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A MAP and Guide to Resolving International Tax Disputes

By John L. Harrington[*]

I. INTRODUCTION

International commerce has always had its share of dangers. Valuable goods were lost in shipwrecks or taken by bandits, people were seized by pirates or princes, and tolls and taxes were paid all along the way. There have been noticeable improvements over time (e.g., fewer shipwrecks), but generally old risks have just been replaced by new risks. Granted, there is less physical danger, but why rob tangible goods when the theft of intellectual property may be easier and more profitable? And identity theft and cyber theft can be more rewarding, and more likely to go unpunished, than traditional captive-taking.

At least the constant risk of taxation (and the related thrill of sneaking past tax collectors) has continued throughout the years. Still, there is a lot more cross-border commerce these days, and that means more instances of taxation and more individuals and companies potentially exposed to it. This article provides some guidance as to how taxpayers should approach cross-border tax disputes and the options and choices they face in resolving such disputes.

A. Role and Nature of Tax Treaties

A taxpayer's ability to resolve a cross-border tax dispute frequently turns on whether the taxpayer can access an income tax treaty between the taxpayer's home country and the jurisdiction(s) with which the dispute arises. Unless a tax treaty or similar instrument obliges a reluctant tax authority (or permits a sympathetic tax authority) to depart from enforcing its domestic tax rules against the taxpayer, the taxpayer has limited ability to prevent a proposed assessment or charge by that tax authority. Of course, the mere existence of a tax treaty between the relevant jurisdictions is not enough: the relief available to the taxpayer will depend on the specific provisions of the treaty and whether the taxpayer is eligible for the benefits of the treaty. Finally, eligibility for treaty benefits is typically necessary but not sufficient grounds for resolution. Even if there are clear grounds for relief under the treaty, that relief is rarely automatic unless the affected tax authorities are of like mind.

An explanation of the benefits that income tax treaties provide, and their role in preventing or resolving disputes, is far beyond the scope of this article. Very generally, though, in a typical bilateral income tax treaty each jurisdiction agrees to limit its taxation rights in exchange for its treaty partner agreeing to limit its taxation rights. These mutual concessions usually mean that the ''source'' jurisdiction, or jurisdiction where the taxpayer is not resident, limits its taxation of nonresident individuals or companies and reduces or eliminates withholding tax on payments made by its residents to nonresidents. Income tax treaties typically permit the tax authorities in the treaty jurisdictions (the ''competent authorities'') to communicate and cooperate on tax issues, whether directly related to the treaty or not.

Treaty benefits are not granted liberally, however. Rather, the more favorable the benefits provided by a treaty, the more selective the jurisdiction providing the benefits will be in its invitations to partake in those benefits. Some limitations are part of the design of the benefit. For example, many provisions in a treaty have specific requirements: one must be a beneficial owner of the particular income or property, meet certain ownership requirements, or not have certain unwanted characteristics or intentions. Increasingly, treaties also require supplicants to meet some kind of ''limitation on benefits'' or anti-abuse requirements. These general restrictions, whether a U.S.-style

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limitation on benefits article,[1] or the more menu-like Part III of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the ''MLI''), can deny the benefits of a particular treaty provision to a resident that facially meets the requirements for that benefit.

B. Tax Disputes

How a taxpayer addresses a tax dispute depends on the number of jurisdictions involved (or potentially involved) in the dispute.

1. Single-Jurisdiction Disputes

If all of a taxpayer's activities take place in a single jurisdiction, any dispute regarding the proper application of the jurisdiction's tax rules to the taxpayer is between the taxpayer and the tax authority of that jurisdiction, and the means of addressing any such tax dispute are those set forth in that jurisdiction's rules. The taxpayer will typically have formal and/or informal administrative remedies with the tax authority. If those administrative efforts do not result in a satisfactory resolution from the taxpayer's standpoint, the taxpayer will typically have judicial remedies it can pursue. Although jurisdictions vary in the number of opportunities they may give the taxpayer or tax authority to appeal an adverse decision, at the end of the process, the final (judicial) decision is binding on the taxpayer and the tax authority.

In this single-jurisdiction scenario, the taxpayer faces two questions:

- First, can the taxpayer convince the relevant administrative or judicial decision-maker that the taxpayer's interpretation of the tax law and how it applies to the facts of the case is more correct than that of the tax authority? In short, ''Is the taxpayer right as a legal matter?''

- Second, given the taxpayer's chances of success and likely costs of appeal, at what stage is it not cost-effective to continue to pursue judicial remedies? In short, ''Is it worthwhile to appeal?''[2]

2. Two-Jurisdiction Disputes

Let's introduce a second tax authority. Assume that the taxpayer is a resident of Country A but engages in activities which Country B seeks to tax. Assume further that the taxpayer disagrees with the taxation imposed by one of the tax authorities. If there is no tax treaty between Country A (the residence country) and Country B (the source country), or if there is such a treaty but the taxpayer is not eligible for its benefits, then the taxpayer has to pursue remedies under applicable domestic law.

At first blush, this looks like the single-jurisdiction dispute scenario described above. If the taxpayer disagrees with the amount of Country B tax assessed, it could challenge the assessment in accordance with Country B rules. And, if the taxpayer is able to convince Country B's tax authority or court that no Country B tax is applicable, then that is probably the end of the dispute.

A problem arises, however, if the Country A and Country B tax authorities disagree as to Country B's taxing rights. Absent a tax treaty or other agreement that permits the two tax authorities to depart from one of the country's domestic tax rules, the taxpayer has to comply with two inconsistent tax regimes, potentially suffering double or excessive taxation.

The specific consequences of this No Treaty scenario would depend on the specific facts and laws at issue. For example, if Country A is the United States, it will not allow the taxpayer to take a foreign tax credit for the Country B taxes if it determines that the taxpayer did not sufficiently contest the Country B taxes.[3] Similarly, if Country A is the United States and the income that Country B taxes is determined to be U.S.-source, the Country B taxes will be allocable to U.S.-source income even though they may otherwise be creditable. In either case, the taxpayer will suffer double taxation given that the Country B taxes cannot be used to offset its Country A taxes.[4]

Myriad disagreements could arise between the Country A and Country B tax authorities. In each case, the taxpayer typically has the right under each country's law to resolve the dispute with that country's tax authority. What the taxpayer lacks, due to the absence of a tax treaty, is the ability to reconcile with the Country A tax authority resolutions of disputes with the Country B tax authority and vice versa.

It's not that the taxpayer lacks rights to resolve a tax dispute. Rather, the taxpayer lacks the ability to exercise its rights in a comprehensive manner. The taxpayer could separately win resolution of disputes in the Country A and Country B courts but still suffer double or excessive taxation due to the inconsistent approaches taken by the courts.

3. Using the Competent Authority Process Under an Applicable Treaty

Now, suppose the taxpayer still has a potential two-jurisdiction tax dispute, but Country A and Country B have a tax treaty and the taxpayer is fully eligible for the benefits of that treaty.

Most income tax treaties have an article setting forth how the tax authorities in the two jurisdictions

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[1] *See, e.g.,* Article 26 of the 2016 United States Model Income Tax Convention (the ''U.S. Model'').

[2] More specifically, as Ambrose Bierce defined ''appeal'' in *The Devil's Dictionary*, ''in law, to put the dice in the box for another throw.''

[3] *See* the ''noncompulsory payment'' rules of Reg. §1.901-2(e)(5).

All section references are to the Internal Revenue Code of 1986, as amended, or the Treasury regulations thereunder, unless otherwise indicated.

[4] Even if Country A uses an exemption system rather than a foreign tax credit system, the same double taxation issue will arise if Country A determines that the income Country B has taxed is ineligible for exemption under Country A law.

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are to cooperate on tax matters and resolve disagreements or questions as to interpretation. Each Mutual Agreement Procedure (MAP) article has its own features, but MAP articles generally have the same fundamental elements:

- If a person determines that the actions of the tax authorities in one or both jurisdictions will result in taxation not in accordance with the income tax treaty, the person may, ''irrespective of the remedies provided by the domestic law'' of those jurisdictions, present its case to the designated competent authority.[5]
- If the competent authority to which the case is presented cannot resolve the issue in a satisfactory manner, it must ''endeavor'' to resolve the dispute with the competent authority of the treaty partner.[6]

The time period in which the claim must be brought by the taxpayer, the ability of the competent authorities to override domestic statutes of limitations and administrative procedures, and other important details that affect the ability of the taxpayer to take advantage of MAP vary treaty by treaty. As a general matter, the United States tends to be much more willing to suspend or relax domestic limitations to obtain a resolution of a dispute. However, unless the treaty partner is of a similar view regarding taxpayer rights, those more generous provisions to which the United States would agree do not make it into the treaty.

MAP articles typically require the taxpayer to bring the dispute to the attention of the competent authority identified in the MAP article, usually the competent authority of the residence jurisdiction. The taxpayer must meet the other requirements of the MAP article, including bringing the case within the time limits explicitly or implicitly set forth in the MAP article.[7] The taxpayer must also comply with the procedures set forth by the relevant competent authority. For example, a taxpayer bringing a case to the U.S. competent authority generally must follow the requirements and procedures of Rev. Proc. 2015-40.[8]

Some tax treaties go beyond the traditional ''shall endeavor'' language and create procedures intended to lead to resolution. As part of Action Item 14 of the OECD Base Erosion and Profits Shifting (''BEPS'') Action Plan, a group of countries (responsible for 90% of outstanding MAP cases as of the end of 2013) expressed an interest in committing to binding mandatory arbitration.[9]

The most typical approach is to permit arbitration if the competent authorities are not able to reach agreement within a certain time limit. The United States has several income tax treaties with such a provision. These are the U.S.-Belgium income tax treaty, the U.S.-Canada income tax treaty, the U.S.-France income tax treaty, the U.S.-Germany income tax treaty, the U.S.-Japan income tax treaty, the U.S.-Spain income tax treaty,[10] and the U.S.-Switzerland income tax treaty. U.S. income tax treaties follow the last-best-offer approach in which the arbiter must choose one of the two competent authority submissions.

Beyond specific language in a tax treaty, some countries are subject to supranational rules intended to resolve tax treaty disputes. For example, members of the European Union are subject to Council Directive 2017/1852, which sets forth different potential dispute resolution mechanisms. The potential means of dispute resolution range from traditional arbitration approaches to mediation approaches, and the arbiter or advisory group may suggest resolutions that were not offered by either competent authority.

Thus, whether a tax treaty is available and, if so, the particular rights and remedies the tax treaty offers are key in deciding how a taxpayer should proceed in a cross-border tax dispute. The next two sections of this article explore the approaches and consequences for taxpayers in various scenarios.

II. ANALYSIS OF TWO-JURISDICTION DISPUTES

Let's start with a two-country dispute. Taxpayer resides in Country A but has income from or operations in Country B. Even in this simple scenario, several variations are possible.

A. Dispute Between Tax Authorities of Country A and Country B

Assume the Country A and Country B tax authorities disagree on a matter and Taxpayer is caught in the middle. This would typically manifest itself by one tax authority (Country A's) making an adjustment to Taxpayer's (or a related party's) tax returns and the other tax authority (Country B's) refusing to make conforming changes to Taxpayer's (or a related party's) tax returns. For example, Country A might determine that the royalties Taxpayer pays to an affiliate in

[5] Article 25(1) of the OECD Model Tax Convention on Income and Capital (the ''OECD Model''), of the United Nations Model Double Tax Convention between Developed and Developing Countries (the ''UN Model''), and of the U.S. Model. Under the OECD Model and the UN Model, the competent authority to which the presentation must be made is the jurisdiction of residence.

[6] Article 25(2) of the OECD Model, of the UN Model, and of the U.S. Model.

[7] If the MAP article is silent as to time periods, many competent authorities interpret the treaty as not modifying domestic time periods.

[8] https://www.irs.gov/pub/irs-drop/rp-15-40.pdf.

[9] *See* OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14 — 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/9789264241633-en.

[10] The protocol including the arbitration provision is scheduled to enter into force on November 27, 2019. See ''Treasury Announces Action on Tax Protocols with Two Key Trading Partners,'' http://src.bna.com/K3h.

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Country B are too great and reduce Taxpayer's deduction for such royalties commensurately. If the Country B tax authority refuses to make a correlative adjustment to the affiliate's income, there would be a dispute between the two tax authorities.

1. No Treaty Between Country A and Country B

If there is no tax treaty between Country A and Country B, resolution of the dispute will be difficult. Unless Country A and Country B have an agreement that permits the exchange of tax information (e.g., a tax information exchange agreement or "TIEA"), one or both tax authorities may not be able to disclose information regarding Taxpayer or its related parties, making productive discussions between the tax authorities impossible. If there is a TIEA between the countries, the tax authorities may be able, through spontaneous exchanges of information, to clear up factual misunderstandings that one of the tax authorities may have. Nonetheless, if Taxpayer needs one or both tax authorities to do something beyond sharing information, a TIEA will not help. Taxpayer has no choice other than to pursue remedies under Country A's and Country B's laws.

In this No Treaty scenario, as in the single-jurisdiction dispute, Taxpayer must determine whether it has a valid argument under the relevant country's law (the "Is taxpayer right as a legal matter?" question). If Taxpayer believes it has a valid case under that country's laws and procedures, then, as in the single-jurisdiction dispute, Taxpayer must undertake a cost-benefit analysis based on the size and nature of the dispute and the likelihood of obtaining a satisfactory outcome (the "Is it worthwhile to appeal?" question).

2. Treaty Between Country A-Country B

If Country A and Country B have a tax treaty, Taxpayer has a better chance for a successful resolution of the dispute. Still, for the treaty to be of help, the dispute must be one that is covered by the treaty. Just because a company or individual disagrees with the decision of a tax authority, even in a cross-border context, does not mean that there is a dispute subject to MAP. For example, the IRS might challenge a U.S. taxpayer claiming a foreign tax credit for certain taxes paid to a treaty partner. The treaty may clearly require the residence country to provide a foreign tax credit.[11] The United States, however, generally subjects the taxpayer's right to credit foreign taxes under this provision of the treaty to its general foreign tax credit limitation rules. As noted earlier, one foreign tax credit limitation is that the taxes must not be noncompulsory payments.[12] If the IRS disallows the taxpayer's crediting of certain taxes paid to the treaty partner because the IRS believes that the taxpayer failed to take the steps necessary to exhaust its remedies under the treaty partner's law, disallowance of the foreign tax credit is not a violation of the treaty. Rather, to dispute the IRS's determination that the taxes paid were noncompulsory payments under Reg. §1.901-2(e)(5), the taxpayer must pursue its administrative and judicial remedies against the IRS under U.S. domestic law.

In contrast, suppose the IRS disallows a credit to a U.S. taxpayer for a payment made to the treaty partner pursuant to a tax specifically listed as a covered income tax in the treaty[13] solely because the IRS determines that the particular foreign tax does not meet the definition of income tax in Reg. §1.902-1. In that case, the IRS's denial of the foreign tax credit is not in accordance with the treaty and is therefore eligible for MAP.

If the dispute is one covered by the treaty, how the taxpayer should respond depends upon the type of dispute and with whom the taxpayer agrees. The basic choices and decisions are shown in this chart.

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[11] *See, e.g.,* Article 23(2) of the U.S. Model and 23B(1) of the OECD Model.

[12] *See* Reg. §1.901-2(e)(5).

[13] *See, e.g.,* Article 2(3)(a) of the U.S. Model.

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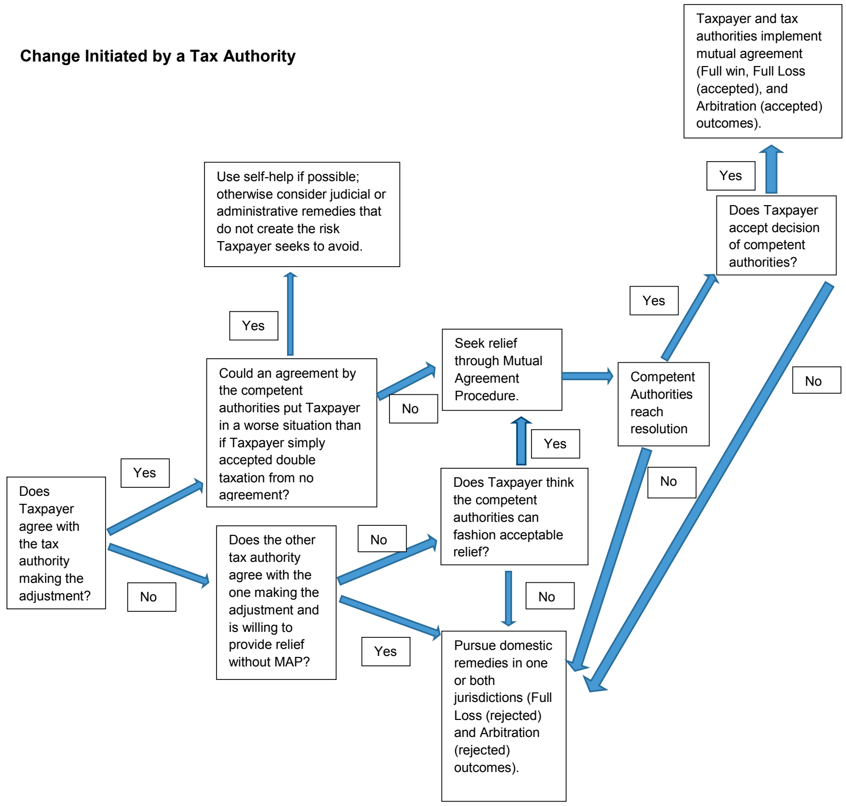
Change Initiated by a Tax Authority



Of course, the devil (and the potential perdition of taxpayer's hopes) are in the details. Let's consider different types of disputes, starting with disputes between tax authorities that are zero sum.

a. Zero-Sum Disputes

In a zero-sum dispute, any revenue Country A gains is at Country B's expense and vice versa. For purposes of analysis, we will distinguish between zero-sum choices that have a clear yes-or-no answer (in which either Country A or Country B wins exclusively) and zero-sum choices in which there can be partial winners and losers.

(1) Zero Sum Choice With a Clear Yes-or-No Answer

Let's first consider a binary choice. Either Country A's position is correct or Country B's position is correct.

Examples of a zero-sum choice in which there are only two possible answers include:

- Is Taxpayer a resident of Country A or Country B?
- Does Taxpayer, who is resident in Country A, have a permanent establishment (PE) in Country B?
- Is a payment to Taxpayer by a resident of Country B a royalty or a payment for services?

In a zero-sum, binary dispute, Taxpayer necessarily has to agree with one of the tax authorities. In this scenario, except in the one circumstance noted below (where the tax authority with which Taxpayer agrees not only drops its position but adopts the other tax authority's position with disastrous results for Taxpayer), Taxpayer should take advantage of the treaty's MAP article.

As an illustration, suppose the issue is whether Taxpayer is a resident of Country A or Country B under the treaty, and each tax authority argues that Taxpayer is a resident of its country. This is a zero-sum, binary dispute in which one tax authority should prevail completely and the other should lose completely. For purposes of the analysis below, assume that the taxpayer agrees with the Country A tax authority that Taxpayer is a resident of Country A, and Taxpayer takes its case to the competent authorities pursuant to the Country A-Country B income tax treaty MAP article.

(a) Full Win Outcome: Competent Authorities Agree That Country A's Position Is Correct

The two tax authorities go to MAP, and the Country B tax authority concedes that Taxpayer is a resident of Country A. This is the best outcome for Taxpayer because (1) it is Taxpayer's desired outcome, and (2) both competent authorities agree to that outcome. There is nothing for Taxpayer to do, other than make whatever filings are necessary to implement the competent authority agreement.

Although the example deals with Taxpayer's residence, the same rationale and conclusion would apply in any zero-sum, binary dispute between the two tax authorities, such as whether Taxpayer had a PE in Country B or whether to characterize a payment by Taxpayer as a royalty.

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(b) Full Loss Outcome: Competent Authorities Agree That Country B's Position Is Correct

The two tax authorities go to MAP, and the Country B tax authority prevails. This is not the outcome Taxpayer wanted. What Taxpayer should do depends on how bad the outcome is.

Accept Competent Authority Agreement. If Taxpayer can accept being a Country B tax resident and not a Country A tax resident (or having a PE in Country B or having a payment treated as a royalty, etc.), then Taxpayer may reluctantly accept the competent authority decision. Taxpayer would accept this outcome if the value of resolving the dispute is greater than the cost of the undesired outcome (i.e., the answer to the "Is it worthwhile to appeal?" question is "no").

Reject Competent Authority Agreement. If Taxpayer cannot accept this outcome, then Taxpayer has to reject the competent authority agreement and pursue remedies (if any) under Country B's (and possibly Country A's) domestic law.

Country B treatment:

- *If Taxpayer is successful in Country B courts.* If Taxpayer can pursue rights in Country B courts and Taxpayer prevails, then Taxpayer is treated as not being a Country B resident (or not having a PE in Country B, or the payment is not treated as a royalty, etc.). Taxpayer can continue to take the position on Country B tax returns that it is a resident of Country A and not Country B (or does not have a PE in Country B or that the payment is not a royalty).

- *If Taxpayer is unsuccessful in Country B courts.* If Taxpayer pursues its remedies under Country B law but the Country B courts affirm that Taxpayer is a Country B resident (or has a PE in Country B, or that the payment is a royalty), then Taxpayer has no choice but to file Country B tax returns as a resident of Country B (or as a nonresident with a PE in Country B, or suffer Country B withholding tax upon payment of the royalty).

  Due to the court decision in Country B, how Taxpayer complies with Country B law is clear. Far less clear is how Taxpayer complies with Country A law. Because the Country A tax authority is not bound by the Country B court decision, Taxpayer has to take into account various possibilities, depending on the result of the decision in Country B.

Country A treatment:

- *If Taxpayer was successful in Country B courts.* Suppose that Taxpayer prevailed in the Country B courts and continues to file Country A tax returns as a resident (or to take the position that Taxpayer does not have a PE in Country B or that a payment is not a royalty). This was the status quo before the MAP proceeding, and so the Country A tax authority should be willing to accept it again, notwithstanding that it reached a different conclusion in the rejected MAP proceeding.

  Still, there can be circumstances in which the Country A tax authority now wants to treat Taxpayer as a nonresident. For example, treating Taxpayer as a nonresident under the treaty may cause Taxpayer to be subject to the Country A exit tax. In that case, Taxpayer may have to pursue judicial remedies in Country A if the Country A tax authority insists on following the position it adopted in the rejected MAP proceeding.

  This nightmare outcome for Taxpayer requires that it pursue remedies and prevail in both jurisdictions. If Taxpayer believes that a competent authority that agreed with Taxpayer's position before MAP may possibly change its mind with potentially disastrous consequences for Taxpayer, then this is one instance in which it ought to forgo MAP.

- *If Taxpayer was unsuccessful in Country B courts.* Suppose that Taxpayer loses in the Country B courts. Taxpayer would have to file tax returns in Country B as a resident (or as has having a PE in Country B or be subject to Country B withholding tax on the payment), but that does not settle how Taxpayer should file returns in Country A.

  Taxpayer could file Country A tax returns consistent with the County B decision. This would be consistent with the MAP decision that Taxpayer rejected, and so the Country A tax authority may be willing to adopt the same position in Taxpayer's Country A returns that it took in the MAP. However, the Country A tax authority may determine that it does not have the discretion under domestic law to adopt the position it adopted in MAP. Or, the Country A tax authority may not want to reward Taxpayer for rejecting MAP, only to seek the same outcome after losing in Country B courts. In any case, if the Country A tax authority permits Taxpayer to file consistent with the Country B court decision and rejected MAP proceeding, then the result is the same as the Full Loss (accepted) outcome.

  If the Country A tax authority does not accept the Country B court decision or Taxpayer does not want to raise the issue, Taxpayer could file Country A tax returns as a Country A resident (or not claim a PE in Country B or treat the payment as a royalty). The result for Taxpayer would be double taxation. This is effectively the same result as if there were no income tax treaty between Country A and Country B. To wind up in this situation, Taxpayer made a serious miscalculation

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that going to Country B courts would produce better results than going with MAP. Taxpayer's best course of action now is using self-help to find a way to avoid the double taxation in future years.

(c) No Agreement Outcome: Competent Authorities Do Not Agree

In this situation, Taxpayer's initial course of action depends on whether the Country A-Country B treaty provides for arbitration or other dispute resolution upon a failure of the competent authorities to reach resolution.

- *Country A-Country B treaty does not have an arbitration mechanism*. Assuming Country A agreed with Taxpayer, Taxpayer must pursue (and prevail) in Country B courts to achieve relief. Because the competent authorities could not reach a decision, the outcome to Taxpayer is the same as if there were no Country A-Country B treaty, except that Taxpayer went through the additional cost of a failed MAP.

- *Country A-Country B treaty has an arbitration mechanism*. Unless Taxpayer fears winding up in the nightmare situation discussed above, Taxpayer should pursue arbitration. In this particular case, because the issue is a zero-sum, binary one, it does not matter whether the arbitration process set forth in the Country A-Country B treaty is the last-best-offer approach generally adopted in U.S. tax treaties or the more traditional arbitration approach.

  - o If the arbiter agrees with Country A, then Taxpayer is in the Full Win outcome. There is nothing for Taxpayer to do other than implement the competent authority agreement dictated by the arbitration result.

  - o If the arbiter agrees with Country B, then Taxpayer is in the Full Loss outcome. As discussed in II.A.2.a.(1)(b), above, Taxpayer has to decide whether to reject the competent authority agreement and pursue domestic remedies.

Of course, just because the treaty has an arbitration provision does not mean it will apply upon a deadlock of the competent authorities, as not all disputes are eligible for arbitration.[14] If not eligible or Taxpayer declines arbitration, then Taxpayer is in the same situation as in the No Agreement (no arbitration provision) outcome and has to pursue domestic remedies.

(2) ZeroSum Choice With No Clear Yes-or-No Answer

The dispute between the tax authorities in Country A and Country B could be zero sum but not require a binary choice. For example, the Country A and Country B tax authorities may agree that Taxpayer has a PE in Country B but disagree as to how much income should be attributable to the PE. Or, the Country A and Country B tax authorities may agree that a payment to Taxpayer is both a payment for services (which are not subject to Country B withholding tax) and a license (which is subject to Country B withholding tax), but disagree as to the allocation of the payment between the two. Although there may be a range of possible answers, any additional revenue Country A gets comes at County B's expense, and vice versa.

The primary difference between a zero-sum, binary dispute (discussed immediately above) and a zero-sum, non-binary dispute occurs at the very beginning of the decision-making matrix. A zero-sum, non-binary dispute offers a range of possible solutions. Thus, unlike in the zero-sum, binary scenario, Taxpayer may not necessarily agree with either of the competent authorities.

(a) Taxpayer Agrees With One of the Competent Authorities

If Taxpayer happens to agree with one of the competent authorities, then Taxpayer's decision-making choices are generally the same as set forth in the zero-sum, binary analysis above. The way of dealing with Full Win and Full Loss outcomes would be the same. Indeed, the Full Loss outcome may be easier for Taxpayer to digest in a non-binary dispute because, as a result of the negotiations in MAP, the differences between the two tax authorities may be less stark. Thus, it may be easier for Taxpayer to agree to an adverse MAP or apply self-help in case of a loss in the Country B courts simply because the final outcome is less adverse than the tax authority's initial position.

In certain cases, however, there is a distinction between binary and non-binary disputes in the No Agreement outcome. If the Country A-Country B treaty has arbitration, the type of arbitration provision matters more in a non-binary dispute than in a binary one. If the Country A-Country B treaty adopts the last-best-offer approach, the arbiter must adopt the position of one of the two competent authorities, thereby effectively turning a non-binary dispute into a binary dispute. On the other hand, if more traditional arbitration applies (or some mediator or advisory board is used), the arbiter may choose a result different from what either competent authority proposed. For good or bad, this type of arbitration injects into a non-binary dispute a level of uncertainty that does not exist in a binary dispute or if last-best-offer arbitration applies in a non-binary dispute. Granted, this is the same risk Taxpayer would face in litigation, where Taxpayer could wind up better than the Full Win outcome, worse than the Full Loss outcome, or somewhere in between.

(b) Taxpayer Does Not Agree With Either Competent Authority

If Taxpayer prefers a third alternative not advocated by either competent authority, then the Full Win out-

[14] For example, the U.S.-Germany income tax treaty, the U.S.-Spain income tax treaty, and the U.S.-Canada income tax treaty allow arbitration regarding residence only if the taxpayer is a natural person. Similarly, the U.S.-Germany and U.S.-Canada treaties are generally limited to disputes under certain articles.

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come is not possible, given that it is not being considered by the competent authorities. Accordingly, the threshold question is how much Taxpayer's preferred position differs from that of one or both competent authorities. There are three possibilities:

(i) Taxpayer may be indifferent as to where the two competent authorities end up, as long as they agree. For example, suppose the Country A tax authority argues that 30% of Taxpayer's business profits are attributable to a PE in Country B while the Country B tax authority argues that 80% of Taxpayer's business profits are attributable to a PE in Country B. If Country A and Country B calculate Taxpayer's business profits in a similar way and impose a similar rate of tax, Taxpayer may not care how much business profits Country B taxes as long as Country A agrees to credit the tax paid to Country B or exempt the income taxed by Country B. In this case, Taxpayer would seek MAP not because Taxpayer has a preferred outcome but because Taxpayer wants to avoid being double taxed in the absence of an agreement among the competent authorities. If the competent authorities reach agreement, Taxpayer would accept the MAP decision for that reason. If they fail to reach agreement, Taxpayer would follow the approach described above under "No Agreement Outcome," seeking arbitration if possible given that Taxpayer is more interested in a solution that prevents double taxation than in the specifics of that solution.

(ii) If Taxpayer's preferred position is between the two competent authorities, then Taxpayer would still want to pursue MAP. For example, suppose the Country A and Country B tax authorities agree that payments Taxpayer receives from a Country B customer are attributable to a combination of (1) services Taxpayer performs in Country A, and (2) a license Taxpayer grants the customer to use IP in Country B. The Country A tax authority argues that 80% of the payment is attributable to services performed in Country A, and so only 20% may be withheld by Country B at a reduced rate under the Country A-Country B treaty. The Country B tax authority argues that only 20% of the payment is attributable to services performed in Country A, and so Country B may withhold on 80% of the payment at a reduced rate under the Country A-Country B treaty. Taxpayer, in contrast, believes that the correct split is 50/50. Taxpayer should pursue remedies under MAP.

- o It is possible that the Country A and Country B tax authorities may compromise in MAP, resulting in an agreement that is closer to Taxpayer's preference than either tax authority's current position.
- o If the competent authorities agree to a position much less favorable to Taxpayer, Taxpayer would approach the issue the same way as in the Full Loss outcome.
- o If they fail to agree, Taxpayer would approach the issue like other No Agreement outcomes. Note that in this case, traditional arbitration (as opposed to last-best-offer arbitration) carries greater upsides (Taxpayer may get a compromise that is closer to its preferred outcome) and downsides (Taxpayer may get a decision that, from Taxpayer's perspective, is worse than what either tax authority sought). Still, last-best-offer arbitration would be preferred in this case, given the nature of the dispute. Last-best-offer arbitration is intended to operate as an incentive for the two tax authorities to reach agreement. If it works as intended, Taxpayer is more likely to get its preferred solution as an agreement by the competent authorities in MAP without needing to resort to arbitration.

(iii) If Taxpayer's preferred position is outside of the range of possible agreement between the two tax authorities, Taxpayer is unlikely to achieve its preferred outcome in MAP. For example, assume that the Country A and Country B tax authorities agree that Taxpayer has a PE in Country B due to the actions of a dependent agent. The Country A tax authority argues that 20% of Taxpayer's business profits are attributable to that dependent agent PE, and the Country B tax authority argues that 50% of Taxpayer's business profits are attributable to that dependent agent PE. In contrast, Taxpayer believes that the dependent agent performs only non-income-producing activities, and so no business profits should be attributable to the dependent agent PE. Taxpayer has to decide whether it thinks MAP will result in an acceptable outcome to Taxpayer. In other words, given that the Country A position is closer to Taxpayer's preferred position, could Taxpayer accept the Country A position? If so, does Taxpayer believe that the Country A position is likely to prevail in MAP?

- o If the answer to both questions is "yes," then Taxpayer would go to MAP, following the approach set forth above for when a taxpayer agrees with the position of a competent authority.
- o If Taxpayer thinks MAP is unlikely to produce an acceptable outcome, then Taxpayer will have to pursue its remedies under Country B tax law.

b. Disputes That Are Not Purely Zero Sum

Most disputes will not be as simple as described above. The dispute may be more complex or the tax authorities may have multiple issues in dispute.

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Many tax disputes cannot be resolved with a single answer. The underlying dispute may require the resolution of several, often contingent or otherwise related, issues. For example, Country A and Country B may disagree whether an individual or company is a resident of Country A or a resident of Country B under Country A-Country B treaty. Depending on which country is deemed to be the residence country, they may have a further disagreement as to whether the individual or company has a PE in the non-resident country. Or, they may disagree as to whether a payment should be treated as made for the use of intangible property, for the use of tangible property, for services, or for some combination of the three. Depending on the answers to those questions, there will be follow-up issues, such as where the property is located and used and where the services are performed.

The more contingent and complex the dispute between the competent authorities, the less likely a taxpayer is to realistically obtain a Full Win or Full Loss outcome. Rather, the Full Win and Full Loss outcomes would represent the ends of a range of possible outcomes. An individual or company is much more likely to find itself somewhere in between the Full Win and Full Loss outcomes, in what we could call the Mixed Bag outcome.

For the same reasons, the odds of an individual or company finding a satisfactory resolution outside of MAP decrease as the complexity of the dispute increases. In a simple dispute, a taxpayer may see little downside to rejecting an unfavorable MAP outcome and seeking judicial relief in one or more jurisdictions. If multiple questions are involved, however, the odds that an individual, company, or group can cobble together comprehensive relief drop significantly. Even if a taxpayer wins in whole or in part each case, the judicial results may not fit together in a way that provides the taxpayer adequate relief. For example, a court in Country A and a court in Country B may each adopt a position that, in isolation, is ostensibly favorable to a taxpayer, but, because they adopted different rationales or characterizations, comprehensively fail to provide the the desired relief.

Accordingly, the more complex the dispute between the two tax authorities, the more important it becomes for a taxpayer that (1) there be an income tax treaty between Country A and Country B, (2) the taxpayer be able to take advantage of the treaty's MAP process, and (3) the treaty have arbitration or other means of dispute resolution.

B. Country A-Country B Dispute Initiated by Taxpayer

Not all tax disputes are initiated by a tax authority. The taxpayer may adopt a new reporting position, file an amended return with a changed position, or file a refund for overwithheld tax. If this ''taxpayer-initiated'' adjustment affects only one tax authority, then the taxpayer would follow that jurisdiction's rules for filing an amended return or refund claim (if the change in reporting is retroactive) or complying with the applicable disclosure, change in method of accounting, and other rules (if the change in reporting is prospective). An example of such a unilateral, single-jurisdiction change would be if an individual that is a U.S. citizen or resident determined that payments from a foreign corporation that the taxpayer had been treating as interest (and subject to U.S. income tax at ordinary income tax rates) was qualified dividend income (and subject to U.S. income tax at a preferential rate). Whether the taxpayer's position is correct and, if so, how to implement it affects only the U.S. tax authority.[15]

If the taxpayer's change in position affects tax withheld or paid to another jurisdiction, then the taxpayer must go through an analysis similar to that discussed above for adjustments initiated by a tax authority. Although the basic analysis is the same, there are special considerations to take into account because the adjustment is taxpayer-initiated. First, if the taxpayer is seeking a refund of past taxes or adopting a position that will result in lower tax liability, the tax authority facing the shortfall is likely to contest the taxpayer's position. Although the taxpayer will have remedies under domestic law to address this dispute with the tax authority, whether the taxpayer has rights under an income tax treaty to contest the tax authority depends not just on whether a tax treaty exists. It also depends on whether the contesting tax authority is seeking to tax the taxpayer in a way that is ''not in accordance with the treaty,'' therefore opening the door to MAP.

For example, if the taxpayer seeks a refund of past taxes and the tax authority demands that the taxpayer make certain filings and provide significant documentation, the tax authority's actions are not in violation of the treaty if the tax authority is simply making the taxpayer go through the normal process for refunds. Similarly, if the taxpayer is not challenging the tax authority's right to tax the taxpayer on a certain amount of income but rather the dispute is whether the taxpayer met the local law's requirements for a preferential rate of taxation, then that dispute is not for the competent authorities but rather is for the local administrative and judicial system to handle.

Let's assume, though, that an individual or company is taking a position that is being challenged by a tax authority whose argument is inconsistent with the rules of a tax treaty for which Taxpayer is eligible. The first question is whether Taxpayer's dispute is with the *residence* country tax authority or with the *source* country tax authority.

For example, assume Taxpayer is a resident of Country A and conducts operations in Country B, earning income that is considered business profits. There is an income tax treaty between Country A and

[15] Granted, there may be tax consequences in the foreign corporation's jurisdiction if the taxpayer's change in position results in the creation of a hybrid instrument. The number of instances in which a tax authority cares not at all how the transaction or arrangement is treated by another relevant tax authority is rapidly shrinking.

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Country B, and Taxpayer is eligible for the benefits of that treaty. If Country B imposes higher tax rates than does Country A, Taxpayer has an incentive to argue that it does not have a PE in Country B. After several years of filing Country B income tax returns premised on Taxpayer having a PE in Country B, Taxpayer belatedly recognizes this incentive. Taxpayer changes its operations in Country B and takes the position that it no longer has a PE in Country B. If Country B insists that Taxpayer continues to have a PE in Country B, then whether Country B's actions are in accordance with the Country A-Country B treaty turn on the factual determination as to whether Taxpayer has a PE in Country B. In other words, Taxpayer can challenge the Country B continued taxation under the Country A-Country B tax treaty only if Taxpayer can convince the Country A tax authority that the Country B tax authority is violating the treaty by taxing Taxpayer on its business profits in the absence of a PE in Country B. If Taxpayer cannot do that, then Taxpayer may challenge the Country B tax authority's continued taxation only under Country B law.

Alternatively, let's assume that Taxpayer's residence country, Country A, imposes tax at a higher rate than Country B, but Country A has an exemption system or Taxpayer has excess foreign tax credits or other attributes that mean that Taxpayer owes no residual Country A tax on income that Country B taxes. In this case, Taxpayer has an incentive to argue that it has a PE in Country B and that Country B can tax its business profits. The Country B tax authority similarly has an incentive to agree with Taxpayer as to the existence of a PE in Country B, and they both have an incentive to have the largest amount of income possible attributed to the PE.

If there is a dispute between Taxpayer and a tax authority, it will be the Country A tax authority, which sees its revenue being reduced by Taxpayer's change in position. If Country A refuses to exempt or allow foreign tax credits against Taxpayer's Country B business profits, then whether Country A's actions are in accordance with the Country A-Country B treaty depend on whether Taxpayer has a PE in Country B. Challenging the Country A tax authority for failure to provide relief from double taxation under Country A law will not require the support of either competent authority, but such a challenge under the Country A-Country B tax treaty will require that Taxpayer convince the Country B competent authority that the Country A tax authority is violating the treaty by failing to give Country B priority in taxing Taxpayer's business profits in Country B.

If the Country A-Country B tax treaty, like Article 25(1) of the U.S. Model, gives Taxpayer discretion regarding which competent authority to approach with its request for relief, Taxpayer should approach first the more sympathetic competent authority, generally the one that stands to gain revenue from Taxpayer's change in position. If the treaty dictates which competent authority Taxpayer must approach (again, like Article 25(1)), Taxpayer must approach that competent authority, usually of the resident state. That is advantageous in our first example but not in our second example. In the second example, it is hard to see Taxpayer making headway with the Country A tax authority, who has already concluded that it is not violating the treaty, unless Taxpayer gets the Country B tax authority involved. Thus, when the competent authority who disagrees with Taxpayer is the one that Taxpayer must approach, Taxpayer will need to turn this into a dispute between the Country A and Country B tax authorities. For there to be a dispute needing MAP, the Country B tax authority must conclude that Country A's actions are not in accordance with the Country A-Country B treaty — e.g., Country A is failing to eliminate double taxation in accordance with the applicable Relief from Double Taxation article[16] of the treaty or failing to make the appropriate adjustments in accordance with the Associated Enterprises article[17] of the treaty.

Once one gets over the hump of convincing the tax authorities that the dispute is indeed covered by the treaty, the analysis that Taxpayer goes through with a taxpayer-initiated adjustment is similar to that when the tax authorities make the adjustment.

[16] Article 23 of the OECD Model, U.S. Model, and UN Model.

[17] Article 9 of the OECD Model, U.S. Model, and UN Model.

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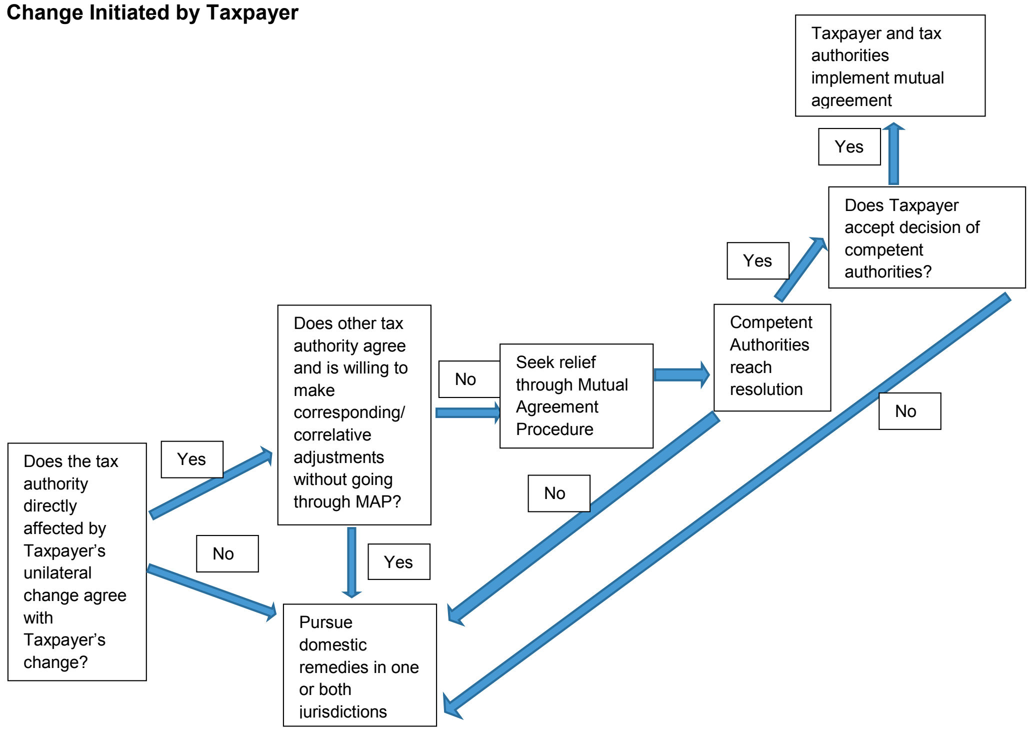
Change Initiated by Taxpayer



Because MAP is a proceeding between the tax authorities, it is available to Taxpayer only if the competent authorities agree that the dispute belongs there. Unless Taxpayer can convince one of the competent authorities to support Taxpayer's unilateral adjustment with the same vigor as if it were the tax authority's own, Taxpayer is less likely to make it to the MAP stage or, if making it to MAP, less likely to obtain a favorable resolution from the competent authorities. Thus, in a taxpayer-initiated dispute, there is a greater likelihood that Taxpayer will wind up seeking validation of its position in the courts of one or both jurisdictions. Note that the existence of an arbitration provision in the Country A-Country B treaty helps Taxpayer only if Taxpayer reaches the stage where the competent authorities have gone through MAP but not agreed on a resolution. A dispute that does not make it that far, either because one tax authority disagrees that the dispute is eligible for MAP or because the less motivated competent authority conceded in MAP, is not eligible for arbitration.

So, if Taxpayer makes it to MAP and gets an acceptable agreement between the tax authorities, then Taxpayer just follows their instructions for implementing the MAP decision. If Taxpayer disagrees with the MAP outcome, then Taxpayer goes through the analysis process noted in the Full Loss and Mixed Bag outcomes described above. If there is no MAP decision, Taxpayer follows the process noted above in the No Agreement outcome.

III. MULTIJURISDICTION DISPUTES

A. Generally

As described above, an individual or company in a bilateral tax dispute is almost always better off if there is a tax treaty between the two jurisdictions. Comprehensive tax treaties (or at least the type of agreement that taxpayers would want to access) are almost always bilateral. As noted above, bilateral tax treaties are good although not perfect in resolving disputes that are solely between the two jurisdictions. When a tax dispute involves three or more jurisdictions, though, the limitations of bilateral treaties become evident. This is not an inherent flaw in bilateral tax treaties — they do exactly what they are supposed to do. Rather, this suggests that a different type of approach, one intended to address multijurisdictional disputes specifically, will be necessary if multijurisdictional disputes become frequent.

The type of multijurisdictional disputes that could arise are almost infinite.

- They can relate to where a taxpayer is resident. For example, Country A and Country B may each conclude that an individual or company is a resident of its country under its domestic law, but the individual or company disagrees and argues that it is only a resident of Country C. Even if there are income tax treaties between Country A and Country B, Country B and Country C, and Coun-

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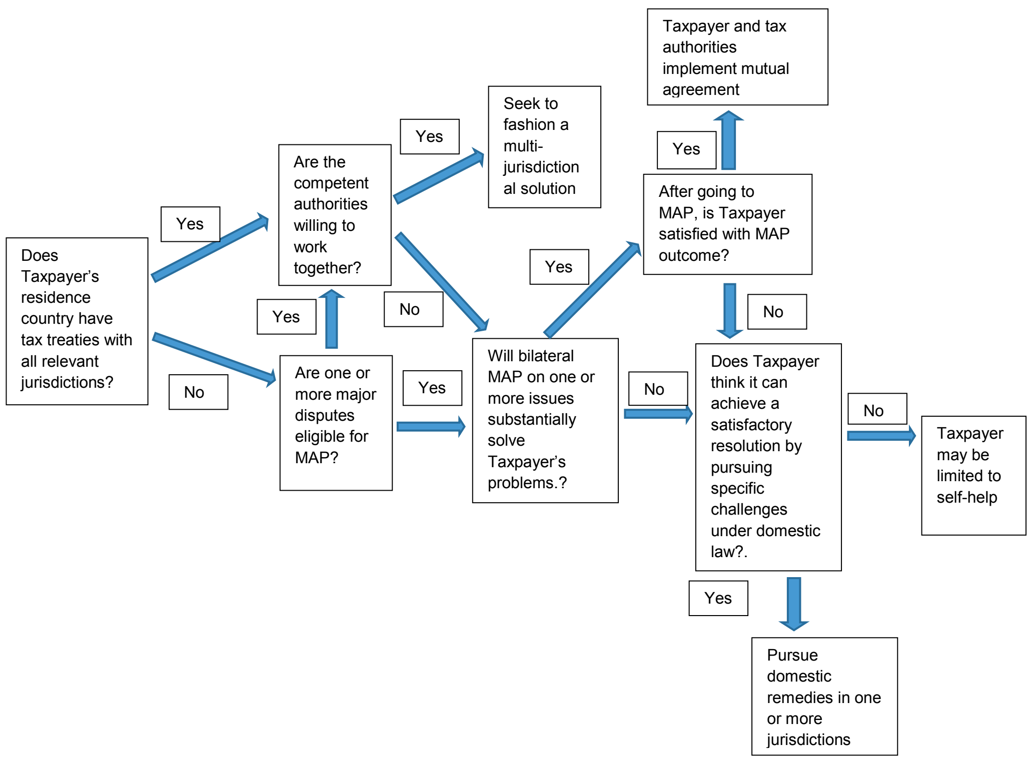
try A and Country C, MAPs under each treaty may not reach the same conclusion about the person's residency.

- They could involve multiple source countries each claiming the right to tax the same income. For example, Country A, Country B, and Country C may each argue that a company resident in another jurisdiction has a PE in that country and seek to tax the business profits of that PE. This would lead to excessive taxation of the company if Country A, Country B, and Country C had expansive views as to the profits attributable to the PE in their country. Even if there is an income tax treaty between the company's resident country and each of the source countries, that would not resolve the issue if Country A, Country B, and Country C are actually fighting over the same pot of source-country income, with each country arguing that most of that pot of income is attributable to the PE in that country.

- The issue may not simply be one of interpretation. Each treaty has its own rules and definitions, foreclosing consistent outcomes across treaties. Most jurisdictions base their treaty on a model (usually, the OECD Model or UN Model), but they typically depart from those models to follow their own treaty policy. Further, model treaties change over time, and so even treaties that adopt model provisions will differ if they are of different vintages. In cases where the treaties have different provisions, neither good-faith negotiations nor binding dispute resolution are going to bring about a satisfactory, consistent solution to the multijurisdiction dispute.

A highly simplified flow chart for resolving multijurisdictional disputes would look like this:



The following is a more detailed, but still high-level, analysis of the decision-making an individual or company caught in a multijurisdictional dispute should follow.

B. Three-Jurisdiction Disputes

Assume that Taxpayer, a resident of Country A, engages in activities in Country B and Country C, whose tax authorities seek to tax Taxpayer's income from the activities in their respective jurisdictions.

1. No Treaties Between the Countries

If Country A has no tax treaty with Country B or Country C, the situation is the same as if this were a bilateral dispute involving two countries with no income tax treaty between them. In this three-country No Treaty scenario, Taxpayer is limited to seeking relief under the domestic law of the relevant jurisdictions. The only difference between this and the two-country No Treaty scenario discussed in II., above, is that a greater number of outcomes are possible with three countries involved. This means that the odds of

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Taxpayer getting partial and conflicting relief, as opposed to fully satisfactory or fully unsatisfactory relief, are much greater than in a two-country scenario. Indeed, such odds rise exponentially as the number of (non)-treaty countries increases.

2. Covered by Treaties

Suppose Country A has an income tax treaty both with Country B and with Country C, and Taxpayer is eligible for the benefits of both treaties. As with the two-country scenario, the first question is whether the dispute at issue is within the scope of both treaties. If it is not, then Taxpayer is in the same position as in the No Treaty scenario.

Let's assume, though, that the issue is within the scope of both treaties. Both the Country A-Country B and Country A-Country C income tax treaties permit the source country to tax the business profits of a Country A resident only if it has a PE in the source country and only to the extent of the amount attributable to the PE.

- If the Country A tax authority is able to convince the Country B and Country C tax authorities — either in separate MAPs or in a combined MAP — that Taxpayer has no PE in the source countries, then Taxpayer will have avoided double taxation. This may not be a Full Win outcome to Taxpayer, however, as Taxpayer might have preferred having a PE in one of the jurisdictions because of lower source-country tax rates and a Country A exemption system.

- If the Country A tax authority reaches agreement with the Country B and Country C tax authorities that there is a PE in each country and determines the amount of profits attributable to each PE, Taxpayer should also avoid double taxation, assuming the Country A tax authority has taken into account the amount of profits expected to be attributed to the "other" PE in each jurisdiction. Whether this is a Full Win, Full Loss, or Mixed Bag outcome depends on Taxpayer's preferences.

Irrespective of whether Taxpayer achieves its desired outcomes, its ability to achieve full relief from double taxation is tied to each issue being within the scope of a treaty and being resolved in a consistent manner. If the Country A tax authority reaches agreement only with the Country B tax authority, Taxpayer may be subject to double or excessive taxation if Country C imposes tax on income that the Country A-Country B MAP agreed Country B could tax. Even if Taxpayer can take the Country A-Country C dispute to arbitration because the Country A-Country C treaty includes an arbitration provision and the two tax authorities failed to agree within that treaty's prescribed time period, there is no guarantee that the arbiter's decision will be consistent with the Country A-Country B MAP decision. In short, for Taxpayer to receive a consistent answer on taxation (whether favorable or not), all of the affected jurisdictions must have treaty relationships, each aspect of the dispute must be within the scope of the relevant treaties, and the MAP decisions have to be consistent with each other. To obtain favorable relief, Taxpayer has to run the table.

C. Multijurisdictional Disputes With Some Treaty Coverage

The more jurisdictions involved in the dispute, the greater the likelihood that some, but not all, of the dispute will be covered by tax treaties. Because there are so many variations, we will focus on just a few scenarios to identify the issues that must be considered.

Let's begin with a hypothetical dispute that would typically be within the scope of a treaty. Countries A, B, and C all have treaties with each other. Country D has a treaty only with Country B. Taxpayer is a resident of Country A and engages in activities in Countries B, C, and D, all of which seek to tax Taxpayer on the income they see attributable to the income in their country. All of Taxpayer's income is business profits.

- Country A argues that Taxpayer does not have a PE in Country A or Country B, and therefore neither country has a right under the applicable treaty to tax Taxpayer's business profits.

- Country B argues that Taxpayer has a PE in Country B and 60% of Taxpayer's profit is attributable to that PE.

- Country C argues that Taxpayer has a PE in Country C and 50% of Taxpayer's profit is attributable to that PE.

- Country D argues that Taxpayer is subject to tax in Country D on 40% of Taxpayer's income.

Suppose Taxpayer seeks competent authority relief under Country A's respective treaties with Country B and Country C, arguing (like Country A) that Taxpayer does not have a PE in the source country.

1. Full Win Outcome

One possible outcome is that Taxpayer/Country A wins both cases. Taxpayer avoids double taxation in Countries B and C, but is still subject to double taxation on the income Country D taxes unless Country A agrees to exempt that income or provide Taxpayer a foreign tax credit for the Country D taxes. So, even if Taxpayer prevails completely in MAP, due to the lack of a Country A-Country D treaty, Taxpayer will be subject to tax on 140%[18] of its income absent the grant of unilateral relief by Taxpayer's residence country. Without unilateral relief from Country A, this is not really a Full Win outcome from Taxpayer's perspective.

2. Mixed Bag Outcome

Another possible outcome is that Taxpayer seeks competent authority relief but prevails in only one in-

[18] Country A taxes 100% of Taxpayer's income, and Country D taxes 40% of Taxpayer's income.

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stance. For example, Taxpayer gets its desired outcome in the Country A-Country B treaty (the Country B competent authority agrees with the Country A competent authority), but not in the Country A-Country C treaty. What Taxpayer should do depends on what happened in the Country A-Country C MAP.

a. The Country A and Country C Competent Authorities Agree That Taxpayer Has a PE in Country C and That 50% of Taxpayer's Profit Is Attributable to the PE

Because the competent authorities reached agreement, Taxpayer does not have to worry about double taxation of the income taxed by Country C. As a result of the Country A-Country C MAP, Country A must exempt the income Country C taxes or else give a credit. Still, as discussed above under ''Full Win Outcome,'' Taxpayer faces potential double taxation on the income taxed by Country D.

But suppose Taxpayer is not satisfied with simply avoiding double taxation of the income taxed by Country C. Taxpayer does not want Country C to tax its income because Taxpayer prefers Country A's rate of tax. Even if Taxpayer is disappointed by this MAP outcome, it should reject the Country A-Country C competent authority agreement and pursue a remedy in Country C courts only if it believes that it is highly likely to prevail in the Country C courts. Further, because Taxpayer would have rejected the Country A-Country C MAP decision, Taxpayer would have to prevail completely in the Country C courts regarding whether it has a PE in Country C. If Taxpayer only partly prevails (i.e., the Country C court finds that Taxpayer has a PE in Country C but attributes a smaller part of profit to the PE than the competent authorities did), then Taxpayer may be worse off than if it had accepted the MAP agreement, which bound Country A to relieve double taxation of income taxed by Country C. Because the Country C taxation (even though smaller) is not pursuant to MAP, the Country A tax authority could reasonably determine that it does not have to provide unilateral relief to prevent double taxation. If the Country A tax authority views the Country C taxation as not in accordance with the treaty, then the Country C taxation, like the Country D taxation, may go unrelieved by Country A.

Granted, there could be situations in which Taxpayer is using the competent authority process not to avoid double taxation but rather to seek lower or no taxation of the income. In that case, Taxpayer's fallback may be single taxation rather than multiple taxation, and Taxpayer may be more aggressive in rejecting MAP. Note that this possibility is becoming infrequent as jurisdictions implement BEPS-related changes in law and treaties and so even if the scenario exists for a particular taxpayer, it probably has a short life span. So, this all-upside scenario will not be considered further.

b. Country A and Country C Competent Authorities Do Not Agree

Suppose the Country A and Country C competent authorities do not agree. If that is the case, whether the Country A-Country C treaty has an arbitration provision is key. If it does, then the next question is whether the provision is for last-best-offer arbitration or traditional arbitration. Although the type of arbitration should not affect the determination of whether there is a PE in Country C, given the yes-or-no nature of that question, it might affect allocation of profits if the arbiter finds a PE. Under the more traditional arbitration, the arbiter could attribute a different amount of business profits to the PE than either competent authority offered. Still, even if Taxpayer may get a very different allocation than either competent authority determined, the arbiter's decision would prevent double taxation. Thus, the only reason why Taxpayer would reject the Country A-Country C MAP agreement (as forced by arbitration) is if, as discussed above, Taxpayer faces significantly higher taxes and sees an extremely high likelihood of prevailing in the Country C courts.

If the Country A-Country C treaty does not have an arbitration provision, then Taxpayer faces potential unrelieved taxation not just in Country D but in Country C as well. Taxpayer has to pursue remedies in Country C courts.

Note that in this example, the treaties need to be with Taxpayer's country of residence and each source country. It is not necessary that there be treaties between the source countries. Indeed, the treaty between Country B and Country D provides no basis for relief to Taxpayer.

Treaties between the source countries may make things more convenient, especially if the competent authorities can all communicate together, but preventing double taxation requires a treaty with the country of residence. For example, suppose Countries B and C have a treaty with each other but neither has one with Country A. Taxpayer is not a resident of Country B or Country C, and thus the Country B-Country C treaty does Taxpayer no good on this matter, other than letting those two tax authorities communicate so that perhaps they decide to tax less than 110% of Taxpayer's income. With no treaty between Taxpayer's country of residence and Country B or Country C, Taxpayer has to pursue remedies under domestic law of those countries.

c. Disputes Involving Groups

Many multilateral disputes will involve a group rather than a single company. Suppose that Taxpayer, a resident of Country A, wholly owns a subsidiary that owns and licenses intellectual property in Country B (''IP Holding Company'') and also wholly owns an operating subsidiary in Country C (''Operating Company'') that pays royalties to IP Holding Company. The Country C tax authority determines that the intellectual property for which Operating Company is paying royalties to IP Holding Company is actually held by Operating Company and disallows the royalty deduction.

This is a dispute between the Country B and Country C tax authorities. The Taxpayer group may not be able to resolve this dispute if there is no tax treaty between Country B and Country C or, if there is, the

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Country C tax authority argues that the treaty is not applicable due to IP Holding Company's lack of substance. Even if there is a treaty and the dispute is within its scope, MAP still may not be available. If the Taxpayer group includes transparent entities (or, from a U.S. tax standpoint, disregarded entities), the treaties have to characterize the entities consistently; otherwise, the disagreements as to the identity of the person that earned the relevant income and the residence of the ''taxpayer'' may prevent the jurisdictions from reaching the necessary initial agreement as to which jurisdictions and treaties are relevant. Even if a common view is eventually reached, the delay can mean that a filing deadline or time limit in one of the relevant jurisdictions has been missed, foreclosing or inhibiting relief even if the tax authorities were to agree in principle.

Let's make the example above a little more complex. Assume that the Country C tax authority denies Operating Company's deduction of royalties paid to IP Holding Company, under a view that all the intellectual property Operating Company is using is in Country C. Country C also asserts that Taxpayer is using that same intellectual property and imputes royalties from Taxpayer to Operating Company. Meanwhile, the Country B tax authority is recharacterizing a loan Taxpayer made to IP Holding Company through a disregarded entity in Country D as equity, denying an interest deduction to IP Holding Company, and applying withholding tax to the payments by IP Holding Company to the disregarded entity in Country D.

If Countries A, B, and C all have income tax treaties with each other, Taxpayer could take to MAP the following disputes:

- Country A and Country B tax authorities' disagreement as to whether (a) payments from IP Holding Company are interest or dividends and (b) whether payments through the disregarded entity in Country D are ignored in applying the Country A-Country B tax treaty.
- Country B and Country C tax authorities' disagreement as to whether payments by Operating Company should be treated as royalties to IP Holding Company.
- Country A and Country C tax authorities' disagreement as to whether Taxpayer's income is overstated in Country A and Operating Company's income is understated in Country C due to Taxpayer's failure to pay royalties to Operating Company.

It is impossible to see how these disputes are resolved satisfactorily without the Country A, Country B, and Country C tax authorities and the affected taxpayers all communicating together. Resolution of one treaty dispute affects another existing treaty dispute and often creates a new one. Even if the competent authorities reached a resolution of each dispute (whether voluntarily or through arbitration), the result may be three independent and inconsistent decisions. For example, if the Country C tax authority prevails in its dispute with the Country B tax authority, and they conclude that the relevant intellectual property is in Operating Company rather than IP Holding Company, then IP Holding Company may have no revenue. In that case, the Country A and Country B tax authorities would have to revisit whatever resolution they had reached, given that IP Holding Company no longer has income.

IV. CONCLUSION

The BEPS Project has not only limited taxpayer (mis)use of tax treaties but turned tax treaties into just as much a tool of tax enforcement as a means of relieving double or excessive taxation. So, greater disputes between tax authorities and taxpayers are expected. Ensuring a reasoned resolution becomes more important and more difficult as the number of tax authorities involved in the tax dispute increases. Although the inventory of MAP disputes is growing, progress is being made in improving bilateral treaty disputes.[19] However, new approaches need to be developed to deal with multilateral disputes, especially those that involve two source countries fighting over amounts they should be able to tax.

What's the best way to deal with multilateral tax disputes? Ideally, the parties would invoke Manjushri, the bodhisattva associated with wisdom. He has a flaming sword that he uses to cut through ignorance and misunderstanding. But, with all the tweets and Internet postings nowadays, he has a lot of demands on his time. One could also invoke Solomon, but the fabled exhibition of his wisdom — splitting the baby in half — would not be helpful in most tax disputes. Tax disputes typically do not engender the maternal instincts necessary to produce the solution Solomon sought. A tax dispute would probably descend into an argument that the baby should not be split in half but rather split in a way that reflected each party's reasonably anticipated benefits.

Still, certain principles seem applicable to disputes generally.

A. Generally

In many of the scenarios discussed above, the taxpayer must resort to remedies under domestic law. Accordingly, even if eligible for and pursuing MAP, the taxpayer needs to preserve its ability to proceed under domestic law by making protective filings, ensuring that statutes of limitations or deadlines are extended or tolled, etc.

Under current treaties and tools, discrete bilateral disagreements are more likely to be resolved favorably (and with certainty) than multilateral disputes. In bilateral tax disputes, some taxpayers may face only one of three possible outcomes: Full Win, Full Loss,

[19] See the OECD's MAP statistics for 2018 at https://www.oecd.org/tax/dispute/mutual-agreement-procedure-statistics.htm/.

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or No Decision. As the complexity of the bilateral tax dispute increase or the number of jurisdictions increase, the odds of the taxpayer encountering a Full Win or Full Loss outcome becomes unlikely, while the odds of taxpayer encountering a Mixed Bag or No Decision outcome increase. How a taxpayer deals with a Mixed Bag or No Decision outcome depends on the particular facts of the dispute and the consequences of foregoing MAP if available.

B. Recommendations

First, any procedure or approach that increases communication — and flexibility in means of communicating — between the taxpayer(s) and the tax authorities can only improve the chances of a resolution. Allowing the tax authorities to speak directly and informally allows candid discussions and quicker resolutions. Bilateral treaties currently permit this, but it is equally important to ensure analogous opportunities to communicate in a multijurisdictional context. Determining the right amount of taxpayer involvement is more difficult. Jurisdictions are still struggling with this in the bilateral context, especially when it comes to arbitration.

Second, if the tax authorities cannot agree on relief, then there needs to be a way to provide efficient and certain resolution. As for specific approaches, it is probably best to distinguish bilateral disputes from multijurisdictional disputes, and disputes covered by a treaty from disputes that are not. Strategies that work in a bilateral context may not be as helpful in a multilateral context, and methods designed in a treaty context may be useless in a non-treaty context. Still, at least when MAP is involved, adoption of procedures that put pressure on the parties to reach an agreement is generally good as an institutional matter. This could be the adoption of action-forcing mechanisms, such as last-best-offer arbitration, but more generally the peer review process and publication of MAP results may be the most effective in a big-picture way.[20]

Third, for potentially recurring disputes (either between a taxpayer and a tax authority or between tax authorities), a negotiated agreement between the taxpayer and the tax authority (or between the tax authorities) is best. If the decision truly is a mutual agreement, it is more likely to be applied in a future case. If a decision is forced on one or more parties, a dissatisfied party will want to re-litigate the issue at a later, more propitious time. On the other hand, if a dispute is unlikely to recur (e.g., the specific fact pattern or combination of countries is unlikely to occur again), then reaching a resolution that limits excessive taxation should be the goal, regardless of whether it is accepted by all parties.

Fourth, unless the taxpayer has full rights in the dispute resolution, the taxpayer must have the right to reject the proposed resolution of the competent authorities. To bind the taxpayer, the taxpayer must have full participation rights.

Finally, different types of disputes call for different types of dispute resolution mechanisms. For example, last-best-offer arbitration works very well when the dispute is among two parties. Ideally, the threat of a taxpayer invoking last-best-offer arbitration will cause the two tax authorities to come to an agreement prior to the onset of arbitration. If that does not happen, the arbiter will choose one of the tax authorities' positions, creating a clear winner and a clear loser. Last-best-offer does not work as well when there are three or more parties advocating different solutions. First, the inherent pressure to move toward the middle ground that last-best-offer arbitration offers in a two-party context does not work the same way in a multi-dimensional context, given the absence of a clear middle ground. Further, not all of the tax authorities have the same issues in dispute. Any proposed resolution of a dispute by some parties likely leaves out the resolution of issues important to another and omitted party.

Tax disputes are numerous and varied, and so the best means of resolving them will be numerous and varied as well.

Bilateral treaty disputes. For those disputes that are bilateral in nature and covered by a tax treaty, a mechanism for resolving cross-border disputes exists. Given the prevalence of tax treaties between major trading partners, this means that the bulk of cross-border disputes probably can be addressed through MAP. The primary focus of improving dispute resolution should be on finding ways to prevent disputes from occurring under bilateral tax treaties and ways to resolve such disputes when they unfortunately occur.

In that regard, it remains to be seen how effectively jurisdictions will implement the Final Report for BEPS Action Item 14, Making Dispute Resolution Mechanisms More Effective.[21] Generally, the report seeks to strengthen the effectiveness and efficiency of the MAP process, ''including the effective and timely resolution of disputes regarding their interpretation or application through the mutual agreement procedure.''[22] More specifically, it requires jurisdictions to commit to certain minimum standards, accompanied by a set of best practices, intended to ensure:

- that treaty obligations related to the mutual agreement procedure are fully implemented in good faith and that MAP cases are resolved in a timely manner;

[20] Indeed, the most recent OECD statistics on MAP show that a significantly higher percentage of cases received after January 1, 2016 (or the year a jurisdiction joined the BEPS Inclusive Framework, if later) were closed during 2018 than cases received prior to that date. The former cases are subject to more detailed public reporting, suggesting a real and positive impact from peer pressure and the potential ''naming and shaming'' of large backlogs. See ''Mutual Agreement Procedure Statistics for 2018,'' http://www.oecd.org/tax/dispute/mutual-agreement-procedure-statistics.htm.

[21] OECD (2015), *Making Dispute Resolution Mechanisms More Effective, Action 14 — 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/9789264241633-en.

[22] *Id*. at p. 9.

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- the implementation of administrative processes that promote the prevention and timely resolution of treaty-related disputes; and
- that taxpayers can access the MAP when eligible.[23]

Pursuant to the report, the Inclusive Framework on BEPS established a peer review process regarding MAP. It is still early in the peer review process, with only a few countries having been reviewed. One is the United States.[24] Based on the review of the United States, a jurisdiction will have a hard time meeting the minimum standards unless the MAP articles in its treaties are up-to-date and reflect the most recent OECD model language regarding MAP. For jurisdictions implementing the MLI with respect to most or all of their treaties, this condition is easily accomplished. For jurisdictions like the United States that are neither adopting the MLI nor speedily entering into new treaties, the limitations of "old" treaties will restrict the ability of taxpayers to have successful MAP outcomes, no matter how well-intentioned the competent authorities are.

Bilateral non-treaty disputes. Despite the prevalence of tax treaties, there will still be bilateral tax disputes not covered by a tax treaty. The two jurisdictions may not have a tax treaty, making implementation of an agreement between the two tax authorities difficult or impossible, even if they are able to communicate with each other. However, problems arise even when two jurisdictions do have a tax treaty. The particular dispute can be outside the treaty because the tax at issue is not covered in the treaty. This would typically be the case for a value-added or sales tax. It would also be the case for a subnational tax in those countries which, like the United States, generally do not cover non-federal taxes in their income tax treaties.

Alternatively, the taxpayer may not be eligible for the benefits of the relevant tax treaty due to the limitation on benefits provision or other anti-abuse rule. Or, the particular issue may be intentionally excluded from the treaty because it relates to benefits under a special tax regime or to certain types of residents of one of the jurisdictions. Even if it is appropriate to exclude such matters and taxpayers from the treaty, it does not change the fact that there needs to be a way to resolve bilateral disputes that cannot be resolved through MAP.

[23] *Id*.

[24] See *Making Dispute Resolution More Effective — MAP Peer Review Report, United States (Stage 2)Inclusive Framework on BEPS: Action 14, https://doi.org/10.1787/305147e9-en*.

Multilateral disputes. The more difficult case is multilateral disputes. Some of the solutions that work well in a bilateral context may not work in a multilateral context. As noted above, it is hard to see how last-best-offer works in multilateral disputes, except as a resolution to one aspect of a multilateral dispute, such as a zero-sum dispute between two parties in which the answer does not affect another party to the broader dispute. An arbitration approach involving all of the parties is more likely to reflect the big picture. Unlike arbitration (or a court decision) on different, narrow issues, a multi-sided dispute resolution permits a more holistic answer rather than a series of answers that may make sense when viewed in isolation but are unsatisfactory when put together, e.g., resulting in income taxed at a rate in excess of 100% or not taxed at all.

On the other hand, the more multi-sided and holistic the approach, the less likely the resulting answer will be consistent with any party's proposal, whether the taxpayer's or a tax authority's. That may be an obstacle, if not a barrier, for some jurisdictions: countries understandably may be reluctant to agree to arbitration if there could be wildly divergent outcomes. If the multilateral dispute arbiter has the ability to reach a resolution that differs from what any jurisdiction or the taxpayer advocated, one can imagine a country (or the taxpayer) getting a better result than it requested or a worse result than any other party requested. Given that the impetus of the BEPS Project was countries' desire to increase their revenues, a country is unlikely to sign up for a dispute resolution procedure that could put it in a worse position than was foreseeable when it began MAP.

This suggests somewhat of a dilemma. Multilateral arbitration or similar dispute resolution will not be widely adopted until jurisdictions subject to it have a higher comfort level in its application. But, taxpayers and jurisdictions cannot achieve that state without multilateral dispute resolution operating in practice and working out kinks, making improvements, abandoning counter-productive aspects, etc.

Still, jurisdictions will have no choice but to deal with this dilemma. The increasing number of disputes is a direct result of a course they chose to take when they signed on to the BEPS Project. Procrastinating will just result in a backlog of unresolved disputes. In that case, their only solace may be those of U.S. Supreme Court Justice Felix Frankfurter: "Wisdom too often never comes, and so one ought not to reject it merely because it comes late."[25]

[25] *Henslee v. Union Planters Nat'l Bank & Tr. Co.*, 335 U.S. 600 (1949) (Dissenting Opinion).

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