

LIUC – Università Carlo Cattaneo

International Tax Law

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Mutual Agreement Procedure

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The Mutual Agreement Procedure

The Mutual Agreement Procedure is a process provided under tax treaties for the resolution of disputes concerning the interpretation and application of the treaty by the Competent Authorities (“CAs”) of the Contracting States.

It is tool that allow CAs to interact with the aim of solving the international tax dispute and eliminate the double taxation.

The Mutual Agreement Procedure: available tools

MAP pursuant to
double tax treaties

Art. 25 OECD MC

MAP pursuant to
EU Arbitration
Convention

**Convention
90/436/EEC**

MAP pursuant to
EU Directive

**Directive (EU)
2017/1852**

Art. 25 OECD Model Convention

- 1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, **present his case to the competent authority of either Contracting State**. The case 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.*
- 2. The competent authority shall **endeavour**, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, **to resolve the case by mutual agreement** with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States.*
- 3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention.*

Art. 25 OECD Model Convention

*4. The competent authorities of the Contracting States may communicate with each other directly, including through a **joint commission** consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs.*

*5. Where, a) under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and b) the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within two years from the date when all the information required by the competent authorities in order to address the case has been provided to both competent authorities, any **unresolved issues** arising from the case shall be submitted to arbitration if the person so requests in writing. These unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or administrative tribunal of either State. Unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.*

Art. 25 OECD Model Convention

- The Mutual Agreement Procedure (MAP) provided by the OECD MC is a tool for the resolution of international tax disputes.
- The MAP provides for a direct consultation between the Tax Administrations of the contracting Parties, which, by means of the respective Competent Authorities, set up a dialogue aimed at the resolution of an international tax dispute (e.g. double taxation cases, correct interpretation/application of a Double Tax Treaty);
- A MAP is usually initiated by a taxpayer, however it can also be started by the initiative of the Competent Authorities themselves, in order to resolve by mutual agreement, difficulties or doubts relevant to the interpretation and/or the implementation of a Double Tax Treaty;
- Besides the Commentary to Article 25, the “**Manual on Effective Mutual Agreement Procedures (MEMAP)**” provides to both tax administrations and taxpayers basic information and useful hints on how the procedure should work, indicating best practices which contracting Countries tax authorities should adopt.

Art. 25 OECD Model Convention

- A MAP can be activated to address events triggering a double taxation, both a juridical and an economic one, affecting **individuals of legal entities**, as well as to all other entities to which a Double Tax Treaty may apply;
- Hence, essentially, the following situations can lead to initiating a MAP:
 - (deemed) violation of Double Tax Treaty's provision in the application of a certain tax or withholding tax at source to a person;
 - tax adjustments performed by a contracting Country's tax administration following tax audits relevant to the transfer pricing between associated enterprises.
- The latter case is by far the most frequent one.

Art. 25 OECD Model Convention

- A MAP application is filed with the CA of the Country in which the event triggering a potential double taxation occurred and should include the following information:
 - taxpayer identification and contact details;
 - address where the CA should send its communications/correspondence;
 - a clear description of the facts and circumstances of the case, with an indication of the tax periods in which a double taxation has occurred or could occur;
 - a description of any other administrative or legal remedy already adopted to solve the case “domestically” or in the other contracting State to avoid the double taxation;
 - copy of the tax acts (typically tax audit reports and/or tax assessment notices) which have triggered or may trigger a taxation in contrast with Treaty’s provisions;
 - any other document or information suitable to facilitate the examination of the case by the CAs involved.

Art. 25 OECD Model Convention

- Although the OECD sets a three-year time limit from the date of the first notification of the action resulting in taxation not in accordance with the provisions of the Convention, many States (Italy included) entered Bilateral DTCs which provide for a shorter time limit – usually **two years**.
- CA should reply within 2 months, accepting or rejecting the application (it may also request additional information: in such a case, the deadline is postponed by another 2 months);
- If the application is accepted, the CA should try and solve the dispute unilaterally;
- Should no unilateral solution be reachable, then the first CA should get in touch with the other one, informing the latter of the initiated case and asking to start a negotiation;
- The CAs shall then **endeavour** to reach an agreement to eliminate the double taxation: this means that the MAP does not impose an obligation to solve the issue.

Art. 25 OECD Model Convention

- **Interplay with domestic legal procedure:**
 - Art. 25(1) OECD MC states that a MAP request can be validly submitted by a taxpayer “*irrespective of the remedies provided by the domestic law of those States*”.
 - Many DTCs (including those entered into by Italy) contain a reservation regarding the MAP article whereby the expression “*irrespective of the remedies provided by the domestic law*” shall be interpreted as:
 - “*the mutual agreement procedure is not alternative to the domestic litigation proceedings which shall be, in any case, preventively initiated, when the claim is related to an assessment of Italian tax not in accordance with the Convention*” (or equivalent).

Art. 25 OECD Model Convention

- Considering the uncertainty of its outcome, together with a MAP, it is often advisable to **start a litigation**, in order to secure a “way out”, in case the CAs do not reach any settlement or their negotiation drag for too long; however, the following caveats should be considered:
 - In certain jurisdictions, tax authorities can not abide from a judicial decision (i.e. a tax court’s decision), meaning that, should that happen, the MAP will have de facto to come to an end;
 - should the Law so provide, a suspension of the litigation process should be rather sought, in order to allow for the MAP negotiation to proceed, without any risk that a decision is made meanwhile by the tax court;
 - a litigation, even suspended, should also ensure that the time limits usually provided under the domestic Law to get a tax refund do not expire while the MAP negotiation goes on;
 - only an ongoing litigation allows the taxpayer to continue its defense, also after a possible failure of the MAP.

Art. 25 OECD Model Convention

- Weaknesses of the MAP:
 - No mandatory outcome (i.e. dispute may not be settled);
 - in practice, need to also initiate a contemporaneous litigation, to be suspended in order not to jeopardize the MAP;
 - lack of any ad hoc administrative tool to obtain a tax collection suspension during the MAP;
 - poor communication to the taxpayers, which are usually contacted only in case they need to provide further documents/information and then left with no updates until the outcome of the negotiation is eventually communicated;
 - CAs may artificially postpone the acceptance of a MAP application, indeed the official start of the negotiation, by requesting additional information.
 - In principle, no agreement shall include interests and penalties.
 - Clear tendency to a slow down case resolutions.

Art. 25 OECD Model Convention

- The report on **BEPS Action 14** (*Making Dispute Resolution Mechanisms More Effective*) contains a commitment by jurisdictions to implement a minimum standard to ensure that they resolve treaty-related disputes in a timely, effective and efficient manner.
- All members of the Inclusive Framework on BEPS (IF) commit to the implementation of the Action 14 minimum standard which includes timely and complete reporting of mutual agreement procedure statistics pursuant to an agreed reporting framework.

OECD 2018 MAP Statistics

- Reporting jurisdictions
 - Up to 89 jurisdictions (85 in 2017)
 - Covering almost all jurisdictions with MAP cases

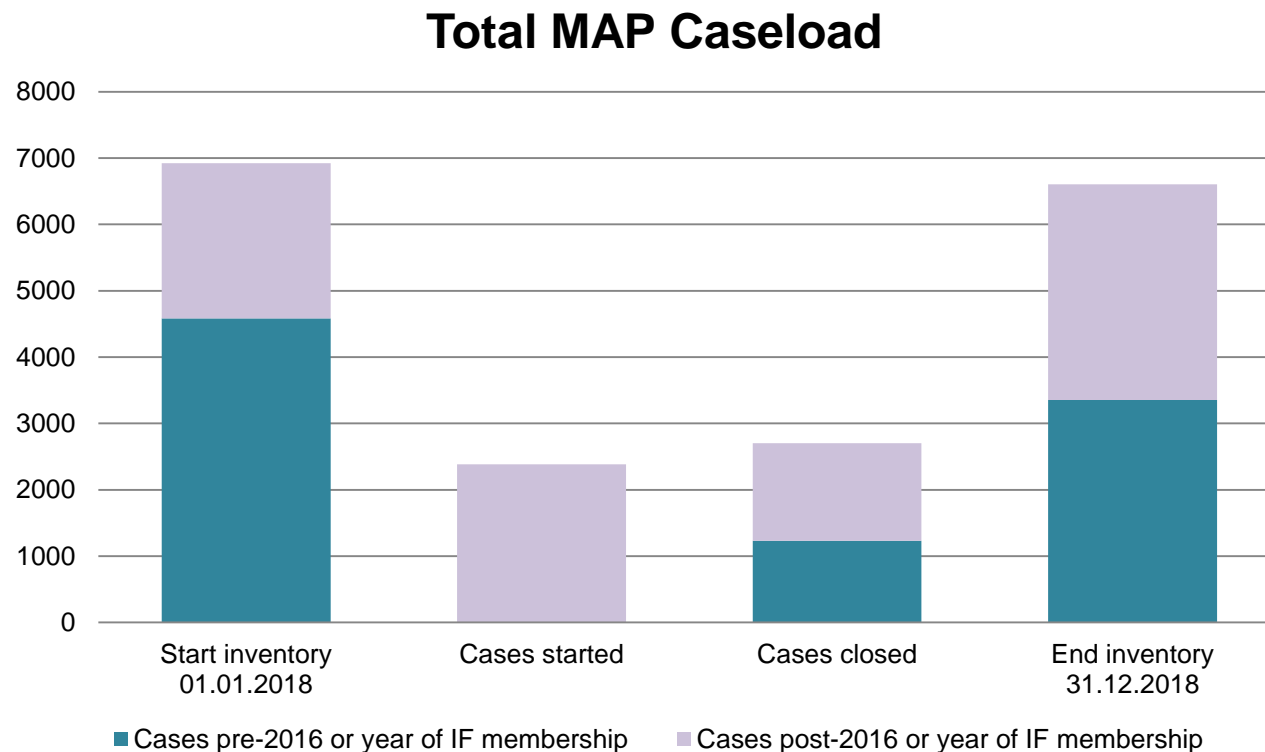


Third year of use of
the common
framework to report
MAP statistics =>
Increased consistency
in the analysis

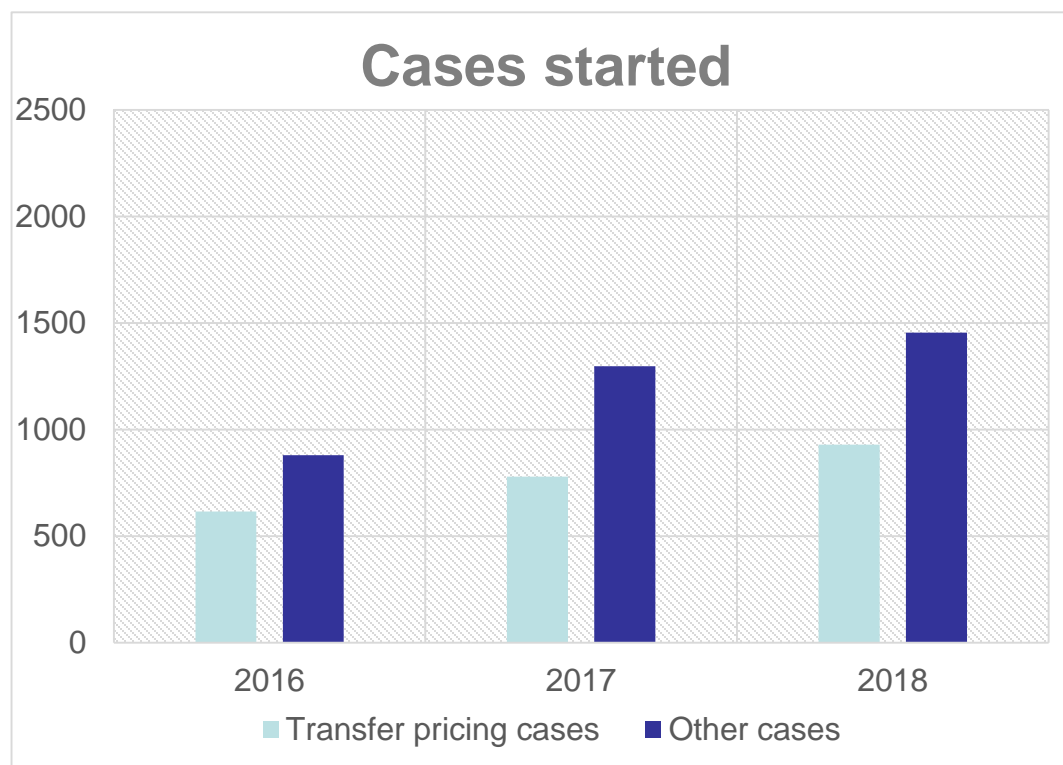


Publication of key
indicators on MAP
statistics (time,
overall performance)

OECD 2018 MAP Statistics



OECD 2018 MAP Statistics

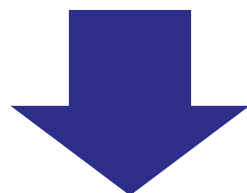


OECD 2018 MAP Statistics

Average time necessary to close MAP cases:



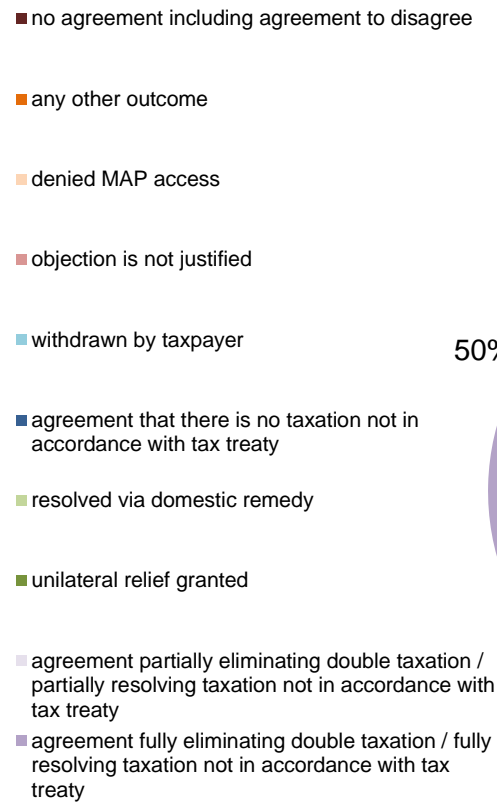
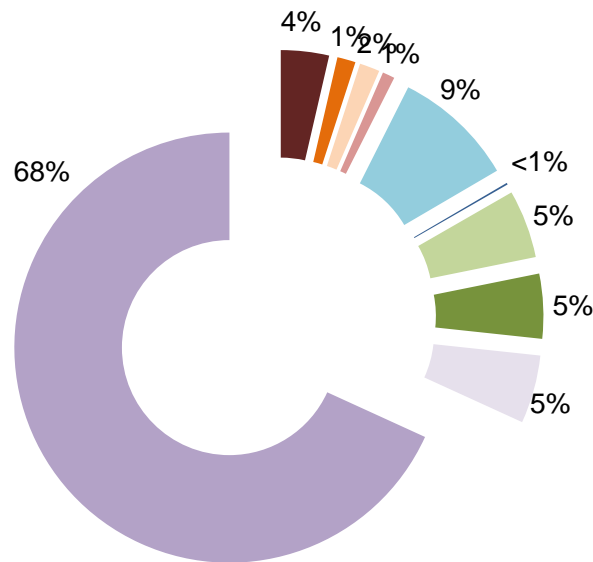
Transfer pricing cases: 33 months (30 months in 2017)



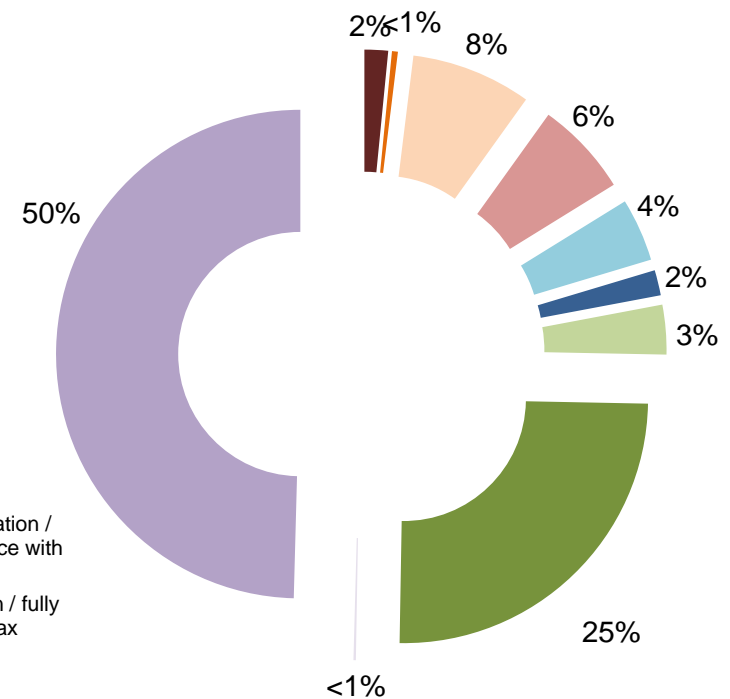
Other cases: 14 months (17 months in 2017)

OECD 2018 MAP Statistics

MAP Outcomes (transfer pricing cases)



MAP Outcomes (other cases)



<1%

EU Arbitration Convention

- The origin of the Arbitration Convention was the Commission's 1976 proposal for a directive to eliminate double taxation in the case of transfers of profits between associated enterprises in different Member States (Official Journal C 301 of 21 December 1976) and the White Paper of 1985 on the completion of the Internal Market.
- After long negotiations in the Council, the Commission proposal was transformed from a Directive into an inter-governmental Convention and it was signed on 23 July 1990 (**Convention 90/436/EEC** on the elimination of double taxation in connection with the adjustment of profits of associated enterprises).

EU Arbitration Convention

- **Personal scope: Art. 1**

- *“This Convention shall apply where, for the purposes of taxation, profits which are included in the profits of an enterprise of a Contracting State are also included or are also likely to be included in the profits of an enterprise of another Contracting State [...] For the purposes of this Convention, the permanent establishment of an enterprise of a Contracting State situated in another Contracting State shall be deemed to be an enterprise of the State in which it is situated”.*

- The EU Arbitration Convention applies to **enterprises resident in a Member State who generate profits in other Member States.**
- The EU Arbitration Convention applies also to **PEs.**

EU Arbitration Convention

- **Objective scope:** disputes concerning transfer pricing adjustments carried out on enterprises and permanent establishments.
- Only relevant cases enabling taxpayers to access to the EU Arbitration Convention concern:
 - violation of Transfer Pricing rules
 - attribution of profits to Permanent Establishments

EU Arbitration Convention

- **Steps of the procedure:**

- the complaint has to be filed within **3 years** following the first notification of the action which results or it is likely to result in double taxation;
- the expression “first notification of the action” must be construed in the most favorable way to the taxpayer: this entails that the 3 years period within which the request must be submitted elapses from the date in which the tax assessment leading to economic double taxation was notified;
- the enterprise shall at the same time notify the competent authority if other States may be concerned in the case;
- the competent authority shall then without delay notify the competent authorities of other involved States;

EU Arbitration Convention

- if the complaint appears to be well-founded and if it is not itself able to arrive at a satisfactory solution, the competent authority shall endeavour to resolve the case by mutual agreement with the competent authority of any other Contracting State concerned, with a view to the elimination of double taxation (for a period no longer than **2 years**);
- if the competent authorities concerned fail to reach an agreement that eliminates the double taxation within 2 years, they shall set up an advisory commission (Arbitration phase), which is made up of:
 - two representative of each competent authority concerned (this number may be reduced to one by agreement between the competent authorities);
 - an even number of independent persons.

EU Arbitration Convention

- **The advisory commission:**
 - shall deliver its opinion not more than **six months** from the date on which the matter was referred to it;
 - shall adopt its opinion by a **simple majority** of its members (the competent authorities concerned may agree on additional rules of procedure).
- After the decision of the advisory commission, the competent authorities involved:
 - shall take a decision which will eliminate the double taxation within **six months** from the date on which the advisory commission delivered its opinion;
 - may take a decision which deviates from the advisory commission's opinion;
 - if they fail to reach agreement, they shall be obliged to act in accordance with that opinion.

EU Arbitration Convention

- **The role of the taxpayer:**

- as for the DTC MAP, the taxpayer is not directly involved in the discussions between the Competent Authorities, but is only required to be co-operative, describing the case at stake and promptly providing requested additional information, if any;
- there is no explicit nor mandatory rule imposing on the Competent Authorities involved the duty to inform at any step of the procedure the taxpayer.

- **Exclusion clause:**

- the Competent Authority of a Member State shall not be obliged to initiate the mutual agreement procedure or to set up the advisory commission where legal or administrative proceedings have resulted in a final ruling that by actions giving rise to an adjustment of transfers of profits one of the enterprises concerned is liable to a serious penalty.

EU Arbitration Convention

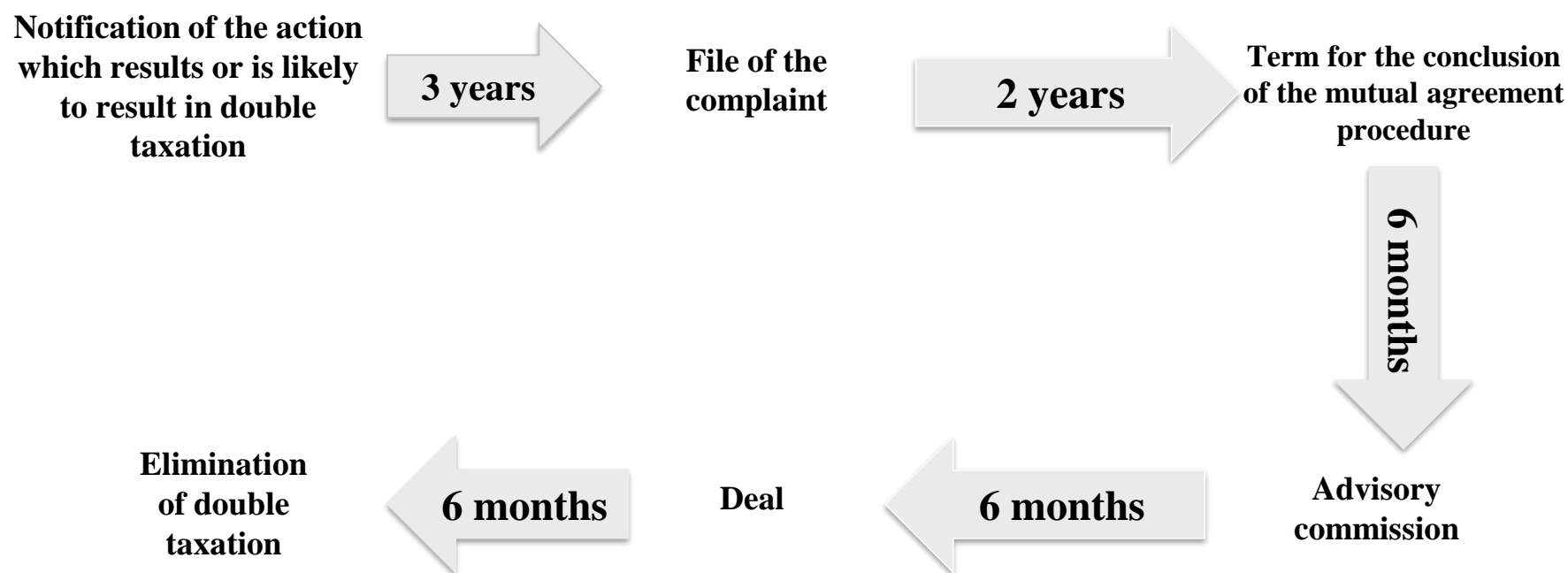
- **Interplay with domestic legal procedure:**
 - the Arbitration Convention MAP can be activated **only and insofar** as the associated enterprise has allowed the time provided for the appeal to expire, or has withdrawn any such appeal before a decision has been delivered;
 - in the event the taxpayer simultaneously submits an Arbitration Convention MAP request and appeals against the assessment notice (regarding elements pertaining to the adjustments leading to double taxation), the existence of a litigation proceeding does not prevent the mutual agreement procedure to begin and/or the Competent Authorities to exchange views regarding the case or information on the pending judicial proceeding;

EU Arbitration Convention

- however, in the event a judicial decision occurs and the double taxation has not been eliminated, the latter will not be removed unless the foreign Competent Authority signs a mutual agreement consistent with the domestic judicial decision;
- in any case, the taxpayer can carry out the appeal on issues other than those falling into the scope of the mutual agreement procedure.

EU Arbitration Convention

Timeframe of the procedure



$2 \text{ years} + 6 \text{ months} + 6 \text{ months} + 6 \text{ months} = \text{MIN } 3 \text{ years and } 6 \text{ months}$

Directive (EU) 2017/1852 of 10 October 2017

- The adoption of EU Directive 2017/1852 (on tax dispute resolution mechanisms in the European Union) has to be seen as a **natural upgrade** toward a **more efficient and effective procedure for the resolution of tax conflicts** by means of the strengthening and enhancing of the already available transnational conflict resolution mechanisms.
- The measure aims at uniforming and enhancing the transnational mutual agreement procedures currently in force in EU Member States, in order to guarantee to taxpayers a far more harmonized, efficient and transparent framework, creating, at the same time, a favorable environment for those companies willing to invest in the EU market.

Directive (EU) 2017/1852 of 10 October 2017

- **Personal scope:**

- Art. 2(1)(d): “*any person, including an individual, that is a resident of a Member State for tax purposes, and whose taxation is directly affected by a question in dispute*”.
- **Any** taxpayer will be able to access this procedure.
- The personal scope is broader than the one of the EU Arbitration Convention.

Directive (EU) 2017/1852 of 10 October 2017

- **Objective scope:**

- Art. 1: *“This Directive lays down rules on a mechanism to resolve disputes between Member States when those disputes arise from the interpretation and application of agreements and conventions that provide for the elimination of double taxation of income and, where applicable, capital. It also lays down the rights and obligations of the affected persons when such disputes arise”*.
- The objective scope is broader than the one of the EU Arbitration Convention.
- Not limited to Transfer Pricing rules and attribution of income to PE.

Directive (EU) 2017/1852 of 10 October 2017

- **Steps of the procedure:**

- the complaint has to be filed within **3 years** following the first notification of the action which results or it is likely to result in double taxation;
- the affected person shall simultaneously submit the complaint with the same information to each competent authority, and shall indicate in the complaint which other Member States are concerned;
- Each Authority shall acknowledge the receipt of the complaint within **2 months** from having received it and communicate, within the **6 months** following the reception of the complaint (or of the integrative information requested), whether the complaint is accepted or rejected;

Directive (EU) 2017/1852 of 10 October 2017

- where the competent authorities of the Member States concerned accept a complaint, they shall endeavour to resolve the question in dispute by mutual agreement within **2 years** starting from the last notification of a decision of one of the Member States on the acceptance of the complaint;
- the period of 2 years referred to in the first subparagraph may be extended by up to **1 year** at the request of a competent authority of a Member State concerned;
- where the competent authorities of the Member States concerned have not reached an agreement on how to resolve the question in dispute, the competent authority of each of the Member States concerned shall inform the affected person indicating the general reasons for the failure to reach agreement.

Directive (EU) 2017/1852 of 10 October 2017

- In case of **failure to reach an agreement**:
 1. upon a request made by the affected person to the Competent Authorities of the Member States concerned, it shall be possible to set up an **Advisory Commission** which will be asked to express an independent opinion;
 2. alternatively, the establishment of an **Alternative Dispute Resolution Commission** can be agreed between the Competent Authorities of the Member States interested to reach an agreement by means of the so-called alternative dispute resolution procedures.

Directive (EU) 2017/1852 of 10 October 2017

- **The Advisory Commission:**

- should be made up of:

- one chair;

- one representative of each competent authority concerned (this number may be increased to two by agreement between the competent authorities);

- one independent person on standing (if the competent authorities agree, the number of such person appointed may be increased to two for each competent authority).

- **The Alternative Dispute Resolution Commission:**

- may differ regarding its composition and form from the Advisory Commission;

- may apply, where appropriate, any dispute resolution processes or technique to solve the question in dispute.

Directive (EU) 2017/1852 of 10 October 2017

- **The Advisory Commission or the Alternative Dispute Resolution Commission:**
 - shall deliver its opinion not more than **six months** from the date on which the matter was referred to it. This period may be extended by 3 months;
 - shall adopt its opinion by a **simple majority** of its members;
 - where a majority cannot be reached, the vote of the chair shall determine the final opinion;
 - The chair shall communicate the opinion of the Advisory Commission or Alternative Dispute Resolution Commission to the competent authorities.

Directive (EU) 2017/1852 of 10 October 2017

- After the decision, the competent authorities involved:
 - shall take a decision which will eliminate the double taxation within **6 months** of the date on which the opinion has been delivered;
 - may take a decision which deviates from the opinion;
 - if they fail to reach agreement, they shall be obliged to act in accordance with that opinion.
- Each Member State shall provide that its competent authority shall notify the final decision on the resolution of the question in dispute to the affected person without delay.
- In the absence of such notification within **30 days** from the decision having been taken, the affected person may appeal in its Member State of residence in accordance with the applicable national rules in order to obtain the final decision.

Directive (EU) 2017/1852 of 10 October 2017

- **Interplay with domestic legal procedure:**

- The fact that the action of a Member State that gave rise to a question in dispute has become final under national law shall not prevent the affected persons from having recourse to the procedures provided for in this Directive.
- The submission of the question in dispute to the mutual agreement procedure or to the dispute resolution procedure shall not prevent a Member State from initiating or continuing judicial proceedings or proceedings for administrative and criminal penalties in relation to the same matters.
- Specific provisions in case a decision on a question in dispute has been rendered by the relevant court or other judicial body of a Member State, and the national law of that Member State does not allow it to derogate from the decision (Art. 16(4)).

Directive (EU) 2017/1852 of 10 October 2017

- Member States may refuse access to the Directive's procedure:
 - in cases where penalties were imposed in that Member State in relation to Question in Dispute for tax fraud, willful default or gross negligence;
 - on a case-by-case basis where the question in dispute does not involve double taxation.

Directive (EU) 2017/1852 of 10 October 2017

- **Review:**

- by 30 June 2024, the Commission shall evaluate the implementation of this Directive and shall present a report to the Council;
- that report shall, if appropriate, be accompanied by a legislative proposal.

- **Transposition:**

- Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 30 June 2019 at the latest;
- they shall forthwith communicate to the Commission the text thereof.

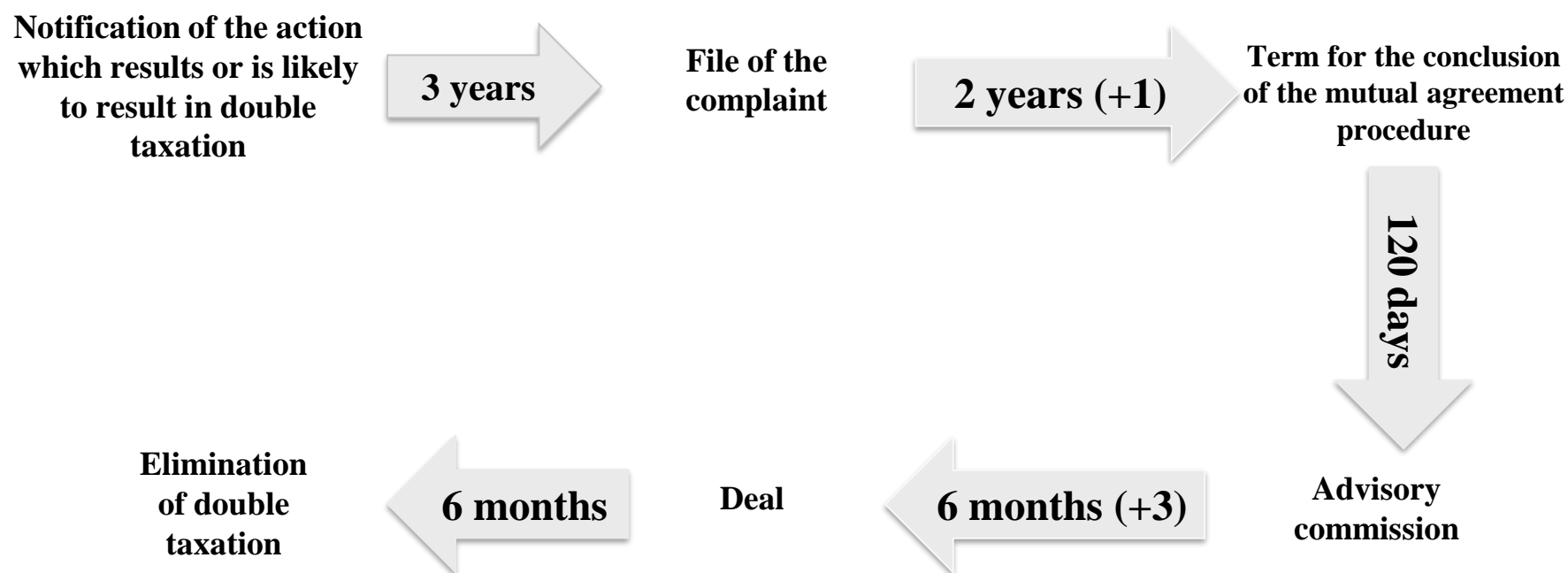
Directive (EU) 2017/1852 of 10 October 2017

- **Entry into force:**

- The Directive applies to any complaint submitted from **1 July 2019 onwards** relating to questions of dispute relating to income or capital earned in a tax year commencing on or after **1 January 2018**;
- competent authorities of Member States concerned may however agree to apply this Directive with regard to any complaint that was submitted prior to that day or to earlier tax years.

Directive (EU) 2017/1852 of 10 October 2017

Timeframe of the procedure



2 years (+1) + 120 days + 6 months (+3) + 6 months = MIN 3 years and 4 months

MAP – Comparisons

	Art. 25 OECD MC	EU Arbitration Convention	Directive (EU) 2017/1852
Personal scope	« Person » meaning a taxpayer resident for tax purposes in one of the Contracting States	Enterprises resident in a Member State with respect to their interest ownership existing with enterprises resident in another Member State or PEs in a EU Member State of enterprises resident in another Member State	Any person , including an individual, that is a resident of a Member State for tax purposes
Objective scope	Events triggering a double taxation	Disputes concerning transfer pricing adjustments carried out on enterprises and permanent establishments.	Disputes between Member States regarding double taxation
Deadline for filing the complaint	3 years from the date in which the event triggering a double taxation occurred, but can be amended by Contracting States	3 years following the first notification of the action which results or it is likely to result in double taxation	3 years following the first notification of the action which results or it is likely to result in double taxation
Obligation to solve the issue	No	Yes	Yes
Interplay with domestic legal procedure	Start of the MAP irrespective of the remedies provided by the domestic law of the States	Arbitration phase available only and insofar as the associated enterprise has allowed the time provided for the appeal to expire, or has withdrawn any such appeal before a decision has been delivered	The fact that the action of a Member State that gave rise to a question in dispute has become final under national law shall not prevent the affected persons from having recourse to the procedures provided for in this Directive

Case study No. 1

A famous Italian singer moves from Italy to UK where he starts living in an apartment he rented there and starts working the greater part of the year for a famous Opera House in UK.

Since the singer's family remains in Italy, the singer comes back to Italy on a regular basis to visit his family, spending in Italy less than 162 days per year.

He retains one bank account in Italy, but his remuneration is remitted by theaters where he performs (around the world, but mainly in UK) on a bank account at a UK bank.

He still holds a telephone contract with an Italian company.

The singer is registered to the A.I.R.E. (Anagrafe Italiani Residenti all'Estero).

Case study No. 1

Where is the centre of vital interests of the Singer?

UK

- Work relationships
- Apartment
- Employment relationships
- Bank account
- Place of work

ITALY

- Family
- Social relationships
- Family home
- Telephone contract with Italian company

Case study No. 1

Art. 4(2) Italy – UK Income Tax Treaty (1988)

Where by reason of the provisions of paragraph 1 of this Article an individual is a resident of both Contracting States, then his status shall be determined in accordance with the following rules:

- a) he shall be deemed to be a resident of the Contracting State in which he has a **permanent home** available to him. If he has a permanent home available to him in both Contracting States, he shall be deemed to be a resident of the Contracting State with which his **personal and economic relations are closer** (centre of vital interests);*
- b) if the Contracting State in which he has his centre of vital interests cannot be determined, or if he has no permanent home available to him in either Contracting State, he shall be deemed to be a resident of the State in which he has an **habitual abode**;*
- c) if he has an habitual abode in both Contracting States or in neither of them, he shall be deemed to be a resident of the Contracting State of which he is a national;*
- d) if he is a national of both Contracting States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.*

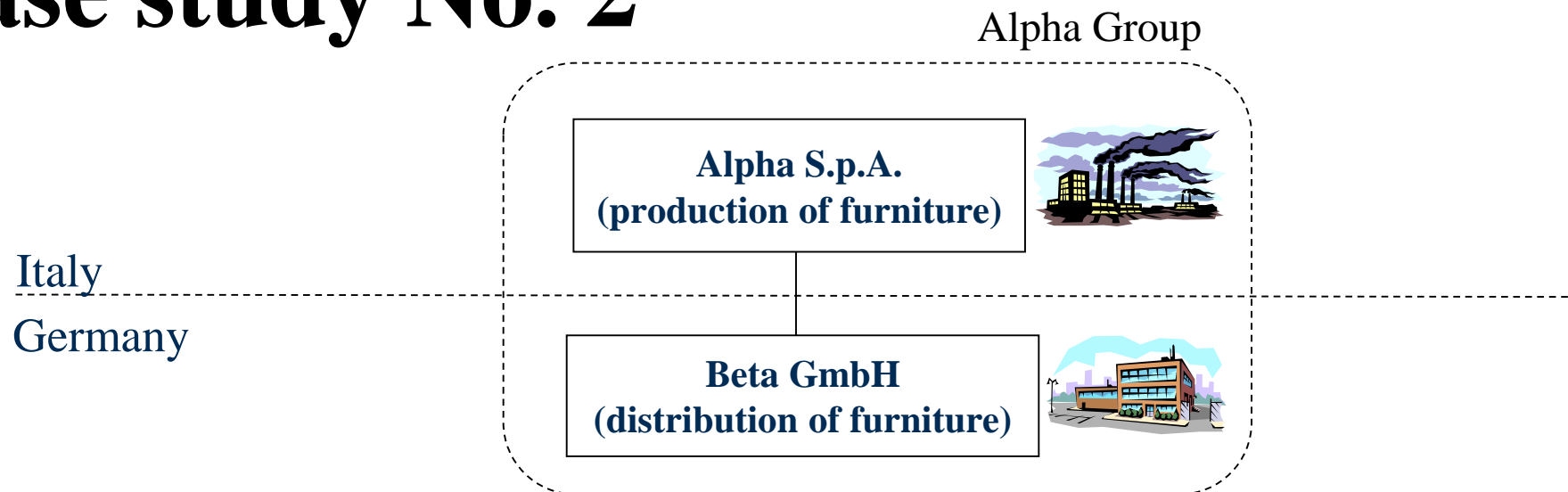
Case study No. 1

The Italian and English CAs may consider that:

- On the one hand, the singer has a permanent home available in UK, where he lives the greatest part of the year and carries on his principal working activity (but he also have a family home in Italy);
- On the other hand, the centre of his vital interests could be deemed in Italy, considering that his personal, key relationships are all in Italy.

Therefore, the CAs shall address the issue considering the provision of Art.4 (2) of the Double Tax Convention between Italy and UK.

Case study No. 2



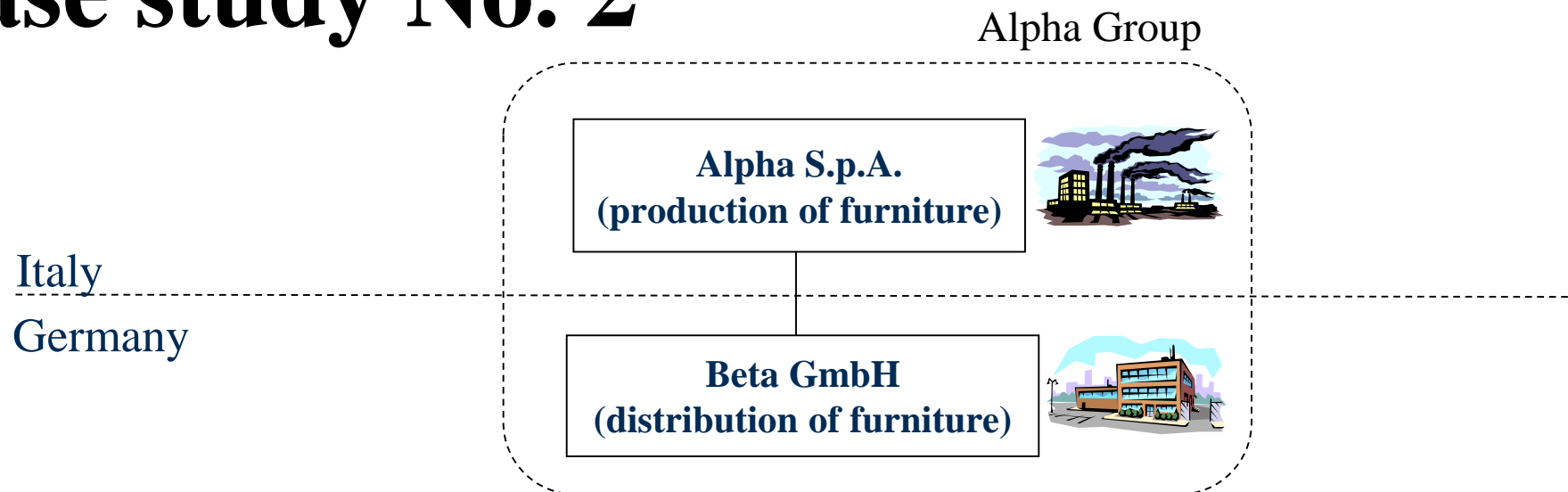
The Italian based company Alpha S.p.A. is a manufacturer of classical Italian design furniture.

In Germany its products are distributed by a subsidiary (Beta GmbH) that was established solely for this purpose.

In 2018, production and distribution generated a joint profit of 100.

Due to differing transfer prices, Italian tax authorities allocate a profit of 70 to Alpha S.p.A. for Corporate Tax purposes while German tax authorities allocate a profit of 50 to Beta GmbH.

Case study No. 2



Questions:

1. Which international procedures can be initiated by the companies in Italy/Germany to eliminate double taxation?
2. Is one of them preferable?
3. Are national appeals in parallel with the international procedures admissible?
4. If so: can both national and international appeal procedures be pursued actively at the same time?