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Research on the Connection Between Mutual Agreement Procedure and Domestic Settlement of International Tax Disputes in China

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Abstract: As the main international settlement to the international tax disputes, the Mutual Agreement Procedure (MAP) coincides with the domestic remedies in China, such as tax administrative review and tax administrative litigation. It is necessary for the law to clarify the order and relationship of those procedure application. Based on China's Tax Collection and Administration Law and other documents, the four possibilities of the connection between MAP and domestic solutions are classified and discussed, showing that the connection is not smooth. Since the root of the problem lies in the lack of law, we can draw on the experience of legislation and tax practice in Canada and other developed countries. It is clear that MAP and domestic settlement cannot be carried out simultaneously. The MAP can be set up as an institutional arrangement at the same level as the administrative review but with priority to be applied. MAP should be regarded as a pre-requirement for the completion of the review in order to initiate the administrative proceedings. We should protect the taxpayers' right to start MAP in the whole process of administrative litigation, as well as firmly maintain the finality and authority of administrative litigation judgment.

Keywords: Mutual Agreement Procedure (MAP); Administrative Review; Administrative Litigation

1. Overview of international tax dispute resolution methods

1.1 Mutual Agreement Procedure still dominates the three common international tax dispute solutions

The traditional way to settle international tax disputes is to use the Mutual Agreement Procedure (MAP) on the basis of domestic law. However, due to the procedural defects and the distorted consequences of international double taxation, the arbitration procedure has gradually entered the field of vision of domestic scholars.[1] Since 2008, Organization for Economic Co-operation and Development (OECD) has proposed to introduce an arbitration mechanism in the settlement of international tax disputes. Arbitration has been developed from component and extension assistance of MAP to a subsidiary procedure, and has the trend of parallel to MAP in the future. [2] At last, the judicial settlement of international tax disputes is summed up as a third common way of settlement.

For the first two methods, on the one hand, arbitration has obvious advantages in transparency, time limit, efficiency, etc.[3], and also facilitates substantial taxpayer participation in the proceedings.[2] On the other hand, the use of adversarial compulsory arbitration for the settlement of disputes may run counter to the concept of mutual respect, mutual benefit and win-win outcomes.[4] Compared with methods such as litigation and arbitration, negotiation has the least influence on state sovereignty and is the most acceptable way to solve international tax disputes.[5] OECD has been working to improve the

MAP, and the BEPS Action Plan 14 sets new rules to improve the effectiveness and efficiency of the MAP.[6]

Therefore, the dominant position of MAP in international tax dispute settlement is irreplaceable. MAP must be the basic way of solving international tax disputes which is favored by developing countries for a long time.[7] In recent years, our country has used the MAP mechanism under the tax agreement to carry out more than 200 cases of bilateral tax consultation. It shows the positive attitude of using MAP to solve the tax disputes and protect the rights and interests of taxpayers in China.[8]

1.2 There is concurrence between MAP and domestic solution in China

The application of domestic law by tax authorities and the priority of tax agreements vary from country to country.[9] China adopts the principle of priority of tax treaty, that is, "If a person considers that the measures of one or both states parties result in or will result in the imposition of taxes on him or her that are inconsistent with the provisions of this agreement, he or she may disregard the remedies available under the domestic law of each state party, submit the case to the competent authorities of the state party of which the person is a resident."[8] Then, when the tax dispute is submitted to the competent tax authority, the procedural choice between MAP and domestic legal remedies would then be competing. Either on the basis of national tax sovereignty or on the basis of treaty primacy, it reflects the legal basis and value orientation behind the national tax legislative power and jurisdiction.[10] And it also reveals the importance of the connection between MAP and our domestic settlement.

There are difficulties in the connection between domestic solutions and MAP, which makes it hard for enterprises to get timely and effective support from domestic tax authorities when facing tax disputes.[9] Therefore, in order to better apply MAP to resolve international tax disputes, our country should coordinate the relationship between MAP and domestic settlement, and encourage enterprises to seek appropriate relief when MAP is rejected.[11]

2. The status quo of the connection between MAP and domestic settlement

MAP is subject to the international tax agreement signed by the contracting parties, and all the tax agreement signed by China has stipulates the provisions of MAP. The Interim Measures for Chinese residents (nationals) to apply for the commencement of the procedures for mutual tax consultation and Measures for the implementation of procedures for mutual consultation of tax agreements are the main documents guiding the development of MAP in China.[6] These documents will enable enterprises to submit to the State Administration of Taxation their applications for MAP activation.

When a tax issue involves both international and domestic tax disputes, there are problems with the applicability of MAP and domestic settlement. What is the relationship between these two methods? Can they be started at the same time, or is there a sequence? Or does the taxpayer need to exhaust domestic remedies to initiate the MAP? At present, the MAP clause in the tax agreement signed by our country all stipulate that the taxpayers do not need to exhaust the domestic remedies when applying for the MAP, that is, MAP and domestic settlement have a parallel institutional relationship, regardless of sequence.[11]

However, in practice, MAP and domestic settlement in the priority of program selection and the rules for handling conflicts of entity results need to be clarified.[12] Documents such as the Tax Collection and Administration Law provide neither for the relationship between the MAP and domestic settlement, nor for the suspension of relevant tax decisions during the course of the MAP process, which may make the hard-won agreements through MAP difficult to reconcile with domestic settlement, leading taxpayers to question the effectiveness of the MAP.

2.1 The connection between MAP and administrative review

Neither the Administrative Review Law, the Implementing Regulations of the Administrative Review Law, nor Rules for Administrative Review of Taxation contain any provisions on the connection between the administrative review and the MAP. The Measures for the Regulation of Special Tax Investigations and Mutual Consultation Procedures issued by the state administration of taxation also did not explain the relationship between the different means of dispute resolution. Therefore,

from the existing system, the connection between MAP and administrative review can be divided into four cases.

First of all, applying for administrative review in cases where the MAP has been initiated but no conclusion has been reached, will cause the original administrative action to be changed or cancelled, which is inconsistent with the agreement to be reached by the MAP. Secondly, an application for administrative review of the MAP conclusions would result in an administrative act agreed between the governments of the two countries once again being subject to unilateral review by a state's administrative review process. Thirdly, the MAP application for administrative review cases that have not yet been closed. According to the OECD Multilateral Convention, the tax authorities in China cannot refuse the application of taxpayers to start MAP on the grounds of maintaining the authority and certainty of administrative review. The simultaneous conduct of the two procedures may result in a chaotic situation with divergent conclusions. At the same time, if the authority terminate the administrative review, there will also be the same embarrassment of the second situation after a long wait for the conclusion of the MAP. Fourthly, it is feasible to file a MAP application against the administrative review decision, which is in line with the provisions of the OECD Multilateral Convention. [13]

2.2 The connection between MAP and administrative litigation

There is no special tax court in our country. Tax cases are heard by the People's Court Administrative Tribunal in accordance with the Administrative Procedure Law and the relevant judicial interpretations. The connection between MAP and administrative proceedings can also be discussed in four situations.

First, it is theoretically possible to proceed simultaneously with an administrative action against MAP without a conclusion. But there is a risk that the conclusions of the two proceedings may differ. Second, because of the existence of the pre-administrative review, we go back to the second situation of the connection between MAP and administrative review. Third, to start the MAP for the application of the administrative litigation in the process of trial, we will still face the embarrassment of the different conclusions of the two procedures. Fourthly, the application to start the MAP after the administrative decision is made, which can not be used because of the finality of the judicial decision in our country, which violates the basic rules of dispute settlement in our country.[13]

3. Foreign practice of connect MAP to domestic settlement of international tax disputes

In order to avoid the conflict of procedure and the difficulty of implementing the agreement, many countries require the implementation of the MAP resolution on the premise that taxpayers accept the MAP resolution and withdraw the legal proceedings that have been resolved in the MAP resolution.

Canada is a representative country that uses the MAP process to efficiently resolve transfer pricing adjustment cases. Over the past decade, Canadian authorities have used the MAP process to resolve hundreds of such cases, and provides effective relief for taxpayers to avoid double taxation.[14] As a former French colony, she inherited the civil law system, and as a British colony, she inherited the common law system. Canada and the neighboring United States have been using the MAP program to negotiate tax cases for years. So Canada is the embodiment of multi-culture in the legal system.

Taking France as an example, on the one hand, the international settlement of tax disputes in France mainly relies on the MAP. On the other hand, France has established the administrative court, which forms the domestic solution through the system of tax administrative reconsideration, litigation and tax arbitration.[9] Tax Agreements in France automatically acquire the force of domestic law without conversion or specific procedures, creating a practice whereby international tax disputes generally give priority to tax agreements concluded with the country concerned.[15] Similar to France, in Canada's two main systems of federal and provincial courts, the Federal High Court level has a special tax court, with special jurisdiction over tax and related matters. The legal rights of taxpayers are protected through the tax appeal system. But Canada does not adopt the French practice of allowing MAP to be conducted in parallel with domestic litigation.[16]

Common law countries generally require that international tax agreements be transformed into domestic law before they

can be applied, but there are great differences among countries in dealing with international tax disputes. In the United Kingdom, tax treaty cannot obtain the legal effect directly on the domestic law of the United Kingdom, but must be explicitly transformed into the domestic law by special legislation. So the procedure is more complicated and time-consuming. They use judicial review and appeal to resolve tax disputes, with a two-tier tax administration tribunal and an Independent Tax Appeals Tribunal to handle tax disputes. In the United States, according to the written Internal Revenue Code of the United States, a taxpayer may submit a tax dispute to the Administrative Review Department of the Federal Revenue Service for administrative review. In the event that they are not satisfied with the outcome of the review or wish to skip the review process to sue directly, the federal appeals court and the Federal District Court can also be courts of first instance in tax cases.[9] If the case has already entered the domestic judicial remedies in the United States, the tax authorities will not accept the application for the activation of the MAP; otherwise, if the case has entered the MAP, the proceedings will be suspended until the end of the MAP.[10]

Drawing on the experience of the United States, the Canadian tax authorities, in order to avoid duplication of effort, provide that taxpayers who wish to continue domestic appeal proceedings cannot simultaneously seek application of the MAP with foreign authorities. Canada Guidance on Competent Authority Assistance under Canada's Tax Conventions 2005 states that a taxpayer may apply to set aside a notice of objection to pay tax and apply the MAP as a matter of priority to resolve the problem. If the taxpayer chooses to continue the objection notice or litigation in the course of the MAP process, the MAP will automatically terminate. If the above four-situation classification of procedural convergence is applied, then the connection of the MAP with Canadian domestic settlement is shown as follows.

First, the MAP is automatically terminated if a suit is filed while the MAP is in progress but has not reached a conclusion. Second, the case of taxpayers seeking domestic settlement against the MAP conclusion cannot be applied in Canada, as the approval of an application to start the MAP process has already been reviewed by the authorities. Taxpayers do not have the right to initiate repeated review or administrative proceedings against the decisions of the competent authorities. Third, taxpayers apply to start the MAP process in the course of litigation, then go directly into the MAP process. Fourth, when a taxpayer applies for the commencement of the MAP against a court decision, the Canadian authorities will submit the details and reasons of the court decision to the other country in the MAP, but the decision itself will not be changed.[14]

4. Better design of the connection between MAP and domestic settlement of international tax disputes in China

The connection between the MAP and the domestic settlement has some deficiencies in both the theoretical research and the legal system in China.[12] The experience of legislation and tax practice in Canada and other developed countries will help our country to perfect the system of international tax dispute settlement.

The connection between those procedures belongs to the category of procedural law, so China can take the opportunity of amending the law of *Tax Collection and Administration Law* to add some provisions to clarify this problem. First of all, it should be made clear that the MAP and domestic settlement cannot be carried out simultaneously, that is, MAP and the domestic settlement must be arranged sequentially in time. Administrative review and administrative litigation are not appropriate for disputes that are still pending in the MAP, in order to avoid the inconsistency between the conclusions of the procedures. Secondly, instead of settling the case unilaterally, MAP provides a comprehensive bilateral settlement mode for the tax-related disputes. Therefore, the application of MAP can be considered to set a certain priority.[11] (see Table 1)

Table 1 Better design of the connection between MAP and administrative review and administrative litigation

the connection between MAP and administrative review		the connection between MAP and administrative litigation	
MAP in progress → Application for administrative review	×Refuse the application for administrative review	MAP in Progress →Application for administrative litigation	× Cannot be done at the same time, must wait for MAP conclusion.
MAP conclusion →Application for administrative review	×Refuse the application for administrative review	MAP conclusion → Bring an administrative action	√Use the idea of "No additional punishment on appeal" to the action
Administrative review in progress →Application for MAP	√ApplyMAP in preference andterminate administrative review	Administrative proceedings →Application for MAP	√In line with the OECD convention, but only for notice in MAP The decision of the administrative proceeding will not be changed
Administrative review decision →Application for MAP	√In line with the OECD convention.	Administrative judgment →Application for MAP	

The MAP can be set up as an institutional arrangement at the same level as the administrative review but with priority to be applied. Taxpayers who meet the application criteria can choose between the MAP and administrative review. Taxpayers can not apply for a domestic administrative review of the same dispute if the tax dispute is already in the course of the MAP or if a MAP agreement has been formed. This is similar to Canada's practice of limiting domestic remedies for MAP results. If the administrative review is pending and the taxpayer files a MAP application, the administrative review can be terminated and the MAP can be applied preferentially. Taxpayers can also apply to start the MAP process for administrative review decisions, meeting the demand of "not considering domestic remedies" of the special provisions in OECD Multilateral Convention.[13] The general tax cases set up the pre-administrative review rules before the administrative litigation. When we accept that MAP is at the same level as administrative review, and we regard MAP as the pre-procedure of starting litigation, then the connection between MAP and administrative litigation will be more reasonable and efficient.

In connection between MAP and administrative litigation, enterprises may choose to reject the agreement if they are dissatisfied with the increase of their own burden or the impairment of their rights caused by the MAP agreement. We can draw lessons from the idea of "No additional punishment on appeal", and guarantee the rights and interests of the applicant to seek domestic settlement on the basis of not increasing the extra tax burden of the applicant. This mode can also increase taxpayers' incentive to choose the MAP to resolve disputes.[12] In Canada, after the taxpayers apply to start the MAP against the court decision, authority only explains and notifies the other country, and does not change the court decision. This way of highlighting the finality of litigation is consistent with our concept of litigation in China. So we can also make similar provisions to guarantee the right to start the MAP under the premise of maintaining the finality and authority of domestic litigation.

Therefore, in order to coordinate the application of MAP with domestic legal settlement measures, the dispute resolution part of Tax Collection and Administration Law and Tax Administrative Review Rules in China should be adjusted. Incorporate the MAP content into the existing domestic tax dispute resolution methods, establish the same level and preferential application mechanism of MAP with administrative review as the core content, allow taxpayers who are not satisfied with the MAP conclusion to file a final administrative action, and reserve their right to initiate the MAP who want to directly file an administrative action against the dispute.

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