

# The Evolution and Future of the Mutual Agreement Procedure

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In this article, the authors, all former competent authority or APA officials from their respective governments, share their views on the mutual agreement procedure process and its future.

International income tax conventions are meant to facilitate the movement of people and capital and reduce barriers to trade. Double taxation has long been recognized as an impediment to those goals, making mechanisms for eliminating it key in tax treaties.

There are several salient milestones in the development of those mechanisms. Perhaps the oldest was part of the treaty between Austria-Hungary and Prussia, signed in 1899. The OECD's 1963 Draft Double Taxation Convention on Income and Capital included the mutual agreement procedure in its modern form (minus arbitration). It remained virtually unchanged until the OECD released the 2008 version of its Model Tax Convention on Income and on Capital, which introduced a mandatory binding MAP arbitration. In 2007 the OECD published its Manual on Effective Mutual Agreement Procedures, which contained a series of recommendations to improve the MAP process. In

2015 the OECD released the final action 14 report of its base erosion and profit-shifting project, in which it made a series of nonbinding recommendations similar to those in the Manual on Effective Mutual Agreement Procedures. The 2016 Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting created as a result of action 15 provides the opportunity for countries to sign on to mandatory binding MAP arbitration.

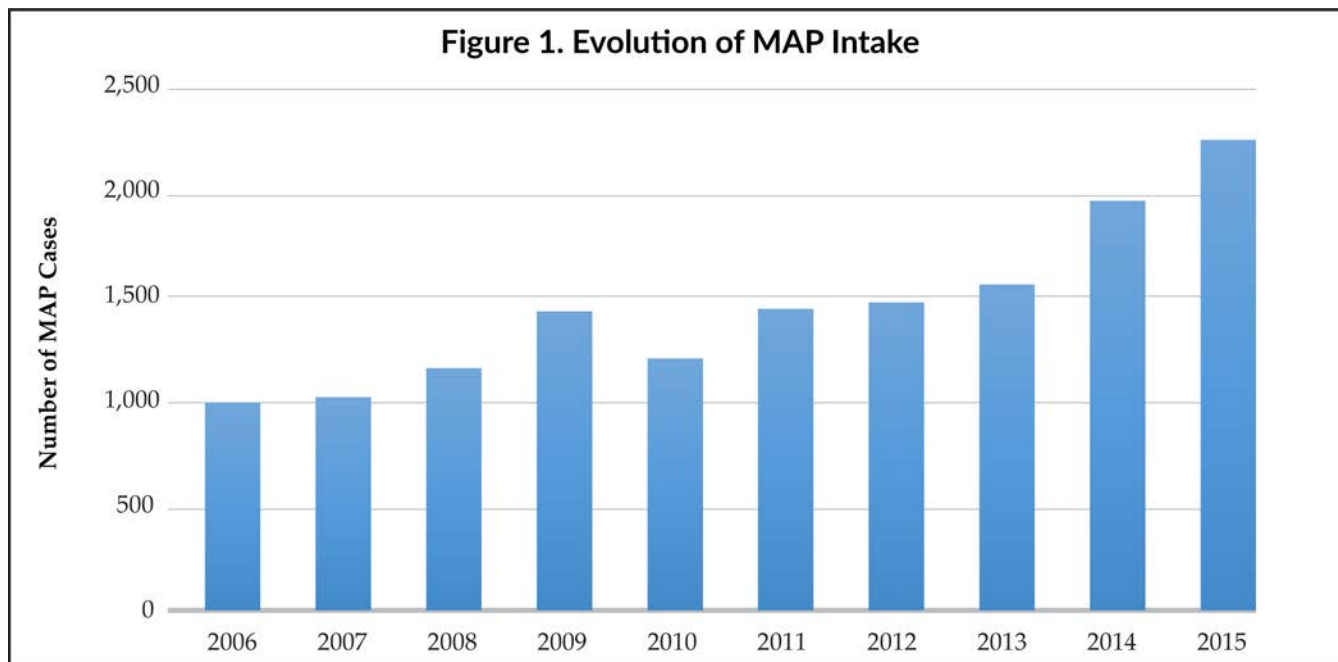
Since the 1990s, a few extensions — including advance pricing agreements and rollbacks, accelerated competent authority procedures, and joint and simultaneous audits — have enhanced the MAP program.

### Recent Statistics

#### Pre-2016

One of the problems with the pre-2016 MAP statistics available on the OECD website is that jurisdictions computed caseloads and time frames using different standards. For instance, some jurisdictions made no distinction between transfer pricing and other cases, and some made that distinction only in given years. Another difficulty in interpreting and comparing pre-2016 stats is that for many jurisdictions, the opening MAP inventory in a given pre-2016 year did not match the preceding year's closing inventory, with some of the oldest cases disappearing with no mention of being closed, withdrawn, or otherwise addressed.

Despite those problems, the statistics provide useful information about trends, even if they are not entirely accurate because of potential “apples to oranges” concerns. To illustrate, if only the 26 jurisdictions that reported MAP data to the OECD for all years from 2006 through 2015 are selected (to avoid biasing the evolution of the number of



MAP cases over time because of more countries providing data in later years), one can see a clear trend in the increase in MAP cases initiated annually. (See Figure 1.)

Figure 2 shows the evolution of the opening MAP inventories for the same countries over the same period.

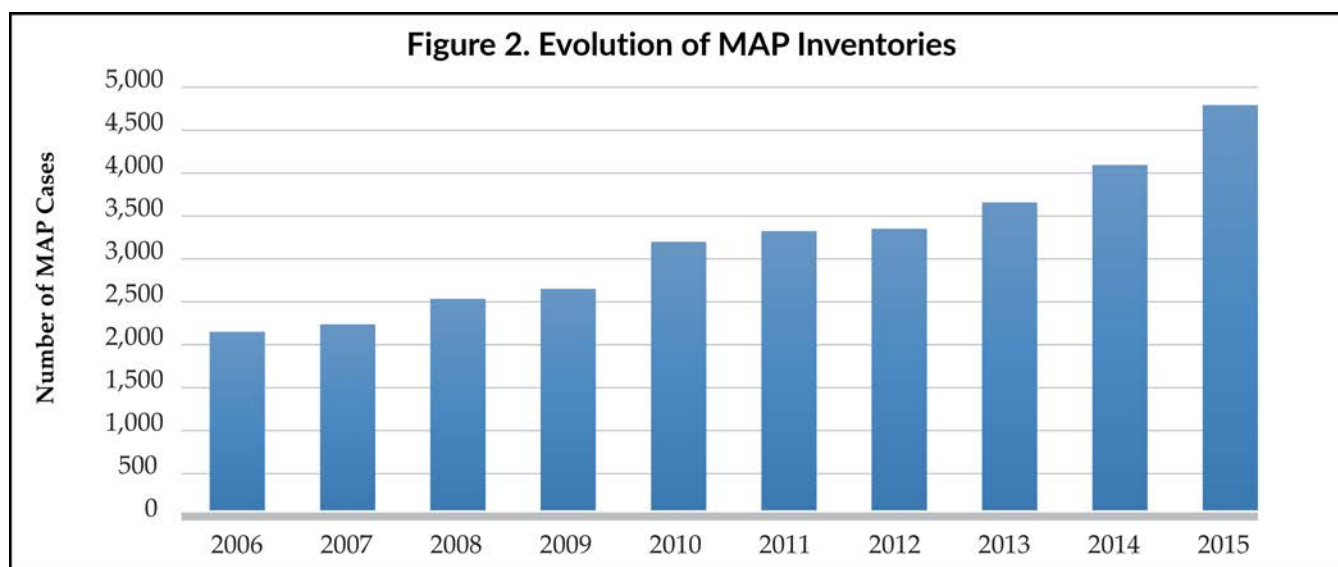
Although there are accuracy and comparability concerns with the pre-2016 stats, one can see clear increases in both MAP intake and inventories.

Importantly, the trend in increasing MAP intake began before the reforms brought about by

the various BEPS actions. Also, the growing number of MAP inventories arguably speaks to the demand for competent assistance outpacing the resources in competent authority programs and suggests that either additional resources or different approaches are needed.

**Post-2015**

As part of BEPS action 14, the OECD adopted a MAP statistics reporting framework that aligns the various data points provided by reporting countries. However, that framework applies only to fiscal years beginning on or after January 1,



## OECD Map Statistics

	Number of Reporting Countries	Starting Inventory	Cases Started In the Year	Cases Closed In the Year	End Inventory
2016	65	4,451	616	1,035	4,032
2017	86	4,137	779	1,235	3,681
2018	89	3,731	930	1,148	3,513

2016, so accurate comparisons cannot be made between pre-2016 and post-2015 data.

Consequently, the OECD also presents the data in a pre-2016 and post-2015 format, which clearly identifies the data on transfer pricing cases. The table illustrates OECD numbers of MAP cases for all reporting countries pre- and post-January 1, 2016.

While three years of data is not enough to draw inferences, one perhaps surprising element is that the aggregate inventory of transfer pricing MAP cases shrunk in 2016, 2017, and 2018, despite the intake increasing. On closer inspection, some of that is because several countries with track records of increasing inventories seem to have made conscious efforts to reverse the trend of intake outpacing the closing of cases. For instance, Germany and China were also able to reduce their inventories in 2016. Canada, France, Spain, and the United States each closed substantially more cases than they started in both 2016 and 2017, with Canada and the United States continuing that trend in 2018.

It remains unclear whether that spike in MAP closures, which coincided with the adoption of the MAP statistics reporting framework, will continue. For instance, in 2016 Canada reported closing 37 transfer pricing MAP cases that had started that year. Given the history of the Canadian MAP program, that would represent either an anomaly (such as a string of simple cases all resolved at once) or, if it becomes a trend, an indication that the Canadian competent authority has decided to unilaterally resolve more cases. By contrast, in 2017 Canada closed only 44 transfer pricing cases started since January 1, 2016, and started 73 new cases (it closed more pre-2016 cases in 2017, which resulted in the reduction in the overall inventory of transfer pricing MAP cases).

And as reported by the U.S. Government Accountability Office, in 2017 the U.S. competent

authority withdrew 74 percent of transfer pricing adjustments proposed by the IRS.

### Average Time to Close MAP Cases

Unfortunately, as described above, the problems with data definitions and computations, as well as in the actual application (with the disappearance of some MAP cases, including older ones in some jurisdictions), make the pre-2016 data on the time to conclude MAP cases unreliable. If anything, it appears that the time frames shown by some jurisdictions may have been underestimated.

Again, three years of post-2015 data is too limited to draw strong inferences. Further, the downward trajectory of the aggregate inventory of MAP cases might, based on historical observations, reflect not so much a sustainable improvement of the time to close MAP cases, but rather a push by tax authorities to clean up their inventories.

According to 2018 OECD data, the average time to close transfer pricing MAP cases is 33 months, up from approximately 23 months in 2006. In our view, and based on individual countries' MAP data, it seems clear that the average time to close those cases will continue climbing, with the intake and inventories increasing and less experienced competent authorities becoming involved in negotiations.

### Country-Specific Comments

#### Australia

The Australian Taxation Office has a long-standing MAP program with a good record of reaching agreement with other tax administrations to relieve double taxation in transfer pricing cases. Further evidence of that is in the OECD's latest MAP statistics for the year

that ended December 31, 2018. Of the 13 transfer pricing MAP cases closed in 2018 that involved at least some relief from double taxation, seven cases provided full relief, one case resulted in partial relief, and three involved unilateral relief.

At the end of 2018, Australia's closing inventory of transfer pricing MAP cases was 19 (72 having started before January 1, 2016, and 12 having started on or after January 1, 2016).

Because of the OECD's change in method for reporting the time taken to close MAP cases, it is now more appropriate to consider the average time taken to close cases that started before January 1, 2016, rather than cases that started on or after that date. In 2018 the ATO took an average of 45.37 months to complete pre-2016 transfer pricing MAP cases and 17.29 months to close cases started after 2015.

New Zealand and India had the largest number of transfer pricing MAP cases with Australia in 2018, which is interesting for several reasons. First, New Zealand and India were Australia's sixth and fifth largest trading partners, respectively, in 2018. Second, neither country has many bilateral or multilateral APAs in place or progress with Australia (as of June 30, 2018). By contrast, the ATO has a relatively large number of bilateral or multilateral APAs in place or progress (as of June 30, 2018) with Japan and the United States, its second and third largest trading partners, respectively, in 2018.

Finally, on November 21, 2018, the ATO withdrew its long-standing tax ruling on obtaining relief from double taxation and the MAP process (TR 2000/16) and replaced it with updated guidance on MAP principles and procedures. One of the reasons given for withdrawing the ruling was that it was not always consistent with the minimum standards and best practices in the OECD's final BEPS action 14 report.

### Canada

Because the United States is Canada's largest trading partner, it is unsurprising that transfer pricing MAP cases involving the United States as the other competent authority have historically represented approximately 80 percent of Canada's caseload (and 72 percent of Canada's APA caseload between 1993 and 2017). Canada

has been the initiator — that is, the tax authority that made the adjustment resulting in double taxation — in roughly 85 percent of those MAP cases.

Mandatory binding MAP arbitration is applicable between Canada and the United States, with the first cases having proceeded to arbitration on December 15, 2010. Although there are no official published data on the number of Canada-U.S. MAP cases resolved by arbitration, we do know it was between two and nine cases.

The real effect of mandatory arbitration has been to ensure that all MAP cases between those countries would be resolved within the two-year limit set by the arbitration rules. That, in turn, has had an undeniable effect on the average time to resolve Canada-U.S. MAP cases. Because cases between those countries are no longer proceeding to arbitration, the conclusion is that they are getting resolved within the 24-month time frame.

However, the same cannot be said about MAP cases between Canada and other countries. The 2017 data shows that on average, pre-2016 Canadian-initiated MAP cases took 34.38 months to complete and foreign-initiated MAP cases took 28.23 months. If we accept that Canada-U.S. cases are almost all completed within 24 months (which is in line with the authors' experiences), then cases with countries other than the United States are taking longer to resolve.

Since 2010, there has also been anecdotal evidence that indicates that the Canadian competent authority has been more proactive in applying the first step in the MAP process and thus resolving double taxation unilaterally. In 2018, seven Canadian cases were resolved unilaterally.

At the end of 2018, Canada's closing inventory of transfer pricing MAP cases was 114 (15 started before 2016; 99 started after 2015). The average time to close pre-2016 transfer pricing MAP cases was 42.47 months, while cases started post-2015 took an average of 15.17 months to close.

### China

According to the statistics as reported to the OECD secretariat, China had 85 transfer pricing MAP cases at the beginning of 2018 and an open inventory of 59 at the end of the year. The average time to close pre-2016 cases was 46.89 months.

Based on market intelligence, we understand that the State Taxation Administration had made additional efforts to resolve an increasing number of bilateral MAP and APA cases. That demonstrates the administration's commitment to implementing the BEPS action 14 minimum standards, including the peer review process.

### Denmark

Denmark completed 65 transfer pricing MAP cases in 2018, its highest completion rate to date, and had 138 open cases at the end of the year. Unilateral relief was granted in one of those cases, and 41 cases fully eliminated double taxation.

The average time to complete pre-2016 transfer pricing MAP cases was approximately 49 months.

### Italy

Italy has taken actions that should help strengthen the efficiency of MAPs by ensuring conclusion in a reasonable time. In 2012 it issued administrative guidance (Circular Letter No. 21/E of June 5, 2012) to establish clear rules for the implementation of MAP under tax treaties and the EU arbitration convention. The circular explains how MAP works and clarifies several other issues. Also, Italy has signed the OECD multilateral instrument and has opted to use mandatory binding MAP arbitration. Finally, on January 1, 2017, the Italian Revenue Agency (Agenzia delle entrate) took over as competent authority for the management of MAPs from the Ministry of Finance.

Italy provides MAP statistics to the OECD and under the arbitration convention to the European Joint Transfer Pricing Forum. The OECD statistics show that at the end of 2018, Italy had 401 post-2015 transfer pricing MAP cases and 100 pre-2016 cases open. It completed 31 pre-2016 cases and 59 post-2015 cases in 2018. Unilateral relief was granted in one of those cases, and 63 cases fully eliminated double taxation.

Pre-2016 transfer pricing MAP cases took on average 58.08 months to close.

### Mexico

Mexico had 39 open MAP cases at the end of 2018 (25 transfer pricing and 14 non-transfer pricing). That year, it completed six transfer pricing MAP cases and one non-transfer-pricing

case. The average time to close pre-2016 transfer pricing MAP cases was approximately 80 months.

Even though Mexico's inventory seems conservative, given the large increase in the number of both domestic and foreign audits, the Mexican tax administration is expecting its MAP inventory to increase significantly in the near future. To address that, it is working on a strategy to maintain a maximum 24-month average time frame to resolve MAP cases.

### New Zealand

New Zealand has 40 tax treaties, each with an article establishing a MAP process for resolving difficulties arising from the treaty's application. New Zealand has in force 11 tax information exchange agreements that contain MAP articles, as well as six supplementary agreements to those TIEAs that include MAP articles. Also, New Zealand's treaties with Australia and Japan contain arbitration clauses for resolving disputes.

The role of the New Zealand competent authority falls to the commissioner of Inland Revenue, but in practice is delegated to the manager of international revenue strategy, who leads double taxation cases arising from audit or compliance activities, and the policy manager, who leads on treaty interpretation issues. Those two competent authorities work together and interact with other divisions of Inland Revenue as needed to resolve MAP cases. The competent authorities act independently of others, forming their own view of issues in dispute.

The New Zealand Inland Revenue's overall aim is to complete MAP cases within 12 months of receiving a request for assistance. The time taken to resolve cases will vary depending largely on the complexity of the matter in dispute.

For 2018, New Zealand closed six post-2015 transfer pricing cases, taking an average of 3.28 months to close cases.

### Spain

The 2017 OECD peer review labeled the Spanish MAP program "satisfactory," meaning Spain is considered a reliable treaty partner with adequate experienced personnel who have improved the program's effectiveness in recent years.

Spain was one of the first countries to issue local procedural regulations for MAPs, which helped provide both certainty and reliability for a procedure that was considered rather exceptional when the local provisions were enacted in 2006.

Spain is also committed to arbitration. Aside from the EU arbitration program, it has included arbitration in treaties when the partner accepts the arbitration model in article 25 of the OECD model convention and has signed the MLI.

Statistics from the OECD and European Joint Transfer Pricing Forum show that as of December 31, 2018, Spain had 408 open MAP cases (257 transfer pricing cases). It initiated 132 transfer pricing cases in 2018 and completed 50 (20 were pre-2016 cases), leaving 257 transfer pricing cases pending. The average time to complete pre-2016 transfer pricing MAP cases was around 52.66 months, with post-2015 cases taking an average of 16.63 months. The pre-2016 case average exceeds the target timeline of 24 months because of some very old cases that are still pending. Spain is working intensively on those.

Overall, while there is room to increase efficiency, there have been great improvements in the management of the program, especially when the treaty partner has a similar approach.

### United Kingdom

The U.K. MAP program continues to deliver good outcomes, settling more cases in 2018 than in recent years. The 2017 OECD peer review of HM Revenue & Customs' MAP practices recognized the United Kingdom's strengths as a good treaty partner with a well-resourced competent authority team that uses a principled and pragmatic approach to resolve cases.

In 2018 HMRC accepted 80 new transfer pricing cases. That year, it settled 89 pre-2016 cases in an average of 46 months and post-2015 cases in 14.98 months.

HMRC recently updated both its statement of MAP practice and the accompanying guidance in the international manual, clarifying some issues and addressing others arising from the OECD review.

The United Kingdom is strongly committed to arbitration. In addition to having included arbitration provisions in many of its bilateral treaties with major trading partners, it remains a

participant in the EU arbitration convention and has signed on to increasing access to arbitration through the MLI.

The combination of that commitment and the general MAP improvements resulting from the BEPS action 14 continues to deliver better outcomes and make MAP an increasingly attractive option for U.K. resident companies.

### United States

In 2018 the IRS's advance pricing and mutual agreement program received 157 requests for transfer pricing-related competent authority assistance. That year, the APMA program closed 181 transfer pricing cases, although its ending inventory remained high at 670 open cases.

India is the U.S. treaty partner with the most MAP cases, with 173 open cases in 2018. Canada is next with 92 cases, followed by various European countries with significantly fewer cases. Historically, foreign-initiated adjustments made up approximately 80 percent of the inventory on average. Based on the authors' experiences with Indian and Canadian MAP cases, that trend has likely continued for 2019.

Consistent with prior years, MAP outcomes for 2018 were positive for taxpayers. More than 85 percent of resolved cases resulted in a full elimination of double taxation. Another 7 percent involved unilateral relief that accepted the foreign-initiated adjustment (compared with 32 percent in 2017). Less than 1 percent of cases resulted in no resolution. Consequently, MAP is an attractive option for taxpayers to resolve transfer pricing disputes with U.S. treaty partners.

As noted, the APMA program unilaterally withdrew 74 percent of U.S.-initiated cases in 2017. That is possibly why the IRS issued a February directive instructing IRS audit teams to consult with the program before issuing adjustments that could end up in a MAP to increase the likelihood that those adjustments could best be defended by the APMA program.

### Where Are We Headed?

First, mandatory binding arbitration must become the standard. Based on the above observations, it is our view that the key for competent authorities to be able to handle the

influx of transfer pricing MAP cases will be the wide adoption of mandatory binding MAP arbitration. That mechanism remains the only proven way to reduce the time needed to complete MAP cases and ensure all cases are addressed. Otherwise, unless tax authorities substantially increase their competent authority resources, MAP case resolution time frames will increase proportionately with the yearly increase in both new MAP requests and preexisting case inventory.

Second, there must be more unilateral withdrawals of adjustments by the initiating competent authority before negotiations. The first step in the MAP process is for the competent authority to whom the MAP request was addressed to determine if it can arrive at a satisfactory solution or unilaterally eliminate double taxation. We believe this step must continue gaining importance to keep inventories and time frames under control.

Finally, there must be more programs to address MAPs more efficiently. Any enhancement to the MAP program that produces additional benefits without additional effort, such as APA rollbacks and accelerated competent authority procedures, would bring substantial improvements to jurisdictions that have not yet adopted them. Also, it might be useful to get ahead of transfer pricing adjustments causing double taxation by encouraging the use of joint audits (audits conducted under the auspices of the MAP whereby two or more tax authorities audit their respective taxpayers of a common MNE regarding the same issues and the same fiscal years, with a view to reaching a common conclusion thereby avoiding the creation of double taxation), which would in turn reduce the need for assistance in the resolution of double taxation via MAP. ■