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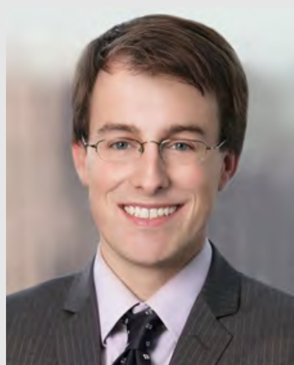
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In this article, the authors examine how the OECD's base erosion and profit-shifting project has changed the way governments handle mutual agreement procedure cases under tax treaties.

The OECD's original base erosion and profit-shifting initiative focused largely on suppressing planning mechanisms and regimes perceived to facilitate inappropriate profit shifting, but one sliver of the 15-action project was intended to benefit taxpayers by calling tax authorities to task: action 14 on dispute resolution. With the 2015 release of the action 14 final report, the members of the BEPS inclusive framework committed to abide by a minimum standard for handling mutual agreement procedure cases under bilateral tax treaties. While a February consultation revealed areas for improvement, it is clear that action 14 has been a major success: The prospects for effective relief of double taxation between treaty partners worldwide are generally very good.

Introduction

MAP is the cornerstone of treaty-based dispute resolution. Except when supplemented by mandatory binding arbitration, a treaty's MAP does not require the competent authorities to reach a successful result, but it does require that they try. In the United States, that is important not just for eliminating double taxation but also for the creditability of foreign taxes and for income tax accounting. As will be shown below, MAP is very successful. But that was not always the case.

Before BEPS action 14, MAP was often more of a theoretical than a practical remedy. Although an enormous network of global tax treaties nominally provided taxpayers with access to MAP, effective MAP relief was often unavailable in practice. The United States was generally effective in reaching MAP resolutions with its treaty partners and, tellingly, was one of the few countries to publish statistics showing MAP outcomes pre-BEPS.[1] In many other countries, MAP was unavailable or unavailing.

[1] IRS, "Annual Competent Authority Statistics" (last updated Dec. 30, 2020).

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Action 14 focused on transforming MAP. In part, that took place through the minimum standard, but perhaps even more important are the strides that action 14 made for transparency. As part of the action 14 minimum standard, countries committed "to seek to resolve MAP cases within an average time frame of 24 months" and to have their compliance monitored by their peers.[2] They also agreed to report MAP statistics according to an agreed framework, and those statistics have been published on the OECD's website since 2016, with more limited data available for prior years.

The Success of MAP

The transparency-based approach to improving MAP outcomes has proven a success. While the absence of comprehensive statistics on MAP outcomes for earlier years frustrates any attempt at a quantitative analysis, it is clear that on the whole, MAP is becoming more effective and must now be regarded as a viable remedy in much of the world. Just as important, taxpayers and practitioners now have access to the data to prove it.

Below is a compilation of statistics indicating the success of MAP for resolving transfer pricing cases in several key jurisdictions. The analysis does not extend to non-transfer-pricing cases, which may vary considerably in type and complexity among jurisdictions and thus present a less useful basis for overall comparisons. The statistics herein differ from those reported by the OECD in that they review only meritorious cases — that is, they exclude several categories used by the OECD:

- "Withdrawn by taxpayer": Cases withdrawn by the taxpayer do not provide a valuable data point for assessing whether MAP will be effective in a case.
- "Objection is not justified," "denied MAP access," and "agreement that there is no taxation not in accordance with tax treaty": Those categories involve cases in which the competent authorities found that the taxpayer's claim lacks merit or the taxpayer failed to comply with procedural requirements; thus, they are not relevant in assessing the success of MAP. On the most recent OECD Tax Certainty Day, November 18, 2020, OECD personnel confirmed that based on peer reviews, cases reported in the "not justified" and "denied access" categories do not represent improper restrictions of the scope of MAP, but rather generally involve principled denials of MAP access in cases involving incomplete or late filing.
- "Resolved via domestic remedy": While these cases may have successful outcomes, they do not represent successful outcomes in MAP and thus must be excluded from the analysis. Cases in this category are resolved via domestic procedures and withdrawn from or no longer eligible for MAP as a result.
- "Any other outcome": This extraordinary category is generally reserved for unusual circumstances, such as cases in which the applicable treaty is terminated during the pendency of cases in which the taxpayer liquidates.

Removing those categories from the statistics, four relevant categories remain. This article groups cases reported under "agreement fully eliminating double taxation" and "unilateral relief granted" together as full success. However, more specificity in the unilateral relief category would be helpful.[3] The other two groups include cases reported as "agreement partially eliminating double taxation" (partial success) and cases resulting in "no agreement, including agreement to disagree" (failure).

[2] Peer reviews are also used to monitor and promote compliance with other aspects of the BEPS project, including the implementation of country-by-country reporting under action 13, exchange of information on tax rulings under action 5, and prevention of treaty shopping under action 6.

[3] *See* KPMG LLP's comment letter in response to the OECD's public consultation on the 2020 review of BEPS action 14 (suggesting that the "unilateral relief" and "domestic remedy" categories should each be split into separate categories for full and partial relief).

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MAP Outcomes in Select Jurisdictions: Transfer Pricing Cases Closed in 2019

Jurisdiction	Number of Meritorious Cases	Full Success	Partial Success	Failure
United States	130	96.2%	1.5%	2.3%
Australia	7	100%	0%	0%
Canada	35	97.1%	0%	2.9%
China	12	25%	50%	25%
India	78	92.3%	7.7%	0%
Japan	46	84.8%	6.5%	8.7%
United Kingdom	66	98.5%	1.5%	0%

Despite covering only a few jurisdictions, those statistics speak to the fact that in many countries where multinational enterprises are likely to have substantial operations, MAP has success rates above 90 percent. At the same time, they show the need for a jurisdiction-by-jurisdiction analysis — problems persist in some countries, including China.

It is also important to recognize that even for countries that can boast a high MAP success rate, time frames for resolving cases remain long. Even though action 14 adopted an aspirational 24-month time frame, in 2019 transfer pricing cases took an average of 30.5 months to resolve — slightly worse than the 30-month average in 2016, the first year for which the OECD reported statistics. More work is needed, and — as will be described below — that work is underway.

Ballooning MAP inventories have exacerbated those difficulties. According to historical data made available by the OECD, OECD member countries had 2,352 MAP cases in inventory at the end of 2006. By the end of 2016, that number had shot up to 6,176. Both figures are reported according to the countries' own statistical frameworks and thus do not address double counting of MAP cases between OECD countries. If all the cases were between OECD members — which was not the case — the actual numbers would be 1,176 and 3,088. The reality, of course, falls somewhere in the middle, but the trend is clear: Between 2006 and 2016, MAP inventories among OECD members almost tripled.

That growth continues. Setting aside pre-2016 cases, which are plagued by the same difficulties with double counting, 2019 saw 1,887 MAP cases closed and 2,690 cases opened. By contrast, only 1,496 new cases were begun in 2016. As acknowledged by the OECD in its release of statistics for 2019, the number of cases resolved has also increased, but it has not kept pace with the rate of new cases. The growth in MAP inventories is likely contributing to the long average time frame for resolving MAP cases.

Room for Improvement

While the success of MAP outcomes has generally improved since the adoption of action 14, problems remain. The most prominent concern is timing. Efforts to attain resolution in an average of 24 months have been unsuccessful in many countries, despite competent authorities' best efforts. At the same time, MAP inventories are increasing. Additional competent authority resources could help alleviate some of the strain, but improvements are necessary if MAP is to retain its effectiveness as a dispute resolution forum.

In November 2020 the OECD released a public consultation document on action 14, which reported that based on peer reviews of inclusive framework members, "significant progress is being made" but that more must be done. The document laid out several proposals for expanding the minimum standard, all of which drew the support of commentators.[4]

[4] As reported during the public consultation meeting held February 1, 2020.

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The proposals with the most potential to allay increasing MAP inventories involve training for auditors, multiyear case resolution, and mandatory binding arbitration. Often, flawed and unreasonable transfer pricing adjustments generate MAP cases that result in the adjustment being withdrawn by the competent authority of the country that proposed it, either before or after consultation with the other competent authority. For example, the U.S. Government Accountability Office found (GAO-19-81) that a staggering 74 percent of IRS adjustments were withdrawn by the U.S. competent authority in 2017. The development of those cases needlessly wastes audit, competent authority, and taxpayer resources. Training for auditors could help them better understand transfer pricing cases and contextualize them, reducing the number of adjustments that need to be withdrawn by the local competent authority.[5] Cases withdrawn by the competent authority of the jurisdiction proposing the adjustment are reported under the "unilateral relief granted" category in the MAP statistics.

While the consultation document proposes only improved training as part of the minimum standard, discussion at the February 1, 2021, consultation meeting raised the possibility of expanding the minimum standard to improve mandatory consultations between a tax authority's audit function and its competent authority in potential treaty cases. The IRS instituted a formal consultation requirement in early 2019, perhaps in response to the large number of IRS adjustments that had to be abandoned in MAP. If properly implemented, a consultation requirement can allow the competent authority to provide invaluable input in potential treaty cases at an early stage — although to ensure that the competent authority retains its independence, the audit function should make the ultimate decision on whether to proceed with an adjustment.

Similarly, multiyear resolution of MAP cases would reduce inventory. Take a case in which a competent authority resolution is reached for year 1, and the same facts are applicable to filed years 2-4, as well as prospective years 5 and on. Without a multiyear resolution option, a tax authority will need to audit the years after year 1 separately and enter into new MAP cases, even if they would be restricted to a pro forma exercise of applying the year 1 resolution. Advance pricing agreements with rollback are useful in many cases but are more costly than MAP and are not available when the facts present in years 1-4 are not present in prospective years. There is a real need for a MAP-based mechanism for rolling forward resolutions to additional years.

The United States and Canada have both experienced success with the accelerated competent authority procedure (ACAP), which allows the taxpayer to include in its MAP request a request that the terms of the MAP resolution be extended to subsequent years for which the taxpayer has filed returns and the relevant facts remain the same. Yet almost no other countries acknowledge a formal ACAP process. In some cases, something like ACAP may be negotiated ad hoc; in others, no multiyear resolution is available. While ACAP requires the tax authorities to review later years and satisfy themselves that the facts remain sufficiently similar, experience with APAs has shown that should not be an impediment. Adding ACAP, or something like it, to the minimum standard would greatly increase the efficiency of MAP programs, and there do not appear to be any principled grounds for declining to do so.

Mandatory binding arbitration is more divisive. Many developing countries oppose it, both as a backstop to MAP and in the context of tax certainty mechanisms under pillar 1 of the inclusive framework's work on the tax challenges of the digitalization of the economy, commonly known as BEPS 2.0.[6] Yet arbitration can offer substantial advantages, the most important of which arises when it is not actually invoked: The threat of binding arbitration pushes competent authorities to work on cases in earnest and reach

[5] For a training document provided by U.S. competent authority personnel at an OECD meeting, see IRS, "Global Awareness Training for International Tax Examiners" (last accessed Mar. 29, 2021).

[6] Concerns stem from a perception that mandatory binding arbitration would infringe on countries' sovereignty and their right to determine tax, as well as from the fear that developing countries would experience worse results in arbitration because of a lack of resources and relative technical sophistication compared with their wealthier counterparts.

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reasonable resolutions before the deadline for triggering arbitration, which is generally two years after commencement. Of course, for that advantage to materialize, competent authorities must not be allowed to undermine the spirit of arbitration by agreeing to suspend its commencement indefinitely, which happens under existing arbitration provisions. If the objections of developing countries can be overcome and arbitration is included in the minimum standard, it will be important to address that concern, perhaps by providing a one-time limited extension of time in which to continue discussions before being required to proceed to arbitration.

Work on a new dispute prevention mechanism under pillar 1 has been progressing side by side with the work to improve MAP. The pillar 1 mechanism is designed to provide multilateral certainty across a potentially large number of jurisdictions and thus differs in important ways from traditional bilateral MAP procedures. Yet the pillar 1 work promises to yield insights that can benefit MAP dispute resolution, regardless of whether pillar 1 is adopted. Technical work on the dispute resolution proposal may pave the way for more widespread and efficient use of multilateral MAP cases, and the pillar 1 review and determination panel processes could be used as models for a binding backstop to MAP that may relieve some of the concerns associated with arbitration. By the same token, improvements to MAP and other dispute prevention mechanisms may yield insights that can improve dispute resolution in the BEPS 2.0 space.

Practical Implications

Continuing to improve and fine-tune MAP, together with associated dispute prevention mechanisms like APAs, will ensure the process remains viable. But just as important is that between most large and midsize treaty partners, MAP is extremely viable now, offering outcomes significantly better than what can be expected in domestic litigation or administrative appeals.

Obviously, that is good news for taxpayers. Indeed, rising MAP inventories in recent years are likely partly the result of increased confidence that the process can effectively eliminate double tax. The strength of the statistics indicates that taxpayers should continue to pursue MAP relief. That means they should file any required notifications in the time limits prescribed by the treaty (if applicable) and take care not to pursue domestic remedies that may preclude effective MAP relief. For instance, U.S. taxpayers should be aware that pursuing a case with IRS Appeals will limit the U.S. competent authority's ability to reach a resolution in MAP.

But the success of MAP has other important implications as well. U.S. Treas. reg. section 1.901-2(e)(5)(i) provides that voluntary payments to foreign government are not compulsory taxes and thus are not eligible for a U.S. foreign tax credit. To ensure that its foreign taxes qualify as compulsory rather than voluntary payments, a company must reasonably interpret and apply foreign law with the aim of reducing its foreign tax liability over time, and it must exhaust all effective and practical remedies to do the same.

The regulations list MAP relief as one of those measures, and *Procter & Gamble*[7] made it clear that competent authority relief, when it is effective and practical, must be invoked to make foreign taxes stemming from a foreign adjustment creditable in the United States. Historically, it may have been possible to secure opinions suggesting that MAP with a particular jurisdiction was not effective, excusing a taxpayer from the need to pursue MAP to receive its FTCs. Today, with the OECD publishing extensive MAP statistics, and with most of those statistics showing impressive success rates, it may be more difficult to secure an opinion that MAP relief is not effective or practical.

The same holds true in the income tax accounting context under Financial Accounting Standards Board Accounting Standards Codification 740 (formerly FASB Interpretation No. 48), which requires that an entity recognize a tax position only if it is more likely than not that it would be sustained on the merits if examined by a tax authority with full knowledge of the relevant facts. That standard looks to the final resolution of the matter, which may result from appeals, litigation, or MAP. If a tax position is recognized,

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[7] *Procter & Gamble Co. v. United States*, No. 1:08-cv-00608 (S.D. Ohio 2010).

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it must also be measured: The amount recognized on the entity's financial statements will be the greatest tax benefit that has a greater than 50 percent likelihood of being realized.

To determine that amount, a company must consider all possible outcomes and their respective probabilities, which includes MAP if a treaty applies. Since action 14 and the publication of the OECD's MAP statistics, measurement under FASB Accounting Standards Codification 740 should not rely on diaphanous judgment calls alone but should also take into account available MAP outcome data. That data will be most reliable when adjusted to exclude non-meritorious cases, as described above. Comparison with outcomes for taxpayers that withdrew their MAP cases or did not have a timely or valid claim does not provide a helpful data point for taxpayers that have MAP-eligible cases and need to determine the appropriate income tax accounting consequences.

Conclusion

MAP has improved since the adoption of action 14, but just as important is the improved visibility of outcomes that taxpayers now have. That information indicates that MAP is generally a very viable remedy. That is good news for taxpayers looking to resolve disputes in a manner that eliminates double taxation, but it also needs to be borne in mind for foreign tax creditability and income tax accounting purposes.

The success of MAP should not mask the challenges that remain. Resolution time frames remain long, and increasing caseloads strain the system. The success of the work to improve and expand MAP is critical to ensuring that the process remains an effective tool for taxpayers.[8] ■

[8]The information in this article is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the authors only and does not necessarily represent the views or professional advice of KPMG LLP.

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