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Opinion Statement FC 4/2017

**on the proposed Directive on Double Taxation Dispute
Resolution Mechanisms in the European Union**

Prepared by the CFE Fiscal Committee

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The CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Our members are 27 professional organisations from 21 European countries with more than 200,000 individual members. Our functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe.

The CFE is registered in the EU Transparency Register (no. 3543183647-05).

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1. Introduction

The CFE welcomes the Commission's proposals to expand and improve the mechanisms available to Member States to resolve double taxation disputes with the introduction of a Council Directive¹ (the "Proposed Directive").

The CFE has also commented on this matter in the context of the OECD BEPS consultation process, in January 2015 and April 2016² and in response to the 2016 EU Commission Public Consultation entitled "*Consultation on Improving Double Taxation Dispute Resolution Mechanisms*". This Opinion Statement complements these previous opinion statements.

2. Background

Double taxation impedes businesses operating cross-border and consequently hampers the development of the single market. Easily accessible, efficient and effective dispute resolution mechanisms are a crucial element to any corporate tax reforms for a fairer and more effective system of taxation within the internal market. Fair and efficient taxation requires not only that business pay a fair share of tax where it arises but also conversely, that business is not subject to double taxation or other tax obstacles to operating their business cross-border.

The experience of CFE members concurs with the findings set out in the preamble to the Proposed Directive that the main problems with the EU Arbitration Convention³ arise from the ability of taxpayers to invoke and rely on the procedures and the length and the effective conclusion of the procedure. In addition, the lack of transparency results in increased uncertainty. Tax certainty is essential for a fair and robust internal market. Therefore, CFE encourages and welcomes any measures that expand the nature of disputes subject to the mechanism, empower taxpayers' involvement within the process, and are result orientated with a focus on mandatory resolution of the disputes within a fixed time-frame.

CFE encourages the swift implementation of the Proposed Directive on the basis that action is urgently required; there is already an unacceptable number of outstanding cases (worth an estimated EUR 10.5 million)⁴ and as set out in the preamble to the Proposed Directive increased and more comprehensive audits by tax authorities are leading to an increase in cases. In this context CFE welcomes the agreement reached at ECOFIN on 23 May 2017 on a final text for the Proposed Directive.

3. Existing mechanisms

¹ Proposal for a Council Directive on Double Taxation Dispute Resolution Mechanisms in the European Union.

² CFE and AOTCA Opinion Statements FC 3/2015 and FC 4/2016, January 2015 and April 2016, available on the CFE website: <http://www.cfe-eutax.org/node/5352>

³ Convention of the elimination of double taxation in connection with the adjustments of profits and associated enterprises (90/436/EEC).

⁴ Figure from European Commission Press Release, Strasbourg 25 October 2016.

3.1 National legal remedies

National legal remedies are generally not very effective when dealing with double taxation disputes on the basis that national courts do not have jurisdiction to rule on the levying or reduction of taxes in another jurisdiction. Therefore, whilst a taxpayer may have the ability to challenge the imposition of a tax under domestic tax legislation or in relation to the provisions of a bilateral or supranational tax treaty, the inability to bind the other jurisdictions in cases of double taxation results in the taxpayer not getting an effective remedy before the national courts. In addition, it is common practice that domestic law prohibits tax authorities from deviating from the decisions of national courts. Therefore, any contrary decision arrived under another mechanism is rendered ineffective in practice.

Given the shortcomings of wholly domestic remedies, other mechanisms have developed to provide redress to taxpayers subject to cross-border double taxation.

3.2 Mutual Agreement Procedure

The primary avenue of recourse is to invoke the Mutual Agreement Procedure contained in bilateral double tax treaties. The wording generally derives from Article 25 of the OECD Model Tax Convention. The countries involved appoint competent authorities to manage the MAP procedure, generally speaking the tax authority assumes the role of the competent authority.

A request to institute a Mutual Agreement Procedure must be submitted within three years of the initial notification of the impugned tax liability. The competent authority can declare the request to be valid, invalid or refuse to accept the request. In many Member States the taxpayer has no legal remedy to contest this decision.

MAP entails the tax authorities negotiating an agreement to cancel the double taxation; the taxpayer is not a party to the proceedings. During the course of the MAP the taxpayer provides all information requested by the tax authorities. In many instances the countries are only required to “endeavour to resolve” the dispute, so in many cases no agreement is reached and the double taxation remains outstanding. This is alleviated in a limited number of tax treaties by a provision for mandatory binding arbitration at the request of the taxpayer if agreement has not been reached within 2 years of the presentation of the case (inserted into the OECD Model Tax Treaty on 2008).

3.3 EU Arbitration Convention

Within the EU, an additional avenue of recourse exists in the form of the EU Arbitration Convention (the “Convention”). The Convention provides a mechanism for the elimination of double taxation, but only in relation to an adjustment of profits between associated enterprises. The Convention contains a provision for mandatory binding arbitration, but only in relation to transfer pricing related disputes, which satisfy three preconditions. The Convention is complemented by the Revised EU Code of Conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, which offers guidance and clarifications on the practical application of the Convention.

The Convention necessitates that Member States appoint competent authorities to take session of this arbitration function. Under the rules of the convention, an arbitration procedure may apply if there are double taxation issues where the following conditions are satisfied:

- The parties are “connected parties”;
- The financial relationship is one which would only apply to connected parties and not to unconnected parties; and
- The profits are or could be subject to tax in two (or more) Member States.

The taxpayer has three years from the date of the impugned notification to invoke the procedure. If the authorities fail to reach agreement within 2 years mandatory binding arbitration is invoked. An advisory commission is set up with both tax authorities represented; a decision is reached within 6 months. OECD transfer pricing guidance and terminology can be relied upon under the procedure.

4. Shortcomings of existing procedures.

Whilst these aforementioned existing procedures assist taxpayers in mitigating and redressing the effects of double taxation to a certain extent, they are no longer sufficient to deal with the complexity and risks associated with the current global tax environment.

Although in theory, the Member States should seek to achieve a satisfactory outcome for the taxpayer, in reality a conflict of interest can arise for the Member States in the negotiating process. Under the present system, negotiations do not take place on a legal level but more on a political level in the sense that they take place between the tax authorities. The taxpayer is not a party to these negotiations between the tax authorities. From a purely procedural perspective this is not ideal as the taxpayer is the party with the most accurate information on pricing policy and decisions taken and not the tax authority. Equally, from a fair procedures perspective it means their interests cannot be central to those proceedings, if they are not a party to them.

Consequently, problems arise in relation to legal certainty and the effectiveness of the process, particularly for the taxpayer. The MAP often costs a great deal of time and money and the outcome of the procedure is extremely uncertain for the taxpayer. CFE members have found that in practice taxpayers reach agreement to settle the dispute with the tax authority rather than embarking on an uncertain, costly and timely MAP procedure. From the taxpayer’s perspective, the aim of the procedure is not solely to resolve the double taxation but also to clarify the nature and extent of the taxing rights of the different jurisdictions, for example, the applicable rate and applicable legislation. In particular, problems arise in cases where there is no mandatory and binding arbitration; where there is no stipulated period in which the competent authorities must reach mutual agreement the taxpayer is subject to increased uncertainty about their tax position for a long and undefined period of time, which is an undesirable outcome for any taxpayer. Conversely, the experience of our members is that the threat of arbitration acts as an impetus for the tax administrations to reach an agreement in terms of the Convention.

5. Comments on the new procedures under Proposed Directive

The Proposed Directive will build upon and expand the existing mechanisms provided under the EU Arbitration Convention broadening the scope, streamlining the process and addressing some of the salient shortcomings. Consequently, CFE considers the Proposed Directive a positive development.

In particular, CFE welcomes the following salient improvements:

5.1 Extension of the scope

A crucial element of the Proposed Directive, which the CFE endorses, is the extension of the scope of relevant disputes beyond just transfer pricing to include all taxpayers that are subject to taxes on income and capital under bilateral tax treaties and the Convention⁵.

5.2 Increased effectiveness & efficiency in the process

In order to increase effectiveness the Proposed Directive introduces a stipulation for the mandatory resolution of disputes subject to strict and enforceable timelines, this is a positive development for taxpayers and for tax certainty generally.

5.3 Taxpayers' role and rights

The Proposed Directive seeks to empower the taxpayer and strengthen their role in the process. Taxpayers have always had the right to institute proceedings. However, the Proposed Directive seeks to empower the taxpayer during the process, for example, by notifying them of the terms of reference of the dispute, the proposed timeframe for completion and the terms of conditions of taxpayers' or a third parties involvement. CFE welcomes these proposals and believes such measures will increase tax certainty and reduce administrative burden for taxpayers. CFE believes that the proposal allowing the taxpayer recourse to the national courts to ensure compliance in the event that the appropriate mechanisms are not applied is essential to a successful system of dispute resolution.

In addition, the incorporation of an independent advisory council to make assessments at different stages, for example, if a taxpayer's complaint is rejected, or in the event that the two Member States fail to reach agreement to eliminate double taxation pursuant to the MAP procedure will be an invaluable development from the perspective of ensuring taxpayers' right are protected.

5.4 Alternative dispute resolution mechanisms

One of the salient improvements under the Proposed Directive is the inclusion of an additional layer of protection in the form of an automatic and mandatory arbitration procedure to be completed within fifteen months in the event that the Member States fail to reach a conclusion to the initial MAP phase.

CFE welcomes the proposal to have an option between an Advisory Commission and an Alternative Dispute Resolution Commission. In particular, CFE believes the broader and more flexible approach to the form of alternative resolution procedure, which can be applied, will greatly improve the process for both the competent authorities and the taxpayer.

5.5 Tax Certainty

The Proposed Directive is essential to improving tax certainty within the EU. The recently published European Commission paper on tax uncertainty states, "*Dispute prevention and early issue resolution*

⁵ Pursuant to the final compromise, reached on 23 May 2017 it was agreed that on a case-by-case basis of excluding disputes that not involve double taxation.

*programs, as well as effective dispute resolution procedures, are considered of particular relevance to enhance tax certainty in the international context.”*⁶

The Proposed Directive specifies that in reaching an opinion the Advisory Commission or Alternative Dispute Resolution Commission must take into account the applicable national rules, and the terms of the relevant double tax treaty, or in the absence of a treaty the terms of the OECD Model Tax Treaty; this is a positive development in terms of improving tax certainty. In addition, the publication of decisions is a positive development; the draft report prepared for the Parliament goes a step further and proposes that the Commission develop a centrally managed webpage containing final decisions for the benefit of all taxpayers. CFE believes this would be a positive initiative.⁷

6. Points to note about the Proposals

6.1 Parallel procedures

Consideration should be given to the practical implications for taxpayers and tax authorities of two parallel arbitration procedures being available to the taxpayer to invoke. At present there are two procedures available to taxpayers *vis a a viz* the MAP procedure under double tax treaties and in addition, the Convention can be invoked in cases of transfer pricing related disputes. Many Member States will become signatories to the MLI in June 2017 and are likely to adopt the arbitration provisions. The proposed Directive does not address parallel MAP proceedings, but – in Art 15(5) – proceedings under the Directive and other arbitration or dispute resolution proceedings by stating that “[t]he submission of the case to the dispute resolution procedure according to Article 6 [i.e., dispute resolution by Advisory Commission] shall put an end to any other ongoing mutual agreement procedure or dispute resolution procedure on the same dispute in case the same Member States are concerned, with effect on the date of appointment of the Advisory Commission or Alternative Dispute Resolution Commission”. Hence, the procedure under the Directive is supposed to take precedence, so that there should not arise cases with two alternative final and binding decisions.

6.2 Form of decision given by the Advisory Commission or Alternative Dispute Resolution Commission (the “Commissions”)

Under the Proposed Directive, the Commissions reach conclusions and issue an Opinion. This can be contrasted with the position under the MLI whereby the competent authorities present their respective proposal to the Arbitration panel and the panel choose one solution (“base-ball arbitration”). CFE welcomes the adoption, in the proposed Directive of the conventional arbitration. Whilst we acknowledge the speed and alleged reduced costs of the procedure, we do not think baseball arbitration is an appropriate tool to deal with complex cases, such as those on transfer pricing issues⁸.

6.3 Role of the European Court of Justice

At present, the Convention is a multi-lateral instrument that is not within the jurisdiction of the ECJ. The Proposed Directive will be a directive; therefore, implementation by Member States into domestic law will be subject to the jurisdiction of the ECJ. In addition, depending on the wording of the final

⁶ European Commission Taxation paper 67-2017 ‘*Tax Uncertainty: Economic Evidence & Policy Responses*’

⁷ Draft Report ‘*Proposal for a Council Directive on Double Taxation Dispute Resolution Mechanisms in the European Union*’ (COM(2016)0686 – C8-0035/2017 – 2016/0338(CNS)) Prepared by the Committee on Economic and Monetary Affairs (Rapporteur: Michael Theurer)

⁸ See CFE/AOTCA Joint [Opinion Statement FC 3/2015](#) on making dispute mechanisms more effective. Submitted to the OECD in January 2015.

Directive the ECJ may have competence over the disputes themselves. Whilst this is a positive development for uniformity and tax certainty, given the large volume of cases that may be referred there may be capacity issues for the ECJ dealing with the disputes in a timely manner. The capacity of the ECJ will be further stretched if it is the case that the proposed directive for a common consolidated corporate tax base becomes law. A backlog of cases in the ECJ will frustrate the intentions of the Proposed Directive if the ECJ cannot deal with the referrals in a timely manner.

6.4 Incentives for tax authorities to engage

Whilst, in many cases the tax will already have been paid in the first State prior to dispute procedure being invoked, it has been suggested that it may be worth considering using the payment of the tax as a leverage to encourage speedy resolution of disputes between tax authorities. For example, the use of blocked accounts whereby the tax would become lodged in a blocked account, which would only become unblocked once there has been a satisfactory resolution of the dispute. The sum should be limited to the highest amount of tax, which may become due in order to avoid double taxation.

