

Public Discussion Draft

**BEPS ACTION 14:
MAKE DISPUTE
RESOLUTION
MECHANISMS MORE
EFFECTIVE**

18 December 2014 – 16 January 2015



**PROPOSED DISCUSSION DRAFT ON ACTION 14:
MAKE DISPUTE RESOLUTION MECHANISMS MORE EFFECTIVE**

18 December 2014

**WORK ON ACTION 14 (MAKE DISPUTE RESOLUTION MECHANISMS MORE EFFECTIVE)
OF THE BEPS ACTION PLAN**

In July 2013, the OECD published its *Action Plan on Base Erosion and Profit Shifting*.¹ The Action Plan identifies 15 actions to address BEPS in a comprehensive manner and sets deadlines to implement these actions.

The Action Plan recognises that the actions to counter BEPS must be complemented with actions that ensure certainty and predictability for business. Work to improve the effectiveness of the mutual agreement procedure (MAP) in resolving treaty-related disputes is thus an important component of the work on BEPS issues. Action 14 (Make dispute resolution mechanisms more effective) reads as follows:

ACTION 14

Make dispute resolution mechanisms more effective

Develop solutions to address obstacles that prevent countries from solving treaty-related disputes under MAP, including the absence of arbitration provisions in most treaties and the fact that access to MAP and arbitration may be denied in certain cases.

As part of the transparent and inclusive consultation process mandated by the Action Plan, the Committee on Fiscal Affairs (CFA) invites interested parties to send comments on this discussion draft, which includes the preliminary results of the work carried out pursuant to Action 14.

It is recognised that, in spite of several attempts to make dispute resolution mechanisms work better, further progress remains to be achieved, especially at a time when the number of disputes has increased. Action 14 is a unique opportunity to make a difference in this area and to overcome traditional obstacles. It is also recognised that there is no consensus on moving towards universal mandatory binding MAP arbitration. Therefore, complementary solutions should be provided which will have a practical, measurable impact, rather than merely providing additional measures or guidance which may not be fully used or implemented. This discussion draft is the preliminary result of the work done to identify comprehensively the obstacles that prevent countries from resolving disputes through the MAP and to develop possible measures to address these obstacles. The discussion draft must be read in the broader context of the intention to introduce a three-pronged approach designed to represent a step change in the resolution of treaty-related disputes through the MAP. This three-pronged approach would (i) consist in political commitments to effectively eliminate taxation not in accordance with the Convention (such political commitments reflecting the political dimension of the BEPS Project), (ii) provide new measures to

1. Available at: <http://www.oecd.org/ctp/BEPSActionPlan.pdf>.

improve access to the MAP and improved procedures (this discussion draft describes the envisaged measures) and (iii) establish a monitoring mechanism to check the proper implementation of the political commitment.

The Committee on Fiscal Affairs (the Committee) invites all interested parties to comment on the obstacles and options described in this note. The Committee also invites stakeholders to identify other obstacles to an effective MAP that are not addressed in this discussion draft, as well as additional options to address obstacles identified in this note or in comments. In many cases, this discussion draft invites comment with respect to specific questions or issues; commentators should feel free to provide examples with respect to these and any other questions or issues not specifically identified.

The views and proposals included in this discussion document do not represent the consensus views of either the Committee on Fiscal Affairs or its subsidiary bodies but rather are intended to provide stakeholders with substantive proposals for analysis and comment.

Comments should be sent by **16 January** at the latest (no extension will be granted) and should be sent in Word format by email to taxtreaties@oecd.org (in order to facilitate their distribution to government officials). Comments should be addressed to: Marlies de Ruiter, Head, Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA.

Please note that all comments received regarding this consultation draft will be made publicly available. Comments submitted in the name of a collective “grouping” or “coalition”, or by any person submitting comments on behalf of another person or group of persons, should identify all enterprises or individuals who are members of that collective grouping or coalition, or the person(s) on whose behalf the commentator(s) are acting.

Public consultation meeting

Persons and organisations who will send comments on this discussion document are invited to indicate whether they wish to speak in support of their comments at a public consultation meeting on Action 14 that is scheduled to be held in Paris at the OECD Conference Centre on 23 January 2015. Persons selected as speakers will be informed by email by 16 January at the latest.

This consultation meeting will be open to the public and the press.

Due to space limitations, priority will be given to persons and organisations who register first (we reserve the right to limit the number of participants from the same organisations).

Persons wishing to attend this public consultation meeting should fill out their request for registration online as soon as possible **and by 9 January 2015 at the latest**. Confirmation of participation, including venue access details, will be sent by email to participants by 16 January at the latest.

This meeting will also be broadcast live on the Internet and can be accessed online. No advance registration will be required for this Internet access.

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MAKE DISPUTE RESOLUTION MECHANISMS MORE EFFECTIVE

Action 14 of the BEPS Action Plan

INTRODUCTION

1. At the request of the G20, the OECD published its Action Plan on Base Erosion and Profit Shifting (the BEPS Action Plan)¹ in July 2013. The BEPS Action Plan identified fifteen actions to address base erosion and profit shifting in a comprehensive manner and set deadlines to implement these actions.

2. The Action Plan recognises that the actions to counter BEPS must be complemented with actions that ensure certainty and predictability for business. The work on Action 14, which seeks to improve the effectiveness of the mutual agreement procedure (MAP) in resolving treaty-related disputes, is thus an important component of the work on BEPS issues and reflects the comprehensive and holistic approach of the BEPS Action Plan. The relevant part of the Action Plan reads as follows:

The actions to counter BEPS must be complemented with actions that ensure certainty and predictability for business. Work to improve the effectiveness of the mutual agreement procedure (MAP) will be an important complement to the work on BEPS issues. The interpretation and application of novel rules resulting from the work described above could introduce elements of uncertainty that should be minimised as much as possible. Work will therefore be undertaken in order to examine and address obstacles that prevent countries from [re]solving treaty-related disputes under the MAP. Consideration will also be given to supplementing the existing MAP provisions in tax treaties with a mandatory and binding arbitration provision.

ACTION 14

Make dispute resolution mechanisms more effective

Develop solutions to address obstacles that prevent countries from [re]solving treaty-related disputes under MAP, including the absence of arbitration provisions in most treaties and the fact that access to MAP and arbitration may be denied in certain cases.

3. It is recognised that, in spite of several attempts to make dispute resolution mechanisms work better, further progress remains to be achieved, especially at a time when the number of disputes has increased. Action 14 is a unique opportunity to make a difference in this area and to overcome traditional obstacles. It is also recognised that there is no consensus on moving towards universal mandatory binding MAP arbitration. Therefore, complementary solutions should be provided which will have a practical, measurable impact, rather than merely providing additional measures or guidance which may not be fully

1. Available at: <http://www.oecd.org/ctp/BEPSActionPlan.pdf>.

used or implemented. This discussion draft is the preliminary result of the work done to identify comprehensively the obstacles that prevent countries from resolving disputes through the MAP and to develop possible measures to address these obstacles. The discussion draft must be read in the broader context of the intention to introduce a three-pronged approach designed to represent a step change in the resolution of treaty-related disputes through the MAP. This three-pronged approach would (i) consist in political commitments to effectively eliminate taxation not in accordance with the Convention (such political commitments reflecting the political dimension of the BEPS Project), (ii) provide new measures to improve access to the MAP and improved procedures (this discussion draft describes the envisaged measures) and (iii) establish a monitoring mechanism to check the proper implementation of the political commitment.

4. It is expected that the work on Action 14 will result in a political commitment to substantially improve the MAP process through the adoption of specific measures intended to address the obstacles that currently prevent the resolution of treaty-related disputes. The political commitment and the measures through which it will be implemented will be guided by the following four principles:

1. ***Ensuring that treaty obligations related to the mutual agreement procedure are fully implemented in good faith.***
2. ***Ensuring that administrative processes promote the prevention and resolution of treaty-related disputes.***
3. ***Ensuring that taxpayers can access the mutual agreement procedure when eligible.***
4. ***Ensuring that cases are resolved once they are in the mutual agreement procedure.***

5. For each of the above four principles, the discussion draft lists obstacles that may prevent the principle from being fully implemented and puts forward options as to how these obstacles could be addressed.

6. The Committee on Fiscal Affairs (the Committee) invites all interested parties to comment on the obstacles and options described in this note. The Committee also invites stakeholders to identify other obstacles to an effective MAP that are not addressed in this discussion draft, as well as additional options to address obstacles identified in this note or in comments. In many cases, this discussion draft invites comment with respect to specific questions or issues; commentators should feel free to provide examples with respect to these and any other questions or issues not specifically identified. The Committee stresses, however, that this note is merely intended to provide stakeholders with substantive proposals for analysis and comment; it does not represent the consensus views of the Committee or of its subsidiary bodies on what are the obstacles that prevent the resolution of treaty-related disputes through the MAP or on the various options put forward to address these obstacles. In particular, not all countries associated to the OECD/G20 BEPS Project agree that mandatory and binding arbitration is an appropriate tool to resolve issues that prevent competent authority agreement in a MAP case.

7. Specific measures that will result from the work on Action 14 will constitute a minimum standard to which participating countries will commit. Notwithstanding this minimum standard, it is expected that the final results of the work on Action 14 will also include additional measures (such as, for example, MAP arbitration) that some countries may also wish to commit to adopt in order to address obstacles to an effective MAP in a more comprehensive way.

8. The exact contents of the political commitment and the specific measures through which it will be implemented will be determined as part of the future work on Action 14. It is expected that these specific measures will be complemented by a process for monitoring the overall functioning of the mutual

agreement procedure, including assessment of the measures to which countries will have committed (as the monitoring process will depend on the nature of the measures finally adopted, no specific proposals for such a monitoring process have been included in this discussion draft, although it is envisaged that an appropriate forum of competent authorities could be responsible for such monitoring; such a forum would also facilitate experience sharing and capacity building and, more generally, work to foster co-operative and collaborative competent authority relationships).

1. ENSURING THAT TREATY OBLIGATIONS RELATED TO THE MUTUAL AGREEMENT PROCEDURE ARE FULLY IMPLEMENTED IN GOOD FAITH

9. The dispute resolution mechanism provided by Article 25 of the OECD Model forms an integral part of the obligations assumed by a Contracting State in entering into a tax treaty and the provisions of the Article must be fully implemented in good faith, in accordance with its terms and in the light of the object and purpose of tax treaties. This section addresses two obstacles that may prevent the full implementation of Article 25 and includes options aimed at removing them.

A. *Absence of an obligation to resolve MAP cases presented under Article 25(1)*

Description of the obstacle

10. Paragraph 2 of Article 25 provides that competent authorities “shall endeavour” to resolve a MAP case by mutual agreement. It has been argued that the absence of an obligation to resolve an Article 25(1) MAP case is itself an obstacle to the resolution of treaty-related disputes through the MAP (although it is important to note that Article 25(2) entails an obligation to effectively attempt to resolve the case).

OPTION 1 – Clarify in the Commentary the importance of resolving cases presented under Article 25(1)

The following paragraph could be added to the Commentary on Article 25 in order to emphasise that the mutual agreement procedure is an integral part of the obligations that follow from concluding a tax treaty:

Add the following paragraph 5.1 to the Commentary on Article 25:

5.1 *The undertaking to resolve by mutual agreement cases of taxation not in accordance with the Convention is an integral part of the obligations assumed by a Contracting State in entering into a tax treaty and must be performed in good faith. In particular, the requirement in paragraph 2 that the competent authority “shall endeavour” to resolve the case by mutual agreement with the competent authority of the other Contracting State means that the competent authorities are obliged to seek to resolve the case in a principled, fair and objective manner, on its merits, in accordance with the terms of the Convention and applicable principles of international law.*

B. *Absence of paragraph 2 of Article 9 in some tax treaties*

Description of the obstacle

11. Most countries consider that the economic double taxation resulting from the inclusion of profits of associated enterprises under paragraph 1 of Article 9 is not in accordance with the object and purpose of

the Convention and falls within the scope of the mutual agreement procedure under Article 25.² Some countries, however, take the position that, in the absence of a treaty provision based on paragraph 2 of Article 9, they are not obliged to make corresponding adjustments or to grant access to the MAP with respect to the economic double taxation that may otherwise result from a primary transfer pricing adjustment by a treaty partner. Such a position may frustrate a primary objective of tax treaties – the elimination of double taxation – and prevent bilateral consultation to determine appropriate transfer pricing adjustments.

OPTION 2 – Ensure that paragraph 2 of Article 9 is included in tax treaties

Participating countries could commit to include paragraph 2 of Article 9 in all their tax treaties, using the multilateral instrument envisaged by Action 15 where appropriate. It would also be clarified that such a change is not intended to create any negative inference with respect to treaties that do not currently contain a provision based on paragraph 2 of Article 9.

2. ENSURING THAT ADMINISTRATIVE PROCESSES PROMOTE THE PREVENTION AND RESOLUTION OF TREATY-RELATED DISPUTES

12. Appropriate tax administration practices are important to ensure an environment in which competent authorities are able to fully and effectively carry out their mandate. The effectiveness of the MAP may be undermined where a competent authority is not sufficiently independent, where a competent authority is not provided with adequate resources or where the competent authority function is evaluated based on inappropriate performance indicators. In addition, competent authorities may not actively employ their authority under Article 25(3) to pre-empt potential disputes by reaching mutual agreement on matters of a general nature involving treaty interpretation or application and countries may not have implemented bilateral APA programmes. This section deals with these various obstacles.

13. Administrative processes that promote the prevention and resolution of treaty-related disputes are being comprehensively examined in the parallel work being undertaken by the Forum on Tax Administration's MAP Forum (the FTA MAP Forum). The FTA MAP Forum has recognised, for example, that audit programmes which are not aligned with international norms with respect to either principle or procedure may significantly hinder the functioning of mutual agreement procedures. Audit practices are accordingly a strategic focus of the FTA MAP Forum³, which will discuss the complex interactions between competent authorities and their respective audit functions in order to identify best practices for ensuring that mutual agreement procedures are not burdened by audit practices such as audit settlements that block MAP access or insufficient global awareness in audit functions. It is anticipated that the results of the work on Action 14 and the work of the FTA MAP Forum will be complementary and mutually reinforcing.

2. See generally paragraphs 10 to 12 of the Commentary on Article 25.

3. See the "Multilateral Strategic Plan on Mutual Agreement Procedures: A Vision for Continuous MAP Improvement" (available at: <http://www.oecd.org/site/ctpfta/map-strategic-plan.pdf>), adopted at the Ninth Meeting of the Forum on Tax Administration (held in Dublin on 23-24 October 2014), hereinafter referred to as the "FTA MAP Forum Strategic Plan".

C. Lack of independence of the competent authority and inappropriate influence of considerations related to the negotiation of possible treaty changes

Description of the obstacle

14. In the context of the mutual agreement procedure, the role of the competent authority is to take an objective view of the provisions of the applicable treaty and apply it to the facts of the taxpayer's case, with a view to eliminating taxation not in accordance with the terms of the treaty. Objectivity may be compromised where the competent authority function is not sufficiently independent from a tax administration's audit or examination function (*i.e.* from the field personnel who were directly or indirectly involved in the initial adjustment). As emphasised in the FTA MAP Forum Strategic Plan, the empowerment challenges faced by competent authorities are a critical issue: "*The office and authority of competent authorities derive from those bilateral conventions and, in order to discharge their responsibilities effectively, competent authorities must not be unduly influenced or constrained by competing considerations derived from policies, practices, or goals associated with other offices within their administrations.*"

15. Similar issues may also arise where the competent authority also performs a policy-making function (*e.g.* tax treaty negotiation) and does not adequately distinguish between its role of administering treaties that have entered into force and its role of negotiating changes to these treaties. Challenges to the objective application of existing treaty provisions may be presented where a competent authority's approach to a MAP case is influenced by changes that the competent authority would like to make to its country's treaties.

OPTION 3 – Ensure the independence of a competent authority

Participating countries could commit to adopt the best practices currently included in the OECD Manual on Effective Mutual Agreement Procedures (MEMAP)⁴ concerning the independence of a competent authority. In particular, they should take the necessary steps to ensure the autonomy of the competent authority from the audit and examination functions, as well as to guarantee, in practice, an appropriate distinction between the objective application of existing treaties and the forward-looking determination of the policy to be adopted and reflected in future treaties.

D. Lack of resources of a competent authority

Description of the obstacle

16. The lack of sufficient resources (personnel, funding, training, etc.) allocated to a competent authority in order to deal with its inventory of MAP cases is likely to result in an increasing inventory of such cases and in increased delays in processing these cases. This will have a fundamental impact on a Contracting State's ability to operate an effective MAP programme.

OPTION 4 – Provide sufficient resources to a competent authority

Participating countries could commit to adopt the best practices currently included in the MEMAP concerning the provision of sufficient resources to their competent authorities. They could, in particular,

4. Available at: <http://www.oecd.org/ctp/38061910.pdf>.

commit to provide their competent authorities with sufficient resources in terms of personnel, funding, training, etc. to carry out their mandate to resolve cases of taxation not in accordance with the provisions of a tax treaty in a timely and efficient manner.

E. Performance indicators for the competent authority function and staff

Description of the obstacle

17. The evaluation of the competent authority function or staff based on criteria such as sustained audit adjustments or tax revenue may be expected to create disincentives to the competent authority's objective consideration of MAP cases and to present obstacles to good faith bilateral MAP negotiations.

OPTION 5 – Use of appropriate performance indicators

Participating countries could commit to adopt the best practices currently included in the MEMAP concerning the use of appropriate performance indicators for their competent authority functions and staffs based on factors such as consistency, time to resolve cases, and principled and objective MAP outcomes and not on factors such as sustained audit adjustments or maintaining tax revenues already collected.

F. Insufficient use of paragraph 3 of Article 25

Description of the obstacle

18. Paragraph 3 of Article 25 authorises competent authorities “to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention”. The question may arise, however, whether competent authorities make use of this authority. The second sentence of paragraph 3 provides in addition that competent authorities “may also consult together for the elimination of double taxation not provided for in the Convention”, although the competent authorities of some countries consider that they may lack the legal authority to resolve issues under that sentence. Finally, the legal value and enforceability of a mutual agreement reached under that paragraph is sometimes questioned (whilst a similar issue could theoretically arise with respect to mutual agreements reached under paragraph 2 of Article 25, this is unlikely to be a practical issue to the extent that a taxpayer's consent is typically requested before such a mutual agreement is finalised).

OPTION 6 – Better use of paragraph 3 of Article 25

Participating countries could commit to using paragraph 3 of Article 25 more effectively in order to reinforce the consistent bilateral application of tax treaties. In particular –

- Participating countries could commit to make more use of the authority provided by the first sentence of Article 25(3) and, where an Article 25(3) mutual agreement relates to a general matter which affects the application of the treaty to all taxpayers or to a category of taxpayers (rather than to a specific taxpayer's MAP case), to publish the agreement in order to provide guidance and prevent future disputes.
- Participating countries could commit to adopt the best practices currently included in the MEMAP concerning the use of the Article 25(3) power to relieve double taxation in cases not provided for in the Convention (*e.g.* in the case of a resident of a third State having permanent establishments in

both Contracting States – see paragraph 55 of the Commentary on Article 25).

In addition, changes to the Commentary on Article 3 could expand upon existing guidance regarding the role of Article 25(3) mutual agreements in resolving difficulties or doubts as to the application or interpretation of the Convention where such difficulties or doubts arise as a result of an incompletely or ambiguously defined term or a conflict in meaning under the laws of the Contracting States. Additional changes to the Commentary on Article 25 could also clarify the legal status of an Article 25(3) mutual agreement, making specific reference to the principles of international law for the interpretation of treaties.

G. Audit settlements as an obstacle to MAP access

Description of the obstacle

19. Field auditors in some countries may, on occasion, seek to influence taxpayers not to utilise their right to initiate a mutual agreement procedure in relation to audit adjustments that result in taxation not in accordance with an applicable tax treaty (*e.g.* by entering into a settlement with the taxpayer under which the tax authorities will agree not to apply penalties in return for the taxpayer’s waiver of its right to seek MAP assistance under the applicable treaty). Taxpayers may feel pressured into giving up access to the mutual agreement procedure if they are given the choice between a high assessment without any suspension of collection, but with access to MAP, or a relatively moderate assessment without access to MAP. Taxpayers may additionally accept such settlements based on broader concerns for their future relationship with the tax administration involved. Such audit settlements may be a significant obstacle to the proper application of the treaty as well as to the functioning of the mutual agreement procedure. They lead to situations in which taxation not in accordance with the Convention remains whilst the treaty partner is not aware of the situation and may be vulnerable to self-help measures taken by the taxpayer. As a result of such settlements, the competent authority of the country where the audit took place may also remain unaware that the treaty has been improperly applied and is thus unable to take appropriate measures to ensure that the treaty is applied according to its object and purpose.

OPTION 7 – Ensure that audit settlements do not block access to the mutual agreement procedure

Participating countries that allow their tax administrations to conclude audit settlements with respect to treaty-related disputes which preclude a taxpayer’s access to the mutual agreement procedure could commit to take appropriate steps to discontinue that practice or to implement procedures for the spontaneous notification of the competent authorities of both Contracting States of the details of such settlements. Changes to the Commentary on Article 25 could also address the obstacles to an effective mutual agreement procedure created by audit settlements.

20. The FTA MAP Forum Strategic Plan recognises the importance of the “global awareness” of the audit functions involved in international matters – *i.e.* awareness of (i) the potential for creating double taxation, (ii) the impact of proposed adjustments on one or more other jurisdictions and (iii) the processes and principles by which competing jurisdictional claims are reconciled by competent authorities. In this regard, stakeholders are invited to comment on best audit practices that reflect an appropriate global awareness and that facilitate an effective mutual agreement procedure.

H. Lack of advance pricing arrangement (APA) programmes

Description of the obstacle

21. An advance pricing arrangement (APA) is an “arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and 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”. Where concluded bilaterally between treaty partner competent authorities, bilateral APAs provide an increased level of tax certainty in both jurisdictions, lessen the likelihood of double taxation and may proactively prevent transfer pricing disputes. To date, however, not all countries have implemented bilateral APA programmes.

OPTION 8 – Implement bilateral APA programmes

Participating countries could commit to implement bilateral Advance Pricing Arrangement (APA) programmes.

I. Failure to consider the implications of a taxpayer’s MAP or APA case for other tax years

Description of the obstacle

22. In certain cases, a request for competent authority assistance in respect of a specific adjustment to income may present recurring issues which will also be relevant in previous or subsequent filed tax years. Some competent authorities may allow taxpayers also to request MAP assistance with respect to such recurring issues for these other filed tax years, provided that the relevant facts and circumstance are the same and subject to the verification of such facts and circumstances. Although such practices may help to avoid duplicative MAP requests and permit a more efficient use of competent authority resources, not all countries have in place administrative processes to allow them.

23. Similar issues may be presented in certain cases where the issues resolved through an advance pricing arrangement are relevant with respect to previous filed tax years not included within the original scope of the APA. Such a situation could arise, for example, where the taxpayer has missed the deadline for requesting an APA with respect to those earlier tax years, regardless of whether any adjustment or MAP request has been made with respect to such earlier years. In some countries, competent authorities will also consider the “roll-back” of the APA to previous years under appropriate circumstances where the facts and circumstances are the same, and subject to the verification of such facts and circumstances. Whilst the roll-back of advance pricing arrangements may be helpful to prevent or resolve potential transfer pricing disputes, not all countries that have implemented APA programmes provide for roll-backs.

OPTION 9 – Implement administrative procedures to permit taxpayer requests for MAP assistance with respect to recurring (multi-year) issues and the roll-back of APAs

Participating countries could commit, in certain cases and after an initial tax assessment, to implement appropriate procedures to permit taxpayer requests for the multi-year resolution 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.

Participating countries that have implemented APA programmes could similarly commit to provide for the roll-back of advance pricing arrangements in appropriate cases, subject to the applicable time limits

provided by domestic law (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.

3. ENSURING THAT TAXPAYERS CAN ACCESS THE MUTUAL AGREEMENT PROCEDURE WHEN ELIGIBLE

24. Certain of the main obstacles to the resolution of treaty-related disputes through the mutual agreement procedure are issues regarding the extent of the treaty obligation to provide MAP access. Such issues are likely to become more significant as a result of the work on BEPS, as more stringent rules are implemented and tax administrations are required to develop both practical experience and common interpretations in relation to new tax treaty and transfer pricing rules. This section discusses various obstacles to MAP access and options to address them.

J. Complexity and lack of transparency of the procedures to access and use the MAP

Description of the obstacle

25. Where procedures to access and use the MAP are not transparent or are unduly complex, taxpayers may not seek MAP assistance and, as a result, may face unrelieved double taxation or otherwise improperly be denied treaty benefits.

OPTION 10 – Improve the transparency and simplicity of the procedures to access and use the MAP

Participating countries could commit to adopt the best practices currently included in the MEMAP concerning the transparency and simplicity of the procedures to access and use the mutual agreement procedure, which should minimise the formalities involved in the MAP process taking into account the challenges that may be faced by taxpayers. This would include a commitment –

- To develop and publicise rules, guidelines and procedures for the use of the MAP (and to provide, where possible, appropriate notice to taxpayers of such guidance).
- To identify the office that has been delegated the responsibility to carry out the competent authority function (along with contact details).

K. Excessive or unduly onerous documentation requirements

Description of the obstacle

26. Article 25(2) MAP cases are generally initiated by a taxpayer's request for competent authority assistance under Article 25(1). Through such a request, the taxpayer notifies the competent authority that it considers that the actions of one or both of the Contracting States have resulted or will result in taxation not in accordance with the provisions of a treaty. Such a request must be accompanied by complete and accurate information to enable the competent authority to understand and evaluate the taxpayer's objection. Excessive or unduly onerous documentation requirements may, however, discourage requests for MAP assistance and be an obstacle to an effective mutual agreement procedure.

OPTION 11 – Provide additional guidance on the minimum contents of a request for MAP assistance

Participating countries could commit to adopt the best practices currently included in the MEMAP concerning the minimum contents of a request for MAP assistance. This would include a commitment –

- To identify, in public guidance, the specific information and documentation that a taxpayer is required to submit with a request for MAP assistance, seeking to balance the burdens involved in supplying such information with the complexity of the issues the competent authority is called upon to resolve. Competent authorities would in turn expect taxpayers to submit complete and accurate information consistent with such guidance, and to respond promptly to requests for missing or other relevant information.
- Where a country has not yet provided guidance and a taxpayer’s request for MAP assistance is accompanied by relevant information in line with the guidance in Section 2.2.1 of the MEMAP, a competent authority should not, without consulting the other competent authority, deny access to MAP on the basis that the taxpayer has provided insufficient information.

27. Commentators are invited to indicate whether existing country guidance or practices with respect to the information required to be submitted with a request for MAP assistance create other obstacles to the proper functioning of the mutual agreement procedure and, where this is the case, to provide suggestions on ways to address these obstacles.

L. Right to access MAP may be unclear where domestic or treaty-based anti-abuse rules have been applied

Description of the obstacle

28. There is currently considerable uncertainty as to how Article 25 should be interpreted and applied when it comes to MAP access in cases of application of a domestic law or treaty-based general anti-avoidance rule (GAAR) (or of other similar rules or legal doctrines), and current practice appears to differ significantly from country to country. Whilst paragraph 26 of the Commentary on Article 25 provides that – in the absence of a special provision – there is no *general* rule denying MAP access in cases of perceived abuse, the Commentary on Article 25 leaves open the question whether it may be justified to deny access to MAP in *some* cases involving avoidance or abuse. Paragraphs 9.1 to 9.5 of the Commentary on Article 1 are also relevant to the question whether there is an obligation to provide MAP access in cases of abuse; paragraph 9.5 provides in particular that treaty benefits may be denied through the application of an anti-abuse provision where obtaining a more favourable treatment based on the applicable treaty would be contrary to the object and purpose of the relevant treaty provisions. The guiding principle reflected in paragraph 9.5 of the Commentary on Article 1 will be incorporated into a number of tax treaties through the work on Action 6 of the BEPS Action Plan, which has developed a general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purposes test or PPT rule), according to which the benefits of a tax treaty shall not be available where one of the principal purposes of arrangements or transactions is to secure a benefit under a tax treaty and obtaining the benefit in these circumstances would be contrary to the object and purpose of the relevant provisions of the tax treaty. The interpretation and/or application of that rule would clearly fall within the scope of the MAP.

29. In this regard, it should be emphasised that the obligation to provide access to the mutual agreement procedure pursuant to paragraph 1 of Article 25 is distinct from the obligation to endeavour to resolve the case pursuant to paragraph 2 of Article 25. The provisions of paragraph 1 give the taxpayer

concerned the right to present a case to the competent authority where the taxpayer considers that there is or will be taxation not in accordance with the provisions of the Convention. To be admissible, a case presented under paragraph 1 must be presented to the competent authority of the taxpayer's State of residence (or of the State of which he is a national in cases under paragraph 1 of Article 24) within three years from the first notification of the action which gives rise to taxation not in accordance with the Convention. A competent authority should accept to consider a case that has been presented under paragraph 1 provided that the case is eligible for the mutual agreement procedure. This consideration will first involve the determination, by the competent authority to which it has been presented, of whether the taxpayer's objection appears to be justified. If that is the case, that competent authority may be able to solve the case unilaterally, *e.g.* by the State that the competent authority represents providing relief from tax levied contrary to the provisions of the Convention. A MAP case that has been accepted will only move to the second, bilateral stage of the mutual agreement procedure where it meets the two requirements provided by paragraph 2: (i) the taxpayer's objection appears to be justified to the competent authority to which it has been presented and (ii) that competent authority is not itself able to arrive at a satisfactory unilateral solution. Option 12 below concerns the threshold issue of the acceptance of a MAP case for consideration (*i.e.* MAP access); Options 13 to 15, in contrast, are intended to address obstacles that may prevent a MAP case that has been accepted pursuant to paragraph 1 of Article 25 from proceeding to the second stage of the mutual agreement procedure for bilateral resolution.

OPTION 12 – Clarify the availability of MAP access where an anti-abuse provision is applied

Where there is a disagreement between the taxpayer and the competent authority to which its MAP case is presented as to whether the conditions for the application of a treaty anti-abuse rule (*e.g.* a treaty-based rule such as the PPT rule) have been met or whether the application of a domestic anti-abuse rule conflicts with the provisions of a treaty, participating countries could commit to provide access to the mutual agreement procedure, provided the requirements of Article 25(1) are met. If participating countries would seek to limit or deny MAP access in all or certain of these cases, they could commit to specifically and expressly agree upon such limitations with their treaty partners. In addition, where a participating country would deny MAP access based on the application of domestic law or treaty anti-abuse provisions (or similar rules or doctrines), that country could commit to notify its treaty partner about the case and the circumstances involved.

M. Cases where a competent authority considers unilaterally that a taxpayer's objection is not justified

Description of the obstacle

30. As interpretations of treaty provisions may vary between treaty partners, circumstances may arise in which one competent authority does not find the objection presented by the taxpayer under paragraph 1 of Article 25 to be justified, whilst the other competent authority would find the objection to be justified. For example, some competent authorities may be hesitant or find it difficult to overturn assessments made by their own tax administrations and, consequently, may unilaterally determine, under paragraph 2 of Article 25, that the taxpayer's objection is not justified and therefore refuse to discuss the case with the competent authority of the other State (which may consider the objection to be justified). Given this dynamic, a process in which a competent authority can unilaterally determine, under paragraph 2 of Article 25, that the taxpayer's objection is not justified – and thereby prevent the case from being addressed bilaterally through the second stage of the MAP – raises legitimate issues as to the bilateral nature of treaty application and implementation.

OPTION 13 – Ensure that whether the taxpayer’s objection is justified is evaluated prima facie by both competent authorities

Where the relevant Convention follows the current wording of paragraph 1 of Article 25, participating countries could commit to a bilateral notification and/or consultation process where the competent authority to which a MAP case is presented does not consider the taxpayer’s objection to be justified. Whilst such a process would ensure that the determination whether the objection is justified is made taking into account all potentially relevant facts and circumstances, it would be clarified that such notification and/or consultation should not be interpreted as consultation as to how to resolve the case.

OPTION 14 – Clarify the meaning of “if the taxpayer’s objection appears to it to be justified”

Participating countries could commit to clarify, in the Commentary on Article 25, the meaning of the phrase “if the taxpayer’s objection appears to it to be justified”.

OPTION 15 – Amend Article 25(1) to permit a request for MAP assistance to be made to the competent authority of either Contracting State

Paragraph 1 of Article 25 could be amended to permit a request for MAP assistance to be made to the competent authority of either Contracting State (*i.e.* to the competent authority of one or both Contracting States). Such an amendment could be accompanied by corresponding changes to the Commentary on Article 25, which would include the current text of paragraph 1 of Article 25 as an alternative provision to accommodate the preferences of some countries.

31. Persons and organisations that will comment on Options 13 and 15 are invited, in particular, to provide examples where the presentation of a case to the competent authority referred to in the current wording of paragraph 1 of Article 25 may not have resulted in the discussion of that case with the competent authority of the other State in a situation where that other competent authority would likely have considered that there was taxation not in accordance with the provisions of the Convention.

N. The use of domestic law remedies may have an impact on the use of the MAP

Description of the obstacle

32. The mutual agreement procedure provided for by Article 25 is available to taxpayers irrespective of the judicial and administrative remedies provided by the domestic law of the Contracting States. Moreover, the constitutions and/or domestic law of many countries provide that no person can be deprived of the judicial remedies available under domestic law. In most cases, a taxpayer’s choice of recourse is thus only constrained by the circumstance that most tax administrations will not deal with a taxpayer’s case through the MAP and in a domestic court or administrative proceeding at the same time (*i.e.* one process will take precedence over the other). Because the interaction of domestic law remedies and the MAP is generally governed by a Contracting State’s domestic law and/or administrative procedures (*i.e.* a tax treaty will typically not itself contain any provisions on this point) there may be uncertainty and mismatches between the different approaches adopted, which may impede the elimination of double

taxation in some cases. Uncertainties may also arise with respect to the extent to which a competent authority may depart from a decision by a domestic court. Taking into account these uncertainties, it is recognised that it may generally be preferable to pursue the MAP first and to suspend domestic law procedure(s) because an agreement reached through the MAP will typically provide a comprehensive, bilateral resolution of the case. A domestic law recourse procedure, in contrast, will only settle the issue(s) in one State and may consequently fail to relieve international double taxation.

OPTION 16 – Clarify the relationship between the MAP and domestic law remedies

Participating countries could commit to clarify the relationship between the mutual agreement procedure and domestic law remedies. They could, in particular, commit –

- To facilitate recourse to the mutual agreement procedure as a first option to resolve treaty-related disputes through appropriate adaptations to their domestic legislation and administrative procedures, which may include provision for the suspension of domestic law proceedings as long as a MAP case is pending.
- To publish clear guidance on the relationship between the MAP and domestic law remedies, the processes involved and the conditions and rules underlying these processes. Such guidance could address, specifically, 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, and thereby permit taxpayers to make an informed choice between the MAP and domestic law remedies. The Commentary on Article 25 could also be amended to address this issue.

O. Issues connected with the collection of taxes

Description of the obstacle

33. Where the payment of tax is a requirement for MAP access, the taxpayer concerned may face significant financial difficulties: if both Contracting States collect the disputed taxes, double taxation will in fact occur and the resultant cash flow problems may have a substantial impact on a taxpayer's business, at least for as long as it takes to resolve the MAP case. A competent authority may also find it more difficult to enter into good faith MAP discussions when it considers that it may likely have to refund taxes already collected.

OPTION 17 – Clarify issues connected with the collection of taxes and the mutual agreement procedure

Participating countries could commit to further clarify issues connected with the collection of taxes and the mutual agreement procedure, which could include a commitment to examine, in the context of treaty negotiations, each Contracting State's domestic law and procedures for the collection of taxes, with a view to a clear shared understanding of such law and procedures and to address directly any obstacles to MAP access that they may effectively create. Changes to the Commentary on Article 25 could also address the suspension of collection procedures pending resolution of a MAP case; these amendments could further clarify, in particular, the policy considerations supporting a suspension of collection procedures during the period that any mutual agreement proceeding is pending and provide that such suspension should be available under the same conditions as apply to a person pursuing a domestic administrative or judicial remedy.

P. Time limits to access the MAP

Description of the obstacle

34. Time limits connected with the mutual agreement procedure present particular obstacles to an effective MAP. In some cases, uncertainty regarding the “*first notification of the action resulting in taxation not in accordance with the provisions of the Convention*” may present interpretive difficulties. More importantly, some countries may be reluctant to accept “late” cases – *i.e.* cases initiated by a taxpayer within the deadline provided by Article 25(1) but long after the taxable year at issue. Countries have adopted various mechanisms to protect their competent authorities against late objections, which include requirements to present a MAP case to the “other” competent authority within an agreed-upon period in order for MAP relief to be implemented and treaty provisions limiting the period during which transfer pricing adjustments may be made. In practice, competent authorities have found that the early discussion of MAP cases may contribute to a more effective and timely MAP process (recognising that competent authority consultation prior to the conclusion of the audit should respect the principle of the independence of the competent authority and audit functions).

OPTION 18 – Clarify issues connected with time limits to access the mutual agreement procedure

Participating countries could commit to different measures to clarify issues connected with time limits to access the mutual agreement procedure, including, in particular –

- To adopt the best practices currently included in the MEMAP concerning time limits to access the mutual agreement procedure, in particular to allow early resolution of MAP cases and to provide the benefit of the doubt to taxpayers when interpreting a tax treaty’s time limitation for MAP requests in borderline cases (*e.g.* where it is not clear when “first notification” has occurred).
- To include in their 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*”). Where a country does not include that sentence or deviates from its wording, it could commit to ensure that its audit practices do not unduly create the risk of late adjustments for which taxpayers may not be able to obtain MAP relief.
- Where there are difficulties or doubts as to what constitutes “first notification” for purposes of paragraph 1 of Article 25, to discuss and agree on the necessary clarifications with their treaty partners.

In order to provide guidance to countries that wish to use treaty provisions that require a MAP case to be presented to the other competent authority within a specified period in order for relief to be implemented, an alternative provision – and an explanation of the circumstances in which Contracting States might consider it appropriate – could be added to the Commentary on Article 25. An alternative provision could also be added to the Commentary on Article 9 to limit the time during which a Contracting State may make an adjustment pursuant to paragraph 1 of Article 9. Similarly, to provide guidance to countries that wish to use treaty provisions that deal with the length of time during which a Contracting State is obliged to make an appropriate corresponding adjustment under Article 9(2), an alternative provision could be added to the Commentary on Article 9.

Q. Issues related to self-initiated foreign adjustments

Description of the obstacle

35. Under the laws of some States, a taxpayer may be permitted under appropriate circumstances to amend a previously filed tax return to adjust the price for a controlled transaction between associated enterprises, or to adjust the profits attributable to a permanent establishment, to reflect a result in accordance (in the taxpayer’s opinion) with the arm’s length principle. Such a “self-initiated adjustment” – *i.e.* any action undertaken at the initiative of the taxpayer to adjust the previously-reported results of controlled transactions in order to reflect an arm’s length result – may include, for example, the filing of an amended tax return to reflect an arm’s length price of a controlled transaction or other taxpayer action to adjust the previously-reported attribution of profits to a permanent establishment to conform such attribution to the separate entity and arm’s length principles on which Article 7 is based. Uncertainty exists, however, with respect to the obligation to make a corresponding adjustment under Article 9(2) or Article 7(3) in the case of a self-initiated foreign adjustment – *i.e.* whether a self-initiated foreign adjustment gives rise to circumstances in which a Contracting State adjusts (and taxes accordingly) the allocation of profits in a controlled transaction or the attribution of profits to a permanent establishment. Similar uncertainty may exist whether a self-initiated foreign adjustment is an “action” of a Contracting State that could trigger a taxpayer entitlement to request MAP consideration under Article 25(1). These issues may become increasingly significant as a consequence of the increased pressure on transfer pricing outcomes and permanent establishment issues resulting from the work on BEPS.

OPTION 19 – Clarify issues related to self-initiated foreign adjustments and the mutual agreement procedure

Changes to the Commentaries on Articles 7, 9 and 25 could be made to clarify the circumstances where double taxation could be resolved under MAP in the case of self-initiated foreign adjustments and to emphasise the importance of bilateral competent authority consultation to determine appropriate corresponding adjustments and to ensure the relief of double taxation.

4. ENSURING THAT CASES ARE RESOLVED ONCE THEY ARE IN THE MUTUAL AGREEMENT PROCEDURE

36. Certain of the main obstacles to the resolution of treaty-related disputes through the MAP are issues related to MAP processes – *i.e.* procedural and other blockages that impede the timely and effective resolution of MAP cases that have been accepted for bilateral competent authority consideration. Like issues related to MAP access, MAP process issues are likely to become more significant as a result of the work on BEPS, as more stringent standards are adopted and competent authorities are called upon to develop common interpretations of new tax treaty and transfer pricing rules through the mutual agreement procedure (in addition to resolving the cases already in their MAP inventories and new “routine” MAP cases). This section addresses a number of issues related to the improvement of MAP processes.

R. Lack of a principled approach to the resolution of MAP cases

Description of the obstacle

37. As already noted, the role of the competent authority is to take an objective view of the provisions of the applicable treaty and apply it in good faith to the facts of the taxpayer’s case, with a view to eliminating taxation not in accordance with the terms of the treaty. Where one or both competent

authorities do not follow that approach, the resolution of MAP cases becomes very difficult and there are risks of inappropriate results.

38. To avoid these problems, a competent authority should engage in discussions with other competent authorities in a fair and principled manner. As part of a principled approach, each MAP case should be approached on its own merits and not by reference to any balance of results in other cases. A principled approach also requires that competent authorities take a consistent approach to the same or similar issues and not change positions from case to case, based, for example, on considerations such as revenue that are irrelevant to the legal or factual issues that the competent authorities are called upon to resolve.

OPTION 20 – Ensure a principled approach to the resolution of MAP cases

Participating countries could commit to different measures to ensure a principled approach to the resolution of MAP cases, including, in particular –

- To adopt the best practice currently included in the MEMAP concerning fair and objective MAP negotiations, based on a good faith application of the treaty, and the resolution of MAP cases on their merits.
- Where the interpretation of a treaty provision is likely to be difficult or controversial, to agree on specific interpretive guidance (*e.g.* in the form of a protocol or exchange of notes) proactively, ideally at the same time the treaty is negotiated. Such interpretive issues could also appropriately be resolved by the competent authorities of the Contracting States under the authority of paragraph 3 of Article 25.

S. *Lack of co-operation, transparency or good competent authority working relationships*

Description of the obstacle

39. A lack of co-operation, transparency or of a good working relationship between competent authorities also creates difficulties for the resolution of MAP cases. A good competent authority working relationship is a fundamental part of an effective mutual agreement procedure and is another strategic focus of the FTA MAP Forum. The FTA MAP Forum Strategic Plan notes that the success of mutual agreement procedures “*critically depends on strong, collegial relationships, grounded in mutual trust, between and among competent authorities around the world. Mutual trust fosters an environment of cooperation and productivity, while a lack of trust fosters an environment of guardedness and suspicion leading to cumbersome resolution processes.*” A closely related strategic focus of the FTA MAP Forum is MAP process improvements; the FTA MAP Forum Strategic Plan calls for relevant work to be undertaken in areas including internal process improvements, case elevation, and interaction with taxpayers and advisors.

OPTION 21 – Improve competent authority co-operation, transparency and working relationships

Participating countries could commit to adopt the relevant best practices currently included in the MEMAP, which would include, in particular, the following commitments –

- Countries could commit to a co-operative and fully transparent MAP process, in which competent authorities exchange documentation and information in a timely manner and regular competent

authority communications are used to reinforce a collaborative working relationship. Competent authorities could also agree as to when taxpayers would be permitted to make presentations to the competent authorities to clarify – and facilitate a shared understanding of – the relevant facts and issues. Competent authorities could also commit to provide taxpayers with updates on the status of their MAP cases.

- Countries could commit, where possible, to face-to-face meetings between competent authorities, recognising that such meetings may allow for a more open discussion and collegial approach and may also represent a milestone that helps to advance a case by triggering bilateral focus and preparation.

40. Commentators are invited to suggest what additional measures (other than arbitration, which is referred to below) could be adopted in order to facilitate the resolution of a MAP case that competent authorities have been unable to resolve within two years of the MAP case being accepted (or some other reasonable target timeframe).

T. Absence of a mechanism, such as MAP arbitration, to ensure the resolution of all MAP cases

Description of the obstacle

41. Mandatory binding MAP arbitration has been included in a number of bilateral treaties following its introduction in paragraph 5 of Article 25 of the OECD Model in 2008. Action 14 of the BEPS Action Plan recognises, however, that the adoption of MAP arbitration has not been as broad as expected and acknowledges that “*the absence of arbitration provisions in most treaties and the fact that access to ... arbitration may be denied in certain cases*” are obstacles that prevent countries from resolving disputes through the MAP. This section discusses the main policy and practical issues connected with MAP arbitration and options to address them.

1. Policy issues

42. One of the main policy concerns with mandatory binding MAP arbitration relates to national sovereignty. Footnote 1 to Article 25(5) of the OECD Model recognises that, in some States, national law, policy or administrative considerations are considered obstacles to the adoption of mandatory binding MAP arbitration. The footnote acknowledges that, at the time the arbitration provision was adopted, some OECD member countries had concerns that national sovereignty could prove a barrier to arbitration. It also reflects the fact that not all OECD countries involved in the development of the provision intended to adopt mandatory binding MAP arbitration. Whilst the footnote makes it unnecessary for OECD member countries and non-OECD economies to state their observations, reservations and positions on the provision and its interpretation, the footnote also results in a lack of transparency, as country positions on MAP arbitration only become apparent through the conclusion of new treaties or protocols by specific countries.

43. A second significant policy concern relates to access to MAP arbitration and its scope. Although paragraph 68 of the Commentary on Article 25 provides that a taxpayer “*should be able to request arbitration of unresolved issues in all cases dealt with under the mutual agreement procedure that have been presented under paragraph 1 on the basis that the actions of one or both of the Contracting States have resulted for a person in taxation not in accordance with the provisions of this Convention*”, some countries may want to restrict access to arbitration to a specific range of MAP cases. In practice, some OECD member countries have followed this approach and have limited the scope of MAP arbitration to cases regarding the application of specific treaty articles (principally Articles 4, 5, 7, 9 and 12), or exclude arbitration under specific circumstances.

44. A third important policy concern is the co-ordination of MAP arbitration and domestic legal remedies. These concerns relate particularly to avoiding the risk of a conflict between the decision of a court and the decision of an arbitration panel.

45. The following are various options seeking to address these concerns (these options are not mutually exclusive).

OPTION 22 – Policy issues: Increase transparency with respect to MAP arbitration

In order to provide transparency with respect to country positions on mandatory binding MAP arbitration, footnote 1 to Article 25(5) could be deleted (and paragraph 65 of the Commentary on Article 25 modified accordingly).

OPTION 23 – Policy issues: Tailor the scope of MAP arbitration

In order to encourage countries to adopt a MAP arbitration provision with a limited scope (rather than no provision at all) the Commentary on Article 25 could be amended to include such an alternative MAP arbitration provision, which should also expressly provide for the possible extension of its scope of application. Limitations to the scope of MAP arbitration could include, for example: provision for MAP arbitration only with respect to cases involving specific treaty articles; provision for MAP arbitration only in cases of actual double taxation; or exclusion from the scope of arbitration cases involving the application of treaty or domestic law anti-abuse rules. An alternative MAP arbitration provision could also provide that the competent authorities may mutually agree that arbitration is not appropriate in a particular case. The amendments to the Commentary on Article 25 would emphasise that, to ensure clarity and transparency, any limitations to the scope of MAP arbitration should be expressly defined in the arbitration provision itself (*i.e.* in the ratified treaty document).

46. Stakeholders are invited to comment, in particular, on the advantages and disadvantages of potential limits to the scope of MAP arbitration.

OPTION 24 – Policy issues: Facilitate the adoption of MAP arbitration following a change in treaty policy

Because national policies with respect to MAP arbitration may be expected to evolve over time, particularly as more countries gain experience and familiarity with MAP arbitration, most favoured nation (MFN) provisions could be used as an elective mechanism for the quick implementation of MAP arbitration between a country and its treaty partners where that country determines in the future that MAP arbitration should appropriately be included as part of its treaty policy. Commentary would be developed to accompany such provisions to illustrate their potential advantages and disadvantages.

OPTION 25 – Policy issues: Clarify the co-ordination of MAP arbitration and domestic legal remedies

In order to improve the articulation of MAP arbitration and domestic remedies, participating countries could commit to provide guidance on the interaction between the mutual agreement implementing the

decision of the arbitration panel and pending litigation on the issues resolved through the mutual agreement procedure (such guidance would complement the guidance to be developed pursuant to the commitment described above under Option 16). The Commentary on Article 25 could also be amended to provide greater clarity, addressing, for example, the reference to a “decision” in the final sentence of Article 25(5).

2. *Practical issues*

Description of the obstacles

Conditions for arbitration

47. Article 25(5) of the OECD Model provides for the submission of unresolved issues to MAP arbitration after a fixed period of time following the initiation of the MAP case. It is, however, recognised that there may, on occasion, be circumstances in which initiating MAP arbitration may be premature and, consequently, that this automatic referral may be an obstacle to the adoption of arbitration by some countries. Where the competent authorities believe that they will be able to reach a negotiated resolution, it may be appropriate to defer the initiation of MAP arbitration for a defined (preferably short) period of time.

OPTION 26 – Practical issues: Amend Article 25(5) to permit the deferral of MAP arbitration in appropriate circumstances

Paragraph 5 of Article 25 could be amended to permit the competent authorities to defer the initiation of MAP arbitration in appropriate circumstances – *e.g.* to allow the competent authorities to mutually agree to defer the initiation of MAP arbitration under specific conditions.

Appointment of arbitrators

48. There is no standard set of qualifications for prospective MAP arbitrators, although the criteria used in existing agreements and models in general appear to provide that such individuals: (i) should have significant experience in cross-border tax matters, preferably in allocation matters; (ii) should be of a judicial temperament (*i.e.* neutral, decisive, respectful and composed), though not necessarily have experience as a judge or arbitrator; and (iii) should be impartial and independent *vis-à-vis* the Contracting States and the affected taxpayer(s) at the time they accept appointment (as well as for the duration of the arbitration proceeding and a reasonable period of time thereafter). Limited guidance and lack of experience with the appointment of arbitrators may make some countries hesitant to adopt MAP arbitration.

OPTION 27 – Practical issues: Appointment of arbitrators

In order to avoid potential differences, participating countries could agree to develop mutually agreed criteria for the appointment and qualifications of arbitrators, to be included in the text of the arbitration provision itself and/or in competent authority agreements concluded for purposes of the implementation of MAP arbitration, in advance of any MAP arbitration procedure. To ensure that prospective arbitrators are impartial and independent, participating countries may also wish to develop a standardised declaration that would be executed by arbitrators to attest to their fitness to serve as arbitrators and to disclose any potential conflicts of interest.

Confidentiality and communications

49. The security of taxpayer and competent authority information and communications are critical to public confidence in tax administration, including the mutual agreement procedure. There may be an even greater sensitivity in connection with MAP arbitration, as independent arbitrators who are not formally employees of the tax administrations of the Contracting States are brought into the mutual agreement process. Arbitrators must be allowed full access to the information necessary to make an informed decision on the issues submitted to them for resolution and, at the same time, must be held to the same strict confidentiality requirements regarding that information as apply to the competent authorities themselves under paragraph 2 of Article 26 and domestic laws protecting the confidentiality of taxpayer information. Experience has also shown that, in some cases, taxpayers or their representatives may attempt to manipulate MAP discussions through public comments on active competent authority negotiations; such comments are not helpful to the work of the competent authorities and may be particularly problematic in the context of MAP arbitration given the pressures they may create for independent arbitrators.

OPTION 28 – Practical issues: Confidentiality and communications

In order to protect the confidentiality of taxpayer information in the context of MAP arbitration (and the overall integrity of the MAP arbitration process), the Article 25 arbitration provision could be amended as follows:

- To ensure the proper consideration of the relevant information in the MAP arbitration process, any disclosure of taxpayer information by a competent authority to the members of the arbitration panel would be made pursuant to the authority of the Convention and subject to confidentiality requirements that are at least as strong as those applicable to the competent authorities. An express provision in the text of the Convention itself, with a cross-reference to Article 26, would ensure the legal status of the arbitrators.
- The Commentary on Article 25 could provide additional relevant guidance, noting the practice of some competent authorities (i) to request that taxpayers authorise the disclosure of relevant information to the arbitrators and (ii) to require that the arbitrators and their staffs agree in writing to maintain the confidentiality of the information they receive in the course of the arbitration process (subject only to further disclosure in accordance with the requirements and further authorisation of the competent authorities and the affected taxpayers).
- The Commentary on Article 25 could also note the practice of some countries to oblige taxpayers and their representatives to maintain confidentiality regarding arbitration in a MAP case, subject to any necessary disclosures such as for financial reporting purposes, with a view to avoiding potential taxpayer manipulation of the MAP arbitration process.

Form of process for decision

50. There are two principal approaches to decision-making in the arbitration process. The format most commonly used in commercial matters is the “conventional” or “independent opinion” approach, in which the arbitrators are presented with the facts and arguments of the parties based on applicable law and then reach an independent decision, typically in the form of a written, reasoned analysis. This approach strongly resembles a judicial proceeding and is the model for the EU Arbitration Convention as well as the default approach reflected in the Sample Mutual Agreement on Arbitration (the Sample Agreement) included in the Commentary on Article 25 of the OECD Model. The other main format is the “last best

offer” or “Final Offer” approach (often informally referred to as “baseball arbitration”). This approach is reflected in a number of bilateral tax treaties signed by OECD member countries. Under this approach, in general, each of the competent authorities submits to the arbitration panel a proposed resolution (*i.e.* its proposed disposition of the specific amounts of income, expense or taxation at issue in the MAP case), together with a position paper that explains the rationale for the proposed resolution. The arbitration panel is required to adopt as its determination one of the proposed resolutions submitted by the competent authorities. The determination by the arbitration panel does not state a rationale and has no precedential value.

OPTION 29 – Practical issues: Default form of decision-making in MAP arbitration

In light of experience with MAP arbitration, participating countries could develop additional guidance under Article 25 of the OECD Model on the use of different decision-making mechanisms as default approaches in MAP arbitration, with an explanation of the respective advantages and disadvantages of the independent opinion and Final Offer approaches.

Stakeholder comments are invited in particular on the preferred default form of decision-making in MAP arbitration.

Evidence

51. The evidence considered by the arbitration panel may largely be determined by the form of the decision-making process. The independent opinion approach ordinarily envisions a formal evidentiary process involving testimony, the *de novo* presentation of evidence to the arbitration panel and (potentially) taxpayer presentations. The Final Offer approach, on the other hand, generally contemplates that the arbitration panel will make a decision based on the facts and arguments as presented in the competent authorities’ submissions to the arbitration panel (a so-called “on the record” approach). The most important principle relating to evidence is that there be no opportunity or incentive for the taxpayer to undermine the MAP negotiation process (*e.g.* by seeking to have the arbitration panel consider information which had been withheld or otherwise not provided to the competent authorities).

Role of the taxpayer

52. Consistent with the nature of the mutual agreement procedure as a government-to-government activity in which taxpayers play no direct role, MAP arbitration processes do not require direct taxpayer input to, or appearance before, the arbitration panel (although such taxpayer participation is not precluded). Whilst it is sometimes asserted that the arbitration panel might benefit from direct interaction with taxpayers, there is a concern that taxpayer involvement in the MAP arbitration procedure could result in a lengthier, more expensive and more complicated process, and thus undermine the effectiveness of MAP arbitration.

OPTION 30 – Practical issues: Evidence

In light of experience with MAP arbitration, guidance in the Commentary on Article 25 of the OECD Model could be developed to address particular evidentiary issues that may arise in connection with different forms of arbitral decision-making. Such guidance could provide, for example, that where the format for arbitral decision-making is the Final Offer approach, an “on the record” evidentiary format should be used. This guidance could also provide, for example, that where the format for arbitral decision-making is the independent opinion approach, it may be appropriate in some cases for the competent

authorities to permit the taxpayer to present its position orally during the arbitration procedure, at the request, or with the permission, of the arbitrators. Stakeholder comments are invited on approaches to evidentiary issues in the MAP arbitration process.

In addition, in order to ensure that the taxpayer's position is clearly communicated to the arbitration panel, guidance under Article 25 could allow for the taxpayer's submission of some form of brief for consideration by the panel (subject to review and comment by the competent authorities); such a brief should not, however, contain new facts which have not previously been considered by the competent authorities.

Multiple, contingent and integrated issues

53. Many MAP cases may require competent authority consideration of more than one assessment or adjustment to a taxpayer's reported income, expense or liability. The simplest of such cases may require the resolution of multiple unconnected issues (*e.g.* the audit of a member of a MNE group could result in an adjustment to the transfer pricing of a tangible good as well as adjustments to other amounts paid to associated enterprises, such as a management fee or royalty). Two other, more complex types of MAP cases involve multiple issues: MAP cases involving contingent issues and MAP cases involving integrated operations. Contingent issues may be presented in MAP cases involving the application of Articles 5 and 7, which require the competent authorities to resolve a threshold question (is there a permanent establishment?) before considering other issues (in the PE case, the attribution of profits). Integrated operations may be presented in a MAP case involving "bundled intangibles". Such a case could involve, for example, a large retail organization that has formed affiliates to which a variety of intangibles are licensed, and to which a variety of branded goods are sold, and there is potential for overlap between the two sets of transactions.

OPTION 31 – Practical issues: Multiple, contingent and integrated issues

Participating countries could establish mutually-agreed guidance for arbitrators on how to deal with multiple, contingent and integrated issues.

54. Commentators are invited to identify other examples of multiple, contingent and integrated issues that may need to be addressed in mutually-agreed guidance for arbitrators.

Costs and administration

55. In light of the significant resource constraints experienced by many countries in recent years, concerns about the potential costs of MAP arbitration are an important consideration in designing the format of the arbitration process. The costs associated with arbitration fall into three categories: (i) costs related to engaging the arbitration panel, consisting principally of the fees paid to the arbitrators; (ii) costs related to each competent authority's participation in the arbitration procedure, which include, for example, costs related to the preparation and presentation of proposed resolutions and position papers; and (iii) administrative costs, such as telecommunications and secretarial expenses, miscellaneous expenses (*e.g.* translation or interpretation) and, possibly, travel costs (airfare, lodging, etc.). Depending upon the evidentiary procedures established, the compensation of the arbitration panel can constitute the most significant cost of arbitration. The costs of MAP arbitration, however, do not have to be significant, and various design features (such as a streamlined evidentiary process that limits the material to be considered

by the arbitration panel or a time limit for the arbitration panel to reach its decision) can significantly reduce the time and other resources necessary for the arbitration process.

OPTION 32 – Practical issues: Costs and administration

In order to address the particular concerns that costs may present an obstacle to the adoption of MAP arbitration, participating countries could consider ways to reduce the costs of MAP arbitration procedures, with a view to developing guidance in the Commentary on Article 25 on these issues and approaches to address them.

56. Commentators are invited to submit specific suggestions on how to improve the functioning of MAP arbitration. Commentators are also invited to identify other alternative dispute resolution mechanisms that could contribute to a more effective mutual agreement procedure.

U. Issues related to multilateral MAPs and advance pricing arrangements (APAs)

Description of the issue

57. In recent years, the substantial increase in the pace of globalisation has created unique challenges for existing tax treaty dispute resolution mechanisms. Whilst the mutual agreement procedure provided for in Article 25 of the OECD Model has traditionally focused on the resolution of bilateral disputes, phenomena such as the adoption of regional and global business models and the accelerated integration of national economies and markets have emphasised the need for effective mechanisms to resolve multi-jurisdictional international tax disputes.

58. Multilateral situations that raise issues for the mutual agreement procedure, which is traditionally conducted on a purely bilateral basis, include:

- So-called “triangular cases”, *e.g.* where an enterprise of State A transfers goods or services, through its permanent establishment situated in State B, to an associated enterprise situated in State C and where an adjustment to the transfer price of the transfer is made by the tax administration of State B.
- Situations where an adjustment in one State results in cascading adjustments in other States, *e.g.* where the transfer price of sales made by an enterprise of State B to an associated enterprise of State C is adjusted downward by State C, which results in State C making a downward adjustment to the sales revenues of the enterprise of State C but also reducing the amount of royalties paid to an associated enterprise of State A because these royalties are based on the amount of sales by the enterprise of State B.
- Situations where an entity that is a member of an MNE group performs certain functions for the benefit of a number of associated enterprises (*e.g.* through a cost-sharing arrangement or transactions for the provision of intra-group services) and different transfer pricing adjustments are made to the resulting charges in the various States of residence of these associated enterprises.

59. Commentators are invited to provide other examples of multilateral situations that raise issues for the mutual agreement procedure.

OPTION 33 – Address issues related to multilateral MAPs and advance pricing arrangements (APAs)

Changes to Article 25 and/or its Commentary could also be made in order to address directly the interpretation and application of Article 25 with respect to multilateral MAPs and APAs, in particular to address the issue of how the arbitration process could be used in a multilateral MAP and to address legal, practical and/or procedural issues, including issues connected with time limits (e.g. domestic statutes of limitation for assessment) and issues connected with ensuring that third-State competent authorities are made aware of cases with multilateral implications.

The possibility of developing a specific provision that would address mutual agreement procedure issues that arise in multilateral situations, including how the arbitration process could be used in such situations, could be considered by the interested parties that will participate in the development of the multilateral instrument contemplated by Action 15 (*Develop a multilateral instrument*) of the BEPS Action Plan.

V. *Issues related to consideration of interest and penalties in the mutual agreement procedure*

Description of the issue

60. Issues related to the consideration of interest and penalties in the mutual agreement procedure are of significant importance, particularly in light of the potential for the work on BEPS to increase pressure on the mutual agreement procedure. In the context of the MAP, there appear to be three main practical issues related to interest and penalties:

- a) ***Suspension:*** Can interest and/or penalties be suspended while the case is considered in the MAP, so that their proper application/imposition can be determined following the resolution of the primary substantive issues?
- b) ***Negotiation:*** Can the application and/or computation of interest or penalties be considered primary substantive issues that may be negotiated by the competent authorities?
- c) ***Waiver:*** Can a competent authority waive the collection of interest on a deficiency if the treaty partner does not pay interest on a corresponding refund of tax (or pays interest at a lesser rate)? Can a competent authority waive the payment of interest on a refund if the treaty partner is willing to waive collection of interest on the deficiency (or collects interest at a lesser rate)?

OPTION 34 – Provide guidance on consideration of interest and penalties in the mutual agreement procedure

Changes to Article 25 or its Commentary could be made to address the treatment of interest and penalties in the MAP, in particular to explain that whilst it is not appropriate to consider interest and penalties as “taxes” in order to apply limitations on source State taxation or for purposes of the obligation of the State of residence to relieve double taxation, interest and administrative penalties that are directly connected to the taxes to which they are related should be treated in the same way as taxes to which they are directly connected (in particular where interest and penalties are computed with reference to the amount of the underlying tax and the underlying tax is found not to have been levied in accordance with the provisions of the Convention).

