by, for example, dealing with taxpayers' complaints related to the services provided by the tax administration. The tax ombudsman is a specialized version of the more general concept of ombudsman, which historically has been referred to as an institution that defends the people. The increased use of tax ombudsman bodies may reflect a recognition across countries of the complexity of their respective tax systems and the importance of ensuring that the rights of taxpayers are respected, that the services of the tax administration are provided in an equitable and efficient manner and that the government should facilitate the resolution of controversies between the tax administration and taxpayers.

103. While the tax ombudsman body described in this section is an independent party, countries wishing to establish a tax ombudsman may also decide to set it up within the tax administration. In such a case, it is important that the ombudsman be allowed to operate independently, in particular from the audit, examination and collection functions, and be allocated adequate resources to perform its functions.[25] Both types of bodies exist in practice and have been found to provide positive results.

104. The creation of tax ombudsman bodies has become more common in recent years, although the names given to these bodies differ. In Australia, it is referred to as the Inspector-General of Taxation, which is a body separate from the Australian Taxation Office. In the United States, the Taxpayer Advocate Service is an independent organization within the Internal Revenue Service. Ombudsman bodies in Spanish-speaking countries are commonly referred to as the Defender of the Taxpayer (*Defensoría del Contribuyente*).

105. The establishment of a tax ombudsman body outside the tax administration may enhance the confidence that taxpayers will have

25 See section 3.4.2 above.

in the ability of the tax ombudsman to perform its functions because taxpayers may consider that a separate agency is more likely to ensure an equitable treatment of disputes with the tax administration. The efficiency of the tax ombudsman body depends not only on that independence but also on the expertise of its officials. Where the tax ombudsman is set up as a body independent from the tax administration, it is also important to ensure that it has the legal authority to access taxpayer-specific and other confidential information and that it is required to maintain that confidentiality.

106. When the tax ombudsman is established within the tax administration, it is critical that it be separate from all the other operating functions of the administration and that it operate independently from these other functions. This is especially true regarding the audit, examination and collection functions. Where the tax ombudsman performs the more general role of monitoring the tax administration's provision of services to taxpayers, it will also be important to ensure its independence from other offices such as those that establish generally applicable administrative practices (e.g. audit and collection policies), promulgate regulations or other guidance and draft forms. The independence of the tax ombudsman may also require that its budget be allocated and administered separately.

107. Recourse to the services of a tax ombudsman should be as simple as possible. It is also important that taxpayers be made aware of the existence and role of the tax ombudsman.

Box 1: Tax ombudsman: the positive experience of Mexico

The *Procuraduría de la Defensa del Contribuyente* (PRODECON) was established in Mexico in 2011 as an agency independent of the tax administration that carries out the functions of a tax ombudsman. PRODECON has been granted powers under Mexico's domestic law that authorize it to address both taxpayer-specific matters as well as issues of general concern relating to the operation of the tax administration.

The taxpayer-specific dispute resolution remedies provided by PRODECON allow taxpayers to submit service-related complaints regarding actions taken by the tax administration. These complaints are dealt with under PRODECON's complaint procedures. In addition, taxpayers may request, through the conclusive agreement procedure, mediation assistance from PRODECON to facilitate communications in their dealing with the tax administration. Yet another taxpayer-specific service provided by PRODECON is the legal representation of certain taxpayers to assist them in their dealings with the tax administration.

PRODECON's complaint procedure

The complaint procedure allows PRODECON to investigate any action of the tax administration that may infringe or has infringed on the rights of a taxpayer. This procedure may be requested by any individual or legal entity that believes that its rights as taxpayer have been infringed, regardless of the amount of the tax liability at stake.

Under the complaint procedure, PRODECON reviews and analyses the protest of the taxpayer and gives the tax official involved in the controversy a period of 72 hours to present that official's views in the form of a report. If, after reviewing the official's report, PRODECON determines that the complaint has merit, it issues non-binding recommendations for modifying the position of the tax administration with a view to resolving the dispute. If the official declines to follow the recommendations, PRODECON makes the recommendations publicly available in a way that maintains the confidentiality of the taxpayer's particular data.

Since PRODECON's establishment, the complaint procedure has been widely used by Mexican taxpayers. According to data provided by PRODECON, by 2019, 170,000 requests for assistance had been submitted under the complaint procedure since its creation.

PRODECON's conclusive agreement procedure

The conclusive agreement procedure, established in 2014, is an alternative dispute resolution mechanism for tax controversies in Mexico. Taxpayers under audit who do not agree with the position and findings of the tax authority have the right to appear before

PRODECON to request its intervention as a mediator.[26] The procedure provides a transparent and amicable forum for the taxpayer and the tax authority, with an impartial third-party observer, to discuss the tax treatment or the tax law's interpretation that is being applied during the audit, with the objective of achieving consensus to resolve the dispute.

According to data provided by PRODECON, 10,500 mediation requests have been processed so far by PRODECON, which facilitated resolution of the majority of the disputes involved. The procedure allows for the resolution of disputes without judicial recourse, thus avoiding litigation costs for both taxpayers and the government.

The conclusive agreement procedure acts as an alternative, and not a complement, to the administrative appeal procedure provided by the tax administration. Under the conclusive agreement procedure, PRODECON's primary function is not merely to facilitate communications between the administration and the taxpayer but also to resolve the dispute by facilitating the negotiation of a mutually agreeable settlement through the exchange of proposals between the disputing parties.

The conclusive agreement procedure is only available while a case is in audit or examination. Initiating the procedure suspends the relevant domestic time limits, as well as the audit and any collection procedures.

Although the aim of the conclusive agreement is to reach an agreement that resolves the entirety of the tax dispute, partial resolutions are also permitted. In the case of a partial resolution, the tax administration may resume applicable audit and collection procedures with respect to the unresolved issues.

If the conclusive agreement procedure does not successfully resolve the audit dispute, the taxpayer may seek recourse through the tax administration's administrative appeal procedure or the

26 This aspect of the work of the PRODECON is mentioned here even though it is not a dispute resolution mechanism within the meaning of this chapter.

courts. Upon closing a failed conclusive agreement case, PRODECON is empowered to issue an "infringement of rights" declaration if it determines that the tax administration has acted in an arbitrary manner during the relevant audit. While an infringement of rights declaration is non-binding, it may nevertheless be useful to the taxpayer if the dispute proceeds to administrative appeals or to court.

PRODECON's legal representation and defence service

Under this procedure, PRODECON provides legal representation to taxpayers to assist in their dealings with the tax administration. This service is generally offered to small taxpayers: it is available only to taxpayers when the amount of tax assessed by the tax administration in a particular year does not exceed 1 million pesos, not counting fines, surcharges or inflationary adjustments.

3.5.4 Independent mediation[27]

108. The conclusive agreement procedure offered by the PRODECON (see Box 1 above) provides a good example of an independent mediation mechanism. While the aim and techniques of an independent mediation mechanism are somewhat similar to those of the administrative mediation service described in section 3.4.2, a key difference is that the independent mediation allows recourse to a mediator who does not belong to the tax administration and may therefore be perceived by the taxpayer as being more independent.

109. As is the case for a tax ombudsman service set up as a body separate from the tax administration,[28] countries wishing to provide an independent mediation service need to ensure that the mediators have the legal authority to access taxpayer-specific and other confidential information and that they have the legal obligation to maintain such confidentiality.

27 While this section focuses on the role that an independent mediator can play in the resolution of domestic tax disputes, Chapter 6 explains how mediation could be used in the context of the mutual agreement procedure provided by tax treaties.

28 See para. 105 above.

3.5.5 Expert determination

110. In some countries, purely factual questions, such as the market value of an asset, may be referred to an expert whose mandate is simply to make the required factual determination. This may be done as part of judicial proceedings when it is decided that a purely factual and technically complex matter should be determined by an independent expert whose finding is then submitted to the court. In these circumstances, the determination of the expert is binding on the parties.

111. Recourse to an expert determination may help avoid the costs of a "battle of expert witnesses" where both sides try to influence a court's decision on a complex factual issue by having their own expert witnesses present their opinions to the court which is then called upon to make a decision on that issue.

112. Expert determination should not be confused with the use of expert witnesses, who may be used by one or both parties in judicial proceedings in order to try to establish some factual aspects of a tax case. Expert witnesses do not determine the relevant factual question but simply present their position (orally or in writing) to the court, which is solely responsible for reaching a decision on the relevant question of fact. Similarly, expert determination should not be confused with cases where the court appoints its own expert in order to provide advice to the court regarding certain aspects of a tax dispute.

3.5.6 Arbitration

113. In a few countries (e.g. Portugal), a domestic arbitration procedure allows for the binding resolution of a dispute between the tax administration and the taxpayer by one or more independent parties acting outside a formal judiciary framework. In these countries, arbitration is typically allowed only after available recourses to the tax administration (e.g. an administrative appeal) have failed to result in an agreement to resolve the issue.

114. Such domestic arbitration procedures applicable to tax disputes are fundamentally different from the MAP arbitration provisions sometimes found in bilateral tax treaties or provided by Part VI of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS.* As explained in Chapter 5, MAP arbitration provisions

are used to resolve disputes that prevent the competent authorities of the countries that are party to a tax treaty from concluding a mutual agreement under the mutual agreement procedure provided by these treaties. MAP arbitration is therefore a procedure to resolve disputes between two tax administrations as opposed to disputes between taxpayers and tax administrations.

115. Domestic arbitration procedures may be provided by law or may be available through agreements with the tax administration. In the first case, arbitration may be available as a right (if the applicable conditions are met). Otherwise, arbitration is only available with respect to a specific case if both the taxpayer and the tax administration agree.

116. The domestic arbitration of tax disputes may be restricted to questions of fact, such as the valuation of an asset or the arm's length price of a transaction, but, in some countries, questions of law are also eligible for arbitration.

117. A number of different aspects must be addressed when designing a domestic arbitration procedure. These include:

— *The selection of arbitrators*: The number of arbitrators and the process for their selection should be clear. In domestic tax arbitration, it is frequent to have a single arbitrator who is jointly selected by the taxpayer and the tax administration. Any requisite qualifications or selection criteria that arbitrators must satisfy should be specified. As far as possible, the parties should seek to appoint an arbitrator who has relevant expertise. For example, if the dispute involves a disagreement over the valuation of an asset, the parties may wish to require that an arbitrator possess at least five years of experience in asset valuation. Also, in order to avoid conflicts of interests, an arbitrator should not have had any prior involvement with the particular dispute or the taxpayer concerned.

— *The form of the arbitration procedure*: Arbitration may take different forms. For instance, under the so-called "baseball" or "final offer" arbitration, the arbitrator is only asked to make a choice between the position of the taxpayer and that of the tax administration and cannot adopt an intermediary solution, which has the benefit of forcing the parties to abandon extreme positions. Under the "independent opinion" approach, the arbitrators have more discretion but may then require more information and may need to provide a more complete justification of their decisions. Whatever form is used, it will be important to provide procedural rules for the conduct of the arbitration proceedings, such as the deadlines for the different steps leading to the arbitration decision and the rules governing the conduct of the arbitrators (e.g. the arbitrator should be precluded from any *ex parte* communications with either party prior and during the arbitration proceedings).

— *Arbitration costs*: Applicable rules should provide which party will bear the costs of arbitration, including the remuneration of arbitrator(s), or how these costs will be shared between the parties. For instance, it could be provided that each party will pay one half of the arbitrator's compensation, expenses and related fees and costs.

— *Confidentiality of information*: Unlike court proceedings, the domestic arbitration procedure is usually confidential. It will therefore be necessary to ensure that arbitrators have access to taxpayer-specific and other confidential information and that they are legally bound to maintain the confidentiality of any such information, for instance through a binding arrangement with the tax administration.

— *Binding nature of the decision*: A critical aspect of the arbitration procedure is the extent to which the arbitration decision should be final and binding for both the taxpayer and the tax administration. If arbitration is intended to be an alternative to judicial proceedings, it would be logical to assume that the arbitration decision would be final and binding on both parties. In some countries, however, the taxpayer may have the right to reject an arbitration decision and take the issue to court. Also, in many countries, it is generally possible to ask a court to invalidate an arbitration decision on procedural grounds, such as where the arbitrators exceeded their jurisdiction.

PART 2

THE DISPUTE RESOLUTION MECHANISM OF TAX TREATIES: THE MUTUAL AGREEMENT PROCEDURE

Chapter 4

The Mutual Agreement Procedure

4.1 Introduction

1. This chapter deals with the mutual agreement procedure (MAP), which is the dispute resolution procedure provided for in tax treaties.[1] That procedure, which is separate and independent from the administrative and judicial dispute resolution mechanisms provided by domestic law, allows representatives of the States that have concluded a tax treaty (usually through officials from their respective tax administrations) to address taxpayer complaints about an incorrect application of the provisions of the treaty as well as difficulties or doubts arising in relation to the interpretation or application of the treaty.

2. The MAP plays a crucial role in promoting the fulfilment of treaty obligations. It is intended to provide foreign taxpayers with the assurance that a potentially incorrect application of treaty provisions by one treaty State may be brought to the attention of tax officials from the other treaty State. The MAP is therefore a critical component of a tax treaty and a key provision for foreign investors and other taxpayers. This is especially the case in countries where foreigners may be reluctant to rely on domestic administrative and judicial dispute resolution mechanisms, for example because of a perception that the tax administrations, administrative tribunals and courts of these

1 This chapter does not deal with the type of mutual agreement procedure envisaged by either the EU *Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprise* (90/436/EEC), often referred to as the EU Arbitration Convention, or the EU Council Directive 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union. More information on these instruments, which are applicable within the European Union, are available at https://ec.europa.eu/taxation_customs/business/company-tax/transfer-pricing-eu-context/transfer-pricing-arbitration-convention_en and at https://ec.europa.eu/taxation_customs/business/company-tax/resolution-double-taxation-disputes_en_deT, accessed on 12 March 2021.

countries lack the necessary resources or tax treaty expertise to deal with treaty issues, which can often be complex.

3. As already indicated, statistics on the MAP show that the number of MAP cases increased on average by more than 11 per cent each year between 2006 and 2015.[2] However, these statistics also show that the majority of developing countries have no or limited experience with the MAP[3] even though these countries, like all countries that enter into tax treaties, must be prepared to meet their treaty obligations with respect to the MAP regardless of any lack of experience.

4. This chapter provides practical guidance on the MAP and is primarily intended for developing countries that have little experience with that procedure, although its contents will also be relevant for a broader range of countries. It replaces the United Nations *Guide to the Mutual Agreement Procedure* which was approved by the United Nations Committee of Experts on International Cooperation in Tax Matters at its 2012 meeting.[4] The guidance included in this chapter complements the guidance on the mutual agreement procedure found in the Commentary on the United Nations Model Tax Convention, which constitutes the most authoritative source of information on the interpretation of the provisions included in that model; in case of divergences between the guidance of this chapter and that of the Commentary on the United Nations Model Tax Convention, the latter prevails. Also, to the extent that the provisions of the United Nations Model Tax Convention dealing with the MAP are similar to those of the OECD Model Tax Convention, and because the Commentary of the United Nations Model Tax Convention quotes large parts of the Commentary of the OECD Model Tax Convention, the Commentary of the OECD Model Tax Convention will also be relevant, in particular as regards treaties that follow the wording of the OECD Model Tax Convention rather than that of the United Nations Model Tax Convention. Obviously, however, the guidance in this chapter is only relevant to the extent that the MAP provisions of the individual treaty under which a MAP case arises are identical or substantially similar to those found in the United Nations and OECD models.

2 See chap. 1, para. 11.

3 See chap. 1, footnote 8.

4 See Preface, footnote 10.

5. Chapter 1 described how Action 14 (Making dispute resolution mechanisms more effective) of the G20/OECD project on base erosion and profit shifting (BEPS) has had a significant impact on the implementation of the MAP.[5] The large number of countries that have joined the Inclusive Framework on BEPS[6] have committed to implement the minimum standard included in the final report on Action 14.[7]

6. For that reason, the elements of that minimum standard and the best practices included in the final report on Action 14 are included in the Annex to this chapter and are referred to where relevant. It is important to remember, however, that countries that have not joined the Inclusive Framework on BEPS are not required to apply that minimum standard.

7. Since many of the countries that have joined the Inclusive Framework on BEPS are developing countries and these countries will be subject to a peer review of their MAP practices,[8] there has been an emphasis by the international community on the provision of assistance to these countries to help them minimize and resolve cross-border tax disputes. This assistance may help these countries overcome challenges that they often experience with respect to the MAP. The following are some of these challenges:

- Many developing countries, especially least developed countries, currently have a limited capacity to deal with complex international tax treaty issues and few have set up the administrative framework that would allow them to conduct a MAP effectively.
- In some cases, the relationship between MAP and domestic law is unclear and may hinder the application of the MAP.
- Countries with limited experience with international tax law (e.g. transfer pricing audits/studies and treaty application) or with domestic tax laws that lack robust rules to deal with cross-border issues may be tempted to try to avoid resolving international tax disputes through the MAP.

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5 See chap. 1, section 1.2.

6 See chap. 1, footnote 13.

7 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14 —2015 Final Report*, chap. 1, footnote 10.

8 See chap. 1, footnote 15.

— Not all countries are aware that the inclusion of MAP provisions in a tax treaty creates legal obligations for the treaty countries. Also, some countries may not have fully considered the procedural aspects of the MAP and may therefore be tempted to discourage its use.

— The protection of taxpayer rights, including the right to confidentiality, may be an issue in some countries, particularly in countries which have limited experience with international tax law; if taxpayers do not trust the MAP because they do not trust the officials involved or the institutional process, they may be reluctant to use it.

8. Despite these challenges, developing countries should be mindful of the need to provide mechanisms to address disputes related to tax treaties. These countries are confronted with international tax cases, and transfer pricing cases in particular: cross-border transactions between different parts of MNE groups do not occur only between developed countries but also with developing countries. With those cases comes the need to implement mechanisms in order to prevent obstacles to international trade and investment. Since domestic dispute resolution mechanisms only address a dispute in one treaty country and ignore the tax treatment in the other country, thereby not addressing potential double taxation, a country cannot rely exclusively on domestic recourses to address international double taxation cases. The MAP allows such cases to be resolved in a way that is binding on both countries involved.

4.2 What is the MAP?

4.2.1 Role of the MAP

9. Almost all modern tax treaties include an article that provides a procedure for addressing difficulties that may arise in the interpretation and application of the treaty. This procedure, the MAP, is particularly relevant where such difficulties may result in double taxation, the prevention of double taxation being one of the main purposes for entering into tax treaties;[9] indeed, even cases of double taxation not addressed by the treaty may be dealt with under the MAP.

9 As recognized in the Title and Preamble proposed in the United Nations and OECD models.

10. The MAP offers taxpayers an avenue for the resolution of a dispute concerning the application of tax treaty provisions that is distinct and independent from any available domestic dispute resolution mechanisms. While this avenue may not always be successful, it presents some advantages over purely domestic dispute resolution mechanisms:

— The MAP allows a consideration of the issue by tax officials of the two treaty States and any agreement reached in the context of the MAP may impact taxation in both treaty States, whereas the impact of a domestic dispute resolution system available in a treaty State is generally restricted to taxation in that State and thus may not be able to resolve the issue.

— The MAP involves consideration of tax treaty issues by officials who have tax treaty familiarity and expertise, which is not necessarily the case of officials and judges who deal with different types of tax disputes and even non-tax disputes.

— The MAP, being less formal than domestic judicial proceedings (especially if such recourses would be required in the two treaty States in order to eliminate double taxation), may be less expensive for taxpayers and tax administrations. It may also provide a quicker resolution of the case in countries where there are lengthy delays in the processing of cases by courts and quasi-judicial tribunals.[10]

— The MAP does not preclude recourse to domestic dispute resolution mechanisms in one or both treaty States (although taxpayers may be precluded from pursuing the MAP and such recourses at the same time so as to avoid the risk of conflicting decisions).

— Since the MAP may be initiated as soon as the risk of taxation not in accordance with the provisions of a tax treaty becomes probable, it may involve a quicker access to a dispute resolution mechanism than is possible under domestic law.

10 This is especially true in light of the minimum standard 1.3 of BEPS Action 14, under which countries that have joined the Inclusive Framework on BEPS commit to seek to resolve MAP cases within an average time frame of 24 months (see para. 179 below).

4.2.2 Legal basis for the MAP

11. The tax treaty article that provides for the MAP is typically based on Article 25 of the United Nations or OECD model. Article 25, as found in both models, provides three different situations in which the MAP may be used:

- The first situation, by far the most frequent, is where a person that considers that its tax treatment in one or both treaty States is not in accordance with the treaty (or will not be so in the future), requests that this issue be addressed under the MAP. This is dealt with in paragraphs 1 and 2 of Article 25.
- The second situation is where tax officials of the two treaty States try to resolve by mutual agreement issues relating to interpretation or application of a treaty provision (such as the meaning of a term that is not defined in the treaty). These cases are usually related to issues that affect more than one person; they may involve issues of treaty interpretation that concern a category of taxpayers or issues relating to how provisions of the treaty will be applied in practice. This situation is dealt with under the first sentence of paragraph 3 of Article 25.
- The third situation is where the tax officials of the two treaty States consult each other for the elimination of double taxation in cases not dealt with under the treaty, for example, where a resident of a third State has a permanent establishment in both treaty States and double taxation arises because of the way that these States calculate the profits of the two permanent establishments. This third situation is dealt with under the second sentence of paragraph 3 of Article 25.

12. The guidance included in this chapter deals primarily with cases falling within the first category, which involves requests made to the tax authorities by persons that consider that they have not been taxed in conformity with the treaty.

13. The tax officials of a treaty State who are responsible for applying the MAP are referred to in tax treaties as the "competent authority" of that State. The term "competent authority" is defined in paragraph 1(*e*) of Article 3 of the United Nations Model Tax Convention.[11] While

11 Paragraph 1(*f*) of Article 3 of the OECD Model Tax Convention.

countries are free to choose who is designated for that purpose, it is important that the persons or authorities so designated have sufficient authority to effectively negotiate with their counterparts in the other treaty State and to make binding decisions with respect to the cases brought before them. The competent authority will therefore generally be defined as the relevant minister or head of the tax administration and its authorized representatives, which means that senior officials in the tax administration or the relevant ministry (and not the minister or head of the tax administration personally) will perform the role assigned to the competent authority by the treaty.

14. The United Nations Model Tax Convention has two alternative versions of Article 25. The only difference between these two versions (alternative A and alternative B) is that alternative B includes an additional paragraph (paragraph 5) which provides for the mandatory arbitration of issues that the competent authorities are unable to resolve within three years. The arbitration process envisaged by that paragraph is discussed in Chapter 5.

15. The following provides a brief description of paragraphs 1 to 4 of both alternative versions of Article 25. Other parts of this chapter provide a detailed analysis of the requirements and obligations of each paragraph and provide guidance on their practical application.

16. Paragraph 1 provides an avenue for taxpayers to ask the competent authority to address potential violations of the provisions of a tax treaty. The requirements of that paragraph are:

- The taxpayer considers that its tax treatment in one or both States is not, or will not be, in accordance with the treaty.
- The case must be presented to the competent authority of the State of residence of the taxpayer or, in cases involving a claim of discriminatory taxation based on nationality to which paragraph 1 of Article 24 could apply, of the State of nationality of the taxpayer.
- The case must be presented within three years from the time the person is notified of the action that allegedly result in taxation not in accordance with the treaty (for instance, a notice of assessment).

17. The only difference between paragraph 1 of the United Nations Model Tax Convention and paragraph 1 of the OECD Model Tax Convention relates to the second requirement. Paragraph 1 of the OECD Model Tax Convention was modified in 2017 to allow a person to present a case to the competent authority of either State. This difference is discussed below.[12]

18. Paragraph 2, which is identical in the United Nations and OECD models, sets out the obligations of the competent authority to whom a case is presented under paragraph 1.

19. Paragraph 3, which is also the same in the United Nations and OECD models, deals with the second and third situations referred to in paragraph 11 above in which the MAP may be used. Under the first sentence of the paragraph, the competent authorities must try to resolve by mutual agreement issues relating to interpretation or application of the treaty. The second sentence of the paragraph also authorizes them to consult each other for the elimination of double taxation in cases not dealt with under the treaty, for example, in the case referred to in the last part of paragraph 11.

20. The first sentence of paragraph 4, which is the same in the United Nations and OECD models, authorizes the competent authorities to communicate directly with each other for purposes of the mutual agreement procedure. The second sentence of the paragraph, which has no equivalent in the OECD Model Tax Convention, allows the competent authorities to develop, through consultation, bilateral procedures for the implementation of the mutual agreement procedure.[13]

21. The BEPS Action 14 minimum standard requires that the countries that have joined the Inclusive Framework on BEPS include paragraphs 1, 2 and 3 of Article 25 of the OECD Model Tax Convention in their tax treaties. It does, however, allow these countries to use alternative mechanisms instead of strictly following the wording of the first sentence of

12 Paras. 47 and 111.

13 While paragraph 4 of the OECD Model Tax Convention does not expressly provide that the competent authority may develop such procedures, there is no substantive difference between the two versions because the authorization to develop these administrative provisions can likewise be found in paragraph 3 of Article 25.

paragraph 1 and the second sentence of paragraph 2.[14] As discussed below, this allows these countries to adopt the different formulation of paragraph 1 found in the United Nations Model Tax Convention.

4.3 Typical treaty issues dealt with through the MAP

4.3.1 List of typical MAP issues

22. As previously mentioned, the vast majority of MAP cases result from requests made by taxpayers under paragraph 1 of Article 25. Issues that give rise to such requests typically result from disagreements related to the facts of a case or to the interpretation of the applicable treaty provisions. They sometimes involve the interpretation of contracts or of provisions of domestic law, such as those related to labour law or copyright law.

23. The Commentary on Article 25 of the United Nations Model Tax Convention[15] identifies a few common issues that are dealt with through the MAP. The following are examples of such issues:

— *Transfer pricing issues and issues related to the attribution of profits to a permanent establishment.* The MAP statistics of the Inclusive Framework on BEPS[16] include a breakdown of MAP cases based on whether they relate to attribution of profit issues[17] or other cases. According to the statistics prepared for 2019, such cases, which are discussed below in sections 4.3.2 and 4.3.3, represented 54 per cent of the reported outstanding MAP cases at the end of that year.

— *Whether a permanent establishment exists in a treaty State.* Where, for example, an enterprise of State A does business in State B and State B considers that the business activities exercised

14 Element 1.1 of the minimum standard (see Annex).

15 Para. 9, quoting paras. 9–10 of the Commentary on Article 25 of the OECD Model Tax Convention.

16 See chap. 1, para. 11.

17 Defined as issues related to the attribution of profits to a permanent establishment or the allocation of profits between associated enterprises and arising under treaty provisions corresponding to Articles 7 and 9 of the United Nations and OECD models.

on its territory constitute a permanent establishment under the definition of that term in the relevant treaty, State B may tax the enterprise's profits that it considers to be attributable to that permanent establishment as well as other profits referred to in treaty provisions similar to those of paragraphs 1(*b*) and (*c*) of Article 7 of the United Nations Model Tax Convention. State A, however, may take the view that there is no permanent establishment and that the treaty gives it the exclusive right to tax the profits of the enterprise. As a result, the profits taxed by State B would also be taxed by State A which may refuse to provide relief from double taxation.

— *Dual treaty residence of a person (individual or legal person)*. For example, an individual who is a resident of both States A and B under the respective domestic laws of these States and who has a permanent home available in both States will, under the provisions of the treaty between States A and B that correspond to paragraph 2(*a*) of Article 4 of the United Nations Model Tax Convention, be deemed to be a resident only of the State with which his or her personal and economic relations are closer (centre of vital interests). Based on this test, the individual considers that he or she is a resident of State A for treaty purposes. State B, however, applies the test differently and taxes the worldwide income of the individual on the basis that the individual is a resident of State B for the purposes of the treaty.

— *Alleged application of withholding taxes in contravention to the treaty provisions*. An example would be where a company resident of State A pays a dividend to a company resident of State B and the company withholds tax from the dividend at the rate of 25 per cent provided by State A's domestic law. After the State B company has requested a refund of the tax withheld in excess of the applicable rate provided in paragraph 2 of Article 10 of the treaty between States A and B, the tax authorities of State A reject that request because they consider that the State B company is not the beneficial owner of the dividend. The company disagrees with that view.

— *Issues related to the characterization of income*. Such an issue would arise where, for example, a company resident of one treaty State considers that a software payment that it received from a resident of the other treaty State constitutes business profits (which, under Article 7 of the relevant treaty, the other State may not tax in the absence of a permanent establishment on its territory) but the other State requests the payment of a withholding tax on the amount paid because it considers that the payment constitutes royalties covered by Article 12 of the treaty.

— *Alleged application of domestic anti-abuse provisions in contravention to the treaty provisions.* For example, under a dividend-stripping rule found in the domestic law of State A, that State taxes as dividends the gain realized by a resident of State B upon an alienation of shares that would otherwise fall within a provision of the treaty between the two States that is similar to paragraph 6 of Article 13 of the United Nations Model Tax Convention. The taxpayer disagrees with State A's view that the application of the dividend-stripping rule is justified, notwithstanding the definition of the term "dividends" in the treaty, because the alienation is part of an arrangement that constitutes an abuse of the relevant treaty provision.

— *Alleged taxation by one treaty State in contravention of the treaty rules on non-discrimination.* An example would be where a company resident of a treaty State considers that the denial, under the domestic law of that State, of the deduction of certain payments made to residents of the other treaty State constitutes a violation of a treaty non-discrimination rule similar to that of paragraph 4 of Article 24 of the United Nations Model Tax Convention.

— *Issues related to cross-border employment.* This would include, for example, a case where a treaty State taxes the income derived from employment services performed on its territory by a resident of the other treaty State because it considers that the employee spent more than 183 days on its territory during a 12-month period, but the taxpayer disagrees and considers that the exception of paragraph 2 of Article 15 applies to the income.

24. The above list is not an exhaustive list of treaty issues that are raised in MAP cases initiated under paragraph 1 of Article 25. That paragraph allows a person to raise any issue that may have resulted, or may result, in that person being taxed not in accordance with the provisions of a tax treaty.

25. In many cases, taxation not in accordance with the provisions of a tax treaty will result in double taxation. For example, if the amount of withholding tax that is levied in the source State exceeds what is authorized by the treaty, the treaty does not require the residence State to provide a credit for the excess tax and double taxation of the relevant income may result. However, double taxation is not a required condition for a MAP case to be initiated; all that is required is that the person making a request under paragraph 1 of Article 25 considers that there is, or will be, taxation not in accordance with the treaty provisions.

4.3.2 Transfer pricing issues

26. Given that a large proportion of MAP cases arising under paragraph 1 of Article 25 involve issues related to the allocation of profits between associated enterprises or the attribution of profits to permanent establishments and that, on average, such cases require significantly more time to be processed,[18] it is important to understand the treaty context in which these cases typically arise.

27. Issues related to the allocation of profits between associated enterprises involve the application of treaty rules corresponding to those of Article 9 (Associated enterprises) of the United Nations and OECD models. These rules deal with transfer pricing adjustments based on the arm's length standard.[19] Paragraph 1 of Article 9 acknowledges that a treaty State may adjust the profits of an enterprise of a treaty State that is associated to an enterprise of the other treaty State in order to reflect

18 The OECD MAP statistics for 2019 (chap. 1, footnote 7) show that MAP cases involving transfer pricing issues were completed on average in 30.5 months whereas other cases were completed on average in 22 months.

19 Detailed guidance on the practical application of the arm's length principle in the context of Article 9 may be found in the *United Nations Practical Manual on Transfer Pricing for Developing Countries* (2017), available at http://www.un.org/esa/ffd/publications/united-nations-practical-manual-on-transfer-pricing-for-developing-countries-2017.html, accessed on 12 March 2021, as well as in the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017*, OECD Publishing, Paris, https://doi.org/10.1787/tpg-2017-en, accessed on 12 March 2021.

the profits that would have been realized if the enterprises had been dealing at arm's length. In order to avoid the same profits being taxed by both treaty States, paragraph 2 imposes an obligation on the other treaty State to provide a corresponding adjustment to the profits of the other associated enterprise but only to the extent that the adjustment made by the first State conforms with paragraph 1 of Article 9 and is therefore in accordance with the arm's length standard.[20]

28. The following example illustrates the application of paragraphs 1 and 2 of Article 9. Company A, a resident of State A, is a wholly owned subsidiary of Company B, a resident of State B. The companies are therefore associated enterprises for the purposes of Article 9 of treaty between States A and B. Following a tax audit of company A, the tax administration of State A takes the position that the company paid an excessive amount for management services that were provided to it by Company B. Based on its analysis of what an independent enterprise would have paid for similar services, State A reduces the amount of the deduction claimed by Company A with respect to the payment for these services, which has the effect of increasing the taxable profits of Company A and, therefore, the tax payable by the company. This is referred to as the "initial" or "primary" adjustment.

29. The profits on which Company B has been taxed by State B, however, include the amount initially charged by that company to Company A for the management services. Thus, the additional profits allocated to Company A as a result of the initial adjustment made by State A have already been taxed in State B. In order to eliminate such double taxation,[21] paragraph 2 requires State B to reduce the amount

20 Paragraph 3 of Article 9 of the United Nations Model Tax Convention, which has no equivalent in the OECD Model Tax Convention, indicates that the obligation to provide a corresponding adjustment under paragraph 2 does not arise if, as a result of legal proceedings, there has a been a final ruling that one of the enterprises is liable to penalty with respect to fraud, gross negligence or wilful default in relation to the actions that resulted in the initial transfer pricing adjustment under paragraph 1 of the article.

21 Since this form of double taxation involves two States taxing different taxpayers on the same income, it is often referred to as "economic double taxation" as opposed to "juridical double taxation", which involves two States taxing the same taxpayer on the same income.

of the tax that it charged on those profits (the "corresponding adjustment"). That obligation, however, is dependent on whether or not the initial adjustment made by State A is in conformity with the arm's length standard.

30. Given tax authorities' increased focus on transfer pricing and the element of uncertainty involved in the application of the arm's length principle,[22] transfer pricing adjustments and the obligation to provide corresponding adjustments under paragraph 2 of Article 9 create an important potential for disputes between taxpayers and tax authorities and between tax authorities themselves. As recognized by the last sentence of paragraph 2, which provides that the "competent authorities of the Contracting States shall if necessary consult each other" for the purposes of determining a corresponding adjustment, the MAP plays a critical role in allowing for the resolution of such disputes in a way that ensures that the same profits are not subject to tax in the two treaty States. The BEPS Action 14 minimum standard, which requires countries that have joined the Inclusive Framework on BEPS to "provide access to MAP in transfer pricing cases and implement the resulting mutual agreements (e.g. by making appropriate adjustments to the tax assessed)",[23] acknowledges the importance of allowing such disputes to be dealt with through the MAP:

> … the failure to grant MAP access with respect to a treaty partner's transfer pricing adjustments, with a view to eliminating the economic double taxation that may follow from such an adjustment, will likely frustrate a primary objective of tax treaties. Countries should thus provide access to MAP in transfer pricing cases. Where, in particular, treaty provisions such as paragraph 2 of Article 9 or, in the absence of paragraph 2 of Article 9, provisions of domestic law enable Contracting States to provide for a corresponding adjustment and it is necessary for the competent authorities of the Contracting States to consult to determine the appropriate amount of that corresponding

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22 "As transfer pricing is often referred to as 'an art, not a science', the resulting uncertainty creates the potential for transfer pricing disputes with tax authorities, even if the multinational enterprise is seeking to comply with domestic transfer pricing rules" (*United Nations Practical Manual on Transfer Pricing for Developing Countries*, footnote 19, para. A.4.14).

23 Element 1.2 of the minimum standard (see Annex).

> adjustment with the aim of avoiding double taxation, countries should provide access to MAP.[24]

31. As noted above, access to MAP in transfer pricing cases can thus be allowed even under treaties that do not include the corresponding adjustment provisions of paragraph 2 of Article 9. This is expressly recognized in the Commentary on Article 25 of the United Nations Model Tax Convention, which provides that "…the mere fact that Contracting States inserted in the convention the text of Article 9, as limited to the text of paragraph 1—which usually only confirms broadly similar rules existing in domestic laws—indicates that the intention was to have economic double taxation covered by the Convention."[25] In order to avoid any doubt regarding the issue, the final report on Action 14 recommends that, as a best practice,[26] countries should include paragraph 2 of Article 9 in their tax treaties. Similarly, access to MAP should also be allowed where a corresponding adjustment is denied on the basis of paragraph 3 of Article 9 of the United Nations Model Tax Convention (according to which there is no obligation to make a corresponding adjustment in certain cases)[27] because a taxpayer may reasonably consider that the conditions for the application of that paragraph have not been met. Another issue that may be addressed through the mutual agreement procedure is the application of "secondary adjustments", a question related to the consequences of a primary transfer pricing adjustment which is discussed in the Commentary on Article 9 of the United Nations and OECD models.[28]

32. Many countries offer taxpayers the possibility of minimizing the risk of transfer pricing disputes through the conclusion of

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24 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14—2015 Final Report*, chap. 1, footnote 10, at p. 14.

25 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 11 of the Commentary on Article 25 of the OECD Model Tax Convention.

26 Best practice 1 (see Annex).

27 See footnote 20.

28 Paragraph 7 of the Commentary on Article 9 of the United Nations Model Tax Convention, quoting paragraphs 8 and 9 of the Commentary on Article 9 of the OECD Model Tax Convention.

advance pricing arrangements (APAs). The use of APAs, their advantages and the issues that they may raise are discussed in section 2.3.3 of Chapter 2; as explained in that section, bilateral and multilateral APAs are typically concluded through the use of the mutual agreement procedure.[29]

33. In some cases, the tax administrations of developing countries will have little or no expertise in the area of transfer pricing. The competent authorities of these countries may nevertheless become party to a MAP involving transfer pricing issues. In such cases, they may need to seek assistance and should rely on guidance such as that of the *United Nations Practical Manual on Transfer Pricing for Developing Countries.*[30]

4.3.3 Issues related to the attribution of profits to a permanent establishment

34. Issues related to the attribution of profits to permanent establishments involve the application of treaty rules corresponding to those of Article 7 (Business profits) of the United Nations and OECD models and, in particular, of the provisions of paragraph 2 of that Article.[31] That paragraph contains the basic rule for determining the profits attributable to a permanent establishment and provides that these profits are the profits that the permanent establishment "would have made if, instead of dealing with the rest of the enterprise, it had been

29 Annex II of Chapter IV of the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017* (footnote 19) provides guidance on the use of the MAP for the conclusion of APAs.

30 Footnote 19.

31 Paragraph 1 of Article 7 of the United Nations Model Tax Convention, unlike the corresponding provision of the OECD Model Tax Convention, specifies three categories of profits that may be taxed in the State where there is a permanent establishment: (a) profits attributable to the permanent establishment; (b) profits from sales in that State of goods or merchandise that are of the same or a similar kind as those sold through the permanent establishment and (c) profits from other business activities carried on in that State that are the same or of a similar kind as those carried on through the permanent establishment. Most MAP cases related to Article 7 deal with the first category, i.e. the determination of profits that are attributable to the permanent establishment.

dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market".[32] This means that the profits attributable to a permanent establishment should be determined on the basis of the separate entity and arm's length principles.

35. The application of the arm's length principle to the determination of profits attributable to a permanent establishment raises issues that are very similar to those arising in the application of that principle in the context of Article 9, which deals with associated enterprises. The application of the separate entity principle, however, raises a number of additional difficulties[33] since it requires that some transfers of capital, goods and services between a permanent establishment and its head office and between a permanent establishment and other permanent establishments of the same enterprise be treated as if they were transactions between separate enterprises for purposes of determining the profits of the permanent establishment.

36. Another difference between the MAP issues that may arise under Article 7 and Article 9 is that the basic rule of paragraph 2 of Article 7 concerning the attribution of profits to a permanent establishment applies to both treaty States. That rule is therefore relevant not only for determining what may be taxed by the treaty State where the permanent establishment is situated but also what is the part of the profits of the enterprise with respect to which the other treaty State, being the State of residence, must eliminate double taxation in

32 Paragraph 14 of the Commentary on Article 7 of the United Nations Model Tax Convention, quoting paragraph 14 of the Commentary on Article 7 of the 2008 OECD Model Tax Convention. While the new version of Article 7 that was included in the OECD Model Tax Convention in 2010 differs significantly from Article 7 of the United Nations Model Tax Convention, paragraph 2 of this new version also uses the separate entity and arm's length principles as the basis for determining the profits attributable to a permanent establishment (even though it provides a somewhat different interpretation of these principles).

33 Some of these difficulties are addressed in paragraph 15 of the Commentary on Article 7 of the United Nations Model Tax Convention, quoting paragraphs 12–15.4 of the Commentary on Article 7 of the 2005 OECD Model Tax Convention, as well as in the Commentary on paragraph 3 of Article 7 of the United Nations Model Tax Convention.

accordance with the rules of Articles 23 A and 23 B (Methods for the elimination of double taxation). While this means that risks of double taxation should in theory be avoided in many cases since both countries are obliged to apply the same principles for the determination of profits attributable to a permanent establishment, this may not prevent disputes from arising since the practical application of the separate entity and arm's length principles underlying paragraph 2 of Article 7 raises a number of difficult issues. The MAP has therefore an important role to play in order to ensure that the profits attributable to a permanent establishment are determined in a consistent way by both treaty States.

4.4 How does the MAP work?

4.4.1 Overview of the Art. 25(1) MAP process

37. A typical MAP initiated in accordance with paragraph 1 of Article 25 involves different actions that may be regrouped under the following five steps:

1. The MAP request
2. The unilateral stage of the consideration of the MAP case
3. The bilateral stage of the consideration of the MAP case
4. The conclusion of the MAP
5. The implementation of the mutual agreement reached through the MAP

38. The following diagram summarizes each of these five typical steps. The diagram is followed by a flowchart that indicates the main actions involved in each of these steps. Both the diagram and flowchart refer to actions that are typically carried out during the MAP whether or not they are expressly required by the provisions of the relevant treaty. Sections 4.4.2 to 4.4.6 provide additional details on each of the steps. A more detailed table summarizing the different actions involved in a typical MAP with an indicative timetable is included in section 4.4.7. Section 4.4.8 explains the main differences between the process for a MAP under paragraph 1 of Article 25 and a MAP under the first and second sentences of paragraph 3 of Article 25. Section 4.4.9 deals with the communication between competent authorities in the context of a MAP.

THE FIVE STEPS OF A TYPICAL ART. 25(1) MAP

1. The MAP request (section 4.4.2 below)

The MAP begins with a request made to a competent authority in accordance with paragraph 1 of Article 25. The competent authority that receives the request should first notify the person that made the request, and the competent authority of the other treaty State, that it has received the request. It should then assess whether the request meets the conditions for a valid presentation of a case and, if it does, it must determine that it is admissible (such determination that the request is admissible merely means that the request was validly presented and does not involve a decision on the merits of the objection raised in the request).

2. Unilateral stage of the consideration of the MAP case (section 4.4.3 below)

After the request has been determined to be admissible, the competent authority that received it should proceed to examine the merits of the request. At that stage, the competent authority needs to a make a preliminary assessment as to whether the objection raised by the taxpayer is justified. If it concludes that the objection appears to be justified, it should request that its tax administration make the necessary tax adjustment if that can resolve the case without the need to consult the competent authority of the other State. Otherwise, it should initiate the next step of the MAP.

3. Bilateral stage of the consideration of the MAP case (section 4.4.4 below)

If the competent authority that received the request considers it to be justified but is unable to resolve the case unilaterally, it must contact the competent authority of the other treaty State and both States must use their best efforts to seek to resolve the case through written communication and, if necessary, oral discussions.

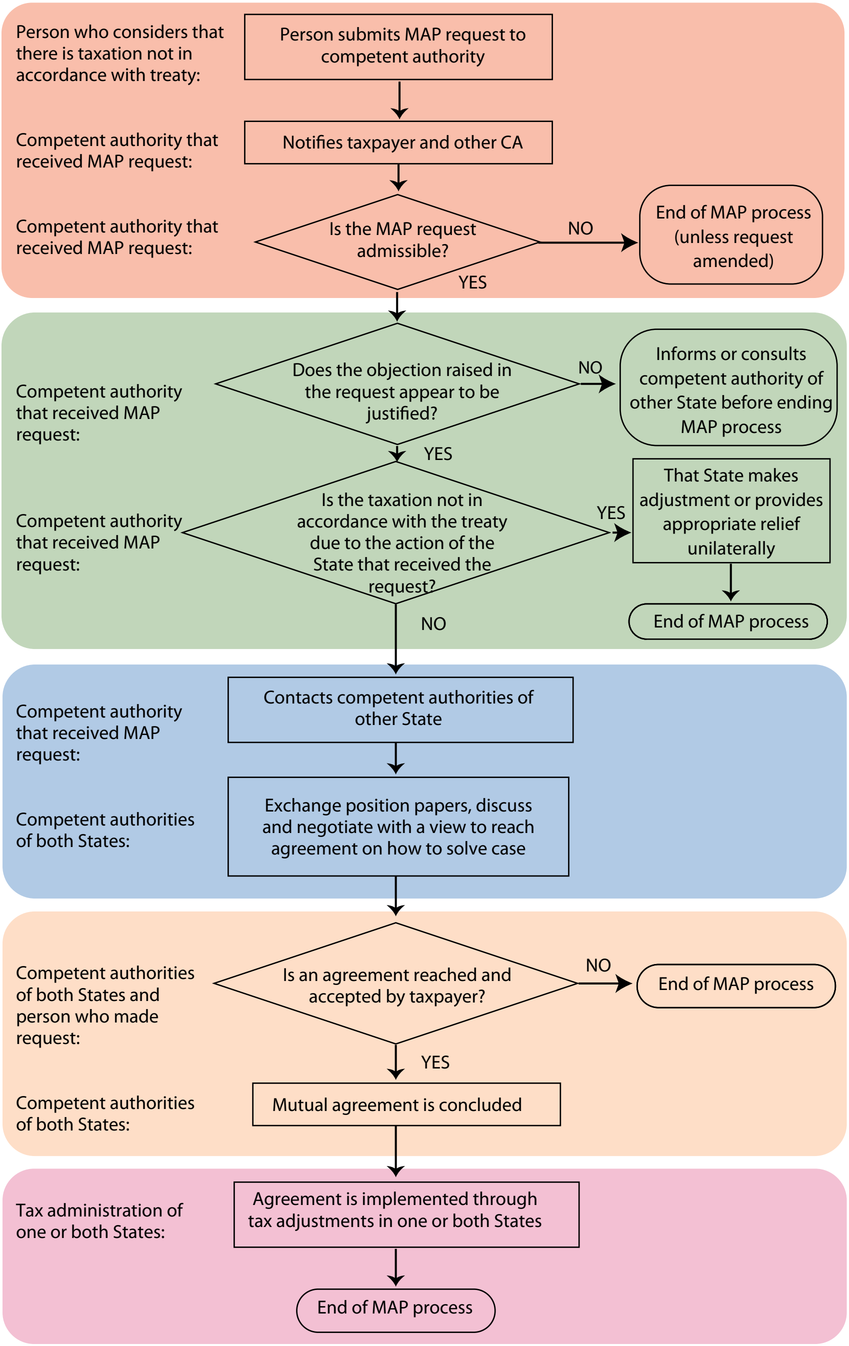
4. Conclusion of the MAP (section 4.4.5 below)

If the competent authorities are able to reach agreement, the contents of a tentative agreement are communicated to the taxpayer. If the taxpayer accepts the agreement, a mutual agreement is concluded by the competent authorities.

In the rare cases where, despite their best efforts, the competent authorities are unable to resolve the case, they should notify the taxpayer that the case has been closed without agreement.

5. Implementation of the mutual agreement (section 4.4.6 below)

Where a mutual agreement has been concluded by the competent authorities, it must be implemented by the tax administration of the State that agreed to eliminate the taxation that was not in accordance with the treaty (or by both tax administrations if the agreement requires tax adjustments in both States).


Person who considers that there is taxation not in accordance with treaty:
Person submits MAP request to competent authority
Competent authority that received MAP request:
Notifies taxpayer and other CA
Competent authority that received MAP request:
Is the MAP request admissible?
NO
End of MAP process (unless request amended)
YES
Competent authority that received MAP request:
Does the objection raised in the request appear to be justified?
NO
Informs or consults competent authority of other State before ending MAP process
YES
Competent authority that received MAP request:
Is the taxation not in accordance with the treaty due to the action of the State that received the request?
YES
That State makes adjustment or provides appropriate relief unilaterally
End of MAP process
NO
Competent authority that received MAP request:
Contacts competent authorities of other State
Competent authorities of both States:
Exchange position papers, discuss and negotiate with a view to reach agreement on how to solve case
Competent authorities of both States and person who made request:
Is an agreement reached and accepted by taxpayer?
NO
End of MAP process
YES
Competent authorities of both States:
Mutual agreement is concluded
Tax administration of one or both States:
Agreement is implemented through tax adjustments in one or both States
End of MAP process

4.4.2 The MAP request

39. The requirements for a MAP request to be validly made under paragraph 1 of Article 25, which are described in paragraph 16 above, relate to which person may make the request, to which competent authority it should be presented and when the request should be made. Each of these requirements, as well as what a MAP request should include, is discussed below.

40. As will be seen in the following paragraphs, countries sometimes apply these requirements differently and may have different views concerning what a MAP request should include. Given these differences and because most taxpayers are unfamiliar with the MAP, the tax administration of each country that has entered into a tax treaty should provide general guidance to taxpayers on the use of the MAP. The importance of doing so is recognized in paragraph 42 of the Commentary on Article 25 of the United Nations Model Tax Convention as well as in the BEPS Action 14 minimum standard, which requires countries that have joined the Inclusive Framework on BEPS to "publish rules, guidelines and procedures to access and use the MAP and take appropriate measures to make such information available to taxpayers".[34] The web site that includes the MAP profiles of these countries[35] allows easy access to the MAP information already published by some of these countries and developing countries may wish to refer to these examples in developing their own MAP guidance.

4.4.2.1 Who is allowed to make a MAP request?

41. Any person, as defined in paragraph 1(*a*) of Article 3 of the United Nations and OECD models, may make a request for MAP under paragraph 1 of Article 25 as long as that person considers that the action of either or both treaty States have resulted, or will result, in that person being taxed in a way that would not be in accordance with the provisions of the treaty. There is no requirement of a minimum amount of taxes in dispute for making a MAP request.

42. The person making a MAP request could be a natural person (i.e. an individual) or a legal person such as a company. In most cases,

34 Minimum standard 2.1 (see Annex).

35 See para. 203 below.

the person will also need to be a resident of one of the treaty States since, under Article 1 (Persons covered), the application of most treaty provisions is restricted to residents of a treaty State. Paragraph 1 of Article 25 of the United Nations Model Tax Convention, however, recognizes that a person that is a national of one of the treaty States, without necessarily being a resident of either State, may also make a MAP request based on the provisions of paragraph 1 of Article 24, which prevents discriminatory taxation based on nationality and which, under the wording of the United Nations and OECD models, applies even to persons who are not residents of the treaty States.

43. The requirement that the person consider that it has been, or will be, taxed not in accordance with the provisions of the treaty must be determined from the perspective of the taxpayer.[36] Clearly, when making a MAP request, a person does not have to provide definitive proof that taxation not in accordance with the provisions of the treaty has occurred or will occur. For the purpose of making a valid request, all that is required is that the taxpayer have a reasonable belief that this is the case based on facts that can be established.[37] Whether that belief appears to be founded or not will be determined by the competent authority that receives the request once that request has been found admissible (see section 4.4.3 below).

44. Although MAP requests frequently involve cases of double taxation, a MAP request may be made even if there is no double taxation as long as the request deals with taxation that allegedly contravenes one or more treaty provisions. For instance, cases related to the application of the non-discrimination provisions of Article 24 will often relate to situations where there is no double taxation.

45. MAP requests related to future taxation that may not be in accordance with the treaty provisions are less frequent in practice than requests dealing with taxation that has already occurred. There is no requirement that the anticipated taxation have been assessed or that tax have be paid before a MAP request is made. However, a MAP request dealing with future taxation should only be made when

36 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 14 of the Commentary on Article 25 of the OECD Model Tax Convention

37 Ibid.

taxation not in accordance with the treaty provisions appears as a risk that is not merely possible but probable. The Commentary[38] includes a few examples of such situations. One of these examples is where a State's domestic transfer pricing rules require a taxpayer to report a higher taxable income from transactions with associated enterprises than what would be required on the basis of the arm's length prices actually used in similar transactions, and it is therefore doubtful that a corresponding adjustment will be provided in a treaty State once the taxpayer is assessed by the first State.

4.4.2.2 To which competent authority should a MAP request be made?

46. Paragraph 1 of Article 25 of the United Nations Model Tax Convention requires that the MAP request be presented to the competent authority of the State of residence of the person making the request or, if the request is based on paragraph 1 of Article 24, which prevents discrimination based on nationality, to the State of which the person is a national.

47. Paragraph 1 of the OECD Model Tax Convention was modified in 2017 to allow a person to present a case to the competent authority of either State. As explained by the Commentary, this change was made in order "to ensure that the decision as to whether a case should proceed to the second stage of the mutual agreement procedure (i.e. be discussed by the competent authorities of both Contracting States) is open to consideration by both competent authorities."[39]

48. While the BEPS Action 14 minimum standard requires countries that are members of the Inclusive Framework on BEPS to include paragraph 1 of the OECD Model Tax Convention in their treaties,[40] it allows the use of the version found in the United Nations Model Tax Convention as long as the country implements "a bilateral notification or consultation process for cases in which the competent authority to which the MAP case was presented does not consider the

38 Ibid.

39 Paragraph 17 of the Commentary on Article 25 of the OECD Model Tax Convention.

40 Minimum standards 1.1 and 3.1 (see Annex).

taxpayer's objection to be justified".[41] Countries that need to comply with the minimum standard because they are members of the Inclusive Framework should implement such a notification or consultation process if they are not willing to allow their residents to present a MAP case (other than a case related to paragraph 1 of Article 24) to the competent authority of the other State.

49. A taxpayer who files a MAP request with a competent authority of a treaty State may send a copy of that request to the competent authority of the other treaty State[42] (in fact, the practice of some competent authorities is to instruct the taxpayer to provide the request to the other competent authority directly). In these cases, the request should mention that fact in order to facilitate coordination between the competent authorities.[43] A taxpayer may also rely on the competent authority that received the request to provide the request to the other competent authority (see section 4.4.2.11 below).

4.4.2.3 When should a MAP request be made?

50. Paragraph 1 of Article 25 provides that a MAP request must be presented within three years from the first notification to the taxpayer of the action by a treaty State that resulted in taxation not in accordance with the provisions of the treaty. The purpose of that time limit is to prevent tax administrations from having to address objections presented many years after the relevant tax event, when the necessary information may no longer be available.

51. Although some bilateral tax treaties provide that a MAP request must be presented within a shorter period of time (typically two years), the Commentary indicates that the three-year period should be considered as a minimum and that countries may agree on a longer period or may even omit the reference to a time limit as long as they agree that

41 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14—2015 Final Report*, chap. 1, footnote 10, at p. 22.

42 The wording of paragraph 1 in the OECD Model Tax Convention permits the request to be presented to both competent authorities at the same time: see paragraph 17 of the Commentary on Article 25 of the OECD Model Tax Convention.

43 See item (v) of the suggested contents of a MAP request, paragraph 58 below.

their domestic time limits are more favourable to the taxpayer, either because their domestic laws provide a longer limit or do not impose any time limit for such requests.[44] Countries that are members of the Inclusive Framework on BEPS, however, have committed to allow the presentation of MAP requests within a period of no less than three years[45] and could not, therefore, apply a lower time limit.

52. The "first notification of the action resulting in taxation not in accordance with the provisions of the Convention" should be interpreted in the manner most favourable to the taxpayer to avoid unduly preventing access to the MAP.[46] The "first notification of the action resulting in taxation" should therefore be interpreted as referring to the notification of the individual action concerning the taxation of a specific person, as evidenced, for instance, by a notice of assessment or an official demand for the payment of tax, as opposed to when an administrative decision that concerns a large number of taxpayers, such as a change of administrative practice concerning how to apply a certain treaty provision, has been taken. Since the practical application of this principle may raise difficulties, the Commentary illustrates its application in a number of cases,[47] including:

— *Where tax is levied by the deduction of a withholding tax at source*: the three-year period should generally begin to run upon the payment of the relevant income from which tax is withheld allegedly in contravention of the treaty. If, however, the taxpayer

44 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 20 of the Commentary on Article 25 of the OECD Model Tax Convention.

45 Minimum standard 1.1 (see Annex), as interpreted in OECD (2016), *BEPS Action 14 on More Effective Dispute Resolution Mechanisms - Peer review documents*, available at http://www.oecd.org/tax/beps/beps-action-14-on-more-effective-dispute-resolution-peer-review-documents.pdf, accessed on 12 March 2021, p. 11, para. 14.

46 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 21 of the Commentary on Article 25 of the OECD Model Tax Convention.

47 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraphs 22–24 of the Commentary on Article 25 of the OECD Model Tax Convention.

can demonstrate that it first became aware of the deduction of the tax at a later date, the beginning of the period should be determined with reference to that later date.

— *Self-assessment cases*: in such cases, there will usually be some notification of the tax payable (such as a notice of tax liability or of the denial, or reduction, of a claim for refund). The time of that notification, rather than the time when the taxpayer files its tax return, would be the starting point for the three-year period. There may be cases, however, where there is no notice of tax liability or similar notification. In such cases, the starting time of the period would be when the taxpayer would, in the normal course of events, be regarded as having been made aware of the taxation allegedly not in accordance with the Convention (e.g. when the taxpayer becomes aware of a transfer of funds representing the tax paid, such as when a bank balance or statement is made available to the taxpayer).

— *Where the taxpayer does not initially consider an action as resulting in taxation not in accordance with the treaty provisions*: the notification of the action is the starting point of the three-year period regardless of when the taxpayer becomes aware that such action may be contrary to the treaty as long as "a reasonably prudent person in the taxpayer's position would have been able to conclude at that stage that the taxation was not in accordance with the Convention". The Commentary qualifies that statement, however, as regards self-assessment cases.[48]

— *Where the taxation not in accordance with the treaty is the result of a combination of actions or decisions taken in both Contracting States:* in that case, the starting point of the time limit for presenting a MAP request should generally be determined with reference to the notification to the taxpayer of the last of the relevant actions or decisions taken by either treaty State. The

48 Where, for example, a taxpayer who filed a tax return and was assessed accordingly is subsequently informed that a judicial decision has determined that the imposition of tax in a case similar to the taxpayer's is contrary to the provisions of the treaty, the Commentary suggests that the judicial decision would be the starting point of the three-year period.

example provided by the Commentary is where the State of source levies tax not in accordance with the treaty but the State of residence initially provides relief of double taxation through the exemption or credit method. If the State of residence subsequently notifies the taxpayer that the relief is denied with the result that the taxpayer suffers double taxation, the time period should be considered to begin with the notification of the denial of relief.

53. Many countries consider that MAP requests should be initiated as soon as it appears likely that an issue will result in taxation contrary to the relevant treaty. Since paragraph 1 of Article 25 authorizes the making of a MAP request even before taxation has actually materialised (provided that such taxation is probable), taxpayers are entitled to make such early requests.[49] The early consideration of a MAP case may facilitate the identification of a pragmatic solution before the tax administration and the taxpayer have devoted significant resources to the case.

54. On the other hand, some countries may be concerned about devoting resources to a MAP case until the alleged taxation not in accordance with the treaty has materialised. Their competent authorities may also have difficulties evaluating a case before the audit function has completed its review of the facts and its analysis. While the fact that a competent authority cannot adequately evaluate a MAP case presented at an early stage may lead to a delay in the processing of the case, it would not constitute a valid reason for rejecting a MAP request that otherwise meets the requirements of paragraph 1 of Article 25.

55. Also, some countries allow taxpayers to make so-called "protective" MAP requests. These requests are typically made to ensure that the request is received within the required three-year period. The taxpayer who makes such a request agrees that the request should not be examined until further notification, which means that while the competent

49 The Commentary recognizes that a request can be made even before any action by the tax administration: see the last sentence of paragraph 21 of the Commentary on Article 25 of the OECD Model Tax Convention, as quoted in paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention.

authority may determine whether the request is admissible, it does not have to examine its merits until such notification is received.[50]

4.4.2.4 Format and contents of a MAP request

56. Article 25 does not include rules or other guidelines concerning the format and contents of a MAP request. While each competent authority may adopt the rules that it feels are appropriate or necessary for that purpose, it is important to maintain a balance between the competent authority's wish to obtain the information necessary to process the case and the need not to impose unreasonable compliance requirements on the taxpayer, which could discourage the use of the MAP.

57. To facilitate access to the MAP, the MAP guidance that a country should publish[51] should include information on how a MAP request should be presented, to whom it should be presented and what information it should include. The importance of doing so was recognized in the BEPS Action 14 minimum standard,[52] which requires countries that are members of the Inclusive Framework on BEPS to publish guidance on the information and documentation that should be submitted with a MAP request. The specific guidance on the contents and format of a MAP request that has been produced in many countries should obviously be followed in those countries.

58. The documents that were prepared for the purposes of the peer review of the compliance with the BEPS Action 14 minimum standard include the following suggestions as to the information and documentation that could be included in a MAP request.[53] While States will

50 While countries that are members of the Inclusive Framework on BEPS have committed to seek to resolve MAP cases within an average timeframe of 24 months (minimum standard 1.3; see para. 179 below), "protective" MAP requests are not taken into account for that purpose until notification is received to examine the case: OECD (2016), *BEPS Action 14 on More Effective Dispute Resolution Mechanisms — Peer review documents*, footnote 45, at p. 52.

51 See para. 40 above.

52 Minimum standard 3.2 (see Annex).

53 "Guidance on Specific Information and Documentation Required to be Submitted with a Request for MAP Assistance", in OECD (2016), *BEPS Action 14 on More Effective Dispute Resolution Mechanisms — Peer*

often have different requirements for the contents of a MAP request, the information listed below is typical of what countries would want to find in a MAP request.

Box 1: Suggested contents of a MAP request

(i) ***Identity of the taxpayer(s) covered in the MAP request***—the identity of the taxpayer(s) covered in a MAP request must be sufficiently specific to allow the competent authority to identify and contact the taxpayer(s) involved. The information provided should include the name, address, taxpayer identification number or birth date, contact details and the relationship between the taxpayers covered in the MAP request (where applicable).

(ii) ***The basis for the request***—the MAP request should state the specific tax treaty including the provision(s) of the specific article(s) which the taxpayer considers is not being correctly applied by either one or both Contracting Party (and to indicate which Party and the contact details of the relevant person(s) in that Party).

(iii) ***Facts of the case***—the MAP request should contain all the relevant facts of the case including any documentation to support these facts, the taxation years or period involved and the amounts involved (in both the local currency and foreign currency).

(iv) ***Analysis of the issue(s) requested to be resolved via MAP***—the taxpayer should provide an analysis of the issue(s) involved, including its interpretation of the application of the specific treaty provision(s), to support its basis for making a claim that the provision of the specific

Review Documents, footnote 45, page 57. Item (vi) of the list in Box 1, which refers to the situation where "the MAP request was also submitted to another authority under another Instrument that provides for a mechanism to resolve treaty-related disputes", deals with situations where a similar procedure may have been initiated under the EU Arbitration Convention or the EU Council Directive on tax dispute resolution mechanisms in the European Union (see footnote 1).

tax treaty is not correctly applied by either one or both Contracting Party. The taxpayer should support its analysis with relevant documentation (for example, documentation required under transfer pricing legislative or published guidance, copies of tax assessments, audits conducted by the tax authorities leading to the incorrectly application of the tax treaty provision).

(v) ***Whether the MAP request was also submitted to the competent authority of the other Contracting Party***—If so, the MAP request should make this clear, together with the date of such submission, the name and the designation of the person or the office to which the MAP request was submitted. A copy of that submission (including all documentations filed with that submission) should also be provided unless the contents of both MAP submissions are exactly the same.

(vi) ***Whether the MAP request was also submitted to another authority under another Instrument that provides for a mechanism to resolve treaty-related disputes***—If yes, the MAP request should clearly state so and the date of such submission, the name and the designation of the person or the office to which the MAP request was submitted, should be provided. A copy of that submission (including all documentations filed with that submission) should also be provided unless the contents of both MAP submissions are exactly the same.

(vii) ***Whether the issue(s) involved were previously dealt with***—the request should state whether the issue(s) presented in the MAP request has been previously dealt with, for example, in an advance ruling, advance pricing arrangement, settlement agreement or by any tax tribunal or court. If yes, a copy of these rulings, agreements or decisions should be provided.

(viii) ***A statement confirming that all information and documentation provided in the MAP request is accurate and that the taxpayer will assist the competent authority in its resolution of the issue(s) presented in the MAP***

request by furnishing any other information or documentation required by the competent authority in a timely manner—the request for any other information or documentation should be well-targeted and responses to the request should be complete and be submitted within the time stipulated in the request for such information or documentation.

59. The following is an example of a fictitious MAP request that would follow these suggestions and would satisfy the requirements of most countries that have published guidance on what a MAP request should include.

EXAMPLE OF A MAP REQUEST

1 November 06
Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

Subject: Request for mutual agreement procedure (MAP) under Art. 25(1) of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion*

Company XCO Inc., Tax identification number: STA-123.456.789C

For State A taxation year ending 31 December 01

Dear Ms Doe,

XCO respectfully requests the assistance of the competent authority of State A for the purposes of eliminating taxation not in accordance with the provisions of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion* (the "Treaty").

This request follows a notice of tax assessment, dated 1 September 04, that was issued to XCO by the tax administration of State B. That notice required XCO to pay SBP 835,000 (representing SBP 200,000 of corporate tax, SBP 400,000 for taxes that should have been withheld on wages and interest expenses attributable to the PE, SBP 100,000 of penalties and SBP 135,000 of interest) by 1 December 04. It related to XCO's activities in State B during State B's taxable year that ended 31 December 01. A copy of the tax assessment issued by State B is enclosed as Annex [X].

The tax assessment was based on the view that XCO had a permanent establishment in State B in B's tax year 01. The assessment required the payment of State B's corporate tax at the rate of 25 per cent on profits of SBP 840,000 which, according to the tax administration of State B, were attributable to the alleged permanent establishment. Tax of SBP 10,000 previously withheld on a rental payment made to XCO was deducted from the amount of that tax. The assessment also required the payment of SBP 400,000 on account of the tax that allegedly should have been withheld on the salaries of the employees of XCO that were attributable to the alleged permanent establishment and on the interest paid by XCO on borrowed money used for the alleged permanent establishment.

In accordance with Art. 25(1) of the treaty, XCO hereby requests that the competent authority of State A ensures that State A provides relief for the tax assessed by State B for the tax year 01. If State A is not itself able to arrive at a satisfactory solution, XCO requests that the competent authority of State A endeavour to resolve the case by mutual agreement with the competent authority of State B, with a view to the avoidance of taxation which is not in accordance with the Treaty.

IDENTIFICATION

1. *Taxpayer's name and address*: Company XCO Inc., 456 Anystreet, Capital City, State A.
2. *Assessing / adjusting tax administration*: The tax administration that issued the assessment / adjustment that triggered this request is the tax administration of State B. The office that issued the assessment is District 9 Tax Office, 444 Alienstreet, Largetown, State B.
3. *Relevant treaty article(s)*: The relevant articles of the Treaty are Articles 5 (Permanent Establishment), 7 (Business Profits), 12 (Royalties), 23 B (Credit Method), and 25 (Mutual Agreement Procedure). The provisions of these articles are identical in all respects to those of the United Nations Model Tax Convention.

4. *Taxation year(s) involved*: This request relates to the taxation year 01 (same taxation year in State A and B).
5. *Prior MAP requests*: XCO has not made a prior MAP request on this issue or any other relevant issue.
6. *Whether the MAP request was also submitted to State B:* Yes. An identical copy of this request has been sent by fax on 1 November 06 to Ms Dame Ma, Assistant-Commissioner and Competent Authority, Ministry of Finance, room 777, 8th Floor, 111 Alienstreet, Largetown, State B, fax +99 8765 4321.
7. *Relevant time limits*: As a general rule, the domestic tax law of State B does not permit a new tax assessment to be made more than 4 years after a prior assessment or the filing of a tax return for the relevant tax year: the domestic law of State B would therefore allow a new assessment if made before 1 September 08.

   As a general rule, the domestic tax law of State A does not permit any adjustment to the amount of tax payable by a person for a given taxable period more than 6 years after the end of that taxable period: the domestic law of State A would therefore allow a new assessment if made before 1 January 08.

   Art. 25(2) of the Treaty provides that a mutual agreement must be implemented notwithstanding any time limits in the domestic law of States A and B.

   Art. 25(1) of the Treaty provides that a MAP request must be presented within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Convention; in this case, the deadline for making the request is 31 August 07, which is three years after the assessment issued by State B on 1 September 04.
8. *Domestic dispute mechanisms*: On 15 October 04, XCO made a formal complaint against the tax assessment issued by the tax administration of State B. The Tax Court of State B, which is the judicial instance to which the complaint was made, will be informed of this MAP request.
9. *Applicable APAs, rulings or similar proceedings:* Not applicable.
10. *Applicable settlement or agreement with the other jurisdiction*: No agreement has been reached with the tax administration of State B concerning the issue raised in this request.

FACTS

1. XCO is a resident of State A.
2. In year 00, XCO concluded a contract with Company YCO, a resident of State B, for the dredging of a canal situated in State B that is owned and operated by Company YCO. The contract provided that the work would take place over a four-month period starting on 15 January 01 and finishing on 15 May 01. XCO is not related to Company YCO.
3. Employees of XCO arrived in State B on 10 January 01 and carried out the dredging operations in State B from 15 January 01 to 15 May 01 using various dredgers owned by XCO. Employees of XCO were therefore present in State B during a total period of 125 days during the taxation year 01.
4. After the completion of the contract and before the dredgers were shipped back to State A, XCO leased one of the dredgers to Company XCOB, a subsidiary of XCO which is a resident of State B, for a period of two months (1 June 01 to 31 July 01).
5. Company XCOB was incorporated on 15 April 01. On 15 May 01, it concluded separate dredging contracts with Company ZCO, the owner and operator of other canals situated in State B, for the dredging of some of these canals. Company XCOB began the performance of these contracts on 1 June 01 and it decided to rent one of XCO's dredgers that were already in State B while waiting for the delivery of a new dredger.
6. XCO's dredger was used in State B by Company XCOB's own employees between 1 June and 31 July 01. On 10 August it was shipped back to State A. A withholding tax of 10 per cent (SBP 10,000) was withheld by Company XCOB's on the rental payment of SBP 100,000 made to XCO, that rental payment being based on market rates for the rental of comparable dredgers between unrelated parties. The amount withheld was remitted to the tax administration of State B. A copy of the remittance receipt is enclosed as Annex [X].
7. XCO took the position that it was not liable to any additional tax in State B for the tax year 01 and, in accordance with State B's domestic law, did not file a return in State B for that year. It also took the position that since it did not have a permanent establishment in State B, it did not have any withholding tax obligations in State B

as regards the employment income of its employees who worked in State B during the taxation year 01 (see Art. 15(2) of the Treaty) and the interest payments that it made during that taxation year on money borrowed to acquire equipment used in State B (see the second sentence of Art. 11(4) of the Treaty).

8. XCO's tax return filed in State A for the taxation year 01 included the profits from its dredging contract with Company Y (SBP 800,000) and from its rental contract with Company XCOB (SBP 80,000). XCO applied against its tax liability in State A a tax credit equivalent to the lower of the tax withheld in State B and the State A tax applicable to net taxable income related to the rental payment received from Company XCOB. As shown below, the amount of that credit was SAD 5,000.

9. The definition of a permanent establishment found in the domestic law of State B provides that a foreign enterprise that carries on business activities in State B during one or more periods aggregating more than 120 days in any 12-month period is deemed to have a permanent establishment in State B in respect of these activities.

10. State B domestic tax law provides for a withholding tax of 10 per cent on payments for royalties and rental charges for the use of tangible property. Until year 05, payments for services were not subject to any withholding tax under the domestic law of State B.

11. In May 04, following an audit of Company XCOB, the tax administration of State B wrote to XCO asking why it had not filed a tax return for the taxation year 01 even though one of its dredgers was used in State B during a period of seven months (10 January to 10 August) during that year. After exchanging letters with representatives of Company XCO, the tax administration of State B took the position that Company XCO had a permanent establishment in State B in the taxation year 01 and that the profits from its contracts with companies YCO and XCOB were subject to State B's corporate tax of 25 per cent. In addition, the tax administration of State B took the position that Company XCO had improperly failed to withhold tax on salaries and interest payments that were borne by the alleged permanent establishment. Copies of the relevant correspondence are enclosed in Annex [X].

12. On 1 September 04, the tax administration of State B assessed XCO for SBP 835,000 (representing SBP 200,000 of corporate tax, SBP 400,000 for taxes that should have been withheld on wages

and interest expenses attributable to the PE, SBP 100,000 of penalties and SBP 135,000 of interest).

COMPETENT AUTHORITY ISSUES

The Taxpayer considers that the following are issues to be considered for relief by the competent authority of State A, or to be resolved by mutual agreement with the competent authority of State B:

1. Whether XCO has a permanent establishment in State B during the taxation year 01 arising from its activities therein, and in particular, whether the mere rental of a dredger to Company XCOB should be taken into account in determining the existence of a potential permanent establishment for XCO.
2. If XCO is determined to have a permanent establishment in State B, the amount of profits attributable to such a permanent establishment and the amounts of taxes that should have been withheld at source by XCO on wages and interest borne by the alleged permanent establishment.
3. If XCO is determined to have a permanent establishment in State B in the taxation year 01, the amount of foreign tax credit available in State A for the tax paid to State B to which XCO is entitled under Article 23 B of the Treaty.
4. Whether the amount of penalties and interest included in the tax assessment issued by the tax administration of State B was justified.

ANALYSIS

Issue 1: Determination of existence of a permanent establishment in State B

1. The explanations provided by the tax administration of State B suggest that the position that XCO had a permanent establishment in State B in the taxation year 01 was based primarily on three arguments.
2. The first argument (the "domestic PE" argument) was based on the presence of employees of XCO in State B for more than 120 days, which is the period of time required for a permanent establishment to exist under the domestic tax law of State B.
3. The second argument (the "183-day presence" argument) was based on the view that XCO was allegedly "present" in State B

for more than 183 days during the taxation year 01, taking into account both the presence of XCO's employees and of XCO's equipment (i.e. the dredger).

4. The third argument (the "similar activity" argument) was based on the view that the renting of the dredger during the period of June–July 01 was arguably related to the dredging operations carried out by XCO between January and May 01.

5. As explained below, we believe that these three arguments are contrary to the proper interpretation of the relevant provisions of the Treaty.

6. Since the term "permanent establishment" is defined in the Treaty, the definition of that term in the domestic tax law of State B is irrelevant for the purposes of the application of the Treaty (although the State B domestic tax law requirement must, of course, also be satisfied to permit an assessment). For that reason, the "domestic PE" argument should be rejected.

7. While the dredging of a canal could constitute a permanent establishment under Art. 5(3)*a*) of the Treaty if it constituted a construction site or installation project (see paragraph 15 of the Commentary on Article 5 of the 2017 United Nations Model Tax Convention, quoting paragraph 17 of the Commentary on Article 5 of the 2010 OECD), this would only be the case if that site or project lasted more than six months. Since XCO was only involved in dredging activities between 15 January and 10 May 01, that condition was not met.

8. The "183-day presence" argument must equally be rejected. While Art. 5(3)b) of the Treaty deems a permanent establishment to exist where services are furnished in a State during a period or periods aggregating more than 183 days in any 12-month period, this only applies if the services are furnished "through employees or other personnel engaged by the enterprise for such purpose". XCO's employees were only present in State B between 10 January and 10 May 01, a period that falls short of the required 183 days. Even if one assumes that the rental of the dredger during the June–July period could constitute a service (a view with which we disagree), such "service" could not be considered to have been furnished in State B through employees or other personnel of XCO.

9. The "similar activity" argument is equally flawed. The rental of the dredger was not connected in any way with the activities

performed in State B by XCO's employees. During our discussion with the tax administration of State B, reference was made to Art. 7(1)*c*) of the Treaty, which refers to profits attributable to "other business activities carried on in that other State of the same or similar kind as those effected through that permanent establishment". That rule, however, is not part of the definition of permanent establishment and is only relevant to determine what may be taxed by a State once a permanent establishment has been found to exist in that State under the definition in Art. 5. In addition, the leasing of equipment cannot reasonably be considered to constitute activities that are of the same or similar kind as the dredging of a canal.

Issue 2: Profit attributable to the alleged permanent establishment and taxes that should have been withheld on payments borne by the alleged permanent establishment

10. The tax administration of State B has determined that the taxable income related to the profits attributable to the alleged PE was SBP 840,000 calculated as follows:

Revenues		
Revenues from contract with YCO	2,000,000	
Revenues from rental of the dredger	100,000	
Total revenues attributable to PE	2,100,000	**2,100,000**
Expenses		
Salaries and benefits for employees	760,000	
Travel and accommodation expenses	190,000	
Fuel and maintenance	220,000	
Insurance	10,000	
Interest	15,000	
General administrative expenses	20,000	
Depreciation of dredgers	45,000	
Total expenses attributable to PE	1,260,000	1,260,000
Taxable income attributable to the PE		**840,000**

11. The profits attributable to the alleged permanent establishment would obviously depend on what constitutes the alleged

permanent establishment. In any event, we do not agree with the tax administration of State B that the income that XCO derived from the short-term rental of the dredger to XCOB should be attributed to the alleged permanent establishment or are profits attributable to "other business activities carried on in that other State of the same or similar kind as those effected through that permanent establishment" within the meaning of Art. 7(1)*c*) of the Treaty.

12. For the purposes of computing the foreign tax credit for the tax withheld on the rental payment for the dredger, the tax return for the taxation year 01 that was filed by XCO shows the following computation of the taxable income derived from State B (the average exchange rate for year 01 was 1 State A dollar (SAD) for 2 State B Pesos (SBP)):

		SBP	SAD
Revenues from rental of the dredger to XCOB		100,000	50,000
Expenses			
Insurance	4,250		
Interest	3,500		
General administrative expenses	3,750		
Depreciation of the dredger for 2 months	8,500		
	20,000	(20,000)	(10,000)
Taxable income derived from State B		**80,000**	**40,000**

13. If it is considered that XCO had a permanent establishment in State B and that the income from the rental of the dredger should be attributed to that PE, the computation of the taxable income derived from State B that needs to be made for the purposes of computing State A's foreign tax credit would be as follows (the difference with the amount calculated by State B is attributable to the different depreciation rate required by the tax laws of each State for the dredgers used in State B, different rules concerning taxable benefits for employees and to the fact that State B restricts the amount of accommodation expenses that are deductible):

Revenues (in SBP)		
Revenues from contract with YCO	2,000,000	
Revenues from rental of the dredger	100,000	
Total revenues attributable to PE	2,100,000	2,100,000
Expenses (in SBP)		
Salaries and benefits for employees	735,000	
Travel and accommodation expenses	225,000	
Fuel and maintenance	220,000	
Insurance	10,000	
Interest	15,000	
General administrative expenses	20,000	
Depreciation of dredgers	75,000	
Total expenses attributable to PE	1,300,000	1,300,000
Taxable income attributable to the PE (in SBP)		**800,000**
Taxable income attributable to the PE (in SAD)		**400,000**

14. Finally, if, contrary to the above analysis of Issue 1, it is concluded that, under Article 5 of the Treaty, XCO had a permanent establishment in State B in taxation year 01, it would be unfair to retroactively require XCO to have collected withholding tax on the wages and interest borne by the permanent establishment. The employees of XCO all took the position that no part of their salary for the taxation year 01 was taxable in State B and the tax administration of State B has not yet assessed these employees for income tax.

Issue 3: Entitlement to credit in State A for tax paid by in State B

15. If, contrary to the above analysis of Issue 1, it is concluded that, under Article 5 of the Treaty, XCO had a permanent establishment in State B in taxation year 01, XCO would be entitled to a tax credit in State A for the amount of tax paid to State B tax calculated under State B tax rules on the profits attributable to that permanent establishment as determined under Issue 2. The credit would

be limited to the amount of State A tax attributable to these profits as computed under State A tax rules.

16. The calculation of the foreign tax credit made in the tax return that XCO filed in State A for the taxation year 01 would be affected by the tax adjustment made by State B. The foreign tax credit for that year would be SAD 80,000 instead of SAD 5,000, resulting in an overpayment of SAD 75,000 which would need to be reimbursed by State A to XCO together with interest calculated from the date on which XCO filed its tax return for the taxation year 01.

Issue 4: Payment of penalties and interest

17. The tax administration of State B has imposed penalties of SBP 60,000 for failure to file a tax return for the taxation year 01 and SBP 40 000 for failure to withhold tax. It has also assessed SBP 35,000 of interest on the amount of unpaid corporate tax and withholding tax. If our position that XCO did not have a permanent establishment in State B in taxation year 01 should prevail, both the penalties and the interest should be eliminated together with the tax.

REQUEST FOR RELIEF

In light of the above, XCO requests that the competent authority of State A determine whether it considers that the tax assessment dated 1 September 04 issued by the tax administration of State B resulted in taxation in accordance with the provisions of the Treaty.

If the competent authority of State A considers that the assessment resulted in taxation in accordance with the provisions of the Treaty, XCO requests that, in accordance with Article 23 B of the Treaty, State A provide a credit to XCO against its tax liability for the tax year 01 for the additional tax imposed by State B through the assessment and that it refund to XCO the overpaid tax together with interest.

However, if the competent authority of State A considers that the assessment resulted in taxation that was not in accordance with the provisions of the Treaty, XCO requests that the competent authority of State A contact the competent Authority of State B under Art. 25(2) of the Treaty to negotiate and reach a mutual agreement that eliminates taxation not in accordance with the provisions of the Treaty together with the interest and penalties that were added to the alleged unpaid tax.

On behalf of Company XCO, I certify that all the information and documentation included in this MAP request and annexes is accurate to the best of my knowledge. XCO Inc. will assist you in the resolution of this MAP case by providing in a timely manner any relevant additional information or documentation that you may require.

For further correspondence and additional information concerning this request, please contact

Mr. John Smith
ABC LLP
HighTower, floor 13
009 Second street
Capital City
STATE A
(email at john.smith@network.com; tel: 01 23 45 67 89)

ABC LLP has been mandated by Company XCO Inc. ("XCO") to present this MAP request on its behalf. The letter authorizing ABC LLP to do so is included in Annex [X].

We appreciate your assistance in this matter.

Sincerely,

[Signed]

Ms Am Elia, director and Chief Financial Officer of XCO Inc
Company XCO Inc.
456 Anystreet,
Capital City
STATE A

[The annexes that would be attached to this request are not included]

60. The above example is merely illustrative of what a MAP request could include. In practice, MAP requests are often less elaborate. As long as a taxpayer provides the information that a country requested in its published guidance on MAP, the competent authority should not seek to deny access to the MAP on the basis that the request that was submitted did not include enough information.[54] It should rather determine that the MAP request is admissible and, if needed, request additional information from the taxpayer as part of its consideration of the case.

54 Minimum standard 3.2 (see Annex).

61. The taxpayer should make every effort to distill substantive and decisive elements of the case in its MAP request. The MAP request may follow a long and extensive audit process at the end of which an adjustment has been made. During that process, large amounts of documentation will typically have been produced, which may include evidence that is irrelevant to the MAP. Hence, it is essential for the taxpayer to select the substantive and decisive elements of the case when deciding what to discuss in the request. This is particularly important in complex transfer pricing cases.

4.4.2.5 Filing the MAP request

62. In the absence of specific rules, a taxpayer should be able to present its MAP case to the competent authority of a country in the same way that it would present other tax-related objections to the tax administration of that country. To the extent feasible and provided that confidentiality is safeguarded, tax administrations may consider it helpful to allow the electronic submission of a MAP request and other documents to be provided during the MAP.[55] This will facilitate the communication of information from the taxpayer to the competent authorities as well as between the competent authorities.

63. A competent authority will typically not charge a fee for receiving or handling a MAP request, although in some countries there may be fees associated with APA programmes.

64. A requirement to pay immediately taxes that are contested through a MAP request, or of interest and penalties on such taxes, may, if a similar requirement does not apply in the case of a domestic recourse, discourage a taxpayer from making a MAP request. This issue is discussed in section 4.4.2.9.

65. The various requirements as to how a MAP request should be made should not prevent a taxpayer from approaching a tax administration before actually filing a MAP request in order to obtain guidance on the use of the MAP. Such pre-filing contacts may allow taxpayers to learn more about the procedural aspects of the MAP. The tax administration may also learn from the taxpayer's experience with the other treaty State. Taxpayers should be mindful, however, that

55 See section 4.4.9.

such pre-filing contacts do not stop the three-year time limit for filing a formal request.

4.4.2.6 Can access to MAP be denied in certain cases?

66. While competent authorities may provide rules and procedures concerning the format and contents of a MAP request and the manner in which the request should be filed, a taxpayer cannot be prevented from making a MAP request if its case meets the requirements of paragraph 1 of Article 25. The following paragraphs illustrate this principle in relation to three situations in which access to MAP may have been questioned in the past.

Cases involving the application of anti-abuse provisions

67. The issue has sometimes arisen whether a MAP request could be made concerning the application of anti-abuse provisions, whether found in a country's domestic law (e.g. a legislative general anti-abuse rule) or in the treaty itself (e.g. the so-called "principal purpose test" rule of paragraph 9 of Article 29 of the United Nations and OECD models).

68. There is nothing in the wording of Article 25 of the United Nations and OECD models that authorizes a competent authority to deny MAP access merely because the case concerns the application of anti-abuse rules. The incorrect interpretation or application of a treaty anti-abuse rule or the application of a domestic anti-abuse rule in contravention of treaty provisions could clearly result in taxation not in accordance with treaty provisions and thus be the object of a MAP request.

69. This is confirmed in the Commentary,[56] which provides that "[i] n the absence of a special provision, there is no general rule denying perceived abusive situations going to the mutual agreement procedure". While the Commentary also notes that some countries may wish to deny access to the MAP in case of serious violations of domestic laws resulting in significant penalties, it makes it clear that this exception must be expressly provided in the treaty itself.[57]

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56 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 26 of the Commentary on Article 25 of the OECD Model Tax Convention.

57 Ibid., last sentence.

70. As part of the BEPS Action 14 minimum standard,[58] countries that are part of the Inclusive Framework on BEPS have committed to "provide MAP access in cases in which there is a disagreement between the taxpayer and the tax authorities making the adjustment as to whether the conditions for the application of a treaty anti-abuse provision have been met or as to whether the application of a domestic law anti-abuse provision is in conflict with the provisions of a treaty".[59]

71. Thus, the application of the principal purpose test of paragraph 9 of Article 29 of the United Nations and OECD models, which denies treaty benefits in cases of improper use of treaty provisions, does not prevent in any way a taxpayer from making a MAP request because it considers that the conditions of the paragraph were not met and treaty benefits should therefore have been granted. Another example is that of paragraph 3 of Article 9 of the United Nations Model Tax Convention, which applies where there has been a final ruling that one of the associated enterprises is "liable to penalty with respect to fraud, gross negligence or wilful default": the effect of the paragraph is to deny the benefits of the corresponding adjustment provisions of paragraph 2 of Article 9 and not to prevent access to the MAP, for instance where the taxpayer considers that the provisions of paragraph 3 have been incorrectly applied.

Domestic audit settlements

72. In many countries, the tax administration is allowed to negotiate with a taxpayer for the purposes of reaching an agreement that will close an audit. Since such an "audit settlement" represents the result of a negotiation process, some tax administrations may wish to restrict access to further recourses, including the mutual agreement procedure, concerning issues that are addressed in that settlement.

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58 Minimum standard 1.2 (see Annex).

59 The explanations of the minimum standard 1.2 also provide that "[i]f a country would seek to limit or deny MAP access in all or certain of these cases, it should specifically and expressly agree on such limitations with its treaty partners, which should include a requirement to notify treaty partner competent authorities about such cases and the facts and circumstances involved." OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14–2015 Final Report*, chap. 1, footnote 10, at p. 15, para. 15.

73. Since an audit settlement reached in one treaty country does not bind the other treaty country, denying access to the MAP in the case of an audit settlement could result in unrelieved double taxation. For that reason, when concluding audit settlements under their domestic law, tax administrations should not require taxpayers to renounce the right to make a MAP request.[60] This is expressly provided for in the minimum standard on BEPS Action 14, which requires countries that have joined the Inclusive Framework on BEPS to "clarify in their MAP guidance that audit settlements between tax authorities and taxpayers do not preclude access to MAP".[61]

74. For that purpose, however, it is important to distinguish an audit settlement, which is an agreement reached between the taxpayer and the part of the tax administration in charge of audits, from a negotiated settlement reached under a dispute resolution mechanism that is separate from the audit function and that can only be initiated at the request of the taxpayer. Thus, it is acceptable to restrict access to MAP in the case of the settlement of proceedings before an independent party, such as a taxpayer ombudsman, who may only address disputes initiated by the taxpayer. In that case, however, the BEPS Action 14 minimum standard would require a country that has joined the Inclusive Framework on BEPS and that has put in place such a mechanism to notify its treaty partners of that mechanism and to address the impact of that mechanism on access to MAP in its published MAP guidance.[62]

Self-initiated adjustments

75. In certain circumstances, some countries allow taxpayers to make changes to a tax return previously filed. For instance, it may be possible for a taxpayer to amend a tax return filed a few years before in order to reflect the arm's length price of a transaction entered into with an associated enterprise or of a transfer between a permanent establishment and another part of the same enterprise.

60 Paragraph 45.1 of the Commentary on Article 25 of the OECD Model Tax Convention.

61 Minimum standard 2.6 (see Annex).

62 Ibid.

76. Such a change made in good faith to reflect the arm's length principle could obviously result in double taxation to the extent that it would increase the profits taxable in one treaty country without a corresponding adjustment to the profits of the associated enterprise or the other part of the enterprise that have been taxed in the other treaty country.

77. In order to ensure that competent authorities are allowed to resolve the double taxation that could arise from such a taxpayer-initiated adjustment made in good faith, taxpayers should be allowed to access the MAP so that the primary adjustment and a possible corresponding adjustment may be discussed with the competent authority of the other treaty country. This is one of the best practices included in the final report on Action 14.[63] Although this issue is not addressed in the Commentary on the United Nations Model Tax Convention, a MAP request should not be rejected by a competent authority merely because it results from a taxpayer-initiated adjustment made in good faith as long as the request reflects the taxpayer's legitimate concern about the correct application of Article 7 or 9 in its case.

4.4.2.7 What happens if the taxpayer who requests a MAP is also pursuing domestic recourses such as a court challenge?

78. Paragraph 1 of Article 25 provides that access to MAP is available "irrespective of the remedies provided by domestic law". The MAP is a treaty-based dispute resolution mechanism that exists in addition to any recourse allowed by domestic law remedies. For that reason, nothing should prevent a taxpayer from initiating both the MAP and available domestic recourses, such as a court challenge to the action of a tax administration that the taxpayer considers to be in violation of the treaty provisions.

79. Indeed, since Article 25, as drafted in most tax treaties, does not compel the competent authorities to reach agreement under the MAP but requires them only to use their best efforts to do so, a taxpayer will often be well advised to initiate domestic law recourses, such as

63 Best practice 9 (see Annex). The same guidance appears in paragraph 14 of the Commentary on Article 25 of the OECD Model Tax Convention.

judicial or administrative proceedings, in parallel to making a MAP request. While the MAP will generally provide a comprehensive resolution of the taxpayer's case that will be binding on both treaty States, thereby ensuring that double taxation is avoided, the taxpayer should not have to take the risk that if the MAP is ultimately unsuccessful, it will be too late to initiate domestic recourses. Although such domestic recourses will only provide a solution in the State in which they are initiated, in some cases they may be sufficient to address the alleged violation of the treaty provisions.

80. While most countries will allow the MAP and domestic recourses to be initiated in parallel, they will also often want to ensure that both processes are not actively pursued simultaneously with the risk of conflicting decisions. In other words, they may require that either the MAP or the domestic recourses be pursued first. In most countries, this will be achieved by allowing the taxpayer to decide which of the MAP or the domestic recourses is pursued first and by putting the other process on hold (through the mechanisms and to the extent allowed by domestic law[64]) pending the conclusion of the process that the taxpayer chooses to pursue first. This is an area, however, where country practice varies and competent authorities are encouraged to follow the best practice, identified in the final report on BEPS Action 14,[65] of providing in their published MAP guidance[66] information on how taxpayers can coordinate the MAP process with any available domestic law remedies.

81. If a country were to allow MAP access only after a taxpayer is precluded from initiating domestic law recourses (e.g. by requiring that the taxpayer waive its right to initiate such remedies or by insisting that the MAP request be made only after the end of the period of time for initiating these remedies), the taxpayer would run the risk of losing the right to initiate domestic recourses while being unable to get a MAP solution to its case because the competent authorities cannot reach an agreement. Allowing a taxpayer to initiate both proceedings in parallel subject to choosing which process will first be actively

64 See paragraph 25 of the Commentary on Article 25 of the OECD Model Tax Convention, which discusses how this could be done.

65 Best practice 8 (see Annex).

66 See para. 40 above.

pursued avoids this issue. In practice, taxpayers will typically prefer to pursue the MAP first and suspend domestic litigation.[67] As explained below, this is due to the fact that the vast majority of countries consider that, once a judicial decision has been rendered by a domestic court in a given case, the competent authority of the country is precluded from agreeing to a different resolution of that case through the MAP.

82. Allowing the MAP and domestic recourses to be initiated in parallel while requiring one of the two processes to be actively pursued before the other may, however, give rise to the following issues.

83. Where the MAP is pursued first, most competent authorities would not want to reach a mutual agreement that the two countries would be required to implement while the taxpayer would resume its domestic recourses with the hope of getting a better outcome in one of the two countries. As explained in paragraph 156 below and as recommended in the Commentary,[68] most countries avoid this situation by requiring that the formal conclusion of a mutual agreement be conditional on the taxpayer's express acceptance of the terms of the mutual agreement within a reasonable period of time as well as on the taxpayer's withdrawal of any administrative or judicial proceedings regarding the matters dealt with in the proposed agreement.

84. In some cases, however, the taxpayer who is asked to accept a proposed mutual agreement and to terminate domestic judicial recourses may wish to defer its decision until the court delivers its decision. This issue is discussed in paragraph 160 below.

85. Where domestic law recourses are actively pursued before the MAP, the main issue that may arise is that once a final court decision is rendered, the competent authorities may consider that they do not have the legal authority, through the MAP, to deviate from the final decision of a domestic court (a question that is ultimately a matter of

67 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraphs 25 and 44 of the Commentary on Article 25 of the United Nations Model Tax Convention.

68 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 45 of the Commentary on Article 25 of the OECD Model Tax Convention.

domestic law).[69] If this is the case, the competent authority of the State in which the decision was rendered will consider itself bound by the final decision rendered by the domestic court and will be unable to reach a different conclusion through the MAP. In such circumstances, the only additional relief that the competent authority of that State could pursue for the taxpayer would be to seek relief from the competent authority of the other State. Assume, for example, that following litigation initiated by a State A company, a court of State A confirms a transfer pricing adjustment made by the State A tax administration which had the effect of increasing the profits derived by that company from a non-arm's length transaction with an associated enterprise of State B. Following that court decision, the competent authority of State A will consider that the only thing that it can do through the MAP is to try to convince State B to make a corresponding adjustment that would reflect a corresponding reduction of the profits of the enterprise of State B with an eventual refund of the tax paid in State B. The tax administration of State B will not, of course, be bound by the court decision rendered in State A. Any relief provided through the MAP in these circumstances will necessarily depend on whether the competent authority of State B agrees with the adjustment that was made by State A and which was validated by the court.

86. In order to allow taxpayers to make an informed choice as to which of the MAP or the domestic recourses should be actively pursued first, competent authorities should therefore clarify, in their published MAP guidance,[70] whether they consider themselves legally bound to follow a final domestic court decision in the context of a MAP or will not deviate from such a decision as a matter of administrative policy or practice.

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69 As noted in the Commentary (see, in particular, the last part of paragraph 42 of the Commentary on Article 25 of the OECD Model Tax Convention), in some countries a competent authority would not be legally bound to follow a court decision and would not be required to do so by administrative policy or practice. In that case, nothing would prevent such a competent authority from reaching a mutual agreement that would depart from the decision of a domestic court.

70 As suggested in the last part of best practice 8 of the final report on BEPS Action 14.

4.4.2.8 MAP request related to recurring issues

87. The taxation measure that gave rise to a MAP request for a particular taxation year or event will sometimes have relevance for other taxation years or similar events. For instance, a series of payments made over a number of years pursuant to a transaction that is the subject of a transfer pricing adjustment may give rise to issues affecting the withholding tax on each payment and to issues related to the relief of double taxation that will affect each taxation year during which these payments are made. In these situations, provided that the relevant facts and circumstances are substantially the same across the events and years concerned and that this can be verified, it will be efficient to address the recurring issue through a single MAP case covering all the relevant taxation years or similar events. This will avoid substantially similar MAP requests based on the same facts as well as the resulting waste of resources and risk of inconsistent resolutions.

88. This is recognized in the final report on BEPS Action 14. According to one of the best practices included in that report,[71] countries should put in place procedures to allow MAP requests for the resolution of recurring issues where the relevant facts and circumstances are the same (subject to verification though audit). As noted in the report, however, this would only be possible with respect to each event or taxation year for which a MAP request may still be made within the three-year period provided by paragraph 1 of Article 25.

4.4.2.9 Can taxes be collected once a MAP request has been filed?

89. Country practice varies as regards the collection of the taxes that are the object of a MAP request. Some countries seek explicit provisions in their tax treaties that oblige both competent authorities to suspend the collection of such taxes.[72] Other countries allow for the

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71 Best practice 5 (see Annex).

72 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention quotes paragraph 48 of the Commentary on Article 25 of the OECD Model Tax Convention, which suggests the following additional sentence that countries may add to paragraph 2 of Article 25 for that purpose: "Assessment and collection procedures shall be suspended during the period that any mutual agreement proceeding is pending."

suspension or deferral of the collection of such taxes either as a general administrative practice or as a negotiated arrangement with their treaty partners. Yet other countries do not provide for the suspension of the collection of taxes pending the MAP.

90. The Commentary indicates that while Article 25 does not address the question of whether MAP may be denied if the tax in dispute has not been paid, there are various reasons that support the practice of suspending the collection of tax during the MAP.[73] First, suspending or deferring collection furthers the general goal of making MAP more accessible to taxpayers. Even where the competent authorities eliminate double taxation through the MAP, the taxpayer may lose the time value of any amounts that are ultimately refunded to it if collection is not suspended during the MAP negotiation process. In addition, even where the taxpayer's pre-MAP tax payment is ultimately reimbursed as a result of a mutual agreement, the taxpayer may face a significant temporary cash-flow burden because of the obligation to make that initial payment.

91. Second, countries favouring the suspension or deferral of the taxes that are the object of a MAP believe that doing so encourages the competent authorities to negotiate and reach agreements through the MAP without delay. If a competent authority has secured the collection of the tax, it may be hesitant to make reasonable efforts to conclude a MAP with the other competent authority.

92. On the other hand, some countries prefer to nevertheless collect or allow for only partial deferral of the taxes that are the object of a MAP in order to avoid any tax collection risks.

93. One of the best practices included in the final report on Action 14 is that countries should take appropriate measures to provide for a suspension of collection procedures during the period a MAP case is pending and that, at a minimum, such a suspension of collection should be available under the same conditions applicable to a person pursuing a domestic administrative or judicial remedy.[74] As recog-

73 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraphs 46 to 48 of the Commentary on Article 25 of the OECD Model Tax Convention.

74 Best practice 6 (see Annex).

nized in the Commentary, however, the suspension of collection of tax may require legislative changes in a number of countries.[75]

94. Given the economic importance of this issue for taxpayers, countries should make public to both taxpayers and their treaty partners their position with regard to the suspension or deferral of collection of taxes that are the object of a MAP.

95. A similar issue arises with respect to the payment of interest and penalties associated with the tax that is subject to a MAP. This issue is discussed in the Commentary, which recommends that, as is the case for the payment of the tax itself, the requirements concerning the payment of interest and penalties should not be more onerous in the case of request for MAP than they are in the case of a domestic recourse.[76]

4.4.2.10 Withdrawal of a MAP request

96. While Article 25 does not expressly deal with the withdrawal of a MAP request, a taxpayer who made such a request certainly has the right to withdraw the request at any time before the procedure is completed. In fact, the MAP statistics of the Inclusive Framework on BEPS[77] show that in 2019, around 6 per cent of the MAP cases completed in that year were closed as a result of the request being withdrawn by the taxpayer. There are different reasons for which a taxpayer may want to withdraw a request previously made. In some cases, the withdrawal will simply result from the fact that the issue that was the subject of the request was resolved through domestic administrative or judicial remedies.

97. A taxpayer's withdrawal of a MAP request should not preclude a later presentation of another request dealing with the same issue if

75 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 48 of the Commentary on Article 25 of the OECD Model Tax Convention. That paragraph also includes a suggested additional sentence that countries may add to paragraph 2 of Article 25 to expressly provide for the suspension of assessment and collection procedures.

76 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 49.4 of the Commentary on Article 25 of the OECD Model Tax Convention.

77 See chap.1, footnote 7.

that issue is still unresolved, provided that the presentation of the new request is made before the applicable time limit and that the competent authorities, either at the unilateral or bilateral phase of the procedure, have not already reached a proposed conclusion that would effectively close the case.

4.4.2.11 Role of the competent authority that receives the request

98. The competent authority that receives a request made pursuant to paragraph 1 of Article 25 will normally perform two initial tasks:

- — Determine whether the request is valid and should therefore be considered admissible. While a competent authority may reject a request that does not meet the requirements of the paragraph as interpreted in its own published rules, guidelines and procedures, it does not have the discretion to reject a request that was validly made.[78] Although a valid MAP request must be considered admissible by the competent authority to which it is presented, admissibility simply means that the competent authority will subsequently undertake to examine the request on its merits and does not imply, at that initial stage, that the competent authority agrees with the taxpayer's position.
- — Notify the taxpayer and the competent authority of the other treaty State involved that it has received the request.

Is the request valid?

99. The determination of whether the request is valid is limited to determining that the request meets the requirements of paragraph 1 of Article 25 as interpreted in the country's own published rules, guidelines and procedures on MAP. This initial review of the request will usually require the competent authority to address the following questions:

- — *Was the request made in time?* As explained in section 4.4.2.3 above, paragraph 1 of Article 25 provides that a MAP request must be made within three years from the first notification of the action(s) that allegedly resulted in taxation not in accordance with

78 In many countries, the decision to reject a MAP request is an administrative decision that could, under administrative law, be subject to judicial review by a court.

the Convention. A request that is clearly made after that period would not be admissible as such. The determination of whether a request was made within the required time period will initially be based on the information included in the request and on information readily available to the competent authority. Where, however, the information provided in the request is subsequently found to be incorrect or not meeting the requirements for a valid request, the competent authority that initially considered the request to have been made within the required time will certainly be able to reject that request even if it has started to examine its merits.

— *Was the request submitted in accordance with applicable guidance?* Sections 4.4.2.4 and 4.4.2.5 above indicate that a country's published MAP guidance[79] will normally determine what should be included in a MAP request and how it should be filed.

— *Does the request contain sufficient information to understand and evaluate the taxpayer's objection?* As mentioned in paragraph 58, a country's published MAP guidance should describe the information and documentation that must be included in a MAP request. The minimum standard on BEPS Action 14, which requires countries that have joined the Inclusive Framework on BEPS to publish such guidance, recognizes that a competent authority should not prevent access to MAP "based on the argument that insufficient information was provided if the taxpayer has provided the required information."[80] At a minimum, a MAP request should include the information requested in a country's own published rules, guidelines and procedures on MAP and only the absence of such information should constitute a reason for considering that a request is invalid and should not be considered admissible.

100. When determining whether a request is valid, formalism should be avoided. A competent authority should not, for instance, determine that a MAP request is invalid merely because the request does not satisfy some minor procedural requirement.

101. Given the time limit involved for making a valid MAP request, it is crucial that a taxpayer be quickly informed whether its request

79 Para. 40 above.

80 Minimum standard 3.2 (see Annex).

has been found admissible. In the event that the MAP request is found to be inadmissible, the competent authority should inform the taxpayer of the reason(s) for the rejection. For instance, the competent authority that receives a request that lacks critical information should quickly indicate to the taxpayer what information is missing so that the taxpayer may submit a valid request before the applicable time limit.[81] Also, instead of rejecting a MAP request that does not include the necessary information, a competent authority may prefer to delay its decision until the missing information is received. When determining whether a MAP request that lacks the necessary information should be rejected, a competent authority should also keep in mind that it will always be able to require additional relevant information when examining the merits of a MAP request.

Notification that a request has been received

102. Following the submission of a MAP request, the competent authority should promptly confirm to the taxpayer that the request has been received. This should be done as soon as possible and not later than four weeks after the receipt of the request.

103. The following is an example of the notification that could be sent to the taxpayer following the receipt of the fictitious MAP request included in paragraph 59 above.

EXAMPLE OF A NOTIFICATION TO THE TAXPAYER OF THE RECEIPT OF A MAP REQUEST

10 November 06

John Smith
ABC LLP
HighTower, floor 13
009 Second street
Capital City
STATE A

81 If a request is found to be invalid, it is reasonable to consider that the taxpayer has not yet presented its case in accordance with paragraph 1 of Article 25 and is therefore still entitled to do so as long as the time for presenting a MAP request has not expired.

Subject: Request for mutual agreement procedure (MAP) under Art. 25(1) of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion made on behalf of Company XCO Inc.

Tax identification number: STA-123.456.789C

Mr. Smith,

I hereby acknowledge receipt of the request for mutual agreement procedure that you made on behalf of Company XCO Inc. for the taxation year ending 31 December 01.

As a first step, we will determine whether that request appears to have been made in accordance with our published guidance on MAP and with Art. 25(1) of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion*. As soon as a preliminary decision on this matter has been reached, we will inform you and will begin the consideration of the merits of the case.

Please note that any correspondence or additional information concerning this case should be sent directly to me at the address below.

Sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

104. In many cases, a competent authority will be able to inform the taxpayer that the request has been found admissible at the same time that it will confirm the receipt of the request. Where this is not the case, the notification of the receipt should be quickly followed by a notification of the decision as to whether the request is admissible. The following is an example of such a subsequent notification of the admissibility of the fictitious MAP request included in paragraph 59 above.

EXAMPLE OF A NOTIFICATION OF THE ADMISSIBILITY OF A MAP REQUEST

20 December 06

Mr. John Smith
ABC LLP
HighTower, floor 13
009 Second street
Capital City
STATE A

Subject: ***Request for mutual agreement procedure (MAP) under Art. 25(1) of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion made on behalf of Company XCO Inc.***

Tax identification number: STA-123.456.789C

Mr. Smith,

As a follow-up to my letter of 10 November 06 in which I acknowledged receipt of the request for mutual agreement procedure made on behalf of Company XCO Inc. for the taxation year ending 31 December 01, I wish to inform you that, based on an initial review of the information included in the request and in light of Art. 25(1) of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion* and of our published guidance on MAP, the request has been found admissible under our MAP programme. We will now review the merits of that request.

Sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

105. The competent authority that receives a MAP request should also notify the other competent authority of that receipt. The guidelines for the preparation of the MAP statistics of the Inclusive Framework on BEPS[82] recommend that this notification be given within four weeks from the receipt of the MAP request.

106. The following is an example of the notification that could be sent to the other competent authority following the receipt of the fictitious MAP request included in paragraph 59 above.

EXAMPLE OF A NOTIFICATION TO THE OTHER COMPETENT AUTHORITY OF THE RECEIPT OF A MAP REQUEST

15 November 06

Ms Dame Ma
Assistant-Commissioner and Competent Authority
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

Subject: ***Request for mutual agreement procedure (MAP) under Art. 25(1) of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion (the "Treaty") made on behalf of Company XCO Inc. (Tax identification number in State A: STA-123.456.789C)***

Dear Ms Ma,

Please be advised that we have received a MAP request from Company XCO Inc., a resident of State A, in accordance with paragraph 1 of Article 25 of the Treaty. The request alleges that a tax assessment issued to XCO Inc. by the tax administration of your country for the taxation year 01 was not in accordance with the provisions of Articles 5 and 7 of the Treaty.

82 OECD (2016), *BEPS Action 14 on More Effective Dispute Resolution Mechanisms — Peer review documents*, footnote 45, p. 33, para. 9.

I understand that a copy of the request has already been sent to you by the taxpayer (please let me know if that is not the case).

We will now proceed to determine whether the request is admissible and, if that is the case, we will examine its merits and determine whether we can provide unilateral relief. We will inform you once we have reached a decision in these matters.

Please note that any correspondence concerning this case should be sent directly to me at the address below.

I would appreciate it if you could confirm receipt of this notification as soon as possible.

Sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

107. In some cases, a competent authority will be able to determine within a very short period of time that a MAP request is admissible, that the objection included in the request appears to be justified and that it is not itself able to arrive at a satisfactory solution so as to be in a position to initiate the second stage of the MAP. In such a case, the notification of the request that the competent authority would send to the competent authority of the other State could also serve to indicate that the unilateral stage of the MAP has been completed and to initiate the bilateral stage of the MAP (see below).

4.4.3 *The unilateral stage of the consideration of the MAP case*

108. The unilateral stage of the MAP begins once the competent authority that received the MAP request has determined that it is admissible. While the competent authority of the other treaty State will have been notified of the request, it will not be directly involved in this stage of the process during which the competent authority that received the request will, according to paragraph 2 of Article 25 of the United Nations and OECD models,

- — examine the merits of the request in order to determine whether it appears to be justified and, if that is the case,
- — determine whether it can unilaterally eliminate the taxation not in accordance with the treaty provisions.

4.4.3.1 Consideration of the merits of a MAP case

109. During its examination of the merits of the request, the competent authority will review the facts and analysis presented in the MAP request. If the request relates to an action taken by its own tax administration, it will typically consult the relevant auditors or officials who took that action.

110. If, as a result of its examination of the merits of the request, the competent authority reaches the final conclusion that the taxpayer's objection is not justified, the MAP comes to an end regardless of the position that could eventually be taken by the other competent authority. Given this result, it is important that before reaching that conclusion, the competent authority be convinced that the taxpayer's objection is without merit.

111. Recognizing the risk that a competent authority might wrongly conclude that a MAP request is without merit, in particular where the request alleges that it was the action of the State that received the request that was not in accordance with the treaty provisions, the final report on BEPS Action 14 requires countries that have joined the Inclusive Framework on BEPS[83] to implement the following alternative solutions:

- — Amend the wording of their tax treaties to allow the taxpayer to present its request to the competent authority of either State,[84] or
- — Implement a process through which a competent authority that considers that a MAP request that it has received is without merit must notify or consult with the competent authority of the other treaty State involved.

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83 Minimum standard 3.1 (see para. 48 above).

84 As explained in section 4.4.2.2 above, that change was made to paragraph 1 of Article 25 of the OECD Model Tax Convention but was not made in the United Nations Model Tax Convention, which simply presents it as an option (see paragraph 9 of the Commentary on Article 25).

112. According to the final report on BEPS Action 14, this requirement seeks to ensure that the competent authorities of both treaty States "have the opportunity to provide their views on whether the MAP request should be accepted or rejected and on whether the taxpayer's objection is considered to be justified". The report makes clear, however, that the notification or consultation process that it proposes "should not be interpreted as consultation as to how to resolve the case".[85]

113. Where, notwithstanding the notification or consultation process referred to above, the competent authority that received the request reaches a final conclusion that the objection included in the request is without merit, it should notify the taxpayer that it considers that the taxation that was the object of the request did not violate the treaty provisions and close the MAP case. Such notification should include an explanation of the competent authority's conclusion.

114. The MAP statistics produced for 2019[86] indicate that such a unilateral conclusion that the objection included in the request was without merit was the outcome of only 6 per cent of the MAP cases that were closed during that year. In the vast majority of the cases that reach the unilateral stage of the MAP, therefore, the competent authority that received the request concludes that there are sufficient reasons to continue the process.

115. When considering the merits of a MAP request, a competent authority will sometimes need to obtain additional information from the taxpayer, especially where the action that led to the MAP request was taken in the other treaty State. The competent authority may also ask the taxpayer for assistance in interpreting the information provided, such as economic models and legal analyses justifying the taxpayer's application of the arm's length principle or its position on other treaty issues concerned.

116. The following illustrates a request for additional information, as well as the response from the taxpayer, in the case of the fictitious MAP request included in paragraph 59 above.

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85 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14—2015 Final Report*, chap. 1, footnote 10, at p. 22, para. 35.

86 See chap. 1, footnote 7.

EXAMPLE OF A REQUEST FOR ADDITIONAL INFORMATION

23 January 07

Mr. John Smith
ABC LLP
HighTower, floor 13
009 Second street
Capital City
STATE A

Subject: Request for additional information
Company XCO Inc., Tax identification number: STA-123.456.789C
Taxation year ending 31 December 01

Mr. Smith,

We need to obtain the following additional information in order to determine our position concerning the MAP request referenced above:

1. The changes that would need to be made to the computation of the foreign tax credit claimed by XCO Inc. in its tax return for the taxation year 01 if the tax assessment issued by the tax administration of State B on 1 September 04 were found to be in accordance with the provisions of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion.

Please send the requested information within 30 days of the date of this letter.

Please note that if we do not receive the requested information within the requested time, the processing of your MAP request will be delayed and that failure to provide the information could lead to the case being closed without further action.

Yours sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

EXAMPLE OF A RESPONSE TO A REQUEST FOR ADDITIONAL INFORMATION

15 February 07

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

Subject: Request for additional information
Company XCO Inc., Tax identification number: STA-123.456.789C

Dear Ms Doe,

This letter is in response to your letter dated 23 January 07 in which you asked us to provide additional information on the computation of the foreign tax credit to be granted by State A if the tax assessment issued by the tax administration of State B on 1 September 04 were found to be in accordance with the provisions of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion.*

If it were considered, contrary to our position, that XCO had a permanent establishment in State B and that the income from the rental of the dredger should be attributed to that PE, the computation of State A's foreign credit and of the tax payable made in our taxation year 01 tax return would need to be modified as follows:

		Paid to B (in SBP) State	Declared in 01 (in SAD)	After 04 adjustment (in SAD)
1.	Taxable income for 01		8,000,000	8,000,000
2.	Taxable income attributable to State B (as filed in 01) SBP 80 000 = SAD 40 000		40,000	–
3.	Taxable income attributable to State B (after 04 adjustment) SBP 800 000 = SAD 400 000		–	400,000

4.	Tax payable in State A at 20% (before foreign tax credit)		1,600,000	1,600,000
5.	Tax paid in State B in 01	10,000	5,000	5,000
6.	Additional tax claimed by State B in 04	200,000	--	100,000
7.	State A tax related to State B income (as filed in 01): 20% x 40 000		8,000	
8.	State A tax related to State B income (after 04 adjustment): 20% x 400 000			80,000
9.	Foreign credit: lower of State B tax (lines 5 + 6) or State A tax on State B income (line 7 or 8)		5,000	80,000
10.	Tax payable in State A (line 4 – line 9)		**1,595,000**	**1,520,000**
11.	Overpayment for 01		**75,000**	

If you need any additional information concerning the above or concerning our MAP request, please do not hesitate to contact me.

Sincerely,

[Signed]
John Smith
ABC LLP
On behalf of Company XCO Inc.

117. Circumstances may arise where a taxpayer is involved in the preparation of information that is provided separately to both competent authorities. For example, where a MAP request presented to the competent authority of one treaty State relates to a transaction between a taxpayer and a related company resident of the other treaty State and that related company has itself presented a MAP request to the competent authority of that other State in relation to the same transaction, the taxpayer may be involved in the preparation of information that is presented to the competent authority of that other State as part of that other MAP request. In such cases where information regarding the same transaction

(or set of transactions) is being provided separately to the two competent authorities, the tax authorities should urge the taxpayers involved to ensure that both sets of information are complete and fully consistent.

4.4.3.2 Can unilateral relief be provided?

118. The second part of the unilateral stage of the MAP is for the competent authority that received a request that it considers to be justified to determine whether its own tax administration can provide relief (commonly referred to as “unilateral relief”) without the need to consult the competent authority of the other State involved.

119. A typical example of unilateral relief would be where a taxpayer resident of State A makes a MAP request to the competent authority of that State because it has just been asked to pay tax in State B which, according to the treaty between States A and B, should have been paid a few years before. The request seeks to have State A grant a foreign tax credit to the taxpayer for the tax paid to State B with respect to that previous year. Assuming that the information provided to the competent authority of State A is sufficient to establish that the relevant income was taxed by State B in accordance with the treaty provisions and that tax was indeed paid to State B, the competent authority will be able to conclude that the tax administration of State A is required to provide a foreign tax credit in accordance with treaty provisions corresponding to those of Article 23 B of the United Nations Model Tax Convention.

120. Once a competent authority has determined that it should provide unilateral relief, it should promptly notify the taxpayer of its decision and inform the competent authority of the other State that the MAP case is closed as a result of its decision. The decision should then be implemented promptly. The mechanism that will be used to implement the decision with depend on the nature of the relief, on domestic law and on procedures that might have been developed by the competent authority for that purpose. That implementation will typically require coordination with other parts of the tax administration, such as the service responsible for issuing refunds.

121. The MAP statistics produced for 2019[87] indicate that unilateral relief was provided in 15 per cent of the MAP cases closed during that

87 See chap. 1, footnote 7.

year. The fact that so many MAP cases result in unilateral relief shows that competent authorities are often able to resolve MAP cases without the need to initiate the bilateral stage of the MAP.

122. In many cases, however, a competent authority will want to discuss the case with the competent authority of the other State either because it considers that the other State's tax was not levied in accordance with the treaty provisions or because it simply wants to obtain additional information or confirmation concerning the facts or analysis included in the MAP request. In these cases, the competent authority will initiate the bilateral stage of the MAP.

4.4.4 The bilateral stage of the consideration of the MAP case

4.4.4.1 Initiation of substantive discussions with the other competent authority

123. If the competent authority that received the MAP request concludes that the objection included in the request appears to be justified but that it is not able to resolve the case unilaterally, it must initiate the bilateral stage of the MAP by engaging with the competent authority of the other treaty State with the objective of jointly arriving at a satisfactory resolution of the case. This will typically be done by inviting the other competent authority to provide a position paper or by offering to do so (see the example below).

124. As noted in the Commentary,[88] once the bilateral stage of the MAP process is under way, the competent authorities need to agree on how they will communicate for the purpose of resolving the case. This will naturally depend on the nature of the case but will also depend on whether there is only one or a number of MAP cases between the two countries involved. Different methods of communication may be used for that purpose,[89] including written correspondence, informal consultations through telecommunication, meetings between officials of each country's competent authority service and, more exceptionally, appointment of a joint commission for a complicated case or a series

88 Paragraph 36 of the Commentary on Article 25 of the United Nations Model Tax Convention.

89 Paragraph 37 of the Commentary on Article 25 of the United Nations Model Tax Convention. See also section 4.4.9.

of cases.[90] Competent authorities should remain flexible and consider every method of communication.

125. In some circumstances, competent authorities of countries that have to deal with a large number of MAP cases will want to record in the form of a memorandum of understanding or similar document the bilateral procedures they have developed for the conduct of the bilateral stage of the MAP. This guidance may be broadly applicable (for example, establishing general objectives or timelines for all MAP cases) or concern a specific sub-set of MAP cases (for example, clarifying documentation requirements for transfer pricing cases). Such arrangements could help promote a consistent approach to MAP cases and advance the MAP process, especially where they free the competent authorities to focus on substantive issues rather than procedural matters.

126. An important initial step in the bilateral discussions of a MAP case is ensuring that both competent authorities are working from the same set of facts and have a common understanding of those facts. The competent authority that initiates the bilateral stage should ensure that the other competent authority has received all the information submitted by the taxpayer with the MAP request or afterwards even if that information will have been submitted by the taxpayer directly to both competent authorities (see paragraphs 49 and 117 above).

127. The following illustrates how the competent authority that received the MAP request could initiate the bilateral stage of the MAP by writing to the competent authority of the other State in the case of the fictitious MAP request included in paragraph 59 above.

EXAMPLE OF A REQUEST FOR BILATERAL DISCUSSION OF A MAP CASE

19 April 07

Ms Dame Ma
Assistant-Commissioner and Competent Authority
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

90 See paragraph 4 of Article 25 of the United Nations and OECD models.

***Subject:* MAP request from Company XCO Inc.**
State A Tax identification number: STA-123.456.789C
Taxation year ending 31 December 01

Dear Ms Ma,

This follows up on my letter dated 15 November 06 in which I informed you that we had received a MAP request on behalf of Company XCO Inc.

We have found that request admissible and our preliminary assessment of the case suggests that Company XCO's claim that it did not have a permanent establishment in State B in the taxation year 01 seems to be justified.

I would therefore appreciate receiving your position paper explaining the basis on which your tax administration considered that Company XCO had a permanent establishment in State B during taxation year 01 and explaining how the profits attributable to the alleged permanent establishment were determined.

Sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

4.4.4.2 Position paper and response

128. A key part of the bilateral stage of the MAP is for the competent authorities to exchange views as to how the treaty provisions should be interpreted and applied to the facts of the case. Each competent authority should seek to provide a reasoned and principled position on how the MAP case should be resolved and should therefore be able to present in a clear manner the treaty and domestic law basis for any relevant tax administration's action taken with respect to the taxpayer.

129. The usual practice for doing so is for one of the competent authorities to present to the other competent authority its own analysis of the MAP case in a document commonly referred to as the "position paper" and to invite the other competent authority to respond to that position paper.

130. In transfer pricing cases, the State that made the initial adjustment will typically be expected to produce the initial position paper because it will have more information concerning the basis for determining that the relevant transaction was not at arm's length. There is no settled practice, however, in non-transfer pricing cases: in some cases, the competent authority that received the MAP request will offer to present its position paper first while in others it will invite the competent authority of the treaty State that took the action(s) that triggered the MAP request to do so. Country practice varies and it is also possible that each competent authority will want to present its own position paper on the case before commenting on the position paper prepared by the other competent authority.

131. The position paper does not need to follow any specific format; the competent authority is free to structure it as it wishes. A clearly structured position paper that describes a country's position succinctly but comprehensively will facilitate a timely and satisfactory resolution of the case. Time invested in the diligent preparation of the position paper may help shorten the overall duration of the MAP.

132. The key point of reference for the preparation of a position paper should be the provisions of the tax treaty itself. The competent authority should also take account of any guidance promulgated under the treaty, such as a memorandum of understanding, exchange of notes or previous mutual agreement dealing with the meaning of a treaty term or the application of the treaty in specific circumstances. Where a MAP case relates to treaty provisions based on the United Nations and OECD models, the Commentary of these models will also constitute relevant guidance. Similarly, the guidance found in the United Nations *Practical Manual on Transfer Pricing for Developing Countries 2017* and in the OECD *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017*[91] will be relevant when dealing with transfer pricing issues.

133. When the MAP request deals with a tax measure, such as an adjustment or assessment, that originated from auditors or officials of the country of the competent authority that prepares the position paper, these auditors or officials may be consulted during the preparation of that paper.

91 See footnote 19.

134. The following is an example of a position paper based on the fictitious MAP request in paragraph 59 above.

EXAMPLE OF A POSITION PAPER

20 June 07

Subject: ***Position paper***
MAP request to State A by Company XCO Inc.
State A Tax identification number: STA-123.456.789C
Our MAP case reference: STBMAP06-12345LT

Dear Ms Doe,

This is in response to your letter of 19 April 07 in which you invited us to provide a position paper explaining the basis on which our tax administration considered that Company XCO's had a permanent establishment in State B during the taxation year 01 and explaining how the profits attributable to the alleged permanent establishment were determined.

Please note that this case has been assigned to me and that you may contact me at the address below or by email at rob.inson@fin.gov.sta or by phone at +007 12 2333 4444.

You will find attached the position paper requested.

We hope that you can agree with the conclusions in paragraph 15 of the attached position paper. If not, we would be grateful if you could set out fully the reasons why you disagree with these conclusions.

Unless you consider that a meeting is necessary to resolve this case, I look forward to receiving your response and to closing this case in the near future.

The information given in this letter is provided under the terms of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion* and its use and disclosure are governed by the provisions of that Convention.

Sincerely,

[Signed]

Mr. Robinson, Senior Analyst
State B MAP Programme Unit
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

* * *

18 June 07

MAP request to State A by Company XCO Inc.
Tax identification number in State A: STA-123.456.789C

Our MAP case reference: STBMAP06-12345LT

Position Paper by State B Competent Authority

Facts

The relevant facts of the case may be summarized as follows:

1. In year 00, XCO, a resident of State A, concluded a contract with Company YCO, a resident of State B, for the dredging of a canal situated in State B that is owned and operated by Company YCO. The contract provided that the work would take place over a four-month period starting on 15 January 01 and finishing on 15 May 01.
2. Employees of XCO arrived in State B on 10 January 01 and carried out the dredging operations in State B from 15 January 01 to 15 May 01 using different dredgers owned by XCO. Employees of XCO were in State B during a total period of 125 days during the taxation year 01.
3. After the completion of the contract and before the dredger was shipped back to State A, XCO leased one of the dredgers to Company XCOB, a subsidiary of XCO which is a resident of State B, for a period of two months (1 June 01 to 31 July 01). On 10 August 01, the dredger was shipped back to State A. A withholding tax of 10 per cent (SBP 10,000) was withheld by Company XCOB's on the rental payment of SBP 100,000 made to XCO and was remitted to the tax administration of State B.
4. XCO did not file a return in State B for the taxation year ending 31 December 01. It also took the position that it did not have any

withholding tax obligations in State B as regards the employment income of its employees who worked in State B in tax year 01 and the interest payments that it made in tax year 01 on money borrowed to acquire equipment used in State B.

5. On 1 September 04, the tax administration of State B assessed XCO for SBP 835,000 (representing SBP 200,000 of corporate tax, SBP 400,00 for taxes that should have been withheld on wages and interest expenses attributable to the PE, SBP 100,000 of penalties and SBP 135,000 of interest).

Relevant provisions of the State A–State B treaty

6. The most relevant provisions of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion (the "Treaty") are Article 12 (Royalties) and Article 12A (Fees for Technical Services). These Articles are similar to Article 12 and 12A of the *United Nations Model Double Taxation Convention between Developed and Developing Countries, 2017 version* (the United Nations Model Tax Convention).

7. Paragraph 2 of Article 12 allows taxation of royalties that arise in a Contracting State but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax cannot exceed more than 10 per cent of the gross amount of the royalties.

8. Paragraph 2 of Article 12A allows taxation of fees for technical services that arise in a Contracting State but if the beneficial owner of the fees for technical services is a resident of the other Contracting State the tax cannot exceed more than 10 per cent of the gross amount of the fees.

Relevant provisions of the domestic law of State B

9. Sec. 45 of the *Income Tax Law* of State B, as it read throughout year 01, provided for a withholding tax of 10 per cent on all payments made by residents to non-residents for royalties and rental charges for the use of tangible property.

10. While Sec. 47A of the *Income Tax Law* of State B now provides for a withholding tax of 15 per cent on all payments for services made by a resident of State B to a non-resident, that section was only enacted in year 05 and did not apply to payments made to Company XCO in taxation year 01.

11. Throughout year 01, however, Section 4 of the *Income Tax Law* of State B provided than a non-resident company that had a permanent establishment in State B was liable to tax in State B on the profits of that permanent establishment in the same manner as a company resident of State B. The definition of "permanent establishment" in Section 2 provided that "any foreign enterprise that carries on business activities in State B during one or more periods aggregating more than 120 days in any 12-month period is deemed to have a permanent establishment in State B in respect of these activities." This clearly applies to Company XCO Inc. which, in its own MAP request, indicated that its employees were present in State B for more than 120 days in year 01.

Position of State B

12. During taxation year 01, Company XCO received two different types of payments from State B residents which may be taxed by State B in accordance with the treaty:

    a. The payment of SBP 2,000,000 made by YCO for dredging services, which constitutes fees for technical services provided by XCO to YCO and as such was taxable under Article 12A of the Treaty but on which no tax was paid by XCO.

    b. The payment of SBP 100,000 made by XCOB for the rental of a dredger, which was subject to a withholding tax of 10 per cent in accordance with both Article 12 of the Treaty and Section 45 of the Income Tax Law.

13. While it is true that during the relevant taxation year, the domestic tax law of State B did not provide for a withholding tax on fees for technical services, there is nothing in Article 12A that requires that the tax provided by that Article be levied by withholding. Article 12A simply provides that State B is allowed to tax the payment of SBP 2,000,000 but that the tax shall not exceed 10 per cent of that payment (i.e. SBP 200,000). How this taxing right is exercised by State B is purely a matter of domestic law.

14. Once a tax treaty allocates taxing rights to a country, it is a matter of domestic law how these taxing rights are exercised (see, for instance, paragraph 2 of the Commentary on Article 15 of the United Nations Model Tax Convention, quoting paragraph 12.4 of the Commentary on the same Article of the OECD Model Tax Convention). Having the right to tax the payment of SBP 2,000,000

(subject to its tax not exceeding SBP 200,000), State B exercised that right with respect to taxation year 01 by taxing XCO under the provisions of its domestic tax law related to permanent establishments. In doing so, it did not apply Articles 5 and 7 of the Treaty, contrary to what the MAP request alleges. It simply used the permanent establishment rules of its domestic law rather than a more typical withholding tax mechanism when exercising the taxing rights allocated by Article 12A.

15. On the basis of the preceding analysis, we would therefore respond as follows to each of the issues raised in the MAP request:

   a. *Whether XCO had a permanent establishment in State B in tax year 01*: our answer to that question is no under the definition of permanent establishment found in the Treaty but yes under the definition of permanent establishment found in State B domestic law, which is only applicable for purposes of the domestic law application of the taxing right allocated by Article 12A of the Treaty.

   b. *If XCO is determined to have a permanent establishment in State B, the amount of profits attributable to such a permanent establishment*: this question does not arise under the

      Treaty since there is no permanent establishment for the purposes of the Treaty. Under the domestic law of State B, the profits attributable to the permanent establishment are SBP 1,445,000 (no deduction may be claimed for the wages, insurance, interest and administrative expenses shown in the calculation of profits included in the MAP request since Section 82 of the *Income Tax Law* does not allow the deduction of any payment made to a non-resident on which withholding tax was not applied). That amount is taxable at the corporate rate of 25 per cent, which means a domestic tax of SBP 361,250 but the maximum tax allowed by Article 12A of the Treaty is SBP 200,000 (i.e 10 per cent of 2,000,000).

   c. *If XCO is determined to have a permanent establishment in State B, the amount that should have been withheld at source by XCO on wages and interest borne by the alleged permanent establishment*: we agree with the analysis included in the MAP request concerning the absence of a permanent establishment under the Treaty definition of permanent establishment. For that reason, we also agree that the Treaty did not allow State B to tax the wages and interest (note, however, that, as indicated above, no deduction may be claimed for such amounts in computing the State B domestic law profits related to the contract with YCO). For that reason, we agree to reduce the tax owed by XCO by the amount of SBP 400,000 representing withholding taxes on wages and interest.

d. *If XCO is determined to have a permanent establishment in State B in tax year 01, the amount of foreign tax credit available in State A for the tax paid to State B to which XCO is entitled under* Article 23 B *of the Treaty*: based on the above analysis, XCO would be entitled to a foreign tax credit for the amount of SBP 200,000 of tax on its profits from the contract with YCO in addition to an amount of SBP 10,000 of tax on its profits from the rental payment received from XCOB.

e. *Whether the amount of penalties and interest included in the tax assessment issued by the tax administration of State B was justified:* we do not consider that penalties and interest are covered by the provisions of tax treaties, and for that reason, do not consider that these should be discussed in the context of a MAP.

135. The competent authority that receives the position paper should send a reasoned reply to the initial position paper. Ideally, that reply would include the following:

— An indication of whether a view, resolution, or proposed relief presented in the initial position paper can be accepted

— An indication of the areas or issues where the competent authorities are in agreement or disagreement

— If relevant, a request for any required additional information or clarification

— If relevant, any other additional information that would be useful for the consideration of the case but that was not presented in the initial position paper

— In case of disagreement with the resolution proposed in the initial position paper, any alternative reasoned proposal for resolution of the case

136. The following is an example of a response to the preceding position paper based on the fictitious MAP request in paragraph 59 above.

EXAMPLE OF A RESPONSE TO THE POSITION PAPER

10 July 07

Mr. Rob Inson, Senior Analyst
State B MAP Programme Unit
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

Subject: ***Response to your position paper***
MAP request to State A by Company XCO Inc.
Tax identification number: STA-123.456.789C
(Your MAP case reference: STBMAP06-12345LT)

Dear Mr. Inson,

Thank you for the position paper included in your letter of 20 June 07.

We have discussed the analysis and positions put forward in your position paper with the representative of Company XCO Inc. You will find below our response concerning your views on each of the issues raised in the MAP request.

1. *Your view that the contract with YCO generated fees for technical services taxable in State B, which State B could tax under its domestic law definition of permanent establishment even though there was no permanent establishment under the Treaty*

Based on your analysis, I accept the part of the assessment according to which an amount of SBP 200,000 of tax is owed by XCO to State B for the taxation year 01.

2. *If XCO is determined to have a permanent establishment in State B, the amount of profits attributable to such a permanent establishment*

Given my response to your views on the preceding issue, I am prepared to accept that tax payable to State B by XCO for year 01 should be limited to 200,000. I therefore do not think that we need to discuss the domestic law computation of that tax, even though I must express reservations on the part of your position paper that suggests that the wages, insurance, interest and administrative expenses shown in the calculation of profits included in the MAP request would not be deductible.

3. *If XCO is determined to have a permanent establishment in State B, the amount that should have been withheld at source by XCO on wages and interest borne by the alleged permanent establishment*

I am pleased to note your conclusion that in the absence of a permanent establishment under the Treaty, Company XCO did not have withholding tax obligations in State B with respect to the wages and interest paid in 01. We take note of your agreement to reduce the tax owed by XCO by the amount of SBP 400,000 representing withholding taxes on wages and interest.

4. *If XCO is determined to have a permanent establishment in State B in tax year 01, the amount of foreign tax credit available in State A for the tax paid to State B to which XCO is entitled under Article 23 B of the Treaty*

As indicated above, I am prepared to recognize that XCO has a corporate tax liability of SBP 200,000 in State B for taxation year 01. Upon payment of that amount, Company XCO will be entitled to a foreign tax credit for its taxation year 01 with respect to the amount of that foreign tax. The amount of the credit will, however, be limited to the amount of tax paid in State A by XCO on the profits associated to the 2,000,000 of revenues received from YCO. The computation of the additional foreign tax credit that will be granted will therefore be made based on the domestic tax law rules of State A.

5. *Whether the amount of penalties and interest included in the tax assessment issued by the tax administration of State B was justified*

On the basis of your own analysis, it seems clear to us that whereas there may be an argument for maintaining the penalty of SBP 60,000 for failure to file a tax return for 01, the penalty for failure to withhold tax should be eliminated. As regards the interest, we consider that only the interest on 200,000 of unpaid tax should be payable; there should be no interest charged on the amount of withholding tax since, by your own admission, no withholding tax was payable.

While it is true that tax treaty provisions do not address the issue of interest and penalties, this is an issue that should be addressed when you will implement the mutual agreement that will result from this case. As indicated in paragraph 4 of the Commentary on Article 2 of the United Nations Model Tax Convention, quoting paragraph 4 of the Commentary on Article 2 of the OECD Model Tax Convention: "where taxation is withdrawn or reduced in accordance with a mutual agreement under Article 25, interest and administrative penalties accessory to such taxation should be withdrawn or reduced to the extent that they are directly connected to the taxation (i.e. a tax liability) that is relieved under the mutual agreement."

Based on the preceding, I would suggest that we discuss the remaining issues of this case by phone. I would propose to schedule that call for 10.00am (Capital City time) on Tuesday 25 July. Please let me know whether this suggestion and the proposed time are acceptable to you.

Sincerely,

[Signed]

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

137. There may be cases in which such a detailed response to the initial position paper will not be necessary, e.g. if face-to-face meetings are imminent or the receiving competent authority simply informs the competent authority that produced the position paper that it completely agrees with the views and proposals put forward in the position paper.

138. Either competent authority may request additional information or clarification as the MAP discussions develop, either from each other or from the taxpayer. Such requests should be made, and responded to, as soon as practicable, given that delays in receiving additional information or clarification may delay the substantive consideration (and thus the resolution) of a MAP case. More generally, the competent authorities should endeavour to exchange all relevant information well in advance of any meetings that may be agreed to. Where both competent authorities have adequate time prior to a meeting to review the materials and to consider fully the case and issues, the competent

authorities can make the most effective use of their meeting time and the MAP consultations are more productive.

139. While there is no time limit for the conclusion of the bilateral phase of the MAP,[92] competent authorities should strive to resolve cases in a timely manner and keep the taxpayer informed of the status of its request on an on-going basis. Time will be saved, for instance, if competent authorities use a common language in all communications that do not legally require the use of a country's official language. It will also be helpful for the competent authorities to advise each other on a regular basis (for example, every three months) of their progress on a MAP case. Such regular updates should keep both competent authorities focused on the details of the case and its overall progress and should thereby facilitate its timely resolution. Also, where a competent authority encounters delays in the preparation or review of a position paper, it should inform its counterpart of the reasons for the delay and provide a projected timeframe for completion.

4.4.4.3 Treatment of interest and penalties associated with the taxes at issue in a MAP case

140. Article 25 does not directly address the treatment of any interest and penalties that are associated with the taxes at issue in a MAP. As indicated in the Commentary on Article 2 (Taxes covered), most countries do not consider that Article 2 of the United Nations and OECD models, which determines which are the taxes covered by the treaty, applies to interest and administrative penalties associated to taxes that are themselves covered by that Article. The Commentary goes on, however, to indicate that "where taxation is withdrawn or reduced in accordance with a mutual agreement under Article 25, interest and administrative penalties accessory to such taxation should be withdrawn or reduced to the extent that they are directly connected to the

92 Some treaties, however, provide for the mandatory arbitration of unresolved issues after a certain time: see paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention and the corresponding provisions of the OECD Model Tax Convention, which are discussed in Chapter 5. It should also be noted that the countries that have joined the Inclusive Framework on BEPS have committed "to seek to resolve MAP cases within an average timeframe of 24 months" (minimum standard 1.3; see Annex).

taxation (i.e. a tax liability) that is relieved under the mutual agreement."[93] This only applies, however, where the interest or penalties are computed with reference to the amount of the underlying tax liability or some other amount relevant to the determination of tax.

141. An example provided by the Commentary is where interest and administrative penalties based on the amount of a transfer pricing adjustment are imposed by a country at the time of making that transfer pricing adjustment and that adjustment is subsequently reduced or withdrawn as a result of a mutual agreement. In that case, the interest and penalties should be proportionally reduced.[94]

142. The Commentary adds that some countries may prefer to amend paragraph 2 of Article 25 to expressly provide that the competent authorities shall endeavour to agree on the application of domestic law provisions regarding interest and administrative penalties related to a MAP case.[95] In any event, as recognized by the final report on Action 14, it is a good practice for countries to make sure that their positions regarding the treatment of interest and penalties are publicly known.[96]

143. Since interest is typically calculated on the basis of the amount of tax charged, it should be relatively straightforward to determine when it is directly connected to the underlying tax liability and should therefore be withdrawn or reduced as a result of a mutual agreement. A different issue may arise where a treaty country has required the immediate payment of an amount of tax that is subject to a MAP and that amount is subsequently reduced or eliminated as a result of a

93 Paragraph 4 of the Commentary on Article 2 of the United Nations Model Tax Convention, quoting paragraph 4 of the Commentary on Article 2 of the OECD Model Tax Convention. A similar statement is included in paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 49 of the Commentary on Article 25 of the OECD Model Tax Convention.

94 Ibid.

95 Last sentence of paragraph 49.1 of the Commentary on Article 25 of the OECD Model Tax Convention, as quoted in paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention.

96 Best practice 10 (see Annex).

mutual agreement. In that case, that country should pay a reasonable amount of interest on the amount of tax that will be reimbursed to the taxpayer.[97] This will be particularly important if there are differences between the domestic law of the two treaty States on the accrual of interest on tax liabilities and refunds. Assume, for instance, that a MAP results in the confirmation of a tax liability in one country and a corresponding refund of tax in the other country. If the first country has collected the relevant tax prior to the MAP or charges interest on the late payment of that tax but the other country does not pay interest on the corresponding amount of tax refunded to the taxpayer, this will result in a substantial economic burden on the taxpayer.

144. As noted in the Commentary, countries should try to adopt flexible approaches with respect to the provision of relief for interest in the MAP. Such relief from interest is especially appropriate for the period during which the MAP is ongoing, given that the amount of time it takes to resolve a case through the MAP is, for the most part, outside the taxpayer's control. It is recognized, however, that in some cases, changes to the domestic law of a country may be required to permit the competent authority of that country to provide interest relief.[98]

145. The decision of whether to allow relief in MAP for penalties associated with taxes that are reduced or eliminated through a mutual agreement will depend on the nature of the specific penalty. Certain penalties—for example, a penalty for failure to maintain proper transfer pricing documentation—may concern domestic law compliance issues that are not connected to the tax liability that is the subject of a MAP. In the case of such penalties, as well as criminal penalties, the competent authorities may be unable or unwilling to discuss them in the MAP.[99] Competent authorities may, how-

97 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting the last part of paragraph 48 of the Commentary on Article 25 of the OECD Model Tax Convention.

98 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting the last part of paragraph 49.3 of the Commentary on Article 25 of the OECD Model Tax Convention.

99 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraphs 49.1 and 49.2 of the Commentary on Article 25 of the OECD Model Tax Convention.

ever, agree under paragraph 3 of Article 25 to reduce or withdraw any administrative penalties that are not based on the amount of the underlying tax liability where the MAP reveals that there was no cause for such penalties. For example, where a penalty has been imposed for fraud or wilful conduct and the MAP conclusion is that there was no such conduct, the penalties may be withdrawn.[100] Some countries may also be willing to provide relief from penalties through the MAP even where the adjustment that gave rise to the MAP is fully or partially sustained as a result of the MAP. A country may feel that such relief is appropriate, for example, if it appears from the MAP review that the application of the penalty is no longer justified.

4.4.4.4 Taxpayer's involvement in the MAP

146. The MAP is a government-to-government process through which issues related to the interpretation and application of tax treaties may be discussed and resolved between the competent authorities, which are the two parties involved. The taxpayer is therefore involved only in certain parts of the process, typically:[101]

- Submitting the MAP request and ensuring that both competent authorities have all of the information required to consider the case (see section 4.4.2 above)
- Offering, or responding to requests for, engagement with each competent authority as they analyse the issues at hand and prepare position papers and replies (see below), and
- Accepting or rejecting the proposed mutual agreement (see section 4.4.5 below).

147. While this reflects the general practice of most competent authorities, tax treaties do not preclude the taxpayer from participating more actively in the MAP process if competent authorities consider it appropriate. For instance, competent authorities may permit taxpayers to present briefs or make presentations to both competent authorities as part of the MAP process. These presentations may in some cases also include the taxpayer's proposals for the resolution of

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100 Ibid.

101 In some countries, domestic law may impact the extent to which a taxpayer is involved in the MAP process.

the MAP case. Both competent authorities should be encouraged to communicate with the taxpayer.

148. Providing taxpayers with appropriate opportunities to present relevant information may help both competent authorities to reach a common understanding of the facts and issues, especially in particularly complex MAP cases, and thereby improve the functioning of the MAP. Competent authorities may wish to use their published MAP guidance to make their position on taxpayer involvement known to both taxpayers and other competent authorities.

149. Even though a taxpayer will usually not be directly involved in MAP discussions, the competent authority to which a MAP request was submitted should regularly communicate with the taxpayer regarding the status of its case and of the relevant consultations. Such regular communication will encourage the taxpayer to cooperate when asked to do so (for example, by promptly submitting additional information that is requested) and will also contribute to the overall transparency of the MAP process.

4.4.5 The conclusion of the MAP

150. A MAP case typically reaches its conclusion when one of the following occurs:

— The competent authority to which the MAP request was presented considers that the actions taken by both treaty States resulted in taxation that was in accordance with the provisions of the treaty and that the request is therefore without merit

— The competent authority to which the MAP request was presented provides unilateral relief that eliminates the taxation that was not in accordance with the provisions of the treaty

— The MAP request is withdrawn by the taxpayer or becomes irrelevant because the taxation not in accordance with the provisions of the treaty has been eliminated through other mechanisms (such as a domestic court decision)

— The competent authorities of both treaty States reach a mutual agreement after a proposed agreement was presented and accepted by the taxpayer

— A proposed agreement was reached by the competent authorities and presented to the taxpayer, but the taxpayer rejected that proposed agreement

— The competent authorities conclude that they cannot reach an agreement, or the case is no longer actively pursued (e.g. as a result of inaction by the taxpayer)

151. Situations where a MAP case does not proceed to the bilateral stage of the MAP, where the request is withdrawn or where taxation not in accordance with the treaty is eliminated as a result of domestic remedies have already been dealt with. The following paragraphs address the cases where the competent authorities reach a proposed agreement and the rare cases where there is no agreement.

4.4.5.1 Proposed mutual agreement

152. When the competent authorities reach a tentative agreement in a MAP case, they should document the details of that proposed agreement in writing. Their correspondence should describe the extent to which each State will provide relief, the method of relief, when and for which period the relief will be provided as well as any other relevant details.

153. To avoid possible disagreement as to what was agreed to during the MAP discussions, facilitate the presentation of the proposed agreement to the taxpayer and expedite the implementation of the agreed solution once accepted by the taxpayer, this correspondence should take place as soon as possible after the conclusion of these discussions.

154. When the resolution of a MAP case is tentatively agreed to during a meeting that involves the discussion of a number of other cases, the proposed solution of each case completed during the meeting could be documented through the agreed minutes of the meeting.

4.4.5.2 Taxpayer's notification and acceptance of a proposed agreement

155. The taxpayer should be promptly notified of the proposed agreement. If two taxpayers are involved (which is often the case in transfer pricing MAP cases), each competent authority will typically notify the taxpayer that is its own resident. In other cases, the notification will be provided by the competent authority that received the MAP request

unless agreed otherwise. The manner in which a competent authority will provide this notification may be governed by domestic law or administrative practice. The notification may, for example, take the form of an oral presentation or of a letter providing a short description of what was tentatively agreed to. The following provides an example of a letter notifying the taxpayer of the proposed agreement reached as regards the fictitious MAP request referred to in paragraph 59 above:

EXAMPLE OF A NOTIFICATION TO THE TAXPAYER OF THE PROPOSED AGREEMENT REACHED

28 July 07

Mr. John Smith
ABC LLP
HighTower, floor 13
009 Second street
Capital City
STATE A

Subject: Proposed mutual agreement under Art. 25(2) of the Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion with respect to the MAP request made on behalf of Company XCO Inc.

Tax identification number: STA-123.456.789C

Mr. Smith,

As you are aware from our previous conversations, I have exchanged correspondence and had phone conversations with my counterpart in State B concerning the mutual agreement request referred to above.

My discussions with the competent authority of State B have allowed us to reach the following conclusions and we now consider the case to be settled, subject to your agreement:

— *Amount of 200,000 of unpaid corporate tax included in the tax assessment issued by the tax administration of State B*: Both competent authorities agree that Company XCO did not have a permanent establishment (within the meaning of the treaty) in State B during the relevant period. For the sole purpose of reaching an agreement that would eliminate double taxation, we have conceded, however, that the payment of SBP 2,000,000 made by Company YCO to Company XCO for dredging services performed in State B is taxable by State B pursuant to Article 12A of the treaty. An amount of SBP 200,000, which is the maximum amount of tax allowed by the treaty, is therefore owed by XCO to State B for the taxation year 01.

— *Amount of unpaid withholding taxes included in the tax assessment issued by the tax administration of State B:* In the absence of a permanent establishment within the meaning of the treaty, Company XCO did not have withholding tax obligations in State B with respect to the wages and interest that it paid in 01. The amount of SBP 400,000 of unpaid withholding taxes related to wages and interest paid by Company XCO that was included in the tax assessment of 4 September 04 will be withdrawn by the tax administration of State B.

— *Foreign tax credit in State A:* Upon proof of the payment to State B of 200,000 of additional tax for the taxation year 01, we will recognize that Company XCO is entitled to claim a foreign tax credit in State A for the same taxation year. That credit will correspond to the lower of the amount of SBP 200,000 (expressed in SAD at the rate applicable at the date of the payment to State B) and the amount of tax paid in State A by XCO on the profits associated to the 2,000,000 of revenues received from YCO.

I have also been informed that when implementing the above agreement, the tax administration of State B would maintain the penalty of SBP 60,000 imposed on Company XCO for failure to file a tax return in State B for taxation year 01 but the penalty of SBP 40,000 for failure to withhold tax would be withdrawn. Also, the interest of SBP 135,000 included in the assessment of 4 September 04 would be reduced so that interest would only be charged on 200,000 of unpaid tax to be calculated by the tax administration of State B from the day when the tax return for year 01 was due to be filed in State B.

I look forward to receiving written confirmation, before 6 August 07, that you agree with the terms of the above agreement and agree to terminate, or renounce to, any domestic law recourses that might still be available in States A and B concerning the issues raised by your request.

Sincerely,

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City,
STATE A

156. The Commentary on Article 25 of the United Nations Model Tax Convention indicates that "in most countries, a mutual agreement cannot be finalized before the taxpayer has given agreement and renounced domestic legal remedies."[102] In order to avoid a situation where the competent authorities would conclude a mutual agreement that would be binding on the tax administrations of the treaty States but where the taxpayer would resume or initiate judicial proceedings in order to obtain a different result in one of these States, the Commentary goes on to recommend that the conclusion of a mutual agreement be subject to the taxpayer acceptance and to the termination and relinquishment of any available domestic law recourse, such as continuing previously-suspended court proceedings on the same matters as those dealt with through the MAP,[103] even though Article 25 does not expressly require such acceptance.

157. As a general rule, a taxpayer will not be permitted to accept only parts of the proposed agreement (such as the decisions tentatively reached with respect to certain issues or certain taxable periods) unless both competent authorities agree to such a partial acceptance. Since the proposed agreement may represent a series of compromises and concessions, the competent authorities may find it unacceptable, especially in complex cases, to separate the proposed agreement into

102 Footnote 51 to the Commentary on Article 25 of the United Nations Model Tax Convention.

103 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 45 of the Commentary on Article 25 of the OECD Model Tax Convention.

different parts and to accept only some parts of the overall negotiated resolution.

158. The competent authorities may, however, wish to consider any alternative proposed resolution that the taxpayer could formulate at this stage. This could be particularly helpful where the taxpayer identifies unforeseen consequences that the proposed agreement could have. In such cases, the competent authorities will be able to modify the proposed agreement before it is finalized.

159. A taxpayer presented with the terms of a proposed agreement could obviously decide to reject it. However, the experience of countries that have substantial experience with the MAP suggests that it is very rare for a taxpayer to do so.

160. A taxpayer may also wish to defer acceptance of the proposed mutual agreement until the conclusion of ongoing judicial proceedings in one of the treaty States dealing with the same issues. While the Commentary[104] indicates that there would no grounds for rejecting a request for such a deferred acceptance, as an efficiency and administrative matter, the practice of some competent authorities is to require that the taxpayer express his acceptance or rejection of the MAP resolution within a specified number of days.[105]

161. Where the taxpayer definitively rejects the proposed agreement, the competent authorities may consider that the MAP has reached its conclusion. The competent authority to which the MAP request was presented should then formally notify the taxpayer that the MAP case has been closed. In that case, it is open to the taxpayer to resume or

104 Paragraph 9 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 42 of the Commentary on Article 25 of the OECD Model Tax Convention. The Commentary on the United Nations Model Tax Convention adds, however, that one member of the United Nations Tax Committee disagreed with that view and considered that a taxpayer should decide within a reasonable time whether to accept the proposed agreement and should not be allowed to defer acceptance until a court has delivered its decision.

105 The Commentary also notes that the competent authorities may take the view that where a taxpayer has undertaken both a MAP and judicial proceedings on the same issues, they will defer discussing the MAP case in depth until a court decision has been rendered.

initiate any domestic tax remedies that may still be available concerning the issues that were the subject of the MAP case.

162. Where the proposed agreement has been accepted by the taxpayer and, as part of that acceptance, domestic legal remedies have been terminated or relinquished, the next step is the formal conclusion of the mutual agreement by the competent authorities. This may involve an exchange of letters between the competent authorities confirming the proposed agreement. Alternatively, the proposed agreement reached between the competent authorities may have been drafted in the form of a conditional agreement subject to the acceptance of the taxpayer, which means that once this condition is met, the mutual agreement is automatically concluded.

163. The following provides an example of an exchange of letters by the competent authorities (sometimes referred to as "closing letters") concerning the agreement reached as regards the fictitious MAP request referred to in paragraph 59 above:

EXAMPLE OF A CLOSING LETTER FROM STATE A TO STATE B

8 August 07

Mr. Rob Inson, Senior Analyst
State B MAP Programme Unit
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

Subject: Closing of MAP request made by Company XCO Inc.
Tax identification number: STA-123.456.789C
Taxation year ending 31 December 0101
(Your MAP case reference: STBMAP06-12345LT)

Dear Mr. Inson,

As a follow-up to our successful conversation on 25 July 07 and to my exchange of emails with Mr. John Smith on 28 July 07, when I was informed that Company XCO accepted the proposed agreement that we reached, I would like to confirm the agreement that we have reached in the MAP case referred to above:

— *Amount of 200,000 of unpaid corporate tax included in the tax assessment issued by the tax administration of State B:* The amount of SBP 200,000 of unpaid corporate taxes that was included in the tax assessment of 4 September 04 will be maintained and a new assessment replacing the one of 4 September 04 will be issued by the tax administration of State B for that amount as well as for the revised amount of penalties and interest referred to below.

— *Amount of unpaid withholding taxes included in the tax assessment issued by the tax administration of State B:* The amount of SBP 400,000 of unpaid withholding taxes related to wages and interest paid by Company XCO that was included in the tax assessment of 4 September 04 will be withdrawn by the tax administration of State B.

— *Foreign tax credit in State A:* Upon proof of the payment to State B of 200,000 of additional tax for the taxation year 01, the tax administration of State A will recognize that Company XCO is entitled to claim a foreign tax credit in State A for the same taxation year. That credit will correspond to the lower of the amount of SBP 200,000 (expressed in SAD at the rate applicable at the date of the payment to State B) and the amount of tax paid in State A by XCO on the profits associated to the 2,000,000 of revenues received from YCO. The computation of that additional foreign tax credit will be made by the tax administration of State A on the basis of the domestic tax rules of State A.

I propose that this letter and your reply thereto constitute a mutual agreement between the competent authorities of our two States within paragraph 2 of Article 25 of the *Convention between State A and State B for the elimination of double taxation with respect to taxes on income and capital and the prevention of tax avoidance and evasion* and that this mutual agreement be implemented by both States as soon as possible.

I also understand that, in implementing that mutual agreement, the penalty of SBP 60,000 imposed on Company XCO for failure to file a tax return in State B for taxation year 01 will be maintained but the penalty of SBP 40,000 for failure to withhold tax will be withdrawn by the tax administration of State B. The interest of SBP 135,000 included in the assessment of 4 September 04 will be reduced so that interest is only charged on 200,000 of unpaid tax to be calculated by the tax administration of State B from the day when the tax return for year 01 was due to be filed in State B.

The only issue left is for us is to determine the relevant dates for the purposes of our respective MAP statistics. I would propose the dates below and would be grateful to receive your agreement or your alternative proposals.

a. Date MAP request was received from taxpayer: 1 November 06

b. Start Date: 22 November 06

c. Milestone 1: 20 June 07

d. End date: 28 July 07 (the date when we received confirmation from XCO Inc. that it accepted the proposed agreement described in our letter of 28 July)

e. Outcome of MAP: Fully resolving taxation not in accordance with tax treaty

Sincerely,

Ms Jane Doe, Delegated Competent Authority
State A Taxation Office
123 Mainstreet
Capital City
STATE A

EXAMPLE OF RESPONSE TO THE CLOSING LETTER FROM STATE A

11 August 07

Ms Jane Doe, Delegated Competent Authority
MAP Programme Unit
State A Taxation Office
123 Mainstreet
Capital City
STATE A

Subject: Closing of MAP case
MAP request to State A by Company XCO Inc.
Tax identification number: STA-123.456.789C

MAP case reference: STBMAP06-12345LT

Dear Ms Doe,

This is in response to your letter of 8 August 07 informing us that the MAP case referred to above has been closed with the following agreement, duly accepted by Company XCO, which was reached between the competent authorities of our two countries and which fully eliminates any double taxation that the taxpayer might otherwise have suffered:

— *Amount of 200,000 of unpaid corporate tax included in the tax assessment issued by the tax administration of State B:* The amount of SBP 200,000 of unpaid corporate taxes that was included in the tax assessment of 4 September 04 will be maintained and a new assessment replacing the one issued on 4 September 04 will be issued by the tax administration of State B for that amount as well as for the revised amount of penalties and interest referred to below.

— *Amount of unpaid withholding taxes included in the tax assessment issued by the tax administration of State B:* The amount of SBP 400,000 of unpaid withholding taxes related to wages and interest paid by Company XCO that was included in the tax assessment of 4 September 04 will be withdrawn by the tax administration of State B.

— *Foreign tax credit in State A:* Upon proof of the payment to State B of 200,000 of additional tax for the taxation year 01, the tax administration of State A will recognize that Company XCO is entitled to claim a foreign tax credit in State A for the same taxation year. That credit will correspond to the lower of the amount of SBP 200,000 (expressed in SAD at the rate applicable at the date of the payment to State B) and the amount of tax paid in State A by XCO on the profits associated to the 2,000,000 of revenues received from YCO. The computation of that additional foreign tax credit will be made by the tax administration of State A on the basis of the domestic tax rules of State A.

I confirm these outcomes. Our exchange of letters constitutes a mutual agreement within paragraph 2 of Article 25 of the *Convention between State A and State B for the elimination of double taxation with respect to* *taxes on income and capital and the prevention of tax avoidance and evasion* and that mutual agreement shall be implemented by both States as soon as possible.

I also confirm that, when implementing this agreement, the penalty of SBP 60,000 imposed on Company XCO for failure to file a tax return for taxation year 01 will be maintained but the penalty of SBP 40,000 for failure to withhold tax will be withdrawn. The interest of SBP 135,000 included in the assessment of 4 September 04 will be reduced so that interest is only charged on 200,000 of unpaid tax to be calculated from the day when the tax return for year 01 was due to be filed.

I finally confirm the following statistical information:

a. Date MAP request was received from taxpayer: 1 November 06

b. Start Date: 22 November 06

c. Milestone 1: 20 June 07

d. End date: 28 July 07 (the date when you received confirmation from XCO Inc. that it accepted the proposed agreement described in your letter of 28 July)

e. Outcome of MAP: Fully resolving taxation not in accordance with tax treaty

Sincerely,

Mr. Rob Inson, Senior Analyst
State B MAP Programme Unit
Ministry of Finance
Room 777, 8th Floor
111 Alienstreet
Largetown
STATE B

4.4.5.3 No agreement

164. It is relatively rare for a MAP case to result in a situation where the competent authorities are unable to reach a mutually acceptable resolution either because they disagree on substantive issues or because of inaction on the part of one or both competent authorities.

The MAP statistics produced for 2019[106] indicate that this happened in only 2 per cent of MAP cases closed during that year.

165. The competent authorities may be able to reach a partial agreement concerning some issues raised by a MAP case even though they are unable to resolve other issues arising from that case. In such a case, a partial agreement could be proposed to the taxpayer.

166. The competent authorities should formalize the closure of a MAP case that is the result of a failure to reach agreement. It is important that the taxpayer be informed that its MAP case is no longer being actively pursued since other recourses, such as domestic legal proceedings, may then be resumed or undertaken. While it is acknowledged that competent authorities may implicitly cease to pursue a MAP case without having formally decided to close the case (in particular, where the lack of progress results from the inaction of one of the competent authorities), the better course of action in these situations is for the competent authorities to formally end the MAP case to avoid undermining the reliability of the MAP and creating uncertainty for taxpayers.

4.4.6 The implementation of a mutual agreement reached through the MAP

167. As indicated in the last sentence of paragraph 2 of Article 25, there is an obligation to implement the mutual agreement reached under that paragraph regardless of any time limits that may exist under the domestic law of the treaty States.

168. The implementation of a mutual agreement should be done promptly. It will typically require that a competent authority coordinate with other parts of the tax administration, such as the service responsible for issuing refunds. The implementation of a mutual agreement will often depend on specific unilateral procedures that were developed by the competent authority for this purpose taking into account the division of responsibilities and functions within the tax administration.

169. The actions needed to implement a mutual agreement will, of course, depend on the nature of the relief to be provided to the taxpayer. In certain cases, the implementation of the agreement may

106 See chap. 1, footnote 7.

require nothing more than a refund of tax by one of the treaty States. Where, for example, a MAP case concerns the proper rate of withholding tax to be applied to a dividend payment made by a company resident of State A to a resident of State B, the mutual agreement may provide that State A should not have levied withholding tax at the rate provided by State A domestic law, but rather at the lower rate provided in the State A–State B tax treaty. Relief would therefore be provided to the State B resident through a refund by State A of the tax withheld in excess of the rate provided in the treaty.

170. A second example is where the competent authorities mutually agree that an enterprise of State A did not have a permanent establishment in State B and, accordingly, that the enterprise's business profits should not have been taxed by State B, as provided in the first sentence of paragraph 1 of Article 7 of the relevant tax treaty. In such a case, relief would typically be provided through a refund of the tax levied by State B on the relevant business profits. Since the existence of a permanent establishment may trigger other tax obligations, such as a liability for withholding taxes on interest borne by the permanent establishment,[107] the implementation of the mutual agreement may require relief beyond the refund of the tax levied on the business profits, such as the refund of the source tax on interest that would have been previously collected by State B from the enterprise because the enterprise did not withhold that tax when it made the interest payment.

171. In cases dealing with transfer pricing issues, the competent authority of a State may agree to provide relief under paragraph 2 of Article 9 following a primary transfer pricing adjustment made by the other treaty State. Such relief will often be provided through a reduction of the taxable profits of an associated enterprise of the State that must provide the corresponding adjustment, with a consequential reduction of the tax previously paid on these profits.[108]

172. For example, assume that the tax administration of State A makes a transfer pricing adjustment that increases the taxable profits

107 Under the second sentence of paragraph 5 of Article 11 of the United Nations Model Tax Convention.

108 Paragraph 7 of the Commentary on Article 9 of the United Nations Model Tax Convention, quoting paragraph 7 of the Commentary on Article 9 of the OECD Model Tax Convention.

of a company resident of State A with respect to a non-arm's length transaction with an associated enterprise of State B. If the competent authority of State B concludes a mutual agreement requiring State B to provide a corresponding adjustment to the associated enterprise of State B, the tax administration of State B will typically do so by reducing the taxable profits of the associated enterprise for the relevant taxable period. That corresponding adjustment may result in a refund of the tax previously levied by State B.

173. Paragraph 44 of the Commentary on Article 25 of the United Nations Model Tax Convention provides the following additional examples of the procedures that may be used to provide different types of reliefs that may be needed to implement a mutual agreement dealing with transfer pricing issues:

> (i) The first country may consider deferring a tax payment under the adjustment or even waiving the payment if, for example, payment or reimbursement of an expense charge by the associated enterprise is prohibited at the time because of currency or other restrictions imposed by the second country.
>
> (ii) The first country may consider steps to facilitate carrying out the adjustment and payment of a reallocated amount. Thus, if income is imputed and taxed to a parent corporation because of service to a related foreign subsidiary, the related subsidiary may be allowed, as far as the parent country is concerned, to establish on its books an account payable in favour of the parent, and the parent will not be subject to a second tax in its country on the establishment or payment of the amount receivable. Such payment should not be considered a dividend by the country of the subsidiary.
>
> (iii) The second country may consider steps to facilitate carrying out the adjustment and payment of a reallocated amount. This may, for example, involve recognition of the payment made as a deductible item, even though prior to the adjustment there was no legal obligation to pay such amount…

174. Since the last sentence of paragraph 2 of Article 25 of both the United Nations and OECD models provides that the implementation of a mutual agreement is not subject to any time limits found in the domestic law of the treaty States (for instance a time limit beyond which the tax administration could not make any tax adjustment with respect to a given tax year), the competent authority may need

to coordinate with those officials of the tax administration in charge of applying domestic time limits, such as statutes of limitation, that would otherwise prevent the adjustment of tax liabilities for previous tax years.

175. While some countries consider that the implementation of mutual agreements should be subject to the time limits of domestic law and have therefore, in their treaties, omitted the second sentence of paragraph 2 or expressly provided a time limit for the implementation of a mutual agreement,[109] it should be noted that the application of the time limits of domestic law may effectively remove the taxpayer's ability to obtain relief under the MAP. This would be the case, for example, where a late adjustment is made in one country and domestic law time limits prevent a corresponding adjustment in the other country. In any event, countries that are members of the Inclusive Framework on BEPS are, in principle, required to include the second sentence of paragraph 2 in their treaties. The BEPS Action 14 minimum standard[110] allows them, however, to depart from this requirement provided that they are willing to accept alternative treaty provisions that limit the time during which a State may make an adjustment to the profits of an enterprise under paragraph 1 of Article 9 or to the profits of a permanent establishment under paragraph 2 of Article 7.

4.4.7 Summary and timetable of the different actions involved in a MAP

176. The table included at the end of this section summarizes the different actions involved in a MAP process that were discussed in the preceding sections. It also provides a tentative timetable showing reasonable deadlines for each of these different actions.

177. While the deadline for the presentation of a valid MAP request is mandatory (pursuant to paragraph 1 of Article 25), the other deadlines included in the table are merely suggestions based on previous MAP cases or on recommendations derived from BEPS Action 14.

109 See for example, paragraph 2 of Article 26 of the Norway-Philippines tax treaty signed in 1987.

110 Minimum standard 3.3 (see Annex).

178. Unless the relevant treaty provides for the mandatory arbitration of issues that have not been resolved within a certain time,[111] there is no time limit by which a MAP case must be completed. The time required for doing so will obviously depend on many factors, including the complexity of the case, the resources available to the competent authorities and their overall caseloads. As already noted, the MAP statistics produced for 2019 show that the MAP cases completed during that year took approximately 30 months for transfer pricing cases and 22 months for other cases.[112]

179. Countries that have joined the Inclusive Framework on BEPS have committed to seek to resolve MAP cases within an average time frame of 24 months.[113] As already indicated, that commitment will be monitored through the Action 14 peer review process.[114]

180. It may also be advisable for senior officials in charge of the competent authority function to periodically review older MAP cases in order to determine the causes of the delays and to agree on any steps that could help resolve these cases. Such review may also permit the competent authorities to identify more general issues with the handling of MAP cases and areas where broader improvements may be made to their MAP programmes. In addition, the competent authorities should maintain a list of their MAP cases in which each case is identified and each action taken in relation to the case is indicated with the date on which the action occurred. Such a list provides competent authorities, especially

111 In the case of the arbitration provisions of paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention, that time is three years from the presentation of the case to the competent authority of the State to which the request was not initially made (see Chapter 5).

112 See footnote 18.

113 Minimum standard 1.3 (see Annex). The start date of that 24-month period will generally be the earlier of one week from the date when the competent authority that received the MAP request notified the other competent authority or five weeks from the receipt of the MAP request. An exception is made, however, where the MAP request does not include all the required information: see OECD (2016), *BEPS Action 14 on More Effective Dispute Resolution Mechanisms—Peer review documents*, footnote 45, at p. 36, para. 10.

114 See chap. 1, para. 13.

those that handle a large number of MAP cases, with a general view of the progress made and the delays incurred with respect to all the cases.

181. In practice, some of the actions included in the following table will be omitted or will be done simultaneously. For instance, a competent authority that receives a MAP request may be able to notify the taxpayer that is has received the request at the same time that it will indicate that the request is valid and that it needs additional information to pursue its examination of the case. A competent authority may also be able to notify the other competent authority of the request at the same time that it will provide a position paper that will initiate the bilateral stage of the MAP.

SUMMARY AND SUGGESTED TIMETABLE FOR THE ACTIONS INVOLVED IN A MAP

BY WHOM?	WHAT?	WHEN?
Person who considers that there is (or will) be taxation not in accordance with the treaty	Submits MAP request to relevant competent authority	**Mandatory deadline under Art. 25(1):** within 3 years after the first notification of the actions resulting in taxation not in accordance with the treaty
Competent authority that received the request	Notifies receipt of the request to taxpayer and competent authority of the other State	Within **4 weeks** of the receipt of the request
Competent authority of the other State	Confirms that it has received the notification that the MAP request was presented	Within **1 week** from being notified of the presentation of the MAP request
Competent authority that received the request	▪ Determination of whether a valid request was made: ▫ Examines the request in light of the conditions for a valid request ▫ Where necessary, requests additional information from person who made the request	Within **2 months** of the receipt of the request or after all necessary information for a valid request has been submitted

BY WHOM?	WHAT?	WHEN?
	▪ Determination of the admissibility of a valid request or rejection of an invalid request	
Competent authority that received the request	▪ Examination of the merits of the objection raised in the MAP request ▪ Determination of whether that objection appears to be justified ▪ Determination of whether the case may be resolved through unilateral relief to be provided by the State that received the request	Within **4 months** of the *"**start date**" of the MAP* [*"start date is the **earlier of:*** ▪ ***1 week** after notification of MAP case to other competent authority by the competent authority that received the request* ▪ ***5 weeks** after the receipt of the MAP request (unless additional information is requested within **2 months** from such receipt)*]
Tax administration of the State that received the Request	**If the competent authority determined that the case may be resolved through unilateral relief**, the tax administration makes the necessary tax adjustment	Within **3 months** after the competent authority's determination
Competent authority that received the request	**If the competent authority determined that the case cannot be resolved unilaterally** ▪ Contacts the competent authority of the other State to initiate bilateral MAP discussion ▪ Sends to the competent authority of the other State all the information necessary to process the case	Within **2 months** of the determination that the objection seems justified and that the case may not be resolved unilaterally

BY WHOM?	WHAT?	WHEN?
Competent authority of the other State	▪ May confirm that it is willing to undertake discussion of the case ▪ If necessary, requests additional information from the competent authority that received the request (which may have to be requested from the person that made the request) ▪ If there is a legitimate objection to discussing the case, may use the opportunity to inform the competent authority that received the request	Within **1 month** of being contacted
One of the competent authorities (in allocation of profit cases, typically the one that made the initial adjustment)	Sends to the competent authority of the other State a position paper stating its view of the case	Within **4 months** from *the "**start date**" of the MAP case*
Competent authority of the State that received the position paper	Sends a response to the position paper received from the competent authority of the other State	Within **6 months** of the receipt of the position paper
Competent authorities of both States	Competent authorities negotiate, with face-to-face meetings where appropriate, in order to reach an agreement on the case	Negotiation should start within 6 months after the response to the position paper, with a view to completing the case within **24 months** from the "***start date***" of the MAP case

BY WHOM?	WHAT?	WHEN?
Competent authority that received the request	▪ Notifies the person who made the MAP request of the proposed mutual agreement ▪ Request that the person indicate whether it accepts the proposed mutual agreement	Within **1 month** from the competent authorities reaching a tentative agreement
Person who made the MAP request	Person who made the MAP request indicates whether it accepts the proposed mutual agreement	Within **1 month** of the presentation of the proposed agreement
Competent authorities of both States	Competent authorities exchange letters formalizing the mutual agreement (the closing letters)	Within **1 month** of the acceptance of the tentative agreement by the person who made the request
Tax administration of the State(s) that agreed to make MAP adjustment	Implements the mutual agreement through domestic tax adjustment	Within **3 months** of the exchange of closing letters

4.4.8 The process for a MAP under paragraph 3 of Article 25

182. As already mentioned,[115] paragraph 3 of Article 25 provides for two types of MAP that are different from the taxpayer-initiated MAP under paragraph 1:

— Under the first sentence of paragraph 3, the competent authorities seek to resolve by mutual agreement issues relating to the interpretation or application of the treaty provisions. Typically, this type of MAP relates to matters of a general nature that concern a category of taxpayers and may be initiated by the competent authorities without a request from a taxpayer. For example, competent authorities may reach such a mutual agreement in order to complete or clarify the definition of a term in the tax

115 Para. 11 above.

treaty or to determine appropriate procedures for the application of specific treaty provisions (e.g. the procedures for confirming a taxpayer's status as a resident of a Contracting State, or the procedures and criteria used to grant treaty benefits to fiscally transparent entities).

— Under the second sentence of the paragraph, the competent authorities consult each other for the elimination of double taxation in cases not dealt with under the treaty, for example, where a resident of a third State has a permanent establishment in both treaty States and the double taxation concerns the profits of these two permanent establishments.

183. Where mutual agreements reached under paragraph 3 deal with issues of interpretation or application of tax treaty provisions that are relevant for all taxpayers or a category of taxpayers, the publication of such agreements, which are not specific to particular cases and should not, therefore, include any taxpayer-specific information, will serve to provide guidance and may prevent potential future disputes. As recognized in the final report on Action 14, it is therefore a good practice for countries to publish such agreements[116] (keeping in mind the need to maintain the confidentiality of taxpayer-specific information).

184. Paragraph 2 of Article 3 provides that a term that is not defined in the treaty "shall, unless the context otherwise requires" have the meaning that it has under the domestic law of the State that applies the treaty. A competent authority wishing to conclude a mutual agreement under paragraph 3 of Article 25 that would reflect an agreed meaning to be given to a term not defined in a treaty should therefore consider to what extent such agreed meaning could be applied in its country if it differed from the meaning that the term has under domestic law.

185. The case of an enterprise of a third State that has permanent establishments in both of the treaty States is the most-often cited example of double taxation not addressed by the provisions of a treaty that may be dealt with under the second sentence of paragraph 3. The following example illustrates such a case:

116 Best practice 2 (see Annex). Publication may actually be required under the domestic law of some countries.

Box 2: Application of Art. 25(3)

Company T, a resident of State T, has a permanent establishment situated in State A where it manufactures spare parts for appliances. Company T also has a permanent establishment situated in State B from which it sells these spare parts to consumers.

Spare parts are regularly shipped from the permanent establishment situated in State A to the permanent establishment situated in State B. For the purposes of determining the profits attributable to both permanent establishments, Company T treats such transfers as sales.

Following a tax audit of the activities carried on through the permanent establishment situated in State A, the tax administration of State A has increased by 30,000 the profits attributable to that permanent establishment after concluding that the arm's length price that an independent manufacturer would have charged for the sale of specific spare parts that were transferred to the other permanent establishment would have been 100,000 rather than 70,000, which is the amount shown as sales in the accounts prepared for the permanent establishment situated in State A.

Since the profits attributable to the permanent establishment in State B were computed on the basis that the cost of the spare parts transferred to that permanent establishment was 70,000, the adjustment made by the tax administration of State A results in double taxation of 30,000 of profits.

Company T being a resident of neither State A nor State B, the provisions of the treaty between these two States (and of Article 7 thereof in particular) do not apply to address that form of double taxation. Despite that fact, the second sentence of paragraph 3 of Article allows the competent authorities of States A and B to consult for the elimination of that double taxation. This will be particularly important if there is no tax treaty between one or both of these States and State T.

186. The second sentence of paragraph 3 allows the treaty States to consult each other in order to eliminate double taxation in accordance with their respective domestic laws or in accordance with a tax treaty that one of the States has concluded with a third State (such as a treaty with State T, in the example in Box 2). Although the second sentence plays an important role as it allows the competent authorities to consult each other to ensure that tax treaties operate in a coordinated and effective manner, the domestic law of some States does not allow the tax administration to provide a solution under that sentence in a case that is not explicitly or at least implicitly dealt with in the treaty.[117]

187. Paragraph 3 does not include any condition or indication as to how and when a MAP case under that paragraph should be initiated. Competent authorities may of course approach each other when and how they wish to in order to address general issues of interpretation or application of the treaty. They may also do so if they want to discuss cases concerning specific taxpayers, such as the one described in the example in Box 2.

188. However, as is the case for a taxpayer-initiated MAP under paragraph 1, any agreement reached under paragraph 3 is binding on the tax administrations and must be implemented by them (unless rescinded or replaced, in the case of an agreement of a general nature reached under the first sentence of the paragraph).

4.4.9 Communication with the other competent authority

189. The competent authorities have a lot of flexibility as regards the ways in which they may communicate in the context of a MAP under either paragraph 1 or paragraph 3 of Article 25. Paragraph 4 of the article allows them to communicate with each other directly and they can do so by letter, telephone, email, physical meeting or other means of communication; there is therefore no need to use diplomatic channels.

190. Although paragraph 4 also indicates that they may communicate "through a joint commission consisting of themselves or representatives", competent authorities that deal with few MAP cases rarely

117 Paragraph 10 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 55.1 of the Commentary on Article 25 of the OECD Model Tax Convention.

find it necessary to set up such a commission. The Commentary's explanations of how such a commission would work and, in particular, the suggestions that each delegation should be chaired by "a high official or judge chosen primarily on account of his special experience" and that the taxpayer would have "the right to make representations in writing or orally, either in person or through a representative"[118] suggest the setting up of a body that is more formal than what is typically found necessary to deal with MAP cases.

191. Despite the flexibility available as regards the manner in which the competent authorities communicate with each other, it is important to remember that to the extent that a MAP case deals with information that is confidential under domestic law, such information may only be exchanged as authorized by provisions similar to those of Article 26 (Exchange of information) of the United Nations and OECD models. Since paragraph 1 of Article 26 authorizes the exchange of information that is "foreseeably relevant for carrying out the provisions" of a tax treaty that includes the MAP article, the competent authorities acting in the context of a MAP can directly exchange confidential information.

192. It is important to remember, however, that paragraph 2 of Article 26 provides that any information exchanged between the competent authorities is required to be treated as secret in the same manner as if such information were obtained under the domestic laws of the respective States. Thus, information obtained in the context of a MAP must remain confidential. Officials performing competent authority functions should continually keep in mind this confidentiality requirement, which extends the scope of the confidentiality obligations to which they are subject under their domestic law.

193. Developing and maintaining good personal relationships with competent authorities of other countries plays an important role in ensuring successful MAP communications, especially where a large number of MAP cases between two countries require frequent exchanges between the competent authorities. The dialogue between competent authorities, and ultimately the resolution of MAP cases, will

118 Paragraph 11 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraphs 60 and 62 of the Commentary on Article 25 of the OECD Model Tax Convention.

be greatly facilitated if both sides show flexibility, fairness, openness and the ability to appreciate their counterpart's point of view, which are key ingredients for developing a relationship based on trust.[119]

4.5 How should the competent authority perform its MAP functions?

4.5.1 Organization of the MAP function

194. Tax treaties typically assign different roles to the competent authority of a State. The provisions of the United Nations Model Tax Convention provide that, apart from dealing with MAP, the competent authority is responsible for notifying the other State of significant changes made to the domestic tax law (paragraph 4 of Article 2), for the exchange of information (Article 26), for the assistance in the collection of taxes (Article 27) and for granting discretionary treaty benefits in certain circumstances (paragraphs 6 and 8(*c*) of Article 29). Some tax treaties add other responsibilities to that list. With crucial developments in the area of exchange of tax information,[120] the addition to many treaties of provisions on assistance in collection of taxes[121] and the increased number of MAP cases,[122] the importance of these different roles has increased significantly over the last decades.

195. As already noted,[123] countries are free to choose who is formally designated as competent authority and to whom the competent authority powers are delegated. For practical and administrative reasons, the

119 See Rajat Bansal, "Tax Dispute Resolution in Post BEPS World through MAP: What makes Competent Authority Relationships Tick?", in International Fiscal Association, India Branch, *Emerging International Tax Landscape*, Wolter Kluwers India, 2019, p. 135.

120 In particular, the work done under the umbrella of the *Global Forum on Transparency and Exchange of Information*: see http://www.oecd.org/tax/transparency/about-the-global-forum/, accessed on 12 March 2021.

121 The provisions of Article 27 on assistance in the collection of taxes were added to the United Nations Model Tax Convention in 2011 on the basis of provisions previously added to the OECD Model Tax Convention in 2003.

122 See chap. 1, para. 11.

123 Para. 13 above.

power and authority to perform the competent authority functions will typically be delegated to subordinate officials (the "authorized representatives") who will carry out the day-to-day functions of the competent authority.[124]

196. The administrative organization of the various competent authority functions will clearly depend on the number of tax treaties concluded and the resources needed to effectively meet the obligations assigned to the competent authority under these treaties. States that have a large MAP caseload will frequently separate the performance of the MAP responsibility from that of the other roles of the competent authority. In some States, different MAP cases will even be assigned to different offices based on the nature of the case,[125] the region, the industry or the type of taxpayer (individual, company, large taxpayer etc.). On the other hand, a State that has rarely or never been involved in MAP cases might prefer to delegate the MAP function to the officials in charge of the negotiation of tax treaties given the tax treaty knowledge of these officials.

197. In most countries, the administrative organization of the MAP function and of the MAP process is a purely administrative issue that does not require changes to domestic law: the provisions of tax treaties will provide all the necessary legal basis for dealing with MAP cases and reaching and implementing mutual agreements. As already explained,[126] however, it is important for the competent authority to provide taxpayers with information on the availability of the MAP and on the process to be followed when making a MAP request and dealing with MAP cases. This information should indicate who can request and initiate the MAP and explain the legal basis for conducting the

124 Since treaties are silent on the way this delegation should be made, it should be done in accordance with the domestic law or administrative practices of each State. This may involve regulations, an order or directive issued by the minister designated as competent authority under the treaty, or any other administrative procedure for the delegation of responsibilities to officials.

125 For instance, it is not unusual to have bilateral or multilateral advance pricing arrangements dealt with by an office that is different from the one in charge of other MAP cases.

126 Para. 40 above.

MAP, the form of the MAP request, the standard of assessment by the competent authority, the relationship with domestic dispute resolution mechanisms, the process involved in the MAP discussions, and the rights of the taxpayer in a MAP case.

198. Regardless of the administrative organization of the MAP function, it is important that the persons who will actually perform that function have sufficient authority (with sufficient safeguards to ensure accountability) to effectively negotiate with their counterparts in other treaty States and to make binding decisions with respect to the cases brought before them. Practical experience with the MAP process has shown that the efficiency and effectiveness of the MAP is enhanced if the competent authority function is delegated to senior tax officials who are actively and directly engaged in the MAP process.[127]

199. Countries with extensive practical experience with the MAP have also found that it is of fundamental importance to provide the competent authority with adequate resources. The BEPS Action 14 minimum standard requires that countries that have joined the Inclusive Framework on BEPS ensure that adequate resources are provided to the MAP function.[128]

200. Human resources, in the form of skilled personnel, will often be the most crucial factor in operating an efficient and effective MAP programme. Maintaining and developing the skills of the competent authority staff also require that a tax administration devote appropriate resources to their training.

201. Also, measures used to evaluate the work performance of officials involved in MAP cases should relate to factors such as the number of cases resolved, the time taken to resolve cases (taking into account the complexity of the cases and matters not under the control of the officials), consistency as well as principled and objective outcomes. The use of such criteria reinforces the goals and objectivity of the competent authority function and thereby improves the overall effectiveness of the MAP programme. By contrast, the evaluation of

127 Which means that officials with decision-making authority with respect to MAP cases remain informed of the details of MAP cases and are closely involved in detailed bilateral MAP discussions.

128 Minimum standard 2.5 (see Annex).

the performance of these officials should not be based on factors such as the magnitude of proposed or sustained audit adjustments or the amount of tax revenues resulting from the decisions taken through the MAP. The BEPS Action 14 minimum standard prevents countries that have joined the Inclusive Framework on BEPS from using such performance indicators,[129] which could deter a competent authority from compromising and reaching agreements.

202. In addition to having skilled personnel, the competent authority of a country should be provided with adequate financial resources to meet its obligations under that country's tax treaties. In some cases, expenses related to face-to-face meetings with other competent authorities (such as travel and accommodation expenses) may need to be incurred, although developing countries with few MAP cases may prefer to use telecommunication or, if a face-to-face meeting is necessary, may prefer to host it in order to avoid such costs. Also, while the competent authorities of developing countries may not have financial resources to pay for the translation of documents (for example, translations of contracts or foreign tax law), the taxpayer will often provide such translations.

203. It is crucial that information on how to contact the competent authority of a State be readily available. The availability of such information is needed in order to ensure that taxpayers are able to make a request under paragraph 1 of Article 25. These details should be included in the information that a country makes available on its MAP process.[130] Also, the BEPS Action 14 minimum standard requires countries that have joined the Inclusive Framework on BEPS to "publish their country MAP profiles on a shared public platform."[131] This means that the contact details of the competent authorities of a large number of countries may be accessed from a single web site.[132]

204. It is also crucial that the officials in charge of dealing with MAP cases implement a reliable system of internal recordkeeping that facilitates access to information concerning MAP requests received, MAP

129 Minimum standard 2.4 (see Annex).

130 Para. 40 above.

131 Minimum standard 2.2 (see Annex).

132 These MAP profiles are available at http://www.oecd.org/tax/dispute/country-map-profiles.htm, accessed on 12 March 2021.

cases currently under discussion and previously completed MAP cases while ensuring the confidentiality of the relevant information. Such recordkeeping should, among other things, allow the monitoring of the progress of MAP cases, thereby facilitating compliance with the target deadlines for the various actions involved in a MAP case. They should also facilitate the preparation of the MAP statistics that the BEPS Action 14 minimum standard requires from the countries that have joined the Inclusive Framework on BEPS.[133] Internal records of previous MAP cases facilitate the processing of similar cases and contribute to the consistent interpretation of a treaty where the issues and material facts are the same.

205. Competent authorities, while often part of the tax administration, need a high degree of independence from the audit and review functions to be effective. Competent authorities have to make decisions on both factual and legal questions in the cases they are dealing with and have to focus primarily on the resolution of cases that involve taxation not in accordance with tax treaty provisions. Typically, they will have to rely on the cooperation of other parts of the tax administration, such as the audit department that examined the facts of the case in the first place. A good internal communication is therefore crucial for the effectiveness of the competent authority function.

206. While the relationship between the competent authority and the audit and tax adjustment functions will generally not be hierarchical, it should be clear that the competent authority is not constrained by the positions adopted by officials performing these functions (e.g. auditors, assessors or inspectors).

207. The specific circumstances of developing countries will obviously need to be taken into account in the organization of the MAP function:

— Given their limited resources, tax administrations of developing countries may be reluctant to divert resources to the MAP function, especially since this function requires skilled personnel and may also require financial resources (e.g. to cover travel expenses). The fact that these countries are typically involved in very few MAP cases,[134] however, suggests that an efficient

133 Minimum standard 1.5 (see Annex).

134 See chap. 1, para. 11.

approach would be to allocate the MAP function to the officials in charge of treaty negotiations, who are familiar with treaty provisions and with dealing with foreign tax officials. Officials involved in MAP cases will learn and develop specific skills most significantly through actual work on such cases. Having no experience in dispute resolution should not result in rejecting the cases for the lack of such experience.

— In order for competent authorities of developing countries to have the ability and power to negotiate with other competent authorities and implement mutual agreements domestically, responsible politicians and high-ranking officials may need to back the MAP, recognizing that positive effects on the revenues will mostly materialise indirectly through a better investment climate, even though it will be difficult to measure these effects.

— The proper application of transfer pricing rules and tax treaties by the tax administration is important to a successful MAP. The application of domestic law and tax treaties in a manner consistent with global standards will not only reduce disputes but will also facilitate the work of the competent authority. A MAP case involving a transfer pricing dispute is only as strong as the inputs from the domestic transfer pricing team during the transfer pricing audit or study.

4.5.2 How should a competent authority approach a MAP case?

208. The competent authority of a treaty State that is involved in a MAP represents that State in matters related to the interpretation or application of the relevant tax treaty.

209. In broad terms, the role of the competent authority in the MAP is to ensure that a tax treaty is properly applied and to endeavour in good faith to resolve any issues that may arise in the application and interpretation of the treaty provisions.

210. When addressing a MAP case, the competent authority is to be guided first by the terms of the treaty itself and the relevant provisions of domestic law; it should not be influenced by opinions on whether or not the treaty or the law reflects an appropriate tax policy and whether or not these should be amended.

211. Competent authorities should make every effort to resolve cases in a principled, fair and objective manner, deciding each case on its own merits and not with reference to revenue considerations or an overall balance of results. Moreover, competent authorities should strive to be consistent in their approach to an issue, regardless of the State that benefits from that approach in a particular case and regardless of the position taken by colleagues who have produced the disputed tax adjustment. Notwithstanding disagreements on facts or principles, competent authorities should seek and be able to compromise in order to reach a mutual agreement.

ANNEX

Action 14: The Minimum Standard and Best Practices on the Resolution of Treaty-Related Disputes through the MAP[135]

Minimum Standard

1. Countries should ensure that treaty obligations related to the mutual agreement procedure are fully implemented in good faith and that MAP cases are resolved in a timely manner

1.1 Countries should include paragraphs 1 through 3 of Article 25 in their tax treaties, as interpreted in the Commentary and subject to the variations in these paragraphs provided for under elements 3.1 and 3.3 of the minimum standard; they should provide access to MAP in transfer pricing cases and should implement the resulting mutual agreements (e.g. by making appropriate adjustments to the tax assessed).

1.2 Countries should provide MAP access in cases in which there is a disagreement between the taxpayer and the tax authorities making the adjustment as to whether the conditions for the application of a treaty anti-abuse provision have been met or as to whether the application of a domestic law anti-abuse provision is in conflict with the provisions of a treaty.

1.3 Countries should commit to a timely resolution of MAP cases: countries commit to seek to resolve MAP cases within an average timeframe of 24 months. Countries' progress toward meeting that target will be periodically reviewed on the basis of the statistics prepared in accordance with the agreed reporting framework referred to in element 1.5.

1.4 Countries should enhance their competent authority relationships and work collectively to improve the effectiveness

135 OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14 – 2015 Final Report*, chap. 1, footnote 10.

of the MAP by becoming members of the Forum on Tax Administration MAP Forum (FTA MAP Forum).

1.5 Countries should provide timely and complete reporting of MAP statistics, pursuant to an agreed reporting framework to be developed in co-ordination with the FTA MAP Forum.

1.6 Countries should commit to have their compliance with the minimum standard reviewed by their peers in the context of the FTA MAP Forum.

1.7 Countries should provide transparency with respect to their positions on MAP arbitration.

2. Countries should ensure that administrative processes promote the prevention and timely resolution of treaty-related disputes

2.1 Countries should publish rules, guidelines and procedures to access and use the MAP and take appropriate measures to make such information available to taxpayers. Countries should ensure that their MAP guidance is clear and easily accessible to the public.

2.2 Countries should publish their country MAP profiles on a shared public platform (pursuant to an agreed template to be developed in co-ordination with the FTA MAP Forum).

2.3 Countries should ensure that the staff in charge of MAP processes have the authority to resolve MAP cases in accordance with the terms of the applicable tax treaty, in particular without being dependent on the approval or the direction of the tax administration personnel who made the adjustments at issue or being influenced by considerations of the policy that the country would like to see reflected in future amendments to the treaty.

2.4 Countries should not use performance indicators for their competent authority functions and staff in charge of MAP processes based on the amount of sustained audit adjustments or maintaining tax revenue.

2.5 Countries should ensure that adequate resources are provided to the MAP function.

2.6 Countries should clarify in their MAP guidance that audit settlements between tax authorities and taxpayers do not preclude access to MAP. If countries have an administrative or statutory dispute settlement/resolution process independent from the audit and examination functions and that can only be accessed through a request by the taxpayer, countries may limit access to the MAP with respect to the matters resolved through that process. Countries should notify their treaty partners of such administrative or statutory processes and should expressly address the effects of those processes with respect to the MAP in their public guidance on such processes and in their public MAP programme guidance.

2.7 Countries with bilateral advance pricing arrangement (APA) programmes should provide for the roll-back of APAs in appropriate cases, subject to the applicable time limits (such as statutes of limitation for assessment) where the relevant facts and circumstances in the earlier tax years are the same and subject to the verification of these facts and circumstances on audit.

3. Countries should ensure that taxpayers that meet the requirements of paragraph 1 of Article 25 can access the mutual agreement procedure

3.1 Both competent authorities should be made aware of MAP requests being submitted and should be able to give their views on whether the request is accepted or rejected. In order to achieve this, countries should either: amend paragraph 1 of Article 25 to permit a request for MAP assistance to be made to the competent authority of either Contracting State, or where a treaty does not permit a MAP request to be made to either Contracting State, implement a bilateral notification or consultation process for cases in which the competent authority to which the MAP case was presented does not consider the taxpayer's objection to be justified (such consultation shall not be interpreted as consultation as to how to resolve the case).

3.2 Countries' published MAP guidance should identify the specific information and documentation that a taxpayer is required to submit with a request for MAP assistance. Countries should not limit access to MAP based on the argument that insufficient information was provided if the taxpayer has provided the required information.

3.3 Countries should include in their tax treaties the second sentence of paragraph 2 of Article 25 ("Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States"). Countries that cannot include the second sentence of paragraph 2 of Article 25 in their tax treaties should be willing to accept alternative treaty provisions that limit the time during which a Contracting State may make an adjustment pursuant to Article 9(1) or Article 7(2), in order to avoid late adjustments with respect to which MAP relief will not be available.

Best practices

1. Countries should ensure that treaty obligations related to the mutual agreement procedure are fully implemented in good faith and that MAP cases are resolved in a timely manner

1. Countries should include paragraph 2 of Article 9 in their tax treaties.

2. Countries should ensure that administrative processes promote the prevention and timely resolution of treaty-related disputes

2. Countries should have appropriate procedures in place to publish agreements reached pursuant to the authority provided by the first sentence of paragraph 3 of Article 25 "to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention" that affect the application of a treaty to all taxpayers or to a category of taxpayers (rather than to a specific taxpayer's MAP case) where such agreements provide guidance that would be useful to prevent future disputes and where the competent authorities agree that such publication is consistent with principles of sound tax administration.

3. Countries should develop the "global awareness" of the audit/examination functions involved in international matters through the delivery of the Forum on Tax Administration's "Global Awareness Training Module" to appropriate personnel.

4. *Countries should implement bilateral APA programmes.*

5. *Countries should implement appropriate procedures to permit, in certain cases and after an initial tax assessment, taxpayer requests for the multiyear resolution through the MAP of recurring issues with respect to filed tax years, where the relevant facts and circumstances are the same and subject to the verification of such facts and circumstances on audit. Such procedures would remain subject to the requirements of paragraph 1 of Article 25: a request to resolve an issue with respect to a particular taxable year would only be allowed where the case has been presented within three years of the first notification of the action resulting in taxation not in accordance with the Convention with respect to that taxable year.*

3. Countries should ensure that taxpayers that meet the requirements of paragraph 1 of Article 25 can access the mutual agreement procedure

6. *Countries should take appropriate measures to provide for a suspension of collections procedures during the period a MAP case is pending. Such a suspension of collections should be available, at a minimum, under the same conditions as apply to a person pursuing a domestic administrative or judicial remedy.*

7. *Countries should implement appropriate administrative measures to facilitate recourse to the MAP to resolve treaty-related disputes, recognizing the general principle that the choice of remedies should remain with the taxpayer.*

8. *Countries should include in their published MAP guidance an explanation of the relationship between the MAP and domestic law administrative and judicial remedies. Such public guidance should address, in particular, whether the competent authority considers itself to be legally bound to follow a domestic court decision in the MAP or whether the competent authority will not deviate from a domestic court decision as a matter of administrative policy or practice.*

9. *Countries' published MAP guidance should provide that taxpayers will be allowed access to the MAP so that the competent authorities may resolve through consultation the double*

taxation that can arise in the case of bona fide taxpayer-initiated foreign adjustments—i.e. taxpayer-initiated adjustments permitted under the domestic laws of a treaty partner which allow a taxpayer under appropriate circumstances to amend a previously-filed tax return to adjust (i) the price for a transaction between associated enterprises or (ii) the profits attributable to a permanent establishment, with a view to reporting a result that is, in the view of the taxpayer, in accordance with the arm's length principle. For such purposes, a taxpayer-initiated foreign adjustment should be considered bona fide where it reflects the good faith effort of the taxpayer to report correctly the taxable income from a controlled transaction or the profits attributable to a permanent establishment and where the taxpayer has otherwise timely and properly fulfilled all of its obligations related to such taxable income or profits under the tax laws of the two Contracting States.

10. *Countries' published MAP guidance should provide guidance on the consideration of interest and penalties in the mutual agreement procedure.*

11. *Countries' published MAP guidance should provide guidance on multilateral MAPs and advance pricing arrangements (APAs).*

Chapter 5

MAP Arbitration

5.1 Introduction

1. The previous chapter, which provided a description of the mutual agreement procedure (MAP), did not address the provisions of paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention and of Article 25 of the OECD Model Tax Convention, which provide for the mandatory[1] arbitration of issues arising from a MAP request presented under Art. 25(1) that competent authorities are unable to resolve within a certain time.

2. This chapter examines the use of arbitration as part of the MAP. The chapter first explains how MAP arbitration works in practice, then examines the different positions that have been put forward concerning its use and finally sets out some design considerations for countries that want to move in this direction.

5.2 Legal Basis

5.2.1 Concept of MAP arbitration

3. Although MAP has generally been successful in resolving the majority of cases brought in countries with an active MAP program,[2] some countries have decided to include a mandatory arbitration mechanism in the MAP process.

4. This is done through the adoption of treaty provisions that allow issues that prevent the resolution of MAP cases within a certain time to be submitted to one or more independent persons for a decision that both countries are bound to follow. This process is referred to as "MAP arbitration" throughout this chapter.

1 This chapter does not deal with the non-mandatory arbitration provisions that were included in some older bilateral tax treaties and that allowed the use of arbitration on a case-by-case basis if both competent authorities agreed to do so. There are no reported cases where arbitration was used pursuant to such provisions.

2 See chap. 4, para. 164.

5. It is important to note that MAP arbitration is fundamentally different from commercial arbitration. While commercial arbitration is an alternative dispute resolution mechanism through which business disputes can be resolved by independent parties, MAP arbitration is merely an extension of the MAP process described in the previous chapter and may be used only where one or more issues arising in a MAP case cannot be resolved by the competent authorities within a prescribed time (usually two or three years).

6. Further, unlike an arbitration award in commercial arbitration that requires enforcement through a court system, MAP arbitration results in a decision that must be implemented by the competent authorities themselves. In fact, competent authorities may even be given the discretion to reach an agreement different from the decision resulting from the arbitration.[3]

7. Finally, whether initiated by the taxpayer or the competent authorities (depending on the tax treaty provision), arbitration results in a State-State procedure and usually does not involve the taxpayer directly, unlike investment arbitration.

8. One of the main reasons why MAP arbitration is included in some treaties is to encourage competent authorities to resolve cases through MAP negotiations, thereby avoiding the need for arbitration.[4]

5.2.2 MAP arbitration under the United Nations Model Tax Convention

9. As already noted, Article 25 of the United Nations Model Tax Convention contains two alternative versions. Alternative A provides

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3 As provided in paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention. That possibility is also allowed under the alternative wording for paragraph 5 of Article 25 of the OECD Model Tax Convention that appears in paragraph 84 of the Commentary on that article.

4 Paragraph 18 of the Commentary on Article 25 of the United Nations Model Tax Convention, quoting paragraph 64 of the Commentary on Article 25 of the OECD Model Tax Convention. See also Hugh J. Ault and Jacques Sasseville, “2008 OECD Model: The New Arbitration Provision”, IBFD, *Bulletin for International Taxation*, 2009 (Volume 63), No. 5.

only for the MAP described in Chapter 4. Alternative B, however, includes an additional paragraph 5 according to which issues that are unresolved through the MAP may be submitted to arbitration.

10. Under paragraph 5, where the competent authorities of the two treaty States are unable to reach a mutual agreement within three years from the presentation of a MAP request under paragraph 1 of Article 25, the unresolved issues arising from the case may be submitted to arbitration at the request of either competent authority[5] (once arbitration is initiated, the taxpayer involved in the MAP case should be notified).

11. However, issues that have been decided by a court or tribunal in either State cannot be submitted to arbitration.

12. Paragraph 5 also provides that the competent authorities may agree on a different decision within six months of the arbitration decision. Unless they do so within that period, the arbitration decision is binding on both competent authorities and needs to be implemented irrespective of domestic time limits, unless the proposed mutual agreement that implements the arbitration decision is not accepted by a person directly affected by the MAP case.

13. Under paragraph 5, the competent authorities have the discretion to determine the procedural aspects of the MAP arbitration. The Commentary on Article 25 provides additional guidance on this matter, including through a "sample mutual agreement" that countries may use to implement the MAP arbitration. This "sample mutual agreement" proposes detailed rules as regards the type of arbitration procedure, the selection of arbitrators, the independence required from the arbitrators, the transparency of the process, the payment of the remuneration of the arbitrators and other costs, the procedural and evidentiary rules to be followed, the sharing of information and related confidentiality requirements as well as the implementation of the arbitration decision.

5 However, paragraph 17 of the of the Commentary on Article 25 of the United Nations Model Tax Convention includes alternative wording for Art. 25(5) under which the request for arbitration is made by the taxpayer and not by one of the competent authorities.

14. The Commentary also provides additional guidance on the relationship between the arbitration process and domestic remedies.[6] Given that issues that have already been decided by a court or tribunal in either country may not be submitted to arbitration, the taxpayer may have to suspend domestic law remedies in order to pursue arbitration. Most countries do not allow the parallel pursuit of arbitration and domestic law remedies.

15. Therefore, countries may require that if a taxpayer has initiated domestic remedies but a decision has not yet been reached by a court or tribunal, the domestic remedies should be suspended until the arbitration has been completed in order to prevent an abrupt termination of the arbitration proceedings upon the rendering of the court's or tribunal's decision. In some countries, it may be possible to require the taxpayer to renounce the right to domestic law remedies but this would raise constitutional or other legal difficulties in other countries.

16. In the case of countries where the competent authorities can deviate from a final court decision, there is no need for the part of paragraph 5 that prevents MAP arbitration where issues arising from a MAP case have already been decided by a court or tribunal.[7]

5.2.3 MAP arbitration under the OECD Model Tax Convention and the MLI

17. Paragraph 5 of Article 25 of the OECD Model Tax Convention is largely similar to paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention.

18. However, there are some significant differences. First, the OECD Model Tax Convention does not contain alternative provisions and simply provides for the inclusion of arbitration provisions. Second, the OECD Model Tax Convention allows for arbitration when a MAP case is unresolved after two years (from the date when all the information

6 Under MAP arbitration, the decision of the arbitrators is implemented through the conclusion of a mutual agreement, which means that the explanations provided in section 4.4.2.7 of Chapter 4 concerning the relationship between the mutual agreement procedure and domestic law are also relevant.

7 Paragraph 7 of the Commentary on Article 25 of the United Nations Model Tax Convention.

required by the competent authorities in order to address the case has been provided to both competent authorities) rather than the three years (from the presentation of the case to the competent authority of the other Contracting State) under the United Nations Model Tax Convention. Third, the OECD Model Tax Convention allows for the arbitration request to be made by the taxpayer rather than by one of the competent authorities. Fourth, the OECD Model Tax Convention does not allow the competent authorities to depart from the arbitration decision.[8] The Commentary on Article 25 of the OECD Model Tax Convention includes guidance on the conduct of the MAP arbitration process and a large part of that guidance is quoted in the corresponding Commentary of the UN Model Tax Convention.

19. As indicated in Chapter 1, the treaty-related changes proposed by the BEPS project may be implemented bilaterally or through the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (MLI).[9]

20. Part VI of the MLI contains an option for mandatory binding MAP arbitration. The optional rules of Part VI are more detailed than the arbitration provisions of the United Nations and OECD models: these rules deal expressly with access to arbitration, information requests and timelines, appointment of arbitrators and costs, mode of conduct of arbitration, independence, transparency and confidentiality.[10]

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8 See, however, footnote 3, which indicates that this is possible under the alternative wording included in the OECD Commentary.

9 Chap. 1, footnote 24.

10 There are also rules for arbitration in tax treaty matters within the European Union. The EU *Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises* (see https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41990A0436&from=en, accessed on 12 March 2021, as subsequently amended) provides for arbitration. A directive to govern cross-border dispute resolution through instruments such as the Arbitration Convention and tax treaties has also been adopted in the EU in 2017 (see Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union, available at https://eur-lex.europa.eu/eli/dir/2017/1852/oj, accessed on 12 March 2021).

5.3 Different views on the appropriateness of arbitration

21. Countries hold different views on the need for arbitration in the context of the MAP. These views partly reflect their own economic, social and legal environment and partly reflect their experience with existing dispute resolution mechanisms in tax and non-tax agreements. The views of countries, which may evolve over time, are also influenced by their capacity to engage in what is sometimes perceived as a complex process. This section sets out the views that have been expressed on the need and desirability of arbitration in the context of the MAP.

5.3.1 The perceived concerns

22. Several concerns raised by members from the United Nations Tax Committee have been recorded in the Commentary on Article 25 of the United Nations Model Tax Convention.[11] These include concerns about:[12]

— Possible sovereignty and constitutionality impediments
— Costs and lack of resources
— Lack of experience and familiarity with MAP and arbitration
— Even-handedness
— Transparency

Possible sovereignty and constitutionality impediments

23. Some countries may take the view that arbitration in tax treaty disputes affects their sovereignty. Some countries may also consider that their constitution prevents the inclusion of arbitration provisions in a tax treaty while other countries may consider that the inclusion of arbitration, while constitutional, may create other constitutional obligations such as the extension of such remedies in domestic cases.

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11 Paragraph 4 of the Commentary on Article 25 of the United Nations Model Tax Convention.

12 See also United Nations (2015), *Secretariat Paper on Alternative Dispute Resolution in Taxation*, E/C.18/2015/CRP.8, available at: http://www.un.org/esa/ffd/wp-content/uploads/2015/10/11STM_CRP8_DisputeResolution.pdf, accessed on 12 March 2021.

Other countries that do not have the above concerns may raise the issue of shifting of decision-making power from the State to members of an arbitration panel. While the importance of such concerns really depends on the constitutional rules and principles specific to each country, other countries may, however, take the view that legal and constitutional concerns should generally not arise with MAP arbitration since sovereignty is legally ceded to the extent of the tax treaty and the dispute resolution mechanism in a treaty merely enforces such provisions. In doing so, these countries may also rely on their experience with arbitration and mandatory dispute settlement in treaties in other areas such as trade and investment to argue that sovereignty concerns should generally not arise.

Costs and lack of resources

24. Some countries may have concerns as regards the costs of arbitration. Arbitration necessarily entails costs in terms of fees for the arbitrators and may entail costs for facilities and additional fees for counsel or representation. Also, developing countries may be concerned that these fees could be payable in a foreign currency on a scale that is not proportional to the resources available to them. There may also be concerns by developing countries that they may need to hire outside experts to assist them in a MAP arbitration process, although previous MAP arbitration cases suggest that this would not be necessary. On the other hand, other countries may believe that the costs associated with arbitration may be lower than expected owing to the limited number of cases that may go to arbitration and the ability to structure an efficient arbitration process and to put a cap on the compensation of arbitrators (e.g. as is sometimes done with the last best offer form of arbitration).

Lack of experience and familiarity with MAP and arbitration

25. Several developing countries may also be concerned with their perceived lack of experience in arbitration as compared to developed countries. This may put undue pressure on the competent authorities of developing countries. Some commentators, however, have claimed that impartial decisions by arbitrators from all backgrounds, including from developing countries, may help overcome the lack of experience of developing countries.

26. Some developing countries may not rule out an eventual recourse to MAP arbitration but may consider that they are not yet ready for such a mechanism, especially given the negative experience of some developing countries with the application to tax measures of the arbitration provisions of bilateral investment agreements. It has also been noted that, in the current environment, most MAP arbitration cases that would involve developing countries would focus on tax collected by these countries as opposed to tax collected by developed countries.

Even-handedness

27. Some countries believe that arbitration may also lead to concerns of even-handedness. They consider that, as of today, there is only a small pool of possible arbitrators who can deal with complex international tax and transfer pricing issues and most of them come from the developed world. Although this group may include academics and people having no affiliation with governments or business, these countries claim that their thought process and understanding of international taxation may be tuned to the developed world and might not be familiar with concerns of developing countries. There are also concerns that few potential arbitrators would be fluent with the official languages of some developing countries, which might make it difficult for these arbitrators to fully understand the position of the competent authorities of these countries.

Transparency

28. Some countries may take the view that MAP arbitration may also raise transparency concerns, although such concerns would seem to be applicable to all MAP cases, whether or not they involve arbitration. Like other parts of the MAP process, MAP arbitration proceedings are generally considered confidential and opinions are not published. Further, in mandatory binding arbitration in tax treaties, decisions are considered binding on the competent authorities (even though they have no precedential value for other cases).

5.3.2 The perceived benefits

29. Potential benefits of arbitration that were put forward during discussions of the United Nations Tax Committee have been recorded

in the Commentary on Article 25 of the United Nations Model Tax Convention.[13] These include:

— Guarantees the resolution of MAP cases
— Prophylactic effect
— Increased certainty
— Reduces reliance on unilateral domestic remedies

Guarantees the resolution of MAP cases

30. Arbitration is the preferred approach of some countries which are concerned that there is no assurance that the MAP will resolve all disputes and will do so in a timely fashion. These countries may consider that including arbitration in their tax treaties to improve the MAP process would be a step forward in guaranteeing to the taxpayer relief from double taxation and from taxation not in accordance with the treaty. Although there may only be a few cases that remain unresolved by the MAP between the particular countries concerned, such countries emphasize the importance of resolving MAP issues in such cases as well.

Prophylactic effect

31. It has been argued that the most significant benefit perceived by some countries in adding arbitration to the MAP process is the "prophylactic effect". Since the purpose of arbitration is not to replace the MAP with an independent evaluation of the case by arbitration, but to supplement the current MAP process in those few cases where the competent authorities are unable to agree on a resolution in a timely manner, the view has been expressed that the inclusion of arbitration would encourage the conclusion of more cases in an efficient manner. In practice, this has been the experience under the Canada-United States tax treaty, which has included mandatory binding arbitration since 2010. On the other hand, it could be considered that the risk of arbitration puts pressure on the competent authorities of developing countries, especially those that lack experience with the MAP, to agree to certain controversial solutions.

13 Paragraph 5 of the Commentary on Article 25 of the United Nations Model Tax Convention.

Increased certainty

32. Countries may also take the view that arbitration in the context of the MAP may provide more certainty to taxpayers. Since the MAP may not guarantee a resolution, adding arbitration to the MAP process may increase the certainty that a taxpayer expects as regards the conclusion of the MAP and the eventual resolution of cases of double taxation and taxation not in accordance with the treaty. These countries may also believe that this will help encourage cross-border investment. It has also been suggested that the addition of arbitration to a tax treaty may make it easier for a developed country to agree to the addition of controversial provisions to the allocative rules of a tax treaty, especially when the practical application of such provisions is likely to create uncertainty.

Reduces reliance on unilateral domestic remedies

33. Some countries may also consider that arbitration helps reinforce taxpayers' faith in the MAP, thereby reducing reliance on sometimes inadequate unilateral domestic remedies. The alternative for the taxpayer to take the case to court may not be the best solution for the tax administration either since it might be more cost-efficient for the tax administration to go for arbitration as opposed to prolonged judicial processes. On the other hand, some countries may consider that judicial proceedings are more likely to ensure a more transparent and technically sound application and legal interpretation of treaties and domestic law.

5.4 Procedural guidelines for the implementation of arbitration by opting countries

5.4.1 General overview

34. In general, for countries opting for arbitration, the competent authorities are free to design procedural rules as regards the conduct of proceedings under the treaty arbitration provisions. As envisaged by the United Nations and OECD models and the MLI, competent authorities typically enter into (and need to do so in order to practically implement arbitration) a competent authority agreement as regards such proceedings.[14] However, since procedural rules not only

14 Using, where appropriate, the provisions of the sample mutual

impact the effectiveness of the relevant treaty provisions but also play a key role in alleviating the concerns about arbitration that are described above, a country should pay careful attention to the procedural rules applicable with respect to each of its treaties that allows for arbitration.

35. Although the need for flexibility explains the variations of treaty provisions related to arbitration, a country should seek to ensure that the rules governing arbitration in its different treaties are clear, are suitable for all cases where arbitration may be used and are fairly consistent in order to facilitate the understanding of these rules by taxpayers and facilitate the training of tax officials involved in the MAP process.

5.4.2 Initiation of arbitration

36. As already mentioned, the United Nations Model Tax Convention provides that the request for arbitration may be made by the competent authority of one of the Contracting States but the OECD Model Tax Convention and the MLI allow the taxpayer to make the request directly. However, because of the costs involved, where arbitration is triggered by a competent authority, both competent authorities may wish to request the taxpayer's consent before engaging in arbitration so as to avoid spending resources on the arbitration of issues in situations where the taxpayer is likely to reject the mutual agreement that would implement the arbitration decision on these issues.

37. Certain rules as regards the arbitration request should be prescribed in the competent authority agreement referred to in paragraph 34 above. Ideally, the request for initiating an arbitration process should be made in writing and should contain all the information that is necessary to clearly identify the case. Where arbitration may be initiated by a competent authority, the competent authority wishing to do so should notify the other competent authority and the person who has presented the MAP case. Where it is the taxpayer that may initiate arbitration, the competent authority receiving the taxpayer's request for arbitration should, within a specified period of time, share that request with the other competent authority so as to formally initiate the process.

agreement included in the Annex to the Commentary on Article 25 of the United Nations and OECD models.

38. Where there are restrictions as to the cases that may be submitted to arbitration, such as where arbitration is restricted to certain issues or where issues that have been decided by a court or tribunal are excluded from arbitration, the taxpayer may be asked to provide a declaration stating that the MAP case falls within the accepted categories.

39. Where the taxpayer is allowed to make the request for arbitration,[15] it would seem possible to present that request to either competent authority, although the countries may require that the request be presented to the competent authority of the State to which the MAP case was initially presented under Art. 25(1). Such a requirement should be clearly stated in the applicable treaty or the agreement setting up the arbitration process.

40. Under the MLI as well as the United Nations and the OECD sample mutual agreements, if information required by either competent authority pursuant to its published MAP procedures has not been provided by the taxpayer in a timely manner, this delays the start time of the two-year or three-year period during which the case is not eligible for arbitration.

5.4.3 Terms of reference

41. The expression "terms of reference" refers to the questions that must be decided by the arbitration panel in a specific case submitted to arbitration. Although the arbitration provisions of the United Nations and OECD models are silent as regards the terms of reference, it may be important to refer to them in a competent authority agreement. According to the United Nations sample mutual agreement, the competent authorities must decide the terms of reference of the arbitration within three months from the receipt of the arbitration request by the second competent authority. The Commentary on Article 25 of the OECD Model Tax Convention suggests a shorter period of 60 days.

42. The terms of reference determine the jurisdictional basis of a particular case that is subject to arbitration. Where competent authorities make the arbitration request, they could determine whether to restrict the process to certain issues. However, where the taxpayer

15 See para. 18 and footnote 5.

makes the request, the main issues dealt with in the request should ideally be covered in the terms of reference.

43. However, the rules for determining the questions to be arbitrated should ideally be reflected in the treaty or an accompanying document so as to prevent an impasse between the competent authorities in this regard.

44. Separate rules may be laid out for failure to communicate the terms of reference in a timely manner. If the terms of reference have not been agreed to by the competent authorities and communicated to the person who has presented the case within three months, the competent authority agreement may allow each competent authority, within one additional month, to communicate in writing to each other a list of the issues to be resolved by arbitration, which would then constitute the tentative terms of reference. Within one month after all the arbitrators have been appointed, the arbitrators may then communicate to the competent authorities and the person who presented the case a revised version of the tentative terms of reference. Within another one month, the competent authorities may also be provided with the possibility to agree on different terms of reference and to communicate them in writing to the arbitrators and the person who presented the case.

5.4.4 Selection of the arbitration panel

45. Countries should carefully select the members of the arbitration panel. It is of paramount importance that these members be selected on the basis of their experience and qualifications as well as their independence and absence of bias.

46. Rules applicable to the selection of the arbitration panel may be included either in the treaty arbitration provisions or in the competent authority agreement. Countries have several options as regards the design of such rules.

47. The United Nations sample mutual agreement suggests a three-member panel. It provides that each competent authority shall appoint one arbitrator within three months from the notification of the terms of reference to the taxpayer (or, where the terms of reference have not been finalized, within four months from when a competent authority receives notification of the arbitration request made by the other competent authority). Within two months of the last

appointment, the two appointed arbitrators shall appoint the third arbitrator, who shall act as the Chair of the panel. A similar approach is followed in the OECD sample mutual agreement.

48. However, the two models differ as to what happens when there is a failure to appoint arbitrators as provided above. The Commentary on the United Nations Model Tax Convention provides that if an appointment is not made within the prescribed time, the Chair of the United Nations Tax Committee shall make the appointment within 10 days from a request for such appointment by either competent authority. If the Chair is a national of either State involved, the longest serving Committee member who is not a national of these States shall make the appointment. The Commentary on the OECD Model Tax Convention gives that power of appointment in case of default to the highest ranking official of the OECD Centre for Tax Policy and Administration who is not a national of either State involved. The MLI arbitration provisions follow the approach proposed in the Commentary on the OECD Model Tax Convention.

49. Countries are free to depart from these proposed rules and to create customized arbitration panels. For instance, countries could prefer to have a single arbitrator or a five-member panel. However, countries are urged to provide for panels composed of an odd number of members to avoid having decisions without a clear majority. Countries may also wish to have different rules to address cases where there is a failure to appoint one or more arbitrators (for instance, where one country wishes to follow the approach suggested in the Commentary on the OECD Model Tax Convention while the other prefers the approach put forward in the Commentary on the United Nations Model Tax Convention).

50. Countries may also consider other approaches based on their own policy goals when devising such rules. For instance, paragraph 15 of the Annex to the Commentary on Article 25 of the United Nations Model Tax Convention considers the creation of a list of suitable potential arbitrators by the United Nations Tax Committee.[16] Countries

16 Similarly, the approach adopted under the EU Arbitration Convention and the EU Dispute Resolution Directive (see footnote 10) involves the maintenance of a panel of "independent persons" as well as detailed rules regarding the selection of the Chair.

may accordingly agree on a list of potential arbitrators from which arbitrators may be chosen for each arbitration case arising out of their tax treaty.

51. Specific rules may also be adopted with respect to replacement of arbitrators. Such a process may be initiated in cases of incapacity, disqualification or resignation. However, in order to avoid undue delay, countries may consider allowing replacement of only arbitrators who have been found to be compromised, retaining the rest of the Panel. Ideally, replacement of arbitrators should be made by the remaining members of the Panel by unanimous decision. The replacement of arbitrators may also lead to extension of any timelines that are prescribed for the completion of the process in the treaty provision or the competent authority agreement.

52. Each arbitrator must be qualified to serve in such position. The treaty arbitration provisions or the competent authority agreement may stipulate that arbitrators should be persons with recognized competence in the field of international tax law who may be relied upon to exercise independent judgment in deciding tax treaty disputes. Countries may also consider selecting multiple potential arbitrators and agreeing on a list of arbitrators that may be called upon in respect of each treaty.

53. Each arbitrator must be independent. The United Nations sample mutual agreement suggests that any person, including government officials of either State involved, may be an arbitrator unless the person was previously involved in the case going to arbitration. The Commentary on Article 25 of the OECD Model Tax Convention includes a similar provision. However, the Commentary on Article 25 of the United Nations Model Tax Convention also suggests that the arbitrator should provide a written attestation of that arbitrator's independence and impartiality.

54. The MLI provides that each arbitrator should be impartial and independent vis-à-vis the tax authorities, the competent authorities and the ministry of finance of each State, and all persons affected by the case at the time of that arbitrator's appointment. In addition, it provides that the arbitrator should maintain that status throughout the arbitration process and for a reasonable time thereafter.

55. Countries may consider these options and agree on independence and transparency rules as regards the arbitrators. Countries may consider using the following format for the written attestation referred to in paragraph 53 above:

Box 1: Sample declaration by an arbitrator

To the best of my knowledge there is no reason why I should not serve on the arbitration panel constituted by [ ] with respect to a dispute between_[ ] and [ ], due to a conflict of interest arising from any previous relation with either of the parties or jurisdictions involved.

I shall keep confidential all information coming to my knowledge as a result of my participation in this proceeding, as well as the contents of any decision delivered by the Panel. I shall judge fairly as between the parties, according to the applicable law, and shall not accept any instruction or compensation with regard to the proceeding from any source except as allowed by the law and Rules made pursuant thereto. I shall also not indulge in any *ex parte* discussions with any of the parties as regards the matter and all questions that I make to the competent authorities shall be in writing with copies shared simultaneously with the other parties.

Attached is a statement of (*a*) my past and present professional, business and other relationships (if any) with the parties and (*b*) any other circumstance that might cause my reliability for independent judgment to be questioned by a party. I acknowledge that by signing this declaration, I assume a continuing obligation promptly to notify both parties of any such relationship or circumstance that subsequently arises during this proceeding.

Source: International Centre for the Settlement of Investment Disputes (ICSID), "Conciliation Rules", in ICSID Convention, Regulations and Rules,[17] *Rule 6(*2), p. 88.

17 Available at https://icsid.worldbank.org/sites/default/files/documents/ICSID%20Convention%20English.pdf#search=icsid%20convention, accessed on 12 March 2021.

56. Either competent authority may propose the disqualification of an arbitrator if the above independence and transparency rules are not respected. If such disqualification is proposed by a competent authority, the other members of the panel should, after giving the impugned member the opportunity to be heard, decide the issue by unanimous decision (in case of a three- member panels) or majority vote (in case of larger panels). If the arbitrator is disqualified, the procedure applicable to the replacement of an arbitrator should be activated.

57. All official communications between the members of the panel and between the panel and the competent authorities or the taxpayer should require confidentiality. For instance, competent authorities should be mindful of confidentiality requirements when disclosing information concerning the identity of the taxpayers involved for the purposes of allowing prospective arbitrators and the organizations to which they belong to identify any potential conflict of interest. One possible approach would be to obtain the taxpayer's consent to disclose such information for the limited purpose of selecting the arbitration panel.

5.4.5 The arbitration process

58. Countries opting for arbitration should also provide for the type of arbitration process that will be followed, either in the arbitration provisions of the tax treaty or in the competent authority agreement. Arbitration may be done in different ways such as the "independent opinion" arbitration, where the arbitrators are asked to produce a reasoned decision that includes their conclusions as regards the facts, the evidence and the legal arguments, and the "last best offer" or "baseball" arbitration where each competent authority submits its most reasonable resolution of the case and the arbitration panel is asked to decide which of these proposed resolutions will prevail based on their views on the facts and arguments presented by each competent authority.

59. The sample mutual agreement included in the Commentary on Article 25 of both the United Nations and OECD models endorses the use of the last best offer (or baseball) arbitration approach. Under that approach, each competent authority must submit its proposed resolution within two months from the appointment of all arbitrators and a

decision must be delivered by the arbitration panel within the following three months.[18]

60. The MLI allows jurisdictions the option to choose one of these two approaches for all cases or to decide on a default approach with the possibility of using another approach if both competent authorities agree to do so in a specific case.

61. Specific rules may be required as regards the "last best offer" approach. The proposed resolution should ideally be limited to a disposition of specific monetary amounts or the maximum tax rate applicable, depending on the case. Where substantive issues are pending as well (for example, whether a permanent establishment exists), the competent authorities may give alternative proposed resolutions for either result. Competent authorities may also provide supporting position papers to which replies may be provided by the other competent authority. However, page limits may be set for the proposed resolutions, position papers and replies to ensure that this method works in an efficient and timely manner.[19]

62. Specific rules may also be prescribed as regards the independent opinion approach. Such rules could provide, for example, that within a reasonable time agreed to by both countries, each competent authority should provide the arbitration panel with a description of the facts and of the unresolved issues to be decided, together with the position of the competent authority concerning these issues and the arguments supporting that position. Competent authorities may also prevent the panel from considering arguments that were not presented to it.

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18 Article 6 of the sample mutual agreement included in the Annex to the Commentary on Article 25 of the United Nations Model Tax Convention.

19 Examples of such page limits are found in paragraphs 9(a) and 9(d) of the *Memorandum of Understanding Between the Competent Authorities of Canada and the United States of America* regarding the application of the arbitration procedure of the Canada-United States tax treaty (available at https://www.canada.ca/en/revenue-agency/services/tax/international-non-residents/memorandum-understanding-between-competent-authorities-canada-united-states-america.html, accessed on 12 March 2021).

63. Where one competent authority fails to submit a proposed resolution or a position paper, the arbitration decision would follow the other side's proposal. Countries may also prescribe strict time limits within which each step of this process should be completed.

64. Countries should obviously weigh the pros and cons of each approach before choosing the applicable arbitration process. At this point in time, however, there is not enough experience with MAP arbitration to identify clear benefits and disadvantages of each approach with respect to issues such as costs, duration and creation of precedents. Given the fundamental differences between MAP arbitration and arbitration under commercial contracts or investment or trade treaties (which often involves very high costs), the experience with these latter forms of arbitration does not provide useful guidance as to the design of MAP arbitration. Such guidance may be developed in the future as a result of the experience gained by countries that adopt MAP arbitration.

65. Countries may also prescribe rules related to the conduct of the arbitration proceedings. The treaty arbitration provisions or the competent authority agreement may require the arbitration panel to meet within a reasonable time from its creation and may require further meetings within particular time periods. The arbitration panel may also be allowed to use video-conference or tele-conference facilities for its meetings. In addition, rules may be prescribed as regards the language to be used in such proceedings.

66. Countries should keep timelines in mind if they intend MAP arbitration to proceed expeditiously. Neither the United Nations nor the OECD model prescribes an overall time limit within which the whole arbitration process should be completed. However, the sample mutual agreements found in these models provide specific time limits for various steps of that process. For instance, the United Nations sample mutual agreement provides that, under the last best offer approach, the panel should communicate its decision to both competent authorities within three months from having received the last proposal from these competent authorities. Under the alternative independent opinion approach, the United Nations sample mutual agreement provides that the decision should be communicated within six months from the date on which the Chair of the panel notifies that the necessary

information has been received.[20] However, the OECD sample mutual agreement provides that the decision should be communicated to both competent authorities within 60 days after the reception by the arbitrators of the last reply submission or, if no reply submission has been submitted, within 150 days after the appointment of the Chair of the panel (under the last best offer approach) and within 365 days from the appointment of the Chair (under the independent opinion approach). Countries may draw from that guidance and from the practices adopted by countries that have already dealt with the issue of time limits (e.g. default time limits, and the applicable remedies if these are not respected, are provided under the EU Directive[21] and with respect to the arbitration provisions of some United States treaties).

67. Countries should generally be free to agree on the location where the arbitration meetings will be held. Physical meetings may not be necessary under the last best offer approach. In the case of arbitration provisions included in treaties with developing countries, the choice of the meeting location should take account of the costs involved. The

20 Paragraph 11 of the United Nations sample mutual agreement also indicates:

> If within two months from the date on which the last arbitrator was appointed, the Chair, with the consent of one of the competent authorities, notifies in writing the other competent authority and the person who presented the case that he has not received all the information necessary to begin consideration of the case, then
>
> — if the Chair receives the necessary information within two months after the date on which that notice was sent, the arbitration decision must be communicated to the competent authorities and the person who presented the case within six months from the date on which the information was received by the Chair, and
>
> — if the Chair has not received the necessary information within two months after the date on which that notice was sent, the arbitration decision must, unless the competent authorities agree otherwise, be reached without taking into account that information even if the Chair receives it later and the decision must be communicated to the competent authorities and the person who presented the case within eight months from the date on which the notice was sent.

21 See footnote 10.

use of technology such as video conferencing may provide a speedy and cost-efficient alternative for the conduct of arbitration meetings.

68. The United Nations and OECD sample mutual agreements suggest that the competent authority to which the case giving rise to the arbitration was initially presented should be responsible for the logistical arrangements for the meetings of the arbitration panel and should provide the administrative personnel necessary for the conduct of the arbitration process. However, if significantly more MAP cases are presented to the competent authority of one country, countries may consider a rule under which the responsibility for the logistical arrangements will alternate between the competent authorities.

69. Neither the United Nations Model Tax Convention nor the OECD Model Tax Convention specifically allows for taxpayer participation in the arbitration process. While the OECD sample mutual agreement allows participation in writing by the person requesting the arbitration process to the extent allowed in MAP, and orally if allowed by the arbitration panel, the issue is not addressed in the Commentary of the United Nations Model Tax Convention and in the MLI.

70. Countries may also adopt other procedural or evidentiary rules that they may consider appropriate. For example, countries may bilaterally agree on a list of documents that may be accepted as evidence by the arbitration panel.

5.4.6 Confidentiality

71. Since arbitration proceedings involve third parties receiving information, it is important to ensure the confidentiality of taxpayer information and the impartiality and independence of the procedure. The United Nations and OECD sample mutual agreements provide that both countries should agree that the arbitrators will be deemed to be authorized representatives of the appointing competent authority for the purposes of applying Article 26 of these models with respect to the communication of information and the confidentiality of the information received. The MLI adds another layer of protection by increasing the number of persons subject to the confidentiality requirements: it provides that not only the arbitrators but also their support staff (up to three staff members per arbitrator) will constitute authorized representatives of the competent authorities. It also requires a written

statement from each arbitrator and designated staff member recognizing expressly these confidentiality and non-disclosure obligations.

72. In line with these suggestions, countries should ensure that arbitrators (and prospective arbitrators, as indicated in paragraph 57 above) are bound by the relevant confidentiality provisions of the tax treaty and applicable domestic laws. This should also be done with respect to any staff member involved in the arbitration process. In doing so, countries should require that arbitrators and staff members destroy all confidential information received once the arbitration process is over.

73. Countries should also adopt rules to ensure that all exchanges of information between the competent authorities and the arbitration panel are done through secure, encrypted channels so that confidential and sensitive taxpayer information remains protected.

5.4.7 Remuneration of the arbitrators and other costs

74. Countries must take into account the costs involved in the arbitration process and provide rules for allocating these costs. The arbitration process necessarily entails costs in terms of fees for the arbitrators and, depending on the type of arbitration used, costs for meetings.

75. The Commentary on Article 25 of both the United Nations and OECD models includes the following guidelines with respect to these costs:

— Each competent authority bears the costs, including travel costs, related to its own participation and the participation of the arbitrator that was appointed by, or on behalf of, that competent authority

— Costs related to the meetings of the arbitration panel and the personnel necessary for the arbitration process are borne by the competent authority to which the MAP case giving rise to the arbitration was initially presented[22]

— All other costs, including the costs related to other arbitrators, are borne equally by the two countries

22 If the request was presented to both countries, the costs would be shared equally.

76. The MLI merely provides that the issue of costs will be settled by mutual agreement between the competent authorities and, if there is no such agreement, that each party will bear its own costs while other costs will be shared equally.

77. Competent authorities may also agree to simply share all expenses, including the remuneration of the arbitrators. Countries may also agree on a separate approach with respect to the remuneration of the arbitrators and may provide specific fees or adopt a fee schedule for that purpose.

78. The United Nations sample mutual agreement provides additional suggestions concerning the remuneration of the arbitrators. It suggests paying them an hourly fee for a maximum of three days of preparation, two meeting days (including video conferencing) and the related travel days. Reasonable expenses shall also be reimbursed under this approach.

79. Where there is a clear disparity in the financial status of the two treaty countries, it may be appropriate for the countries to agree that the richer country will bear a larger share of the costs of the arbitration process.

5.4.8 The decision

80. Countries should be clear as to how a decision will be arrived at where there is more than one arbitrator. While a decision by simple majority would be the logical rule, there might be cases where an even number of arbitrators will render the decision (e.g. where one of three arbitrators is unable to render a decision).

81. Countries should also clarify the criteria that the arbitration panel must apply to arrive at a decision. The panel should decide the issues submitted to arbitration in accordance with the applicable provisions of the tax treaty and the applicable domestic laws of the countries involved. Countries may also allow the panel to consider any other sources that the competent authorities may expressly identify, or which may be identified in the applicable treaty or accompanying bilateral agreements.

82. Countries should clarify whether arbitration decisions should be published or not. The United Nations sample mutual agreement does

not refer to the possibility of publishing arbitration decisions because it adopts the last best offer approach. However, it follows the approach adopted in the Commentary on the OECD Model Tax Convention if the independent opinion approach is chosen. That approach is to allow publication, with the omission of taxpayer-specific details, if that is agreed to by the taxpayer who made the MAP request and by both competent authorities, on the understanding that the published decision carries no precedential value.

83. Both the Commentary on the United Nations Model Tax Convention and the Commentary on the OECD Model Tax Convention suggest that arbitration decisions have no precedential value. Countries that wish to provide otherwise would need to make this clear in the competent authority agreement.

84. The treaty arbitration provisions may clarify that the competent authorities may resolve the MAP case while the arbitration proceedings are under way, which would lead to the termination of the arbitration process.

85. Both the United Nations and OECD models provide that the arbitration decision shall be final and binding on the competent authorities. The decision must be implemented through a mutual agreement, unless the taxpayer rejects that agreement. However, as explained in paragraph 12 above, treaties that adopt the formulation of paragraph 5 of Article 25 (alternative B) of the United Nations Model Tax Convention allow the competent authorities to agree, within six months of the decision, to depart from the arbitration decision. In practice, this possibility is likely to be more relevant for an arbitration decision rendered under the independent opinion approach than for a decision rendered under the last best offer approach.

Chapter 6

Possible improvements to the MAP

6.1 Introduction

1. A country that concludes a tax treaty that includes provisions based on those of Article 25 of the United Nations or OECD model has a legal obligation to endeavour to resolve through MAP any admissible case presented to its competent authority under paragraph 1 of that article. Many developing countries, however, have no or little experience with MAP and may therefore need assistance in dealing with MAP cases, which requires not only a good understanding of the MAP process but also of treaty provisions and transfer pricing principles. Even countries with significant MAP caseloads may experience difficulties in resolving MAP cases with some of their treaty partners.

2. This chapter examines measures that could possibly improve MAP in these and other cases. Some of these measures have already been used to a limited extent while others have yet to be used.

3. Section 6.2 deals with the provision of technical assistance to a country with respect to one or more specific MAP cases under a programme such as Tax Inspectors Without Borders (TIWB). Section 6.3 refers to capacity-building efforts intended to improve the capacity of developing countries to meet their MAP obligations. Section 6.4 describes how the conclusion of framework agreements may help address some of the difficulties that the competent authorities of two countries encounter in dealing with their mutual MAP caseload. Section 6.5 examines how new technologies may facilitate the MAP process. Section 6.6 discusses the possible use of non-binding dispute resolution mechanisms in MAP cases.[1]

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1 It has also been suggested that MAP could be improved if a taxpayer could, if both competent authorities agreed in a specific case, access arbitration before the end of the two-year or three-year period provided respectively in Art. 25(5) OECD Model Tax Convention and Art. 25(5) (alternative B) United Nations Model Tax Convention. However, this chapter does not address possible improvements that could result from changing some of the rules applicable to arbitration.

6.2 Technical assistance with respect to specific MAP cases

4. The competent authority of a country that has no or little MAP experience and that is faced with a MAP request could benefit from the assistance of persons who have expertise in the MAP process and the relevant treaty provisions.

5. Obviously, few developing countries would be in a position to pay consultants for that purpose. Also, MAP experience is primarily gained through work within the competent authority team of a tax administration. For these reasons, the type of case-specific MAP assistance that would likely be needed by the competent authority of a developing country would seem to be similar to the kind of assistance that is provided to the tax auditors of developing countries' tax administrations under the Tax Inspectors Without Borders (TIWB) programme (see Box 1 below).

6. The TIWB program, which promotes hands-on assistance by sending experts to build developing countries' audit and audit-related skills pertaining to specific international tax matters, could be expanded (or a similar programme could be set up) in order to allow the competent authorities of developing countries to benefit from the assistance of former tax officials familiar with the MAP process and the different types of treaty disputes that are typically dealt through that process. Since the TIWB has already developed mechanisms that ensure the respect of confidentiality requirements applicable to the audit function, the same form of assistance could be provided with respect to MAP cases without breaching the similar confidentiality requirements that apply to the MAP process under tax treaties and domestic law. The 2020 Annual Report of the TIWB[2] indicated that the programme would be expanded to cover new areas of tax assistance, including tax treaty negotiation and administration. This should result in increased assistance being provided in relation to treaty issues, including the mutual agreement procedure.

2 OECD/UNDP (2020), *Tax Inspectors Without Borders Annual Report 2020*, available at http://tiwb.org/resources/reports-case-studies/tax-inspectors-without-borders-annual-report-2020.htm, accessed on 12 March 2021, at p. 10.

Box 1: Tax Inspectors Without Borders

Tax Inspectors Without Borders (TIWB) was launched as a joint UNDP and OECD initiative in July 2015, to support countries to build tax audit capacity.

The 2015 Addis Ababa Action Agenda recognized the need to mobilise more domestic resources for development. For many developing countries, this implies strengthening tax and other revenue collection capacities. TIWB was identified as one of the tools to support developing countries to build the capacities of national tax administration and mobilise more domestic revenues for the Sustainable Development Goals.

UNDP's country-level presence and policy and programme expertise in public financial management is complemented by the OECD's technical expertise in international tax matters and access to networks of key players in the tax field. The joint initiative complements the broader efforts of the international community to strengthen cooperation on tax matters.

TIWB Objective

The objective of the TIWB Initiative is to enable sharing of tax audit knowledge and skills with tax administrations in developing countries through a targeted, real time "learning by doing" approach. Selected experts will work with local tax officials directly on current audits and audit-related issues concerning international tax matters and general audit practices relevant for specific cases. This is a specialized area of tax audit assistance, given its focus on providing assistance on real, current cases.

For each TIWB audit assistance programme, the goal will be to enhance capacity in the tax audit practice of the developing country tax administration (Host Administration). Through TIWB Programmes, the Host Administration benefits by improving the quality and consistency of its audits, which in turn brings greater certainty and potentially more revenues for the Host Administration. Over the longer term, the overall investment climate is likely to improve and a culture of taxpayer compliance can be built through more effective enforcement. More broadly, the state-society relationship can also be enhanced through greater engagement and confidence by taxpayers in the taxation process. This may lead ultimately to more effective and accountable governance. TIWB Programmes can complement existing tax-focused assistance programmes, to bring a practical approach to applying new knowledge.

Areas and forms of assistance

TIWB is focused on promoting hands-on assistance by sending Experts to build audit and audit-related skills pertaining to specific international tax matters and the development of general audit skills within developing tax administrations. Experts will work together with tax auditors from the Host Administration on actual audit cases.

TIWB facilitates expert audit assistance in areas such as transfer pricing; thin capitalization; advance pricing arrangements; anti-avoidance rules; consumption taxes (e.g. VAT, GST); high net-worth individuals; pre-audit risk assessment and case selection; audit investigatory techniques; and industry-specific or sector-specific issues. TIWB does not cover assistance relating to customs matters nor is concerned with providing policy support, advice on legislative changes, issues related to (re)negotiations or other aspects of international tax treaties, or litigation, as existing organisations and programmes already offer support to developing country tax administrations on these matters.

The form and duration of audit assistance can vary, depending on the needs of the Host Administration as well as the types of tax matters involved, the availability of appropriate experts, and funding. For example, it may require eight weeks of assistance over three visits in the course of a six-month period.

Source: https://www.undp.org/content/undp/en/home/programmes-and-initiatives/tax-inspectors-without-borders.html and http://www.tiwb.org/about/, accessed on 12 March 2021

6.3 Capacity-building related to MAP

7. Technical assistance could also be provided to developing countries that have no or little MAP experience in the form of general training on the MAP process. That type of training, which does not require involvement in actual MAP cases between countries and does not, therefore, raise confidentiality concerns, could be provided at the national or regional level. This training could focus not only on the MAP process but also on the MAP-related commitments of the large number of countries that have joined the BEPS Inclusive Framework.[3] Active or retired tax officials of the competent authority units of countries that have substantial MAP experience should be involved in that type of capacity-building in order to make it as practical as possible.

8. The United Nations Secretariat and the OECD Secretariat have already started to provide capacity-building workshops on MAP. For example, in 2019, the United Nations, OECD and World Bank jointly delivered a MAP workshop for developing countries based on the contents of Chapter 4 of this Handbook. That workshop combined presentations on the different steps of the MAP process with a case study that allowed participants to gain hands-on experience of that process by working on a fictitious MAP case. That workshop is an example of collaboration between the partners of the Platform for Collaboration on Tax[4] which all support, in their different capacities, technical assistance and capacity building as well as knowledge creation and dissemination in developing countries.

9. Training should also be available with respect to MAP arbitration for countries that wish to adopt that mechanism.

6.4 Framework agreements

10. The functioning of the MAP may be improved through the conclusion, under paragraph 3 of Article 25, of framework agreements between the competent authorities. Such framework agreements may address procedural or administrative issues related to the MAP (as is envisaged by the second sentence of paragraph 4 of the United Nations

3 See chap. 1, para. 13.

4 See chap. 1, footnote 27.

Model Tax Convention) or may deal with specific substantive treaty issues. For instance, where several MAP cases raising similar issues are pending, such framework agreements may allow for a quicker resolution of these cases by addressing the underlying substantive treaty issues. This approach was found to be particularly useful in the case of the India-United States tax treaty: within one year of its conclusion, a framework agreement signed in January 2015 facilitated the resolution of more than 100 cases in the information technology (software development and information technology enabled services) sector.[5]

11. The usefulness of such agreements will depend on the specific situation of the countries involved. They may be particularly helpful where there is a large number of pending MAP cases between two countries. They may also facilitate future discussions between countries that have not previously discussed MAP cases or that had difficulties in addressing a few cases. In that case, the agreements would address administrative issues and procedural issues such as the conduct of regular meetings and the implementation of specific deadlines for the processing of the cases.

6.5 Use of technology

12. Since technology is ever evolving, the question arises whether new technologies could be used to improve how competent authorities deal with the MAP and, in particular, how technology can complement and make more effective the way competent authorities interact during the MAP process. For developing and least developed countries, resource constraints still pose a great challenge in meeting the requirements for a successful implementation of the MAP. This section briefly describes some technologies that may be particularly relevant to the performance of the MAP function, especially for procedural matters. New technology can facilitate the contacts and sharing of information between the taxpayers and competent authorities involved in a MAP case, facilitate documentation and filing requirements and help in setting up databases containing

5 Press release dated 16 January 2016 issued by India's Central Board of Direct Taxes, available at https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/439/PressRelease_28-1-16.pdf, accessed on 12 March 2021.

information relevant to the work of the competent authorities. The decision to implement any new technology would obviously require, especially for countries that have very few MAP cases, a careful cost-benefit analysis.

13. Technology now offers a range of tools that could be used to facilitate the contacts between the parties in a way which would make such exchanges more secure, structured and low cost by creating a common platform. The common platform may involve the use of secure clouds (i.e. shared platforms that are secure and with controlled access) or shared software (the same software programs deployed in multiple locations that are able to securely communicate with each other). Either would make it possible to deliver this sort of capability at much lower costs than in the past. When using these tools, a key consideration is the security of the shared information. Without a secure system, users would be hesitant to share sensitive information or even prevented from doing so by laws or regulations applicable in their jurisdiction.

14. In the context of a MAP, information needs to be shared between the taxpayers and competent authorities and between the competent authorities themselves. In the case of tax treaties with respect to which MAP arbitration is allowed, information also needs to be exchanged between the competent authorities and the members of the arbitration panel (and their staff, in some cases). This information must be kept confidential and can be extremely sensitive (e.g. a taxpayer's trade secrets). An access control system must be in place to provide adequate permissions to all of these parties.

15. A number of competent authorities are currently using technical platforms for processing exchange of information requests and the question arises whether the experience gained in that area can be shared and how new, innovative technologies may be used by developing countries.

16. One possible approach would be to set up a secure cloud server for the relevant dispute, to which the taxpayer and the competent authorities could upload the documents that they wish to share. The access to the documents would be restricted depending on the folder in which they are stored.

17. Technology might also help in setting feasible time schedules and deadlines as well as organizing the workflow of steps and approvals required by a MAP, thereby contributing to the timely resolution of MAP cases. Such a scheduling tool could help the parties involved to schedule their meetings more efficiently by synchronizing with their other schedules, sending timely reminders of meetings etc.

18. Technology could provide simpler access to MAP for all taxpayers as well as providing them information concerning developments in their cases. The question of access to MAP does not only concern the availability of existing information, but also the submission of new information and even the filing of a MAP request. A common platform may help ensure that relevant data is structured and presented in a consistent way, facilitating its treatment. The documentation required to file a request for MAP could also be provided online, where it could easily be updated and accessed by the competent authorities. Ideally, the tool would include pre-programmed information concerning the type of documents necessary and a separate upload of each document type would be possible.

19. Similarly, where arbitration may be used to resolve issues that arise in a MAP case, technology could facilitate cost-effective cooperation between the competent authorities and the arbitrators as regards communications, meetings with arbitrators and transfer of documentation.

20. In addition, technology could help the competent authorities with time management concerning MAP cases prior to arbitration. The deadline before which the MAP has to be resolved and the timeframe recommended for certain actions may be automatically calculated and an additional electronic notification shall be sent as an "alert" to each of the officials assigned to a MAP case, letting them know that the deadline to complete a MAP prior to arbitration is approaching.

21. Technology could also help protect the privacy concerns of taxpayers in arbitration. Since arbitration involves third parties who may receive sensitive information concerning the taxpayer, technology could help provide a secure and protected environment under which such information is accessible to the arbitrators for limited use under the arbitration process.

6.6 Non-binding dispute resolution (NBDR) mechanisms

6.6.1 The possibility of using NBDR in the MAP context

22. As explained in Chapter 5, following amendments to both the United Nations and OECD models, countries, especially those with long experience with MAP, have undertaken to resolve "stalled" MAP cases by way of arbitration. The arbitration procedure applicable to the relevant tax treaties is part of the MAP process and is only triggered where negotiations between the competent authorities have been unsuccessful in resolving a case within a two-year or three-year period.[6]

23. It has been suggested that expert evaluation, mediation and other forms of non-binding dispute resolution (NBDR) could constitute an alternative (e.g. for countries which question the appropriateness of arbitration for resolving tax disputes in their respective contexts), or a precursory step, to arbitration.

24. NBDR as discussed in this section would not require any prior commitment to a binding resolution of the matter in dispute. It would be part of the MAP process and if the competent authorities were able to resolve a case through the assistance of NBDR, they would implement the agreed solution though the conclusion of a mutual agreement as in any other case resolved through the MAP.

25. The Commentary on Article 25 of both the United Nations and OECD models recognizes the possibility of using NBDR in order to assist in the resolution of MAP cases. As noted in paragraphs 41 and 41.1 of the United Nations Commentary:[7]

> 41. It is recognized that, for some countries, the process of agreement might well be facilitated if competent authorities, when faced with an extremely difficult case or an impasse, could call, either informally or formally, upon outside experts to give an advisory opinion or otherwise assist in the resolution of the matter. Such experts could be persons currently or previously associated with other tax administrations

6 See chap. 5, para. 18, which explains that the United Nations Model Tax Convention provides for three years while the OECD Model Tax Convention provides for two years.

7 See also paragraphs 86 – 87 of the Commentary on Article 25 of the OECD Model tax Convention.

> and possessing the requisite experience in this field. In essence, it would largely be the personal experience of these experts that would be significant. This resort to outside assistance could be useful even where the competent authorities are not operating under the standard of an "agreement to agree", since the outside assistance, by providing a fresh point of view, may help to resolve an impasse.
>
> 41.1 The possibility for such assistance may include the utilization of non-binding methods of dispute resolution, such as mediation. For countries that wish to use such procedures, there are several non-binding methods that can be used to resolve disputes between parties at an early or later stage of the competent authority process. Such non-binding means of dispute resolution could range from facilitating the relational aspects of the competent authority process to providing insights or views on the substantive tax matters at hand in the dispute. Such methods are presently used for the resolution of tax disputes under the domestic laws of a number of countries. These procedures should, however, be utilized with due regard to issues such as the timing and duration of the procedures, the mechanism and criteria for selection of the mediator or other such appointed person and, the treatment of confidential information.

26. Unlike arbitration, where the arbitrators provide a solution to issues that the competent authorities are unable to resolve within a certain period of time, NBDR would involve an independent third person who could facilitate the reaching of an agreement but who would not decide the case for the parties (which is why this approach is referred to as "non-binding").

27. A widespread form of multi-tiered dispute resolution mechanism found in non-tax international treaties and commercial contracts is to: (i) give the parties a certain time for reaching agreement through negotiation; (ii) then obtain input of an expert or mediator; and (iii) finally, if these "non-binding" attempts are not successful within the fixed timeframe, the dispute can (or must) be escalated to binding dispute settlement (e.g. arbitration).

28. While there does not seem to be any tax treaty that provides for the use of a similar multi-tiered process, it has been suggested that the type of NBDR described in (ii) could be used in MAP cases. Proponents of that suggestion refer to the fact that NBDR has been used by a number of tax administrations, with varying degrees of success, to facilitate the resolution of domestic tax disputes.

29. It should be noted, however, that the experience of NBDR in the domestic tax context may not be easily transferred to the MAP context because the MAP process involves tax officials from two countries rather than a taxpayer and the tax administration of a country. Although NBDR is frequently used in the domestic tax context, there are no reported cases where NBDR has been used to successfully resolve a MAP case.

30. This section focusses on the possible use in the MAP context of two specific NBDR mechanisms – expert advice and mediation.

31. Expert advice is a NBDR mechanism that consists of a technical expert reviewing evidence presented by both parties. This procedure involves an independent third party acting as an expert and rendering advice, in contrast to a judge or arbitrator appointed to decide a dispute. In such a procedure, the determination made by the expert is advisory in nature with respect to the issue referred to by the parties. In a non-tax context, expert advice is especially useful with respect to disputes related to valuation as well as disputes of a purely technical nature in commercial or business sectors, including in particular financial services, hydrocarbons, environmental issues, water resources or renewable energy sources.

32. Mediation is a form of process-related assistance that involves the use of a mediator or facilitator to aid in solving a dispute. As with expert advice, the input of a mediator is advisory in nature. The degree of activity of the mediator can range from a rather passive to a more active role, depending on the needs of the parties and the nature of the dispute. It can include, for instance, monitoring the treatment of the dispute, making process-related suggestions, facilitating the discussions, identifying missing information, discussing with the parties the strengths and weaknesses of their respective arguments and offering input on total or partial resolution of the dispute via compromise of respective positions. This mechanism is frequently used to resolve various types of disputes outside the MAP context.

6.6.2 Different views on the appropriateness of using NBDR in the MAP context

33. Proponents of using NBDR in the MAP context suggest that doing so could have the following benefits:

— May help develop confidence in international tax dispute resolution under the United Nations Model Tax Convention in a manner consistent with each country's comfort level and allow the competent authorities to maintain control of the case resolution
— May help clarify complicated issues and fact patterns and better target the discussions between tax authorities, thereby allowing them to reach a MAP agreement more efficiently
— May provide a flexible and cost-efficient way for the competent authorities to get the views of third parties on disputed issues
— May provide a means of levelling the playing field where the experience of the competent authorities is unequal

34. Others, however, argue that the addition of NBDR to the MAP could have the following disadvantages:

— As NBDR is not binding, there is no guarantee that the case will be resolved
— If no agreement is found through the NBDR process, the dispute remains unresolved despite the additional costs incurred. While the MAP process would then continue, the NBDR may have caused further delays, which may be particularly relevant where the dispute has also been submitted to the domestic litigation process in one or both countries
— Time and resources would need to be used to develop and test NBDR in the MAP context
— Finding independent third parties that have the appropriate skills and the necessary confidence of both parties may require time and efforts

6.6.3 Possible use of expert advice and mediation in MAP

35. In the MAP context, expert advice could involve the competent authorities relying on the services of a professional with experience in the issues that the parties are unable to resolve.

36. It has been suggested that mediation could be adapted to the MAP process in specific situations. It could, for instance, be used between countries with different levels of experience to try to build confidence and experience in the handling of MAP cases or to overcome an impasse.

37. A mediator could offer an opportunity for the competent authorities to view a specific case, or the MAP process itself, from a different perspective. Such perspective could be acquired through the mediator's restatement of the positions or of the critical issues, which could highlight elements of the case or procedural context that are not possible to be recognized when seen from the perspective of a tax administration which seeks to resolve a MAP case while keeping in mind the need to protect its country's taxing powers in accordance with the relevant treaty provisions.

38. As explained in Chapter 4, treaty provisions based on Article 25 of both the United Nations and OECD models impose a legal obligation on the competent authorities to endeavour to resolve admissible MAP cases presented pursuant to Art. 25(1). These treaty provisions do not, however, prescribe the process through which the competent authorities should do so. Subject to the possible application of other treaty provisions (including in particular the confidentiality requirements of Article 26), the competent authorities are therefore free to use mechanisms such as NBDR when seeking to resolve MAP cases and, to the extent that such mechanisms are non-binding, no treaty provisions are required in order to allow their use. The use of such mechanisms does not, however, restrict the competent authorities' obligation to endeavour to resolve MAP cases: a competent authority could not, therefore, justify a failure to genuinely attempt to resolve a MAP case on the fact that NBDR was used in that case.

39. Since NBDR mechanisms do not require competent authorities to implement solutions with which they do not agree, it is unlikely that a country which has committed to MAP would have serious domestic law issues with using such mechanisms. To the extent that a competent authority has the legal authority to negotiate a MAP case and enter into a mutual agreement, domestic law is unlikely to prevent it from committing, when doing so, to a process whose outcome is not binding upon it without its consent.[8]

40. A different issue is whether countries should provide the terms and conditions for the use of NBDR for MAP proceedings on a case-by-case basis or adopt a general framework for doing so.

8 The extensive practical and legal experience with the use of NBDR in non-tax areas may be consulted for guidance on domestic legal aspects.

41. If they are determined on a case-by-case basis, these terms and conditions could be agreed informally by the competent authorities when deciding to use NBDR in a specific case or could be documented more formally in a procedural mutual agreement concluded under paragraph 3 of Article 25. The conclusion of such a procedural mutual agreement would seem more important if competent authorities decided to implement NBDR through a general framework that could apply to multiple cases. Such a general framework could avoid the need to renegotiate over and over the process through which NBDR could be used. On the other hand, a disadvantage could be inflexibility, especially if the rules cannot easily be amended.

42. An alternative approach could be to agree, through a procedural mutual agreement, on a general framework with a set of default rules and allow the competent authorities to negotiate alternative or additional rules applicable to any specific case.

43. The terms and conditions governing the use of NBDR as part of the MAP process could include the following:

- Nature of the procedure: expert advice or mediation, or the option to combine both
- When and how should NBDR be initiated
- Whether the use of NBDR would be mandatory
- How to determine the issues to be submitted to NBDR
- The different stages of the NBDR procedure and whether some of them could be omitted in specific cases
- If necessary, clarification of the interaction with domestic dispute resolution mechanisms and tax treaty arbitration (if available)
- Default timelines
- The process of selection of the expert or mediator
- The role, function and attributions of the expert or mediator
- The interaction between the expert and the mediator if they are different and both are used in the same case
- Issues related to the eligibility, qualifications, potential conflicts of interest (and disclosure thereof), vetting and appointment of the expert or mediator.

- — Impartiality obligations and rules on the safeguarding of the independence of the expert or mediator
- — The confidentiality obligations of the expert or mediator and the regime applicable to disclosed information
- — Guidance on whether information submitted, or proposals made, during NBDR discussions may be disclosed in subsequent court proceedings or other contexts (so-called “without prejudice rules”)
- — Logistical aspects of the NBDR process (place, language, translations, participants, transcripts and meeting minutes etc.)
- — Whether the expert or mediator is allowed to communicate separately with a competent authority in the hope of finding grounds for mutual agreement without disclosing the contents of the discussion or the results to the other competent authority
- — The possibility and extent of the participation of the taxpayer
- — The termination of proceedings
- — Who should pay the costs of the NBDR process

Many of these issues are similar to those addressed in the parts of Chapter 5 and of the Commentary on Article 25 of the United Nations and OECD models that deal with the logistical aspects of arbitration.

44. As already noted, NBDR could be envisaged either in the absence of MAP arbitration or as a supplementary means of dispute resolution preceding arbitration.

45. NBDR as a precursory step to arbitration could increase the efficiency of arbitration, notably because the arbitration could more easily focus on the key issues and could, if the competent authorities agreed, make use of specific fact findings or economic evaluations made by an independent expert.

ANNEX

List of Participants in the Subcommittee on Dispute Avoidance and Resolution

(Established on 20 October 2017)

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