

# TAXPAYERS' RIGHTS IN MUTUAL AGREEMENT PROCEDURE ON THE BASIS OF DOUBLE TAXATION TREATIES AND THE BRICS COUNTRIES

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## ABSTRACT

*Taxpayers' rights are of utmost importance in the context of the fundamental changes in the regulation of international tax relations determined by the necessity to combat tax avoidance at the global level. These changes create high level of uncertainty among taxpayers that might have negative effect on the economic development of states especially developing ones because of decrease of investment and entrepreneurial activities. Thus, contemporary states should provide high level of efficiency of dispute resolution mechanisms including mutual agreement procedure (MAP). It is the procedural mechanism allowing taxpayers to resolve their cases of taxation not in accordance with the provisions of double taxation treaties by the way of initiation of the communication between the competent authorities of contracting states that have concluded double taxation treaties. Based on the analysis of pros and cons of MAP, it might be stated that its attractiveness is not so obvious for taxpayers in the absence of certain guarantees such as the right to confidentiality or the right to be informed about the process of negotiation between competent authorities. The success of international community is only partial in this context because of the difficulty to find common denominator and the difference of interests at the global level. At the same time, the example of the EU demonstrates that the regional cooperation might be crucial in the improvement of taxpayers' rights in the context of MAP that might be taken into account by the BRICS countries in their attempts to improve tax dispute resolution mechanisms.*

**Keywords:** Double Taxation Treaties, Human Rights, Taxpayers' Rights, Mutual Agreement Procedure, Dispute Resolution.

## INTRODUCTION

As it is stated by Lombardo, mutual agreement procedure (MAP) should be understood as

*“A special procedure outside domestic law aimed at representing the dispute on an amicable basis”,*

I.e. by the agreement between the competent authorities of the contracting states in cases where tax has been charged, or is going to be charged, not in accordance with the provisions of the double taxation treaty concluded between such states (Lombardo, 2008). Its potential allows contracting states to strengthen tax certainty that is mentioned by the G20 Leaders as one of the areas of their common efforts in an attempt to promote investment and trade in Hangzhou Communique adopted in September 2016 (para. 19) (G20 Information Centre, 2016).

The statistics of MAPs demonstrates the obvious fact that its importance continues to grow among developing and developed states in the context of the post-BEPS era including five BRICS states: Brazil had 13 MAP cases at the beginning of 2017 and 19-at the end of the same year, China-111 and 131 respectively, India-725 and 763, Russia-7 and 14 and South Africa-26 and 28 (OECD, 2018). It should be admitted that the MAP is

*“The first and most used treaty-based form of international tax dispute resolution” (Christians, 2012).*

The absence of effective MAP mechanism deprives the taxpayers of contracting states of opportunities for resolving tax treaty disputes that might lead to double taxation. At the same time, it is worth mentioning that the existence of MAP mechanism is undesirable without clear definition of the content of taxpayers’ rights because does not create the conditions for trust as well as confidence between taxpayers and competent authorities. Based on this need, the list of positive taxpayers’ rights concerning MAP might be desirable as an additional step in setting the balance between the interests of taxpayers and competent authorities.

## RESULTS AND DISCUSSION

The provisions on MAP are implemented in Art. 25 of the OECD Model Tax Convention (OECD MTC) that is widely recognized as constituting element of so-called “*international tax language*” (Vogel, 1997). Thus, the appearance of the OECD MTC is mentioned by R. Williams as

*“The beginning of a new era in international taxation” because it was accepted “as a pattern on which bilateral tax conventions might thereafter be shaped” (Williams, 2014).*

Obviously, the inclusion of Art. 25 has determined the presence of the provisions on MAP in the largest part of modern double taxation treaties.

The above mentioned article consists of five paragraphs.

The first two paragraphs formulate the obligation of the competent authorities to cooperate in an attempt to endeavor by mutual agreement to resolve the situation of taxpayers where they are subjected to taxation not in accordance with the provisions of double taxation treaty. The third paragraph gives the competent authorities the opportunity to resolve by mutual agreement problems that might arise in the process of interpretation or application of the provisions of double taxation treaty. Besides, it also authorizes the competent authorities to consult together for the elimination of double taxation in cases not provided for in the provisions of double taxation treaty. The fourth paragraph is dedicated to the issue of forms of interaction between competent authorities in the process of MAP and states that they may communicate with each other directly, including through a joint commission consisting of themselves or their representatives. The fifth paragraph provides a mechanism aimed at the arbitration of unresolved issues that hamper reaching a mutual agreement between competent authorities within two years. Such mechanism is activated by sending a request from the affected taxpayer.

It is worth mentioning that the potential of mandatory arbitration is rarely used by developing countries and the BRICS countries are not an exception in this case. They have refused to recognize themselves as being obliged by the provisions of Part VI of the Multilateral

Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) that enables countries to include mandatory binding treaty arbitration in their double taxation treaties in accordance with the special procedures. Besides, mandatory arbitration is not placed among the elements of obligatory minimum standard that has been adopted in the process of the global anti-BEPS campaign. Taking into account cautious positions of the dominant number of modern states concerning mandatory arbitration, it seems that the scope of our research might be limited to the issues of MAP that is initiated by person in case of its taxation not in accordance with the provisions of double taxation treaty.

First of all, one might admit that the text of Art. 25 (1) of the OECD MTC expressively gives a taxpayer the right to initiate the MAP procedure, irrespective of the remedies provided by the domestic law of contracting states, in case of the actions of contracting states that result or might result in taxation not in accordance with the provisions of the double taxation treaty (OECD, 2017).

The Commentary on Art. 25 of the OECD MTC gives more detailed description of the right to initiate MAP:

1. The MAP process is applicable in case of double taxation as well as in the absence of any double taxation contrary to the provisions of double taxation treaty on the basis of the fact that the taxation in dispute is not in accordance with the treaty norms (para. 13);
2. A taxpayer might initiate MAP without waiting until the taxation not in accordance with the provisions of double taxation treaty has been charged against or notified to him but it has to be added that such taxation appears at risk which is not merely possible but probable (para. 14);
3. A taxpayer should present his objections to the competent authorities of either contracting state and they must be so presented within the three years of the first notification of the action which gives rise to taxation that is in contravention with the provisions of double taxation treaty (para. 16);
4. A taxpayer is not precluded from presenting his case to the competent authorities of both contracting states at the same time but there is an obligation of taxpayer to inform both competent authorities about that, in order to facilitate a coordinated approach to the case (para. 17);
5. The expression “*first notification of the action resulting in taxation not in accordance with the provisions of the Convention*” should be interpreted in a way that the time limit begins to run only from the date of the notification of the individual action giving rise to such taxation (para. 21);
6. The period of three years for initiating MAP is not interrupted by the fact that there is and domestic law (including administrative) proceedings (para. 25);
7. A taxpayer is entitled to present his case to competent authority of either state whether or not he may have made claim or commenced litigation under the domestic law of one (or both) of the contracting states (para. 34);
8. The implementation of a mutual agreement between competent authorities should normally be made subject to the acceptance of such agreement by the taxpayer, and to the taxpayers’ withdrawal of the suit at law concerning those points settled in the mutual agreement (para. 45);
9. Interest and administrative penalties accessory to taxation not in accordance with the provisions of double taxation treaty should be appropriately reduced or withdrawn pursuant to the MAP but other administrative penalties (for example, a penalty for failure to maintain proper transfer pricing documentation) are not fall within the scope of the MAP in accordance with the treaty norms (para. 49).

These provisions are not able to hide the fact that there are no more references to rights of taxpayers neither in Art.25 of the OECD MTC nor its Commentary. As it is stated by Lombardo, the legal position of the taxpayer himself in the context of MAP is not spelled out at all in Art. 25 of the OECD MTC:

*“It has no specifically defined obligation to participate, give evidence or proof any kind any kind, but it is not possible to see how the procedure could be affected if the taxpayer were to be totally uncooperative” (Lombardo, 2008).*

Based on the opportunities of taxpayers to initiate MAP in accordance with Art. 25 (1) of the OECD MTC, M. Lang states that MAP might be considered as an important element in *“the legal protection of the taxpayer”* because it allows to cure the deficiencies that might arise in case of conflicting interpretations of the same treaty norms by the competent authorities of contracting states. Nevertheless, he has to recognize that the OECD MTC does not include any provisions that refer to the taxpayer’s position in the MAP in addition to the taxpayer’s right to present objections. At the same time,

*“It is the duty of the contracting states to give the taxpayers certain essential guarantees” (Lang, 2013).*

Obviously, the content of these guarantees might be interpreted freely by the contracting states in the absence of the clear set of recommended standards that makes the system of the legal protection of the taxpayer weaker than it should be.

Taking into account the nature of the MAP as intergovernmental mechanism of dispute resolution, Züger admits that:

*“The taxpayer is not party to the procedure and has-subject to domestic law providing otherwise- neither a right to inspect the case files nor the right to be heard in the procedure”.*

Moreover, he states that the tax authorities of the OECD member states are only willing to give taxpayers two rights:

1. The right to present written or oral statements themselves or through a representative;
2. The right to choose a counsel in case of the joint commission formed by the competent authorities of the contracting states in accordance with Art. 25 (4) of the OECD MTC.

It has to be added that there is no visible result of the presence of such common willing in the provision of Art. 25 of the OECD MTC and its Commentary despite the fact that they have been changed in the provisions on MAP in 2017. The taxpayers are still lack the concrete procedural rights in the context of MAP. Thus, one might agree with the statement that

*“The participation rights for taxpayers promised by the OECD Commentaries are of little practical significance because there is no consensus on their content between states” (Züger, 2001).*

Higher level of protection of taxpayers’ rights in the context of MAP on the basis of double taxation treaties of the EU member states clearly points out at the advisability of further improvements of the approach implemented in the OECD MTC and its Commentaries. Additionally, there are demands from the taxpayers concerning further developments of their procedural rights in the context of MAP as it follows from the materials of discussion concerning the final report on Action 14 of the anti-BEPS campaign described above.

The proposed way of further development of MAP as dispute resolution mechanism is also supported by researchers. Among them are Baker and Pistone. They propose a list of rights that might be understood:

*“As a ‘minimum standard’ in the regulation of MAP by contracting states. It includes the following:*

- 1. A right to initiate an MAP;*
- 2. The taxpayer should be given a challengeable reason why the matter has not been taken forward if for any reason the competent authority decides not to take forward the procedure;*
- 3. The taxpayer should be kept fully informed during the procedure;*
- 4. The taxpayer should be entitled to see any documents employed in the process (except those for which a genuine case for secrecy can be made);*
- 5. A right of taxpayer to be represented;*
- 6. A right of taxpayer to a hearing by one or both competent authorities before a resolution is reached” (Baker & Pistone, 2015).*

The proposed list of taxpayers’ rights in the context of MAP might be criticized in some of its elements. For example, H. Ault states that the right of direct participation of taxpayers and the right to make presentations should be conditioned by the presence of permit from the competent authorities of contracting states:

*“Depending on the situation, the competent authorities may permit the taxpayer to submit briefs or make presentations to either one or both of them. These presentations may also contain taxpayer proposals for the resolution of the case. However, direct taxpayer’s participation in the competent authority negotiations would not be appropriate, given the differing interests of the parties, through timely indications to the taxpayer of the status of the negotiations would be useful in moving the case forward” (Ault, 2013).*

Despite the difference among researchers on the content of taxpayers’ rights under MAP, it is obvious that strengthening their protection might be desirable based on the needs of taxpayers and the changes of modern system of regulation of international tax relations that might have negative influence on investment and trade activity. This trend might be affirmed by the example of setting of higher standards of taxpayers’ protection in the EU.

At the same time, the BRICS states decide to follow the approach that is stricter in comparison with the EU approach as it is followed from the provisions of draft of Multilateral Convention between the Government of Brazil, the Government of the Russian Federation, the Government of India, the Government of People’s Republic of China and the Government of Republic of South Africa for Settlement of Cross-Border Tax Disputes. This document is the result of work of the Second Coordination Committee Meeting of the BRICS Law Institute and the BRICS and Developing Countries Legal Experts Forum (Yekaterinburg, 2-10 June 2017) (draft of the BRICS Convention) (Vinnitsky, 2018). Its provisions give taxpayers the right to tax arbitration in case where MAP between the competent authorities of the contracting states does not eliminate taxation that does not comply with the double taxation treaty between the contracting states (Art. 3).

First, the provisions of the draft of the BRICS Convention concerning the right of tax arbitration include the threshold of the amount of the dispute that should exceed \$100,000 or the equivalent amount in the national currency of the contracting states. One might suggest that usual taxpayers might be in a less favorable position than large taxpayers only based on the amount of the dispute.

Second, the provisions of the draft of the BRICS Convention adds nothing to the list of the taxpayers’ rights in the context of MAPs based on the double taxation treaties of the BRICS

states if it is compared with the OECD approach in Art. 25 of the OECD MTC and its Commentaries. The only exception is the right to tax arbitration.

Third, the taxpayer initiated the MAP is deprived of the right of refusal in case of the decision of the Arbitration Panel (Art. 5(2)). It has to be noted that the OECD approach includes the condition of taxpayer's acceptance of the arbitration decision in accordance with Art. 25(5) of the OECD MTC. In other words, the proposed approach limits the list of rights that is included in Art. 25 of the OECD MTC.

It is widely recognized that tax arbitrage "*is an integral part*" of MAP on the basis of the provisions of double taxation treaties and does not constitute an alternative route to solving disputes concerning the application of the treaty norms (para. 5 of the Commentary on Art. 25 of the OECD MTC). Thus, the right to tax arbitrage should complement the right to initiate MAP.

Consequently, the protection of taxpayer's demands to make the list of their rights wider than it is proposed now in the context of MAP on the basis of double taxation treaties concluded by the BRICS states. As minimum, these rights should include the right to be informed about the process of negotiation between competent authorities, the right to be informed of all documents that are presented in the process of MAP by competent authorities (except those for which a genuine case for secrecy can be made), the right to be informed about the reasons of refusal in initiating of MAP by competent authorities and the right of refusal of the mutual agreement negotiated by the competent authorities or the arbitration decision.

## CONCLUSION

Taking into consideration unique characteristics of MAP as dispute resolution mechanism, the right to initiate MAP is of paramount importance in the process of the interpretation and application of double taxation treaties especially these days. The unprecedented changes of tax rules resulted from the global anti-BEPS campaign has created the necessity in the efficient and effective MAP since the beginning of the project. In the other case, negative effects of taxation not in accordance with the provisions of double taxation treaties might destimulate the development of transboundary economic relations between contracting states.

At the same time, there is no consensus among the members of international community on the issue of concrete package of taxpayers' rights in the process of MAP except the right to initiate MAP. It is also absent on the level of researchers. Nevertheless, the example of the EU member states cooperation on improvement of dispute resolution on the basis of MAP demonstrates that the list of taxpayers' rights has a real chance to be widened at the regional level because of the similarity of economic interests of cooperating states. The EU member states widened the package of taxpayers' rights in the context of MAP on the basis of their double taxation treaties by the way of adopting of the Council Directive 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the EU.

Based on the example of the EU Member States in the context of improvement of MAP, it is suggested that the similar approach might be tried to realize by the BRICS countries. Thus, the list of taxpayers' rights should be widened in the process of MAP by adding

1. The right to be informed about the process of negotiation between competent authorities;
2. The right to be informed of all documents that are presented in the process of MAP by competent authorities (except those for which a genuine case for secrecy can be made);

3. The right to be informed about the reasons of refusal in initiating of MAP by competent authorities;
4. The right of refusal of the mutual agreement negotiated by the competent authorities or the arbitration decision.

The realization of this opportunity gives the BRICS countries the chance to avoid possible negative effects of unresolved problems of taxation not in accordance with the treaty norms, to strengthen the atmosphere of trust and confidence of taxpayers and to provide the balance between public and private interests in the area of taxation. Thus, the appropriate changes should be made in the draft of Multilateral Convention between the Government of Brazil, the Government of the Russian Federation, the Government of India, the Government of People's Republic of China and the Government of Republic of South Africa for Settlement of Cross-Border Tax Disputes.

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