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## **Committee of Experts on International Cooperation in Tax Matters**

New York, 23-26 April 2019  
Item 3 (g) of the provisional agenda  
**Dispute avoidance and resolution**

### **Preliminary Draft of the Chapter on Domestic Dispute Resolution Mechanisms**

#### **Note by the Subcommittee on Dispute Avoidance and Resolution**

*Summary*

This note is presented FOR DISCUSSION (and not for approval) at the eighteenth session of the Committee to be held in New York on 23-26 April 2019.

The note includes a preliminary draft of Chapter 3 (Domestic Dispute Resolution Mechanisms) of the proposed *United Nations Handbook on Dispute Avoidance and Resolution* on which the Subcommittee on Dispute Avoidance and Resolution is currently working. This draft was prepared on the basis of the discussion of a previous draft at the last meeting of the Subcommittee held in London on 13-15 March 2019.

At its eighteenth session on 23-26 April 2019, the Committee is first invited to confirm its agreement with t \_\_\_\_\_ concerning the scope of the Handbook and of Chapter 3. It is then invited to discuss the attached preliminary draft of Chapter 3, focusing primarily on the table of contents.

Based on the discussion of this note at the Committe \_\_\_\_\_ on subsequent written comments, the Subcommittee intends to revise and complete the draft Chapter at its meeting scheduled for 1- \_\_\_\_\_ it would be presented for discussion with a view to its approval for inclusion in the *UN Handbook on Dispute Avoidance and Resolution*.

1. Paragraphs 8 and 9 of note [E/C.18/2018/CRP.13](#), which was presented at the seventeenth session of the Committee (Geneva, 16-20 October 2018), described the next steps leading to the finalization of the proposed *United Nations Handbook on Dispute Avoidance and Resolution*.
2. In accordance with the timetable outlined in these paragraphs, the Subcommittee on Dispute Avoidance and Resolution, at its meeting of 13-15 March 2019, finalized the contents of Chapter 5 on Mutual Agreement Procedure (which is presented to the Committee for





# Chapter 3

## Domestic Dispute Resolution Mechanisms

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## **3.1 Introduction**

### ***3.1.1 Overview***

1. This chapter explores the mechanisms that are generally available to resolve disputes that can arise between tax administrations and taxpayers with respect to income taxes.<sup>1</sup> Whilst the primary function of the tax administration is to confirm that taxpayers are complying with the law and paying the correct amount of tax, tax administrations should recognize that disputes with taxpayers are inevitable. Therefore, it is of critical importance that mechanisms be available to resolve disputes in as efficient and timely manner as possible, and that these mechanisms be consistent with the legal framework of the country in which they are implemented.

2. These disputes can originate in a number of different ways, although they commonly arise from an enforcement action undertaken by the tax administration with which the affected taxpayer does not agree. While definitive statistics regarding the number of disputes between tax administrations and taxpayers are not available, the increased frequency of enforcement actions taken by tax administrations to, for example, examine or audit filed tax returns or impose collection measures likely also translate into an increase in the frequency of disputes with the impacted taxpayers.

3. The goal of this chapter is to provide practical guidance to countries that wish to improve certain aspects of their domestic dispute resolution mechanisms. These include both mechanisms that are created within, and thus as part of, the tax administration, as well as mechanisms that operate independently of the tax administration. Practice has shown that countries around the world have often chosen to adopt several different dispute resolution mechanisms instead of just relying on one. Countries should therefore determine which of the mechanisms described best suit their circumstances, the nature of the tax disputes that typically arise for their tax administration and their own legal framework.

### ***3.1.2 Disputes covered by this chapter***

4. This chapter deals with mechanisms for resolving disputes between that relate to taxes that have been assessed or reassessed. It therefore excludes, for instance, dispute resolution mechanisms, such as certain forms of mediation, that may be available in some countries to resolve disputes that may arise during the audit process, i.e. before the audit results in a reassessment or demand to pay tax. Some of these mechanisms are discussed in Chapter 2.

5. Also, this chapter does not deal with disputes concerning the exercise, by the tax administration, of its enforcement and collection powers including disputes concerning information exchanges and documentation requirements. These types of disputes do not relate

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1 Including corporate taxes.

to issues related to the determination of taxes payable and typically involve the application of dispute resolution mechanisms set up to oversee governmental actions.

### ***3.1.3 Importance of resolving disputes***

6. Tax administrations around the world have the power to verify that their taxpayers have complied with

of the tax paid and/or the return that is filed may conclude with a determination of an underpayment of tax, followed by the assessment and collection of the determined tax deficiency. The tax administration may also conclude that a taxpayer is not paying the taxes owed in a timely manner, and may assess interest and/or penalties and enforce collection actions. Given this relationship, it is inevitable that disagreements between the tax administration and taxpayers will arise.

7. It is of critical importance to the best interests of both the tax administration and taxpayers that disputes, when they arise, are addressed and resolved as quickly and efficiently as possible. Ensuring effective resolution of disputes will contribute to and enhance public confidence and the integrity of the tax administration in its role as collecting tax revenues for the government. In this regard, it is also important that tax administrations also provide avenues to air disputes with taxpayers regarding certain matters of a general nature, such as concerns by taxpayers over the adoption of new audit or collection policies or the issuance of new tax forms, as doing so will contribute to the public confidence of the tax administration.

8. From the point of view of the taxpayer, access to recourse to resolve disputes should be available to ensure the action giving rise to the dispute, such as an assessment of additional taxes owed, was accurately determined and does not result in an over calculation of the tax liability owed.

9. It is beneficial to both the tax administration and taxpayers to be able to resolve disputes as early, quickly and efficiently as possible. For example, the administrative mediation procedure described in section 3.4.3 below may sometimes be initiated by the taxpayer while its case before the tax administration is still in the examination stage, and thus potentially avoid a dispute before it formally arises. Moreover, procedures such as those providing for an independent review of statement of audit position (section 3.4.2), administrative appeals (section 3.4.1) and facilitation by a so-called tax ombudsman (section 3.5.3) can potentially avoid costly and protracted judicial procedures (described in section 3.5.1).

## **3.2 Overview of the main types of disputes and of domestic dispute resolution mechanisms covered by this chapter**

### ***3.2.1 Main types of disputes***

10. Disputes may arise where, after an audit or examination, the tax administration concludes that additional taxes should be payable and issues an assessment or reassessment or demand of payment of tax. Some examples of findings from an audit or examination that lead to disputes regarding the amount of tax liability include:





15. The third type of dispute resolution mechanism discussed (section 3.4.3) can be referred to as mediation. Mediators trained in dispute resolution techniques facilitate the dialogue between the relevant officials in the tax administration and the taxpayer with the aim of helping to resolve the dispute. Whereas under the procedures for administrative appeals and independent reviews of audit position the intervening parties provide their own analysis of the action or actions taken by the tax administration that led to the dispute, the role of mediation is merely to enhance the communication between the disputing parties. Through such facilitation, the mediators could help the parties reach an acceptable compromise.

16. The remaining dispute resolution procedures discussed in this chapter (section 3.5) involve parties independent of the tax administration. First, resolution of a tax dispute through the judicial system is allowed under the legal framework of most countries. The parties in

some bilateral income tax treaties. A more detailed description of arbitration is provided in Chapter 7.

### **3.3 Common issues for domestic dispute resolution mechanisms**

21. While the various domestic dispute resolution mechanisms described in this Chapter operate differently, a number of common issues present themselves with most of these alternatives. Countries should be aware of these issues when designing any mechanism to facilitate the resolution of disputes between the tax administration and a taxpayer.

#### **3.3.1 *Negotiated settlements***

22. Tax settlements are widely used by tax administrations around the world to solve tax disputes at the administrative or judicial level. They provide an effective and efficient mechanism to solve disputes between taxpayers and the tax authority without the need to resort to a judicial decision.

23. Taxpayers may usually settle their disputes with the tax authority through settlement agreements. Settlement agreements are not always available since some jurisdictions do not permit them as is the case of Peru; on the other hand, settlements are common in the U.S. where taxpayers and tax authorities find an effective and efficient



30. In some jurisdictions, with the agreement of the taxpayer, tax authorities may be able to extend the time period for assessment of additional tax. Such an extension may be requested during an examination

its review. In some countries, taxpayers may be able to request that an extension of the time period be limited to certain issues, meaning that the revenue authority may assess additional tax only with respect to those issues.

31. Taxpayers who seek a refund of already paid tax are also often limited to a specific time

### 3.3.4 Penalties and fines

35. To enhance voluntary compliance, countries with self-reporting tax systems often provide for penalties for non-compliance.

36. There are various types of penalties which may be asserted. Delinquency penalties may be asserted against taxpayers who either fail to pay a tax liability or file required tax forms. Accuracy-related penalties may be asserted where a taxpayer fails to report the correct amount of tax due and underpays the correct tax liability. Penalties may generally be based upon a willful or intentional disregard of the tax law. Penalties may also be asserted where the taxpayer has undertaken a transaction that is specifically designed to avoid tax and has no other business purpose.

37. A revenue authority may consider waiving or removing a penalty if the taxpayer can prove that it had cause for its failure to comply with the various obligations. For example, penalties may be inappropriate if circumstances leading to non-compliance were beyond the taxpayer's control. In such cases, a waiver may be granted upon the advice of the revenue authority, a tax professional, or legal precedent such as court decisions.<sup>4</sup>

Some jurisdictions may also impose penalties upon tax return preparers who are negligent or willfully disregard their own obligations to represent taxpayers with a high level of diligence.

39. <sup>5</sup> which is empowered





### **3.4 Mechanisms through which dispute resolution is provided by the tax administration**

47. This section describes a number of dispute resolution mechanisms that operate within and as part of the tax administration. These procedures are typically administered through an office within the administration that is separate and independent from the audit, exam and collection functions.

#### ***3.4.1 Administrative appeals procedure***

*[THIS SECTION SHOULD BETTER EXPLAIN THE CONCEPT OF “ADMINISTRATIVE APPEAL”, WHICH IS BASICALLY A REVIEW BY THE TAX ADMINISTRATION ITSELF. IN DOING SO, IT SHOULD EXPLAIN THE “OBJECTION” PROCESS USED BY SOME COUNTRIES AND EXPLAIN HOW IT IS AN ADMINISTRATIVE APPEAL REQUEST]*

48. The purpose of the administrative appeals procedure is to provide taxpayers that disagree with certain actions of the tax administration the ability to request a review of the action at the root of the dispute. The most crucial aspect of a successful administrative appeals program is that it operates independently from the exam, audit and collections functions of the administration.

49. If the taxpayer and examiner cannot agree on the proposed adjustment at the conclusion of the examination process, taxpayers are typically afforded the right to challenge the

While some

jurisdictions (e.g., Brazil and Angola) do not allow for an administrative review of the administrative review (and not litigation) is much less costly from both a financial and resource perspective, and it is generally more cost efficient for both the government and the taxpayer. Most jurisdictions do not require taxpayers to pay any potential tax due prior to filing an administrative appeal. Moreover, an administrative review function that can resolve disputes prior to litigation not only saves taxpayers and the revenue authority time and money, but it also alleviates the potential burden on the court system, which would otherwise experience a potentially unmanageable increase in the influx of tax cases. *[THIS SECTION SHOULD BETTER EXPLAIN THE PROS AND CONS OF AN INDEPENDENT ADMINISTRATIVE REVIEW OF TAX ASSESSMENT IN DEVELOPING COUNTRIES, INCLUDING RISKS OF ALLEGED CORRUPTION. IT SHOULD ALSO RECOMMEND THE PUBLICATION OF STATISTICS ON DECISIONS REACHED THROUGH THE ADMINISTRATIVE APPEAL PROCESS]*

50. The office function and seek to resolve tax disputes in a fair and impartial manner, with the goal of resolving cases without requiring the taxpayer to file a lawsuit. As such, the administrative review body should consider all facts present in the file and all relevant legal authorities when determining the appropriate resolution of a tax dispute.



Fiscal Code of Mexico. This new procedure is similar to the existing administrative appeal process, but focuses exclusively in solving the substance of the case with an emphasis on oral arguments instead of focusing on the formalities of the examination process. The appeal is only available when the tax liability at issue is at least (approximately) 310,000 USD.

#### *3.4.1.1 Function of the office in charge of administrative appeals*

52. While it resides as an office within the tax administration, it is critical that the office in charge of appeals operate separately and independently from the functions of the tax administration whose actions could lead to controversies with taxpayers, such as the exam, audit and collection functions. An administrative appeals review should be conducted in an objective, and impartial fashion.

53. In order to maintain the independence from the rest of the tax administration, the office in charge of appeals should be precluded from engaging in any prior communication with other offices, in particular the offices responsible for the exam, audit and collection functions. [*THIS PARAGRAPH SHOULD BE REVIEWED BECAUSE IN SOME COUNTRIES, THE OFFICE IN CHARGE OF APPEALS MAY BE ALLOWED TO CONSULT WITH THE TAX OFFICIALS WHO MADE THE DECISION GIVING RISE TO THE DISPUTE IN ORDER TO BETTER UNDERSTAND THE REASONS AND ANALYSIS UNDERLYING THE DECISION.*]

54. The function of the office in charge of appeals is to provide a *de novo* evaluation, at the request of the taxpayer, of an exam, audit or collection action taken by the tax administration with which the affected taxpayer disagrees, with a view to resolving the disagreement. In order to fulfil its objective, it is important that the office in charge of appeals have the ability to arrive at its own independent conclusions concerning  
deems appropriate, either uphold or reduce the taxes owed as a result of the original decision. For example, if after reviewing the results of an exam of a tax return that resulted in an assessment of additional tax of 100, the office in charge of appeals determines that the appropriate amount of additional tax that should have been assessed was only 80, the administration should be obligated to reduce the amount of the assessment accordingly, if the taxpayer accepts the revised amount. In doing so, if the taxpayer accepts the reduced amount, the dispute would be resolved.

55. The administrative appeals function is intended to be beneficial to taxpayers. Accordingly, it is customary that while the office in charge of appeals has the authority to either justify or reduce an initial decision against a taxpayer, it does not have the authority to increase the initial decision in favour of the administration.

56. The specifics of the administrative appeal process vary from one jurisdiction to another. Consistent differences arise between countries with legal systems that are based on common law and countries that are not based on such legal system. In the United States, for example, the administrative review officers are authorized to negotiate and conclude a final settlement

on behalf of the government during the administrative appeal process. In other countries like Peru the possibility of reaching a legal settlement at this stage does not even exist.

57. In countries where settlements are not available at the administrative appeal stage, the procedure is limited to the analysis of the appeal/rebuttal and evidence filed by both parties

### **3.4.2 *Independent review of statement of audit position***

61.

some similarities to an administrative appeal, but is significantly narrower in its scope and powers. The overall objective of the independent review procedure is to allow eligible taxpayers that have been the subject of an audit to request a review of the findings of the audit by an official of the tax administration that works independently and separately from the audit function. Whereas under the administrative appeals procedure, the office in charge of appeals is empowered to either uphold or reduce the decision against the taxpayer, the independent review described in this section attempts to facilitate the resolution of disputes by either providing greater clarity and explanation to the taxpayer of the positions taken by the administration in the audit, or by elevating the review of the matters at dispute to more senior officials who may be empowered to engage with the audit function to modify the initial positions that were taken in audit.

~~62.~~ Countries interested in establishing an independent review procedure in their tax administration should create a division that works independently and separately from the audit function. As is the case with the administrative appeals procedure, the independent and impartial operation of this function is critical to its success. Such a division would be dedicated to providing dispute resolution facilitation and should be staffed with officials with sufficient expertise in substantive tax matters that will allow them to fully perform a review of the audit position.

63. When the tax administration desires to provide dispute resolution recourses for its taxpayers, it must take into account its financial and human resources, which are often limited. As such, a new division dedicated to facilitating resolution of disputes by providing a service like an independent review may have a small number of employees. In such cases, the tax administration may need to limit the number and nature of cases that can be eligible for an independent review. For example, as an efficiency matter, it may be appropriate to provide access to the independent review procedure only for audits of large taxpayers, such as those with annual income in excess of an established amount. This would avoid having to devote scarce resources to resolve small-dollar disputes.

64. As mentioned above, the powers of the independent review function are somewhat more limited than that of the administrative review function. Whereas appeals officials have the authority to modify initial decisions, independent review officials do not have such authority. When the independent review officials are in agreement with the statement of audit position, their primary task will be to provide to the taxpayer greater clarity and explanations of the issues in dispute.

65. In contrast, when the independent review officials do not agree with the statement of audit position, instead of themselves modifying the audit findings, they will refer the matters in dispute to more senior officials, such as the senior a

review. Under an ideal independent review procedure, if these senior reviewing officials agree with the independent reviewer, recommendations will be made to the audit team to bring the audit in line with the independent review. *[THIS SECTION WILL NEED TO BE REVIEWED TO ENSURE THAT IT DEALS WITH A DISPUTE RESOLUTION MECHANISM APPLICABLE AFTER TAX HAS BEEN ASSESSED AS A RESULT OF AN AUDIT]*

### ***3.4.3 Administrative mediation***

66.

70. An administrative mediation program should be structured in such a way that it could be initiated early in the appeals process. Given the potential benefits that could be gained from mediation before a decision is taken by the tax administration, mediation could even be made available while the matters in dispute are in the pre-appeals stage, such as in exam, audit or collections (see Chapter 2). Moreover, it is critical that both parties to the dispute agree to submit to the administrative mediation and express their desire to seek a resolution to the dispute. The administrative mediation is typically conducted by convening the two parties with the mediators in a meeting that will be fac594.96 842.04 reW\*nBa 67(adep3( )-139(de)4(sir)-9(e)4( )-139(to )

74. The benefits of judicial resolution include securing a final tax liability, which cannot be re-examined by the tax authority or another court (except to the extent the jurisdiction provides for judicial appeals). In addition, judges and members of an independent tribunal may be perceived as more impartial and objective than representatives (administrative reviewers) from a tax authority. Further, cases decided in courts and tribunals are usually made public, thus providing other taxpayers with precedential value.

75. Taxpayers in most jurisdictions may raise challenges in different types of courts, such as courts (courts that hear business disputes), administrative courts or tribunals, or in special tax courts or tribunals where the case is heard and judged by specialized tax judges or experts.<sup>7</sup>

76. Some jurisdictions have pre-trial fact findings that may be formal or informal. Informal fact- stipulate to the facts in advance of a trial, which speeds up the litigation process and assists in settlement of many cases prior to trial. Formal discovery, on the other hand, may involve, for example, requests for documents from the opposing party and depositions of witnesses. The parties are not required to stipulate to any facts; instead, the facts are determined by the fact-finder either a judge or a jury.<sup>8</sup>

77. Other jurisdictions however, do not have pre-trial fact findings. The facts and legal arguments are presented by the parties (taxpayer and tax authority) to the court at the moment the lawsuit is filed along with the information and evidence they were able to obtain. Litigation procedures may be imminently oral or written, it varies from one jurisdiction to another.

78. In some jurisdictions, the taxpayer is required to pay the tax liability prior to bringing a challenge in a particular judicial venue. The requirement that the taxpayer pay or guarantee the tax liability will often preclude taxpayers from availing themselves of these judicial venues. [WILL BE DISCUSSED IN SECTION 3.3]

79. Almost all jurisdictions provide the parties (both the taxpayer and the revenue authority) with the right to appeal a decision of a lower court. Some appellate level courts will review only the legal argument (i.e., the courts will not act as fact-finder), while other courts will of fact.

80. In the U.S. taxpayers may bring suit in a specialized tax court, a federal district court (a court of general competency), or the federal Court of Claims (a specific forum to bring litigation against the government and its agencies). To bring a lawsuit in the latter two fora, taxpayers must first pay the tax, penalties, and interest that the revenue authority believes the taxpayer to owe and then file a formal claim for a refund of such tax with the revenue authority. If the revenue authority den

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<sup>7</sup> Specialized tax courts and tribunal are discussed in more detail in the next section.

<sup>8</sup>

may challenge that determination by bringing a suit for a refund of the tax paid in district court or the Court of Claims.<sup>9</sup> [*NEED TO REVIEW WHETHER TH*





*SECTION SHOULD CLARIFY THE DISTINCTION BETWEEN COURTS AND ADMINISTRATIVE TRIBUNALS]*

**3.5.3 “Tax Ombudsman”**

93. The dispute resolution mechanism described in this section shares certain similarities with the mediation procedure discussed in section (3.2.4) above, while at the same time it also addresses certain other matters of a more general nature, such as the safeguarding of taxpayer rights and ensuring that the adminis

provision of services to taxpayers generally, it will also be important that the ombudsman operate independently from those offices that establish generally applicable administrative practices, such as audit or collection policies, the promulgation of regulations and other guidance, and the drafting of forms.

98 Countries wishing to organize the tax ombudsman as a body independent of the tax administration will need to ensure that it will have the legal authority to access taxpayer-specific and other confidential information. This will be especially true if one of its intended functions will be as mediator to facilitate communications between the administrations and taxpayer to resolve disputes.

99. The variety of functions that could be performed by the tax ombudsman make it difficult to describe a singular format and suggested content for a request for assistance from the tax ombudsman. For example, the manner in which a taxpayer requests mediation assistance to facilitate communications with the tax administration would be different from the format that a taxpayer would follow to submit a service-related complaint. Furthermore, the tax ombudsman may wish to follow yet another format for filing concerns related to a general administrative practices, such as the establishment of a new collection policy or creation and drafting of a new tax form.

100. In order to provide the widest possible access to the services of the tax ombudsman, it is recommended that any admissibility analysis or criteria to pre-select requests for assistance not be overly restrictive or narrow.

### ***Box 1. Tax Ombudsman: the positive experience of Mexico***

The *Procuraduría de la Defensa del Contribuyente* (PRODECON) was established in Mexico in 2011 as an agency independent of the tax administration that carries out the functions of a tax

it to address both taxpayer-specific matters as well as issues of general concern relating to the operation of the tax administration.

submit service-related complaints regarding actions taken by the tax administration. These

may request, through the conclusive agreements procedure, mediation assistance from PRODECON to facilitate communications in their dealing with the tax administration. Yet another taxpayer-specific service provided by PRODECON is the legal representation of certain taxpayers to assist them in their dealings with the tax administration.

#### ***PRODECON's complaint procedure***

of the complaint in the form of a report.

the complaint has merit, PRODECON will issue non-binding recommendations for modifying the position of the tax administration with a view to resolving the dispute. If the officer declines to follow the recommendations, PRODECON will make the recommendations publicly available.

Mexican taxpayers. According to data provided by PRODECON, one hundred and thirty thousand requests for assistance have been submitted under the complaint procedure through 2017.

***PRODECON's conclusive agreement procedure***

The conclusive agreement procedure, established in 2014, was the first alternative dispute resolution mechanism for tax controversies in Mexico. Taxpayers under audit who do not agree with the position and findings of the tax authority have the right to appear before PRODECON to request its intervention as a mediator. The procedure provides a transparent and amicable forum for the taxpayer and the tax authority, with an impartial third party observer, to discuss

objective of achieving consensus to solve the dispute.

According to data provided by PRODECON, more than 8,500 mediation requests have been processed by PRODECON, which facilitated resolution of the majority of the disputes involved. PRODECON reports that over one billion dollars of tax revenue was collected through the conclusive agreements. The procedure allows for the resolution of disputes without judicial recourses, thus saving litigation costs for both taxpayers and the government.

The conclusive agreement procedure acts as an alternative, and not a complement, to the administrative appeals process of the tax administration. Under the conclusive agreement

the administration and the taxpayer but also to resolve the dispute by facilitating the negotiation of a mutually agreeable settlement through the exchange of proposals between the disputing parties.

The conclusive agreement procedure is only available while a case is in audit or examination. Initiating the procedure suspends relevant domestic time limits, as well the audit and any collection procedures.

Although the aim of the conclusive agreement is to reach an agreement that resolves the entirety of tax controversy, partial resolutions are also permitted. In the case of a partial resolution, the

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