

## **Discussion Draft on Chapter 4: Special issues faced by developing countries (and LDCs in particular)<sup>1</sup>**

### 3.1 Issues and experience in developing countries

#### 3.1.1. Legal issues and experiences

Economies are different and every country and every region has specific approaches to tax policy, varying economic circumstances, and more or less resources available. However, there is a set of issues concerning international tax dispute resolution that has been observed in many different places over the last years. Those issues are in particular:



Case Study I:

**Taxpayer rights are neglected or even ignored in international dispute procedures such as MAP.** It is widely accepted that every taxpayer has certain rights versus tax administrations even in a procedure like MAP, that is legally only conducted between states, but directly effects taxpayers. Typically

using a domestic safe harbor or secret comparables

set up the institutional framework, like designing internal and external guidance and developing model processes. It could well be that in an early phase of work on international tax law, a country would actually want to conduct MAP but is not able to do so because of capacity constraints.

**To be included: Box with country example of case rejection**

**Taxpayers are concerned about reliability and predictability of MAP.** In a recently published report of OECD/IMF<sup>5</sup> on tax certainty the importance of tax certainty and predictability for taxpayers has been pointed out. According to this report concerns over the inconsistent approaches of different tax authorities towards the application of international tax standards

resolution<sup>10</sup>. This standard foresees the obligatory publication of statistics<sup>11</sup>, and countries<sup>12</sup> of the Inclusive Framework (IF) are committed to implementing it.

**To be included: Figure with graph on stats**

### 3.2 Why developing countries have to be concerned with dispute resolution

**Developing countries are confronted with international tax cases, as in particular TP cases.** International transactions do not only occur between different entities of MNEs located in developed countries but also with entities located in developing countries. And there is no reason to believe that in so far there is less potential of conflict. Recent publicly discussed cases show that in particular transfer pricing cases are common not only in highly industrialized countries. With those cases comes the need to implement mechanisms to avoid double taxation to prevent obstacles to international trade and investment. It has to be noted that the lack of a domestic transfer pricing audit program does not hinder the appearance of those cases in international procedures

Box x:

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**Effective resolution of tax disputes is needed for guaranteeing tax certainty.** Tax certainty is essential for a good business climate, as explained above. Well-functioning processes increase investors trust in a jurisdiction and accordingly have positive effects on their openness to invest in a specific country. In so far, not only tax certainty according to the application of dispute resolution mechanisms such as MAP, has to be considered, but also more general certainty on the consistent application of material tax law.

**Domestic dispute resolution often does not help because it primarily does not aim at the avoidance of double taxation.** When double taxation occurs, domestic instruments of dispute resolution usually do not warrant satisfying solutions, since they mostly ignore the tax treatment in the other country. Also, domestic solutions usually cannot be enforced in the other involved country. Finally, domestic courts might be biased towards their own tax authorities, although currently no empirical evidence supports this view.

**BEPS final report on Action 14<sup>13</sup> formulates a new standard on MAP, that is legally binding for many countries.** The standard has three dimensions: (i) Treaty obligations related to the mutual agreement procedure should be fully implemented in good faith and MAP cases are resolved in timely manner; (ii) Administrative processes promoting the prevention and timely resolution of treaty related disputes should be ensured, and (iii) Taxpayers that meet the requirements of paragraph 1 Article 25 should be able to access the mutual agreement procedure. Binding tax treaty arbitration has been discussed during the process, but has not become part of the standard, although it is included in the OECD MC. The legally binding character of the standard is mainly achieved through the inclusive framework, where all members have to commit themselves to its implementation and agree to a peer review process.

**Developing countries have fewer cases, however, budgetary effects can still be significant.** Cases that are subject to international procedures can be large with significant amounts of tax at stake (maybe insert example of large case). Hence, the mere fact that a country has low case numbers should not automatically lead to the conclusion that international tax dispute resolution is not (urgently) needed. Additionally, indicators point towards increasing cases of tax

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<sup>13</sup> OECD/G20. 2015. Making Dispute Resolution More Effective. Final Report







## CASE II: The Fun Group

The Fun Group (FG) is a MNE in the entertainment business. The ultimate parent (FP) of the group is located in Northstan. FP decides to invest in Centralia. Therefore, it establishes a joint venture with an independent local enterprise with the purpose to build and maintain a casino and entertainment complex in a Centralian costal resort.

FG successfully developed projects like this for the last twenty years in many other regions of the world. Projects of this kind are either set up as wholly owned subsidiaries or, like in the case at hand, by way of joint ventures with local businesses, depending on regulatory requirements.

In order to allow the local joint venture to benefit most from the experience and technical know-how of FG an additional local support infrastructure is established by way of a local office of FP in Centralia. During the initial phase of the project technical and commercial advisors of FG are present in that office, thus constituting a permanent establishment of FP both under domestic and tax treaty law.

For the support delivered by the local office FP receives an annual fee of 100k, of which it attributes 1/3 to the local PE and 2/3 to the headquarters in Northstan. However, the local tax authorities do not (1)-4.6 (oc)-1.6 (

## **CASE III: The Oil Group**

The Oil Group (OG) is a multinational enterprise in the oil and gas sector. The ultimate parent (OP) of OG is located in Highland an OECD member country.

OG holds oil- and gasfields in all major oil- and gas producing regions. 2s (oduc) Pea(i)-2d3tuciate