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International taxation aspects that affect management of the tax administrations

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INTERNATIONAL TAXATION ASPECTS THAT AFFECT MANAGEMENT OF THE TAX ADMINISTRATIONS

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ABOUT CIAT

CIAT is a public, nonprofit international organization established in 1967, with the mission of providing an integral service for the modernization, strengthening and technical development of the Tax Administrations of its member countries. Its membership currently consists of 39 member and associate member countries from four continents: 31 countries from the Americas, five from Europe, two from Africa and one from Asia. India and South Africa are associate member countries.

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TOPIC 1

DOUBLE TAXATION, INTERNATIONAL TAX EVASION AND TREATIES FOR THE AVOIDANCE OF DOUBLE TAXATION

Lecture

Topic 1

DOUBLE TAXATION, INTERNATIONAL TAX EVASION AND DOUBLE TAXATION AGREEMENTS - DTCs"

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Institutional Technical Coordination, Federal
Administration of Public Revenues
(Argentina)

Content: *Double taxation, international tax evasion and double taxation agreements - DTCs".- Case.*

Double (or multiple) taxation has negative consequences on normal international economic relations, not only because it distorts the efficient assignment of economic resources and investment decisions, but it also affects the reasonable and proportional tax burden of taxpayers, which must correspond to their specific taxpaying capacities.

Consequently, national states admit that the double international taxation must be eliminated or minimized through different mechanisms, such as a credit for similar taxes paid abroad or as the tax exemption for the foreign source incomes, or internationally agreed through double taxation agreements. These mechanisms or methods used to eliminate the international double taxation are a challenge for the national States to implement them, because they are an implicit cession or limitation for each state's sovereign power to define and apply taxation.

Regarding the agreements to avoid the double taxation, another issue is how the States parties will share the costs of the international double taxation elimination, in terms of smaller tax income, and political positions on issues such as giving priority to the territoriality criterion, or to the residence criterion.

It is clear that either criterion will depend on the particular situation of each country and its condition as exporter or importer of capitals. We can see that the OECD member countries have adopted the Tax Convention Model which, as stated by Vega Borego, substantially limits the taxation of incomes from territorial obligation and, consequently, the taxation based on the territoriality principle. This results from agreements granting the power for taxation to the State of residence or through the establishment of a taxation threshold to the source State[1].

The Republic of Argentina, as a developing country, negotiates its agreements to avoid the double taxation based on the United Nations Double Taxation Model, in which a significantly greater taxation power belongs to the source country and, consequently, a lesser sacrifice in tax collection is requested from the State of residence, which must eliminate double taxation through any of the two methods provided by the Model.

Regardless the development level of the countries signing a tax convention, and their political preference or negotiation position, they always accept to eliminate the distortions caused by international double taxation. States manage to differently decide a bilateral mechanism that distributes the tax burdens, the costs to eliminate the double taxation and the granting of credits or exemptions, by considering the legitimate recipients' benefits, of those who are residents in these countries.

This situation may be considered "normal", when States try to eliminate the double taxation, as well as to decrease the impact it generates on tax income, accepting concessions in favor of their counterparts. Nevertheless, nowadays tax administrations are frequently in contact, because they face situations in which "global taxpayers" use their talent to obtain tax benefits through legal maneuvers which are considered deceitful by the States since they don't respect the intentions of the negotiations and the tax agreements.

In 1978 Stanley Surrey stated that the United States complained that the first multinationals located there did not pay an adequate amount for interests, services or royalties and were not charging prices adapted to the products they were selling, On the other hand, the subsidiaries installed in the developing world had to support payments for excessive interests and royalties, and were paying for services that they did not receive and bought products at excessive prices. He concluded: "Clearly these two images cannot be describing the same *direct* transaction"[2]. He was referring to the sophisticated tax planning, which abuses the internal legislation, the tax agreements and the use of tax havens, which allow multinational investors to evade taxation both in their residence jurisdictions and in the markets in which they operate.

1 *Vega Borrego, Felix Alberto "THE CLAUSES OF LIMITATION OF BENEFITS IN CONVENTIONS TO AVOID DOUBLE TAXATION", p. 22. Legal investigation 1/03, Institute of Fiscal Studies, Madrid, 2003.*

2 *Surrey, Stanley S., "Reflections on the Allocation of Income and Expenses among National Tax Jurisdictions." (1978) 10 Law and Policy in International Business, pp. 431.*

This issue is not new, but the world-wide trend indicates that these types of behaviors are growing, both in magnitude and in sophistication.

In fact, aggressive tax planning is growing, and certain taxpayers with operations structured at global level try to access tax benefits of which they are not legitimate beneficiaries, because they are not residents in any of the States which are parties to a tax treaty. In other cases, residents of the States parties to the treaty use artificial structures in jurisdictions with opacity and low levels of taxation, to take advantage both in the source country and through deferral (or nonpayment) of the tax in the residence jurisdiction, resulting in what we call as double no taxation.

Allow me to explain this concept and the form in which it is considered in the administrative practice and in the Argentinian regulation. This phenomenon of the double no taxation derives from false returns or the use of legal structures in trading, with the objective to hide the reality or the economic purpose of the activities, relations or situations that affect the determination of taxes, and this is a straightforward international tax evasion.

I do not, of course, refer to the situations in which a taxpayer makes legal procedures which do not comply with the tax law, because in this case there is no determination of tax obligation or illicit behavior. I am referring to the verified illegal actions regulated in the law, and when these actions are performed using legal structures which do not represent this reality. In that sense, *avoidance* is characterized to interpret the validity of the action or its legal form which does not allows any fraud, and this is already covered by the Argentinian legislation.

Regardless the legal characterization of the behaviors generating the double no taxation, its existence can never be understood as the intention of the tax agreement signatory States, or as an implicit acceptance of a situation derived from the application of the agreement and their interrelation with the internal tax regimes of these countries.

The absence of taxation derived from the use of artificial legal structures in most countries is considered as an abuse of the legal system, an abuse of the internal legal regulations or an abuse of international treaties, and in such cases the international tax planning crosses the threshold of any legal system that tries to be fair[3].

3 *Vogel, Klaus. "Double Tax Treaties and Their Interpretation", Berkeley Journal of International Law, Bowl. 4, Issue 1 (1986), p. 79.*

In the same perspective, the Commentaries to Article 1 of the OECD Model, after mentioning the risk of abusive uses of the agreements by using artificial legal structures in order to obtain the tax benefits provided in the internal laws as well as the tax benefits from the double taxation agreements, highlights as general criterion that the States do not have to grant the benefits of double taxation treaties when there is evidence of abusive use of their provisions[4].

In regard to these commentaries, we must admit that the possibility to apply general anti abuse dispositions does not mean that it is not necessary to include specific provisions against certain forms of tax evasion in the tax agreements. One of these cases is the effective beneficiary clause. This clause, which application and interpretation has generated much legal discussions and academic controversies, is very useful to avoid this abusive use of these provisions in the agreements.

Currently, this clause is applied with a greater scope and form and I venture to say that it has obtained certain consensus on at least two basic aspects. One of them is to find a definition or an international independent meaning of this concept, regarding the context of this particular clause for the object of the treaty. That independent interpretation of the effective beneficiary concept is already present in the commentaries to article 10 of the OECD Model[5], in most of the specialized doctrine[6] and in the international jurisprudence[7].

The other aspect which has generated a certain consensus, at least at the tax authorities' level, is about the scope and meaning of this concept and its economic importance. When we refer to the effective beneficiary we should understand it as the one with rights to use and obtain income benefit (profits, interest or royalty) without being bound to any obligation to transfer the payment to another person. This limitation normally derives from a contractual instrument (legal documents) and also it can be from facts and circumstances that prove that the payment receiver does not

4 *Paragraphs 8 and 9, 4 of the Commentaries to the article the 1 of the "Model Tax Convention on income and property of the OECD", ps. 60-61. OECD Publications, Paris, 2010.*

5 *Paragraphs 12 of the Commentaries to the article 10 of the "Model Tax Convention on income and property of the OECD", ps. 187. OECD Publications, Paris, 2010.*

6 *Sees also Cordon Ezquerro, Teodoro "the effective beneficiary as anti-abuse provision in the CDIs", in 2nd IFA Regional Latin American Encounter 2010, p. 41. Argentine Association of Fiscal Studies, Buenos Aires, 2011*

7 *Indofood International Finance Ltd vs. JP Morgan Chase Bank N.A (Court of Appeals of the United Kingdom, 2 March 2006); Royal Bank of Scotland versus Ministry of Economy, Finances and Industry (Conseil d'Etat, 29 of December of 2006, No 283314); and Real Madrid F.C. versus National office of Inspection (National Hearing, July 18, 2006).*

have the free availability of the payments received, because he is limited by contractual obligations to yield it to another person[8].

This clause of the effective beneficiary is only one of the many provisions that countries use in their tax treaties to avoid abusive maneuvers and to prevent the fraudulent practices and the double no taxation. Of course, many approaches and special clauses are used in different tax agreements, trying to prevent specific abusive and evasion techniques. These clauses have been developed and improved with time in the different agreements and modifying protocols negotiated by the parties, in answer to the increasingly sophisticated and aggressive behaviors by the multinational groups and their tax advisory services.

These clauses, even if they are effective for preventing specific cases, they seem to be developed too slowly by comparison with the active and innovating behaviors observed in the harmful international tax planning area. They are not only developed by the tax planners' talent, but also by the innovations of multinational groups or global taxpayers.

In this context, it is important for our tax administrations to develop a joint operation framework to adjust the practices that each one develops in their national jurisdictions and to adapt them to the current global world, so that we can efficiently fight against avoidance behaviors of economic groups which plan their tax burden at world-wide level.

The strong impulse that the G20 has given to the effective international interchange of tax information has obviously contributed. The results that have been obtained thanks to the work of the Global Forum on Transparency and Exchange of information and the Revision of Pairs Group show the need for a global political support to the issues of international taxation regarding transparency. These results go from a spectacular increase in exchange of information agreements since the conformation of the present Global Forum in 2009[9], to the significant improvement in the commitments to transparency and cooperation demonstrated in many countries, which previously had been less favorable to tax information exchange.

We must also highlight the strong support to multilateral approaches in exchange of information, which are efficient solutions for a fast

8 *See document OECD MODEL TAX CONVENTION on the matter: REVISED PROPOSALS CONCERNING THE MEANING OF "BENEFICIAL OWNER" IN ARTICLES 10, 11 AND 12, in http://www.oecd.org/ctp/taxtreaties/Beneficialownership.pdf*

9 *See "The Global Forum on Transparency and Exchange of Information for Tax Purposes - Information Brief", en http://www.oecd.org/tax/transparency/Journalist's%20brief%20December%202012.pdf*

development of international cooperation networks[10]. In that sense, the Argentine tax Administration has noticed the requirements of the present international arena and has promoted the our country's entrance as first South American member to the OECD and Council of Europe Convention On Mutual Administrative Tax Assistance, after its modification and extension in 2010 (effective since 2011).

In addition to the cooperation and mutual assistance between tax administrations, it is necessary to develop a framework of coordinated action to fight against international evasion, for the benefit of the international community, because harmful international tax planning affects the tax interests of all countries, regardless their development level.

In that sense, with the support of the G20, the initiative for fighting the Base Erosion and profits shifting, known as BEPS, was launched. This OECD initiative tries to identify aggressive tax planning forms that are common to their member countries, to detect the causes that allow the erosion of the tax bases and to design common strategies to modify the legal schemes used by multinational groups to take advantage of existing legal gaps and to disarticulate fraudulent mechanisms. The innovative aspect of this initiative is the awareness of the harmful tax planning problem and the need to coordinate and structure solutions based on international cooperation, in order to obtain efficient results.

Tax administrations of countries that are not OECD members must also become involved in this or in similar initiatives, because tax planning schemes causing tax bases erosion and profits shifting affect all of us and solutions will come from the cooperation and design of common solutions.

In recent years, the Republic of Argentina made significant progresses for detecting and correcting some issues of aggressive tax planning, by the abusive use of benefits anticipated in agreements to avoid the double taxation. The successful solutions found resulted from unilateral initiatives of our country and not from coordinated schemes and this is why the withdrawal and renegotiation of some tax agreements is required. A description of some of the schemes and the applied solutions is presented hereinafter.

But before, we must keep in mind that the Argentine Republic is a developing country and, as such, a net capital importer, and this is why it is necessary to adopt coordinated evaluation mechanisms, in order

10 Sees on this matter the Final Official notice of the Meeting of Ministers of Economy and Presidents of Central banks of the G20, Moscow, 15-16 February 2013, paragraph 20.

to determine whether the tax sacrifice imposed by renouncing to the full taxation power through the application of the agreements to avoid double taxation is fair, since they were signed in different international contexts.

In that sense, it was necessary to perform a periodic follow-up of the tax implications of the mentioned agreements, as well as to carry out a multidisciplinary analysis and evaluation of the agreements, in force or in process, not only for the tax result but also for other macroeconomic aspects.

As a result, the Evaluation and Review of Agreements to avoid the Double Taxation Commission was created by the joint resolution Nº 56/2011 and Nº 80/2011 from the Ministry of Economy and Finances and the Ministry of Foreign Relations, International Trade and Cult. It includes an official appointed by the Minister of Economy and Public Finances, an official appointed by the Minister of Foreign Relations and Cult, and it is presided by the Federal Administrator of Public Revenue.

The main tasks of this Commission are the analysis and evaluation of the agreements to avoid double taxation in the following aspects:

a) The impact of the application of these agreements on the national taxation. In that sense, the tax cost resulting from the application of taxation limits in Argentina is analyzed, in comparison with the general tax regime included in the agreement. The higher tax income for the national administration resulting from computing similar foreign taxes is also taken into account, in application of the agreement.

b) The suitable and effective relation between the tax sacrifice and the objectives pursued when signing each agreement. This analysis is significantly more complex than the calculation of the tax cost derived from an agreement, because it involves a macroeconomic variable that will have to be weighed in order to obtain a correct representation of the reality under analysis and a reasonable result. Among the objectives of an agreement to avoid the double taxation is the offering of a stable and reliable legal tax framework by eliminating distortions that negatively affect the investment decisions in a developing country that tries to expand its productive resources through genuine investments.

Since investment flows between developed countries and developing countries are not balanced, is not difficult to understand that in this type of tax relations, the developing country will end up yielding tax collection, by limiting its taxation at source in application of the agreement to avoid the double taxation. This tax sacrifice will be, justified by the location of foreign investments since they considerably increase the economy, the industrial production and the employment. This analysis must be regularly performed in time, because the economic relations between the countries can significantly change and affect the validity of the referred tax sacrifice.

c) The possibility of generating an inadequate taxation by illegal application of the agreement: through harmful international tax planning, taxpayers take advantage of agreements to avoid double taxation and by using structures designed to obtain illegal tax advantages; they reduce or avoid their respective taxes. As we have seen, States do not sign the tax agreements improperly or abusively used and they have tools to avoid such abuses. However, in certain cases the judicial interpretations of innovative businesses forms in the modern global economy compel States to modify certain clauses in the agreements, to directly introduce new dispositions to end the inadequate application of the agreement.

d) It is possible that the application could lead to double no taxation under the domestic legislation of the contracting states. After the signature and entry into force of an agreement to avoid double taxation, States can introduce modifications to their internal legislation that affect or modify the application of the agreement, as they were previously determined and agreed by the parties in the negotiation. For example, this is the case if one of the States introduces exemptions or preferential treatments which modify certain definitions in their national legislation that directly affect the concepts used in the agreement. In such cases, these legal modifications should be analyzed since they may be susceptible of an appropriate interpretation, allowing the application of the provisions so they do not modify the intention of the treaty and the expectations of the parties or, on the contrary, if it is necessary to negotiate a modification of the agreement or withdraw from it.

Based on the relevant information, the Commission performs a periodic follow-up of tax implications within the agreements to avoid double taxation and proposes, based on the resulting evaluations, the respective actions, such as: partial modification, complete renegotiation or withdrawal from the existing agreements.

On the other hand, the Commission also analyzes the negotiation proposals received from countries interested in signing this type of agreement with Argentina, through the Ministry of Economy and Public Finances or directly through the Commission.

As a result of this Commission's work, for example, a conclusion was reached that certain tax treaties required partial modifications in order to maintain the above mentioned balance between tax sacrifice and economic benefits. Hereinafter are presented some detected schemes:

CASE 1:

As a result of investigations, it was found that different Argentine taxpayers used the provisions of a double taxation agreement to elude payment for property taxes and taxes on profits from investments securities from resident entities in the counterparty of the treaty. In that particular case, the agreement established the exclusive taxation in the source country, both for the source income as well as assets located in this jurisdiction. This way, the Argentine taxpayers transferred the obtained income from a third jurisdiction (triangle them through low or zero taxation countries), through companies in the counterparty of the tax agreement.

The use of the general anti-abuse provisions of the Argentine internal legislation (article 2 of the Law 11,683 of Tax Procedure, which establishes the principle of the economic reality) was possible, given the circumstances of a limited exchange of information with that jurisdiction and the fact that it involved entities formally constituted according to the country's legislation, but due to the size of the tax loss it was politically decided to denounce the referred bilateral instrument.

It should be noted that the truth is, this decision to denounce was based on the abusive use of the terms of the agreement which, as mentioned before, only allowed the property taxation at the source by resident entities in a contracting state (including the state itself), through the total conversion of the Argentine taxpayers investments at the closing of each fiscal year for the preferred securities.

CASE 2:

Tax planning manoeuvers were detected by using clauses from an agreement to avoid the double taxation, which provided for tax exemption at the source in the case of royalties. The investigations performed gave hints that different multinational companies in third countries would have constituted subsidiaries in the counterparty of the agreement to elude the payment of the profits on royalties at source, using different concepts.

Once the subsidiaries were constituted, the intangible goods that gave rise to the payment of royalties were assigned and this way the taxation at source previously applied to the respective payments was avoided. Given the limited exchange of information with the counterparty, it was not possible to obtain the necessary evidence against those maneuvers by using the general anti-abuse clauses of the Argentine legislation. For such reasons and given the magnitude of tax damage, it was decided to end the application of the agreement.

There were also other additional reasons to end this agreement, for example the impossibility of applying the taxation at source with respect to capital taxes on stocks and shares in Argentinian companies and enterprises.

CASE 3:

In another case, from investigations performed made by the acting control unit, the illegal use of an agreement to avoid double taxation was detected, in which a taxpayer who could not benefit from its provisions, took control of these benefits through of a company in the other contracting State, distorting the object and aim of the treaty. In this case, the agreement provided the exclusive taxation of property taxes on the company shares in the shareholder or partner`s residence state.

Thus, until a determined date, the shares of an Argentinian company belonged to a taxpayer located in a third country. Complying with the current legislation, the Argentinian company made the payment of property tax as responsible substitute.

However, later, the mentioned shares package was transferred successively to a company located in a country with no tax opacity and shortly after to a holding company located in the counterparty of the agreement. This situation allowed the Argentinian company to avoid paying the property tax on the shares by abusive application of the agreement.

In this case the general anti-abuse clause of the Argentinian legislation was applicable, in the understanding that conditions of treaty abuse were met, i.e.:

- The main objective of the transaction was to obtain the more favorable tax treatment; and
- The benefit of the more favorable tax treatment is against the object and purpose of the respective treaty provision.

In order to avoid the reproduction of this type of behaviors, the renegotiation of the agreement was decided.

As previously mentioned in these situations, the task of the Argentinian Tax Administration to identify and prevent evasion and abusive use of agreements to avoid double taxation has intensified in the last years through Evaluation and Review of Agreements to avoid Double Taxation Commission's actions. The main data source of this Commission is the information from data bases of the Argentinian Tax Administration and their efficient use through crossings of information and sector enquiries.

These data bases are also fed with the information regimes established by the strategic regulations issued by the Argentinian Tax Administration. Some of those information regimes are:

The GR 3364/12 is an information regime on all economic operations, whichever their nature is, free of charge, arranged between residents in the country and those who act as representatives of external taxpayers or entities.

The GR 3293/2012 establishes an information regime on the ownership of shares from Argentinian companies and enterprises, as well as civil associations, foundations, and some common investment funds, which have to act as information agents.

The General Resolution 3312/12 establishes an information regime that will have to be fulfilled by agents that act as financial or non-financial fiduciaries for trusts constituted in the country, as well as by the taxpayers resident in the country that are trustees/fiduciaries or similar, trustees/settlors or similar and/or beneficiaries (beneficiaries) of trusts (trusts) constituted abroad.

The GR 3421/2012 establishes an information regime for financial entities by law Nº 21,526 and its amendments, where the operations performed by nonresident taxpayers should be informed through the mentioned entities. Nonresident subjects are those determined by the profit tax regulations. The following are excluded: governments from other countries and their dependencies (central banks, etc.); international organizations and their subsidiaries or agencies. Operations in the regime are:

1. The payments, profits and fees paid to the nonresident taxpayers through these entities, regardless their nature.
2. The investments or assets of these taxpayers in the mentioned entities.

Finally, the Commission's work directly affects the decisions related to the negotiation of Argentinian tax agreements. This policy has been varying in the last years, due to the emphasis given to the new development approaches implemented in our country, which the tax policy has been part of.

Within the negotiation policy guidelines, we must highlight our country's new vision promoted in the last negotiation (or renegotiation) proposals for the agreements to avoid double taxation. This new vision implies carrying out a periodic inspection of the tax treaties clauses, to the light of the effects of their application in comparison with the parties' expected results at the time of the negotiation.

Since the main objective of the agreements to avoid double taxation is to prevent distortions in the development of goods and services exchanges and the capitals, technologies and people's movements, the elimination of this obstacle of double taxation should favor an expansion of the economic relations between the signatory countries.

Given that the distribution of the taxation decided in an agreement to avoid double taxation implies a renouncement to a tax resource, and a higher one for the developing countries that do not preserve their power of taxation at source, that fiscal sacrifice must be correlated with a greater development of international investments and the consequent beneficial effects in employment and development.

The new approach that Argentine is introducing is a reference to the possibility for a periodical revision of the agreement to the light of the mentioned objectives. The parties will have to also determine the periodicity of the revisions as well as the detail that they wish to include in the definition of parameters used to evaluate the fulfillment of these objectives. In summary, beyond the fact that the possibility for revision is a right of the parties based on their sovereignty, it is understood that it is very useful to include in the treaty's text that parties admit a relation between the elimination of the double taxation and the development of economic relations among them.

CONCLUSIONS:

Based on the previously mentioned considerations, we can notice that the fight against international tax evasion is a hard work that seems to reach deeper levels of complexity as new forms of structuring transnational businesses are developed. When the maneuvers of international tax evasion involve the application of agreements to avoid double taxation, which only or main objective is to obtain a double no-taxation, the complexity of the tax administrations' task increases, because the guarantees and rights of the taxpayers must be respected, as well as the international commitments assumed by the countries in the negotiations of tax treaties.

This complexity is perfectly well-known by the multinational groups and their tax advisers in charge of their global business tax planning. Sophisticated tax engineering structures take advantage of this situation, exceeding the individual capacities of tax administrations, which operate only within the limits of their national jurisdiction.

In that sense, an efficient and necessary solution to the tax reality of this globalized world is within the international cooperation and the identification of common problems that affect countries with different development levels. The adoption of homogenous coordinated solutions to legal and administrative issues, with are closely related, is very important.

There is no doubt, this task is not simple. But the size of the aggressive tax planning problem requires an answer of equal proportion by tax administrations. That answer must be based on countering the development of fraudulent schemes and abusive use of tax agreements, and also in the design of exemplary sanctions for the most aggressive behaviors of harmful tax planning.

Summary

Double (or multiple) taxation has undoubtedly a negative effect on international economic relations. Nevertheless, the double no taxation effects are also important, as well as harmful tax planning.

If these double no taxation phenomenon derives from false returns or from the use of inadequate legal structures or from inappropriate business practice, it is not different from plain international tax evasion. In that sense, avoidance is characterized to interpret the validity of the action or its legal form which does not allows any fraud, and this is already covered by the Argentinian legislation.

In that sense, the Argentinian Republic has decided to create a Commission to Evaluate and revise the Agreements to avoid Double Taxation, with the purpose to perform a periodic follow up of the tax consequences in the mentioned agreements. It also performs a multidisciplinary analysis and evaluation of the agreements, in force or in process, proposing the adoption of integral and coordinated evaluation mechanisms.

These are to determine if the tax sacrifice by the application of agreements to avoid double taxation is justified.

Similarly, within the new negotiation policy guidelines for tax agreements, Argentina proposes a new vision that implies carrying out a periodic inspection of the tax treaties clauses, to the light of the effects of their application in comparison with the parties' expected results at the time of the negotiation

Finally, it is essential for our tax administrations to develop a joint operation framework to adjust the practices that each one develops in their national jurisdictions and to adapt them to the current global world, so that we can efficiently fight against avoidance behaviors of economic groups which plan their tax burden at world-wide level. In that sense, the Global Forum on Transparency and Exchange of information, the Group of Revision of Pairs, as well as the OECD initiative in the fight against the Base Erosion and profits shifting (BEPS), is all developing very important tasks.

Lecture

Topic 1

DOUBLE TAXATION, INTERNATIONAL TAX EVASION AND DOUBLE TAXATION CONVENTIONS (DTCs)

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Content: *1. Areas of work for the focus group # 1 on anti-abuse measures. 2- The work of the focus group # 2 on territoriality.-3. Issues of transfer pricing under the focus group 3*

The evolution of the economy, particularly marked by the increasing internationalization of business and the strengthening of the strategic importance of intangible assets (patents, trademarks, etc.), has increased opportunities for tax planning for businesses.

For tax administrations the issue is to fight against this tax evasion, paying attention not to create double taxation, which is unfavourable to the development of international trade, but also with the aim of eradicating cases of double non-taxation.

In response, during the summit held on 18 and 19 June 2012 in Los Cabos, the Heads of States and Governments of the G20 countries, at the initiative of France and the United States, requested the Organization for Economic Cooperation and Development (OECD) to propose an action plan against the erosion of bases in terms of corporate tax and transfer of profits (Base Erosion and Profit Shifting -
BEPS). OECD presented a document about this issue to the Finance Ministers in Moscow on 14 and 15 February. It will present in June 2013 a roadmap on possible options.

These works, organized by the OECD, are made in three groups.

The first group examines more particularly the topics relating to anti-abuse measures, the packages based on differences of qualification between states (hybrid), the abuse of conventions, the deductibility of payments and the preferential regimes. The second group carries out reflections on the rules of territoriality and more precisely on the notion of permanent establishment, withholding, the concept of residence, the tax regimes of the controlled foreign corporations. Finally, the third group focuses its

1. AREAS OF WORK FOR THE FOCUS GROUP # 1 ON ANTI-ABUSE MEASURES

In order to limit the erosion of the bases, the first working group focuses on the strengthening of the measures that, in tax treaties and national laws, help to fight against abusive schemes and to prevent the tax-free transfer of the profits towards States where they will be submitted to little or no tax.

It also deals with the regimes designed and implemented for aggressive tax competition.

France is involved on this issue within the OECD through its chairmanship of the Forum on harmful tax practices.

In the frame of the BEPS project, France wants to promote the strengthening of the actions undertaken, in particular by extending this approach to third countries, which seems to be winning a consensus within the working group.

The first consideration concerns the harmful tax. The challenge is to move beyond a purely legal analysis of preferential arrangements, to take an interest in their economic effects and their use, especially by proposing broader criteria (vehicles for tax minimization, regimes that foster transactions for tax purposes).

France stands up for an approach that better takes into account the real economic effects of the tax measures to assess their own damaging features, by overcoming their legal characteristics.

The second axis of work focuses on the analysis and the search for joint solutions against strategies based on asymmetries of qualifications between different national laws and treaty provisions.

These asymmetries render possible the formation of hybrid structures (equity loans, transparent companies, permanent establishments, etc.). designed to lead to situations of either double non-taxation or double deduction.

The third issue is to review the national legislations on abuse, in order to recommend their strengthening. On this point, the solutions seem to lie in a commitment of the States to improve their systems. In addition, the Member States of the European Union will increasingly fall within the limits of the jurisprudence of the Court of Justice of the European Union.

Finally, the BEPS approach can and must be accompanied by action at EU level.

Indeed, the current functioning of the European internal market amplifies, by promoting the elimination of double taxation and economic freedoms, the optimization strategies identified in the BEPS diagnostic, while depriving the Member States of the margins to counter this phenomenon individually.

This has enabled in particular the emergence within the EU of "tunnel States" used to enable the tax free output of profits to tax havens by taking advantage of the European law, the various laws and the provisions of some particularly favourable tax treaties (phenomenon known as treaty shopping, including in the Netherlands).

Therefore, the challenge is to go beyond the simple coordination to achieve a legislative package:

- A draft directive specific to the digital sector, separate from the debate on the Directive on the common consolidated corporate tax base, and proposing the creation of a virtual European permanent establishment, in order to spread the benefits of this sector between the Member States in which these firms operate, will they be physically present or not;

- The strengthening of the existing Directive 2003/43 EC, relating to payments of interest and royalties in order to condition the exemption from withholding tax at a minimum effective taxation in the Member State of the recipient;

- The definition by the legislator of a European anti-abuse clause that goes beyond what the ECJ currently allows the Member States to do in their national laws;

- A legislative initiative to solve the problems of hybridisation when they can not be solved through coordination;

- The definition of a rule ensuring effective taxation of profits going out of the EU and allowing the source States to regain their right to taxation when a profit, thanks to the derived and conventional laws, circulates free of tax within the EU internal market and exits without actually being taxed;

- The adoption of a safeguard clause to limit the effects of the free movement of capital, currently granted to third States without compensation.

2. THE WORK OF THE FOCUS GROUP # 2 ON TERRITORIALITY

Work on the rules of territoriality of corporate income tax includes a reflection on the concept of permanent establishment, which allows taxing the activity of a company in a state where it does not have its headquarters.

Currently, the characterisation of the existence of a permanent establishment relies on the presence of material, technical and human means and resources and the ability of these means and resources to commit an enterprise from a State towards its customers on the territory of another State. However, activities are now developing, particularly lucrative, which can be performed through modern means of communication without having human and material resources on a specific territory.

The evolution of the rules only proves necessary in the case of volatile activities, hardly attributable to a territory.

This is the case with digital companies' activities. Thinking on the rules provided by tax treaties to allocate the right to tax some of these non-physical operations, and the separation of these from traditional notions of residence and permanent establishment, now appears necessary.

However, companies like some states do not want to face flat rate approaches, disconnected from well established tax concepts.

As regards withholding taxes, the OECD model recommends an exemption to limit cases of double taxation. Thus, the vast majority of tax treaties concluded by France provides either an exemption or a limitation in the rate of applicable withholding tax to5% or more rarely 10%.

France supports a case-by-case approach of the level of withholding taxation with respect to non-EU States depending on the local taxation level and strives to changethe rules designed to fight against double exemption situations in the EU.

Finally, France can not but endorse proposals of reflections on the evolution of someconcepts (such as residence) to restrict in some instances access to benefits provided by the treaties, including treaty based reductions or exemptions on withholding tax (front companies without economic substance, symbolic flat rate taxation ...). They fully meet our concerns already included in many of our tax treaties

3. ISSUES OF TRANSFER PRICING UNDER THE FOCUS GROUP 3

The growing internationalisation of business and groups restructuring, as well as the rise of the strategic significance of intangible assets (patents, trademarks, etc.) have multiplied the opportunities for corporate tax optimisation.

Transfer pricing is a stake and an allocation tool for the tax base between states. In order to ensure avoidance of double taxation for companies, domestic laws adopted by states are now governed by the OECD standard based on arm's length principle.

The first discussion addresses the relevance of the arm's length principle itself.

The alternative options to this principle consist in establishing a flat rate method for profit allocation between states. This method either depends on a unilateral determination by each State of the level of profits it considers should be attributed to it or on the application of an allocation key based upon objective criteria (assets localised in each state, domestic turnover, amount of wages therein paid ...) to a group worldwide profits.

However, the first alternative would likely result in double taxations, going backwards from development of international trade targets.

For its part, setting allocation keys would result in a project of an unprecedented magnitude, both materially and technically. In addition, objective criteria may, more than the arm's length principle, be likely not to match the reality of the profit made on a territory: a group can operate in an area while locating most of its payroll and intangible assets in low tax burden states. The criterion of turnover can also promote certain markets.

However, it is clear that in some situations the implementation of arm's length principle based on the sales comparison approach comprises such practical obstacles that it hinders the control and the fight against tax evasion. It should then be looked for specific solutions to address these special difficulties.

The second discussion relates to intangible assets. As a matter of principle, France is committed to the completion of work on the intangible assets, but in compliance with the arm's length principle.

OECD's Secretariat, in the preparatory documents, suggests a broadening of the definition and an evolution of the treatment of income derived from intangible assets under transfer pricing (sharing of economic ownership within the group).

France supports a limited evolution of standard which should be technically robust, so as to avoid any unilateral arbitrary statist approach. Recognition of the existence of an intangible asset may be based on a legal analysis of the concept of assets likely to benefit from some form of legal protection (intellectual property law, commercial or competition law). The income derived from them should be taxed in the state of legal ownership, unless abusive situation.

4. ISSUES RELATED TO THE TAXATION OF THE DIGITAL ECONOMY

France is currently thinking about the taxation of digital economy. In this purpose the Minister of Economy and Finance, Pierre Moscovici, commissioned a report in July 2012 to Pierre Collin, State Councillor, and Nicolas Colin, Inspector of Finance. This report provides a detailed picture of the rise of the digital economy and calls for new tax regulations, in particular for budgetary reasons.

The digital revolution calls entirely into question our understanding of value creation. The digital economy is indeed based on traditional production of goods and services activities. But increasingly, seeding start-up companies or global firms dealing with hundreds of millions of users overturn the rules of the game and radically alter every sector of the economy.

Even though the digital economy now affects billions of people its added value slips out of our hands. How it is organized, its powerful network effects and the extent of externalities caused by its business models circumvent the rules of added value. The number of terminals and connected objects increases exponentially, the time spent using them is experiencing sustained growth, entertainment, purchasing and production, are now held in a digital economy that penetrates everyone's daily routine.

Yet a significant part of the created value is collected by companies benefiting from preferential tax regimes. Large firms in the digital economy pay almost no taxes anymore.

1 - The digital economy presents characteristics and obeys logic radically different from mature activities

Firstly the digital economy is accelerating the pace of innovation and dissemination of new goods and services. Thus, such an application as Facebook has gained 1 billion users in less than eight years.

The digital economy channels massive investments financed by venture capital firms which select businesses that successfully generate returns offsetting the failures of others.

The digital economy often leads to the acquisition of a dominant position covering various related markets.

The digital economy is built on a model of reinvestment of most profits, rather than distributing dividends, shareholders are obtaining their remuneration by potential capital gains.

The digital economy is perpetually evolving so that it is difficult to identify areas of stability to establish a tax.

The digital economy constantly disconnects the place of establishment from the place of consumption. It is increasingly difficult to spot the created value and to apply to it the rules of tax law henceforth inadequate.

2 - Large firms in the digital economy make profits by exploiting data from regular and systematic monitoring of user activity

Data, including personal data, are the key resource of the digital economy. They allow companies that collect them to measure and improve the performance of an application, to customize the service, to recommend purchases to customers, to support innovative efforts giving rise to other applications, to make strategic decisions. They can also be valued by licensing them to third parties.

In short, it is the lever that enables large digital companies to achieve greater scales and a high degree of profitability.

Yet data collection is based on the free labor provided by users. Through regular and systematic monitoring of their online activity, applications' user data can be collected without any compensation. This lack of compensation partly explains the striking productivity gains in this economy. Is it normal that companies established in a territory do not contribute to the tax revenue of the state where their customers live and contributed to generate profits?

Attracted by the quality of the interfaces and the network effects, users become, through this data, output auxiliaries and create value generating profits on the different sides of the digital economy's business models. Yet the activity of applications' users is enabled and tenfold by public expenditures especially in education, social protection and deployment of networks throughout the territory of a State.

3 - Digital technology gradually devours every sector of the economy

The intermediation model that predominates the digital economy guts the tax base.

Thus, online advertising allows redirecting the consumer to a provider established in another State. Transactions between individuals get growing.

In addition, digital sector companies exert downward pressure on prices. The margin of companies established in a territory declines as the position of the digital intermediate is becoming inevitable and it is essential for a supplier to be indexed.

In tourism, banking, telecommunications, automotive, health, digital economy's companies are currently inserting themselves into the value chains. They focus their efforts on a strategic link, make their users work and capture a growing share of the margin of local enterprises.

As the digital technology spreads throughout the economy, the margins of the various sectors will relocate abroad and disappear from the GDP of some countries depriving public authorities of the tax revenue needed, particularly in times of crisis or to contribute in funding development.

4 - A common feature of global firms of the digital economy is the low level of taxation of their profits

Even if they are not alone in practicing tax optimisation, firms in the digital economy have more opportunities to benefit from the competition states are engaged in.

Instruments which the multinationals rely on to reduce their effective tax rate are well known.

- The reclassification of certain activities in the value chain to reduce profit andto ensure the absence of permanent establishment: the transformation of adistribution subsidiary into a mere commission agent reduces its turnover to its sole margin and minimizes the business risk associated with its activity.

- The strategic location in some states in order to enjoy tax benefits from legislations or conventions. National schemes may allow a more favourable taxation for holding companies, intellectual property rights or research and development activities. Legal asymmetries in terms of deductibility of loan interest make it possible to reach situations of double non-taxation of some profits. Finally, some states called "tunnel states" do not practice withholding tax on profits transferred to tax havens.

- Centralisation of intangible assets in the country where the income tax is the most advantageous. In the functional analysis of a multinational group, ownership of intangible assets is the main characteristic of entrepreneurial functions. So-called routine functions are compensated by a steady and minimal profit while entrepreneurial functions capture the residual profit, albeit volatile but potentially higher.

- Optimisation of transfer pricing practiced among the different entities of a group is all the easier that practicing some small variations on a multitude of transactions groups can significantly reduce their overall tax rate.

So it is easy for digital companies to transfer their profits in tax havens by paying intangible assets the value of which is tenfold by the returns to scale.

Since these profits do not result in a dividend payment, they can be retained and reinvested without being subject to tax.

These companies focus the activity from which they earn their income on territories where it is easier to transfer profits to tax havens. The "double Irish arrangement" and the "Dutch Sandwich" and its variants are apparently implemented by most of these companies.

The increasing dominance of intermediaries business models allows companies described as prime contractors to capture a growing share of the margin at the expense of other actors in the chain of value creation.

Newly established, digital companies immediately were organized to get the most ofdifferences between States tax systems, including choosing the one where they set their headquarters, localize their assets or their employees.

5. The national and international tax law is struggling to adapt to the effects of the digital revolution

In principle, the bilateral model tax treaty established by the OECD to prevent double taxation situations, assigns the authority to impose the profits to the State in which the company has its headquarters.

There is an exception to this rule in the presence of a permanent establishment on the territory of another State. However, the concept of permanent establishment refers to that of fixed place of business or dependent agent which involve both the tangible presence of buildings or people. It is proving inadequate to the digital economy.

Although since 2003, it is recognized that a server, where a software application is hosted and through which it is available, may constitute a fixed place of business. But the OECD considers the data and computer code do not constitute a permanent establishment due to their intangible nature.

In Europe, the debate on a Common Consolidated Corporate Tax to eliminate tax competition does not advance and does not take into account the specificities of the digital economy. Within the OECD, thinking has just begun.

At the national level, the first attempts to create a specific tax for the digital economy have missed their target.

6. States should be able to tax the profits that are made on their territory by digital economy companies.

The need to find the power to tax corporate profits of the digital sector companies must be satisfied with strategies that operate on several grounds.

In the short term, tax audits can enable to:

- highlight permanent establishments thanks to the analysis of the reality of theactivity in a localised area, either by demonstrating that the subsidiary is a fixed place of business from which the operations of the foreign company are made, or by demonstrating that it is actually a dependent agent with authority to engage theliability of the foreign company to carry out its operations.

In this regard, the comments on section 5-5 of OECD model convention indicate that the agent has actual authority to conclude contracts when soliciting and receiving orders without formally finalizing them and when the foreign company does nothing but approve foreign transactions routinely.

- In case of treaty shopping, it is possible to apply a withholding tax if the beneficial owner of the royalties is located in a State to which it is applicable.

In the longer term the conventional way can be used, either bilaterally or through a multilateral convention whose provisions would replace the bilateral agreements.

The income tax seems the most appropriate tool to search for a contribution in proportion to the value creation in a localized area.

This requires a concept of territoriality adapted to the digital economy.

But a reflection on the rules of territoriality is probably not sufficient, it is also important to think about the determination of transfer prices based on various factors of production that contribute to the value creation in the digital economy.

In conclusion, the digital economy is far from being the most difficult to control by tax authorities, it is abundantly commented and digital workflows are measurable. What remains to be done is to bring out valuation rules accepted by all.

Case Study

Topic 1.1

INTERNAL REGULATIONS TO PREVENT INTERNATIONAL TAX EVASION

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Content: *1. Extension of the scope of the already existing legal rules on tah havens.- 2. Introduction of new legal basis*

The topic we are to discuss about is to be examined keeping in mind that is has been analyzed by the OECD – that released several reports on this – and, at the top level, by the G20 meetings, moving from the one held in London in April, 2009.

Thus, a coordinate framework of actions undertaken by the international community appears, aimed both at promoting tax transparency and tackling economic and financial crisis.

Then, no domestic position, regulation or elsewhere is defined in my country disregarding this framework; moreover, the European Union policies and regulations must be considered, too.

Due to all this, my Country, strongly emphasized the fight against tax havens over the last years, which has become one of the main objectives of its economic-fiscal policy.

In view of the above, significant and fast changes occurred in our domestic tax laws, entailing a general enhancement of the legislative system in place against misuse of tax havens, both through:

1. the extension of the scope of already existing rules;
2. the introduction of new rules.

We shall now analyze the two areas as follows.

Now, the first area to be considered is, as I said before, the

1. EXTENSION OF THE SCOPE OF THE ALREADY EXISTING LEGAL RULES ON TAH HAVENS

For starting, I must say what a tax haven is according to Italian legislation.

The Italian tax system draws up **lists of countries**, whose legal and regulatory frameworks can be exploited to commit tax evasion.

In detail, the reference standard is made up of three ministerial decrees in which about **70 foreign legislations** are considered not in line with some our specific tax rules.

The first set of rules that have been updated is related to the so called

a. Participation Exemption - Pex

In conformity with other fiscal legislations of industrialized member Countries, the Italian Government established a tax exemption system for revenues of companies holding stakes in other businesses.

To this end, the so called participation exemption – also known as PEX – was introduced. As a result, the capital gains obtained from shares or stakes in companies or other entities, may, if some requirements are met, be deducted from taxable income.

Since 2003 – when this rule entered into force - the rate of exemption of these capital gains changed several times. The current exemption rate is very high, as it arises up to 95% of the value of capital gains.

For obtaining the exemption, a stake – holding company must not resident of a State or territory having a privileged tax system, that is a tax haven.

Furthermore, demonstration must be given that the profits from the stakes have not been placed in States or territories in which they are subjected to privileged tax systems (tax havens, again).

Then, in few words, no benefit (no exemption, in this case) is allowed if any link exists between the stake holder and a tax haven.

An additional aim of this rule should be considered, that is promoting the setting up in Italy of holding companies, both foreign and domestic, preventing at the same time, the abuse of off-shore entities.

Our law is now very similar to those already existing in other countries on the same topic of participation exemption.

Eventually, the rule also aimes at avoiding any double taxation of profits from stakes holding, as taxation is only established in respect of the legal person which ontaines the profit, and not in respect of the natural person who transfers the stakes.

The second issue in the area is related to the so called

b. Controlled Foreign Company (CFC)

For the purpose of preventing any misuse, whereby a foreign company in which a stake is held, located in tax haven, does not carry out an actual activity but is set up solely for hiding the incomes of a legal or natural person, the Italian legislator provided for the taxation of the incomes of any company, in which a stake is held, having domicile in tax havens.

Such a provision is given in most of tax legislations of the OECD Countries, even if with distinctive features, State by State, according to the taxation approach of the different fiscal systems (“transactional approach”, “entity approach”, “global approach”).

Then, according to the Italian law, the incomes of a CFC based in a tax haven are taxed in Italy, and related taxes must be paid by the resident controlling entity.

Obviously, to this end the requirements of the absence of an actual economic activity in the tax haven and of a mere passive utilization of the sources of income (so-called passive income) in the foreign State must be met both.

In Italy, the specific CFC legislation provides for the direct allocation to the shareholding entity of the incomes of its own controlled entity, regardless for the actual distribution of such proceeds: this makes useless for fiscal purposes, at the same time, both the foreign corporate screen (so-called base company), and the formal fragmentation of the group in legally independent entities.

Art. 13 of Decree-Law 78/2009 furthermore prescribes that, by analogy and harmonization with the provisions already in place in other European systems, in order to prevent undue tax arbitrages, the schemes which may favour disparities of treatment, with particular regard to infra-group operations, must be checked in order to assess whether such transactions are real or fictitious.

Moreover, the law includes in the scope of application of the rule those companies that are located in Countries which, even if not falling within the black list, may be deemed to have privileged taxation.

Such extension occurs for the CFCs which benefit from an actual taxation lower for more than half of the Italian one, and profit mostly from passive incomes or which carry out mainly services in favour of companies belonging to the same group.

The third point to be discussed is

c. The Non-Deductibility Of Costs Scheme

Italian tax legislation also provides for the non-deductibility of the costs deriving from transactions held between resident businesses and entities based in States or territories outside the European Union and having privileged tax systems.

The aim of the rule is to prevent the erosion of taxable base, implemented through transactions carried out with companies or professionals based in black list territories which entail the assignment of costs – and as a result, an undue reduction of taxes - to the Italian taxpayer, whereas the related income would not be taxed in the foreign jurisdiction, or it would be with very low rate.

However, the Italian taxpayers are granted the possibility to “overcome” the related legal presumption if they are able to demonstrate the truthfulness of the activity carried out by the foreign subject with whom business relations have been held.

So, this is a typical case in which the burden of proof is inverted, as no activity must be done by the Tax Administration for tax assessment purposes.

The fourth item is the

d. ADAPTATION TO OECD DIRECTIVES IN THE FIELD OF TRANSFER PRICES DOCUMENTATION

A domestic law in 2010 aligned the national legislation in the field of transfer prices documentation to the OECD directives and to the principles of cooperation between taxpayers and financial Administration. In view of this, a rule was included providing, in the cases of adjustment of the normal value of transfer prices practiced in the framework of operations with non-resident entities, the non-

applicability of the relevant penalties if the taxpayer, also when a tax audit is on-going, delivers to the Tax Administration documents showing the conformity of the normal price with the transfer prices themselves.
Next topic is

e. False personal residence

In our fiscal legislation people are considered resident in the territory of the State when, for the greater part of the tax period, anyone of the three following conditions occurs: entry in the registers of resident population; domicile in the territory of the State under the civil code, or the residence in the territory of the State under the civil code.

On the other hand, the Tax Administration does not need give evidence the of any of the aforementioned conditions in relation to Italian nationals struck off the Registers of resident population and emigrated to a tax haven.

This is due to the fact that, in 1999, the legislator has introduced an inconclusive legal presumption of residence in Italy of such subjects. In this case, the burden of proof is established upon the taxpayer, with whom lies the obligation of proving the truthfulness of the relocation abroad.

This legislative solution has been adopted in order to strengthen the system in place to counter the phenomenon of relocation abroad of natural persons, i.e. the fictitious moving of the residence in States with privileged taxation schemes, solely for fiscal saving purposes. It is a rule widely criticized in regard to legitimacy and fairness, also in consideration of the fact that, whereas for persons, also non-nationals, entered in the register of resident population, the registration has the validity of conclusive presumption, for those nationals who entered the Register of Italians Residing Abroad, this presumption has the validity of inconclusive presumption.

The monitoring of the transfers of residence abroad of natural persons forms subject matter of close attention on the part of the Italian legislator; article 83 of decree-law 25 June 2008, n. 112, indeed prescribed the carrying out of control plans in respect of the tax and contributive requirements for non-resident subjects, as well as the obligation for Municipalities to confirm to the competent Revenue Agency Office, within 6 months of the application for inclusion in the register of Italians residing abroad, that the applicant has actually ceased the residence in the national territory; it is also established that for the three-year period following the aforesaid application, the actuality of the cessation of residence in the national territory is under the surveillance on the part of the Municipalities and the Revenue Agency.

Last topic in this first area I related to

f. Company fictitious tax residency abroad and trusts

In the same way as natural persons, also in the field of tax residences for entities and companies, the domestic legislation, continuously evolved, legislator, aimes at tackling the abuse of abroad residency, especially as “fictitious tax residency abroad”. The usual outcome of such a misuse of residency allows the taxpayer to not comply with the domestic tax obligations and, on the other hand, to benefit from a more favourable tax regime than the Italian one.

To this purpose, in the same way as for natural persons, also for entities and companies specific provisions were introduced, establishing several inconclusive presumptions regarding the residence, lying upon the principle known as substance over form, regarding particular juridical institutes which, according to the national and international experience have shown that they can be used for the setting up of “fictitious tax residency abroad” schemes.

Reference is firstly made to the trusts: Italian law foresees two cases in which an inconclusive legal presumption of residence in Italy can be applied to foreign trusts established in countries that do not allow an adequate exchange of information. The first case is the one in which at least one of the transferors and at least one of the beneficiaries are Italian residents; the second one occurs when a resident natural person has arranged, in favour of the trust: transfer deeds of the property right on real estate; and: establishment or transfer of real estate rights, also for shares. Such provisions aim at countering possible forms of abuse, with elusive purposes, in the use of these mechanisms of asset segregation, as the expected result is taxation in our country incomes produced in the country itself by trusts established in tax havens.

Now, I am going to explain the second main area of activity of the Italian Government and Parliament, related to the

2. **INTRODUCTION OF NEW LEGAL BASIS**

The first item is the

a. Art. 12 of legislative decree 78/2009.

This rule set up in 2009 an inconclusive presumption according to which the financial investments and activities held in the States or territories with a privileged tax regime (tax havens), in violation of the declaring obligations regarding tax monitoring, are considered established through non-taxed income.

At the same time, harsher penalties for violation of the tax monitoring obligations were introduced.

The rule Art. 12 was adopted with the purpose - explicitly stated by the rule itself – of implementing the understandings reached between the O.E.C.D. concerning the surfacing of economic and financial resources held in Countries having privileged tax systems.

The discovery of investments and financial assets in black list Countries, besides triggering the inconclusive presumption described above, determines the application of doubled penalties compared with those ordinarily decreed for tax offences, and as a result the range of the penalties is between 200% and 480% of due taxes.

Additionally, if the income has been produced abroad, the penalties are furtherly increased by a third.

Furthermore, the deadline for tax assessment is doubled in comparison to the ordinary one, and as a result it extends until the eight year after the one in which the tax declaration was submitted to the Tax Administration (or was to be submitted).

Finally, the penalties established for the violation of the tax monitoring were doubled too, and as a result they must be determined in such cases from 10% up to 50% percent of the amounts not reported in the tax return.

The second point is related to

b. Communication obligations

The law foresees that the VAT taxpayers must inform the Tax Administration of all the sales of goods and services rendered and received, registered or subject to registration, to economic traders located, residing or domiciled in countries indicated in the domestic black list through a specific form, that must be electronically sent within the last day of the month following the period of reference.

Moreover, recently, the reporting obligation has been extended to some typologies of supplies of services territorially not relevant in the State for VAT purposes, but that are particularly relevant in the prevention and fight against VAT frauds.

Eventually, a Law Decree of the year 2012 removed the obligation to notify the Tax Administration of any transfers of goods and supplies of services done and received, registered or subject to registration, for business operators having office, residence or domicile in privileged taxation Countries, in all cases of operations for amounts lower than 500 Euros.

The very last topic is the

c. Contractors' blacklist

In the framework of some recent decisions mad ad international level, and with specific reference to the initiatives adopted by the G20 in the mentioned Summit of July 2009, the national legislator introduced a new legal provision in public contract matters: this provision meets the need to ensure full knowledge of the property and management of entities entitled to take part in the procedures called by the contracting entity in accordance with the national legislation. This also aims at ensuring equal conditions for entities participating in public calls for tenders.

So, the companies having their headquarters, residence or domicile in blacklisted countries are allowed to taking part in public calls for tenders concerning works, services and supplies, but they need a preliminary authorization released by the Ministry of Economics and Finance, based upon an application submitted by the company itself.

Case Study

Topic 1.1

INTERNAL REGULATIONS TO PREVENT INTERNATIONAL TAX EVASION

Beatriz Gloria Miguel
General Director, State
Agency of Tax Administration
(Spain)

Content: *Internal regulations to prevent international tax evasion*

First I would like to thank CIAT and the Argentine Administration for this kind invitation to participate as a speaker at this CIAT Assembly.

The Assembly has focused on an extraordinary important issue such as international taxation and how it affects the tax administrations management.

Economic and technological changes have led to a world where borders have stopped being as tight as before. The transit of goods and persons are now much easier than two decades ago. The pressure of the markets has led our countries to reduce our fiscal barriers for foreign trade by eliminating tariffs through bilateral, regional or global agreements. This change basically started last century and it is a small one if we compare it with the great digital revolution we are in now.

We have also been witnesses of the capital liberation process which does not find obstacles for its free movement. And with such liberalization, the possibility for capital flight increases.

These permanent changes in the economic reality require our tax administrations to be more aware of these changes in order to adapt to the taxpayers' new behavior.

We are currently facing an economic reality which offers more favorable alternative tax regimes to the taxpayer. This has been a widespread concern among tax administrations, stated in various specialized forums, such as the BEPS (Base Erosion and Profit Shifting), an OECD initiative or the action plan to strengthen the fight against fraud and tax evasion presented by the European Union.

Due to this internationalization of the economy, many companies not only look for profits through a better economic organization of goods and services, but try to have tax advantages by using, sometimes abusively, inconsistencies in domestic regulations and conventions to avoid double taxation, seeking to create opportunities for what has been called the double non taxation.

This activity is based on the elimination of the tax base elements in such a way that essentially artificial connection points are created, for breaking down the tax base into its different components and to establish them where the greatest tax benefits can be obtained.

The classic example is to artificially search for the generation of deductible expenses for interest payments on investments in a country while for various reasons the income resident in another country is not computed in the tax base: The result is the double advantage from a deductible expense in a jurisdiction with an income that is not taxed in another jurisdiction.

This reality has been shown by international initiatives such as those of the OECD and the European Union, which try to address this issue in a comprehensive way from different perspectives, but considering the need to respond to this situation.

The OECD has created several working groups, involving several of the countries present here, which will report to the fiscal affairs Committee the results of their analysis. The OECD fiscal affairs Committee will adopt an action plan according to these findings.

The European Union has also undertaken the fight against fraud and tax evasion through aggressive tax planning by measures aimed to promote the implementation of minimum standards of good governance in the tax area by third countries. It has also submitted an action plan with a set of measures to reinforce the fight against fraud and tax evasion.

Not only International organizations are addressing this problem. Each of us, in our domestic environment, is suffering the consequences of these abusive and often fraudulent behaviors that undermine our tax bases and, in the current crisis and budgetary austerity context, makes tax fraud more reprehensible than ever.

For that reason, in Spain we have undertaken a reform to keep our legal system in the forefront of the fight against fraud.

But, without being exhaustive, throughout my presentation I'm going to focus on the four most important measures.

The first three are of material nature and the fourth is organizational.

First, the most striking measure has been the regulation to comply with **information on goods and rights located abroad.**

Such obligation has been established in the additional 18th provision of the General tax law (hereinafter LGT), introduced by article 1, section 17 of the law 7/2012: This provision establishes the obligation to file an annual information statement on accounts, securities and real estate located abroad for persons and entities resident in the Spanish territory.

This measure intends to serve as a seal against the fraudster who would receive income from abroad, would not declare it and would wait for the prescription period to put the profits in accounts or assets abroad, out of the scope of information and actions of the Spanish Treasury.

This measure will be reinforced by the tax information that the Administration expects to obtain through bilateral or multilateral instruments of cooperation that are already in force, and the agreement signed with the United States for the application of the FATCA regulations and the improvement of international tax compliance.

The tax information exchange agreements recently signed along with the renegotiation of the exchange of information clause in some old conventions establish the appropriate legal framework for the exchange of tax information which has surged in recent times as the undisputed protagonist in the fight against harmful tax competition, tax fraud and tax evasion.

Furthermore, the agreement reached with the United States, which will enter into force in the coming months, opens a new perspective by facilitating the information on financial investments by Spanish residents in the United States. At the same time, we are sure that the FATCA initiative will help us to have the same information not only from United States but also from other countries, based on the most-favored-nation clause of the FATCA agreement or on the European Union legislation.

But this does not preclude Spain from strengthening its legislation to avoid the assets relocation problem, either as a result of prior tax fraud or just to prevent the global integration of the income that such assets may produce.

The obligation to report refers to three elements:

- Accounts in financial institutions located abroad.
- Assets, rights, insurance and income deposited, managed or obtained abroad.
- Real estate and rights over immovable property located abroad.

1. ACCOUNTS IN FINANCIAL INSTITUTIONS LOCATED IN FOREIGN COUNTRIES,

a) Are required to report:

- Individuals and legal entities resident in the Spanish territory, non-residents permanent establishments and entities of art. 35.4 LGT (unsettled estates, community estate, and other bodies which having non-corporate status, make up a separate financial asset unit which is liable to tax)

The obligation will be effective when by December 31 of each year they are:

- Holders or real holders of accounts located abroad (art. 4.2 Law 10/2010),

- Representatives, authorized or beneficiaries or power holders over accounts. This is to avoid the use of proxies allowing hiding the true owner.

This obligation also affects all those who have been holders at some point during the year. This provision seeks to avoid that by December 30 they are dismissed as holders and on January 1 the holder is replaced with the corresponding power.

b) Data to report:

Account identification data: entity, opening or closing date and balance at December 31, and the average balance from the last quarter of the year.

c) Do not have the obligation to report:

- Entities exempt from article 9.1 of the revised Text of the corporate tax law (hereinafter TRLIS) (State, autonomous communities, local entities...)

- Entities and individuals with economic activity having accounts registered individually in their accounting. We are trying to avoid new obligations to those who normally comply; the purpose is to only affect “non-reported” accounts.

- Accounts which balances or their average balance for the last quarter by December 31 do not exceed jointly 50,000 euros. If any of those limits are exceeded, all accounts should be reported. Here the aim is to prevent fraud through numerous accounts with balances less than €50,000. On the other hand, a €50,000 limit prevents from numerous people from having to report accounts abroad, such as for the studies of their children abroad

d) Term for submitting the statement.

Between January 1 and March 31 of the year following the required information

e) Submission of subsequent years

Once the yearly statement is submitted, there is no obligation to report in successive years, except if the joint balances until December 31 (average balances in the past quarter) exceed 20,000 euros increase in regard to those in the last statement.

The report must also be submitted when the holder, representative or authorized person is replaced.

2 ASSETS, RIGHTS, INSURANCE AND INCOME DEPOSITED, MANAGED OR OBTAINED ABROAD

a) Are required to declare:

- Individuals and legal entities resident in the Spanish territory, non-residents permanent establishments and entities of art. 35.4 LGT (unsettled estates, community estate, and other bodies which having non-corporate status, make up a separate financial or asset unit that are liable to be taxed)

The obligation will be effective when by December 31 of each year they are:

- Holders or real holders of accounts located abroad (art. 4.2 Law 10/2010),

- Representatives, authorized or beneficiaries or power holders over accounts. This is to avoid the use of proxies allowing hiding the true owner.

This obligation also affects all those who have been holders at some point during the year. This provision seeks to avoid that by December 30 they are dismissed as holders and on January 1 the holder is replaced with the corresponding power.

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Account identification data: entity, opening or closing date and balance at December 31, and the average balance from the last quarter of the year.

c) Do not have the obligation to declare:

- Entities exempt from article 9.1 of the revised Text of the corporate tax law (hereinafter TRLIS) (State, autonomous communities, local entities...)

- Entities and individuals with economic activity having accounts registered individually in their accounting. We are trying to avoid new obligations to those who normally comply; the purpose is to only affect “non-reported” accounts.

- Accounts which balances or their average balance for the last quarter by December 31 do not exceed jointly 50,000 euros. If any of those limits are exceeded, all accounts should be reported. Here the aim is to prevent fraud through numerous accounts with balances less than €50,000. On the other hand, a €50,000 limit prevents from numerous people from having to report accounts abroad, such as for the studies of their children abroad

d) Term for submitting the statement.

Between January 1 and March 31 of the year following the required information

e) Submission of subsequent years

Once the yearly statement is submitted, there is no obligation to report in successive years, except if the joint balances until December 31 (average balances in the past quarter) exceed 20,000 euros increase in regard to those in the last statement.

A statement must be submitted when the holder is replaced.

3 . REAL ESTATE AND RIGHTS OVER IMMOVABLE PROPERTY LOCATED ABROAD.

a) Are required to declare:

- Individuals and legal entities resident in the Spanish territory, non-residents permanent establishments and entities of art. 35.4 LGT (unsettled estates, community estate, and other bodies which having non-corporate status, make up a separate financial or asset unit that are liable to be taxed)

The obligation will be effective when by December 31 of each year they are:

- Holders or real holders of accounts located abroad (art. 4.2 Law 10/2010),

- Representatives, authorized or beneficiaries or power holders over accounts. This is to avoid the use of proxies allowing hiding the true owner.

This obligation also affects all those who have been holders at some point during the year. This provision seeks to avoid that by December 30 they are dismissed as holders and on January 1 the holder is replaced with the corresponding power.

b) Data to be declared:

Account identification data: entity, opening or closing date and balance at December 31, and the average balance from the last quarter of the year.

c) Do not have the obligation to report:

- Entities exempt from article 9.1 of the revised Text of the corporate tax law (hereinafter TRLIS) (State, autonomous communities, local entities...)

- Entities and individuals with economic activity having accounts registered individually in their accounting. We are trying to avoid new obligations to those who normally comply; the purpose is to only affect “non-reported” accounts.

- Accounts which balances or their average balance for the last quarter by December 31 do not exceed jointly 50,000 euros. If any of those limits are exceeded, all accounts should be reported. Here the aim is to prevent fraud through numerous accounts with balances less than €50,000. On the other hand, a €50,000 limit prevents from numerous people from having to report accounts abroad, such as for the studies of their children abroad

d) Term for submitting the statement.

Between January 1 and March 31 of the year following the required information

e) Submission of subsequent years

Once the yearly statement is submitted, there is no obligation to report in successive years, except if the joint balances until December 31 (average balances in the past quarter) exceed 20,000 euros increase in regard to those in the last statement.

The report must also be submitted when the holder is replaced.

But the most relevant modification is not the introduction of a new information obligation but the **effects or consequences established by the law in case the obligation to report is not fulfilled.**

First, the noncompliance to report is a very serious infringement and the penalties are €5,000 for each piece or set of data relating to a non-reported asset or incomplete, inaccurate or false reported data, with a minimum of €10,000. If it is reported out of term without prior notice to the administration, these quantities are reduced to €100 per data or set of data with a minimum of €1,500.

Second consequence: This is the integration of the value of the assets or rights on the income tax of individuals and corporations that should have been reported and was not.

Article 39.2 of the income tax Law establishes that in any case, the tenure, declaration or acquisition of goods or rights that have not fulfilled the obligation of information in the established term shall be considered as unjustified capital gains and the value of such assets or rights will be taxed as an additional element of the general taxable base.

Article 134.6 of the corporate tax law establishes a similar provision that goods and rights not reported by taxpayers in the time limit set for this purpose will be understood as being acquired through unreported income which will fall within the oldest tax period subject to regularization.

Third consequence: This is the offence provided in the income tax for integrating the unjustified gain and in the corporate tax for unreported income from value of the non-reported properties or rights. It is qualified as a very serious tax infringement, and punishable by a proportional fine of 150 percent of the base amount sanction.

The basis of the sanction will be the amount of the total tax without taking into account for its calculation outstanding compensations, deductions or applications from earlier exercises or from the period subject to verification that could lower the taxable base or the total tax.

Second. The second measure refers to **a limitation on the deduction of financial expenses in the corporate profit tax**. This reform places us in line with the legislative trend existing in States within our economic environment.

Limitations on deductions of financial expenses with insufficient economic cause were already applied by the Inspections in cases where this practice was detected. The use of mechanisms or financial schemes that did not respond to economic criteria has been a very common practice in the large companies, using these tactics causing an abusive erosion of tax bases. Notwithstanding that the judgments of the courts of Justice have been favorable to the restrictive interpretation implemented in the tax inspections, it seemed appropriate to line up with other neighboring countries and provide greater legal certainty for taxpayers. This has been done through a regulatory amendment in two ways.

First of all, article 14 of the TRLIS which regulates non-deductible expenses has been modified. An item has been added which states that financial expenses generated within a commercial group, and intended for certain transactions (the purchase of shares in capital stock or own funds of any type of entities to other entities of the group and contributions in capital or own funds to other companies of the Group) between entities from the same group will not be tax-deductible.

This specific rule introduced in the law has two main aspects that I would like to comment.

On one hand, it achieves a greater equality, since until now, only those who had used these tricks and were subject to a review by the tax administration could be subject to correction when the inspection proved that there was not a valid economic reason. This is a disadvantage for those who had been inspected with respect to those who, having done the same thing, had not been inspected yet. Therefore, the amendment provides a normative interpretation of the previous law that had been already implemented by inspection with the courts approval.

On the other hand the rule admits the possibility for those financial expenses to be qualified as deductible expenses but only whenever the taxpayer shows that there are good economic reasons for such operations. In fact, this implies to continue admitting intra-group financing but subject to a reversal burden of proof, since the taxpayer is the one who must now prove that there is a valid economic reason for making such financing. Before, in case of controversy, it was the Administration that had to prove that there was no valid economic reason.

Secondly, there has been a modification in article 20 of the TRLIS, which formerly regulated the sub-capitalization rules, by redrafting it under the statement of limitation on the deductibility of expenses.

The general principle is that the net financial expenses will be deductible with a limit of 30 percent of the operating benefit of the exercise. This limitation becomes, indeed, a specific imputation rule, allowing the deduction of future periods excesses (for the following 18 years). It also sets a threshold that softens the limitation since it states that in any case, net financial expenses from the tax period amounting to EUR 1 million will be deductible.

This measure favors indirect business capitalization and responds, with figures similar to our comparative law, the current tax treatment of financial expenses in the international arena.

The financial expenditure percentage limitation shall not be applied to credit entities or to those which are not part of a group unless they have a direct or indirect participation exceeding 20 per cent.

Third. There is another regulation, with a more internal than international character, but which as a result of fraud in other countries, can also help to prevent money-laundering in Spain. I mean the **limitation of cash payments** established in article 7 of the law 7/2012, October 29.

In accordance to that article, operations in which any of the parties involved act as an entrepreneur or professional may not be paid in cash, for an amount equal to or greater than 2,500 euros or its equivalent in foreign currency.

However, the amount will be 15,000 euros or its equivalent in a foreign currency when the payer is an individual who justifies that he has no fiscal domicile in Spain and does not act as entrepreneur or professional.

Regarding operations which may not be paid in cash, those involved shall keep the payment vouchers for a five years period from the date thereof in order to prove the payment was not done in cash. They also must provide these documents to the State tax administration agency upon request.

To avoid the common fraud consisting in fractioning the payment of operations, the Law requires accumulating all fraction payments from goods or provision of services. The limitation shall apply according to the accumulated amount.

The sanction provided in the rule is 25 per cent of the amount paid and can be required for both the payer as well as for the one who receives such payment.

As I have already mentioned the essential purpose of the rule is to make more difficult the money-laundering or the use of capital irregularly obtained, either in Spain or abroad.

Fourth. The fourth adopted measure by the Spanish tax administration has been organizational and consist in the **creation** of an Office highly specialized in taxation for international operations; **the National Office of International Taxation** will part of the Financial and Tax Inspection Department of the Tax Agency.

The tax agency had already adopted years ago organizational measures to respond to specific challenges as a result of the internationalization of our economy. The two most relevant were the creation of the National Bureau for Fraud Investigation (ONIF in Spanish) and the creation of the Central Unit of Large Taxpayers.

The ONIF includes two special units for international issues within its specialized units.

The first one is the Central information Team which among its activities includes the liaison office, Central Liaison Office (CLO), to meet the demands for information derived from agreements to avoid double taxation, as well as the Exchange of Information Agreements and those according to the European law regarding direct taxation, taxation of savings as well as the value-added tax. The requirements of safety and efficiency deriving from the international information exchange advised to centralize this operational unit in a few specialized bodies that would also assume the internal task to deliver the demands and responses to the competent territorial bodies according to the affected taxpayer.

The second specialized unit was the creation of a team dedicated to the fight against the value added tax fraud within intra-Community transactions (between Member countries of the European Union), which replies to similar units from other countries of the European Union. Their main characteristics for specialized knowledge, national competence, coordination with equivalent units from other Member States of the European Union and the territorial units in Spain have been considered essential for their operation.

On the other hand, the creation of the Central Department for Large Taxpayers was the administrative response in order to give a differentiated treatment to taxpayers who by their size and entity could not be treated by territorial units. It has been a satisfactory experience and the specialization of the integrated units allows the relationship with large taxpayers to be more fluid and effective.

The strong internationalization of the Spanish economy in recent decades has caused the international component to affect, in more cases and in higher amounts, the taxable bases. The international conventions network to avoid double taxation has substantially grown, as well as the rules to be applied in cases where the international component affects the tax base. The Ministry of finance in recent years has made great efforts to improve the staff training about this new reality. Hundreds of officers have taken specialization courses in international taxation. But even with this response, the administration requires additional steps to insert this high specialization in an organizational scheme that would provide a coordinated response from the tax agency to the internationalization of our economy.

In this context, and based on the structures of neighboring countries, on April 1, 2013 the National Office of International Taxation was created, with a nationwide jurisdiction for the management, planning, impulse and operational coordination in the matter, and is a support to other units. It also has a unit of economic and financial appraisals with tax relevance.

The National Office of International Taxation is part of the Financial and Tax Inspection Department of the Tax Agency and reports directly to the Director of the Department.

Currently 30 highly specialized officials are in the office although it is expected that in a short period of time 20 additional officials will be incorporated. Specializing in international taxation, foreign language skills, negotiating skills and coordination ability will be highly valued elements for the Office’s staff selection team.

The main activity of the Office is the international related transactions and the analysis of transfer pricing applied, as well as the non-residents taxation.
It should be remembered that in non-resident taxation, the Spanish tax system has a peculiarity that taxes income obtained in Spain from non-residents, whether individuals or companies; it is a separate tax, independent, regulated by law different from the tax law that taxes income from individuals and companies.

We are confident that this organizational change allows the Spanish tax administration to strengthen its effectiveness and its commitment to effectively apply the legislation of international taxation and prevents abuses that erode our tax bases and attempt against free competition between complying companies

I conclude by confirming my belief that the effective response to international taxation challenges may not be faced by each country in an isolated way. The answer is based on three main axes, information, legislation and the application of the rules.

Without information it is impossible to manage taxes and in case of international operations, that information must come from third parties. Tax administrations should support the international initiatives in favor of the information exchange and we should reorganize ourselves for an effective information exchange.

National authorities and international organizations should ensure an appropriate legal framework to tax international operations based on the real possibilities of the involved parties, both taxpayers and administrations.

Tax administrations must organize to implement rules to facilitate voluntary compliance and detect and react against noncompliance, and within the international environment, a balanced and fair cooperation must exist between us.

Case Study

Topic 1.2

EFFECTIVE APPLICATION OF ANTI-ABUSE CLAUSES TO AVOID DOUBLE TAXATION

Carlos Alberto Barreto
Secretary of Federal Revenues
(Brazil)

Content: *Introduction.- 1. International Context.- 2 Anti-abuse clauses in the conventions to avoid Double Taxation.- 3. Developments in administrative litigation in Brazil.- 4. The Brazilian case-application of the substance over form principle and results of fighting abusive tax planning.- 5. Excerpts: profits abroad through indirect subsidiaries. - 6. Challenges of tax administrations.*

INTRODUCTION

The increase in the international flow of income arising from services, interest, dividends and royalties has led to opportunities to decrease the tax burden of taxpayers through tax avoidance or evasion1. These tax advantages not only cause losses in tax revenue, but also competitive imbalances, both in the country of the investor as well as in the investee country. The large international capital mobility, together with the intangibility of transactions involved in revenues, have raised challenges for tax administrations to fight abusive tax planning using related parties abroad.

Within the framework of international organizations, there is a global trend to fight abusive tax planning involving the use of several countries, causing, among other effects, the erosion of tax revenue base and adverse effects on local competition. The Organization for economic co-operation and Development – OECD recently published a report

1 *Tax evasion is the practice of an unlawful act, by which the taxpayer violates tax liabilities, providing false statements or directly disobeying the law. On the other hand, tax avoidance corresponds to practice a lawful act, by which the taxpayer wants fiscal savings by using a Transaction or structure which makes a specific tax rule no longer applicable. Internationally, this practice occurs through manipulation of facts or creation of structures in a given territory, in order to influence the characterization. The term "tax avoidance" does not necessarily correspond to any irregular or improper tax planning. Therefore, given the scope of the expression, it is necessary that its interpretation is always within a context, and never in a separate way.*

on Addressing Base Erosion and Profit Shifting 2 which concludes in the need of a greater dynamism and co-operation between tax administrations, both in regards to the update of the legal bases, as well as in terms of exchange of information and adoption of effective and integrated anti-abuse measures in fighting this type of practice.

Often, this type of tax planning is accomplished using conventions for the avoidance of double taxation. A clear purpose of the conventions is to promote freedom of investment decisions by eliminating international double taxation. Furthermore, its objectives also include the prevention and the fight against abusive tax planning and international tax avoidance.

1.INTERNATIONAL CONTEXT

The global financial crisis of 2008 led to hardening the fight against tax avoidance and evasion, given the difficulty of Governments to provide a favorable environment for investments without compromising the tax base. At the G-20 meeting held in London in 2009, leaders expressed the importance of adopting measures to fight abusive tax planning, through the adoption of countermeasures such as: request for greater transparency by taxpayers and financial institutions; taxation at source on payments; non deductibility of expenses paid to residents in uncooperative jurisdictions and review of policies and conventions to avoid double taxation.

Another point worth mentioning is the effective fight against international tax planning through conventions for the avoidance of double taxation such as the work of the Global Forum on Transparency and exchange of information for tax purposes (Global Forum).

With the standards established by the Global Forum, the exchange of information has become a more solid and efficient instrument in fighting the abusive use of conventions.

Without an intense and coordinated information exchange, the fight becomes unsuccessful, since obtaining data about parties abroad depends mainly on the cooperation from foreign tax authorities. The work of the Global Forum can make tax administrations identify hidden structures and international operations before the control. Undoubtedly, it is an essential factor in the fight against the abusive use of conventions.

2 *OCDE, 2013, Addressing Base Erosion and Profit Shifting - BEPS*

2. ANTI-ABUSE CLAUSES IN THE CONVENTIONS TO AVOID DOUBLE TAXATION

Since 2003, the Tax Affairs Committee of the Organization for the Economic Co-operation and Development (OECD) comments on art. 1 of its Model Convention stand towards the existence of a general principle of the conventions to avoid double taxation, whereby their benefits should not be applied when the main purpose for certain operations is to ensure a more favorable tax position, contrary to the objective and purpose of the Convention.

According to the OECD (paragraph 22 and 22.1 of the comments to article 1rst), rules that offer ways to fight abuse of treaties as "the principle of substance over the form", "economic substance" and "general anti-abuse rules" do not conflict with the treaties.

Thus, when analyzing a supposed conflict of a particular situation with the treaties, the following must be reminded:

(i) the benefits of a Convention should not be applied when the main purpose is to ensure a more favorable tax position
(ii) (ii) the purpose of a Tax Convention is to avoid double taxation and not promote the "double taxation", and
(iii) (iii) the Convention does not exclude the application of domestic anti-abuse rules.

In Brazil, in 2001, the single paragraph of art. 116 was inserted in the national tax code (CTN), establishing that "the administrative authority may disregard acts or legal transactions carried out for the purpose of disguising the taxation event or the nature of the constituent elements of the tax obligation, in compliance with the procedures established by the ordinary law". In spite of the law referred in the clause, which has not yet been issued, the control of the Federal Revenue Service has discussed, in certain cases, situations that may intend to basically reduce taxes, and the anti-avoidance principle stated in the CTN has been adopted in judicial and administrative tax litigation decisions, in favor of the Public Administration when there is evidence of avoidance.

3. DEVELOPMENTS IN ADMINISTRATIVE LITIGATION IN BRAZIL

Until 2003, the Administrative Council of Tax Appeals (CARF), the second instance in the Brazilian tax litigation, adopted a more formal position in their trials. Since 2004, the CARF made changes of its position and has held infringement notices issued by the Brazilian tax authorities based on mechanisms to fight the abuses such as fraud to law, simulation, abuse of rights and discussion about the purpose of negotiations. In these courts, there are possibilities of abusive tax planning both internal (not involving parties abroad) and external.

In cases such as operations routinely called "House and separates" (Constitution and changes in corporate membership with only one day apart, for exclusive tax saving purposes), retroactive incorporation (companies with huge accumulated losses incorporate large and profitable companies, when the opposite would be more probable) and the registration of legal entities without economic substance in countries with which Brazil holds treaties have been analyzed considering more the principles involved and the substance of negotiations rather than just formalities and mere legal compliance.

This fact demonstrates a clear change of approach of Brazilian judges who are applying typical mechanisms and mainly from countries governed by common law systems in a civil law country.

4. THE BRAZILIAN CASE-APPLICATION OF THE SUBSTANCE OVER FORM PRINCIPLE AND RESULTS OF FIGHTING ABUSIVE TAX PLANNING

An emblematic case of Brazilian litigation concerns the attempt by the taxpayer, to use a Convention for the avoidance of double taxation between Brazil and Spain, aiming at preventing the taxation on income arising from a third company, Spanish subsidiary, established in Uruguay, a country with which Brazil has no treaty signed.

According to domestic legislation, the profits of a subsidiary of a Brazilian company abroad are subject to taxation by the internal revenue service of Brazil. The particular situation involved a Brazilian "Company A", who owned a direct subsidiary in Spain ("company B"), a country with which Brazil has signed a Convention for the avoidance of double taxation. "Company B”, in turn, had two direct subsidiaries "C" and "D" in Uruguay and Argentina, respectively. The Brazilian taxpayer argued that, as a result of the Treaty with Spain, the profits of its indirect subsidiary in Uruguay ("company C") would be free from taxation in Brazil, since the link between the Brazilian company would only be with the "Company B”, located in Spain.

The second instance of administrative litigation has considered that the Treaty with Spain could only be used to exempt from taxation its own operating profits of "company B", in the amount of R $ 80,562.176,03. The result of the indirect subsidiaries, for a total value of $ 1,456,791,283 .68, should be taxed in Brazil, since there is no Convention for the avoidance of double taxation between Brazil and Uruguay, country where the indirect subsidiary "C" is located.

The specific case reported above is described with more detail in Judgment No. 101-97,070 CARF. The following are excerpts from the trial with the reasoning used by counselors:

5. EXCERPTS: PROFITS ABROAD THROUGH INDIRECT SUBSIDIARIES

With the aim to apply art. 74 of the provisional measure No. 2,158-35, the results of indirect subsidiaries are considered directly received by the Brazilian investor and their taxation in Brazil is not subject to the rules of the international treaty signed with the country of residence of the direct-controlled one, especially when these results were not produced in operations carried out in the country of residence of the subsidiary, showing the tax planning for not taxing them in Brazil.
(...)

"The applicant cannot invoke in his favor the Treaty signed between the contracting States, that aimed to avoid double taxation of profits earned by residents of the respective States in order to obtain a tax saving resulting from profits earned by other controlled/interconnected company residing in a third State and which are not entitled to benefit because of its substantial situation."
(…)

"In fact, there is no way to consider under the Brazil-Spain Treaty, profits earned in a third country without a Treaty, which is just like crossing one of the Contracting States, since by the rule stated in art. 7 of the Treaty, the profits earned through another legal entity, in which the subsidiary or affiliate abroad keep any type of corporate participation, even if it is indirectly, they will be considered in the balance sheet for corporate purposes, as well as, for the purpose of determining the taxable income and the tax base of the CSLL of beneficiary in Brazil. " (Judgement No. 101 CARF-97,070-process nº 16327.000530/2005-28)

* MP-Provisional Measure

Since 2010, approximately R$ 30 billion (US$ 15 billion) related to cases of abusive tax planning (national and international) have already been released, considering, among others, the substance principle over form. The developments in litigation have demonstrated the importance of this principle, reflecting the number of cases held in with taxpayers.

6. CHALLENGES OF TAX ADMINISTRATIONS

On the international scene, Tax administrations have the challenge of dealing with the reality of a globalized world, without imposing unnecessary barriers to the capital flow, giving the desired tax neutrality in the natural economic formation processes of transnational groups, preserving the basis of each State.

In this context, it may be necessary to review the principles for a new paradigm in treaties, discussing mechanisms to avoid both double taxation and double non-taxation.

Another important point to be studied is the search for more objective criteria for the standardization of international regulations, such as transfer pricing. The growing stream of income from interest, royalties and intangible services impose challenges to bring objective solutions on matters that often lie in the subjectivity field.

Finally, there is a need for a commitment for establishing a convergence to an international standard that facilitates the exchange of information between tax administrations. Only with an effective flow of information and cooperation between the worlds it is possible to fight international planning.

TOPIC 2

CONTROL OF TRANSFER PRICING

Lecture

Topic 2

CONTROL OF TRANSFER PRICING

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(CIAT)

Content: *Introduction. 1. Heterogeneous region. 2. Legislations for controlling the abusive transfer pricing manipulation. 3. Principle and methods for transfer pricing control. 4. Transactions subject to the transfer pricing system. 5. Related party concept. 6. Comparability adjustments. 7. Burden of proof. 8. Income tax exemption vs. TP Systems. 9. Income tax exemption vs. TP Systems. 10. Simplification Measures. 11. Administrative aspects. 12. Conclusions.*

INTRODUCTION

The purpose of this presentation is to disseminate some of the main results of the Study on "The control of transfer pricing manipulation in Latin America and the Caribbean" prepared by CIAT, GIZ[1] and BMZ[2] within the framework of the "International Tax Compact" (ITC[3]) initiative and published in December 2012.

The reason why the aforementioned institutions joined, within the framework of ITC, was the need to count on a single document that would provide detailed legal and administrative aspects regarding the control of abusive transfer pricing manipulation in the Latin American and Caribbean countries.

Prior to this study, the CIAT Directorate of International Cooperation and Taxation published a working document on the main legal aspects of transfer pricing control which, even though it has been very useful up till now, it did not deal with administrative aspects.

1 *GIZ is the International Cooperation Office of the Government of Germany.*
2 *BMZ is the Federal Ministry of Economic Cooperation and Development of the Government of Germany.*
3 *ITC is an initiative promoted by the Governments of Germany, Spain and France; aimed at strengthening tax policy and administration in developing countries, in order to promote the mobilization of their domestic resources and their tax sustainability.*

Another relevant aspect of this document is the collaboration of the Latin American and Caribbean countries that allowed us to obtain not only administrative data; but also to get to know, validate and update legal data. Such collaboration is evidenced in the quality of the data published.

Likewise, several institutions interested in this subject matter: the World Bank, ICEFI, Inter-American Development Bank and International Monetary Fund have made comments regarding their vision of transfer pricing control in the Latin American and Caribbean countries, for which reason we were able to present a document with more objective opinions on the subject.

Thus, this study constitutes “unpublished material for the international tax community.

The information in the Study is updated through November 2012 and covers a group of Latin American countries: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela; as well as two Caribbean countries: Jamaica and Trinidad and Tobago.

1. HETEROGENEOUS REGION

In the countries of Latin America and the Caribbean there has been disparity in the evolution of transfer pricing control.

If we classify the countries by taking into consideration a series of indicators, such as the years of existence of their legislations, progress in control/auditing and human resources related aspects, we could separate them into five groups:

- A first group formed by those countries that have been implementing regulations for over a decade, as is the case of Argentina, Brazil and Mexico;

- a second group of countries that have subsequently implemented legislations, but which have managed substantial progress, as is the case Chile, Dominican Republic, Ecuador and Venezuela.

In all the countries that are part of these two first groups, the legislations cover all or most of the aspects dealing with transfer pricing control, in addition to having units exclusively devoted to such control, documentation obligations, auditing, as well as court cases.

- A third group consists of countries that have strengthened their transfer pricing legislations and have created, or are in the process of developing specialized units, as is the case of Colombia, Peru and Uruguay.
- In a fourth group of countries their regulations are in a more premature stage of development. Although their legislations have been promulgated, some have only recently entered into force, or have not yet entered into force. Likewise, their transfer pricing units are being developed. In this group we may find El Salvador, Guatemala, Honduras and Panama.

- The fifth group includes those countries that have not yet introduced regulations. These are Bolivia, Costa Rica, Jamaica, Nicaragua, Paraguay and Trinidad and Tobago. However, all of the aforementioned countries, except for Jamaica and Bolivia, are currently formulating their systems for transfer pricing control.

The heterodoxy in the region is evidenced in the use of the method described in the Argentine regulations, specially designed for the export of agricultural "commodities"[4], methods for determining the prices of all-inclusive hotels and jeopardy assessments in the Dominican Republic; "protection regimes" or "safe harbors" for the maquila companies in Mexico and the simplified Brazilian methods that have been the source of significant discussions in international tax forums.

Undoubtedly there has been significant learning, replication of best practices and experiences in the countries of the region. For example, five of the countries analyzed (Brazil, Ecuador, Guatemala, Peru and Uruguay) benefitted from Argentina's experience and implemented similar measures to those of paragraph Six of Article 8 of the Profit Tax Law to determine the value of goods with quotation in transparent markets or "commodities", when there is participation of an intermediary located abroad.

4 *Paragraph Six of article 8 of the Profit Tax Law*

The following Table shows a schematic view of the comments made in the above paragraphs:

Countries	Consider legislation	Legislation prior to 2002	Verification in process	Cases in Courts	Use of data base	Transfer Pricing area in the TA	Groups
Argentina	Yes	Yes	Yes	Yes	Yes	Yes	I
Bolivia	No	No	No	No	No	No	V
Brazil	Yes	Yes	Yes	Yes	Yes	Yes	I
Chile	Yes	Yes	Yes	No	Yes	Yes	II
Colombia	Yes	Yes	No	No	Yes	Yes	III
Costa Rica	No	No	No	No	No	Yes	V
Ecuador	Yes	No	Yes	Yes	Yes	Yes	II
El Salvador	Yes	No	No	No	No	Yes	IV
Guatemala	Yes	No	No	No	No	Yes	IV
Honduras	Yes	No	No	No	No	No	IV
Jamaica	No	No	No	No	No	No	V
Mexico	Yes	Yes	Yes	Yes	Yes	Yes	I
Panama	Yes	No	No	No	No	Yes	IV
Nicaragua	No	No	No	No	No	No	V
Paraguay	No	No	No	No	No	No	V
Peru	Yes	Yes	Yes	No	Yes	Yes	III
Dominican Republic	Yes	No	Yes	Yes	Yes	Yes	II
Trinidad and Tobago	No	No	No	No	No	No	V
Uruguay	Yes	No	Yes	No	No	Yes	III
Venezuela	Yes	Yes	Yes	No	Yes	Yes	II

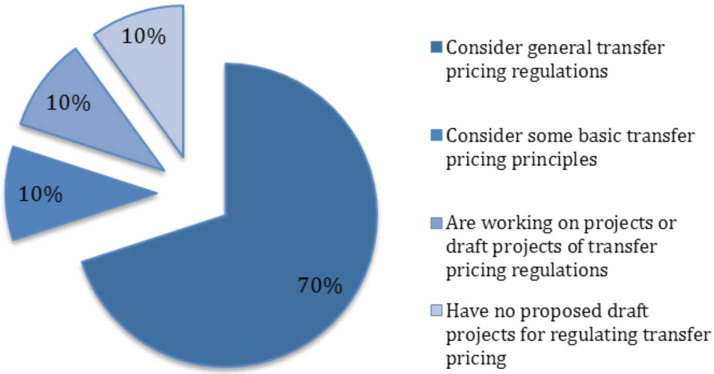
Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

2. LEGISLATIONS FOR CONTROLLING THE ABUSIVE TRANSFER PRICING MANIPULATION

Starting in the nineties, some Latin American countries, namely: Mexico, Brazil and Argentina, among others, introduced the first legislative reforms. The purpose, among other things, was to include therein principles and methodologies for preventing abusive transfer pricing manipulation.

On observing the Latin American countries that have adopted regulations for transfer pricing control or countries working on a draft or bill for regulating this type of transactions, it is evidenced that of the 20 countries comprising Latin America, 14 have regulations for preventing harmful transfer pricing manipulation.

The following graph shows the regulatory situation of the Latin American countries:



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ e ITC. Published in December 2012.

This graph shows that 90% of the Latin American and Caribbean countries have recognized the importance of implementing transfer pricing legislation.

Shown below are the countries that have introduced regulations for controlling harmful transfer pricing manipulation, classified according to the periods of their promulgation:

1992 – 1997	1998 – 2002	2003 – 2007	2008 – 2012
Brazil			
Mexico			
Chile			
	Argentina		
	Venezuela		
	Peru		
	Colombia		
		Dominican Republic	
		Costa Rica[1/]	
		Ecuador	
		Uruguay	
			El Salvador
			Bolivia[1/]
			Panama
			Honduras
			Guatemala

1/Countries that have established basic principles on transfer pricing.
Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012

The tax administrations of the Latin American countries that have adopted general transfer pricing regulations have included the arm's length principle. The countries that have established basic transfer pricing principles apply the principle of economic reality. Worth noting is the specific case of Brazil, whose transfer pricing system is based on objective methods determined according to fixed margins.

The Caribbean countries do not have transfer pricing legislation. Their regulations include general principles that could be useful for controlling transfer pricing. For example, Trinidad & Tobago's current legislation is based on the "Artificial Transactions"[5] legal provision stipulated in section 67 of its Income Tax Act, while Jamaica provides for the arm's length principle in its Tax Code.

The following table shows the situation of two countries that have no anti-abusive transfer pricing regulations in Latin America and the Caribbean:

Countries having no transfer pricing regulations – Current situation (As of November 2012)	
Nicaragua	Paraguay
A transfer pricing analysis and bill has been developed since 2004 and it includes the information of the proposed transfer pricing law model for Central America. It is deemed tha the latter will be introduced as Administrative Regulation (General Resolution).	Is in the process of developing a Transfer Pricing Bill. The State Undersecretaries of Taxation is currently working on a draft Regulatory Decree of Article 16 of Law 125/91.
Provision whereby the tax administrations handle the transfer pricing cases or risks	
Market prices are applied internally for making risk analyses.	Wholesale price: Article 16 of Law 125/91 and interpretation of the generating event: Article 247 of Law 125/91.

Source: Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

Costa Rica and Trinidad & Tobago are in the process of preparing specific bills for the transfer pricing system. The first country is expected to promulgate an Administrative Regulation (General Resolution). In Trinidad & Tobago, it would be introduced in its legislation under the figure of a Code.

3. PRINCIPLE AND METHODS FOR TRANSFER PRICING CONTROL

The basic principle mainly accepted is the "arm's length principle".

The predominant criteria when establishing transfer pricing control systems are those provided by the OECD guidelines. Nevertheless, in most of the countries analyzed there have been variations in these criteria.

5 *"Artificial Transactions" within the context of the legislation, refers to transactions which are not actually intended to be carried out; in other words, it is a fictitious transaction.*

Shown below is the status of the aforementioned countries:

OECD Criteria	OECD and country's own criteria	Own criteria
Chile	Argentina	Brazil[1/]
Colombia	Ecuador	
Costa Rica[2/]	El Salvador	
	Guatemala	
	Honduras	
	Mexico	
	Panama[3/]	
	Peru	
	Dominican Republic	
	Uruguay	
	Venezuela	

1/ Brazil adopted the fixed margin methodology through the "Cost Plus" and "Resale Price" methods.
2/ Criteria applied more in practice than as provided in the legislation.
3/ Official Gazette, Tuesday, August 28, de 2012 – No 27108: Law 52, which amends the Fiscal Code and issues other tax provisions being in force since January 1st, 2013. It is observed that its criteria are similar to those established by the OECD.
Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

4. TRANSACTIONS SUBJECT TO THE TRANSFER PRICING SYSTEM

The implementation of these principles calls for determining their scope of application; that is, the individuals and commercial and/or financial transactions that will be subject to the transfer pricing regulation.

The common criteria established in Latin America for transactions subject to transfer pricing are described in the following table:

Countries	All transactions with related parties	Transactions with individuals established in "Tax Havens"	Another additional condition
Argentina	X	X	
Brazil	X	X	Provided tht the prices agreed are lower than 90% of the price established in the local market.
Chile	X	X	
Colombia		X	Economically linked or related parties from abroad, whose gross net worth at December 31, 2010 was equal to or above 100,000 Tax Value Units (TVUs) or whose gross revenues are equal to or above TVUs
Costa Rica	X	X	
Ecuador	X	X	
El Salvador	X		
Guatemala	X		
Honduras	X	X	
Mexico	X		

Countries	All transactions with related parties	Transactions with individuals established in "Tax Havens"	Another additional condition
Panama	1/		A taxpayer carries out transactions with related parties that are fiscal residents of countries that may have entered into Treaties or Conventions to Avoid Double Taxation
Peru	X	X	
Dominican Republic	X	X	
Uruguay	X	X	
Venezuela	X	X	

1/ Official Gazette, Tuesday, August 28, 2012 – No 27108: Law 52,which amends the Fiscal Code and issues other tax provisions, being in force since January 1st, 2013 will be applicable to any transactions carried out with a related party.
Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

5. RELATED PARTY CONCEPT

In order for two companies to be considered related or associated, one should influence the other. To determine the existence of associated and/or related parties for transfer pricing purposes the regulations must indicate the assumptions that define the level of relationship.

Usually, a typical regulation poses legal-type criteria determined by direct or indirect participation in management, control or capital stock in another company, and of a factual or operational nature as, for example: when there is exclusiveness as agent, distributor or concessionaire for the purchase-sale of goods, services or rights by another; when one company assume the losses or expenses of the other, etc.

The relationship assumptions considered in the legislations of the countries examined are shown in the following table:

	Countries																
Relationship Assumption	ARG	BOL	BRA	CHI	COL	CRC	ECU	ESA	GUA	HON	MEX	PAN	PAR	PER	DOM	URU	VEN
Parent company and its affiliates, subsidiaries and permanent establishments	X		X	X	X	X	X	X	X		X	X	X	X	X	X	
Affiliates, subsidiaries and permanent establishments, among themselves	X		X	X	X		X	X	X	X	X			X	X	X	
Direct or indirect participation in management, administration, control or capital	X	X	X	X	X		X	X	X	X	X	X		X	X	X	X

	Countries																
Relationship Assumption	ARG	BOL	BRA	CHI	COL	CRC	ECU	ESA	GUA	HON	MEX	PAN	PAR	PER	DOM	URU	VEN
Same members, partners or stockholders participating in board of directors or decision-making	X		X	1/	X		X	X	X	X	X			X	X	X	
Through kinship or affinity up to a certain level with the directors or administrators	X		X	1/	X		X	X	X					X	X		
For rights maintained in a trust (the company with the trust)					X		X										
Distribution of profits			X		X		X									X	
Actual management			X		X		X							X	X	X	
Proportion of transactions	X		X		X		X							X	X	X	
Price mechanisms used between the parties				X	X		X									X	
Companies domiciled in tax havens or preferential tax regimes	X		X	X	X		X	X			X			X	X	X	X
Others	X						X	X	X	X	X				X		

1/ Included in Amendment to Law 20630 dated September 27, 2012, which enters into force on January 1st, 2013.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

Every country may regulate or establish additional criteria for delimiting the taxpayer universe or transactions subject to the transfer pricing system. The following table describes other relationship assumptions:

	COUNTRIES											
Relationship Assumption	BOL	BRA	CHI	COL	ECU	ESA	GUA	HON	MEX	PER	DOM	URU
Direct or indirect participation in stock	50% or more	20% or more		50% or more	25% or more	25% or more	25% or more	50% or more		30% or more	50% or more	10% or more
Decision-making or control	50% or more	50% or more	X[1/]		25% or more						50% or more	
Presumed relationship due to domicile in tax haven or preferential tax regime			X		X						X	
Proportion in transactions (e.g. sales, purchases, etc.)					50% or more	50% or more					50% or more[2/]	
Exclusive Agent			X[1/]				X				X	
Consanguinity and/or affinity			X[1/, 3/]		X[4/]				X[4/]		X[5/]	

1/ Included in Amendment to Law 20630 dated September 27, 2012, which enters into force on January 1st, 2013.

2/ Included in amendment to Law 253-12 of November 9, 2012.

3/ Up to fourth degree of consanguinity

4/ Up to fourth degree of consanguinity and second degree of affinity

5/ Up to second degree of consanguinity or due to affinity.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

In most of the cases shown in the foregoing table, the relationship criterion is based on a maximum or minimum percentage of the capital stock. Collaterally, this will help the tax administrations to reduce the number of taxpayers subject to the regulation as well as to be more precise in the control of transactions between related parties.

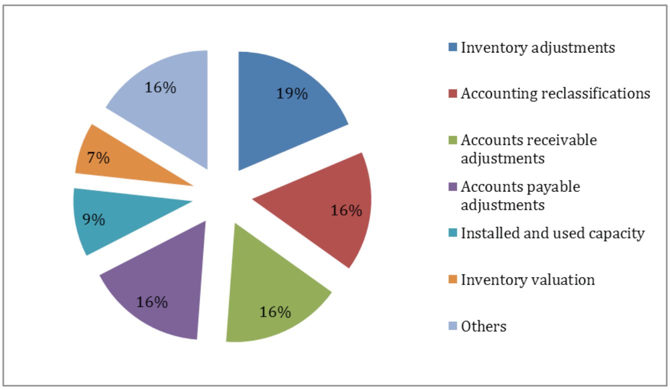
6. COMPARABILITY ADJUSTMENTS

Adjustments are possible in order to increase or improve the comparability levels within the framework of the transfer pricing analysis. Shown below are the adjustments observed by the tax administrations for improving the comparability analysis in transfer pricing:

Adjustments	ARG	CHI	COL	CRC	ECU	MEX	PER	URU	VEN
Monetary correction									X
Accounting reclassifications	X	X			X	X	X	X	X
Inventory valuation			X			X			X
Monetary Assets									X
Accounts receivable adjustments	X	X	X		X	X		X	X
Nonmonetary Assets									X
Deferred taxes									X
Installed and used capacity	X		X			X			X
Capitalized financing costs									X
Adjustment for payment of tariffs									X
Inventory adjustments	X	X	X		X	X	X	X	X
Accounts payable adjustments	X	X	X		X	X		X	X
Freight				X					

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

The following graph allows for observing in an aggregate manner, what has been described in the table above.



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

The inventory adjustment is the one mainly used by the taxpayers and analyzed by the tax administrations for their evaluation. It is usually made when there are differences in the inventory valuation methods, as well as when there is difference in the valuation of accounts receivable and payable, mainly in the establishment of the terms for collecting or paying, respectively.

It was observed that the accounting reclassifications that originate the accounts receivable and payable adjustments, likewise tend to be adjustments that are frequently made and which the tax administrations take into account when designing their procedures and performing their analyses.

The aforementioned comparability adjustments may be applied to the taxpayers, the comparable or both, which will directly depend on the methodology or criterion determined for carrying out said adjustments.

The following are among the main reasons for rejecting a comparability analysis:

a. They do not improve the comparability.
b. Inappropriate idle capacity.
c. Excessive or defective intermediation costs.
d. The adjustment has no economic justification and/or the adjustment does not correspond to reality.
e. The adjustment is not reasonable.
f. The adjustment is not based on documentary evidence.
g. There are mathematical and fundamental errors in the formulas.
h. The implicit interest rates of the capital adjustments are incorrect.

Comparability adjustments are necessary to the extent they fulfill the objective of improving the analysis made between the parties and they are given due use, ensuring that the transactions and their comparable are as similar as possible.

7. BURDEN OF PROOF

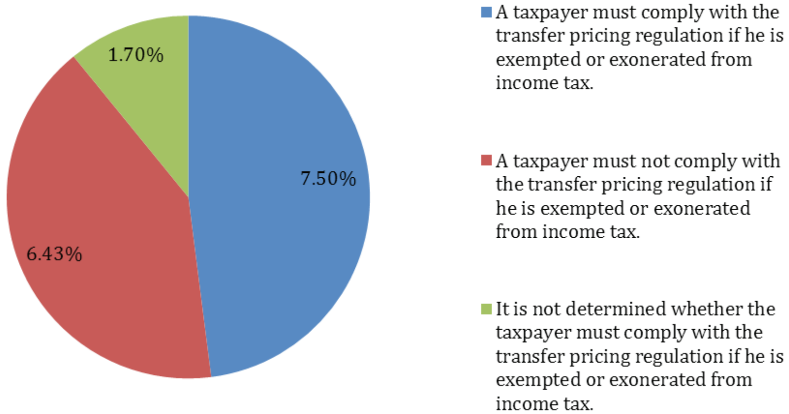
In four of the countries analyzed, the burden of proof falls on the tax administrations, while in the eleven remaining it is established that the taxpayers are responsible for providing the proving elements. The following table shows the countries in which the burden of proof falls on the Tax Administration and those where it falls on the Taxpayer:

Tax Administration	Taxpayer
Chile	Argentina
Costa Rica	Brazil
Panama	Colombia
Uruguay	Ecuador
	El Salvador
	Guatemala
	Honduras
	Mexico
	Peru
	Dominican Republic
	Venezuela

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

8. INCOME TAX EXEMPTION VS. TP SYSTEMS

When a taxpayer is exempt or exonerated from income tax, the obligation to request information and the valuation of transfer prices would seem not to make great sense. Nevertheless, there are different conceptions in the Latin American countries: 6 countries (Argentina, Brazil, Colombia, Ecuador, El Salvador and Dominican Republic) understand that while they are exempt from the income obligation, they need not comply with the requirements for information, while 7 countries understand that they must do so. These latter countries are Chile, Guatemala, Mexico, Panama, Peru, Uruguay and Venezuela.



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

9. PENALTIES AND SANCTIONS FOR NONCOMPLIANCE

As of November 2012, approximately 80% of the countries with transfer pricing systems had considered therein sanctions or penalties for noncompliance with the obligations thereon. The establishment of sanctions and penalties with significant amounts for taxpayers that fail to comply with the regulation allows for exercising pressure for the correct application of the regulation and its timely compliance. Otherwise, by virtue of the costs associated with compliance with the transfer pricing system, among other aspects, the taxpayer could be tempted to not comply or manipulate the regulation.

Seventy nine per cent of the countries impose specific penalties for violations resulting from international transactions, while 21% applies the general regimes.

In addition, with respect to the specific penalties related to noncompliance with the transfer pricing systems, a brief detail may be observed in the following tables:

	Formal violations			Substantial violations
	Nonfiling or incorrect filing of return / technical study	Not providing information / Methodology	Failure to keep documents	
Argentina	$150-20.000 or $500-45.000	$150-450.000	$150-450.000	100-400% of omitted tax
Brazil	20% adequate tax or min. of R$500	Method	Method	N/A
Chile[1/]	10 to 50 tax units	N/A	N/A	N/A
Colombia	Table III- 16 Violations established in the Colombian legislation			
Ecuador	Up to US$ 15.000	Up to US$ 15.000 / closing	US$ 30 to 1.000	Up to US$ 15.000
El Salvador	N/A	N/A	Not deducted from payments to related parties	N/A
Mexico	35,000 - 70,000 pesos updated	N/A	Not deducted from payments to related parties	50-100% of the omitted contribution
Dominican Republic	RD$85,000 – RD$154,000	N/A	N/A	N/A
Panama	N/A	N/A	N/A	N/A
Peru	0.6% for net revenues, between the range of 10% of 1 TU and 25 TUs	N/A	N/A	Up to 50% of omitted tax
Uruguay	N/A	N/A	N/A	N/A
Venezuela	Incomplete or out of term: 5 to 25 TUs nonfiling: 10 to 50 TUs	300 to 500 TUs (methodology)	300 to 500 TUs (methodology)	25 to 200% of omitted tax Prison: 6 months to 7 years

1/ Included in Amendment to Law 20630 dated September 27, 2012, which enters into force on January 1st, 2013.

Source: Comparative study on the current situation of transfer pricing legislation in Latin America. Legal and Administrative Aspects. Isaác Gonzalo Arias Esteban. Published in November 2011.

The penalties provided in the Colombian legislation may be seen in the following table:

DOCUMENTARY EVIDENCE (STUDY ON TP)	SANCTIONS ON INFORMATION RETURN	REDUCTIONS
Out-of-term filing, with errors, which does not allow for verifying the Transfer Pricing application	**For late filing**	
General rule: 1% OV up to 15.000 TVUs (C$377M) **The base cannot be determined:** 0.5% of net revenues. **There are no revenues:** 0.5% of gross net worth up to C$500 mill	**General rule:** 1% OV up to 20.000 TVUs **The base cannot be determined:** 0.5% of net revenues. **There are no revenues:** 0.5% of gross net worth up to C$700 mill	At 50%: If the irregularity is rectified prior to notifying application of the sanction. At 75%; If the irregularity is recitivied within 2 months of notification of the sanction.
Nonprovision of documents	**For filing the return after the request**	
General rule: 1% OV up to 20.000 TVUs + rejection of costs and deductions for nondocumented OV **The base cannot be determined:** 0.5% of net revenues. **There are no revenues:** 0.5% of gross net worth up to C$700 mill	Double the sanctions anticipated in these cases: - The base cannot be determined - There are no revenues	
	For correction of the return	
	General rule: 1% OV up to 20.000 TVUs (it is increased 30% if the sanction is not paid)	

Source: Comparative study on the current situation of transfer pricing legislation in Latin America. Legal and Administrative Aspects. Isaác Gonzalo Arias Esteban. Published in November 2011.

10. SIMPLIFICATION MEASURES

Many countries have implemented simplified system in order to afford taxpayers greater juridical security, better focus the tax administration's resources in specific sectors and reduce the cost of taxpayer compliance. These measures have become a fast and efficient manner for controlling transfer pricing.

Of the twenty countries analyzed, 5 of them, regardless of the level of experience in the implementation of transfer pricing legislation, indicate that they have some type of simplified measure in their legislation and in practice. These are: Brazil, Colombia, Ecuador, Mexico and Uruguay. In the case of this latter country, its legislation[6] empowers the Executive Body to establish special general useful systems, but nothing has yet been regulated in this respect[7].

6 *Article 44 of Chap. VII of Title 4 of TO 1996.*

7 *Law No. 253 of November 2012 recently approved in the Dominican Republic allows the Tax Administration the possibility of establishing Protection Systems for specific economic sectors or activities.*

Among the most common simplification measures there are those that provide for fixed margins for economic sectors, simplifications with respect to the rate of interest, exemptions in relation to small transactions and/or small businesses, simplified transfer pricing methods, exemptions with request to provision of information and exemptions to transfer pricing rules. The following table shows the situation of these measures in the countries of the region:

Measure	Number	Countries
Exemption from transfer pricing system	3	Brazil, Colombia and Mexico
Exemption from documentary evidence	3	Colombia, Mexico and Ecuador
"Safe harbour" methods	3	Mexico and Brazil
"Safe harbour" type of interest	2	Brazil and Bolivia

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

With respect to the first measure, Exemption from transfer pricing system, in the countries where it is available, it is applicable to small and medium enterprises (S&MEs). In determining the S&MEs concept, usually the countries set a maximum threshold based on gross revenues or net worth, whereby all taxpayers below said threshold would not be subject to the regulations provided in each country's regulations. The scope of these measures is shown below:

Country	Detail of measure	Beneficiaries	Year of introduction
Brazil[1]	Exemption	Taxpayers who declare the price at a value of 90% of the national market.	1997
Colombia[2]	Exemption to S&Mes	Taxpayers who do not exceed 100.000 TVUs of Gross Net Worth or 61.000 TVUs of Gross Sales.	2004
Mexico	Exemption to S&Mes	Individuals whose revenues from business activities and interest do not exceed 2 million Pesos.	2002

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

The exemption from documentary evidence, releases the taxpayer from the obligation to undertake analyses for transfer pricing valuation and any other type of related documentation.

8 *Exemption from transfer pricing control when the price is applied at a value of 90% of the national market.*

9 *Taxpayers who do not exceed 100.000 TVUs of Net Worth or 61.000 TVUs of Gross Sales are not subject to the TP system*

The detail of benefits by country is broken down in the following table:

Country	Detail of measure	Beneficiaries[1/]	Year of introduction
Colombia	Exemption of documentation of small transactions	Types of transaction that do not exceed 10,000 TVUs	2004
Ecuador	Exemption of documentation for tax incurred	Individuals or businesses with TET[2/] above 3%	2009
Mexico[3/]	Exemption of documentation S&MEs	- Individuals whose income in the previous period did not exceed MEX $ 13,000,000. - Businesses with income from business activities not exceeding MEX $13,000,000; and income from professional services not exceeding MEX $ 3,000,000	2002 & 2012

1/ In all cases the exemption is not applicable if the transaction was carried out with persons domiciled in Tax Havens. In the case of Ecuador, it is not applicable to companies having an exploitation contract with the State.

2/ Tax incurred over total taxable revenues

3/This same exemption was promulgated on November 12, 2012 for transactions with national related parties in Mexico.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

The countries the use "Safe Harbours" in the region (Mexico and Brazil), estimate margins based on parameters as indicators of profitability for the industry. In Mexico, the "safe harbours" is exclusively intended for companies devoted to the maquilas[10] operation. These taxpayers will determine their taxable profit based on predefined ratios according to total assets or total costs and expenses, whichever is greater.

Technically, the "safe harbour" is the application of the Transactional Net Margin Method using as indicators of the profitability level, the operational margin and the return on assets. Companies carrying out maquila operations that opt for this measure are exempt from the obligation to obtain and preserve the transfer pricing documentary evidence. Nevertheless, they must submit before the tax authorities a writ stating that the taxable profit of the period represented at least the larger amount resulting from applying the "safe harbour", at the latest, within the three months following the date on which said period ends. This system is described in greater detail in chapter III, section B.

In the case of Brazil, the simplification measures are in force since 1997 and are based on pre-determined margins beginning with the transfer pricing methods: the Resale Method and the Cost Plus Method. The assigned margin depends on whether the taxpayer is an exporter or importer. It is worth noting that Brazil's entire transfer pricing system is determined on the basis of fixed margins and presumptive income.

10 Maquilas refer to companies devoted to the production of manufactured goods for export.

Below is a description of the scope of these measures:

Country	Method	"Safe harbour" margin or price
Brazil	RPM/ Resale Method	Fixed margins: Import: 40%; 30% and 20% Export: 15% and 30%
	CPM/ Cost Plus Method	Fixed margins: Import: 20% - Export: 15% and 30%
Mexico	TNMM/ Transactional Net Margin Method	6.9% over total value of assets or 6.5% over total amount of costs and expenses.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

In the case of Brazil, other treatments given to international transactions are shown in the following table:

Export to related individuals				
Transaction	Condition		Consequence	Support
	Percentage	Calculation base		
Net Profit from exports to related party	At least 5%*	On export sales to obtain net profit	Show compliance with Transfer Pricing	Documents proving the transaction
*This calculation is baed on the annual average of the current year and two previous years.				
Corporations				
Transaction	Condition		Consequence	Support
	Percentage	Calculation base		
Net profit from exports (One calendar year)	Not exceed 5%	On net profits of the same period	Show compliance with Transfer Pricing	Documents proving the transaction

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

In Ecuador and Mexico, taxpayers to whom one of the simplified systems is applied and is adhered thereto, is exempt from the obligation of sending transfer pricing information. In the specific case of Ecuador, they do not comply with the formal duties such as the filing of the Transfer Pricing Report or Annex, while in Mexico; taxpayers are exempt from the obligation to undertake a transfer pricing analysis for the transactions subject to the simplification system.

"Safe harbour" type of interest. As simplified measure, the legislation of some countries provides for the type of interest that complies with the arm's length principle, which must be used in financing transactions with related parties abroad, as is the case of Brazil. The rate of interest to be considered is the "London Interbank Offered Rate – LIBOR", for deposits in dollars of the United States of America with a six-month term, increased by a percentage margin. Any additional amount will be considered as amount in excess.

Since Bolivia does not have transfer pricing regulations in force, it provides that the interest paid for capital invested in loan to the company by the owners or partners thereof will not be deductible to the extent that such interest exceeds the value of the Libor rate plus 3% in transactions abroad and in local transactions. Shown below are other provisions regarding interest rates:

Country	Description of measure
Costa Rica	The only restriction with respect to deductibility of interest expense is that the rate cannot be greater than the usual market rates and the rates registered in the Central Bank are used as reference.
Ecuador	The legislation provides for a maximum referential rate determined by the Central Bank which cannot be exceeded.
El Salvador	Interest paid is considered nondeductible when applied to the amount of the debt; it exceeds the percentage of active interest of the Central Reserve Bank plus four additional points.
Paraguay	In no case may such loans or placements earn interest at rates lower than the nominal passive average rates corresponding to time deposits at the bank level, for similar periods in force in the month prior to carrying out the transaction.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

11. ADMINISTRATIVE ASPECTS

a. Auditing

Progress in the Latin American and Caribbean region is observed not only in the implementation of legislation, but also in the audit and control practices. There are 10 tax administrations that have begun transfer pricing examination procedures.

From the experience compiled by several tax administrations, it has been verified that the auditing procedures are not exclusive of countries with broad and complete regulations, but also of countries whose regulation only covers basic principles, as is the case of Costa Rica.

The following table shows the tax administrations of the Latin American countries that have begun procedures in this respect in November 2012:

Countries with general transfer pricing regulations	Countries that have begun transfer pricing examination procedures
Argentina	Yes
Brazil	Yes
Chile	No
Colombia	Yes
Ecuador	Yes
El Salvador	No

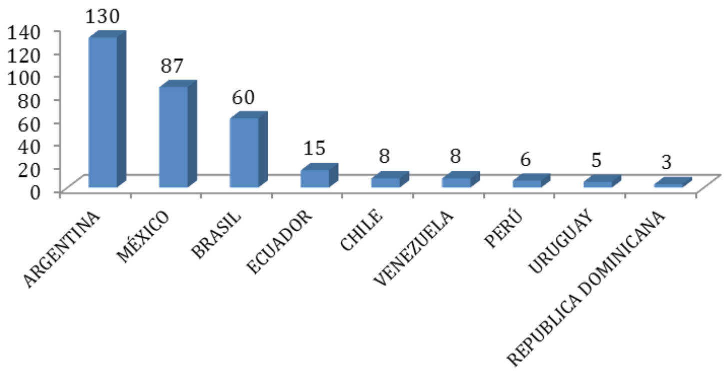
Countries with general transfer pricing regulations	Countries that have begun transfer pricing examination procedures
Guatemala	No
Honduras	No
Mexico	Yes
Panama	No
Peru	Yes
Dominican Republic	Yes
Uruguay	Yes
Venezuela	Yes
Bolivia	No
Costa Rica	Yes

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

As transfer pricing measures move forward, the tax administrations increase their controls in this respect. It is for this reason that by the date of this study, 64% of the tax administrations of countries with general transfer pricing regulations, in implementing their review and control procedures, they evaluate statistical data and the collection behavior of taxpayers that carry out transactions with related parties.

In addition, verification has been made of transfer pricing tax examination or assessment cases that have been in execution in a calendar year.

The following graph shows data corresponding to 2011 in a selection of Latin American countries:



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

As may be observed, tax administrations of such countries like Argentina, Mexico and Brazil, which throughout the years have acquired significant transfer pricing experience, have achieved a larger number of control processes in the region.

With respect to the average time required for carrying out audits in each of the tax administrations of the countries diagnosed, as well as the existence of an administrative instance for a subsequent review of the audit, the average time for a transfer pricing audit ranges between 4, 9, 12 and 24 months.

Country	Time
Argentina	24 months
Chile	12 months
Costa Rica	4 months
Ecuador	12 months
Mexico	24 months
Peru	4 months
Uruguay	9 months
Venezuela	24 months

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

As for the statute of limitations for carrying out actions related to the control of transfer pricing manipulation, in their great majority the regulations of the Latin American and Caribbean countries provide for terms between 3 and 5 years. There are only two cases that do not abide by the criteria identified in the region being analyzed. In Colombia the statute of limitations is 2 years, while in Honduras there is no statute of limitations.

Most of the tax administrations of the countries in this study daily face several problems for carrying out transfer pricing examinations. In this respect, the main barriers were analyzed and as a result, access to information was determined as the main obstacle to effective transfer pricing control. The following table shows the main barriers identified:

Identify comparable transactions.
Lack of information on transactions carried out with related parties.
Identify and obtain information from abroad.
Identify and determine comparable.
Prove association with related parties, when it has not been declared.
Access to taxpayer information.
Lack of local data bases of national or regional companies that show their information.
Lack of information relative to companies that comprise multinational groups.

Lack of a wider network of instruments for tax information exchange.
Lack of information for carrying out comparability analyses.
Lack of comparable price bases.
Lack of regulations providing for the clear (transparent) preparation and dissemination of taxpayer accounting records.
Information presented in languages other than the official one adopted by a country.
Availability of specialized human resources.

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

From the foregoing it follows that an important component for transfer pricing control by the tax administrations is found in technological developments.

b. Risk areas

The main economic sectors showing abusive transfer pricing manipulation risks according to the information provided by the tax administrations consulted for purposes of the diagnoses carried out by CIAT, CAPTAC-DR and the IDB for the Latin American countries and this study are the following (Nº 1: most important; Nº 6: less important):

1. Pharmaceutical
2. Manufacturing industry
3. Agricultural (cereals – flowers – cattle – others)
4. Mining
5. Oil
6. Automotive

Also identified were other sectors that were not as recurrent in the diagnosis made of the tax administrations, but which show transfer pricing risks and are accordingly, of significant importance:

1. Distribution and trade
2. Manufacturing of cleaning and hygiene products
3. Financial
4. Hotel
5. Fishing
6. Transportation and telecommunications

Also analyzed was the concentration by the tax administrations of Latin America and some of the Caribbean in the control processes of economic sectors with transfer pricing risks. In other words, the question was: What proportion of the total control processes carried out is concentrated in a specific sector of the economy? In this respect, the sectors with the highest concentration; that is, with over 40% of the control processes devoted to each of these sectors are the following (Nº 1, highest concentration):

1. Pharmaceutical
2. Hotel
3. Food industry

The sectors with lower concentration; that is, less than 15% are the following:

1. Mining
2. Financial
3. Automotive industry
4. Transportation
5. Fishing
6. Services

The sectors of the economy show a different transfer pricing risk according to the relevance of the activities in each of the countries. Therefore, it is possible that there may be differences in the concentrations diagnosed when analyzing each country individually. However, one may observe sectors that are relevant in most of the countries analyzed, due to the existence of multinational companies that carry out similar activities in different countries. This is one of the fundamental reasons of the practical regulations for transfer pricing control.

c. Transfer pricing office

The structure of the tax administrations of Latin America and the Caribbean vary significantly. One of the most important elements that determine the success of the work carried out by the tax administrations is the human resource that is part of said structure. In this sense, this study endeavors to determine the human resource situation in the sphere of transfer pricing control in the tax administrations of the Latin American and Caribbean countries. Thus, it has been observed that there are important differences, ranging from the structure and composition of the teams, up to the training, recruitment and compensation mechanisms.

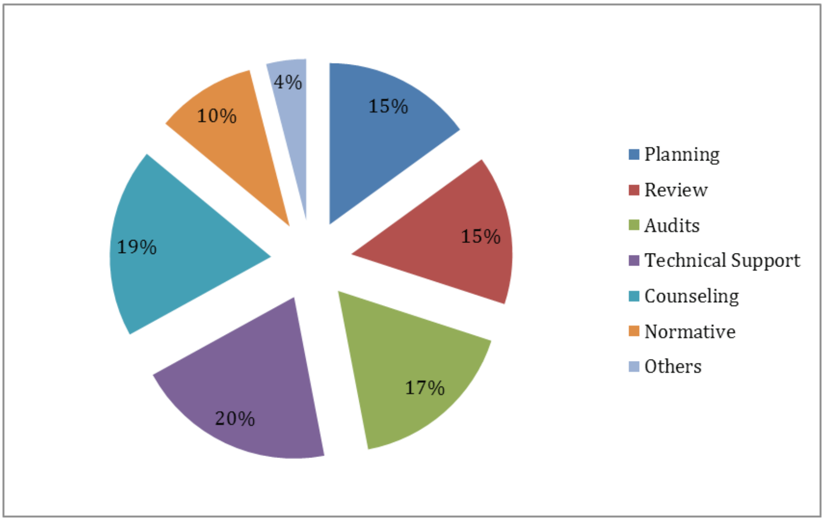
Most of the administrations in the study have departments, areas or teams specialized in international taxation. Seventy five per cent of the Latin American administrations analyzed and a selection of countries from the Caribbean have specialized teams in international taxation issues. Only the remaining 25% of the administrations (five) do not have such teams. It is important to point out that transfer pricing has developed differently in the region. In other words, there are tax administrations with many years of experience and specialized teams, while on the other extreme, there are others that are considering their creation or incorporation.

To conclude, one may say that in the Region, most tax administrations have an entity specialized in international issues and in particular, transfer pricing. The table appearing below lists the entities existing in the countries analyzed.

Most of the tax administrations being analyzed have decentralized organizational structures; that is, they have central offices and regional or zone entities that are in charge of the different tasks of the tax administration[11]. Within these organizational structures one may find units specialized in international tax issues. Each organizational structure has different schemes for handling these international matters that range from the decentralization of the international taxation teams, as is the case of Ecuador, or the centralization of the work of these teams in the main offices of the administration, as is the case of Mexico.

Although with different names or denominations, as one may verify in the previous table, most of the tax administrations have an area, department, unit, management office or division in charge of international and/or transfer pricing issues. In order to consider these units in greater depth, several aspects of the tax administrations of 20 Latin American and Caribbean countries were analyzed: planning, review, auditing, technical support, counseling, normative functions, among others. Commonly, the transfer pricing units carry out audit, technical support and counseling functions. The following graph shows the proportion of the different functions that are carried out by the transfer pricing units in the tax administrations.

11 "State of the Tax Administrations of Latin America: 2006-2010. CIAT-IDB-CAPTAC-DR". Institutional Aspects Section" http://www.ciat.org/index.php/es/productos-y-servicios/ciat-data/administraciontributaria.html



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

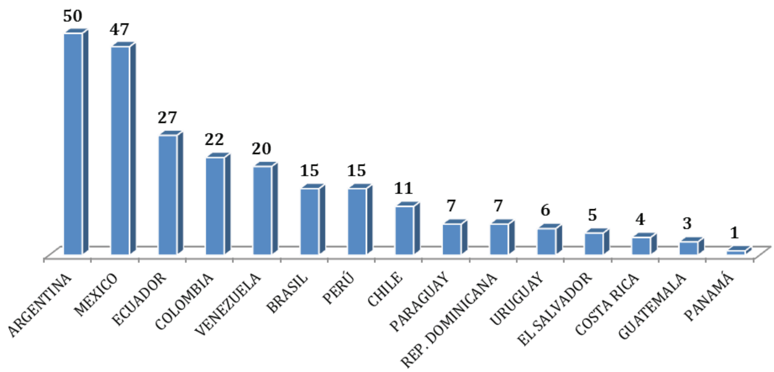
In Mexico, the transfer pricing entity is also in charge, for example, of Advance Pricing Arrangements (APAs) and Multilateral Advance Pricing Arragements (MAPAs).

Success in transfer pricing control is due, among other aspects, to the organizational structure and, in particular, the staff's characteristics. In this sense, the investigation sought to find out about the training given to the officials of the transfer pricing units. It was determined that only 30% of the Latin American tax administrations and a group from the Caribbean do have in their tax administrations special training plans for the team in charge of transfer pricing.

In some countries of the Region, even though they may lack a training plan for transfer pricing officials, efforts are made to provide lectures, courses, workshops, etc., on the subject. These activities, including the plans, are mainly developed every one or two years; while a few countries hold them every three or six years. It is observed that the training processes in the tax administrations lack the speediness shown by the large businesses and taxpayers in general. The training plans should be adapted to the speed with which businesses and taxpayer actions evolve and develop vis-a-vis transfer pricing.

The training given to officials of the transfer pricing units of the tax administrations analyzed is 34% of an international nature, 29% national, 29% internal –within the very tax administration – and 8% is provided through Internet or on-line. The aforementioned training covers participation in workshops, lectures, courses and/or seminars conducted from the private as well as public sectors.

A survey also referred to the number of officials in the transfer pricing units. In the following graph one may observe the distribution of officials in each tax administration for handling these matters.

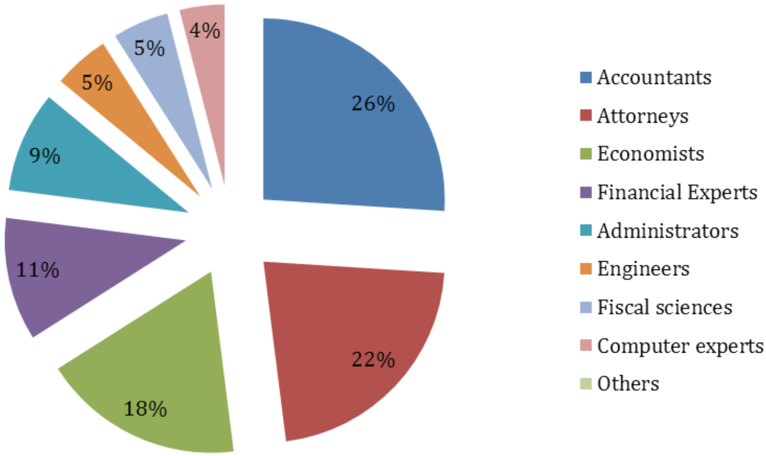


Argentina: of the 50 officials reported, 10 are involved in Information Exchange tasks.
Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

Additionally, to complement the data shown in the above graph, it is important to learn about the composition of those teams; that is, determine the profile of their members. This information could be of interest to the tax administrations that are just beginning to consider this matter and which are designing or redesigning their human resources strategies in order to structure multidisciplinary teams capable of providing optimum results in their control processes.

The composition of multidisciplinary teams is an important factor for achieving success in transfer pricing control. According to the information provided by the twenty countries examined, 65% of them have multidisciplinary teams that comprise the transfer pricing units, while the remaining 35% do not have this type of teams. There are tax administrations that resort to experts and technical reports from other State organizations, which is a valid alternative to make up for the lack of a multidisciplinary team.

The following graph shows the profiles and proportion of recurrence of each in the composition of transfer pricing teams in the different tax administrations. Profiles such as that of accountant, attorney and economist are the most recurrent ones in the transfer pricing units.



Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

d. Advance pricing arrangements

The Advance Pricing Arrangements (APAs) are measures for solving disputes and simplification used by the tax administrations on the basis of provisions in agreements or in their internal legislations. The definition of APA conceived in the DTTs, allows two or more contracting states to discuss and establish mechanisms to avoid double taxation. When APAs are signed between two countries they are considered bilateral; when more than two countries intervene they are considered multilateral. On the other hand, when by means of internal legislation it is possible to request an APA between the taxpayer and the local tax administration, it would be a unilateral agreement.

A unilateral APA may be defined as a contract signed between a taxpayer and the tax authority in order to agree, prior to holding transactions between related parties, the criteria for the valuation of such transactions. In particular, it involves the methods for estimating the market prices or margins, correction adjustments, determination of comparable companies and transactions, goods or services subject to the transfer pricing methodology and other analysis elements in order that both parties may be certain regarding compliance with the arm's length principle. The unilateral APAs have acquired great importance in recent years due to their administrative facility and greater speediness to be formalized, as compared to the bilateral and multilateral ones and, of course, their lower processing cost.

In general, the following are some of the advantages of the APAs:

1. They reduce the compliance costs of the transfer pricing systems for the taxpayers as well as the tax administrations. An APA may avoid the taxpayers and tax administrations fiscal costs and auditing times as well as litigations;
2. They afford greater juridical security to the taxpayer. According to the OECD guidelines, the APAs may assist taxpayers in eliminating uncertainty by increasing assurance of tax treatment for international transactions. Thus, a taxpayer may be in a better position to predict his tax liabilities, thus allowing a favorable fiscal environment for investment;
3. They allow the tax administration to focus resources on other taxpayers or risk areas.

Given the advantages of the APAs, the vision of the countries analyzed is to make good use of them. Evidence of this is the fact that nine of the countries analyzed consider in their internal regulations the possibility for negotiating this type of instrument.

Several countries of the region have mainly opted for including unilateral APAs in their legislations. A case that stands out in the analysis is that of the Dominican Republic, wherein the internal law defines sectorial APAs. Under this scheme, the taxpayers of the sector and the tax administration will agree on the prices, margins or amount of compensations that comply with the arm's length principle. The legislation of this country does not allow a taxpayer to enter into agreements with the tax authority, unless it is through the Association representing the sector and jointly with the other members[12].

According to the Brazilian Law there is the possibility that the taxpayers request the Ministry of Finance for modifications in the fixed margins. This request must be made under justified circumstances which may be proven by means of technical publications, investigations or reports. The Secretariat of Finance of the Ministry may disqualify the act if it considers that the information submitted by the taxpayers is of ill reputation or inconsistent. This Law also provides that the change of margins may be done officially, as published on September 17, 2012.

It is worth mentioning that the countries having internal regulations regarding bilateral and multilateral APAs are those wherein some of the DDTs signed include clauses regarding APAs; this being the case of Mexico and Ecuador.

12 Article 281 of the Dominican Tax Code, Paragraphs II and IV.

With respect to the term of enforcement of the APA, this varies among countries, ranging between 18 and 60 months. The following table shows the term of enforcement according to each country's legislation.

After the term of enforcement of the APA has expired, in some countries, the taxpayer may request its extension. This is the case of Ecuador, Mexico, Dominican Republic and Venezuela[13] where the regulation provides for the extension of an APA for an additional period. The time frame allowed for extending an APA is 36 months in Mexico and the Dominican Republic and 36 months or more in Ecuador. In some countries there is the possibility that upon expiration of the term, the same continues in force until a new one is approved[14].

The negotiation of an APA in most cases and according to the experiences of the countries7 tends to be long. This is so for many reasons, such as, for example, the need to collect detailed information that may allow for analyzing the historical documents of the taxpayer, comparable companies and the transactions. A joint study is undertaken (taxpayer-treasury) regarding the viability of processing the agreement, its scope, the methodologies to be used and the documents required by the tax administration. Although desirable, not all the countries provide specific guidelines in their internal regulations that may direct the entire process. Only the regulations of 6 countries specify the procedure to be followed for requesting an APA. These are: Colombia, Guatemala, Mexico, Peru, Venezuela and Chile, in the latter introduced in a law dated September 27, 2012.

According to the legislation of these countries, the taxpayers must submit to the tax administration their APA proposal, which should be based on a transfer pricing study or other document proving that the valuation of the transaction or transactions with their related parties has been agreed under the transfer pricing guidelines, in keeping with the legislation in this respect. Generally, the request must be accompanied, although not limited to, the following information:

1. General information on the taxpayer and the related company;

2. Description of the contents of the agreement to be formulated, describe each of the types of operation to be covered;

13 Article 165 of the Income Tax Law. "Advance transfer pricing arrangements shall be applied to the fiscal period underway on the date it is signed and for three (3) subsequent fiscal periods. The term may be greater when derived from a friendly procedure, in the terms of an international treaty of which the Republic may be a party".

14 i.e. Dominican Republic

3. Description and justification of the fundamental assumptions of the agreement (for example, economic conditions, quota and market conditions, sales volume and final selling price, rate of exchange and rate of interest);

4. Detailed explanation of the proposed transfer pricing methodology, specifying for the current period and the periods of enforcement of the agreement, the most appropriate valuation method, the selection of comparable companies or transactions, the adjustments to the selected comparable, determination of the price or margin range thereof, or amount of compensation;

5. Generic information regarding this type of agreements, conventions or valuation proposals approved or in process before tax administrations of other states;

6. Generic identification of other types of transaction carried out between the related entities or parties that will not be covered by the agreement;

7. Basic hypotheses or critical assumptions on which the proposal is formulated.

Other administrative aspects in relation to APAs refer to the term in which the tax administrations must respond to the APA requests. According to the regulations of the countries, the time frame ranges between 23 and 24 months.

The preparation of an agreement is technically complex; it requires time and effort on the part of the taxpayer and the tax administration. Besides, when the APAs are bilateral or multilateral, they involve tax administrations abroad, for which reason additional costs are incurred for their negotiation. In this respect, the tax administrations could request the taxpayers the payment of a fee to cover expenses resulting from this procedure. At present, only Mexico and Venezuela have provided for the corresponding payment to process an APA. In the particular case of Mexico, the amount required is 905 Pesos (approximately USD$90 according to quotation of the month of October 2012). Venezuela has not yet determined the amount to be paid by the taxpayer.

An important challenge for the tax administrations as regards the APAs is the availability of qualified staff for managing them. Nevertheless, very few tax administrations in the region count on a team exclusively devoted to handling advance pricing agreements. Only Colombia, Mexico and Uruguay have a team deoted to their control and administration.

Likewise, according to the investigation undertaken in the countries being analyzed, as of October 2012, only Mexico and Uruguay have signed APAs. Uruguay signed its first APA in 2012. On its part, Mexico has a long history in the negotiation of APAs, with a total of 291 to date. Forty three per cent of these APAs (126 APAs) have been agreed with the manufacturing industry.

e. Situation of the courts

Shown below is the number of transfer pricing cases which the countries analyzed have dispute before the courts of justice:

Country	Number of cases
Argentina	29
Costa Rica	3
Ecuador	22
Mexico	80
Dominican Republic	22

Source: Study on "The Control of transfer pricing manipulation in Latin America and the Caribbean". CIAT, GIZ, BMZ and ITC. Published in December 2012.

Likewise of a total of 20 countries analyzed, 40% have specialized courts, 25% do not and 35% did not provide information in this respect.

The following are the countries with courts specialized in tax issues:

- Argentina
- Chile
- Colombia
- Ecuador (judicial)
- Guatemala
- Mexico
- Peru
- Dominican Republic
- Panama (administrative)

Brazil has no justice courts specialized in tax issues. However, the main laws originate in a mixed administrative court formed by representatives of the taxpayers and the Treasury called: CONSELHO ADMINISTRATIVO DE RECURSOS FISCAIS (CARF) (Administrative Tax Resources Council).

Although it is important to count on courts specialized on tax issues, it is also very important that they are familiar with transfer pricing. In this respect, through the analysis carried out it was determined that the countries that have specialized courts only a few of them have sound transfer pricing knowledge. In percentage terms, of the 40% of countries with specialized courts, only 35% have acquired knowledge on the subject. If we refer to such actions as exchange of knowledge and training between tax administrations and specialized courts, this latter percentage diminishes to 25%.

12. CONCLUSIONS

1. There is a great interest in transfer pricing on the part of the Latin American tax administrations. Of the twenty countries of the region, fourteen have regulations to prevent abusive transfer pricing manipulation. Likewise, Nicaragua and Paraguay are working in projects for introducing transfer pricing regulations. This leads us to conclude that an approximate 85% of the Latin American countries have attributed importance and are working in the development of this tax control measure.

2. In the Caribbean Region, Trinidad and Tobago is working on a regulation for the transfer pricing system, while Jamaica anticipates in its legislation the arm’s length principle, according to what has been provided in its Code.

3. Approximately 90% of the countries with transfer pricing regulations have totally or partially adopted the OECD criteria.

4. More than 80% of the countries with transfer pricing regulations have determined that all transactions with related parties should be regulated. However, by specifying the relationship criterion in the regulation, it is possible to reduce the number of taxpayers subject thereto and afford greater precision when orienting the control of transactions between related parties.

5. It is necessary to expressly establish the transactions subject thereto, the relationship criteria, the taxpayer obligations and the sanctions to be applied in the transfer pricing sphere.

6. More than 70% of the countries with transfer pricing regulations have specific sanctions in this respect.

7. More than 80% of the countries with methods for transfer pricing valuation have established some hierarchical criterion for their use in the evaluation of transactions between related parties.

8. Of the methods established for transfer pricing valuation, the transactional net margin method is the one mostly used. This, without disregarding the fact that there may be cases where there

are mainly methods developed by the country itself, for example, those implemented by Brazil, Argentina and the Dominican Republic.

9. When determining the comparability between goods, services, transactions or businesses and the adjustments for increasing it, the adjustments of inventories and accounting reclassifications are in a greater proportion those used by the taxpayers. Given that its use is ever more frequent and it is responsible for a relevant number of differences with the tax administrations, it is imperative that the respective criteria be delimited.

10. More than 70% provide in the regulation that the burden of proof in transfer pricing falls on the taxpayers, and thus they are the ones who must initially demonstrate the arm's length principle.

11. More than 70% of the countries analyzed in this study carry out these inspections, in order to determine and identify the functions, assets and risks that are actually assumed by the verified taxpayers. Likewise, Argentina, Brazil and Mexico are the countries with greater experience in transfer pricing examination processes.

12. More than 60% of the countries provide in their regulations for the presentation of a transfer pricing report. On the other hand, more than 70% have provided for filing a transfer pricing information return.

13. More than 70% of the countries observed have provided in their regulations for the possibility of applying the market /interquartile ranges.

14. It is necessary for tax administrations to count on greater local or regional information that may allow a better use of comparable for transfer pricing analysis. The lack of adequate local or regional information becomes one of the greatest obstacles for the effective implementation of transfer pricing in the region.

15. More than 70% of the tax administrations observed in this study have an entity specialized in international issues and in particular, transfer pricing.

16. Fifty per cent of the tax administrations of countries with transfer pricing regulations have regulations for advance arrangements. Only 25% of the Latin American tax administrations have experience in the application of simplified transfer pricing measures.

Case Study

Topic 2.1

SPECIFIC METHODS FOR THE CONTROL OF TRANSFER PRICING

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Deputy General Directorate of Examination
Federal Administration of Public Revenues
(Argentina)

Content: *Summary - I. Introduction. - II. Description of the verified situation: - 1. The triangle maneuver. - 2. The "no profitability" of enterprises in the agro-export sector in years of prices and harvests records. - III. Control strategy. Application of the sixth method. - IV. Development of the "global taxpayer" concept: 1. Global taxpayer: The taxpayer's whole taxation. - 2. Tax administration development from the single agency perspective. - 3. Expansion of the information exchange treaties network. - V. Conclusion.*

SUMMARY

In the last century, the concentrated economic groups have progressed in a decentralization process in order to expand their territorial presence. In this sense, our country has a strong economic presence of commodities, leading to the possibility for exporting groups to manipulate the prices of their operations looking for planning, in many cases harmfully, their tax structure.

In this context, large concentrated exporter groups, mainly related to the grains, oils and oil seeds, mining and fishing sector are developing a "triangle" maneuver which involves invoicing goods to a destination but sending them to another by using intermediaries (traders) based in jurisdictions of low or zero taxation or with a preferential tax regime (fiscal opacity).

This is to arbitrarily assign part of the income to an intermediary through the artificial conclusion of future operations between the local exporter and an international trader for reducing the tax burden in our country

Based on the study of this situation, AFIP detected that these sectors related to the international commercialization of goods in a transparent market, had a common denominator: most of the exports were invoiced to intermediaries or traders, and the merchandise was never intended to be addressed to this international purchaser but to another located in another country and the operation is invoiced from a different country.

During the explosion in commodities prices and harvest record years, it is logic to imagine that the accounting and taxation profits from the large concentrated exporter groups mainly related to grains, oils and oilseeds sectors, should have reached their peak; on the contrary, the tax profit and the determined taxation levels were below the average, some companies even declared tax losses.

Given this situation the control strategy designed by the AFIP was to verify all their operations with related companies, by verifying the corresponding application of the “sixth method”[1]. To do this, the business knowledge of the company´s operations and the market in which they operate was requested, the support documentation of operations from Argentines companies, subsidiaries and/or related abroad and the comparison of commodities prices of the respective contracts with the market price. è The application of the "sixth method" or the shipment date method is the tool for valuing transfer pricing of commodities operations.

In summary, the purpose of the regulation is to prevent the taxpayer from using, for the determination of the profit tax base, the price agreed with the international trader since it is presumed that they do not deserve any payment because they are just simple intermediaries and therefore do not add any value or make any effort to market the product, unless proven otherwise.

Because of the ongoing controls done by the administration in 2009, the adjusted amounts, the total amounts and the amounts to be determined by judicial processes were significantly increased.

Furthermore, in 2012 AFIP launched a comprehensive control plan for the cereal and mining sector, in order to verify the application of the sixth method.

1 *It is noteworthy that, at the time of its incorporation in the regulatory framework of Argentina, this new method did not register any precedent in the legislation of other countries, making our country the pioneer in its creation and implementation.*

As previously mentioned, the increasing globalization of trade operations is the perfect excuse for large concentrated groups to apply "harmful tax planning" in order to evade tax payment.

Due to this harmful behavior, the AFIP has developed the “Global Taxpayer” concept which allows knowing the whole taxation of taxpayers and concentrated economic groups at local and international level as well as the different taxes of the taxpayer´s activity.

AFIP’s coordinated actions allow understanding the taxpayers’ taxation from a global point of view. In other words, by considering the taxation at tax levels, customs rights and social security resources.

This has been achieved due to the fact that the Administration´s central areas have promoted a coordinated work by the different operational areas. The expansion of the exchange of information treaties network was also one of the key elements to move forward in the taxation of taxpayers since it allows obtaining relevant data regarding their behavior abroad.

I. INTRODUCTION

In the last century, the concentrated economic groups have progressed in a decentralization process in order to expand their territorial presence. In this sense, our country has a strong economic presence of commodities, leading to the possibility for exporting groups to manipulate the prices of their operations looking for planning, in many cases harmfully, their tax structure.

On the basis of the commitment made by the Government-within the G20 framework- on issues related to fiscal transparency, the Federal Administration of Public Revenue (AFIP) has started a new stage characterized by a pro-active attitude in favor of transparency in international trade transactions and in the taxpayers integral taxation developing the GLOBAL TAXPAYER concept when analyzing commercial transactions of concentrated groups.

II. DESCRIPTION OF THE VERIFIED SITUATION

1. The triangle maneuver

The “triangle” maneuver developed by large concentrated exporter groups mainly related to the grains, oils and oil seeds, mining and fishing sectors, involves invoicing goods to a destination but sending them to another by using intermediaries (traders) based in jurisdictions of low or zero taxation or with a preferential tax regime (fiscal opacity)

In practice, the Argentinean exporter completes a sale of commodities with a client abroad, for example sale of soybeans to a Chinese buyer, and sends the merchandise to that destination, but the invoice is issued to an international trader based in a jurisdiction with tax opacity.

To this we must add the rights on exports that did not enter due to the gap in their calculation basis (the FOB value of the transaction).

The purpose of this maneuver is to arbitrarily assign part of the income to an intermediary through the artificial conclusion of future operations between the local exporter and international trader for reducing the tax burden in our country.

The following table shows various detected situations during the development of the analysis:

ARGENTINA	INTERMEDIARIO	CLIENTE FINAL	DIF. PRECIO
CAPITALES HOLANDESES	VINCULADA ASIA	CHINA-EUROPA-BRASIL	5%
CAPITALES EE.UU.	SUCURSAL AMERICA	CHINA-ESPAÑA-MALASIA-INDIA	5%
CAPITALES ALEMANES	CASA MATRIZ EUROPA	CHINA--ESPAÑA-BRASIL-CHILE	5% – 10%
ARGENTINO	SUCURSAL AMERICA	CHINA-ESPAÑA	5% – 10%
CAPITALES EE.UU.	CASA MATRIZ NORTE AMERICA	CHINA-ARABIA-SIRIA	5%

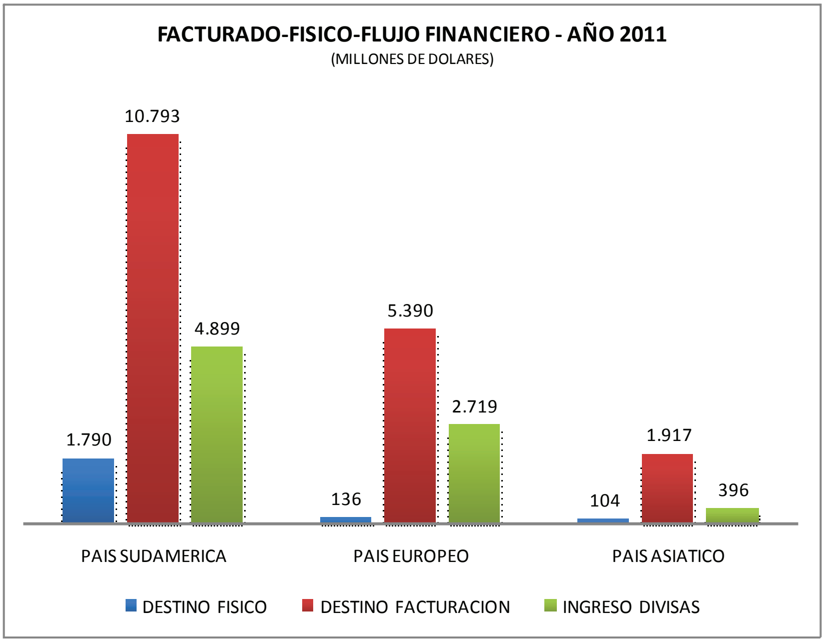
Based on the study of this situation AFIP detected that these sectors related to the international commercialization of goods known in a transparent market, had a common denominator: most of the exports were invoiced to intermediaries or traders and the merchandise was never intended to be addressed to this international purchaser but to another located in another country.

In addition to the above mentioned, these intermediaries and operations were characterized for:

- Lacking of “economic substance”: the intermediaries were always simple resellers, they did not added any value to the product nor developed any task or made any effort for its marketing;
- Lacking of “Transparency”: The traders were always located in jurisdiction with low or no taxation or in territories with fiscal opacity where the national treasury could not obtain any information;
- Extension of the terms: many broader periods were found between the operation´s conclusion date and the shipment deadlines if compared to the market. In some cases, coordinated operations controlled from 180 to 500 days before the shipment date and in certain cases, this control was performed when the products did not exist; when sellers sold directly to independent third parties the period were considerably lower.
- Lower Prices: in all audited cases, when the control was performed, the prices fixed were the lowest in the market, both in relation to prices used by other operators as well as to the official FOB price of the Agriculture, livestock and fishing Secretariat;
- Source of payments: It was found that the payments of operations were not coming from the client´s country or from where the Trader was located but were from a third country (for example from the parent company of the group or from another jurisdiction with “flexible Exchange rate”)

This study was carried out by using a “Risk Matrix” which shows that in most of this type of operations there was a big difference between the destination of the invoicing of goods, their physical destination and the origin of the financial collection flow .

This situation is shown in the following chart:

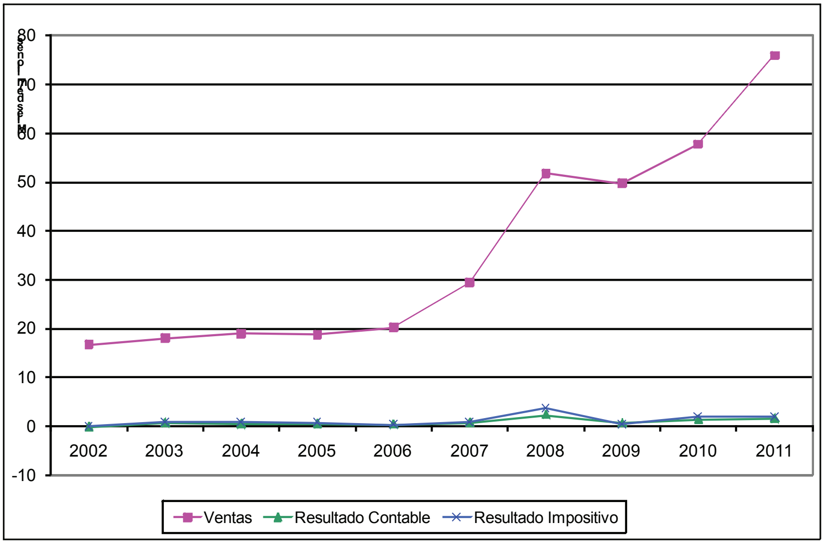


2. The "No profitability" of enterprises in the agro-export sector in years of prices and harvests records

During the explosion in commodities prices and harvest record years, it is logic to imagine that the accounting and taxation profits from the large concentrated exporter groups mainly related to grains, oils and oilseeds sectors, should have reached their peak; on the contrary, the tax profit and the determined taxation levels were below the average, some companies even declared tax losses. .

The following chart develops the above mentioned sequence according to the sales.

Accounting and tax profits from the agro exporter sector.



If we analyze the determined balances, profits and taxes from the agro export companies in recent years, we find that the amounts are beyond the logic of the international context since, as we have mentioned before, it was characterized by a harvest and historical records in the international contributions.

We will also develop the behavior of the main 10 companies in the sector which even though they make up only 18% of the total number of companies, concentrate 91% of the total sales of the sector.

If we analyze the behavior of these companies in 2010, which was deeply impacted by the effective implementation of the tax transparency policies, a significant increase is noted in the tax voluntarily declared by taxpayers representing the sector. We note that only two companies did not determine capital gains tax. In spite of the fact that sales increase 16 %, the determined tax increases around 145 %.
The following table shows the figures for the year 2010:

Major companies in the agro-exporter sector: detail of sales, profits and determined tax year 2010

COMPANY	Sales	Accounting profits		Tax Profit		Determined Tax	
	Amount	amount	% sales	Amount	% sales	Amount	% sales
Company 1	13.700	142	1,04%	325	2,37%	112	0,82%
Company 2	11.304	426	3,77%	586	5,19%	165	1,46%
Company 3	8.257	246	2,99%	317	3,84%	63	0,77%
Company 4	5.239	114	2,18%	153	2,92%	0	0,00%
Company 5	4.569	12	0,26%	1	0,02%	0,27	0,01%
Company 6	3.301	40	1,22%	99	3,01%	35	1,05%
Company 7	3.081	67	2,17%	113	3,66%	49	1,58%
Company 8	1.834	126	6,87%	150	8,20%	26	1,40%
Company 9	684	10	1,40%	-15	-2,16%	0	0,00%
Company 10	666	18	2,64%	31	4,58%	10	1,53%
TOTAL	52.633	1.201	2,28%	1.760	3,34%	460	0,87%

Regarding the evolution of these companies in 2011 it shows that sales increased 44% while the self-declared tax increases 26%.

Major companies in the agro-exporter sector: detail of sales, profits and determined tax year 2011

	Sales	Accounting profits		Tax Profit		Determined Tax	
COMPANY	Amount	Amount	% sales	Amount	% sales	Amount	% sales
Company 1	15.067	298	1,98%	392	2,60%	137	0,91%
Company 2	15.595	522	3,35%	864	5,54%	302	1,94%
Company 3	14.914	232	1,55%	242	1,62%	85	0,57%
Company 4	6.680	193	2,89%	82	1,23%	0,34	0,01%
Company 5	6.922	36	0,51%	121	1,74%	42	0,61%
Company 6	5.089	68	1,33%	44	0,87%	15	0,30%
Company 7	4.432	51	1,16%	93	2,10%	23	0,52%
Company 8	5.761	13	0,23%	-9	-0,16%	0	0,00%
Company 9	377	-1	-0,29%	16	4,16%	0	0,00%
Company 10	1.083	65	6,03%	90	8,35%	31	2,90%
TOTAL	75.921	1.477	1,95%	1.935	2,55%	637	0,84%

III. CONTROL STRATEGY. APPLICATION OF THE SIXTH METHOD

The control strategy designed by the AFIP was to verify all their operations with related companies, by verifying the corresponding application of the "sixth method". To do this, it required the business knowledge of the company´s operations and the market in which they operate the support documentation of operations from Argentines companies, subsidiaries and/or related abroad and the comparison of

commodities prices of the respective contracts with the market price.
è The application of the "sixth method" or the shipment date method: article 15 of the Profit tax Law is the tool for valuing transfer pricing of commodities operations.

To apply the “sixth method” the following conditions are required:

a. It must be a triangle export: an international intermediary (trader) which is not the final recipient of the merchandise must participate, i.e. it is not a direct operation between a local and the final client;
b. The intermediary –not the final recipient of the merchandise- does not fulfills the condition established by the rules to consider that there is economic substance (real activity that justifies the amount of the operation)
   In order to apply this method, the existence of formal or functional relationship with the intermediary is not required.
c. The exported good must be commodities[2], goods traded in well-known transparent markets.

Regarding its application, it is noted that:

d. The value of the good in the transparent market is calculated the day the loading of the good is completed regardless of the transport used.
e. If the price agreed with the intermediary is higher, this last one will be taken to determine the Argentine’s source income.
f. The method is exclusive in regard to its application: if the legal requirements are enforced, only the "sixth method" and no other must be applied.

Regarding the business knowledge of the companies´ and the market operation it is important to interpret their actions not only as separate entities, but also to understand and know the economic group to which the Company belongs- both at vertical as well as at horizontal level -, establishing both the corporate and the functional relation.

It also means to exactly identify clients and suppliers, both for the economic group of the taxpayer under examination as for the countries in which they are located. The analysis must be based on the commercial and/or financial operations or services of the taxpayer.

The application of Double Taxation Agreements and the limits to access to information (as incentives for the localization of Companies) should be analyzed.

2 *They are assets, which due to their low level of development, are poorly differentiated. Thus, for example, the wheat from Argentina and China (the world's leading producer) are very similar. The "commodities" have a well-known market price.*

In regard to the market in which they operate, it is necessary to know their customs, the way in which the contracts are concluded and the prices are fixed, the characteristics of each product and the geographical location of customers and suppliers.

To implement this, it is essential to obtain information from own or external databases. In case of AFIP the following can be mentioned:

- Databases from the organization: the information from the "E-Fisco Base", fed with data that taxpayers report through different applications, customs information or information from other public organizations (such as BCRA). We will have soon the transfer pricing studies in pdf.
- External Database: They are contracted by this Administration to be used in audits, such as the OSIRIS Base (one of the bases used by taxpayers for making transfer pricing reports, which include the company's balance sheets at the global level quoted on the stock market). They allow having information from the sector´s companies and at the same time they copy the company´s sample submitted by the taxpayer in the Price Report. Other web pages: web sites from official organizations, commercial chambers, producers associations and even the web page of the company under examination.

Since the ongoing controls done by the administration in 2009, the adjusted amounts, the total amounts and the amounts to be determined by judicial processes were significantly increased.

However, these adjustments were partly done by taxpayers and others are to be determined by an administrative procedure.

Furthermore, in 2012 AFIP launched a comprehensive control plan for the cereal and mining sector in order to verify the application of the sixth method.

IV. THE DEVELOPMENT OF THE "GLOBAL TAXPAYER" CONCEPT

1. Global taxpayer: The taxpayer's whole taxation

As previously mentioned, the increasing globalization of trade operations is the perfect excuse for large concentrated groups to apply "harmful tax planning" in order to evade tax payment.

Due to this harmful behavior, the AFIP has developed the "Global Taxpayer" concept which allows knowing the whole taxation of taxpayers and concentrated economic groups at local and international level as well as the different taxes of the taxpayer´s activity.

This is based on two pillars: (i) AFIPs work as a "Single Agency", coordinating the actions of the three operational areas (the Internal Revenue Service, the Directorate General of Customs and the Directorate General of Social Security Resources) and (ii) the decision and implementation of the Information exchange Agreements network to obtain data regarding the behavior of their taxpayers abroad, especially the large ones and concentrated economic groups.

2. Tax administration development from the single agency perspective.

AFIP coordinated actions allow to understand the taxpayers' taxation from a global point of view. In other words, by considering the taxation at tax levels, customs rights and resources from social security.

This has been achieved due to the fact that the Administration´s central areas have promoted a coordinated work through the different operational areas.

In 2010, in order to modernize, transform and support the existing process, a reorganization of the organizational structure was carried out.

3. Expansion of the information exchange treaties network

Argentina has given a qualitative jump in the matter from the 2008 global economic crisis and the active presence of the Government within the G20 framework on issues related to international trade and tax transparency.

AFIP played a key role in this strategic decision of the Government and from then started a new phase characterized by a pro-active attitude. In this sense, from the year 2009 their actions were aimed at increasing the agreement network for obtaining data regarding Argentinian residents and/or taxpayers abroad, mainly from large taxpayers and concentrated economic groups allowing detecting undeclared income, to have information on their economic situation, fight triangle operations and detect fictitious transactions.

V. CONCLUSION

We can conclude that the main benefits from the application of the "sixth method" are the following:

- Allows fighting evasion in strategic export sectors of Argentina's economy.
- Avoid the relocation of Argentina's source income through harmful tax planning.
- Allows the detection of intermediaries without economic substance.
- Discourage the use of the triangle mechanism.

Currently, one of the main challenges of the Administration is the control of Companies that could in the scope of this method, in which the wide Exchange of information network is a useful tool in order to obtain data from the operations abroad and from the participating intermediaries.

It has been noted that many agro exporter economic groups have restructured their operations by migrating intermediaries to countries with fiscal opacity or by making a triangle directly with their parent companies in order avoid the test of "economic substance" of the intermediary.

Case Study

Topic 2.1

SPECIFIC METHODS FOR THE CONTROL OF TRANSFER PRICING

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Secretary of the Federal Revenues
(Brazil)

Content: *I. Transfer pricing in the brazilian law - 1. Rationale. - 2. Principles and mechanisms. - 3. Law 9,430/1996. - 4. Other dispositions. - 5. Use of the ministry of finance's rule no. 222, 24 September 2008. - 6. Treatment of royalties in the Brazilian laws. - 7. Changes made by law no. 12,715/2012. - 8. Change made in interest payments by law 12,766/2012. - 9. Representativeness of intercompany transactions.*

I. TRANSFER PRICING IN THE BRAZILIAN LAW

1. RATIONALE

In view of the ever-growing business within multinational companies owned by a common parent entity during the 90's, the Brazilian Government identified the need for a broader control of such activities, so as to avoid the manipulation of prices, both on import and export operations, that may indirectly lead to transfer profits abroad.

Brazil has decided to adopt a transfer pricing model according to its own economic reality, and not simply to import a model from other countries. Brazil does not have the same level of financial resources or investment capacity as that of developed countries. By consequence, the lack of financial resources is an obstacle to the implementation of a set of rules similar to the United States legislation.

In this context, the traditional transfer pricing methods have been adapted, in Brazil, in order to make it possible for the tax authorities to check on compliance with the Brazilian rules. Under such circumstances and in view of the high degree of subjectivity of the Advanced Pricing Agreement (APA) and the high costs of the APA procedure, the Brazilian Government has decided not to adopt the APA.

2. PRINCIPLES AND MECHANISMS

In general, the Brazilian legislation follows the directives set by the OECD Report "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations", especially with regard to the "Arm's Length Principle".

2.2. Methods

The Brazilian methods of determining parameter prices in order to control the prices set by companies are similar to the three traditional methods proposed by OECD, although with different names for export and import operations, but there are also innovative ones for commodities, as follows:

METHODS	BRAZIL	OECD Equivalent
IMPORT	PIC – (for "compared independent prices")	CUP
	PRL – (for "resale price less margin")	RPM
	CPL – (for "production cost plus margin")	CPM
	PCI – (for "price under import quotation")	-
EXPORT	PVEX – (for "exporting sale price")	CUP
	PVA – (for "wholesale at destiny, less margin")	RPM
	PVV – (for "retailer price at destiny, less margin)	RPM
	CAP – (for "acquisition or production cost plus taxes and margin)	COM
	Pecex – (for "price under export quotation)	-

2.3. Differences between the Brazilian Transfer Pricing legislation and the OECD model

The Brazilian legislation is different from the OECD Model in that it presets profit margins wherever the methods are used to show the accuracy of prices established for commercial activities within the same controlled group.

The presetting of a margin actually represents a safe harbour and can be considered as an "adhesion model" or "adhesion APA": if a taxpayer has a profit margin above the fixed margin 20% (twenty per cent), 30% (thirty per cent) or 40% (forty per cent), depending on the economy sector that the enterprise operates, the Federal Revenue of Brazil (RFB) will accept the established transfer pricing, even if this price does not follow the independent market pricing or does not seem to be in accordance with the “Arm’s Length Principle”.

The presetting by law of the profit margin is fundamentally designed to make it easier for both the taxpayer and the Brazilian tax authority to check the parameter price (the price to be accepted as a deductible cost or expense for income tax purposes). Besides, the presetting of a margin aims at adjusting the international transfer pricing rules to a peculiar feature of the Brazilian legal ordinance – objectivity – and eliminates a high degree of subjectivity, which is a characteristic of the OECD model.

The preset margins may, however, be altered. In the case of importation, the company may request a margin alteration from the Minister of Finance, if this company works with a lower profit margin compared to the fixed margin that has been set by law. Thus, the company has the burden of proof and must confirm that it achieves a lower margin and follows the “Arm’s Length Principle”, that is, the company must demonstrate that the lower margins are earned in operations with non-associated companies.

3. LAW 9,430/1996

3.1. Adjustments

According to Law No. 9,430, from 27 December 1996, amended by Law No. 9.959/2000, Law No. 12,715/2012 and Law No. 12,766/2012, import and export transactions of goods, services and rights, carried out by a company domiciled in Brazil with an associated person resident or domiciled abroad, or with an individual or a legal entity resident or domiciled in a tax haven, are subject to transfer pricing adjustments, for the purpose of determining the taxable profit.

Under Article 23 of Law No. 9,430/1996, the following conditions qualify a company or individual as associated with an entity in Brazil:

a. The head-office, when it is domiciled abroad;
b. Its agency or branch, when domiciled abroad;
c. An individual or legal entity, resident or domiciled abroad, whose shares in the capital stock characterises it as a controlling or associated, pursuant to Law No. 6,404, article 243, 15th December 1976[1];
d. A legal entity domiciled abroad that is characterised as its controlled by or associated with company, pursuant to Law No. 6,404/1976;

1 *Law Nr. 6.404/1976, states about incorporated companies.*

e. the legal entity domiciled abroad, when this entity and the company domiciled in Brazil are under a common share control or common administrative control or when at least 10% (ten per cent) of the stock capital of each company belongs to the same individual or legal entity;
f. an individual or legal entity, resident or domiciled abroad, which along with the company domiciled in Brazil, has a corporate interest in the capital stock of a third company, with the total value of this interest characterising them as a unit or of the third company, pursuant to Law No. 6,404/1976.
g. The individual or legal entity, resident or domiciled abroad, that is associated to it in any undertaking under a consortium or a condominium modality;
h. the individual resident abroad who is related to or in-law within the third degree, spouse or partner of any of its directors or of its partner or controlling shareholder in a direct or indirect participation;
i. The individual or legal entity, resident or domiciled abroad, that is its exclusive agent, distributor or a dealer in transactions of purchase or selling of goods, services or rights;
j. the individual or legal entity, resident or domiciled abroad, that, in relation to the legal entity domiciled in Brazil, is its exclusive agent, distributor or dealer in transactions of purchase or selling of goods, services or rights.

3.2. Methods

According to the the Arm’s Length Principle, the adjustments to determine the transfer pricing must follow the Methods established by the legislation. However, taxpayers may choose one of the methods, except in case of commodities that are compulsory the utilization of PCI and Pecex, as long as under the conditions set forth by the Brazilian law.

3.3. Importation

3.3.1. Common rules to Importation Costs

Under Article 4 of Normative Instruction SRF No. 1,312, from 28 December 2012, a Regulatory legislation, the importing legal entity may opt for any method listed in Articles 8 to 16 of the same IN No. 1,312/2012, except in the case of importing commodities.

3.3.2. The following methods can be applied on importation cases, Normative Instruction SRF No.1, 312/2012:

Article 8

a. **Comparable Uncontrolled Price Method (PIC-CUP)**, described as the arithmetic average of prices of identical or similar goods, services or rights found out in the Brazilian market or in other countries in purchase or sale transactions under similar payment conditions.

I – if sold by the same exporting company to a non-associated company, resident or not;
II – if purchased by the same importing company from non-associated legal entities, resident or not;
III – if in purchase and sale operations between other non-associated legal entities, resident or not.

Article 9, paragraph 1:

Values will be adjusted as to minimize the effects on prices, caused by differences in business conditions as well as in physical and contents-related aspects. In case of identical goods, services and rights, adjustments will be permitted only in relation to:

I – terms of payment;
II – quantities;
III – guarantee on work;
IV – obligation to advertise;
V – responsibility for quality control costs;
VI – intermediation costs;
VII – packaging;
VIII – freight and insurance.

Article 9, paragraphs 4-10:

Adjustments deriving from differences in quantities will be made according to documents issued by the selling company, able to prove the larger is quantity the lower will be the price.

In case of adjustments deriving from guarantee on work, the respective value included in the price cannot exceed the result of the division of the total costs incurred in the previous verification period by the amount of goods, services and rights in use in the domestic market during that same period. If the good, service or right has not yet been sold in Brazil, the cost in national currency corresponding to the same guarantee granted abroad will be admitted.

As to obligation to advertise and responsibility for quality control costs, the price of the good, service or right acquired from an associated company domiciled abroad, which bears the cost of such expenses in Brazil, may exceed the price practiced by a company that does not, at up to the value incurred per unit by the exporting company. If the advertisement or publicity aims at promoting:

I – the company's name or brand, costs will be proportionally distributed amongst all goods, services or rights sold in Brazil, based on quantities and respective value;

II – a product, the costs division will be based on its quantities.

Where data are utilized from a purchasing company which has borne the intermediation costs involved in the purchase of a good, service or right whose price is a parameter for the price practiced in a purchase/ sale operation with an associated company, non-subject to such expense, the price practiced by the latter may exceed the first's, up to the value correspondent to the intermediation costs.

For comparison purposes, the prices of goods, services and rights will also be adjusted as regards differences in packaging materials as well as freight / insurance involved in each case.

Articles 10-11:

In the case of similar goods, services or rights, besides the aforementioned adjustments, prices will also be adjusted as regards differences in physical and contents-related aspects.

The comparison may take into consideration prices practiced in earlier / later periods provided there's an adjustment resulting from variations in reference currencies exchange rates, occurred between the dates of both operations.

In the case of adjustments deriving from variations in exchange rates, parameter prices, where resulting from operations carried out in countries whose currency cannot be translated into the national currency, will be firstly converted into American dollars and then, into Reais, at the exchange rate practiced on each operation's date.

Accidental variations in commodities prices, certified by national or international stock quotes, will also be considered.

b. Resale Price less Profit Method (PRL-RPP), described as the arithmetic average of the resale prices of goods, services or rights less discounts given on invoice, taxes imposed on sales, commissions and brokerage paid, and the profit margin[2]. Detailed information regarding this method is given in the next topics of this Technical Report.

Article 12, paragraphs 2-5 and 9:

The average purchase/ resale price will be determined based on the quantities negotiated.

To determine the arithmetic average of prices, the stock values and quantities existing at the beginning of the verification period will be included.

The arithmetic average of prices will be determined from the purchase date to the end of the verification period.

If the operations comprise cash and installment sales, prices related to the latter must not consider any incidence of interest.

The RPP method utilizing a 20% profit margin will only be applied where no value is added to the cost, but a mere resale of the same imported goods, services or rights.

b. Cost Plus Profit Method (CPL-CPP), described as the average production cost of identical or similar goods, services or rights in the country where they were originally produced added by taxes charged in the exportation country and the profit margin of 20% (twenty per cent), determined upon the incurred costs.

Article 15, paragraph 5:

For price determination purposes, it may be considered as part of the cost:

I – acquisition cost of raw materials, intermediate products and packaging materials;
II – cost of any other goods, services or rights employed or consumed in production;

2 *The profit margin is:*
- a) *of 40% (forty per cent), when the imported goods are applied to production of cigarettes, pharmacochemicals and 30% (thirty per cent) for chemical products, among others (Law No. 9.430/1996, article 18; §12,I, II, introduced by Law No. 12,715, de 2012);*
- b) *of 20% (twenty per cent), in other cases (Law No. 9,430/1996, article 18;§12,III,)*

III – personnel costs employed in production, including direct supervision, production facilities maintenance and surveillance, and their respective social duties;
IV – rental, maintenance and repair costs, as well as depreciation, amortization and depletion costs;
V – reasonable breakages and losses during production.

3.4. Exportation

3.4.1. Export Revenue

Normative Instruction SRF No. 1,312 determines under Article 20, paragraph 1:

The average price will be obtained by multiplying the prices practiced by quantities related to each operation; these results will be summed up and then divided by the total quantity, being thus determined the arithmetic average price.

3.4.2. Common rules to Export Revenue

Article 22, paragraph 1:

Values will be adjusted as to minimize the effects on the prices to be compared, caused by differences in business conditions as well as in physical and contents-related aspects. In the case of identical goods, services and rights, adjustments will be permitted only in relation to:

I – terms of payment;
II – quantities;
III – guarantee on work;
IV – obligation to advertise;
V – responsibility for quality control costs;
VI – intermediation costs;
VII – packaging;
VIII – freight and insurance;
IX – credit risks.

Article 22, paragraph 2:

Differences on terms of payment will be adjusted according to the company’s rates.

Article 22, paragraph 4-10:

Adjustments deriving from differences in quantities will be made according to a document issued by the selling company, able to prove that the larger quantity a same purchaser orders the lower the price is.

In the case of adjustments deriving from guarantee on work, the respective value included in the price cannot exceed the result of the division of the total costs incurred in the previous verification period by the amount of goods, services and rights in use in the domestic market during that same period. If the good, service or right has not yet been sold in Brazil, the cost in national currency corresponding to the same guarantee granted abroad will be admitted.

As to obligation to advertise and responsibility for quality control costs, to compare the price of the good, service or right between a purchasing company that bears the cost of such expenses and a purchasing company that does not, the value incurred per unit must be deducted. The same rule applies to intermediation costs.

Prices will also be adjusted according to differences in costs related to packaging material, freight and insurance.

Adjustments resulting from credit risks:

I – will be admitted exclusively in relation to operations between purchaser and seller domiciled in Brazil;
II – will utilize a percentage obtained by comparing total losses and credits from the previous calendar year.

Articles 23,24,25,26:

The average export price is obtained by multiplying prices by quantities. These results are summed up and then divided by the total quantity, being thus determined the arithmetic average price.

In the case of similar goods, services or rights, besides the aforementioned adjustments, prices will also be adjusted as regards differences in physical and contents-related aspects.

The comparison may take into consideration prices practiced in earlier / later periods where it is not possible to identify sale operations at the same period. Accidental variations in commodities prices, certified by national or international stock quotes, will also be considered.

The share of revenue that exceeds the value already booked by the company must be summed up to the net profit for the purpose of determining the actual profit and the CSLL calculation basis. It also must be considered in order to determine the presumed / arbitrated profit.

3.4.3 Methods in exportation

a. Exportation Sale Price Method (ESP), described as the arithmetic average of export prices of identical or similar exported goods, services or rights sold by the company itself or its exporter to other clients, during the same period that the corporate income revenue tax is determined, in similar payment conditions.

Article 30, paragraph 1:

Only sales to clients non-associated with the Brazilian company will be considered.

b. Wholesale Price in Destination Country less Profit Method_(PVA-WPP), described as the arithmetic prices of identical or similar goods, practiced in the wholesale market of the destination country and in similar payment conditions, reduced by taxes included in price, charged in the mentioned country, and the profit margin of 15% (fifteen per cent) over the wholesale price.

c. Retail Price in Destination Country less Profit Method (PVV-RPP), described as the arithmetic average price of identical or similar goods, practiced in the retail market of the destination country, in similar payment conditions, reduced by taxes included in the price, charged in the mentioned country, and the profit margin of 30% (thirty per cent) over the retail price;

d. Acquisition or Production Cost plus Profit Method (ACP), described as the arithmetic average of the acquisition or production costs of exported goods, services or rights, added by taxes charged in Brazil and the profit margin of 15% (fifteen per cent) over the full amount of costs and taxes.

4. OTHER DISPOSITIONS

4.1. Atypical operations

Article 44:

Under no circumstances the use of goods, services and rights' prices practised in atypical purchase / sale operations such as stock liquidation, discontinuance of activities or government subsidised sales will be admitted.

1.1 Percentage alteration

Article 45:

Percentage alterations referred to in this article may have a general, sectoral or specific character. They can be promoted ex officio or in compliance with a request from a class entity representing an economic sector in relation to operations carried out by the companies it represents, as well as in compliance with a request from the interested company itself. Requests for percentage alteration from economic sectors or companies will be analyzed by the Coordination-General of Taxation (Cosit). Even partially compliant decisions will be formalized.

In the case of compliance, cost must inform whether it agrees with the new margin's duration of effectiveness suggested by the entity / interested company. Otherwise, Cosit must propose a more suitable term.

1.2 . Discrepancy margin

Article 51:

In operations with associated companies, where the price adjusted as a parameter diverges up to a plus or minus 5% in relation to the price extracted from the import / export documents, the confirmation will be deemed satisfactory. .In this case, no adjustments will be required from the company.

1.3 . Enforcement Procedures

Article 53:

The company under enforcement procedures must indicate the method adopted and produce the documentation utilized as the basis for price determination. The method not being indicated or documents not being produced – or if insufficient / unable to convince as to price – auditors can determine the price based on other documents at their disposal, by applying a method listed below.

5. USE OF THE MINISTRY OF FINANCE'S RULE NO. 222, 24 SEPTEMBER 2008

5.1. Discretionarity

RFB decisions are based on provisions of the current laws and are not discretionary. As set forth by MF Rule No.222 the requests for alteration of the margin percentages are accepted if they are in conformity with the Brazilian laws.

5.2. Situations using different margins

MF Rule No. 222, is used in general or specific cases or by sector. The percentage alterations may be done in general or by sector in attention to the request made by an association representing an economic sector, regarding goods, services or rights involved in the operations of the represented companies.The percentage alterations may also be done specifically, as requested by the concerned company.

5.3. Alteration of margins according to the "arm's length principle"

The Federal Revenue admits the evidence that the taxpayer follows a different margin from the one foreseen in the law, in accordance with the "arm's length principle", provided that the information rendered by him is complemented by the documents requested in MF Rule No. 222.

Adoption of the "arm's length principle" must be evidenced in accordance with the documents mentioned in MF Rule No. 222. The importance of the requested documents is to make evident that the margin applied by the taxpayer really meets the "arm's length principle".

The Federal Revenue may request other documents that it may find necessary to prove the allegations of the concerned entity or company. The Federal Revenue may consider other documents that could prove the allegations of the concerned entity or company.

The Federal Revenue may consider comparable third parties financial-economic information.

5.4. Taxpayers requests

The margin alteration procedure foreseen in Rule No. 222 has not been frequently used. So far there have been only two requests for margin alteration concerning the application of the Resale Price Method – RPM (article 18, item II, letter d, of Law no. 9,430, of 1996).

5.5. Discussions with other governments

In the last five years, the Federal Revenue has discussed only one case regarding transfer pricing in a mutual agreement procedure.

The international tax agreements signed by Brazil do not contain provisions regarding corresponding adjustments.

5.8. Advanced pricing agreement

The Brazilian transfer pricing laws do not adopt the Advanced Pricing Agreement concept due to the high degree of subjectivity and the high costs involved for the tax administration, when implementing this procedure.

6. TREATMENT OF ROYALTIES IN THE BRAZILIAN LAWS

Payments of royalties are subject to withholding tax at the rate of 15% and are not subject to the transfer pricing laws.

The Brazilian transfer pricing laws are not applicable to the deductibility of the expenses deriving from payments of royalties and fees for technical, scientific, administrative or similar assistance. The deductibility is restricted to the conditions set forth in the domestic law, which assigns to the Minister of Finance the power to set a percentage – up to five percent (5%) – of the net sales of the product concerned as a ceiling for the deductibility of such expenses (Decree 3.000/99, Article 355).

7. CHANGES MADE BY LAW NO. 12,715/2012

Law No. 12,715/2012 went into effect on September 18, 2012, as a result of modifying Provisional Measure No. 563, of April 3, 2012, MP 563 had been responsible, among other matters, for creating new rules on import and export methods.

Concerning to the PIC method, MP had established the criterion of minimun representativeness of transactions that may be used as a parameter for comparison with the effective cost of importation: 5% of the value of imports subject to transfer pricing control, during the period that the calculation method is applied, in the absence of transactions representing 5% the percentage may be supplemented with imports in the preceding calendar year, adjusted for exchange rate differences.

Regarding to new methods PCI and PECEX, Law 12,715 provides that is compulsory their utilization for goods from internationally recognized commodities and negotiated in futures markets, in the absence of prices, the reference methods shall use, in setting price parameters, data obtained from independent sources provided by internationally recognized research institutions. With respect to the PECEX, the law also provides for comparisons with prices set by regulators or agencies that are published in Brazil's Official Gazette of the Union.

Law No. 12,715 entered in force in January 1, 2013, but provides to the taxpayer the option of applying its provisions for the 2012 year calendar. With regard to tax auditing dispositions, they are in force since April.

8. CHANGE MADE IN INTEREST PAYMENTS BY LAW 12,766/2012

Law 12,766, from 27 December 2012, introduced a significant change on intercompany loan rules. It determines a limit of a rate plus spread for paid interest to be deductible from income tax. Different rates are provided, depending on the type of transaction, the currency used, and other factors. The spread will be determined by the minister of finance, according to market average. The new Law also states, in paragraph 9, that the moment of verification is on the contract date of transaction and not periodical.

9. REPRESENTATIVENESS OF INTERCOMPANY TRANSACTIONS

The representativeness of intercompanies transactions has grown in the last decade, as the chart below shows. Furthermore, the total of tax assessments from 2008 to 2012 was 355 that launched in taxes and fines BRL 16,965,244.59.

Tabela 1

Calendar year	Importation[3] (%)	Exportation[4] (%)
2005	29	32
2006	28	36
2007	39	45
2008	29	34
2009	33	32
2010	32	37
2011	37	45

3 *Relation between intercompany import of goods and total of import.*
4 *Relation between intercompany export of goods and total of export.*

Case Study

Topic 2.2

SECTORS OF INTEREST: CASE STUDIES

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National Superintendency of Customs and Tax Administration
(Peru)

Content: *Introduction. - I. Composition of Peruvian exports. - 1. Transfer pricing and main products exported. - 2. Fish flour, importance and productive process. - 3. Cases studies.*

INTRODUCTION

The purpose of this presentation is to describe the Peruvian experience in transfer pricing auditing, whose initial stage has brought about mixed results and has allowed us to formulate the new strategy to be applied in the coming years.

Two cases have been selected which deal with the fish flour producing sector. Therefore, we deem it necessary to briefly provide the economic context in order to understand the importance of this activity in Peru's economy.

Hereunder we will briefly explain the productive process and the main varieties of the product. Finally, we will discuss both cases by presenting the information of greater relevance in relation to each of them.

I. COMPOSITION OF PERUVIAN EXPORTS

As may be seen in the following chart, approximately 78% of our exports consist of traditional products.

FOB Exports According to Economic Sectors 1					
SECTOR	2010		2011		
	US$ Mill.	% Part.	US$ Mill.	% Part.	% Var
TRADITIONAL	28,091	78.5	35,785	77.8	27.4
Mining	21,902	61.2	27,015	58.8	23.3
Oil and natural gas	3,330	9.3	4,997	10.9	50.1
Fishing	1,884	5.3	2,099	4.6	11.4
Agriculture	975	2.7	1,674	3.6	71.7
NONTRADITIONAL	7,715	21.5	10,188	22.2	32.1
Agriculture	,203	6.2	2,844	6.2	29.1
Textile	1,561	4.4	1,990	4.3	27.5
Chemical	1,223	3.4	1,647	3.6	34.6
Fishing	650	1.8	1,051	2.3	61.6
Iron and steel	877	2.4	1,050	2.3	19.7
Nonmetallic mining	251	0.7	491	1.1	95.5
Metal-mechanical	400	1.1	481	1.0	20.2
Wood and paper	359	1.0	399	0.9	11.1
Miscellaneous (inc. Jewelry)	160	0.4	192	0.4	20.2
Hides and leather	29	0.1	38	0.1	30.7
Crafts	1	0.0	5	0.0	673.4
TOTAL	35,806	100.0	45,973	100.0	28.4

1/. Correspond to definitive export systems
Source : SUNAT (at March 5, 2012)
Preparation: MINCETUR- OGEE-OEEI

1. TRANSFER PRICING AND MAIN PRODUCTS EXPORTED

Of the 40 billion dollar transactions subject to transfer pricing control, approximately 10 billion correspond to the products shown in the following chart:

Products	Amount	%
Mining	5,385	51%
Hydrocarbons	3,252	31%
Agricultural	1,497	14%
Fishing	484	5%
TOTAL	10,619	

SOURCE: TP Information Return for 2011
PREPARATION: GFIyPT

2. FISH FLOUR, IMPORTANCE AND PRODUCTIVE PROCESS

Although for purposes of our economy fish flour is not the product generating the highest foreign exchange from exports, fish flour produced in Peru is one with the highest demand at the world level and that is the reason for its importance.

In fact, according to FAO statistics, Peru is the main producer of fish flour at the world level, followed quite far off by China and Chile.

As may be seen, of the total production of fish flour between 2000 and 2009, Peru accounted for 27%.

Fish Flour Production		
Country	Tn. 00- 09	%
Peru	16,347,451	27%
China	8,482,463	14%
Chile	7,722,979	13%
Thailand	4,691,995	8%
Denmark	2,929,145	5%
Japan	2,620,011	4%
USA	2,617,699	4%
Norway	1,903,100	3%
Others (60)	13340168	22%
Total	60,655,011	100%
SOURCE :	FAO	
PREPARATION	GFIyPT	

Actually, fish flour is a product mainly used in the preparation of food for animals, use in aquiculture, breeding of pigs, chicken, cows and pets. It is obtained from the anchovy, a marine species that is abundant in the Peruvian coasts.

In 2007, period in which the transactions being analyzed were carried out, fish flour exports from Peru amounted to approximately 1.5 billion dollars, which is equivalent to more than 5% of its total exports.

Varieties

There are two types of fish flour in the market:

- FD or FAQ type Flour (Flame Dried – FD or Fair Average Quality – FAQ): which is the lower quality flour since it is directly flame-dried and has a low nutritional value.

- SD type flour (Steam Dried – SD): which is the best quality flour since it is steam-dried and has a better nutritional value.

Below is a description of the fish flour manufacturing process, specifying the existing types in the Drying Process:

1. Capture: obtaining the raw material from the fishing boats which have nets.
2. Unloading: is done with the help of large hoses from the barge or dock, to the plant. The equipment receiving the fish eliminates the water contents that flow from the fish, which is then taken to the weighing bins and there they complete the drainage of the remaining water.
3. Weighing and storage in pools: the fish is weighed here. They have an average volume of 1 ton per bin. After weighing the fish, it is stored in pools according to the capture time (CT).
4. Cooking: the fish is cooked by controlling the temperature, in order to clump the proteins, release fat and reduce or eliminate an acceptable amount of microbes1.
5. Pre strainer: at this stage, water is separated from the cooked solid matter.
6. Pressing: the purpose of this process is to obtain the product known as "press cake", which should have the least amount of water and fat2, and to which the necessary antioxidants are added to avoid oxidation of the fat included in the press cake (this process can also be performed after the grinding, which is explained further on). The press cake then goes through a cake breaker in order to transport it already crumbled to the driers.
7. Drying: depending on the type of fish flour to be manufactured, either of the two drying systems is applied.

   · Flame-Dried (FD or Fair Average Quality - FAQ): this will result in the FAQ-type fish flour, of a low nutritional value.
   · Steam-Dried (SD): which results in the SD-type fish flour, of a greater nutritional value and accordingly, with a greater demand than the FAQ.

The purpose of the drying process is to reduce humidity to average levels of 10% approximately.

8. Grinding: at this stage the dry flour is afforded the grading, according to the customer's specifications. After obtaining the required fish flour, the latter is transported to the bagging room.
9. Bagging: at this stage, the flour is put in bags, ensuring the weight and maintaining the flour's humidity and temperature conditions, as well as controlling the required amount of antioxidant.

1 The released fat is separated to be sent to the fish oil production process.

2 The liquid obtained from this separation is called Press Liquor and is used in manufacturing fish oil.

The bagging process thus concludes the manufacturing of fish flour, which is then sent to the finished products stores or shipped to the destinations where it is required.

3. CASES STUDIES:

The cases presented here are real and were selected for audit based on the analysis of noncompliance indicators and their relevance.

CASE 1. Empresa MAR

Economic activity:

Company MAR carries out economic activities that include:

- Extraction of hydro-biological species.
- Transformation into fish flour and fish oil.
- Commercialization in the national and international markets.

Operations analyzed:

- Over 10 million dollar sales of fish flour to clients located in a tax haven, (Hong-Kong).

Analysis method

The internal CUP method was discarded for quality differences of products traded with the taxpayers located in the tax haven.
The external CUP method was discarded due to absence of external information.

The Cost-plus Method is applied.

Audit process

- **The form in which the taxpayer applies the Method is analyzed, and the following peculiarity is detected:**

The value of the Gross Margin/Sales Cost for the comparable is calculated using a three-year average.

The value of gross margin/Sales cost is then analyzed for the audited company (MAR) also using 3-year information and, since the indicator of that three-year period was in the interquartile range established by the comparable, the taxpayer concludes that it is the market value.

MBci MAR			
33.36%	1st Quartile	Mean	3rd Quartile
	32.70%	60.97%	85.93%

- **The possibility of challenging the taxpayer´s proposal is analyzed:**

The conclusion is that there is a fundamental error in the statement, because the issue at stake is whether the value agreed in 2007 is a market value or not.

Secondly, there is no reason to add information on three years about the audited company.

- **It is decided that the method will not be challenged, since there is no information available.**

  Gross Margin according to SUNAT.

MBci MAR			
21.17%	1st Quartile	Mean	3rd Quartile
	31.26%	59.26%	96.23%

The inconsistency was clearly explained to the taxpayer who was convinced and paid 1.5 million dollars for the difference in valuation and the fines.

It is worth mentioning that the taxpayer's adviser tried to object the final compensation. Nevertheless, the auditor informed the company’s board about the findings at all times and they concluded that the most reasonable line of action was to correct the difference.

CASE 2. INCA

This case also refers to a fishery and will evidence how in specific circumstances, even with the odds against him, a taxpayer may resort to litigation.

Economic activity:

INCA carries out economic activities which include:

- Extraction of hydro-biological species.
- Transformation into fish flour and oil.
- Commercialization in national and international markets.

Operations analyzed:

- Sale of fish flour to a client located in a tax haven for 23 million dollars.

Analysis method

The taxpayer proposes the application of the Transactional Net Margin Method

Audit process

- The form in which the taxpayer applies the method is analyzed, and the following peculiarity is detected:

The taxpayer calculates the value of the Profit Level Indicator- Net Additional Cost, of its comparable using 3-year information and defines an interquartile range.

In the analysis of his comparable, coming from Denmark, Norway and Chile, the taxpayer did not prove that they carried out the same functions as the company being examined.

In effect, except for a Chilean company, the other companies were not public, for which reason the taxpayer could never prove that they carried out similar functions to those of the company being examined.

Information according to the taxpayer:

INCA	Comparables		
9.15%	1er. Quartile	Mean	3rd Quartile
	3.32%	5.85%	13.19%

- **The possibility of challenging the taxpayer´s statement is analyzed:**

There were two important reasons for challenging the comparable:

1. It was not proven that they carried out the same functions.
2. They had no public information; therefore, it was impossible to verify the validity of the information.

It is concluded that the comparable were not sustainable and calculations are made with other comparable flour companies that operate in Peru and Chile, which are the main fish flour producers.

Information according to SUNAT:

CAN INCA	CAN comparables		
9.15%	1st Quartile	Mean	3rd Quartile
	12.94%	17.75%	28.70%

- **The taxpayer's decision.**

In view of the argument, the taxpayer changes the technical transfer pricing study, using the External increased cost method, with the financial statements of independent third parties that carry out similar functions as comparable.

MBci INCA	**Mbci comparables**		
47.49%	1st Quartile	Mean	3rd Quartile
	46%	50%	55%

The method offered by the taxpayer in this second study is challenged by the Tax Administration for the following reasons:

1. There is no sufficient information to determine whether the accounting practices are similar. Thus, for example, for INCA, several items are considered indirect costs and it cannot be determined whether the comparable give these items the same treatment.

2. Some of the comparable have other businesses besides fish flour sales and there is no way in which the financial statements may be segmented.

For these reasons, the application of the increased cost method was rejected by the Tax Administration, while continuing to apply the Transactional Net Margin method with the comparable identified by the Tax Administration.

Case Study

Topic 2.3

ADVANCE PRICING AGREEMENT - APA, BI-LATERAL ADVANCE PRICING AGREEMENT - BAPA, MULTI - LATERAL ADVANCE PRICING AGREEMENT – MAPA

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Content: *1. In general. - 2. Characteristics of advance pricing agreements. - 3. Advance pricing agreements within the context of Dominican Republic. - 4. Current situation and future challenges. - 5. Other Experiences. - 6. Lessons learned.*

1. IN GENERAL

Advance pricing agreements (APA's) are agreements between the Tax Administration and the taxpayer, with the objective to establish a previous methodology for certain trading or financial operations between them, and which is valid for a specific period of time. According to the OECD: "An arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparable and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time".

The purpose of these agreements is to avoid conflicts in the control of international transactions, whether they are unilateral1, bilateral2 or multilateral. They should all be legally based through provisions in their domestic legislation and/or under agreements to avoid double taxation and fight tax evasion generally included in article 25 both in the OECD tax Convention Model as well as in the UN Model, considered as a

1 *It is the one where the tax administration and the taxpayer, within the same jurisdiction, made a mutual agreement, without the presence of any other tax administration. In accordance with paragraph 4.129 of the OECD guidelines, the unilateral APA's can affect the tax obligations of companies involved in other tax jurisdictions; so it is suggested to inform the tax administrations interested or affected by the case.*

2 *They are the ones in which the will and the agreement of several tax administrations from different jurisdictions are combined. In this case, the aim is to reduce the double taxation and establish equitable criteria for all the administrations involved in the agreement.*

friendly procedure. It is worth noting that these two conventions are the international reference when referring to the international double taxation.

Given the importance of the use of transfer pricing in transactions between related enterprises, some countries in the region such as Ecuador, Honduras, Mexico, Peru and recently Dominican Republic, have extended their regulations for the control of transfer pricing including the APAs.

2. CHARACTERISTICS OF ADVANCE PRICING AGREEMENTS

The advance pricing agreements are within the framework of an innovative trend with the main object to avoid conflicts between the taxpayer and the tax administrations, reduce compliance control costs, and increase the legal certainty for taxpayers, since it is known that these agreements will govern the ways that each party will play. Among their main characteristics are:

a. They formally begin under the taxpayer´s initiative.
b. It is an agreement that engage both the taxpayer and the Tax Administration.
c. It is an agreement with a fixed period of time.

2.1. APA's Phases

1. Phase for providing the documents and information prior to the proposal: taxpayers will first present a series of documents and information referred to the subjects involved as well as the operation and its valuation.

2. Phase for presenting the proposal: once the period for the evaluation of the documentation and information previously presented is over, the final valuation proposal will be submitted along with the technical documentation.

3. Phase for examining the proposal: this is the preliminary examination phase that takes place within the tax administration in which taxpayers may also be required to cooperate, and even be able to present evidences and arguments.

4. Resolution: the resolution shall approve or reject the proposal. The rejection can be both explicit and therefore motivated, as per silence, if there is no answer within the established time, it will be considered rejected.

5. Recourses: the resolution issued by the administration shall not be liable to any appeal.

3. ADVANCE PRICING AGREEMENTS WITHIN THE CONTEXT OF DOMINICAN REPUBLIC

3.1. Background

Advance pricing agreements for pricing of transactions between related parties were included in the Dominican tax legislation in 2006. The amendment included in the Dominican Tax Code (CTD) sought to provide answers to harmful planning strategies carried out by companies involved in the all-inclusive hotel services3.

In Dominican Republic the business model of the all-inclusive hotels makes possible the relocation of profits to territories of lower taxation and tax havens. This is due to the high level of internationalization and characteristics of the industry. The following risks and functions are distributed through different actors, related to the services provided to the final consumer, the tourist, such as: the administration of the establishment, the distribution and the marketing, among others. In the case of Dominican Republic the tax loss generated by the use of transfer pricing in the sector is around USD$100 to USD$125 million yearly.

3.2. Tax planning of all inclusive business

The revisions made to the all-inclusive hotels activities showed their strong foreign connections, which facilitates transfer pricing in order to relocate profits to other jurisdictions. This premise could be verified through the analysis of a set of elements that emphasized their abusive use such as:

1. The use of all inclusive hotels of a related company that performs the marketing of the rooms (the retailer), located in most cases in tax haven countries or in a very low taxation country;
2. Constant losses and high debts with the marketing companies. For more than 10 years the sectors´ taxpayers showed losses in their financial statements.
3. The night rates per guest declared before the DGII were lower than the operating cost per guest declared.
4. The advertised rates were higher, in more than one hundred per cent, to those declared to the DGII.

3 *The all-inclusive service is a form of hospitality, in which using a fixed rate contract, the hotels provide accommodation services which includes all meals, alcoholic and non-alcoholic beverages, recreational activities and entertainment, access to the beach, among others.*

3.3. APA's examination and negotiation processes

The examination processes carried out before 2006 did not generate the expected results for two reasons: (i) The strong foreign connection presented by the activity and (ii) the lack of legislation for the valuation of operations between related parties. These limitations did not allow the Administration to challenge the planning schemes used by these companies through transfer pricing for moving wealth to other jurisdictions, to schemes of lower taxation and to tax havens and this way reduce the tax burden in Dominican Republic.

The legal provisions on transfer pricing, prior to the 2006, 2011 and 2012 amendments did not allow the Tax Administration to better operate. The above-mentioned provisions neither were updated in relation to the international reality nor established a formal coverage to the regulations on transfer pricing audits.

In 2006, through law No. 495-06, an amendment to the tax code takes place, introducing elements that were necessary for the determination and the valuation of the transfer pricing between related companies and especially for those companies with all inclusive hotel activities. This article established the provisions on advance pricing agreements, being the basis for determining the comparability rates parameters per area, cost analysis and other variables of the all-inclusive hotel activity.

The power to agree APAs was defined as follows:

Section II: For the sector of all-inclusive hotels, which business is connected abroad, the Tax Administration may define advance pricing agreements (APA's) on the prices or rates that will be recognized based on comparability rates parameters per area, cost analysis and other impact variables of the all-inclusive hotel activity. The sector will be represented by National Association of Hotels and Restaurants (ASONAHORES in Spanish) for signing the APA. The agreements will be published by a Resolution and their validity shall be eighteen (18) months. The subsequent agreements may be valid for up to 36 months. In cases in which Advance Pricing Agreement (APA) has expired and there is no new agreement, the previous agreement will continue to be in force until the new APA (Advance Pricing Agreements) is approved. The provisions of the Dominican Republic Tax Code on the determination of the taxes are in force. (Article 281, section f)

These prices or rates shall apply for the purpose of settlement and/ or determination of tax revenues for the transfer of industrialized goods and services tax (ITBIS)1 and from the operating income for income tax (ISR). The Tax Administration may challenge the taxpayers reached by the APA, the declared values when they do not correspond to the included criteria and will apply the penalties established in the Tax Code. The same treatment might be granted to processes related abroad, such as: the insurance, energy and pharmaceutical sectors. (Artícle 281, section g)

Perhaps the most innovative element in the former Dominican legislation with respect to the APA's, as they are defined in the OECD and in the laws of countries that have adopted measures for the control of the operations with related parties, is the impossibility to sign unilateral agreements. This made it extremely difficult to reach consensus on the methodology, margins or transfer pricing between the DGII and hotels. Furthermore, the execution of the APA was blocked by a variety of interests within the hotel industry.

The Tax Administration, after modifying the legislation on transfer pricing included in article of the CTD in 2009, leads again an audit process for the all-inclusive hotels, based on an audit sectorial strategy carried out by the areas responsible for external audits. The audits, to determine the taxable income of Dominican source, were based on the powers and elements that allowed the CTD at the time, basically by considering the limitations of the transfer pricing guidelines4, and complemented with the economic reality principles and the judicial power to determine ex office.

For the fiscal period (January-December) from 2007 until 2010, and in some cases 2005 and 2006, after the companies that operate all inclusive hotels submitted their corresponding returns; The tax base for the determinations of the taxable income of Dominican source, was determined on the basis of the rate per night to be paid by the guest or final client abroad. By using the described procedure between 2009 and 2011, 73 audits were performed. As a result, favorable judgments from courts were achieved as well as tax payments due from taxpayers.

Based on the results of the audits performed, taxpayers were informed about the determinations in order to give to give continuity to the legal provisions of the tax code and agree on advance pricing agreements.

4 *The article in the CTD on transfer pricing, article 281, 2010 was very limited. Even by specifying that the valuation of the benefits between related parties must be carried out in the manner that had been agreed between independents, the legislation did not include important elements for their determination, for example valuation methods. It is not until mid-2011 that general Rule 04-2011, provides a legislative framework that is broad in terms of transfer pricing as a definition of related party, valuation methods, and comparability adjustments to increase comparability, obligation of referral information and penalties for non-compliance.*

Since the APA were defined as collective agreements and in addition to the internal conflicts of interests of the sector, this prevented the signing of the APA DGII/ASONAHORES, despite the audit processes of transfer-pricing which the sector had been subject to in order to improve its tax compliance. This situation triggered the modification in November 2012 of the article about APAs in the Tax Code, eliminating the section on APA's and introducing new regulations in this regard.

4. CURRENT SITUATION AND FUTURE CHALLENGES

4.1. Modification to the Transfer Pricing regulations

With the publication of the law 253-12, to strengthen the State revenue collection for Tax sustainability and sustainable development, new amendments were introduced in the transfer pricing regulations and, in particular, on transfer pricing agreements

Article 281-bis was added, providing regulations on advance pricing agreements, establishing the general format through which the request for agreement will be presented. This article modifies the above mentioned provisions, allowing the negotiation of unilateral Advance Pricing Agreements.

Taxpayers may request agreements regarding transfer pricing from the Tax Administration, in which the trade and financial operations values with related parties will be established. As usual, this agreement has a fixed period of time and must be signed prior to the operations.

According to article 281 provisions, when requesting an APA, the taxpayer must present a proposal based on the values in which the transactions are paid between independent parties in similar operations. APAs can also include the financing of the taxpayers by third parties, in cases where the taxpayer is subject to interest deduction limitation. All these procedures apply for bilateral as well as multilateral agreements.

Once the proposal is reviewed, the Internal Tax General Directorate has the power to approve it, reject it or modify it, and this decision cannot be appealed. Nevertheless, if the proposal is modified, the taxpayer is not bound to sign the agreement. As established in paragraph 3 of article 281 bis, this agreement is effective for the current fiscal year and the three following tax exercises. Similarly, it applies for the tax exercise expired since the signature of the APA, until the agreement signature date, with a limitation of two tax periods.

In addition, article 281bis, paragraph V on protection regimes (safe harbors) was also included, by which the TA determines the arm's length Price in agreement with the activity or transaction, and the taxpayer may or may not accept the regime. Once this enters into force for sectors or transactions with known and identified risks, it would result in a better and more efficient control of tax planning through controlled transactions.

4.2. Application of the Code provisions

According to the current Dominican Tax Code provisions, the approval of APAs requires to complete the phases of knowledge, negotiation and discussion of the proposals, as well as their signature and verification. Currently, representatives from all-inclusive Hotel sector are discussing the signing of the agreements. Even if unilateral APAs can be signed, these negotiations have been collective.

Procedure:

1. ASONAHORES submits the proposal and documentation related to the operations and their valuation
2. The Tax Administration reviews the submitted proposal.
3. The proposal is discussed and negotiated by both parties (ASONAHORES-DGI). The Administration presents alternative proposals in relation to procedures and valuation of the sector activities.

Characteristics and contents of the agreement.

a. Various prices are proposed according to the category and geographical location of the taxpayer.
b. The rate is fixed based on the cost margin method to determine the amount of ITBIS (similar to VAT), and an effective minimal tax rate for the income tax.
c. Submit Information to verify that it complies with APA
d. It is valid for 3 years, plus the negotiation months.

5. OTHER EXPERIENCES

The Tax Administration has also negotiated simplified tax regimes agreements with agricultural associations of the Dominican Republic. In 2010, agreements with rice and milk producers of these associations were negotiated. These agreements establish a simplified tax procedure based on income, for those producers no having an organized accounting. Similarly, in 2012, a similar agreement was signed with banana producers.

The main objective is to reduce the compliance costs for small producers, granting them facilities for submitting of their income tax returns. The agreement exempts them from providing information on the tax vouchers and allows them to determine their net taxable income by applying the proper deductions. In spite of this, it must be noted that they are not Advanced Pricing Agreements, but they enrich the experience and negotiating capacities of the Tax Administration

6. LESSONS LEARNED

The development of negotiations to enforce the Advanced Pricing Agreements shows that there is not just a single method to face the taxpayer's planning strategies through transfer pricing.

It was concluded that strengthening these exchange of information agreements is important for our country, since this is the only way to establish objective criteria to apply transfer pricing rules. It would be an additional resource that the administration would have to reach the truth about the facts surrounding the taxpayer.

With the application of the agreements, legal security is improved, since the criteria and methods are agreed upon for operations described in the agreement, and this application may increase foreign investment. In addition, the risk of double taxation is reduced: In this case it prevents double taxation if the other Tax Administrations accept them.

Until today, the tax administration has not signed any Advanced Pricing Agreement with the Hotel sector. However, meetings have been held with representatives of this sector, in order to determine prices for reaching an APA. In this case, the DGII has established the methodology and has performed the estimates in order to establish the method and the net price/margin to be applied on the costs to determine the hotels' profits.

Case Study

Topic 2.3

ADVANCE PRICING AGREEMENTS (APAS), BI-LATERAL ADVANCE PRICING AGREEMENT, MULTI-LATERAL ADVANCE PRICING AGREEMENT

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Content: *Summary - 1. Introduction -2. Definition and general characteristics - 3. Advantages and disadvantages of the APAs - 4. Aspects of uruguayan legislation - 5. Unilateral versus bilateral (multilateral) agreements - 6. Stages of the procedure. 7. Temporal aspects of the agreement - 8. Administrative aspects - 9. Conclusions*

SUMMARY

In December 2011, the DGI subscribed the first advance pricing agreement; being the first signed in South America. The objective of this study is to describe its main characteristics, point out the various aspects that were considered at the time of its conclusion and, from this experience, highlight some recommendations that may be useful to other tax administrations.

The conclusion of this first agreement was a positive experience for both the tax administration and the taxpayer.

1. INTRODUCTION

1.1. International situation in the 21st century: a globalized economy

In general tax systems that had to deal with the globalization phenomenon were designed after the Second World War, within a trade protection and immobility of capital and labor environment. Therefore, it was about tax rules configured for a global context where the degree of interdependence and interrelatedness between the different national economies was limited. In that environment, it was feasible to apply very different rates of direct and indirect taxes.

However, this situation is no longer valid. The existing tax rules in different systems or national tax laws were formulated and within and for a world that in good measure, does no longer exists.

The last three decades have witnessed a liberalization and globalization of national economies without precedent, and predictions indicate that, at least, over the next three decades, that process will continue to intensify.

There are several reasons why companies internationalize their activity, having as ultimate reason the increase of their magnitude and volume. Business globalization is characterized by a number of factors:

i. The need to open markets to increase production lines and thus achieve higher incomes and a reduction of unit costs;

ii. search for the optimization of their production costs, which involves tax aspects, but also involves extra-taxation aspects (labor, raw materials, energy, etc.), justifying the need for companies to move production processes to those countries where there are certain comparative advantages;

iii. High capital mobility, generators of passive income under new technologies.

Today, we see a massive presence of multinational companies, their subsidiaries and other related ones with presence in different fiscal sovereignties. The international objective of these companies promotes the expansion of the corporate structure worldwide, motivating states to adopt all kind of fiscal measures.

1.2. Impact of economic globalization in tax systems

Economic globalization, as all economic phenomena, has its reflection in the tax field.

States have faced the need to rethink or reconsider the main fiscal rules that inspired the national tax systems, considering that such rules were elaborated and designed for a "World" that has ceased to exist as such. In this sense, the existence of a deficit of "old rules and principles" adaptation to the new economic and political context is warned.

Globalization of economic production processes greatly hinders the determination of the taxable bases of companies, which is due to factors such as the complexity to identify the source of the income (consider, for example, production chain processes carried out in several countries, in certain e-commerce operations or in the global trading operations), or the broad margin of maneuvers that taxpayers have as members of multinational enterprise groups to transfer taxable bases from one place to another in the world (tax base shifting).

An increasing competition among States to attract capital and investments can be identified as the main tax phenomenon; and together with this competition phenomenon the appearance of increasing conflicts in the application of the tax authority by the States (without doubt the most notorious is the conflict between the source and residence) and these conflicts are intensified as the economic and the capital activity is internationalized.

States witness, usually in a passive way, the distribution and location of part of their taxable income in territories outside their fiscal jurisdiction, decreasing the real possibilities to exercise the fiscal sovereignty of each State. The tax environment has led States become aware, and included among the variables that influence the design of fiscal policy: the international factor.

1.3. Transfer pricing

According to data from the OECD in the year 2002, more than 60% of international trade is conducted between multinational enterprises, making 50% of transactions between related companies, i.e., from the same group of companies [1]

As a result, the companies from the same group located in different jurisdictions can, through pricing, transfer benefits or losses from one to another jurisdiction, altering the tax base corresponding to each State.

Faced with this reality, tax rules on transfer pricing - both national and international-for the purpose of preserving the taxable bases in different States have been implemented.

Tax reform in 2007 (law Nº 18.083, of December 27, 2006) introduced the price controls agreed between companies through the establishment of transfer pricing regime in Uruguay.

1 *NEIGHBOUR, JOHN, "Transfer pricing: Keeping it at arm's length", The OCDE observer, April 2002.Available on the website: http://www.oecdobserver.org/news/fullstory.php/aid/670/Transfer_pricing:_Keeping_it_at_arms_length.html.*

This regime is regulated in Chapter VII of the title 4 of the text ordered in 1996, regulated by decrees no. 56/009 and 392/009 and resolutions issued by the General Tax Directorate.

Given that transfer pricing is not an exact science, but require judgments of value both by the tax administration and the taxpayer, usually present uncertainty situations that can result in conflicts between them. The advanced pricing agreements (or "Advance Pricing Agreements", hereafter APAs) are presented as an instrument that aims to minimize the uncertainty.

It is well known, that the application of the arm´s length principle[2] can lead to situations of controversies. These disputes may arise not only between the taxpayer and the tax administration, but also within tax administrations when they analyzed the income which is attributed to their own jurisdiction. Moreover, the increase in international operations between multinational companies requires that tax administrations need to provide human and material resources because it is a very controversial and complex area and in many cases difficult to proof.

Is thus the APAs are presented as a complementary mechanism in the field of transfer pricing that allows to reduce its subjectivity degree, as well as reduce tax evasion and grant greater legal and economic, security both to taxpayers and the tax administration.

They constitute a complementary solution to the traditional procedures provided in domestic legislation and the international treaties to resolve issues relating to this matter.

2. DEFINITION AND GENERAL CHARACTERISTICS

Article 4.123 of OECD guidelines[3] defines the APA as "an agreement that determines, prior to the execution of transactions with related entities, a series of appropriate criteria (concerning, for example, the method, the comparable, appropriate adjustments and the critical assumptions relating to future events), for the determination of the transfer pricing of such operations in a given period of time".

2 *Its Foundation is supported by considering the different members of a multinational group as if they were businesses separate rather than view them as inseparable from a single unified company parties.*

3 *Guidelines on transfer pricing for multinational enterprises and tax administrations issued by the Organization for cooperation and economic development (OECD), published on July 22, 2010.*

With the signature of this agreement, the administration warrants to the company that it will not perform any readjustment of the price if it follows the conditions defined by the APA. [4]

These criteria often include the selection of the most appropriate method, its form of implementation, the identification of the comparable, adjustments for comparison and description of assumptions or critical assumptions that may influence the agreement in the future. In general, the purpose of the APA is not to fix in advance the “transfer pricing operation" but agree on the methodology, criteria and assumptions so that the taxpayer can apply with greater security the arm’s length principle.

Depending on the parties involved in the agreement, the APAs can be classified as unilateral, bilateral or multilateral. In the unilateral APAs, the tax administration and the taxpayer of its jurisdiction establish an agreement without the intervention of other interested tax administration. On the other hand Bilateral (multilateral) agreements, also involve other (or others) tax administrations. While the OECD prefer these last ones, because they guarantee greater legal certainty to the taxpayer as well as reduce the possible effects of double taxation, these turn out to be more complex and more expensive, and require a greater amount of time for their completion. In countries such as Uruguay, where agreements to avoid double taxation and prevent fiscal evasion regarding income and capital taxes (hereinafter, CDI) recently began to be applied and the practice of transfer pricing is relatively new, unilateral agreements constitutes a good starting point in this matter. This position seems to be shared also by the UN when paragraph 3.10.1 of the practical Manual on transfer pricing for developing countries[5] (hereinafter UN Manual) points out that although the unilateral APAs are qualified as partial solutions to double taxation, they are also considered useful in specific cases.

The APAs are different from other instruments such as tax consultation or resolutions.

In general, these last ones are intended to determine the taxation regime of certain facts, only reached for law purposes (i.e., interpretive aspects and/or application of a legal standard). In such cases, the tax administration does no perform research activity on the real situation

4 *In the agreement can be seen a revision or annulment of the same clause when significant variations in operations concluded by the taxpayer, or when the comparable operations in uncontrolled circumstances vary so influence on the reliability of the method in it established.*

5 *The United Nations Practical Manual on Transfer Pricing for Developing Countries. Genève, October 2012.*

presented, which is always subject to further verification. In addition, these instruments can have a broader scope, covering a group or all taxpayers who qualify. On the other hand, during APAs signing procedure, the tax administration should prior verify the facts and circumstances that make the specific case, limited to operations held by the taxpayer with its related entities.

3. ADVANTAGES AND DISADVANTAGES OF THE APAS

Although the APAs are complex projects, which perform time and significant resources of both parties, they present a series of advantages for both.

The main advantages that present include the following[6]:

i. They allow taxpayers to have certainty about the tax treatment of transfer pricing of transactions with related entities, during a given period.

ii. They provide the opportunity for tax administrations and taxpayers to consult and cooperate with each other in a spirit of conciliation. Given that both sides seek to reach an agreement on a framework of friendly negotiation, as opposed to what can happen in a context of auditing or dispute resolution, a greater collaboration on both sides is observed, facilitating a greater exchange of information and a greater objectivity reviewing data and information.

iii. They can avoid long and costly inspections.

iv. Given the context of cooperation between the parties, they allow the tax administration to better understand certain complex international operations carried out by multinational companies. In this sense, it is possible to know and better understand extremely technical aspects and elements of certain areas of activity. Moreover, the development of highly specialized skills on certain sectors or certain types of operations will enable tax administrations to give a better service to taxpayers who are in similar situations. Through the negotiation process, tax administrations can access to sectorial data and the analysis of pricing determination methods is very useful in a collaborative environment.

With respect to unilateral APAs, the UN justifies their existence in particular cases, pointing out as advantages the fact that they can prevent conflicts between the tax administration and the taxpayer, particularly when the local transfer pricing provisions are not sufficiently detailed. They can also be particularly useful when

6 *Based on the comments made in the numerals 4.142 to 4.146 of the OECD guidelines*

analyzing new topics, to the extent that the tax administration has the opportunity to more fully analyze the topic before issuing a general resolution.

The main disadvantages presented, include the following[7]:

i. To the extent that agreements are unilateral, there is no guarantee that they may avoid questions in other jurisdictions with respect to operations subject to the agreement. In that sense, when they are not bilateral or multilateral agreements from the group´s perspective, if avoiding uncertainty in the field of transfer pricing transactions is the purpose of the agreement, possible effects on international double taxation can also follow.

ii. As a consequence of the possible double taxation commented above, the need for correlative adjustments may arise[8]. The flexibility afforded by an agreement can lead the taxpayer and the related company to agree on their prices within an authorized range. As a result, in a unilateral APA it is absolutely necessary that this flexibility will stick to the arm´s length principle (or full competition), since a competent foreign authority will probably refuse a correlative adjustment derived from a not agreed APA, from this point of view.

iii. They can initially be a considerable burden for those responsible for the verification of transfer pricing, because it is likely that tax administrations need to divert resources assigned to other purposes (e.g., inspections, consultations, litigation, etc.).

iv. They often depend on the demands of the business community. These demands may not coincide with the tax administrations resource management plan, which will hinder the efficient development of agreements and other equally important work.

v. Difficulties in the correct identification of the circumstances of fact as well as the critical assumptions of the agreement (to the extent that it is analyzing how to assess future operations).

vi. Tax administrations need time to become experts in specialized fields, in order to respond to requests submitted by the taxpayer or other tax administrations.

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7 Based on the comments made in the numerals 4.142 to 4.146 of the OECD guidelines.

8 Defined in the OECD guidelines as the "adjustment of the tax debt of the undertaking established in a second fiscal jurisdiction, practiced by the tax authorities of that jurisdiction after the primary adjustment made by the tax administration of the first jurisdiction, in order to distribute the benefits between the two countries consistently..

vii. Some countries show that taxpayers interested by the APAs are very large companies regularly subject to inspection. It is also observed that taxpayers who have experienced difficulties with the tax administration in the area of transfer pricing and who wish to put an end to them tend to be interested in the application of these agreements. With this situation, there is a risk to divert those contributing resources and expertise that perhaps would be preferable to allocate to the inspection of other taxpayers, where those resources could be used better by reducing the risk to loss of revenue. The balance of the resources allocated to compliance can be particularly difficult to achieve because APAs program usually requires a very experienced and often specialized staff. Tax administrations need time to become experts in specialized fields.

viii. They may require more detailed information on a branch of activity or a taxpayer. Although, in principle, the documentation required for an agreement should not be more onerous than for an inspection of transfer pricing, tax administrations need more detailed information about predictions and their foundations, which would not be essential in the context of a transfer pricing inspection (which based its analysis on past events).

ix. Not all taxpayers can access the negotiation of the agreements procedure because of the cost and time spent on these, even more when it comes to complex operations that require the participation of independent experts in the field. There may also be budgetary restrictions for the tax administration itself which bring it to reject applications. These problems can be attenuated by making sure that the depth of analysis corresponds to the importance of international operations in question.

Subject to the foregoing, the APA can be considered a conservative procedure that provides taxpayer certainty about the tax treatment in the field of transfer pricing applicable to certain transactions or business segment.

It is important to mention that within the international business scope in which we are immersed, a taxpayer must comply with various tax provisions in each of the jurisdictions in which it carries out business activities; so the establishment of a policy of transfer pricing that can meet the expectations of various tax authorities becomes a primary goal.

As a result, taxpayers often assess the cost-benefits relationship in each of the jurisdictions. They evaluate the risk of being audited (which eventually results in determinations and adjustments in the field of transfer pricing) versus applying a conservative policy which, even if representing a different distribution of profits, reduces risks with the fiscal authorities.

The APA is a procedure that allows both taxpayers and tax administrations to minimize risks in the field of transfer pricing, especially if we speak of a bilateral or multilateral APA.

4. ASPECTS OF URUGUAYAN LEGISLATION

Article 44 bis of Title 4 of the T.O. 1996, in law No. 18.996, sets: "the Executive power may provide the application of an advance pricing agreements system with taxpayers within the framework of the transfer pricing regime established by this chapter. Such agreements must be signed prior to the transactions involved, and may not exceed three fiscal years".

Article 15 bis of the Decree 56/009[9], a regulatory regime that says: "the Argentine tax authority may sign price agreements with taxpayers, who must sign them prior to the transactions involved, and may not exceed three fiscal years. The referred deadline applies to closed exercises from that on which the regime enters into force. The national tax administration shall establish the conditions and formalities prescribed for the signing of such agreements."

Other provisions in the matter have not been issued to the present date.

As it can be seen, domestic legislation provides for the possibility of holding this type of agreements with taxpayers. At first, these will be unilateral, to the extents that they are voluntary agreements between the tax administration and the taxpayer who requests them. Unlike other countries, the signing of bilateral or multilateral agreements has not been explicitly mentioned. However, and as we shall see in paragraph 5 of the present work, these may be held whenever the subject of the analyzed transaction affects a resident of another State with which Uruguay has entered into a Commission which provides for the possibility to carry out a friendly procedure or mutual agreement.

The APAs regime in Uruguay does not include the possibility of retroactive agreements because it excludes transactions before the signature. Once the agreement is signed, the same shall not exceed three fiscal years (it can be one, two or three exercises, at the option of the parties). This period shall apply to exercises from the one becoming effective regime. Given that the APAs signature

9 *Added by article 7 of the 392/009 decree dated 24/8/2009*

process usually takes several months (DGI does not have a certain period to issue it), the computation of this term may present some practical difficulties depending on the type of transaction, which will be discussed in paragraph 8 literal iii of this work.

There is no limitation as to the nature of transactions which may include several or all of the transactions held by the taxpayer with the related entities, whatever their nature. On the other hand, while the taxpayer is to decide which transactions have to be included in the request, the DGI may include other transactions that it deems appropriate (appearance that will be discussed during the process of acceptance of the agreement, as we shall see in paragraph 6 of this paper).

This regime gives broad powers to the DGI to accept or reject the agreement. If the DGI rejects the APA request (if having accepted in the first instance but did not reach an agreement with the taxpayer, his request is dismissed), it should give its view to the taxpayer and explain the reasons for its decision. To the extent that it is an administrative act, it is appealable (although in practice it is difficult that to happen). On the other hand, the taxpayer also reserves the right to accept or reject the Administration's proposal.

Regarding the formal aspects, the DGI has established a manual of internal procedure, which sets the conditions and formalities that will be required for the conclusion of an APA, which are discussed in the paragraph 6 of the present work.

Finally, unlike in some other countries, the present regime does not require the payment of any fee for subscribing this type of agreements.

5. UNILATERAL VERSUS BILATERAL (MULTILATERAL) AGREEMENTS

If problems posed by transfer pricing are likely to produce an effect of double taxation or create difficulties or doubts as to the interpretation or application of the agreement, a bilateral agreement (or multilateral) could be signed.

While Uruguayan law does not explicitly mention bilateral or multilateral APAs, but simply states that the DGI may conclude price agreements with taxpayers, it can be argued that these can be concluded under the mutual agreement procedure provided for in DTC.

According to Calatayud Vazquez [10] (2011): “The APAs in which the competent authority of a treaty member is involved must be considered within the scope of the mutual agreement procedure mentioned in art 25 of the OECD Model Tax Agreement (...), even if such arrangements are not mentioned explicitly "(p. 257). For this author, "when a tax treaty has a clause on mutual agreement procedures similar to Article 25 of the OECD Model, the competent authorities, in general, should be allowed to conclude APA, because otherwise aspects of transfer pricing situations could result in double taxation or pose difficulties or doubts concerning the interpretation or application of the treaty "(p. 258).

In a similar vein, Rodriguez Ondarza[11] notes that "to the extent that tax treaties take precedence over domestic law, the absence of a legal basis in domestic law for the conclusion of an APA would not prevent the implementation of an APA on basis of mutual agreement procedure ". This would imply that even in those countries which do not provide expressly for APAs regimes, such agreements could also be concluded under the DTC framework.

As noted Calatayud Vázquez[12]: "If this procedure is performed under the mutual agreement procedure provisions contained in tax treaties, the agreement eventually reached is an agreement between competent authorities, so that if the taxpayer does not accept the terms of the agreement, he could withdraw its request for bilateral APA.

This entails that in cases of bilateral APAs, authorities and taxpayers must be competent and in constant communication. "

Pursuant to the foregoing, the existence of DTCs in practice makes possible that unilateral agreements become-in fact-in bilateral within the mutual agreement procedure provided therein.

At the time of this study, Uruguay has nine DTCs and two Information Exchange Agreements in force. In general, the DTCs concluded by Uruguay include art. 25 of the OECD Model Tax Convention on Income and on Capital (hereinafter OECD MC), which would allow the tax authorities to conclude such agreements. Given the early

10 *CALATAYUD VÁZQUEZ, Adolfo: “Acuerdos anticipados en materia de precios de transferencia APA”. In Precios de Transferencia. Mexico: Instituto Mexicano de Contadores Público, A.C., 2011.*

11 *RODRIGUEZ ONDARZA, José Antonio. Una revisión global de la aplicación de los acuerdos previos sobre precios de transferencia y sus implicancias para España. Madrid: Universidad Complutense de Madrid, 1998.*

12 *CALATAYUD VÁZQUEZ, Adolfo. Op. Cit., pág. 281.*

stage of the rules in question, to this date Uruguay has no experience in the conclusion of bilateral or multilateral agreements.

Notwithstanding this, it is worth noting some aspects that should be considered in this context:

i. First, there is consensus that such agreements can reduce the possible effects of double taxation, to the extent that the Tax Administration agrees. If they are not able to agree, it should be considered if the agreement in question provides an arbitration provision. The arbitration provided is an integral part of the mutual agreement procedure and does not constitute an alternative way of resolving tax disputes between States.

ii. It will be noted that the bilateral (multilateral) APA involves negotiations with another tax administration, which will focus on the application of the arm's length principle, as a guiding principle to allocate the income between jurisdictions. In this context, the variables to ponder in an area of negotiation are others. So numeral 4.162 in OECD Guidelines states that from the perspective of the taxpayer, it is less likely that they will feel compelled to conclude or to accept an agreement if it does not comply with the full competence principle in order to avoid costly and lengthy inspections and possible sanctions. In these cases, any disputes that may arise do not constitute mere disputes between the taxpayer and the tax authorities, but involve differences between Tax Administrations, so the negotiation process is more complex. It can be seen that in this case the taxpayer's role is more passive, but as said before, the taxpayer should be informed of the progress in the process.

iii. In case an agreement between the Tax Administrations is not reached, the question arises whether the DGI can also hold a unilateral agreement with the taxpayer. This question is not covered by the internal normative. Some Spanish authors argue "that the lack of agreement with the other state should imply, in most cases, the internal approval of the proposal by the taxpayer since, by having submitted the proposal to the other State means that the Spanish Administration considered it appropriate, otherwise, they would have denied the processing.

However, this automatic approval effect is not provided by domestic law[13]. The same question is posed from the Uruguayan perspective. To our knowledge, the

13 *In opinion of MORENO FERNANDEZ, quoted by VILLAVERDE GOMEZ, Maria Begoña, in: "Acuerdos anticipados de Precios de Transferencia", Precios de Transferencia, Revista Latinoamericana de Derecho Tributario, 01, Del Instituto Latinoamericano de Derecho Tributario (ILADT). Editions Tributarias Latinoamericanas, Venezuela, 2005. Pag. 204*

Tax Administration retains the right to conclude an agreement with the taxpayer as long as the legislation does not forbid it, even if it had been rejected by other tax authorities in connection with a DTC.

iv. If it is the external Tax Administration which proposes the agreement, the DGI should respond to this request under the mutual agreement procedure provided in its DTCs. This can be important because, although to this date there is no clear conclusion of such agreements in the short term (because of their complexity and the time and costs involved), it may be that foreign tax administrations implement this mechanism, ahead of planning.

v. Developing countries have disadvantages due to their limited resources and expertise in the field, leaving their tax administrations in unfavorable position against the tax administrations of developed countries. In this area, resources for staff training are usually required, access to databases-usually-expensive, consulting independent experts, foreign travel and training in general, etc. To minimize the need for resource (already scarce) of the Tax Administration, it is very important to design the process of mutual agreement as efficiently as possible.

vi. While the mutual agreement procedure program is viewed as complex, consuming time and specialized resources, which often curb tax administrations to take this step, the UN notes that those countries that have implemented it (despite the disadvantages discussed above), have been able to benefit from these experiences. Thus, numeral 3.11.5 of the UN Manual states "In the early stages of the mutual agreement procedure, Japan experienced the disadvantages commented earlier. However, after developing a good relationship with several partner countries, a lot of information was shared successfully. Therefore, practical and intensive discussions on transfer pricing methodology or the comparability analysis quickly improved the ability of the Japanese tax authorities. (...) The Indian experience has been similar to that effect. ."[14]

6. STAGES OF THE PROCEDURE

The process of concluding an APA generally involves a series of steps that, in one way or another, are recognized in all countries. These steps relate mainly to the following instances: preliminary meetings, agreement proposal, analysis, documentation and control.

In the case of Uruguay, the DGI held the first APA (unilateral) with the taxpayer in December 2011. Based on this practical experience, the

14 Numerals 3.11.5 y 3.11.6 of UN Manual.

Large Taxpayers Division of the DGI developed a procedure manual on the conditions and formalities for the conclusion of such agreements, which are defined as internal use for the Tax Administration officials.

Here are summarized the general features of the stages defined in the manual, namely:

i. Pre-Interview

The taxpayer has the opportunity to request to meet the DGI General Directorate prior to the formal application of the agreement. The main purpose is to determine its feasibility and scope.

At that time, the taxpayer explains the type of operations to be analyzed, the characteristics of the goods or services concerned, the functions, risks and assets of the company, the special economic circumstances that must be taken into account, the transfer pricing methodology to be applied, apart from all other considerations deemed relevant.

This procedure allows the DGI have an informal approach to the situation in order to assess the circumstances and complexity of the case.

ii. Formal request for agreement

Without prejudice to the previous point, the taxpayer who wants to conclude an APA with the DGI must formally request it in writing.

The request will be submitted along with a transfer pricing study made by the taxpayer, formalized in a file.

iii. Analysis conducted by the General Directorate

The General Directorate will review the request and, if applicable, authorizes its study, referring the case to the Large Taxpayers Division, for consideration by the Department of International Taxation.

iv. Technical Report

This stage includes analyzing the transfer pricing study which must contain the following information, without prejudice of any other requested during the negotiation phase, namely:

- Identification of the taxpayer;
- Operations analyzed in the present agreement;
- Requested period;

- Overview of the business and operational detail;
- Local and international Organizational structure;
- Composition of the share capital;
- Transfer pricing policies;
- Business Strategies;
- Functional analysis of each of the companies involved in the operations object of the analysis, explaining the functions performed, assets involved and risks assumed;
- Description of operating procedures;
- Method used for the determination of transfer pricing operations, indicating the reasons that justified this method as the most appropriate, and the reasons for rejection of other methods.;
- Numerical applications on historical and / or projected balances figures.
- If applicable, appropriate net income indicators;
- Description of criteria for the selection of comparable. To identify the potential selected comparable, indicating the reasons for their acceptance or rejection;
- Quantification and methodology used to apply the necessary adjustments on the selected comparable (comparability adjustments);
- Economic circumstances underlying the validity of the agreement which must be maintained so that the proposed methodology remains acceptable (critical hypothesis);
- Financial statements and financial information detailed by product line or business segment;
- Existing Contracts between the parties;
- Administrative or judicial antecedents related to the proposed methodology, if any;
- APAs concluded with other tax administrations, signed by the taxpayer as well as by other related entities related to the multinational group to which it belongs, especially those APAS that have operations similar to the one considered in the analysis.
- Accreditation of persons authorized to represent the applicant;

The International Tax Department will examine the petition, along with the information and documentation provided during this phase. On base of this information and other items that may arise during the negotiation itself, a first draft agreement will be elaborated.

v. Anticipated Pricing agreement

If the opinion of the International Taxation Department is favorable and the General Directorate supports it, the agreement will be implemented in accordance with the draft prepared, which is a contract.

This contract will be signed by the taxpayer and the Director General of Revenue, highest authority of the DGI.

v. Adverse decision

If the opinion of the International Taxation Department is unfavorable, in agreement with the General Directorate, the request will be rejected and this decision will be communicated to the taxpayer. The rationale and grounds of the decision will be communicated to the taxpayer.

a. Practical aspects taken into account in order to conclude an APA

In this chapter, we present some of the most relevant practical issues that were taken into account in the specific case:

i. As we noted above, such agreements define a series of criteria related to the selection of the comparable method of analysis, comparability adjustments and definition of hypotheses or critical assumptions that determine the above definitions and are related to future events.

To the extent that these agreements must be subscribed prior to the completion of the transactions involved, a number of assumptions must be made and some variables must be predicted (commonly known as hypotheses or critical assumptions). In this regard, it is particularly important to be extremely cautious as the facts and circumstances that are part of the agreement may change in future periods.

The OECD Guidelines admit in numeral 4.124 that the degree of specificity is one of the key issues in the conclusion of such agreements. i.e., if they only refer to the definition of the methodology, application and critical assumptions, or if they further comprise specific issues that relate to future results (for example, the comparable rates of return, etc.).

When considering the scope of an APA, it is necessary that the TA provide particular attention to the nature of the analyzed transaction, as well as the facts and circumstances that determine it. The degree of specificity of the predictions will depend on their nature and the critical assumptions which condition them. In the approved APA it was understood that it was possible to adopt a more focused approach regarding its scope and a broad approach in defining critical assumptions, since it was justified by the specific circumstances. However, this aspect will need to be evaluated in each specific situation.

ii. It is understood that while an APA contains a consensual element it should be assimilated to a "contract" between the tax authorities and the taxpayer, not to a resolution of the DGI, which is an unilateral act of the Administration.

iii. Given the need for highly specialized resources (already scarce), it was not possible to accept all applications submitted to the Department during the preliminary interview stage discussed above. For this purpose, selection criteria (or rejection) are cases presenting certain characteristics, such as a recently audited similar company (where the Tax Administration had already invested time and resources in the audit); a company which would not operate in the marketing of goods with price known in transparent markets (because of the complexity of the transaction), etc.

Taking this into account, it was understood that during the pre-interview stage it is possible to have a preliminary meeting with the advisers of the taxpayer only (at his request), with no obligation to disclose the name of the taxpayer.

In 2011 two cases were accepted for study.

During the review process of the two requests formally submitted for the conclusion of the agreement, one of them was withdrawn by the taxpayer.

iv. For the purpose of monitoring the correct application of the APA, it was understood that taxpayers must submit an annual report which is a record of compliance with the agreement and the maintenance of all hypotheses and critical assumptions on which it was agreed. This report will include a copy of the financial statements.

b. Recommendations

Based on the experience mentioned above, some general recommendations can be drawn, namely:

i. Adoption of the regime in domestic law

To conclude the first APA some years after the application of the transfer pricing regime was a positive experience.

The Tax Administration adopted conservative criteria to define the number of agreements that it could manage with the available resources and to define the profile of the taxpayer that could lead to his identification (or not).

Meanwhile, the regulatory framework governing the scheme is flexible, because it simply gives the option to enter into such agreements for a specific period, empowering the Tax Administration to define the requested conditions and formalities.

ii. Scope of the agreement

While the APA is scheduled for transactions between related parties under the transfer pricing regime framework, it might be advisable to expand its scope to other international operations. For example issues having to do with the allocation of income and / or expenses from permanent establishments.

7. TEMPORAL ASPECTS OF THE AGREEMENT

While the legislation is clear about who will comprise a maximum period of three fiscal years, some practical issues regarding the computation of these exercises may arise.

From the time the taxpayer files the application and the moment of signing the agreement, more than a year can elapse, and the new agreement will apply to transactions after the signature. The regulations of some countries include within the APA the transactions from the time the taxpayer files the application. This solution seems reasonable given the cost and time invested by taxpayers and the tax authorities in the conclusion of such agreements. In such cases, the period between the request and its signature should be adjusted later, after the signature; adjustment which we believe should be defined in the agreement itself. As of this date, the current legislation does not allow to adopt such solutions.

For years prior to the application of the APA, although the rules are clear in that they are not included in the agreement, there may be questions regarding the criteria adopted by the taxpayer so far, especially regarding exercises not yet audited by the tax administration. That is why taxpayers who have been audited are preferred for concluding such agreements.

8. ADMINISTRATIVE ASPECTS

As noted, the APA process must be designed to be as efficient and effective as possible, especially in countries like ours where resources are scarce.

Although to date there is no plan for bilateral (multilateral) agreements in the short term, it is possible that foreign administrations accelerate the implementation of this mechanism.

In this regard, it should be noted that although domestic legislation does not provide for the bilateral (multilateral) agreements, even if tax authorities have no intention to request such arrangements from other countries that are part of its network of treaties; the TA should in conditions to agree to such a request as part of a DTC. This request may be made by the taxpayer or by the foreign Tax Administration. An analysis of comparative law shows that the APAs procedure offers the possibility for the taxpayer to request such agreements, subject to the acceptation or rejection by the Tax Administration. A similar approach could be adopted in such cases.

v. Technological aspects

In general, the application of transfer pricing rules require intensive use of computer tools to enable them to access market information on the industry, knowledge of the sectors, pricing of goods in transparent stocks markets, potentially comparable transactions or companies, etc.

APAs regime takes into account this reality.

The use of these tools typically has high costs leading the administration to weigh its needs and evaluate the associated costs.

9. CONCLUSIONS

The APAs are intended to complement traditional mechanisms to resolve transfer pricing issues and will be useful tools in the extent that they favor the application of the arm's length principle, are flexible, and if a collaborative atmosphere exists between the taxpayers and the administration. Undoubtedly, APAs are a resource which virtue is to shorten the discrepancies that occur at the fringes of a regime as sinuous as transfer pricing. They also have disadvantages, since it is not easy in all cases to define those criteria. The parties must be extremely careful, because in terms of inter-sectorial fairness, this works to the extent that it can be applied to a significant number of taxpayers on equal terms.

While it is known that these mechanisms are complex to implement, they are enriching experiences for the tax administration and are not limited to a specific case but have a positive impact on the practice of transfer pricing in general. The acquired knowledge and experience can be positively duplicated to monitor and control other taxpayers.

TOPIC 3

EXCHANGE OF INFORMATION AND MUTUAL ADMINISTRATIVE ASSISTANCE BETWEEN TAX ADMINISTRATIONS

Lecture

Topic 3

EXCHANGE OF IFORMATION AND MUTUAL ADMINISTRATIVE ASSISTANCE BETWEEN TAX ADMINISTRATIONS

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Content: *1.Role of AFIP in information exchange. - 1.1. Vision. - 1.2. Background. - 1.3. Current organization and recent improvements. - 1.4. Successful review of Argentina by PRG. - 1.5. Participation in international organizations. - 2. Expansion of the exchange partners' network. - 3. Problems and challenges of information exchange management - 3.1. Technical support to the operational areas in international taxation issues to encourage a greater use of the information exchange tool. - 3.2. Integrated computerized system for information exchange management, follow-up and evaluation. - 3.3. Use of automatic information exchange. - 3.4. Strategies for speeding up information exchange management. - 3.5. Problems regarding effective information exchange. - 4. Conclusions.*

SUMMARY

In this presentation we will be discussing tax information exchange carried out by this Federal Administration since February 2010, when significant organizational improvements and specific working guidelines were set with respect to information exchange, which, among other factors, constitute an important qualitative and quantitative leap in said management.

The impressive development in the information exchange agreements and conventions network since 2009 was a key element in the success of information exchange management wherein very relevant partners were introduced. The current network includes 50 countries considering the Agreements to Avoid Double Taxation, Specific Information Exchange Agreements and the OECD-European Union Multilateral Convention on Fiscal Affairs.

The successful combined review (regulation and practice) by the Peer Review Group highlights the fact that Argentina presents itself to the world as a jurisdiction with high transparency and effective information exchange.

Likewise, through AFIP, Argentina participates in several international organizations, thus evidencing the important commitment assumed. In this context it takes part in meetings, working groups and other activities dealing with information exchange and related matters.

The working experience throughout these years has made it evident that there are problems and challenges to be faced, such as:

- Taking advantage of the automatic modality or in-block information exchange, assuming the pertinent commitments.
- Implementation of strategies for speeding up management and facilitating contact with exchange partners.
- Importance of counting on a computerized system for information exchange management, follow-up and evaluation that may ensure effectiveness, efficiency and security.
- Identification of jurisdictions that are not prepared for receiving a certain amount of information requests or with whom there may be an unbalance in flows (greater requests made than those received).

Of the abovementioned issues, the last one is of fundamental importance if one wants to achieve an effective information exchange. Thus, it is absolutely necessary not to disregard such situation and consider the implementation of different types of compensation mechanisms vis-a-vis a possible unbalance.

The topics to be discussed in this presentation are those dealing with the current operational aspects of tax information exchange management at AFIP, to conclude with the problems and challenges that have been detected and the solutions implemented.

1. ROLE OF AFIP IN INFORMATION EXCHANGE

1.1. Vision

The Federal Administration shares the vision that international information exchange is a fundamental tool for the intelligent control of global taxpayers. The valuable information obtained through this tool, in addition to allowing for testing evasion and international tax planning practices in specific cases, as well as in the automatic or block modality helps to promote crosschecks and detect omissions resulting from undeclared income, properties and activities abroad.

Within the framework of said vision and under the “Single Agency” concept, since 2010 the integrated management of international information exchange is centralized in the International Information Management Department, which is dependent on the International Examination Directorate that in turn is part of the Deputy General Directorate of Examination. As of this time, there has been a significant progress toward a very strengthened organization that is in charge of all taxes, whether internal or customs duties and which renders possible an effective increase in the perception of taxpayers and customs operators risk, through coordinated control and at times joint actions; although recognizing their respective operational and functional specialties.

With respect to the joint use of international tax and customs information, the following specific benefits are generated:

- Identification of more precise and realistic risk profiles that are integrated with the tax and customs information, which results in a more selective and intelligent control, thereby facilitating foreign trade and ensuring the logistic chain.
- Use in planning examination strategies in regular operations, covering not only fraud or evasion situations, but also labor exploitation.
- The efficient use of human, technical and administrative resources, avoiding unnecessary duplicities and thereby affording the taxpayer a faster and better administrative management.

1.2. Background

Until 2010, tax information exchange was carried out with other technical and operational tasks related to international taxation (opinions, reports, case selection, etc.) within the International Operations Department that was dependent on the Deputy General Directorate of Examination.

The international stimulus in the area of transparency and information exchange, along with the vision of AFIP’s current management of taking advantage of the information Exchange tool to control global taxpayers, led to a strategic reconsideration of the structure, organization and working methodology on this subject matter.

1.3. Current organization and recent improvements

Argentina, through AFIP, exchanges information in accordance with the information exchange clauses that are included in the Agreements to Avoid Double Taxation as well the Information Exchange Agreements that have been entered into.

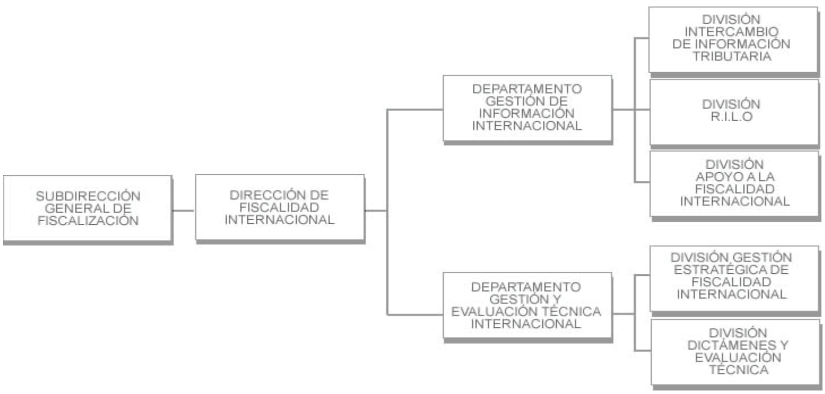
With respect to the Agreements to Avoid Double Taxation entered into by Argentina, although the competent authority is the Ministry of Economy and Public Finance, by virtue of Resolution N° 336/2003 of said Ministry, the processing of information exchanges and the regulation of procedures dealing with information exchange within the framework of said Agreements with the Tax Administrations of other countries has been delegated to AFIP.

On the other hand, AFIP has the power to enter into information exchange agreements with other Tax Administrations, in which case it takes over the capacity of competent authority.

Through Provision N° 258/10 (AFIP) the Federal Administrator has afforded the following areas the capacity of competent authority:

- Deputy General Directorate of Examination.
- International Taxation Directorate.
- International Information Management Department.
- Tax Information Exchange Division

Shown below is the structure of the International Taxation Directorate, created in February 2010 and from which there arises a specific area for information exchange, thereby resulting in the improvement of processes and control on this subject.



Tax information exchange management is centralized at the Tax Information Exchange Division which is dependent on said Department within the International Taxation Directorate.

In those cases where the information requested is not available in the centralized data bases of the Federal Administration, their compilation takes place through the operational areas (Metropolitan and Inland

Regional Tax Directorates, Directorate of Examination of National Large Taxpayers) that may correspond according to the tax jurisdiction of the taxpayer with respect to which information is being requested; there being a total of 27 throughout the country. In turn, these areas are the ones that make the requests for information abroad.

The aforementioned information exchange management includes all the exchange modalities (at request, spontaneous, automatic, etc.) with respect to all countries and taxes involved in the legal instruments signed.

In this respect, it is worth noting that in 2010 single internal regulations of obligatory application in tax information exchange were developed. The guidelines and procedure for processing and managing information requests made and received, including spontaneous reports were set through General Instruction N° 894 (DI PyNF). Subsequently, changes were made to the regulation, based on the experience, whereby a 60-day deadline was set in order for the operational areas to obtain the information and likewise guidelines were determined for the translation of the information and documents received.

1.4. Successful review of Argentina by PRG

The Global Forum on Transparency and Information Exchange, adopting the OECD guidelines, has developed a mechanism for the review of countries, which is intended to control and verify the effective application of information exchange and transparency standards. The mechanism is known as "Peer Review".

Argentina, through AFIP, is a member of said Global Forum[1] and in turn is a member of the more reduced group of countries that are part of the Peer Review Group. Said review consists of monitoring the effective implementation of transparency and information exchange standards for tax purposes.

At the last meeting of the Global Forum on Transparency and Information Exchange held in 2012 in Cape Town, South Africa, final approval of Argentina's evaluation by the member countries was received.

It is worth noting that to said date, 103 reviews (including supplementary ones) were carried out which included reviews by 66 countries only of phase 1 (legal aspects) and 22 countries in a combined manner of phases 1 and 2 (legal aspects and actual information exchange practice).

1 *Currently consisting of 118 jurisdictions.*

Given Argentina's experience in information exchange, the country was subjected to a combined evaluation, thereby becoming the first in Latin America to be subjected to this type of review and the second in the Americas, together with the United States.

As a result of the evaluation it was concluded that Argentina presents and satisfactorily complies with all the parameters analyzed, it being verified that the net worth, accounting and financial information is available and that AFIP may access it and likewise that it may be facilitated through the different information exchange agreements signed with other countries.

Argentina is among the 32% of the countries that have sufficient and reliable information regarding ownership of corporations, trusts and properties, among 51% of the countries analyzed that have obligatory accounting and among the 60% of the countries whose Tax Administration has sufficient power to obtain information.

By way of conclusion, it may be said that Argentina appears as a jurisdiction with high tax transparency, because of the existing regulations as well as effective practice of information exchange, with a prominent situation at the regional as well as world contexts.

1.5. Participation in international organizations

AFIP participates actively in Working Group Nº 10 of the OECD's Tax Policies area, which is currently involved in promoting the inclusion of countries in the Multilateral Convention on Mutual Administrative Assistance, monitoring of the process of the Global Forum on Transparency and Information Exchange, the development of a Common Reporting Standard to unify data to be exchanged under the automatic modality, among others. All these guidelines and international standards are then analyzed and adapted to be applied in the organization's internal policies.

Standing out within the Tax Policies area is Working Group Nº 10 of which Argentina is a member which examines the way in which the governments may cooperate to minimize tax evasion.

The purpose is to provide strategic policies; legal, administrative and technical support to develop and improve the legal, practical and administrative frameworks and thus facilitate information exchange and mutual administrative assistance, with a view to improving tax compliance and at the same time maintain an adequate balance with respect to the protection of taxpayer rights.

In addition, the strengthening of international cooperation in information exchange between tax administrations and those responsible for generating tax policies is being sought, as well as increasing the countries' ability to face tax evasion and counteract harmful tax planning.

On the other hand, this Administration actively participated in Working Groups N° 1 and N° 6 with certain relationships with information exchange.

Also worth noting is the active participation of AFIP representatives in MERCOSUR meetings. In this regard, Argentina proposed analyzing the possibility of entering into a Multilateral Cooperation Agreement between the member countries and participants. One could also include automatic exchange and a unified FRS at the MERCOSUR level.

2. EXPANSION OF THE EXCHANGE PARTNERS' NETWORK

Argentina has information exchange clauses in 15 Double Taxation Agreements (DTA) in force (Germany, Australia, Belgium, Bolivia, Brazil, Canada, Denmark, Finland, France, Italy, Norway, Netherlands, United Kingdom, Russian Federation, Sweden). It should also be mentioned that a new DTA was recently signed with Spain.

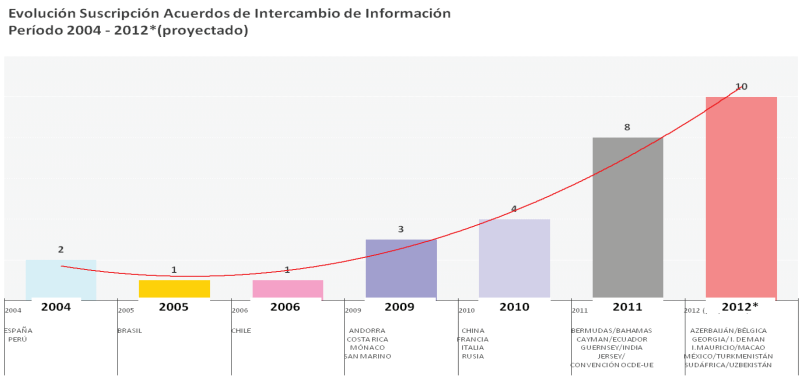
Likewise, the Federal Administration has signed numerous Specific Information Exchange Agreements (SIEA) with strategically selected countries, the latest ones being Azerbaijan, Andorra, Bahamas, Bermuda, China, Costa Rica, Ecuador, Guernsey, India, Italy, Cayman Islands, Isle of Man, Jersey, Monaco, San Marino and Uruguay. It is worth mentioning that there were already SIEAs with Brazil, Spain, Chile and Peru.

A significant achievement is the enforcement since 2013 of the Multilateral Convention on Mutual Assistance in Fiscal Matters of the OECD[2] countries and the European Union. Adhesion to this multilateral mechanism allows for including the United States, Mexico, Colombia, Ireland, Indonesia, Poland, Portugal and Turkey, among others.

All these instruments constitute a contacts network that is extended to 50 countries throughout the world and which has been expanded over 60% in the past three years.

The following graph shows the exponential leap in the number of partners for information exchange that has occurred since 2009 and the subsequent increases.

2 *Formed by 31 countries.*



When making a request, a careful review is made of the fiscal periods or taxable events about which consultations may be made to the exchange counterparts or partners. In some cases, it may be possible, as allowed by certain Agreements to make requests, as of the time they enter into force (even though the fiscal periods or taxable events may have taken place previously), regarding issues that may be provided in the Criminal Tax Law.

3. PROBLEMS AND CHALLENGES OF INFORMATION EXCHANGE MANAGEMENT

In spite of progress achieved in information exchange management, the working experience in recent years has raised the following problems and challenges:

3.2. Technical support to the operational areas in international taxation issues to encourage a greater use of the information exchange tool

There is an evident need to support the operational areas with respect to international taxation, as well as to establish standard criteria that may be applied by these areas throughout the country. The complexity ad specificity of certain issues (transfer pricing and treaty shopping, among others) evidences the need to provide technical support to said areas.

On the other hand, one must also encourage the maximum use of information exchange agreements and conventions.

In this context, the Support to International Taxation Division was also created in 2010, for the purpose of establishing standard criteria and assisting the operational areas in this regard, endeavoring mainly to promote the use of information exchange based on the network of agreements and conventions in force.

Likewise, from this Division crosschecks were promoted which resulted in detecting inconsistencies that gave way to examination actions that, in many cases, used information exchange, based on the network of agreements and conventions.

Said Division has a key role in supporting the operational areas in structuring the request for information from abroad, as well as in the preliminary analysis of the responses obtained from the exchange partners.

It is also in charge of using the information received through the automatic exchange modality, including the crosscheck against data available in the Administration's data bases and follow-up of the cases.

To conclude, it may be said that the joint work of said Division with the Tax Information Exchange Division plays a key role in achieving the objectives determined with respect to the effective use of international information exchange agreements and instruments.

3.3. Integrated computerized system for information exchange management, follow-up and evaluation

On the other hand, there is the need to implement a system that may facilitate the management of exchanges between areas involved in AFIP, while at the same time allowing for a greater and better follow-up and evaluation of results.

Currently, the control, updating and follow-up of information exchange management is carried out through a data base on a platform, wherein one enters and organizes in a structured, reliable, homogeneous, independently organized manner and with the least possible redundancy, the following items: date of entry, CUIT, surname and name or designation/corporate name, activity, reason for the exchange, date of the event, status of the exchange, among others.

It is a local data base, physically located at a working station with restricted access. Its main characteristics are its simplicity, generality, ease of use by the end users and the information inquiries are specified in a simple manner. The interface is friendly, accessible on real time, easy to understand and operate, without it being detrimental to its security and reliability.

The system currently being used is based on the entry of a series of data, by completing a series of fields developed for the purpose of providing necessary and complete information to the request.

According to the proposed guidelines, the fields are divided into obligatory and optional, according to the level of importance of the data to be entered therein.

Each of the requests is individualized (single code) and assigned a consecutive number according to the fields: Country, Year of Request and Type of Exchange (upon request, automatic or spontaneous). It is assigned automatically, after filling out the fields mentioned in the previous paragraph.

Worth noting is the preparation of statistics for different purposes, among them, for th control of terms, monitoring of compliance by the operational entities, managerial reports to high level authorities, use of Agreements and Conventions to Avoid Double Taxation, evolution of requests, etc.:

- General
- Pending
- By country
- By subject consulted
- Detailed by subject
- By the country's operational area
- Inter-annual variation
- Accumulated inter-annual variation

The aforementioned statistics quantify the requests received, the answers given and the pending cases. The data base includes all the information for identifying requests, especially dates, reason for the request, name and/or corporate name, etc. Request and response variation indexes are prepared, with the same closing date each month.

Lastly, it is worth mentioning that a computerized system via Web that may result in a qualitative leap in management information known as system for managing and processing international information exchange is being developed. It is a computerized application intended to automate the internal logistics of international information exchange (between the operational and central areas), and as a result thereof, to provide management data that may serve for decision-making in the pertinent areas.

The creation of this system is based on the need to support the following basic pillars:

- Establish a computerized platform that may generate a direct and fluid communication link with the Operational Areas that request, as well as provide international information.
- On the other hand, generate an automated management and control support that may assist all pertinent areas, by creating alerts to correct possible deviations.
- Likewise, and as a result thereof, to accelerate processing time for the purpose of providing greater international cooperation, by ensuring compliance with the terms resolved in the Agreements and Conventions entered into.
- Finally, and almost as an institutional issue, to advocate for the security of the information. The application design was developed in order that it could run on the safe data bases available in the Organization.

It is clear that the base currently being used, together with the system to be implemented shortly will allow for a permanent monitoring of information exchange management and of the results that it may generate to this Tax Administration. Based thereon, periodic reports showing the progress and achievements are submitted to the top level authorities.

3.4. Use of automatic information exchange

Recently, automatic information exchange has been acquiring importance in the international agendas and thus, AFIP wishes to take advantage of the achievements resulting from this tool.

With respect to automatic information exchange, since 2010, following the creation of the abovementioned specific areas, this modality has been used in a very advantageous manner as indicated below:

- Greater and better use of the information received (Italy, Australia, Denmark, etc.), including a methodology agreed among the areas involved within AFIP which clearly establish the responsibilities and synergies among them.
- Improvement in the data capture mechanisms with respect to nonresident individuals, in the tax returns filed by the taxpayers (profit tax and tax on personal properties) as well as in the information systems (e.g., system for making withholdings to beneficiaries abroad, etc.).
- Use of the information obtained through the new recently implemented electronic examination modality. Based on said online control methodology taxpayers complete a questionnaire with their personal tax code, where it is determined whether or not to continue with an in-depth examination action.

3.5. Strategies for speeding up information exchange management

Without disregarding the obligation of a safe and reliable management of the information exchanged, at present the urgencies and facilitations afforded by the new technologies, call for implementing speedy management mechanisms.

In order to improve information exchange management, hereunder are some of the strategies implemented:

- Participation in events, meetings and working groups that allow for interacting with other competent authorities.
- Telephone and e-mail communication ensuring security and confidentiality measures.
- Agreeing with some countries on specific formats for the requests.
- Visits to verify the status of requests; provide clarification, establish joint working mechanisms, etc.
- Establish memorandum of understanding for the automatic exchange.

3.6. Problems regarding effective information exchange

A relevant issue that is being observed by AFIP deals with the problems that could originate if some jurisdictions are not prepared for managing the number of requests received and even though they may be, there may occur an unbalance in the flows of requests sent and received.

This matter should not slip by, if an effective information exchange is expected. It is clear that the interests between the contracting parties may not be balanced and there may be situations where a country may find itself with a pile of requests it cannot handle.

It is worth pointing out that this Administration is not unaware of the fact that with respect to the recent Agreements signed, problems may arise due to the accumulation of requests that may occur, considering that some Administrations have just recently begun to work with information exchange and that is the reason why the following compensation alternatives may be considered:

- Following the OECD guidelines, a mechanism for the economic compensation of regular and special expenses may be considered.
- Include the possibility of technical support in information exchange and other matters (for example, transfer pricing, agreements to avoid double taxation, etc.).
- Collaborate jointly with the other State in the search for information and in obtaining evidence.

4. CONCLUSIONS

All of the above evidences Argentina's commitment through the current management of the Federal Administration of Public Revenues, with respect to the standards of transparency and effective exchange of information that may be summarized as follows:

- a significant expansion of the information exchange agreements network in recent years, including key partners in information exchange,
- the implementation of a central entity for managing the exchange in all its modalities,
- the establishment of standard and clear working guidelines,
- the continuous training of officials in charge of said management including the participation in meetings and international events,
- the development of a system for the follow-up and control of exchanges, which system has been determined and is in the development stage in order to be implemented this year and which will allow the systematic linking of all areas of the country involved in exchange, thereby achieving a greater level of efficiency in response times.
- the maintenance of data bases that may ensure timely and complete compliance with the requests,
- the preparation and dissemination among all officials of the organization so that they may understand the importance of information exchange, their responsibilities and the use of the powerful data bases for promptly responding to the requests made.
- With respect to management, per se, problems and challenges have been identified, which deal with making greater use and taking advantage of automatic information exchange, with the implementation of strategies that may speed up management, although without disregarding the necessary security and confidentiality of the information exchanged and lastly, considering compensation mechanisms in view of an unbalance that may occur in information exchange with some partners.
- Of the issues mentioned above, the last one is of utmost importance if one wants to achieve an effective information exchange. It evidences the pressing need to not ignore such situation and to consider compensation mechanisms vis-a-vis a possible unbalance.

Case Study

Topic 3.1

INFORMATION EXCHANGE

Donal Godfrey
Deputy Head
Global Forum on Transparency and EOI

Content: *1. What is the international standard? - 2. The transparency triangle. - 3. An introduction to the peer review process. - 4. Phase 2 - Two themes and a paradox. - Annex 1: the terms of reference.- Annex 2: peer review reports adopted and published.*

Thanks to CIAT for the invitation to speak on the work of the Global Forum at this important conference. CIAT is an observer to the Global Forum and a strong supporter of the international standard. We work very closely together on technical assistance activities and I know that some of you will be in Brazil next month at the training seminar that we are running in conjunction with CIAT, the World Bank/IFC and the Federal Revenue of Brazil. You are important partners in our work and we greatly appreciate the strong relationship we have with you.

The international tax scandals which provided the impetus for major changes in international cooperation made 2009 something of a watershed year for tax transparency, with the G20 announcing that the "era of bank secrecy is over" and the restructuring of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) after its meeting in Mexico in September 2009.

Since then many important milestones have been reached:

- Membership of the Global Forum has increased to 119 member jurisdictions plus the European Union and 12 observers, including CIAT.
- All Global Forum member jurisdictions have committed to implementing the internationally agreed standard on transparency and exchange of information.
- Around 2000 new EOI (exchange of information) relationships (bilateral and multilateral) have been created or brought up to the international standard.

- Many member jurisdictions have adopted domestic legislation to improve transparency and permit effective exchange of information
- The Global Forum has met and exceeded the ambitious peer review targets set for it after its restructuring in 2009. A total of 100 peer reviews have been completed and around 20 more are underway.

In short the restructuring of the Global Forum and establishment of the peer review process has produced real change. The ongoing relevance of Global Forum's work to policy makers is clear from the -continuing attention they give to it and calls to all countries to implement the international standard. Evidence for the increasing practical impact of the Global Forum's work is growing but it is also clear from recent press reports that we're not finished yet! And I am sure that the latest round of scandals will lend further impetus to our work. Perhaps 2013 will be another watershed year! Certainly, there has been a major change in our focus from analysing members' legal frameworks to examining how these works in practice.

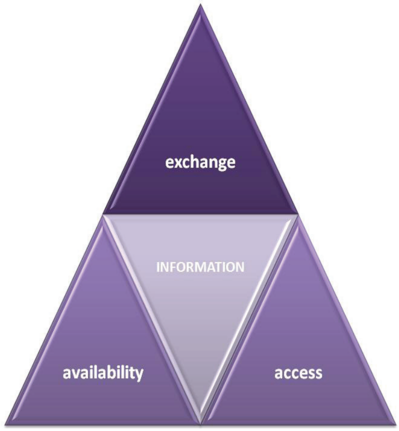
I will start this note with a short introduction to the international standard and the peer review process. I will go on to comment briefly on the outcome of the Phase 1 reviews with a particular focus on CIAT members. I will then up-date you on what we are seeing in the course of some of our Phase 2 reviews. Some of the early results are interesting and suggest that, while a lot of progress has been made in improving transparency domestically and putting EOI agreements in place at the international level, there are sometimes domestic weaknesses within member jurisdictions' administrations which may limit their effectiveness in practice.

1. WHAT IS THE INTERNATIONAL STANDARD?

All of the activities of the Global Forum are carried out with the aim of ensuring the effective global implementation of the international standard of transparency and exchange of information for tax purposes ("the international standard"). At the outset, therefore, I think it's no harm to remind you what I mean by the international standard.

This standard is based mainly on the OECD Model Tax Convention and its Commentary as updated in 2004 and the 2002 Model Tax Information Exchange Agreement and its Commentary. It is helpful to conceive of the standard as a triangle. At the centre of the triangle is information. Information is crucial to the proper administration of tax systems everywhere. At each of the angles are the three pillars on which the standards are based – access, availability and exchange of information.

2. THE TRANSPARENCY TRIANGLE



In other words, the international standard requires that information must be available, competent authorities must have access to the information, and there must be a legal basis for exchange on request.

If any of these elements are missing, information exchange will not be effective and jurisdictions will not be able to enforce their own laws effectively.

The international standard is further elaborated in the Terms of Reference adopted by the Global Forum in February 2010 which is used to determine the level of compliance with the standard. The terms of reference subdivide the three pillars of access; availability and exchange of information into 10 essential elements (see Annex 1).

The standard is also contained in the UN Model Tax Convention and the G20 has called on all countries to implement it. Further, a number of international organisations have incorporated it into their policies.

At a glance

- The Global Forum's standard of transparency and exchange of information for tax purposes is now universally accepted
- The G20 has called on all countries to implement the Global Forum's standard
- The World Bank and EBRD have incorporated the Global Forum's standard into their investment policies

3. AN INTRODUCTION TO THE PEER REVIEW PROCESS

The Global Forum is charged with promoting the effective implementation of the international standard through in depth monitoring and peer review. It undertakes about 40 reviews a year.

It developed the peer review mechanism immediately after its restructuring in Mexico in September 2009. During this period its Peer Review Group (PRG) developed detailed Terms of Reference, a methodology for undertaking the reviews, assessment criteria and a schedule of reviews. These were adopted by the Global Forum in February 2010.

Apart from the PRG and the Global Forum the key players in the peer review process are the staff of the Global Forum Secretariat, the assessors, provided by the member countries and who together with the Secretariat undertake the reviews and the officials in the jurisdictions under review. Each peer review report is drafted by a team consisting of at least one member of the Secretariat and two assessors.

The peer review process comprises two phases. Phase 1 reviews assess the quality of a jurisdiction's legal and regulatory framework for the effective exchange of information, while Phase 2 reviews look at the application of the international standard in practice.

The methodology also provides for Combined – Phase 1 and Phase 2 – reviews mostly of jurisdictions with a long track record of exchange of information (Annex 2 contains a list of the peer reviews already adopted by the Global Forum).

At a glance

To date the Global Forum has completed:
70 Phase 1 reviews
26 Combined reviews
4 stand alone Phase 2 reviews

During Phase 1 of the peer review process, which assesses jurisdictions' legal and regulatory framework, a determination is made as to whether each of the 10 essential elements is "in place", "in place but needing improvement" or "not in place".[1]

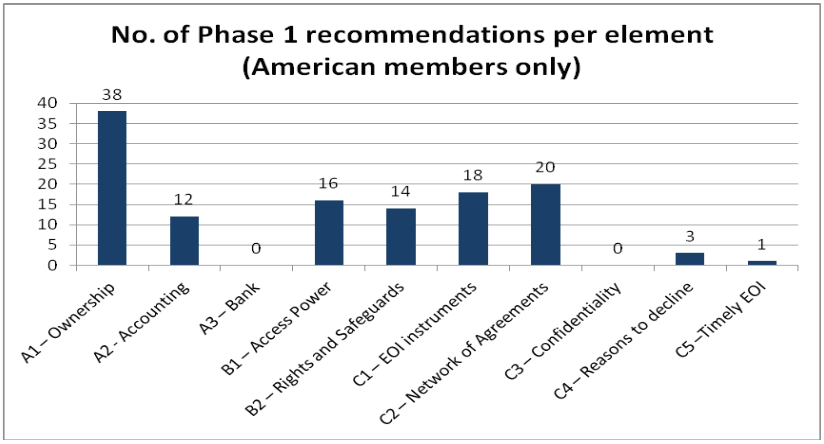
1. *The element on the timeliness of the information exchange is assessed only in a Phase 2 review.*

Determinations are accompanied by recommendations for improvement where necessary. Where a review reveals that some of the essential elements critical to achieving effective exchange of information are not in place, the jurisdiction cannot proceed to the Phase 2 review until it has acted on recommendations made in the Phase 1 report.

At a glance

Of the total number of 862 determinations in initial Phase 1 and Combined reports:
618 elements were found to be "in place";
171 elements were "in place, but needing improvement"; and
73 elements were "not in place".
Following their Phase 1 reviews, 21 jurisdictions could not initially move on to a Phase 2 review. In addition, 3 reviewed jurisdictions could only progress to Phase 2 subject to meeting certain conditions.

For the purpose of Phase 2 of the peer review process, which assesses the implementation of the standards in practice, a four tier rating system for each of the elements applies, ranging from "compliant", to "largely compliant", "partly compliant" and "non compliant". Phase 2 reviews will also lead to an overall rating for each jurisdiction taking into account its legal framework and implementation of the standards in practice.



So come on: does it work?

The Global Forum is charged with encouraging countries to implement the standards and recommendations are only a means to that end. To support and encourage jurisdictions to implement the recommendations all jurisdictions, whether or not they progress to the Phase 2 review, are expected to report within 6 to 12 months following the adoption of their report on how they have addressed any deficiencies identified in their peer reviews. The follow-up reports provided by reviewed jurisdictions make clear that many of them have already made the changes recommended or are in the process of addressing the recommendations made in their initial reports.

At a glance

- 68 jurisdictions have provided follow up reports describing actions they have taken to implement recommendations
- 38 jurisdictions have improved their powers to access information under their domestic laws, of which 17 jurisdictions have obtained or improved access to bank information for tax purposes
- 53 jurisdictions have improved their legislation to ensure the availability of accounting and ownership information, of which 17 jurisdictions have introduced measures to abolish, immobilise or otherwise identify the owners of bearer shares

Notable changes that have been introduced to improve transparency in CIAT member countries include:

- Measures to abolish or identify the owners of bearer shares in Guatemala and Uruguay.
- Measures to improve access to bank information for tax purposes in Costa Rica and Uruguay.
- Measures to eliminate domestic tax interest requirements in Costa Rica and Panama.
- Measures to improve availability of accounting information in Bermuda, Cost Rica and Uruguay.

Jurisdictions that have implemented changes that are likely to result in an upgrade of a determination of an essential element to “the element is in place” can request a supplementary report. The supplementary report process was adopted by the Global Forum in May 2011 to ensure that where significant progress is made in implementing recommendations it can be properly assessed and publicly reflected in a published document. The supplementary report process looks at all the changes made by a jurisdiction and progress is acknowledged by revising determinations and recommendations where applicable.

At a glance

Supplementary reports have been requested by 19 jurisdictions, 10 of which initially could not move to Phase 2. Following the Supplementary reports:

10 jurisdictions, including Barbados, Costa Rica and Uruguay, have been able to move to Phase 2;
49 determinations have been upgraded;
79 recommendations have been removed because the jurisdiction had taken steps to address them and comply with the international standard.

The supplementary report process provides a measure of the Global Forum's impact on policy development in member jurisdictions as well as tangible and public evidence that the international standard is being incorporated into jurisdictions' legal frameworks where previously there were gaps. The changes reflected in the supplementary reports have typically been implemented very quickly by the jurisdictions concerned, in some cases within months of the initial Phase 1 assessment, notwithstanding the difficulty that jurisdictions often face in passing legislation in a short space of time. This has enabled jurisdictions such as Barbados, Costa Rica and Uruguay to move quickly to Phase 2 although some other CIAT members have not moved as quickly and are still stuck at Phase 1. In a number of cases jurisdictions have also changed their laws in advance of their Phase 1 review or in the course of their Phase 1 review, e.g. Guatemala (bearer shares).

Let's focus on EOI agreements

Transparency and exchange of information are necessary not only to uncover tax evasion but also to act as a deterrent to evasion in the first place. The increase in the number of exchange of information agreements signed since 2009 is another indicator of how the international standard is being implemented and by reinforcing a compliance culture is has become a significant deterrent to tax evasion. The perception that tax administrations can access financial and other records held abroad more readily than has been the case in the past will lead to greater levels of disclosure and voluntary compliance. Some member jurisdictions report that they have already experienced increased voluntary disclosures by taxpayers with assets in jurisdictions with which exchange of information agreements have been signed.

Most exchange of information agreements are negotiated on a bilateral basis, but negotiating bilateral agreements can be time-consuming. To assist jurisdictions rapidly expand their network of information exchange agreements, the Global Forum Secretariat has facilitated multilateral negotiations leading to the conclusion of bilateral TIEAs. In Latin America, Belize, Costa Rica, Guatemala and Mexico have all participated in the multilateral negotiations process. Many Global Forum member jurisdictions have also signed the multilateral Convention on Mutual Administrative Assistance in Tax Matters, drawn up under the aegis of the OECD and the Council of Europe, which was updated in 2010 to reflect the international standard. Recent Latin American signatories include Costa Rica and Guatemala.

Full acceptance of the principles of exchange of information has also led a number of jurisdictions that were previously hesitant to broaden the scope of their EOI networks by signing TIEAs or entering into EOI agreements with major trading partners to do so.

This has been the case for Barbados which entered into TIEAs with the Nordics, Uruguay which did not have an EOI relationship with important trading partners (Argentina & Brazil) and Panama which has recently entered into TIEAs the United States, Canada and the Nordics. These jurisdictions have worked hard to extend and update their networks of EOI arrangements since committing to the standard in 2009.

At a glance

Around 1100 new bilateral arrangements (DTCs/Protocols/TIEAs) have been signed that allow for the exchange of information in accordance with the international standard.

Multilateral TIEA negotiations have resulted in the signing of more than 100 bilateral TIEAs.

44 jurisdictions, including 42 Global Forum members, have now signed the amended multilateral Convention on Mutual Administrative Assistance in Tax Matters, creating more than 900 EOI relationships to the standard.

13 jurisdictions have reported improvements in EOI procedures or strengthening of EOI Units to improve the timeliness of information exchange.

These results show that the peer review process is leading to greatly improved transparency, upgraded legal frameworks and wider exchange of information networks.

However the real test of whether the Global Forum is achieving its goals is whether transparency and exchange of information has improved in practice. This can only be determined at the end of the Phase 2 reviews.

4. PHASE 2 - TWO THEMES AND A PARADOX

Where the Phase 1 reviews examine a jurisdiction's legal framework for exchange of information, Phase 2 reviews examine how well that framework does in practice. Phase 2 reviews assess the same ten elements as Phase 1 reviews, except they focus on implementation of those elements in practice. Each element will receive a rating, ranging from Compliant, to Largely Compliant, to Partially Compliant to Non Compliant.

Based on this assessment, each jurisdiction will also be assigned an overall rating of its practical implementation of the standard.

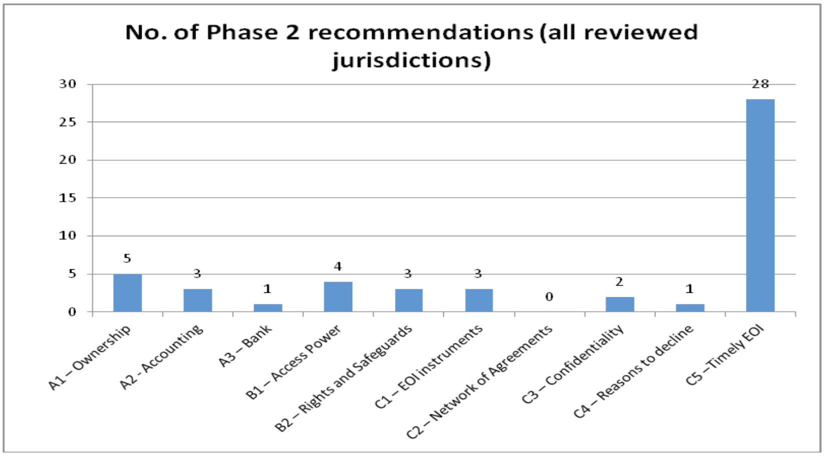
Though some Phase 2 reviews have already been conducted as part of a combined review, stand alone Phase 2 reviews only began in the second half of 2012 and only 4 standalone Phase 2 reviews (Belgium, Cayman Islands, Guernsey and Singapore) have been completed to date. Ratings will be assigned only after a representative subset of Phase 2 reviews has been completed. This is expected to occur by end 2013 when around 50 combined and Phase 2 reviews will have been completed.

Two of the themes that emerge from the Combined and standalone Phase 2 reviews concern the volume of requests and the timeliness of answers. As regards volume, the reviews conducted to date show that while a lot of information is being exchanged, and there has been a significant increase in the volume of requests over the period reviewed (22% on average), this is not as great as might be expected given the increase in the number of EOI arrangements. To an extent this is due to the large number of EOI relationships which have only recently come into force and are only now starting to be used. Also countries that do not have direct taxes tend only to receive requests, rather than making them.

However, there is also a wide variation in the extent to which EOI agreements are being used by different jurisdictions – some rely on the agreements more for their deterrent effect (for example by preventing taxpayers from evading tax in the first place or inciting them to provide information voluntarily) while others also consciously seek to test them in practice right away. Where agreements are used in practice to obtain information, they are effective in countering tax evasion with a number of jurisdictions reporting that they have uncovered cases of significant tax evasion as a result of the new agreements.

It is also evident from the Combined and Phase 2 reviews that the timeliness of responses to exchange of information requests is improving. The international standard requires that requests be responded to within 90 days or, if the request cannot be responded within that time frame, that a status report should be provided within 90 days. In 2009 some jurisdictions would not have met the 90 day threshold in the case of even a single request. Today, it is unlikely that there is any jurisdiction in this position.

However, it is clear from the number or recommendations made in relation to timeliness in the Combined and Phase 2 reviews that there remain issues with respect to the timeliness which need to be addressed in many jurisdictions. There are also issues regarding the quality of requests and responses, which are not confined to jurisdictions new to EOI.



What is becoming clearer, as the Phase 2 reviews proceed, is that the intensity and effectiveness of international cooperation depends on some very practical things. Even though the importance of international transparency and exchange of information is now universally acknowledged, and is evident from the number of new agreements that are in place, paradoxically domestic weaknesses remain which impede the effectiveness of exchange of information. Diplomatic and negotiating skills are required to conclude agreements but implementation is about creating the institutions and infrastructure needed to ensure that they operate effectively. Apart from any legal impediments, weaknesses may exist at a number of levels including:

- Administration - This is focussed on domestic rather than international issues. The level of awareness of EOI and its potential to counteract international tax evasion among senior management and field officers is low. As a result the tax administration has not attached much importance to EOI and makes few outgoing requests.
- Organisational – How EOI work is organised matters. Who does what? How much is done in the EOI Unit and how much in the field? Is there an EOI Unit? Good intentions only get you so far. If you want something done you have to put someone in charge. Here again senior management sets the tone.
- Resources – There is no necessary direct correlation between the number of staff and the volume of requests. Most EOI teams are small. But there has to be some commitment of resources to ensure objectives are met and that staff have adequate training.
- Process issues - Is the jurisdiction able to process, track incoming and outgoing requests and make use of data from other countries? Well run EOI operations have clear policies, tracking systems and performance measures.

These weaknesses may be particularly evident in jurisdictions that are only beginning to exchange information or which are "false beginners" jurisdictions that have had EOI arrangements for some time but which have not made much use of them or not used them very effectively.

Some jurisdictions are now taking action to address these concerns by devoting additional resources to exchange of information, improving coordination between their competent authority/EOI Unit and field officers such as those involved in audits.

Argentina is one example, increasing the number of its outgoing requests by a factor of 10 in the last three years. Other member jurisdictions such as Jamaica have recently established EOI Units. Moreover, improvements in processes are also being made in jurisdictions which have not yet undergone a Combined or Phase 2 review in anticipation of their reviews. This is the case in Panama and Uruguay, for example, which have made considerable efforts to make sure that they get started on the right foot.

In order to further improve the effectiveness of information exchange and hence implementation of the international standard, cooperation and communication between the competent authorities – the officials responsible for exchange of information in practice – is crucial. To this end, the Global Forum has organised meetings of competent authorities to improve this cooperation. In recognition of the fact that many countries joining the Global Forum are developing countries, new to international cooperation in exchange of information, technical assistance is also being provided to create awareness of the international standard, help jurisdictions prepare for their peer reviews and implement the recommendations made. As already indicated, there will be a training seminar next month in Brazil which CIAT is also involved in, and we have run training seminars in Argentina, Barbados and Jamaica as well as providing instructors on courses organised by CIAT or member countries in the region. We also offer more tailored assistance to members on a bilateral basis and some of our CIAT members have benefitted from this assistance. The Global Forum is also developing tools to help jurisdictions implement EOI in practice, including a toolkit, work manual and a tracking system for requests for information.

We're not finished yet

These are significant outcomes of the work the Global Forum has been doing which demonstrate the very practical impact our work is having. As a result of these improvements, exchange of information on request is becoming a much more effective tool as changes in member jurisdictions' transparency and EOI laws, systems and organisations are reflected in an improved service to treaty partners.

The latest round of scandals underscores the importance of the work we are doing.

Some years ago many countries would not be able to do much with the information that has come out but today all of the tools are there and the infrastructure has been built for tax administrations to get the information they need. This will ensure that investigations into these offshore accounts can be taken to their logical end. However, it is also clear that more can be done to make sure that all member jurisdictions adopt an EOI culture throughout their administrations and that they have the tools needed at domestic level to exploit fully the improvements in international transparency that have occurred over the last few years. This is not rocket science – but it's not rocket salad either – and it requires commitment as well as a coordinated effort across member jurisdictions' administrations combining policy, legal and operational measures.

ANNEX 1: THE TERMS OF REFERENCE

The Terms of Reference is available in full in the Key Documents section of the Global Forum website: www.oecd.org/tax/transparency and EOI portal: www.eoi-tax.org. Below is a summary of the key points.

The Terms of Reference

The standard of transparency and exchange of information that have been developed by the OECD are primarily contained in the Article 26 of the OECD Model Tax Convention and the 2002 Model Agreement on Exchange of Information on Tax Matters. The standard strikes a balance between privacy and the need for jurisdictions to enforce their tax laws. They require:

Exchange of information on request where it is “foreseeably relevant” to the administration and enforcement of the domestic laws of the treaty partner.

No restrictions on exchange caused by bank secrecy or domestic tax interest requirements.

Availability of reliable information and powers to obtain it.

Respect for taxpayers’ rights.

Strict confidentiality of information exchanged.

The Terms of Reference developed by the Peer Review Group and agreed by the Global Forum break these standards down into 10 essential elements against which jurisdictions are reviewed.

The 10 essential elements of transparency and exchange of information for tax purposes

A availability of information

A.1. Jurisdictions should ensure that ownership and identity information for all relevant entities and arrangements is available to their competent authorities.

A.2. Jurisdictions should ensure that reliable accounting records are kept for all relevant entities and arrangements.

A.3. Banking information should be available for all account-holders.

B access to information

B.1. Competent authorities should have the power to obtain and provide information that is the subject of a request under an EOI agreement from any person within their territorial jurisdiction who is in possession or control of such information.

B.2. The rights and safeguards that apply to persons in the requested jurisdiction should be compatible with effective exchange of information.

C exchanging information

C.1. EOI mechanisms should provide for effective exchange of information.

C.2. The jurisdictions' network of information exchange mechanisms should cover all relevant partners.

C.3. The jurisdictions' mechanisms for exchange of information should have adequate provisions to ensure the confidentiality of information received.

C.4. The exchange of information mechanisms should respect the rights and safeguards of taxpayers and third parties.

C.5. The jurisdiction should provide information under its network of agreements in a timely manner.

ANNEX 2: PEER REVIEW REPORTS ADOPTED AND PUBLISHED

	Jurisdiction	Type of review	Publication date
1	Andorra	Phase 1	12 September 2011
2	Anguilla	Phase 1	12 September 2011
3	Antigua and Barbuda	Phase 1	12 September 2011
		Supplementary	20 June 2012
4	Argentina	Combined (Phase 1 and Phase 2)	27 October 2012
5	Aruba	Phase 1	14 April 2011
6	Australia	Combined (Phase 1 and Phase 2)	28 January 2011
7	Austria	Phase 1	12 September 2011
8	The Bahamas	Phase 1	14 April 2011
9	Bahrain	Phase 1	12 September 2011
10	Barbados	Phase 1	28 January 2011
		Supplementary	5 April 2012
11	Belgium	Phase 1	14 April 2011
		Supplementary	12 September 2011
		Phase 2	AWAITING ADOPTION BY THE GLOBAL FORUM
12	Belize	Phase 1	AWAITING ADOPTION BY THE GLOBAL FORUM
13	Bermuda	Phase 1	30 September 2010
		Supplementary	5 April 2012
14	Botswana	Phase 1	30 September 2010
15	Brazil	Phase 1	5 April 2012
16	Brunei Darussalam	Phase 1	26 October 2011
17	Canada	Combined (Phase 1 and Phase 2)	14 April 2011
18	The Cayman Islands	Phase 1	30 September 2010
		Supplementary	12 September 2011
		Phase 2	AWAITING ADOPTION BY THE GLOBAL FORUM
19	Chile	Phase 1	5 April 2012
20	China	Combined (Phase 1 and Phase 2)	20 June 2012
21	Cook Islands	Phase 1	20 June 2012
22	Costa Rica	Phase 1	5 April 2012
		Supplementary	AWAITING ADOPTION BY THE GLOBAL FORUM
23	Curacao	Phase 1	12 September 2011
24	Cyprus	Phase 1	5 April 2012
25	Czech Republic	Phase 1	5 April 2012
26	Denmark	Combined (Phase 1 and Phase 2)	28 January 2011
27	Dominica	Phase 1	27 October 2012
28	Estonia	Phase 1	14 April 2011
		Supplementary	20 June 2012
29	Finland	Combined (Phase 1 and Phase 2)	AWAITING ADOPTION BY THE GLOBAL FORUM
30	The Former Yugoslav Republic of Macedonia	Phase 1	26 October 2011

	Jurisdiction	Type of review	Publication date
31	France	Combined (Phase 1 and Phase 2)	1 June 2011
32	Germany	Combined (Phase 1 and Phase 2)	14 April 2011
33	Ghana	Phase 1	14 April 2011
34	Gibraltar	Phase 1	26 October 2011
35	Greece	Combined (Phase 1 and Phase 2)	20 June 2012
36	Grenada	Phase 1	20 June 2012
37	Guatemala	Phase 1	5 April 2012
38	Guernsey	Phase 1	28 January 2011
		Phase 2	AWAITING ADOPTION BY THE GLOBAL FORUM
39	Hong Kong, China	Phase 1	26 October 2011
40	Hungary	Phase 1	1 June 2011
41	Iceland	Combined (Phase 1 and Phase 2)	AWAITING ADOPTION BY THE GLOBAL FORUM
42	India	Phase 1	30 September 2010
43	Indonesia	Phase 1	26 October 2011
44	Ireland	Combined (Phase 1 and Phase 2)	28 January 2011
45	The Isle of Man	Combined (Phase 1 and Phase 2)	1 June 2011
46	Italy	Combined (Phase 1 and Phase 2)	1 June 2011
47	Jamaica	Phase 1	30 September 2010
48	Japan	Combined (Phase 1 and Phase 2)	26 October 2011
49	Jersey	Combined (Phase 1 and Phase 2)	26 October 2011
50	Korea, Republic of	Combined (Phase 1 and Phase 2)	5 April 2012
51	Lebanon	Phase 1	20 June 2012
52	Liberia	Phase 1	20 June 2012
53	Liechtenstein	Phase 1	12 September 2011
		Supplementary	27 October 2012
54	Luxembourg	Phase 1	12 September 2011
55	Macao, China	Phase 1	26 October 2011
56	Malaysia	Phase 1	26 October 2011
57	Malta	Phase 1	5 April 2012
58	Marshall Islands	Phase 1	27 October 2012
59	Mauritius	Combined (Phase 1 and Phase 2)	28 January 2011
		Supplementary	26 October 2011
60	Mexico	Phase 1	5 April 2012
61	Monaco	Phase 1	30 September 2010
		Supplementary	26 October 2011
		Supplementary	27 October 2012
62	Montserrat	Phase 1	20 June 2012
63	The Netherlands	Combined (Phase 1 and Phase 2)	26 October 2011
64	Nauru	Phase 1	AWAITING ADOPTION BY THE GLOBAL FORUM
65	New Zealand	Combined (Phase 1 and Phase 2)	1 June 2011
66	Niue	Phase 1	27 October 2012
67	Norway	Combined (Phase 1 and Phase 2)	28 January 2011
68	Panama	Phase 1	30 September 2010
69	The Philippines	Phase 1	1 June 2011

	Jurisdiction	Type of review	Publication date
70	Poland	Phase 1	AWAITING ADOPTION BY THE GLOBAL FORUM
71	Portugal	Phase 1	AWAITING ADOPTION BY THE GLOBAL FORUM
72	Qatar	Phase 1	30 September 2010
		Supplementary	5 April 2012
73	Russia	Phase 1	27 October 2012
74	Samoa	Phase 1	27 October 2012
75	Saint Kitts and Nevis	Phase 1	12 September 2011
76	Saint Lucia	Phase 1	20 June 2012
77	Saint Vincent and the Grenadines	Phase 1	5 April 2012
78	San Marino	Phase 1	28 January 2011
		Supplementary	26 October 2011
79	The Seychelles	Phase 1	28 January 2011
		Supplementary	20 June 2012
80	Singapore	Phase 1	1 June 2011
		Phase 2	AWAITING ADOPTION BY THE GLOBAL FORUM
81	Sint Maarten	Phase 1	27 October 2012
82	Slovakia	Phase 1	5 April 2012
83	Slovenia	Phase 1	27 October 2012
84	South Africa	Combined (Phase 1 and Phase 2)	27 October 2012
85	Spain	Combined (Phase 1 and Phase 2)	26 October 2011
86	Sweden	Combined (Phase 1 and Phase 2)	AWAITING ADOPTION BY THE GLOBAL FORUM
87	Switzerland	Phase 1	1 June 2011
88	Trinidad and Tobago	Phase 1	28 January 2011
89	Turkey	Combined (Phase 1 and Phase 2)	AWAITING ADOPTION BY THE GLOBAL FORUM
90	The Turks and Caicos Islands	Phase 1	12 September 2011
		Supplementary	26 October 2011
91	United Arab Emirates	Phase 1	20 June 2012
92	The United Kingdom	Combined (Phase 1 and Phase 2)	12 September 2011
		Supplementary	AWAITING ADOPTION BY THE GLOBAL FORUM
93	The United States	Combined (Phase 1 and Phase 2)	1 June 2011
94	Uruguay	Phase 1	26 October 2011
		Supplementary	27 October 2012
95	Vanuatu	Phase 1	26 October 2011
96	The Virgin Islands (British)	Phase 1	12 September 2011
		Supplementary	26 October 2011

Case Study

Topic 3.2

EXAMINATIONS AND COLLECTION ABROAD

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Content: *1. Introduction. - 1.1. The Duties of the Netherlands Tax and Customs Administration (NTCA) in a nutshell. - 1.2. International cooperation. - 2. Regulations. - 2.1. Levying taxes. - 2.2. Collecting taxes. - 3. International cooperation in tax audits s. - 3.1. Exchange of information and tax audits. - 3.2. International tax audits in practice. - 3.3. Simultaneous tax audits: regulations with Belgium and Germany. - 3.4. Multilateral controls (EU). - 3.5. Joint audits (OECD)). - 4. International cooperation in tax collection. - 4.1. Mutual assistance when collecting taxes. - 4.2. International tax collection and general policy principles. - 4.3. Step by step approach. - 4.4. Direct approach.*

1. INTRODUCTION

1.1. The Duties of the Netherlands Tax and Customs Administration (NTCA) in a nutshell

The NTCA performs the following duties.

- Implementing the levying and collecting of state taxes and customs duties
- Monitoring health, safety, environment and economics aspects of imports, exports and transit traffic
- Levying and collecting employee premiums and National Insurance Contributions
- Implementing income-dependent contributions under the 2006 Healthcare Insurance Act
- Performing criminal law enforcement duties in the area of economic structures and financial integrity
- Establishing and paying out income-dependent allowances for such things as childcare and healthcare costs
- Levying and collecting various taxes, charges and other types of recovery for third parties.

28,000 people work at the NTCA in primary and supporting processes.

NTCA promotes compliance by providing appropriate services, exercising adequate supervision and where necessary enforcing compliance by applying the provisions of administrative or criminal law. When acting, the NTCA puts the public and companies centre stage and where justified assumes an attitude of trust. When it comes to compliance, the NTCA attunes the level of enforcement it uses to the attitude and motives of the public and of companies. The NTCA will always choose the most effective instrument at its disposal when seeking compliance from taxpayers. We call this 'compliance risk management'. These efforts are thus directed at influencing behaviour. Besides this, processes are currently being digitalised and standardised as much as possible.

Compliant behaviour manifests itself in terms of one's own taxation in:

- Properly registering the fact that you are liable for tax
- Filing a tax return
- Filing tax returns correctly and fully
- Paying on time.

Compliance manifests itself too in fulfilling the duty to cooperate in imposing taxes on third parties.

1.2. International cooperation

International cooperation in the field of taxation is of increasing importance for the NTCA and for those liable to pay tax. The economy of the Netherlands is closely connected to the outside world and those liable to pay tax are operating more and more on the international stage. This paper describes how the NTCA arranges international cooperation focussing on international examinations and cooperation when collecting taxes. The activities the NTCA has developed when doing so fit within the framework of compliance risk management and are based on national, bilateral and multilateral treaties and regulations. I will first deal with these regulations and the treaty policy of the Netherlands before going on to describe the way in which we have organised international tax examination and tax collection and what our practical experience of this is.

The NTCA is organised in such a way as to place the competent authority for the exchange of information with a centrally empowered authority that has a mandate both to exchange information for direct and indirect tax purposes and to assist with recovery.

2. REGULATIONS[1]

More and more companies are operating internationally, not just multinationals but companies in the Small and Medium Enterprises segment [= SMEs] as well as private individuals. This means the importance of Tax Authorities operating at the international level has become greatly enhanced through for example exchange of information and more intense forms of cooperation. The statutory basis for such cooperation consists of bilateral and multilateral treaties and international and national regulations. The Finance Ministry of the Netherlands published the treaty policy in a memorandum entitled Fiscaal Verdragsbeleid[2] [= Fiscal Policy and Treaties].

2.1. Levying taxes

Bilateral treaties

The exchange of information can be regulated in specifically targeted bilateral Tax Information Exchange Agreements (TIEAs) or in tax treaties containing an Article corresponding to Article 26 of the OECD model treaty as this Article has read since 2005. Both sorts of treaty make it possible to obtain information relevant to the levying of taxes. In principle, the standard Article in tax treaties makes provision for exchange of information on a spontaneous or automatic basis. To cover the latter eventuality, more detailed agreements can be concluded between the tax authorities concerned. The way the Netherlands does this is in the form of cooperative agreements, generally known as MOUs, concluded with colleague tax authorities in which more detailed agreements are made about the set-up of automatic exchange of information, such as e.g. agreements about exchanging categories of information and deadlines. In the Netherlands due to the obligation to notify, such MOUs are published in the Staatscourant [= State Gazette]. This acts as a legal protection measure imposing an obligation on the Tax Authority to inform taxpayers about it prior to providing information at the international level.

Both TIEAs and the more recent tax treaties with an information exchange article correspond with current standards of transparency and information exchange that were established in 2009 by the OECD, G 20 and the Global Forum on Transparency and Exchange

1 *When writing Chapters 2 and 3 of this paper, I made grateful use of ""Intra-Community Tax Audit", Professor Dr. E.C.J.M. van der Hel-van Dijk LL.M., IBFD 2011*

2 *English summary available at http://www.rijksoverheid.nl/onderwerpen/belastingen-internationaal/documenten-en-publicaties/circulaires/2011/02/14/summary-memorandum-dutch-tax-treaty-policy-2011.html*

of Information. One of the standards that was developed, namely, that when receiving any such request for information a requested state cannot refuse to provide information based on their own lack of domestic interest in levying a tax. Moreover the requested state cannot refuse to provide information based on national bank secrecy.

The Netherlands has concluded treaties aimed at avoiding double incidence of tax with more than 90 countries and TIEAs with another 30 countries. The Ministry of Finance publishes a list of treaties along with the current state of affairs surrounding them once a quarter.

Multilateral regulations|

At the level of administrative cooperation, alongside bilateral treaties there are multilateral treaties and regulations. For the Netherlands both the regulations of the EU and the Convention on Mutual Administrative Assistance in Tax Matters are of importance for international audits. This is briefly explained below.

1. Directive (Directive of February 15th 2011 (2011/16/EU)) regarding administrative cooperation at the level of taxation and the repeal of Directive 77/799/EEC.

2. Regulation (Regulation of October 7th 2010, (EU904/910)) regarding administrative cooperation and combating fraud at the level of taxation in relation to added value.

Taken together this Directive and the Regulation constitute the basis for administrative cooperation between EU Member States for both direct and indirect taxes regulating both the exchange of information and, on request, spontaneously and automatically, all aspects of far-reaching cooperation involved in carrying out audits in their various different forms i.e.:

- Presence of officials in the offices of the tax authority in other Member States, also known as ‘assistance in person’
- Simultaneous audits.

Of importance to the Netherlands, besides EU legislation, there is also the January 25th 1988 Convention of the Council of Europe and the OECD, in the form of the Convention on Mutual Administrative Assistance in Tax Matters (hereinafter referred to as: ‘the Convention’). This multilateral treaty has been adapted to the aforementioned new standards. States other than those of the Council of Europe and the OECD can now sign up to this treaty.

The next chapter will discuss the concrete elaboration of these regulations as it applies to foreign audits.

The law of the Netherlands

The aforementioned international regulations have been incorporated into domestic legislation as taken up in the Wet op de Internationale Bijstandsverlening [= International Assistance Act] when levying taxes – EU Regulations work directly. This Act regulates the extent of the exchange of information and the forms of assistance the Netherlands extends and receives.

2.2. Collecting taxes

Bilateral treaties

The Netherlands has concluded bilateral treaties with a variety of countries both within and outside the EU. For example assistance in collection of direct taxes is made possible through a treaty with New Zealand (Verdrag tussen het Koninkrijk der The Nederlanden en Nieuw-Zeeland inzake wederzijdse bijstand bij de invordering van belastingvorderingen) and a treaty with Germany (Verdrag Nederland-Duitsland inzake de wederzijdse administratieve bijstand bij de invordering van belastingschulden en de uitreiking van documenten) based on specific collection assistance agreements with these countries. Besides this, bilateral agreements have been concluded with various countries such as Belgium and Canada to preclude double taxation. Incorporated into these agreements are one or more articles relating to assistance in tax collection.

For the Netherlands assistance in collecting taxes is an important element in its fiscal treaty policy that aims at improving cooperation at the administrative level. Treaty negotiations focus on determining assistance in accordance with Article 27 of the OECD model treaty. Moreover by way of supplement to the OECD model the Netherlands aims at incorporating the following elements.

(i) Submitting applications for tax collection and the limits of suitability

Here we seek to establish a link with the EU Directive on assistance in tax collection. We can think of practical agreements about such things as deadlines, the use of standard forms and digitalisation.

(ii) Guarantees of legal protection

A non-inhabitant/ non-national is likely to be less aware of his options in terms of submitting objections or appeals in the other state and is therefore offered a greater degree of legal protection: payment of a tax debt will only be claimed when this no longer remains open to appeal or a statement by the inspector of taxes is handed over showing that the sum demanded is owed in a material sense. After all, in principle, the point of departure is that the claim will only be pressed if the debt demand has become established as being irrevocable and can be claimed in full i.e. 'finally determined and fully recoverable'. Besides this, in accordance with Article 27 OECD model treaty the principle is that treaty partners will only ever provide assistance for tax collection where existing material tax debts are not in conflict with the tax treaty or some other regulation to which the treaty partners are party. The Netherlands seeks to have a provision included concerning assistance with tax collection based on Article 27 OECD model treaty supplemented by the above two elements.

Multilateral regulations

In addition to bilateral agreements based on Article 27 of the OECD model treaty, multilateral regulation covers international tax collection. Within the EU the new Collection Assistance Directive was established in 2010: Directive of March 16th 2010 (2010/24/EU) concerning the collection of debts resulting from taxation, laws and other enactments. The Convention discussed earlier also applies to providing international support for tax collection. Incidentally when applying the Convention it is important to know what pre-conditions various countries has set.

3. INTERNATIONAL COOPERATION IN TAX AUDITS

3.1. Exchange of information and tax audits

In the light of the regulations referred to above the following forms of mutual assistance in international audits can be combined.

1. Assistance in person/presence of officials abroad.
2. Simultaneous audits.

These forms of international audits are described below before going on to discuss the concrete instruments developed bilaterally and multilaterally to carry out international audits.

To Point 1: Assistance in person/presence of officials abroad

Assistance in person takes place in the context of a request for information. A competent authority requesting information from the Netherlands can apply to be present in the offices of the NTCA or at audits being carried out in the Netherlands. The competent authorities make agreements about this and under certain conditions the Netherlands will allow it. Provision for this possibility is made in EU regulations and in Article 9 of the Convention. In addition international regulations and treaties appear to allow far-reaching powers, namely: an active role in asking questions of persons and tax examinations. The agreement competent authorities reach about this covers powers and conditions and depends in part on regulations and administrative practice prevailing in the receiving country.

To Point 2: Simultaneous Tax Examinations

Article 8 of the WABB Convention defines a simultaneous tax examination when it states that: ‘For the purposes of this Convention, a simultaneous tax examination means an arrangement between two or more Parties to examine simultaneously, each in its own territory, the tax affairs of a person or persons in which they have a common or related interest, with a view to exchanging any relevant information which they so obtain.’

One of the tax authorities takes the initiative to approach one or more colleague authorities to carry out tax examinations. All parties decide themselves as to whether they wish to take part in the simultaneous tax examination. The tax authorities then consult one another about which cases to select and how to set up procedures for the tax examinations they wish to carry out.

NB: Books and records abroad

The forms of presence of officials abroad referred to above take place within the context of a request for information. This should not be confused with a situation in which a company has moved its books and records (partly) abroad so that a tax authority has to conduct audits across borders. In these kinds of situations the Netherlands asks first and foremost that the taxpayer bring his administration to the Netherlands to enable the audit to take place on Dutch soil. Where this proves impossible, we perform audits of financial administration abroad as the only remaining option. Countries cannot just carry out acts of enforcement on one another’s soil just like that. Competent authorities request permission to carry out tax examinations from the competent authority in the country where the accounts are kept. We also ask permission from the company itself.

When doing so we again make it clear to the company that the law of the Netherlands governs the execution of the tax audit as provided for in terms of the administration and duty to cooperate in for example the 1959 State Taxes Act. Similarly we ask other tax authorities to follow a similar approach if the company's financial books and records are kept in the Netherlands.

3.2. International tax audits in practice

Organisation in the Netherlands

In the Netherlands we have set up an Expert Group for International Tax Auditing that is responsible for the coordination of a proper application of the international regulations in international audits. Auditors from tax offices carry out the audits under an experienced auditor as project manager from the Expert Group responsible for coordinating international cooperation.

The Expert Group works for the entire NTCA and is positioned in the SME segment with overall organisational responsibility for the Expert Group falling to a managing director from this segment. The Group, consisting of 11 full and part-time staff, has 5 FTEs carrying out the following jobs:

- management and secretarial support
- work carried out by competent authorities for direct and indirect taxation
- project manager duties
- acting as FISCALIS EU MLC coordinator.

Members of staff at the Expert Group are mandated to exchange information and are authorised to provide auditors involved in individual audits with a mandate.

Frameworks for international tax audits

The following instruments have been developed bilaterally and multilaterally to implement international cooperation when performing audits.

- Bilaterally the Netherlands has agreed regulations with the neighbouring countries of Belgium and Germany to intensify cooperation in simultaneous audits.

- Under the Fiscalis Programme the European Union coordinates the implementation of multilateral controls.
- The OECD's Forum on Tax Administration presented the Joint Audit report in 2010.

What these instruments have in common is their use of the internationally regulated forms of information exchange "presence of officials abroad" and "simultaneous tax audits". The instruments referred to below all offer a framework with varied scope for effective and efficient cooperation.

In general the aims behind implementing these instruments match.

3.3. Simultaneous tax audits: regulations with Belgium and Germany

In the context of international administrative cooperation along the borders with Belgium and Germany the NTCA has concluded special agreements with Belgium (direct taxes and VAT) and Germany (VAT). This forms the basis on which officials operating along the borders can exchange information directly. On both sides of the border officials have been given a mandate from the competent authorities in their own country. Amongst the tasks of these officials is coordination and handling requests for assistance in person or a visit to a tax office or setting up a simultaneous audit in the context of the cooperation agreements in force with Belgium and Germany. Whilst doing so they work closely with the competent authorities and the Expert Group for International Tax Auditing.

3.4. Multilateral controls (EU)

Definition

Multilateral control (MLC) means an arrangement whereby Member States agree to carry out a coordinated financial control of one or more related taxable persons i.e. legal entities and individuals where the control has a common or complementary interest.

Each of the participating Member States will carry out the audits within its own territory.

MLCs may also be carried out simultaneously in each participating Member State, but this is not obligatory. An MLC may relate to indirect taxes, direct taxes or taxes on insurance premiums and customs duties.

The term Multilateral Control is not a statutory or legal term but is used to indicate that the MLC is carried out under the Fiscalis programme and/or more than two countries are involved. MLCs are performed on the basis of legal instruments from the aforementioned Directives for Direct and Indirect Taxes. The Fiscalis programme of the European Commission organises coordination and support for MLCs. The MLC Guide for Tax Auditors and the MLC Management Guide has been developed with this specifically in mind.

Objectives

The main objectives of multilateral controls are as follows.

- To ensure that tax is payable in accordance with EU and National legislation
- To encourage tax officials to consider multilateral controls as part of standard audit activity
- To share knowledge on audit practices with other Participating Countries
- To test the existing multilateral control procedures and improve those procedures where necessary.

The MLC process in broad outline

During the course of an MLC, completed by preference within one year, Participating Member States hold a number of meetings. A Member State takes the initiative in setting up an MLC. As a rule, the background to a proposal to set up an MLC has to do with simple national audits failing to provide the necessary information to assess the correct amount of tax that is owed. Cases emerge amongst national tax authorities especially as a result of compliance risk management approaches.

MLCs in the Netherlands are not just triggered when we receive a request from individual auditors. Members of the Expert Group also scan the market for potential risks. Market monitoring of pleasure yachts and internet services are just two examples of the cases we have been dealing with.

When an MLC is initiated, a start-up meeting is held with the Participating Countries where agreements are made about the strategy, aims and objectives of the joint control.

In this way, Participating Member States gain insight into one another's approach and the statutory options available to Participating Member States. Joint agreements are recorded in an intra-community control plan that then serves as the basis for the control to be performed in the Participating Member States. An additional request can be made for authorisation to allow for the presence of national officials from other Participating Member States. At this stage exchange of information takes place. The concluding stage in an MLC consists of a concluding meeting and a joint report.

Experience of the Netherlands

On average the tax administration of the Netherlands is involved in about 20 new MLCs every year. About 65% of these are developed on the initiative of the Netherlands. The projects that were started in year 2011 cover, amongst others, the following topics:

Internet services, alcoholic beverages, carrousel fraud, real estate, migrant labour and second-hand cars.

17 MLC projects in which the Netherlands took part were concluded in 2011. The European revenue from these projects amounted to more than €583 m, of which €68 m accrued to the Netherlands. Although no Dutch assessments were imposed in 5 projects the Tax and Customs Administration was able to issue valuable information to other states that enabled them to impose assessments. In addition, the European states imposed penalties amounting to a total of more than €18 m.

3.5 Joint audits (OECD)

Definition

The OECD's Forum on Tax Administration developed the instrument of the joint audit in 2010[3]. "A joint audit can be described as two or more countries joining together to form a single audit team to examine an issue(s)/transaction(s) of a company or individual with cross-border business activities perhaps including cross-border transactions involving related affiliated companies organized in the participating countries, where the taxpayer jointly makes presentations and shares information with the countries, and the team includes Competent Authority representatives from each country who are involved to resolve potential differences/stalemates."

"The term 'joint audit' is not a legal term as such. In tax matters the term 'joint audit' has been used in practice to express the idea that two

3 *OECD/Forum on Tax Administration, September 2010, Joint Audit Report http://www.oecd.org/tax/administration/45988932.pdf & Joint Audit Participants' Guide http://www.oecd.org/tax/administration/45988962.pdf*

or more tax administrations work together. If countries wish to carry out a joint audit, it is necessary to determine the legal framework on which they could co-operate. The basis for co-operation can be found in a network of bilateral and multilateral tax treaties in which mutual assistance is incorporated."

For the Netherlands obtaining the consent of the taxpayer concerned is an important element in the statutory underpinning of any such audit.

When to consider a joint audit

The FTA report states that, "A joint" audit should be considered when:

- there is an added value compared to the procedures of exchange of information;
- the countries have a common or complementary interest in the fiscal affairs of one or more related taxpayers, and
- in order to obtain a complete picture of a taxpayer's tax liability in reference to some portion of its operations or to a specific transaction, where a domestic audit is not sufficient."

"The main objectives of joint audits are:

- to reduce taxpayer burden of multiple countries conducting audits of similar interests and/or transactions;
- to improve the case-selection of tax audits by mutual risk identification and analyses;
- to provide as much evidence as possible that the correct and complete income, expense and tax are reported in accordance with national legislation, through efficient and effective administrative cooperation;
- to enhance the awareness of tax officers of the opportunities available in dealing with international tax risks;
- to gain understanding of the differences in legislation and procedures and if necessary to accelerate the Mutual Agreement procedure by early involvement of the Competent Authority, where double taxation is involved;
- to recognise and learn from the different audit methodologies in participating countries;
- to harness the particular strengths and expertise of team members (for example, valuation experts, economists or industry experts) from different administrations for the benefit of the joint audit;
- to identify and improve further areas of collaboration; and
- for all participating countries to reach a joint/mutual agreement on the audit results to avoid double taxation, as applicable."

The FTA Report goes on to state that, “a joint” audit can also contribute to:

- the development of enhanced relationships [= cooperative compliance] between revenue bodies and taxpayers;
- enhancing the compliance of multinational companies;
- providing certainty for taxpayers;
- a reduction in compliance costs for taxpayers through the resolution of tax issues in a timely and cost effective manner;
- more effective management of tax issues in ‘real time’;
- increasing the efficiency and effectiveness of revenue bodies; and
- more effective challenges to those taxpayers who push legal boundaries and who rely on lack of transparency in cross-border transactions.”

Main Steps in the Joint Audit process

The Joint Audit Participants Guide distinguishes a number of steps when setting up and arranging joint audits [= JA] which are comparable to those of the European MLC:

- Preparation process
- Case selection process
- The planning meeting
- Auditing process: joint information requests, examinations and meetings with the taxpayer
- Final stages of the JA: final report and team meeting

The experience of the Netherlands

For the NTCA a joint audit is a relatively new instrument. We have however already had positive experiences with joint approaches as mentioned by the FTA Joint Audit report, in the context of horizontal monitoring or cooperative compliance. In the Netherlands we are carrying out pilot projects for joint audit with colleague tax authorities and have agreed with them to apply the joint audit and work it out in more detail. Such joint audits are carried out in the context of cross-border developments in cooperative compliance relations with multinationals. We expect the pilot to provide us with greater clarity about the following:

- legal aspects such as:
- how to act if not all of the partners have signed up to the Convention
- room for active presence of foreign national officials during controls
- practical aspects such as:

- experience of working with a single audit team e.g. language and travel movements
- reaction and experience of taxpayers

4. INTERNATIONAL COOPERATION IN TAX COLLECTION

4.1. Mutual assistance when collecting taxes

Collecting taxes abroad is about the Netherlands requesting that people in another state assist us and vice versa. The basis for any such request would have to be provided by international regulation or a treaty (see: Chapter 1 of this paper).

We need to distinguish between international regulations for the collection of taxes and for the collection of National Insurance Contributions [= NICs], the latter encompasses collection of specific amounts in the form of allowances that were paid erroneously – a subject beyond the remit of this paper that deals only with the collection of taxes. In the Netherlands income tax and NICs are collected together meaning that where cases occur with differing international regulations assessments have to be split into two with one part dealing with taxation and the other with NICs.

Mutual assistance can take any of the four [sic] following forms.

This relates to notifications from and to another state.

1. Notification (the serving or issuing of documents).
   This relates to requests for notification to another state and requests for notification from another state.
2. Exchange of information. This concerns requests for information by the Netherlands to another state and vice versa. Here too in the context of the exchange of information when collecting taxes “the presence of national officials” abroad is an option.
3. Attachment of property before judgment. This concerns applications for attachment of property before judgment by the Netherlands to another state and vice versa.
4. Taking collection measures. This concerns requests for assistance in collecting taxes by the Netherlands to another state and vice versa.

The policy aim of the NTCA is to intensify international assistance in collecting taxes. To achieve this we have deployed a plan to make the most effective use possible of bilateral and multilateral treaties already in place. Paragraphs 4.3 and 4.4 refer to how these different forms of mutual assistance are deployed.

4.2. International tax collection and general policy principles

- Generally speaking, assistance with collection of taxes in another state is not under discussion unless and until we have exhausted all national means to secure collection of the tax.
- The collector of taxes applies for assistance for the collection of tax assessments that have been established irrevocably, that are recoverable in full and for which a writ of execution for the entire debt has been issued and served. This could be an estimated tax assessment where the suspicion is justified that materially speaking it is due. Where assessments are not undisputed or irrevocably established the collector of taxes can apply for assistance in collecting them if he views measures to secure the debt as necessary. In doing so the collector of taxes does not have to wait till collection procedures have been initiated or concluded. Options that include passport issuance alerts, committal for failure to comply with a judicial order or a notice of liability do not impede an application for assistance in collecting taxes.
- A request for information can be submitted at any stage in the collection process
- An application to notify (issuing or serving documents) can be useful if the collector of taxes needs to be certain that the document subject to notification really has reached the taxpayer. The requested state draws up a statement concerning notification to show whether and if so how the document has been brought to the taxpayer’s attention.
- Notification is next in line to the procedure for the service of documents and the service of a writ of execution abroad.
- To attach property before judgment the collector of taxes must have at his disposal valid title i.e. a writ of execution that has been served upon the taxpayer.
- Mutual assistance when collecting taxes is not just possible for the taxpayer himself but also for any person held liable. By the way, internationally, as far as inheritance laws go, beneficiaries are only liable for the deceased’s debts to the extent of their own share in the estate.
- Unless states have agreed some other minimum amount, there will be no request for assistance from authorities abroad if the amount of tax owing comes to less than €227.

If the amount owing comes to less than €2,269 the collector of taxes will not submit a proposal to attach property before judgment, unless special circumstances justify doing so for a lower amount. Where special circumstances prevail a request for information can be made for a lower amount.

4.3. Step by step approach

Reducing international tax collection arrears can be best done by applying a step-by-step approach. Having first launched a query throughout the Netherlands as to how many and how large amounts receivable are whilst coupling these with addresses abroad of natural persons only, the competent authority proceeds to submit requests for information abroad (Step 1) to establish identity, address and recovery. It would however be more logical if an international regulation were in place to allow the Netherlands to make a simultaneous request for information as well as an application for assistance when collecting the taxes.

Where the requested state knows the person concerned and reports that he does have the means at his disposal with which to pay the debt, the information obtained especially that relating to recovery options will be analysed (Step 2) and a decision made as to whether or not to submit a request for mutual assistance.

4.4 Direct approach

This approach involves communicating directly with the taxpayer and impressing upon him how important it is to still pay his/her taxes due. To do so it would not be necessary per se for a country where taxpayers live to conclude a treaty or that any such treaty would for example be lacking in making provision for tax collection. The approach is attuned to the competent authorities in the taxpayers' country of residence. If it proves to be the case that the taxpayer does not wish to cooperate and a treaty is already in place, the process leading to mutual assistance in collecting the tax will be initiated as a last resort.

The 'direct approach' has its advantages both for the Netherlands and for the requested states abroad. For the Netherlands for example it means that communication is more direct and dossiers can be dealt with quicker. By the way, dossier processing is aimed at solving all of the tax problems at one fell swoop and where possible to sever the bonds with the Netherlands to avoid having to address the taxpayer all over again at some future date. We have found that this approach increases compliance. For the requested state this approach means they are not overwhelmed by a large number of requests for mutual assistance.

Case Study

Topic 3.2

EXAMINATIONS AND COLLECTION ABROAD

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Content: *- Background. - Results. - Considerations*

BACKGROUND

The Nordic Approach is an action by seven Nordic tax authorities in Denmark, Faroe Islands, Greenland, Finland, Iceland, Norway and Sweden. The Nordic authorities have a long tradition of working together in different matters.

1989 Multilateral convention

One of the areas of co-operation for the Nordic countries is to combat international tax evasion. In 1989 the countries developed and adopted a multilateral agreement for the exchange of information (Nordic Mutual Assistance Convention on Mutual Administrative Assistance in Tax Matters). This convention covers all taxes as well as social contributions.

2006 Beginning of joint negotiations of TIEAs

With the aim of following up the OECD's work combating international tax evasion the Nordic authorities decided in June 2006 to begin negotiations with offshore jurisdictions.

In order to strengthen the Nordic negotiating position and to keep costs for this negotiation work down, the countries coordinated their negotiation work under the direction of the Nordic Council of Ministers.

A steering group was set up consisting of representatives from all of the Nordic authorities in order to coordinate the negotiation efforts.

The day-to-day work is managed by a project manager and chief negotiator. The project will last until September 2013, and there are talks about a possible prolongation.

2012 Nordic Working Group on international tax evasion

In 2012 the Nordic Director-Generals set up a Nordic Working Group on Tax Evasion to take yet a step further in sharing experiences and in that way more effectively identify tax evasion and tax avoidance. By working together with foreign tax authorities, e.g. new Tax Information Exchange Agreement (TIEA)-partners Competent Authority Agreements(CAA) could be agreed upon and make things run smoother.

The mandate for the group includes;

- ongoing sharing experiences and monitoring International Tax Evasion
- ongoing monitoring of the renegotiating of TIEA and Exchange of information agreements of international standard
- follow-up the TIEAs and promote the use of the TIEAs and double taxation agreements (DTA)
- spread the knowledge about the TIEAs
- joint Nordic Models, e.g. CAA and templates, dialogue and cooperation with foreign countries
- arrange seminars on “best practice” and share experience inviting cooperation partners from other authorities and TIEA-countries
- work for a common Nordic position in international arenas
- set up a database for TIEAs that all co-workers in the Nordic authorities can use

Internally seminars have also been organized for investigators from the Nordic countries. About 60 investigators from the Nordic countries meet during two days to share best practice and experience through case presentations and break out sessions. This has been a concept for success and very valuable and very appreciated by the participants.

The group also works as a platform for joint responses to TIEA partners when an interpretation is needed regarding the text of the TIEA. Seminars have also been held with participants from the Nordic countries where TIEA partners have been invited.

In general the TIEA partners are committed to fulfilling their obligation according to the agreements and assist the requesting country as much as they can.

RESULTS

The Working Group has been successful.

So far have 40 TIEAs been signed. During the period of August 2010 to August 2012, the Nordic tax authorities have in total submitted more than 300 requests for information to jurisdictions worldwide that have either concluded TIEAs or renegotiated the exchange of the information article in existing DTAs. In 2012 the investigation of transactions resulted in 9,3 million US dollars in increased taxes.

In Sweden and Norway there have been information activities to encourage voluntary disclosures. It is vital to have updated information on the web site and to arrange meetings with advisers and tax consultants.

Statistics that is monitored shown an increasing net inflow of capital from certain jurisdictions. These jurisdictions have in common that they have recently concluded the exchange of information arrangements with the Nordic countries. In Sweden the data is processed from the data from the cross border payments. The net capital inflow for 2011 was approximately 1, 2 billion Euros more than the year before.

CONSIDERATIONS

Another important internal issue is to have an organisation that supports all necessary steps. What is needed is

- Internal ability to identify potential off shore non compliance cases.
- Internal ability to investigate these cases.
- Internal ambition to actually investigate these cases.
- Relevant treaties in place.
- Internal ambition to really use the treaties.
- Practical “user climate” established with the other country.
- Internal organisation that supports all the necessary steps.

Case Study

Topic 3.2

EXAMINATIONS AND COLLECTION ABROAD

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Content: *1. Introduction. 2. Examinations abroad. 3. Collections abroad.*

1. INTRODUCTION

Exchange of information (EOI) is a very important tool for tax administrations. It not only provides for information on specific taxpayers to be exchanged, but is part of the legal framework that provides for other mutual administrative assistance arrangements.

Canada currently has two types of instruments that allow for exchange of tax information with other jurisdictions:

- Tax Information Exchange Agreements (TIEAs)
- Tax Treaties

A third instrument will be in place once the Multilateral Convention on Mutual Legal Assistance in Tax Matters[1] (the Multilateral Convention) is ratified by Canada. A Bill is currently before the Canadian Parliament which would, inter alia, ratify the required change to the Canadian Income Tax Act (The *Act*). We expect the required change will be passed this year.

The Multilateral Convention provides for Assistance in Collection and Service of Documents, in addition to exchange of information.

In the absence of treaties or TIEAs, Mutual Legal Assistance Treaties provide for the possibility of EOI for criminal matters. Treaties and TIEAs are more efficient for tax administrations and allow exchange

1 *The Convention was opened up to all countries for signature in 2011. The text of the Convention is available at: http://www.oecd.org/ctp/exchangeofinformation/Amended_Convention_June2011_EN.pdf*

of information before a determination is made as to whether the case may be criminal. In many cases the information in a foreign jurisdiction is necessary to determine whether there is in fact a potential criminal case.

Canada has a broad treaty and TIEA network (90 treaties, 19 TIEAs concluded, another 11 TIEAs under negotiation)[2], and as a founding member of the Global Forum on Transparency and Exchange of Information, fully supports the international standard for EOI. The international standard is reflected in the update to Article 26 of the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention, approved by the OECD Council in July 2012. The standard requires exchange of information on request, which means information is exchanged based on a specific request from the tax administration that needs the information. The standard supports broad cooperation, not restricted by bank secrecy or any domestic interest requirement.

Two other forms of EOI are: spontaneous exchange of information and automatic exchange. Both are contemplated by the international standard, but not required.

Spontaneous exchange of information is when a tax administration comes across information that it believes may be useful to a treaty partner and sends it spontaneously to the treaty partner. This information may or may not lead to a recovery of taxes, but could do so. Treaty partners receiving spontaneous information need to be aware that the sending treaty partner is not suggesting there is any wrong doing, but rather that the information may be useful.

Automatic exchange is the systematic and periodic transmission of "bulk" taxpayer information by the source country to the residence country concerning various categories of income (e.g. dividends, interest, royalties, salaries, and pensions). This is generally done in electronic format. The information exchanged is normally collected in the source country on a routine basis through reporting requirements imposed on the payer (financial institution, employer, etc.).

More and more pressure is being put on countries to exchange information automatically, and we expect this to continue. The CRA continues to expand the number of countries with which we exchange information automatically and spontaneously under our treaties.

2 *A full list of Canada's tax treaties and TIEAs is available at: http://www.fin.gc.ca/treaties-conventions/treatystatus_-eng.asp*

All administrations face the challenge of using the information automatically exchanged effectively and efficiently, in particular because it is provided in many different formats.

The OECD continues to work on standardizing the format for automatic exchange of information with the goals of improving the quality of the information exchanged and making it possible to use the information more easily and efficiently.

The CRA is an active participant in this work and will continue to work with the OECD and our treaty partners to maximize the benefits of exchange of information and continue the move to more broad use of automatically-exchanged information, which is of better quality and can be more efficiently used by tax administrations.

Exchange of information is also the basis for mutual administrative assistance relating to examinations and collections abroad, which are the subjects of this paper.

2. EXAMINATIONS ABROAD

The Canadian tax system relies heavily on taxpayers to voluntarily report the proper amount of tax owing—this is referred to as a self-assessment tax system. Compliance measures are therefore necessary to ensure that taxpayers understand and respect their obligations, thus maintaining the integrity of Canada's self-assessment tax system.

Compliance functions at the CRA include examinations (compliance audits) of individuals and businesses operating in Canada, which can also include international aspects that impact the administration of our tax legislation.

The administration of tax matters is guided by the provisions contained in the Canadian Income Tax Act. This act outlines our tax rules and also guides the actions of the CRA in matters of tax administration. The following is an overview of the various legislative tools available to CRA officers when conducting examinations and how they operate in conjunction with one another.

2.1. Obtaining Information

In terms of examinations, our starting point is contained in section 231.1 of The *Act*, which provides inspection authority to CRA officials for purposes of its administration or enforcement. A CRA official is entitled to request taxpayer information pursuant to the inspection power found in section 231.1. Any such request for taxpayer information is based on the scope and purpose of the review and CRA officials must consider five key principles when evaluating the need to request information from a taxpayer: legislative authorities, intent, relevance, transparency and impartiality. This is the starting point for seeking information from a taxpayer, whether or not the material is located within or outside of Canada.

As part of the inspection process, CRA officials are permitted to enter any business premises and can also require the owner, manager, or employees to answer all proper questions. The legislative authority for this falls under subsection 231.1(1) of the Income Tax Act. Questions posed to employees must fall within the scope of the examination.

If a taxpayer does not provide the requested information, the CRA official can issue a requirement to provide the information and/or documentation pursuant to section 231.2 of the Income Tax Act. A requirement is a legal document that compels a taxpayer to provide the requested information located in Canada.

If a response is still not received after using these tools, section 231.7 of the Income Tax Act can be used to seek a compliance order with respect to a failure to comply with either a request for information under 231.1 or a requirement under 231.2. This provides a civil remedy to obtain compliance with the CRA's request for information or documents—meaning a judge can order a person to provide the information or documents. The taxpayer must appear before a judge to offer an explanation for non-compliance with a requirement. Further, pursuant to section 238 of the Income Tax Act, a summary conviction for a fine or imprisonment may be sought for failure to comply with any of these provisions.

A foreign-based requirement under section 231.6 of the Income Tax Act applies to information or documents located outside Canada. This tool can be used to require a person resident in Canada or a non-resident person carrying on business in Canada to provide foreign-based information. If a taxpayer does not comply with a foreign-based requirement, they may be prohibited from introducing this information in their defence in later court proceedings. Generally, this means that the CRA can issue a reassessment based on information at hand and reasonable assumptions, and the taxpayer will not be able to present the information in court if the reassessment is appealed.

The provisions of section 231.2 also apply to information or documents required for the purposes of any tax information exchange agreement between Canada and another country (including those covered under a tax treaty). Therefore, compliance orders and summary convictions also apply to the obligations of Canadians to provide information requested through exchange of information provisions. The CRA can use these information gathering tools to compel a taxpayer to provide the requested information, which provides assurances to the foreign tax authority that the CRA has domestic laws that can apply jointly (both for our purposes and the purposes of the foreign tax authority). The benefit to foreign tax administrations is that the information gathering tools available in our *Income Tax Act* can be realized by the foreign jurisdictions when making information exchange requests. This joint application provides for effective exchange of information between Canada and foreign jurisdictions while increasing the opportunity for the foreign tax authority to obtain the requested information.

2.2. Section 247 of the Canadian income tax act – Transfer Pricing

Certain examinations undertaken by CRA officials have international implications. This mostly occurs when services, tangible property and/ or intangible property are traded across international borders between a Canadian taxpayer and related parties (or parties with whom the taxpayer does not deal at arm's length). Pursuant to section 247 of the *Act,* which relates to the transactions or arrangements between a taxpayer and a non-resident person with whom the taxpayer does not deal at arm's length, such international transactions must be established at an arm's length price. Auditors of the CRA examine the terms, conditions and prices of these transactions and, where they differ from those that would have been made between persons dealing at arm's length, audit adjustments can be made.

2.3. Canada's views on international examinations

Multinational enterprises operating in Canada often have books and records relevant to the Canadian operations located in Canada and in other countries. Although the *Income Tax Act* primarily requires books and records be maintained in Canada, the CRA does however recognize the difficult logistics of maintaining books and records when multiple countries are involved. The CRA recognizes that security issues can arise when books and records are transported to different locations. Further, the CRA does not want to place additional burden on multinational enterprises by requiring them to maintain duplicate records in Canada, in addition to those located in their primary jurisdiction, which would place an extra cost on the taxpayer. Given this, our *Income Tax Act* does allow taxpayers to keep books and records outside of Canada under special circumstances.

In accordance with subsection 230(1), taxpayers who wish to keep books and records (which include electronic records) outside Canada must obtain the approval from the Minister of National Revenue. Generally, permission is granted on the condition that the taxpayer signs a written agreement, which states that the books and records will be made available in Canada when the CRA requires them. The taxpayer is required to not only provide the books and records, but they must also allow access to key personnel.

Alternatively, the CRA will accept that the books and records be made available at an offshore location if the taxpayer agrees to reimburse the CRA for costs related to compliance activities carried out in the offshore location.

2.4. Practical considerations

2.4.1. Approval for conducting audits in other countries

Generally speaking, tax officials are not permitted to travel outside of Canada for the purposes of performing taxpayer specific duties without having obtained prior approval from the destination country's Competent Authority. Entering a foreign country for these purposes without Competent Authority permission could offend that country's sovereignty and violate existing tax conventions.

Audits at foreign locations are not conducted without the prior written consent of the taxpayer. The taxpayer must agree to the audit being conducted outside of Canada and they are required to sign an "acknowledgement letter" to confirm that the travel and living costs associated with the audit will be reimbursed to the CRA.

Once the auditor and the taxpayer have confirmed a detailed travel schedule, the CRA auditor must contact the Competent Authority Services Division within the CRA if the destination is a treaty country. The Competent Authority will communicate with the Competent Authority of the destination country to obtain authorization.

2.4.2. Other country's restrictions

Despite the mandate and intentions of the Canadian tax authority, restrictions of other countries do impact our interactions with taxpayers. For example, some countries have a policy of forbidding representatives of foreign tax authorities from performing audits in their jurisdictions, even if the taxpayer agrees in writing to provide access to the CRA in the country where the books and records are located.

2.4.3. Limitations on accessing and/or obtaining information

The CRA has experienced problems with taxpayer compliance where cross-border transactions and transfer pricing are involved. Legislation previously mentioned was enacted as a result of the difficulties encountered when information in the possession and control of non-residents, particularly those residing in countries where no treaty provisions for exchange of information apply, was not voluntarily provided by the Canadian taxpayer and was not obtainable by the Minister.

Foreign non-disclosure laws can have an impact and limit the information received by the CRA. The Income Tax Act does not include a specific reference to foreign non-disclosure laws and including such a clause in the legislation could place a person in a conflict position where that person would have to break the foreign law to comply with Canadian law. Although a foreign jurisdiction may forbid disclosure of certain information in that jurisdiction, this prohibition should not stop the CRA from issuing a requirement under section 231.2 of the Income Tax Act for that information in Canada, nor should it preclude the taxpayer involved from providing such information available in Canada for Canadian income tax purposes. Where the requirement is served on a resident who has to ask an employee of a non-resident affiliate to obtain and disclose the required information, the situation is much more difficult. These situations are examined on a case-by-case basis.

Some auditors have been presented with offshore books and records prepared in a language other than English or French. The Income Tax Act does not legislate taxpayers to use one of Canada's official languages when books and records are being prepared or maintained. However, the Minister does have discretion when deciding to allow the maintenance of books and records offshore. If taxpayers refuse to provide records in English or French (original or translated), then consideration can be given to revoking the Minister's approval.

Delays have been encountered in getting access to electronic records and there have been problems in the adequacy of the electronic records in many instances. Offshore electronic records must be made available to Canada in an electronically readable format.

2.4.4. solicitor-client privilege

In the process of gathering information, situations may arise where the taxpayer claims that the documents being requested are subject to solicitor-client privilege. Solicitor-client privilege can be described as a person's right to refuse to disclose confidential communications between themselves and their legal advisor, made for the purpose of seeking or providing legal advice.

Section 232 of the Income Tax Act allows a person to commence an application before the courts for a determination of a question of privilege. Where the CRA initiates the procedures with respect to a claim of solicitor-client privilege, a compliance application is made pursuant to section 231.7 of the Income Tax Act; the judge presiding at a compliance application has the jurisdiction to make rulings on questions of privilege. If the judge decides the claim in favour of the taxpayer, the CRA cannot compel the taxpayer to produce the material.

During the course of gathering information for an examination or to respond to an exchange of information request, the CRA uses the various information gathering tools previously mentioned to obtain information from a Canadian taxpayer. During this process of requesting information, the taxpayer may claim solicitor-client privilege. In these circumstances, Canada’s Department of Justice would be consulted and a legal opinion as to the validity of the taxpayer claim, as well as the appropriateness of the treaty information request would be sought. If our Department of Justice is of the opinion that the information is not privileged and that the treaty request is acceptable, the CRA would then continue to use the information gathering tools.

During the process, however, the taxpayer is entitled to make an application for judicial review, at which point a judge will decide the validity of the privilege claim. If the judge decides that there is no solicitor-client privilege, the taxpayer will be required to provide the information. If however, the judge favours the taxpayer, the CRA will not obtain the information that is protected under this privilege. This can have implications to a foreign tax authority when requesting information through an exchange provision.

The CRA can also be left in a similar situation. If the CRA requests information through an information exchange agreement with another country, and the foreign entity claims privilege, we often are not able to obtain the information through the exchange provision. The CRA then would be left with our own domestic provisions, which only apply to the Canadian taxpayer and can be contested through the judicial review process. In the end, the CRA may be left without further recourse to obtain the information.

2.5. Canadian experience – simultaneous audits

A simultaneous audit is defined as an arrangement between two or more countries to examine simultaneously, but independently in their own territory, the tax affairs of a particular taxpayer or group of related taxpayers that have carried on activities in those jurisdictions, with the view to exchanging any relevant data either spontaneously or specifically.

Simultaneous audits must involve the Canadian and foreign countries' Competent Authorities. While Canada only has a few formal agreements in place, nothing prevents the conduct of a simultaneous audit with any treaty partner if the foreign Competent Authority agrees.

The main purposes of a simultaneous audit are to determine a taxpayer's correct tax liability and to facilitate an exchange of information.

2.5.1. Benefits of a simultaneous audit

The benefits of a simultaneous audit flow mainly to the tax administrations involved and not the taxpayer. The main benefits of a simultaneous audit are that it promotes the exchange of information and the sharing of knowledge and expertise. Given the complex inter-relations of international taxpayers and the tendency for non-compliance to transcend borders, the opportunity to work cooperatively offers tremendous advantages.

2.5.2. Practical considerations for a simultaneous audit

If the CRA is contemplating a simultaneous audit, we will consider the specific information requests received from the particular foreign jurisdictions. These offer excellent leads and already show the interest by the foreign jurisdiction. We may also consider a simultaneous audit where there appears to be significant related activity in another country. The involvement of the foreign jurisdiction could prove valuable in these circumstances.

All requests for simultaneous audits are sent by and received through our Exchange of Information Section of the Competent Authority Services Division. If CRA auditors are contemplating a simultaneous audit, they will prepare a report for our Exchange of Information Section who will coordinate the transmittal of a Competent Authority letter to Canada's treaty partner. CRA's Exchange of Information Section is responsible for working out the administrative arrangements between the two sides if the request is accepted. If the request is rejected, the other tax administration will be advised of the reasons.

For incoming requests for simultaneous audits, the Exchange of Information Section sends the request to the appropriate CRA tax services office (TSO) for consideration.

The TSO will decide if a case is to be accepted, rejected or countered with an alternate proposal. The final decision rests with the TSO and must be communicated to the Exchange of Information Section. If accepted, the Exchange of Information Section will undertake the necessary administrative arrangements to move the process forward. If rejected, the TSO will provide a full explanation of the reasons so the Exchange of Information Section can communicate this to our treaty partner.

2.5.3. Practical example – The Netherlands

The CRA has recently concluded a simultaneous audit with the Netherlands; an experience that has been positive and beneficial for both countries. In this instance, the CRA audited stock option transactions of an individual and determined that the taxpayer did not report the gains in either country. There was, however, some risk in both countries of not being able to sustain the reassessments. As such, both countries reassessed and decided to let a Mutual Agreement Procedure (MAP) provide relief (on the assumption this person makes a MAP application). This multi-million dollar issue may not have been identified or audited in Canada in the absence of this simultaneous audit process and the Netherlands alerting Canada to the issue.

This particular experience was initiated by the Netherlands who had been considering a regular exchange of information request. However, the Netherlands Tax and Customs Administration concluded that a simultaneous audit would be more practical because of the large amount of information being sought. In addition, there was a third country of interest involved, which added an additional layer of complexity. The usual exchange of information process would have been too static to deal with the informational needs involved. Therefore, a simultaneous audit was considered as the best approach.

2.6. Canadian experience – Joint audits

In October 2009, the Organization for Economic Cooperation and Development (OECD) – Forum on Tax Administration (FTA) commenced a project to consider how joint audits between member countries could be organized and conducted to best contribute to ensure international tax compliance. Increased globalization has resulted in a greater number of taxpayers with international issues, requiring revenue administrations to cooperate more closely to ensure compliance with international and domestic tax laws.

International cooperation between tax administrations has traditionally been on exchange of information under tax treaties and assistance by tax officers using various mechanisms such as simultaneous audits.

Joint audits, as opposed to simultaneous audits, involve two or more revenue administrations forming a single team to examine the transactions of a taxpayer with activities in all of the involved jurisdictions. The intent is to reduce audit times and resolve issues sooner, which benefit both the taxpayer and the tax administration. Joint audits could be contemplated where the audit focus has a common or complementary interest for the tax authorities involved. Furthermore, it is perceived that joint audits could be used to further improve compliance and reduce the volume and time required for the mutual agreement process.

The benefits for a compliant taxpayer who wishes to participate in a joint audit include greater tax certainty, less audit-related burden, and timely resolution of issues.

2.6.1. Practical example – United States of America

Joint audits represent a new form of coordinated action between and among tax administrations. In 2011, the CRA took steps to initiate a joint audit and explored potential partnerships with foreign tax administrations. Subsequently, the Internal Revenue Service (IRS) of the United States of America and the CRA performed a thorough risk assessment of their multi-national enterprises and jointly identified a suitable entity for the pilot.

The joint audit is a very structured process. In this situation, major steps have been well defined, including audit personnel and their roles, information requests, key meetings, and exchange of information. The detailed structure of the audit allows for the effective and efficient use of both the time and resources of the tax administrations and the taxpayer.

This joint audit is being conducted in “real time” and is covering transfer pricing issues.

A joint audit gives a more comprehensive perspective of the company’s operations as the range of questioning during the interview process is expanded as a result of the perspectives from different tax authorities.

It also gives the CRA insight into the audit practices of other tax authorities. This pilot will also give the CRA a better understanding of the feasibility of future joint audits as well as the risks associated with this type of workload.

Although the audit is not yet completed, the process to date has been very encouraging and the taxpayer under review has been both cooperative and transparent with both administrations. The outcomes of this pilot joint audit will be monitored with a view to developing procedures and guidelines for future joint audits with our treaty partners. This experience will impact the potential for future work in this area.

3. COLLECTIONS ABROAD

Assistance in Collection of taxes is a relatively new administrative assistance provision in tax treaties. Article 27 (Assistance in the Collection of Taxes) was added to the OECD Model Convention in 2002 (adopted in January 2003), on the understanding that "In some countries, national law, policy or administrative considerations may not allow or justify the type of assistance envisaged under the Article."[3] Canada has 5 treaties with such a provision and they have proven beneficial for both treaty partners.

Whether AIC is included in a treaty is of course dependent on both countries agreeing to do so. Generally, before concluding assistance in collection provision countries consider a number of criteria, including the following:

- The possibility for assistance under their domestic law
- The importance of cross-border investment/migration
- Whether the tax systems are comparable
- Whether benefits will be balanced and reciprocal
- Similarity of legal standards (particularly concerning taxpayers' rights)
- National law, policy or administrative procedures may not justify tax collection assistance in all countries

Assistance in collection provisions are an obligation to provide assistance, and the OECD Model provision is not limited in application to residents of either state or to taxes covered by the convention. Before a request is made the debt must be finally determined. This means that the debt must be enforceable under the laws of the applicant state, and the debtor cannot, under the law of the applicant state, prevent its collection.

3 *OECD Model Tax Convention on Income and on Capital, footnote to Article 27.*

The foreign tax debt is required to be treated like a domestic tax claim, except that priority rules of the requested State do not apply to the foreign revenue claim and any time limits to be considered are solely those of the requesting State.

Exchange of information is key to assistance in collection. It forms the basis allowing the exchange of information necessary to identify and collect the debt, as well as ensuring the confidentiality of the information exchanged. It can be useful in certain cases where the treaty does not contain assistance in collection provision.

3.1. Canada's approach

When Canada includes Assistance in Collection (AIC) article in a treaty, our preference is for a provision that, like exchange of information, is not limited to taxes covered by the Convention in Article 2 (Taxes Covered) or Article 1 (Persons Covered).

Canadian taxes that Canada seeks to include are "taxes of every kind and description collected, by or on behalf of the Contracting States, or of their political subdivisions", which include:

- Taxes imposed under the Income Tax Act,
- Taxes imposed under the Excise Tax Act (our value added tax),
- Taxes imposed under the Excise Act, and
- Income taxes or sales taxes collected by Canada on behalf of a province or territory.

Steps taken to collect tax debts administered by the CRA are not normally influenced by the type of tax debts outstanding or whether there is an AIC provision, but rather by the revenue risk associated with the tax debt and the domestic collection tools available to pursue payment compliance. The AIC provision is an important tool in the collection of Canadian tax debts should domestic collection measures fail to obtain payment from tax debtors who have left Canada or have assets in a country where Canada has concluded an AIC provision in a tax treaty.

Canada has assistance collection provisions with the following treaty partners:

- Germany
- New Zealand (signed, but not in force)
- The Netherlands
- Norway
- United States

Before Canada implements an AIC article, an administrative Memorandum of Understanding (MOU) is required. The MOU sets out administrative procedures to be followed for AIC.

3.2. Domestic collection practices

The CRA employs collections policies and practices based on the philosophy of responsible enforcement.

Responsible enforcement entails early detection of non-compliance, and directing the taxpayer to file outstanding returns or amend returns where information is found to be inaccurate. With respect to the collection of outstanding tax debts the CRA takes reasonable enforcement action, based on the ability to pay principle.

The CRA attempts to have the tax debtor pay the full balance of a tax debt, or make an arrangement for payment in full within a certain period of time. When it is not possible to arrange a payment from a tax debtor, collection action can be taken if it is determined the tax debtor has the capacity to pay a tax debt but refuses to do so or is uncooperative.

Collection actions include, but are not limited to:

- Garnisheeing wages or pensions or accounts receivable,
- Setting off the debt against other government payments,
- Seizing assets,
- Certifying the debt in Federal Court, and
- Placing a lien on a taxpayer's assets.

The CRA can take tax debtors to court to collect the unpaid debt.

Various strategies are in place to enforce payment compliance of a tax debt, depending on the risk model deployed. Amongst other risk factors, the size of the tax debt and complexity of an account determine which collection mode will be used. Additionally, certain revenue lines or characteristics of a tax assessment (i.e. non-resident withholding debts, aggressive tax planning liabilities, etc.) are segregated into specialized collection workloads for resolution.

3.3. Risk analysis

Collection officers at the CRA’s TSOs and within specialized collection workloads, who work on the larger, more complex, or specialized segregated tax accounts, perform initial and regular revenue risk analysis on enforceable or disputed tax debts and tax debtors, to determine if the tax revenue is in danger of loss. If it is determined the tax revenue is in danger of loss, the CRA can initiate legal collection measures that will remove the collection restrictions on the tax account, and require the tax debtor to pay the disputed tax debt, or be subject to immediate legislative collection remedies.

Additionally, TSO collection teams determine if collection assistance under an AIC provision will be required. Currently all requests for foreign collection assistance are initiated at the CRA TSO level, and routed to the Collection Program Administrator for certification of the finally determined revenue claim before being directed to the Competent Authority for collection assistance.

3.4. Identifying offshore tax debtors

Acquiring information on a tax debtor's location is primarily important in determining what domestic and/or AIC remedies may be used in resolving a domestic tax debt.

Individual tax debtors who do not provide their new address to CRA before leaving Canada can often be located using one or more public or private information sources.

Previous Canadian employers, if any, of tax debtors who have left Canada are usually the best source for identifying the individual's location, followed by public search tools, private (e.g. financial institutions), or EOI requests for a specific address location.

Business tax debtor's (including corporations and partnerships) locations are usually identified through public information sources such as federal or provincial business registry systems. The business registry systems will reveal the business ownership, and owners/directors (resident or non-resident). Other important sources of information are public sources (e.g. internet) and private sources (e.g. accounting or law offices).

Certain CRA collection officers involved with Aggressive Tax Planning tax files use their Internet Search Techniques training to identify domestic and offshore corporate structures and related tax debtors.

3.5. Preventative measures

Canada has requirements when certain payments are made or assets are disposed of to help ensure that tax debts are paid by making third parties liable for taxes outstanding. These are explained below.

3.5.1. Clearance certificate obligations and third party liability

Under the Income Tax Act and Excise Tax Act there are certain obligations to obtain clearance certificates before payments are made to ensure that the appropriate taxes have been paid. A legal representative for an estate, business, or property can be held liable for any outstanding taxes if a clearance certificate is not obtained before distributing the assets of an estate, business, or trust. A legal representative includes an executor, administrator, liquidator, trustee, or like person other than a trustee in bankruptcy.

Non-resident vendors who dispose of certain taxable Canadian property have to notify the CRA either before they dispose of the property or within ten days after the disposition. Once the CRA has received either an amount to cover the tax on any gain the vendor may realize upon the disposition of property, or appropriate security for the tax, the CRA will issue a certificate of compliance to the vendor. A copy of the certificate is also sent to the purchaser. If the purchaser does not receive such certificate, they are required to withhold and remit a 25% cost of the property acquired. Any payments or security provided by the vendor and/or purchaser will be credited to the vendor's account. A final settlement of tax will be made when the vendor's income tax return for the year is assessed.

3.5.2. Director liability

Provisions under the *Income Tax Act* and *Excise Tax Act* enable the Minister of National Revenue to assess a corporation's directors in the event that the corporation fails to deduct, withhold, remit or pay amounts for payroll source deductions or Goods and Services Tax.

The extent of the director's liability is equal to the amount that the corporation was required to remit or pay, plus any related interest or penalty.

3.5.3. Non-Arm’s Length transfer liability

Provisions under the Income Tax Act and Excise Tax Act enable the Minister of National Revenue to hold a recipient jointly and severally liable for unpaid taxes or GST when a debtor transfers to any party, who is not at arm's length to the tax debtor, property at less than market value in order to prevent a debtor with substantial income from preventing the CRA's collection effort by transferring assets.

Related persons are those deemed to not be dealing at arm's length, and include legal spouses as well as common-law spouses, children, brothers, sisters, parents or grandparents of the transferor or the transferor's spouse, as well as corporations controlled by any of the above individuals separately or as a group.

3.6. Benefits of assistance in collection

The benefits of pursuing collection of tax debts through an AIC provision are three-fold, and are explained below.

3.6.1. Efficiency

An AIC provision with a treaty partner can ensure collection of tax debts with minimum administrative or legal hurdles, and related costs, associated with pursing the collection of revenue claims (tax debts) by a foreign tax administration.

The primary administrative pre-condition for a revenue claim to be accepted by a treaty partner is certifying that the revenue claim is finally determined. In accordance with the AIC provision, a revenue claim is finally determined if the Applicant State has a right under its internal law to collect the revenue claim and all administrative and judicial rights of the taxpayer to restrain collection in the Applicant State have lapsed or been exhausted.

Ordinary collection costs are minimized and extra-ordinary costs are controlled within the MOU for AIC, as follows:

- The ordinary costs of providing collection assistance shall be borne by the Requested State and the extraordinary costs (such as the costs of experts and other legal fees) shall be borne by the Applicant State. Ordinary costs include internal administration costs (such as staff salaries and overheads) and minor external costs (such as court filing fees). Any ordinary costs that are recovered may be kept by the Requested State.
- Extraordinary costs, which cannot be recovered from the tax debtor, will not be incurred without prior consent of the collection program administrator of the Applicant State. Should the collection program administrator of the Applicant State refuse to assume extraordinary costs, the collection program administrator of the Requested State may refuse to implement the collection measures that caused

these costs. As soon as the collection program administrator of the Requested State anticipates that extraordinary costs may be incurred, the collection program administrator of the Applicant State will be advised and provided with the estimated amount of such costs, if possible, so that the Applicant State may decide whether such costs should be incurred or the request should be withdrawn.

3.6.2. Effectiveness

AIC provisions are effective legal mechanisms to collect taxes from non-resident tax debtors. In most common law countries, the general principle of international tax law was that a country's revenue officials or courts will not assist in the enforcement of the tax claims of another country. However, this principle, also known as the "revenue rule", has gradually been abandoned as the result of the increased mobility of taxpayers and capital and of government's willingness to enter into bilateral and multilateral AIC provisions. As AIC provisions are considered a legal departure or exception from the "revenue rule", they are viewed as the most effective means to enforce a foreign government's tax claims.

3.6.3. Compliance

Assistance in tax collection has an important compliance effect, for example:

- When taxpayers resident in the requested country are aware that their local tax administration can be asked to collect the tax debt to another country, the may be more inclined to pay their outstanding taxes.

- Similarly, taxpayers may also be less inclined to try to keep funds out of reach of the country to which the debt is owed if they are aware of assistance in collection provisions.

Although it would be very difficult to measure, in some cases the compliance effect may outweigh the benefit of tax debts actually recovered with the assistance of another country.

3.7. Benefits of exchange of information for tax collection purposes

Exchange of Information (EOI) enables treaty partners to share information important to the collection of domestic tax debts that cannot otherwise be obtained through public or private information sources.

Information typically sought under EOI provisions is specific information regarding a tax debtor's:

- Income sources
- Assets
- Property ownership or transfers
- Bank information – deposits, transfers, etc.

Such information is used domestically to ascertain the tax debtor's ability to pay a tax debt or locating a collection source for domestic collection or AIC purposes.

3.8. Best practices for EOI and AIC for collections abroad

Communication of tax collection issues or updates between Competent Authorities and/or collection program administrators, are important to the efficient operation of AIC provisions. Regular information exchanges help to determine the level of complexity or risk associated with the collection of a revenue claim and whether more aggressive or alternative forms of collection action may be warranted. For example, revenue claims related to aggressive international tax planning schemes, tax avoidance, or tax evasion may require experienced collection officers to identify income sources or complex corporate structures for collection assistance purposes. Providing information with the request regarding known or last known occupation, income, assets, and bank accounts related to a tax debtor, will aid in expediting the resolution of the claim in the requested State.

AIC is a relatively new provision that, in addition to directly assisting in the collection of tax debts, encourages payment of tax debts by resident and non-resident taxpayers through knowledge that these tools are available to tax administrations.

In addition to simply accepting a debt for collection, Canada has cooperated with treaty partners by allowing interviews or meetings to take place in Canada between debtors residing in Canada and the treaty partner. These meetings are attended voluntarily by debtors and facilitate making special arrangements for payments that Canada may not be authorized to make when collecting another country's debts. We have found this type of cooperation to be both efficient and effective in the resolution of certain previously uncollectable tax debts.

3.9. Conclusion

Efforts are being made worldwide to ensure that domestic legislation or practices in other nations do not impede the free exchange of information. Information exchanges between countries have proven to be a valuable tool in supporting international examination issues and tax collection, and the CRA has achieved good success with this process largely due to the tax conventions and tax information exchange agreements that we currently have in force. In order to improve the process at the CRA, service delivery standards have been adopted and these types of requests are treated as mandatory workload for our auditors.

Effective and efficient information exchange can only take place when all participants recognize and value its importance and benefit. Exchange of information, through tax treaties or tax information exchange agreements and multilateral instruments, allow countries to better administer and enforce tax laws and to prevent international fiscal evasion. Given this, we encourage other tax authorities to consider implementing or expanding existing information gathering processes in their respective tax administrations.

Case Study

Topic 3.3

EFFECTIVE IMPLEMENTATION OF UNITS FOR INFORMATION EXCHANGE AND INTERNATIONAL TAXATION

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Content: *I. Brief historical analysis. II. Urgent solutions III. Information exchange management. IV. Conclusions*

SUMMARY

Since 1990, Costa Rica has subscribed an Agreement of Tax Information Exchange with the Government of the United States of America, and later, at the beginning of the 2000s, made efforts to negotiate agreements to avoid double taxation. Such an agreement has been signed with the Kingdom of Spain. Nevertheless, Costa Rica didn't join the debates on international Taxation and did not react in time to the evolution that took place in recent years, causing the country to be classified on the OECD "black list".

In spite of this, the present situation of Costa Rica in the scope of international taxation has considerably improved. It can be noted that the impulse for this development was partly because of Costa Rica's presence on that "black list" of jurisdictions not complying with international standards for information exchange. The referred classification was shifted to the "gray list" after Costa Rica committed to implement the international standard at the end of 2009.

The country fulfilled most of the conditions required to exchange information, but there were elements that generated risk, such as the authorization by a judge for the waiving of the banking secrecy, without being clear if this was only a formal or also a material requirement.

Other aspects of risk were the objective criterion based on a Control Plan and the requirement of "strong evidences of tax illegality" instead of the simple "foreseeable pertinence" of the requested information.

Costa Rica also responded to transparency standards in general in the tax regime as well as in the treatment of the data related to ownership, identity and accounting requested from taxpayers. Nevertheless, the existence of bearer shares and the period of obligation to maintain data and registries, limited to four years instead of the five years required internationally, were weak points with respect to the standard.

Costa Rica became aware of its situation and took the necessary measures in order to be removed from the “gray list” and to fulfill the international standard for the information exchange. For this effect it modified its internal legislation by the Law No 9068 of September 10, 2012, for the Tax Transparency Standard Compliance, which reforms the Tax Rules and Procedures Code and the Commerce Code, by increasing from four to five years the term in which the accounting books and the information on identity and property must be kept. It also modified the conditions in which the judge authorizes the access to the banking information, limiting his role to a formal revision of the requirements; and it ensured that the exchange can take place with foreseeably pertinent information, eliminating the requirement of strong evidence.

With this reform, a solid legal base for the fulfillment of the OECD standard and for the effective information exchange was established.

In addition, the International Taxation and Tax Technique Directorate were added to the organization chart of the Tax General Directorate, staffed with trained officers and with the necessary resources. A considerable number of information exchange agreements were subscribed with several countries and the necessary regulation has been issued to implement an effective information exchange, according to the requirements of the international standard.

I. BRIEF HISTORICAL ANALYSIS

In Costa Rica, the need to improve Tax international aspects to accompany the country's increasing integration in the world economy had been perceived for several years. This was reflected with the signing of the “Agreement of Tax Information Exchange between the Government of the Republic of Costa Rica and the Government of the United States of America”, approved by Law No 7194 of August 29, 1990, and later with the first efforts of Costa Rica to approach a policy of negotiated agreements to avoid double Taxation (DTC). This was implemented from the beginning of the 2000s, with the negotiation and signing of the DTC with the Kingdom of Spain, approved by Law No 8888 of November 3, 2010, that entered in force on January 1, 2011.

In 2005, Costa Rica voluntarily agreed to a diagnostic on the development of diverse aspects of international taxation through a program supported by the Inter-American Development Bank. The conclusion from this diagnosis was that Costa Rica had to develop its normative and administrative capacities in this matter. Nevertheless, these topics did not actually progress and this had later very important implications for the country, such as being classified in the “black list” of the Organization for the Cooperation and the Economic Development (OECD).

To be classified in this list was a direct consequence of the country’s weakness in international taxation. By its degree of disconnection with the progress in the international taxation debate, Costa Rica did not react in time to the evolution that took place in the last years.

Later, in answer to a request of technical attendance in tax and customs administration by the Costa Rican authorities, a mission of technical consultant's from the Public Finances Department (FAD) office of the International Monetary Fund (IMF) visited San Jose in September 2009.

Specifically, the authorities asked for support to institutionalize the area of international taxation of the General Tax Directorate (DGT), in order to achieve the international standards ‘requirements.

The urgency of the issue was the classification of the country in the OECD’s “black list” of jurisdictions not committed with the international standards of information exchange.

This classification was changed to the “gray list” under the commitment of the country to implement the so-called "international standard” by the end of the year 2009.

Regarding compliance with the standard, Costa Rica earlier implemented in a relatively high degree the requested conditions to exchange information, including the banking condition. However, some elements subsisted that generated compliance risks with the standard, like the requirement that the judge authorizes the waiving of the banking secret, the use of an objective criterion based on a Control Plan or the requirement of “strong evidence of tax illegality” instead of the simple “foreseeable pertinence” of the required information.

In the scope of taxpayer´s rights, Costa Rica does not have a procedure of notification of information request to the taxpayer or interested legitimate party; a file is not opened either upon request, with possibility of appeal, with exception in the matter of banking information as far as the decision of a judge and the resulting possible appeals.

Nevertheless, the rights of the legitimate interested party are respected, in the sense that the administrative procedure to obtain information from third parties is limited according to article 24 of the Political Constitution, the constitutional jurisprudence and the Tax Rules and Procedures Code.

The confidentiality of the information is strictly enforced, in such a way that the requesting State cannot use that information for other purposes than tax, except with the express written consent of the required State. In addition, there is a disciplinary regime for cases in which the information was incorrectly provided and used for other purposes. For this reason Costa Rica is in line within international standards, since it strictly regulates the public officials' duties.

In general, Costa Rica also complies with transparency standards, in its tax regime as well as in the data related to the property, identity and accounting that are requested from taxpayers. Nevertheless, the existence of bearer shares and the term of obligation of maintenance of data and registries, limited to four years instead of the five years required internationally, were weak points with respect to the requirements of the standard.

II. URGENT SOLUTIONS

In this regard, it was essential to take urgent actions to comply with the standard and to remove Costa Rica permanently from the situation in which it was. In parallel, it was also urgent to develop the institutional capacity to face the demand (internal and external) for information exchange and to be prepared to implement the many aspects related to international taxation that are not yet approached by the DGT.

The IMF mission recommended to gradually implement an International Taxation Unit (ITU) at the DGT. The first step was to satisfy the most urgent necessities (negotiation and application of information exchange agreements), to deal with topics such as transfer pricing and, finally, application of double taxation conventions.

The urgent measures to adopt were:

- To modify some aspects of the internal rules that prevented compliance with the standard, particularly the increase from four to five years for the obligation to keep accounting records

and information on property and identity; the conditions in which the judge should authorize access to banking information in agreement with article 106 paragraph e) of the Code of Tax Rules and Procedures and the existence of bearer shares.
- To sign and implement information exchange agreements with at least 12 countries, as fast as possible, because this process did not depend on the progress in the legal changes required.
- To create the ITU in the structure of the DGT and staff it with trained officers and the necessary resources.

Costa Rica could not wait anymore to develop its legal and administrative capacities in the area of the international taxation. The country had the necessity to solve as soon as possible the problem of the international Information Exchange Standard and, to negotiate Information Exchange Agreements (IEA) and to exchange information with other States or jurisdictions. Therefore, it began to take steps to change this situation.

A. The Tax Reform

Regarding compliance with the OECD standard by Costa Rica, as already mentioned, there were some elements in the tax legislation that generated risk:

a) Elements of risk

1. The requirement that a judge authorize the waiving of the banking secret

According to the standard, no restriction to the information exchange should be motivated by the banking secret.

The intervention of a judge, by itself, is not considered a restriction to the information exchange; but the important point is his specific role. Particularly, if in the procedural phase of the information request, he must examine the material established in the law, or if he just has to make a formal revision.

The Costa Rican law had some access restriction to tax information, in particular to the banking information in agreement with the paragraph e) of the article 106 of the Tax Rules and Procedures Code. In these cases judicial intervention was necessary to avoid affecting the privacy right in article 24 of the Political Constitution. And the role of the judge was not very clear in the normative and in practice.

2. The use of an objective criterion based on a Control Plan

The other element of the article 106 of the Tax Rules and Procedures Code that could exceed the international standard was the requirement by which "the taxpayers have been previously chosen, through objective selection criteria for audit, properly published by the Tax Administration and included in the existing Annual Audit Plan to the date of the request".

It is obvious that these criteria can not always be transposed to third countries, where the administrative organization can follow other taxpayers' selection criteria. It is clear that the judge of Costa Rica could refuse to waive the banking secret for information exchange if it appeared that the taxpayer had not objectively been selected nor by direct or indirect relation with a case of fraud, or when the requesting administration followed other selection criteria.

3. The requirement of strong evidence of a tax infringement

The Costa Rican legislation required the existence of "strong evidence of the potential configuration of a tax infringement." In this aspect, Costa Rica faced two problems: first that the expression "strong evidence" is not equivalent to "foreseeably pertinent information" and, second, strong evidence is more demanding than the concept of "foreseeably pertinent" information to which the standard talks about.

This expression of the standard tries to find a balance between indiscriminate requests and those in which strong evidence exists. In summary, indications that the information will be useful to the ongoing investigation should be sufficient, while in Costa Rica strong evidence was a requirement.

4. The existence of bearer shares

The standard requires the availability of reliable information and sufficient power to obtain it. There are two matters on which information is requested so that the application of the various taxes is effective: Information on property and identity of the people who are behind the different instruments or organizations used with economic or commercial goals; and accounting information.

The information is considered of sufficient quality if it allows the access to the data that the considered tax system can use effectively. In structures like investment funds, for example, the principle is always the same: to be able to know who, really, can be the effective beneficiary, in addition to the information on the "legal" or formal owner of the investment or economic organization.

In general, the bearer shares constitute a problem as far as the transparency requirement, because it is evident that it is not possible to know their holder. In Costa Rica, a business company must constitute itself with registered stocks; nevertheless, the same legal text allowed the conversion of the registered stocks into bearer shares.

For these reasons, it was necessary to make a change in the legislation, to stop allowing bearer shares.

5. The term of obligation of maintenance of data and registries, limited to 4 years instead of 5 years internationally required

This period is coincident with the terms regarding money laundering that establish a 5 years term for the maintenance of data. The Code of Tax Rules and Procedures required only 4 years.

b) Law for the Enforcement of the Tax Transparency Standard

By means of Law No 9068 of 10 of September of 2012, Law for the Enforcement of the Tax Standard of Transparency, that reforms the Code of Tax Rules and Procedures and the Code of Commerce, it was decided:

- That the exchange can take place with foreseeably pertinent information, eliminating the requirement of strong evidence.
- That the role of the judge is limited a formal revision of the requirements.
- Elimination of the requirement of objective selection criteria.
- That the maintenance of data and registries has a term no lesser than five years.
- Elimination of the shares to the bearer.

The article 106bis, which is added to the Code of Tax Rules and Procedures, refers to the information held by financial organizations, force these to provide information on their clients and users, including information on transactions, operations and balance, as well as all class of information on movement of current and saving accounts, deposits, credit certificates, individual loans and credits accounts, trusts, investments, stock-exchange investments in joint portfolios, stock market transactions and other operations, active or passive, as long as the information is **foreseeably pertinent** for tax effects, as much internal effects as to fulfill a request of information according to an international treaty that considers the exchange of tax-related information .

It is specifically stated that any information that is required to fulfill a request of information according to an international treaty that include the exchange of tax information will be considered foreseeably pertinent for tax effects.

With this reform a strong legal base for the fulfillment of the OECD standard and for the effective information exchange was achieved.

B. The creation of the International Taxation Directorate

In countries that do not have an area of International Taxation, the experts affirm that the development of a Unit in this matter can be gradual to satisfy the different necessities that are arising. So, at first it may be sufficient to negotiate agreements to exchange tax information and implement effective information sharing with other administrations on this basis.

In the medium term, once the regulatory framework completed, other areas become relevant, such as the application of transfer pricing and the negotiation of agreements on the matter. The issues arising from the implementation of agreements to avoid double taxation will be addressed in the long run.

In the specific case of Costa Rica, by the historical background, the International Taxation Directorate simultaneously had to start doing a bit of all these aspects. As mentioned at the beginning of this century, Costa Rica had negotiated an agreement to avoid double taxation with the Kingdom of Spain, which took effect in early 2011. For this reason, the Sub-Directorate of negotiation and application of international agreements has had to address the need for regulations to implement the agreement.

And in the area of transfer pricing, by having a standard (although minimal) that allows tax authorities to make adjustments in this area, the Regional Tax Administration, and especially the Large National Taxpayers Directorate, adjustments have been made in this matter, so the Previous Agreements Directorate also plays an advisory role and assess local authorities and the Large National Taxpayers Directorate. In regards to the negotiation of agreements, the issuance of regulations that authorize the Tax Administration to sign such agreements is in process.

In the information exchange, while the requests generated by the IEA to the U.S. were rare (three to four per year), they were processed directly by the Control Department, without having a person responsible for liaison with U.S. In this regard internal procedures were not designed to address this issue.

Obviously, for the short-term commitments with the OECD, the DGT chose as priority that the International Taxation Department negotiate information exchange agreements focus on developing and also implement effective information exchange.

Another important aspect to take into account in the structure of the Costa Rican Tax Administration was the delimitation of workspaces shared with other functional areas and possibly also with the territorial units. Because of the interrelation between these offices, specialized support and coordination from the Sub-Directorate was needed.

The IMF mission of technical assistance, which arrived in Costa Rica in 2009, provided a report which included some recommendations for the ITU and the main functions that it should develop:

a) Recommendations of the IMF Mission

The ITU has to cover a range of functions, both exclusive and shared, mainly consisting in the study and design of tax policy, and the creation of a structure to manage the information exchange with third countries. Specifically:

- To study and propose the need to enter into agreements for the information exchange, considering aspects such as review, promotion and monitoring of the requirements to comply with the international standard, preparation and approval of the IIA model, and negotiating strategy and timetable.

- International Tax Policy: develop and recommend legislation relating to international taxation, participation, and monitoring of international forums that deal with issues related to the development of guidelines to clarify the impact that application of DTC will have on processes and organization, and interpretation of DTCs.

- Information exchange and specifically in organizing exchange upon request: Registering and following requests, standardization of procedures, defining the stages of the proceedings and those responsible for each stage, communication from liaison office and regional offices and attention to the costs of the procedure.

Functions shared with other areas of the DGT should also be developed, including the following:

With Management or the Collection area: Assist in the refinement of the registry to introduce data from non-residents operating with or without a permanent establishment.

In connection with the representatives of non-resident individuals without permanent establishment, review the requirements needed to avoid unnecessary formalities.

Support the technical area in the elaboration of returns and residence certificates. To improve the system of refunds to individuals not established in the country and information and assistance to non-resident taxpayer.

With the Control area: Raise awareness of the relevance and specificity of the audit in the area of international taxation. Coordinate with this area and with customs and, where appropriate, other relevant agencies, the control of foreign direct investment.

Create and implement a specific control policy for international taxation. Coordinate audit criteria on transfer pricing and application methods by sectors. To manage databases of comparable information and to set up a pilot plan to control large multinationals enterprises. It should also have the task of finding solutions to double taxation by advance pricing agreements (APAs) and mutual agreement procedures, as well as international tax arbitrage. Besides the above, it should coordinate future audits or simultaneous control (with third countries), once it has a network of DTCs.

Human and Material Resources: Regarding this aspect, the IMF mission recommended the ITU must have sufficient staff to operate and create a critical mass of knowledge that allows the tax authorities to expand its activity in this area, both in relation to the control as well as to improve the elements that promote voluntary compliance.

The size of this department should be decided according to external and internal factors of the Tax Administration. There is no an internationally accepted size for these units, because some functions may be performed transversally by other functional departments. For example, it is possible and even common for the Control Department to have expertise in transfer pricing and that all these issues are carried from that department, and it also happens that models and forms, including certificates of residence are drafted by specialists and not require the assistance of the Unit for this purpose.

The team should be sufficiently trained and from different backgrounds, legal and economic profiles, and with professional diversity within the Tax Administration. These officials should have Language skills, and enhance their knowledge in areas of International Tax Law and concepts. Officials whose profile has been previously established as the appropriate should be trained to negotiation techniques, control of multinational groups and introduce the necessary and, among others, also the remuneration to ensure continuity and development of the equipment.

As for the material resources, it would be necessary to provide human teams with sufficient material resources, specific and characteristic of this area of taxation, such as sufficient bibliographical documentation, particularly for the area of negotiation and implementation of IEAs and DTCs. The search for criteria is very important, and comparative law bibliography is needed.

A database is also needed to perform a task technically sound and free from arbitrariness in transfer pricing. It was necessary for the DGT to have data on comparable transactions, since all the control process for transfer pricing relies, as is well known, on the concept of comparability and its application in practice. An easy and convenient access to the Internet is also necessary.

The Costa Rican tax authorities began to make serious efforts to build an ITU and to provide it with all the resources necessary for its operation.

b) Creation of the International Taxation Directorate in the DGT

By Decree No. 35688-H of November 27, 2009, Rules of Organization and Functions of the Directorate General of Taxation (DGT), the International Taxation and Tax Technique Directorate were established.

This department was created with two Sub-Directorates that came to fill the gaps (almost total) that Costa Rica had experienced until recently in this area.

The Previous Transfer Pricing Agreement Sub-Directorate was created. Its main functions are:

- Identify and analyze requirements prior agreements on transfer pricing.

- Develop, promote and monitor proposals prior agreements on transfer pricing.

- Educate the relevance and specification of control in the area of international taxation.

- Collaborate with the Department of Supervision on the implementation of a control policy for international taxation.

- Coordinate with the Department of Supervision of the DGT and the Directorate General of Customs and, where appropriate, with other relevant agencies, oversight of foreign direct investment, with an emphasis on companies that are in Free Zones.

- Manage databases of comparable information.

- Suggest and help in the development of standards affecting non-residents or foreign investors, particularly transfer pricing and APAs.

This Sub-Directorate, in its short existence, has contributed in the drafting of the bill and of an executive order to regulate specifically the issue of transfer pricing. It assists the Control Sub-Directorate of the Directorate General of Large Taxpayers on performing audit activities in which they have to apply transfer pricing adjustments.

In addition, the Sub-Directorate provides training courses in the field of transfer pricing to the Large Taxpayer Auditors and to the Large Companies Territorial Offices.

It also advised the Institutional Procurement in the subscription management database system, which contributes to the pursuit of international comparable.

We are currently working on the design of an information return for transfer pricing, to be implemented from 2014 and a resolution is being drafted to regulate the issue of previous agreements, which will be in force from 2014.

Coordination is organized with the Customs control units and other offices such as the Foreign Trade Promoter (PROCOMER), for the control of foreign direct investment. There are also plans in the short and medium term to help control areas on a pilot project to monitor large multinational companies.

The other is the Sub-Directorate for Negotiation and Implementation of International Tax Treaties, which main functions are:

- Design a national negotiating strategy to sign tax treaties and information exchange agreements and conduct these negotiations.

- Understand and analyze the proposals made by other countries to sign agreements with Costa Rica in international taxation.
- Develop a model of double tax and information exchange agreement.
- Establish the process of negotiation, approval and implementation of agreements to avoid double taxation and for the information exchange agreements.
- Establish a procedure for the information exchange on request.
- Follow the requirements to comply with international standards on double taxation and information exchange.
- Implement both types of agreements in all their aspects.
- Analyze existing regulations and documents issued by the OECD and the UN, as well as comparative legislation of agreements to avoid double taxation.
- Apply the internationally accepted criteria and mechanisms that enable effective combating harmful tax practices.
- Collaborate in the attention to queries raised by taxpayers on international tax issues.

The Sub-Directorate carries out only the information exchange on request.

Costa Rica signed in Brasilia last year, joining the OECD Multilateral Convention on Administrative Assistance in Tax Matters, allowing exchanging tax information with other countries, but not yet in force.

This convention provides for automatic exchange. For this reason, we are implementing the necessary steps to start this type of information exchange.

C. Signing agreements to exchange tax information

The effective information exchange with other administrations can only be achieved by signing legal instruments to this effect. For this reason, a Costa Rican Model Information Exchange was developed with the advice of the IMF according to the principles of the OECD Model.

Over thirty international agreements of information exchange have been negotiated to date. We currently have 10 in force with the following countries:

- Argentina
- Canada
- El Salvador
- US
- France
- Guatemala
- Netherlands
- Honduras
- Mexico
- Nicaragua

Eight more agreements are processed through Congress, with:

- Australia
- Denmark
- Finland
- Greenland
- Iceland
- Faroe Islands
- Norway
- Sweden

And 15 additional agreements are in process, pending signature or translation, with the following countries:

- Germany
- Aruba
- Colombia
- South Korea
- Ecuador
- Guernsey
- India
- Indonesia
- England
- Ireland
- Italy
- Japan
- South Africa
- Uruguay

Negotiations with Central American countries were not let bilaterally, but a Customs and Tax Cooperation agreement was approved by the Legislature through Act No. 8880 of November 1, 2010.
A CDI with Spain was already mentioned, and there are DTCs pending with Germany and Switzerland.

III. INFORMATION EXCHANGE MANAGEMENT

Costa Rica has also made continuous efforts for implementing in practice the effective information exchange.

A. Registration and tracking requests.

To process individual files generated in this type of request for information exchange, an individual record of files is needed, both those that go to other states and those who come from outside. Registration requests have to be processed by computer to allow individual and immediate monitoring of each file.

Time must be controlled from the beginning to the end of each file, including control of delays not justified by the complexity of the cases. This time control should allow generation of communications both to local officials who are delaying their reports as well as to countries whose answers are expected. This activity must be centralized and not duplicated.

In Costa Rica, the control regarding terms of time and prevention of delay is performed by the sub Directorate for Negotiation and Application of Conventions. This Sub-Directorate currently has a computer program that records information requests received and can keep track of response times.

The program currently does not allow the generation of warning communication for those who fall behind in their reports or for countries whose answers are expected.

Currently they are taking the necessary steps that will allow the TA to have a system that meets even these aspects of international standards.

B. Standardization of procedures.

It is necessary to define standardized response procedures. These procedures are based on a clear definition of how to act in each case, i.e., to clearly define the phases of the procedure and those responsible in each phase. Essentially, this means to divide the tasks between the liaison office (center) and regional offices.

The International Taxation Directorate, specifically the Division of Trading and application of international agreements, is the liaison office with the Regional Tax Administration Offices. It has a Manual of Procedure for dealing with requests for information exchange. This Manual defines the stages of the procedure and those responsible for each of them, and one of its main objectives is to expedite response times.

It is advisable that the liaison office responsible for developing trade directly applicable to those responses that do not require a specific verification or investigation. Whether the information is already available to the tax authorities, as if it can be obtained through a request to others, performing the necessary actions and the preparation of the response must be provided by the liaison office responsible for trade, reserving more complex cases that required a verification process to research the work of local auditors.

In Costa Rica, the Sub-Directorate performs this type of action required and the preparation of the response. For requirements to third parties, if made by the Tax Administration, and taking advantage of these offices have the authority to carry out this work and to apply the appropriate sanction if the taxpayer fails to provide the information; well as processes in place for that. Currently the Sub-Directorate could not do this job because you do not have sufficient resources to perform these procedures.

C. Communication with liaison office and regional offices.

In cases the local control units are involved in the development of the audit responses, there should be a proper channel between the liaison office and the local offices so the coordination can be guaranteed at all times, most especially in cases the development of a response requires the participation of officials from various offices.

Generally this requires that an international cooperation responsible in each local office to receive requests and documents from other countries and to monitor requests and spontaneous information sending to other countries. In Costa Rica, a small country with relatively small tax authorities, it was not considered necessary to set local managers, and thus, everything is centralized in the liaison office (Sub-Directorate itself) to avoid delays in processing requests.

D. Processing and translation.

An essential element in the proper functioning of information sharing systems is the availability of translation services integrated in the liaison offices that allow immediate treatment of the information, to be easily understood by both locals and destination countries. In this respect, if there is no common language, they usually agree bilaterally on the language in which cooperation is developed, a language that is easily understood by both parties.

Exceptionally, there are two areas that should designate a single responsible their specificity in the case of translation, and the need for a long term permanent monitoring and contact with other institutions (Foreign Ministry, National Assembly) and other authorities in order to process agreements.

Costa Rica does not currently have a translation service in the International Taxation Directorate, so these services are provided by the official translators of the Ministry of Foreign Affairs.
Long-term, permanent contacts with other institutions are necessary for the process. In Costa Rica, it is the case with the Foreign Office and the Legislative Assembly.

Currently the translation and coordination procedures for signing agreements are not performed by the Directorate, but are held in the Office of the Minister of Finance.

E. Costs of the procedure.

In the information exchange agreements it is usually agreed that the recurrent costs incurred in the response to a request for information should be borne by the requested State, while extra costs are often covered by the requesting authority. It is the responsibility of the liaison office to ensure that, in appropriate cases; the costs are recognized and met by the counterparty.

F. Specialization of the liaison office.

The specialty in international cooperation schemes also requires specialization of officials who directly or indirectly perform these functions. Specialization is achieved only through a continuous training program in different subjects related to cooperation versa. The authorities of the Costa Rican Ministry of Finance and Tax Administration are constantly investing resources for the ongoing training of staff in this area.

IV. CONCLUSIONS

As expressed by the current Minister of Finance, Edgar Ayales, "Costa Rica pledged in 2009 to comply with international standards and has since been demonstrated that this commitment is real." Indeed, the country has made great efforts to be able to exchange tax information effectively, including the banking information, which previously was conditional.

Among these efforts, the Tax Transparency Standard Enforcement Act, the creation of the International Taxation Directorate within the organization chart of the Directorate General of Taxation and the establishment of a network of information exchange agreements tax are highlighted.

The main legal changes introduced establish the obligation of financial institutions to provide the tax administration with information on their customers and users, including information about transactions, balances and transactions, as well as all types of information on the movement of current and savings accounts, deposits , term certificates, credit accounts and loans, trusts, individual investments, investments in pooled portfolios, stock transactions, and other transactions, whether active or passive.

The obligation of financial institutions to provide this information is programmed in its foreseeably relevant character for tax purposes, both for internal purposes and to comply with a request for information pursuant to an international agreement providing for the exchange of tax information.

It is expressly stated that any information requested to comply with a tax international exchange agreement will be considered foreseeably pertinent for tax effects. This reform establishes a solid legal basis for the implementation of the OECD standard for effective information exchange.

The provisions concerning foreseeably relevant information are not violating the right to privacy enshrined in the Constitution, since they respect the guarantees of confidentiality and other rights of taxpayers, so consistency with the international standards is maintained.

The creation of the International Taxation Directorate has been a major achievement for the Directorate General of Taxation. A well trained staff in transfer pricing, information exchange, interpretation criteria and other issues related to international taxation is already available.

There is still much work ahead in this vast field of international taxation, but very significant steps have been taken to consolidate this international taxation area and for the country to effectively cooperate in combating international tax evasion.

Case Study

Topic 3.3

EFFECTIVE IMPLEMENTATION OF UNITS FOR INFORMATION EXCHANGE AND INTERNATIONAL TAXATION

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Content: *Introduction. I. Pre-conditions for the adoption of information exchange practices II. Factors that influence the decision for information exchange. III. "Key" aspects to achieve effective information exchange.*

INTRODUCTION

This document discusses the aspects that should be considered by the different levels of State policy makers in order to achieve an effective tax information exchange, which is consolidated with the implementation of the respective units.

The first step to promote the information exchange in a State is the "political will", which should be in line with the "political power". The information exchange must be endorsed by the highest authorities of the government and the legislative. This first step is essential for the country to design its paths.

In recent years many factors have influenced the "political will" of several countries in Latin America and the Caribbean, which have begun to promote information exchange practices; such as signing agreements to avoid double taxation with provisions for the tax information exchange, as well as multilateral instruments such as the " Mutual Assistance Multilateral Convention" which protocol since 2012, enabled all countries of the world to be part of it.

However, it is still necessary that many countries which tax systems have adopted the "territoriality criterion", and match the tax rules with their political sovereignty, be aware that this international cooperation practice should not only be considered a cost to improve their reputation and their transparency levels. For example, there are many benefits that could be obtained from its effective application:

- Control of abusive manipulation of transfer pricing;
- Control of consumption tax such as VAT;
- Control "treaty abuse" schemes;
- Detect unjustified patrimonial increases;
- Avoid double taxation;
- Assistance in enforced collection;
- If the instrument allows it, it could be used for other purposes such as the compliance with the Convention against bribery of foreign public officials, report of financial crimes, etc.

The aspects that are directly linked to the design of the tax information exchange unit are the domestic legal framework, the size of the signed and in force instruments network; and their characteristics. The information exchange unit should be considered based on these aspects, which gives us some clues about the amount of applications that are possible to send / address in a given period of time and the procedures that could be carried out, such as audits abroad, joint or concurrent audits, automatic exchanges, among others.

While the exchange of tax information at the international level is not a complex practice, it has a big impact on different processes of the tax administrations. This impacts not only the processes, but also the "organizational culture". As it can be seen, this practice requires great service dedication and good will, especially when we refer to the spontaneous information exchange; where a State voluntarily and without receiving a prior request, provides information on operations or transactions that could present a risk to tax compliance in another State. It also requires the implementation of measures that ensure the highest levels of confidentiality in all instances where the information received from the abroad is used.

An efficient information exchange unit should at least respect the following basic principles, which compliance involves evaluating numerous tax administrations processes and developments:

a. **Confidentiality:** no information is exchanged when it is considered confidential within the country. When we refer to "Confidentiality", we are not considering the "tax secrecy" since this would be covered by the information exchange instrument when received by another State that will implement the necessary measures to comply with it.

b. **Subsidiarity:** a request for information cannot be processed when all available resource to obtain it has not been previously exhausted

c. **Proportionality:** a request for information should not be attended when it involves a disproportionate administrative effort;

d. **Specialty:** the required information must be exclusively used for tax purposes or for purposes established in the respective information exchange instruments.

Among the mentioned developments we could include first of all, aspects related to internal control, ensuring compliance with the confidentiality rules as well as with the specialty principle. Secondly, the need for the tax administration to effectively apply its verification and control powers, as well as to identify public information sources at internal level and in other States, which contributes to the fulfillment of the subsidiarity principle. Moreover, the effective implementation of the proportionality principle is part of the internal evaluation that each competent authority carries out for determining if a request for information proceeds or not. To do this, general knowledge of the rules and relevant administrative practices of the counterpart is needed.

For developing the topics discussed in this introduction, thereafter we will progress on the following aspects:

a. Preconditions for the adoption of information exchange practices;

b. Factors that influence the decision to exchange information;

c. "Key" issues to achieve effective information exchange:

   A domestic legal framework
   B. negotiation of information exchange instruments
   C. administrative aspects

I. PRE-CONDITIONS FOR THE ADOPTION OF INFORMATION EXCHANGE PRACTICES

Unlike many other practices related to access information by the tax administrations, such as that obtained from State entities, from individuals and/or legal entities; either by capturing, collection or directly; the effective implementation of tax information exchange at the international level requires from the beginning, a strong political support.

If we consider countries that have not entered into the field, we could divide them as follows: those countries that even though their laws do not prohibit the tax information exchange between States, due to strategic issues they do not exchange information; those countries which laws guarantee exchange of information but for various reasons (e.g.: promote the attraction of certain types of capital) they do not exchange information or do so with very few States and because of their political, geographical and economic conditions the exchange is not fluent; and those countries that expressly prohibit the exchange of information. In all these cases, there may be tax regimes considered harmful, for example with low levels of income tax, opacity regarding holders of assets (stocks, furniture and real estate), and impossibility to exchange information because of banking secrecy or other secrets, among others.

In this sense, the countries that meet some or several of the above mentioned characteristics may be considered by other States as "tax havens", either in lists or as a result for applying specific criteria laid down in their internal rules.

The table below shows the countries that to November 2012 were considered as "tax havens" in the lists of various Latin American countries:

Country	Country considered as tax heaven
Argentina	Anguila, Antigua Y Barbuda, Antillas Holandesas, Aruba, Isla de Ascensión, Bahamas, Barbados, Belice, Bermudas, Brunei Darussalam, Campione D"Italia, Gibraltar, Dominica, Emiratos Árabes Unidos, Bahréin, Granada, Puerto Rico, Kuwait, Qatar, San Cristóbal y Nevis. Regime applicable to holding companies: Luxemburg, Groenlandia, Guam, Honk Kong, Azores, Channel islands (Guernesey, Jersey, Alderney, Isla De Great Stark, Herm, Little Sark, Brechou, Jethou Lihou), Islas Caimán , Isla Christmas, Isla De Cocos O Keeling, Islas de Cook, Isla de Man, Isla de Norfolk, Turks y Caicos, Islas Pacifico, Islas Salomón, Isla De San Pedro Y Miguelón, Isla Qeshm, Islas Vírgenes Británicas, Islas Vírgenes EEUU, Kiribati, Labuan, Macao, Madeira, Montserrat, Niue, Patau, Pitcairn, Polinesia Francesa, Andorra, Liechtenstein, Mónaco. Regime applicable to companies Uruguay, Reino de Tonga, Jordania, Swazilandia, Albania, Angola, Cabo Verde, Chipre Djibuti, Guyanae, Panamá, Trinidad y Tobago, Liberia Seychelles, Mauricio, República Tunecina, Maldivas, Islas Marshall, Sri Lanka, Vanuatu, Yemen, Malta, Santa Elena, Santa Lucía, San Vicente y Las Granadinas, Samoa Americana, Samoa Occidental, San Marino, Omán, Archipiélago de Svbalbard, Tuvalú, Tristán da Cunha, Trieste, Tokelau, Zona Libre De Ostrava.
Chile	Andorra, Anguila, Antigua y Barbuda, Aruba, Bahamas, Bahréin, Barbados, Belice, Bermudas, Islas Vírgenes Británicas, Islas Caimán, Islas Cook, Chipre, Dominica, Gibraltar, Granada, Guernesey, Isla de Man, Jersey, República de Liberia, Malta, República de Mauricio, Montserrat, Antillas Neerlandesas, Niue, República de Panamá, Samoa, República de San Marino, San Cristóbal y Nevis, Santa Lucía, Seychelles, San Vicente y Granadinas, Liechtenstein, Mónaco, Islas Marshall, Nauru, Vanuatu, Turcas y Caicos, Islas Vírgenes EEUU.

Country	Country considered as tax heaven
Ecuador	Anguila, Antigua y Barbuda, Antillas Holandesas, Archipiélago De Svalbard, Aruba, Isla de Ascensión, Barbados, Belice, Bermudas, Brunei, Darussalam, Campione D'Italia, Gibraltar, Bahamas, Dominica, Emiratos Árabes Unidos, Granada, Kuwait, Qatar, Puerto Rico, San Cristóbal y Nevis, Luxemburgo, Groenlandia, Guam, Hong Kong, Isla de Cocos, Isla de Cook, Isla de Man, Isla de Norfolk, Isla de San Pedro y Miguelón, Isla Qeshm, Islas Azores, Islas Caimán, Islas Christmas, Islas Del Canal (Guernesey, Jersey, Alderney, Isla De Great Stark, Herm, Little Sark, Brechou, Jethou, Lihou), Islas del Pacífico, Salomón, Turcas y Caicos, Islas Vírgenes Británicas, Islas Vírgenes EEUU, Kiribati, Labuan, Macao, Madeira, Montserrat, Myamar, Nigeria, Niue, Palau, Pitcairn, Polinesia Francesa, Liechtenstein, Mónaco, Andorra, Swazilandia, Tonga, Jordania, Guyana, Albania, Angola, Cabo Verde, Chipre, Djibouti, Islas Marshall, Liberia, Maldivas, Malta, Mauricio, Nauru, Panamá, Seychelles, Trinidad Y Tobago, Túnez, Vanuatu, Yemen, Sri Lanka, Samoa Americana, Samoa Occidental, San Vicente y Las Granadinas, Santa Elena, Santa Lucía, San Marino, Oman, Tokelau, Trieste (Italia), Tristan Da Cunha (Saint Helena), Tuvalu y Zona Libre de Ostrava.
El Salvador	Albania, Andorra, Anguila, Bahamas, Baherein, Bermuda, Chipre, Campione D'Italia, Delaware (USA), Dominica, Emiratos Árabes Unidos, Granada, Herm Qeshm, Isla de Man, Isla de Norfolk, Isla de Azores, Isla Caimán, Islas Cook, Isla Maldivas, Isla de Marshall, Isla Mauricion, Islas Marianas, Turks y Caicos, Islas Vírgenes Británicas, Labuan, Liberia, Liechtenstein, Líbano, Macao, Micronesia, Mónaco, Monserrat, Nauru, Nie, Nevada (USA), Paraguay, Samoa, San Cristobal y Nieves, San Vicente y las Granadinas, Santa Elena y Tristan Da Cunha, Santa Lucia, Seycheles, Singapur, Suiza, Uruguay, Vanatu, Wyoming (USA).
Uruguay	Anguila, Aruba, Bahreim, Belice, Islas Caimán, Chipre, Antigua y Barbuda, Islas vírgenes británicas, Islas de Cook, Bahamas, Bermudas, Dominica, Gibraltar, Grenada, Isla de Man, Malta, Montserrat, Antillas holandesas, Panamá, San Marino, Santa Lucía, San Vicente y las Granadinas, Islas Vírgenes de EEUU, Samoa, Niue, Isla Guernesey, República de Vanuatu; Islas Turcas y Caicos, Saint Kitts y Nevis, Seychelles, Isla de Jersey, Mauricio, Naurú.
Venezuela	Anguila, Antigua y Barbuda, Archipiélago de Svalbard, Aruba, Ascención, Belice, Bermudas, Brunel, Campione D´ Italia, Dominica, Bahamas, Emiratos Árabes Unidos, Estado de Bahrain, Estado de Kuwait, Qatar, Samoa Occidental, Puerto Rico, Gibraltar, Luxemburgo, Granada, Greenlandia, Guam, Hong Kong, Islas Caimán, Isla de Christmas, Isla de Norfolk, Isla de San Pedro y Miguelón, Isla del Hombre, Isla Qechoa, Isla Cook, Isla de Cocoa o Kelling Isla del Canal (Isla de Guemeasey, Jersey, Aldemey, Great Sark, Herm, Little Sark, Brechou, Jehou y Lihou), Islas Malvinas, Islas Pacifico, Islas Salomón,Islas Tucas y Caicos, Islas Vírgenes Británicas, Islas Vírgenes de Estados Unidos de América, Kiribati, Labuán, Macao, Malta, Montserrat, Nioe, Palsu, Piscaira, Polinesia Francesa, Andorra, Liechestentein, Mónaco, Swazilandia, Jordania, República Dominicana, Republica de Gabonesa, Líbano, Albania, Angola, Cabo Verde, Chipre, Djiboati, Guyana, Honduras, Islas Marshall, Libe, Mauricio, Naoria, Panamá, Seychelles, Túnez, Vanuatu, Yemen, Uruguay, Sri Lanka, Samoa Americana, San Vicente y las Granadinas, Santa Elena, San Marino, Sultanato de Omán, Tokelau, Tristán de Cunha, Tuvalu, Zona Especial Canaria y Zona libre Ostrava.

Source: Study on the Control of the handling of the transfer pricing in Latin America and the Caribbean. ITC-GIZ-CIAT. December 2012.

This shows us that while a State could be considered as 'tax haven" by another State, it doesn't mean that it will be considered as a "tax haven" by a third State.

In some cases this is due to the "tax haven" concept. The classification of a country as a "tax haven" will depend on the internal rules, on the cooperation level, on the harmful results that a tax regime may represent for another State and on diplomatic relations.

The above mentioned justifies the need to go to the highest decision-making level of a country to start the right way for an "effective tax information exchange".

The "political will" becomes the first step to move forward with future actions that will finally start an information exchange unit based on the best international standards.

However, this topic doesn't finish here, since it is necessary to highlight the problems that could face political level decision-makers wanting to change the country´s oriented model to benefit from foreign capital on the basis of considerable tax reductions and benefits based on opacity. It could affect the necessary "political power" to implement the modifications or adjustments at the tax policy level. This aspect will be more complex to handle in those countries where the main barriers for information exchange are in the "Magna Carta".

Finally, many could consider the need for financial resources to achieve "effective information exchange". This aspect is the less relevant of all, since this practice doesn't demand a significant investment and it is possible to gradually move forward as the State consolidates its instruments network for the information exchange. In many tax administrations, as for example the SAT from Mexico has mentioned in numerous international forums, the benefits obtained are much higher than the costs for maintaining a tax information exchange unit. Later, in the section referring to administrative aspects, we will provide more details on the resources needed in order to have an information exchange unit for tax purposes.

II. FACTORS THAT INFLUENCE THE DECISION FOR INFORMATION EXCHANGE

When evaluating relevant aspects in order to move forward with the tax information exchange, we could first mention the "international initiatives" effect. Since the nineties international organizations and the countries have been increasingly promoting the information exchange for tax purposes. However, the effects have been minimal mainly between developing countries and jurisdictions considered by the international community as "tax havens".

Since 2008; year in which most countries in the world began to present crisis symptoms, such as low production, high unemployment, high debt and negative payment balances, among others; the international community strongly proposed initiatives to increase transparency levels and information exchange at the global level.

This critical situation greatly affected tax collection of various countries, especially those that had to face high public spending as a result of the previous years of economic growth. This showed the need to more aggressively fight harmful international tax planning schemes.

As a result of this, the "Global Forum on tax transparency and information exchange", has successfully implemented the peer review mechanism; and the following G20 declarations:

- Declaration of the Summit on "Financial Markets and the World Economy". Washington, November 15, 2008: on its ninth paragraph among other aspects, refers to the strengthening of transparency and the need to strengthen international cooperation.

- Declaration of the leaders' Summit. Seoul, Nov. 11-12, 2010: in the "multi-year action plan for development" requests to the OECD, IMF, World Bank, United Nations, ATAF and CIAT, among other things, the need to draw up recommendations for improving the efficiency and transparency of the tax administrations.

These multilateral strategies along with regional organizations efforts such as ATAF and CIAT, and unilateral efforts of countries particularly interested in increasing the information exchange levels have considerably influenced the "political will" to promote these practices.

Slowly, many countries and jurisdictions have gone from "black lists" to "grey lists", until to be considered by the international community as transparent.

For example, 42 financial centers listed as uncooperative have made commitments with the international community which led the OECD to eliminate them from its famous list of "tax havens".

If we focus on Latin America, we can notice that many countries have made considerable efforts to increase their information exchange instruments networks and their administrative structures. For example, 47% of Latin American countries have recently created tax information exchange units.

The following table shows the specific agreements for information exchange (it does not include agreements to avoid double taxation) signed by a group of Latin American countries until November 2012[1]:

Country	Number of Agreements	Signatory countries
Argentina	10	Bermudas, Brazil, Chile, China, Ecuador, Spain Guersney, Jersey, Monaco y Peru
Costa Rica	7	Argentina, France, El Salvador, United States, Guatemala, Honduras and Nicaragua
Ecuador	1	Argentina
Jamaica	8	Denmark, United States, Faroes, Finland, Greenland, Iceland, Macao and South Africa.
Mexico	23	Aruba, Netherlands Antilles, Bahamas, Bahrain, Belize, Bermuda, Canada, Costa Rica, United States, Gibraltar, Cayman Islands, Isle of Man, Cook Islands, Guernsey, Jersey Islands, Marshall Islands, British Virgin Islands, Liechtenstein, Monaco, Samoa , St. Lucia, Turks & Caicos and Vanuatu
Panama	1	United States
Dominican Republic	1	United States
Peru	3	Argentina, Ecuador y United States
Trinidad and Tobago	1	United States
Uruguay	1	France

Source: Study on the Control of the handling of the transfer pricing in Latin America and the Caribbean. ITC- GIZ- CIAT. December 2012.

Another important aspect is the "attraction of genuine foreign investment". In general, countries or jurisdictions not cooperating or considered "tax havens" receive investments that do not have great impact on the country´s economy, in terms of employment, tax resources, or productivity. They are usually speculative investments. In addition, "anti-abuse" or "anti-tax havens" rules have discouraged the inflow of capital into these countries, due to the sanctions on this type of operations (major deductions, assumptions without proof, regular audits, etc...) All this has been discouraging the investment flow, so many financial companies or banks have pulled out their establishments situated in "tax havens".

By having access to transparency and information exchange standards, a country could benefit from foreign investment or protect the existing investment level.

1 *With the following link you could consult the evolution of specific agreements for information exchange and agreements to avoid double taxation in Latin American countries: http://www.ciat.org/index.php/es/productos-y-servicios/ciatdata/tratados.html*

An aspect that must also be valued, but that should not determine the negotiation of cooperation instruments, is the diplomatic relation. It is possible that for diplomatic reasons, two States wish to sign agreements or conventions. However, it is advisable before starting negotiations, to evaluate a range of issues such as trade, investment flow, people flow, risks for the country based on tax planning schemes adopted by companies that operate in the country and the ability to manage the information exchange.

The risk assumed by signing such instruments with the only purpose of feeding diplomatic relations is the noncompliance with the commitments based on administrative weakness or the obligation to face high costs of operation without a tangible return.

Once the above mentioned aspects are evaluated, it is necessary to verify if the tax system and the country´s regulations comply with international standards. For this, it is necessary to identify the major reforms that would be needed, evaluating their impact and the way that the changes will be managed. As previously mentioned when the "political power" was discussed, it is not easy to implement changes that could affect large economic groups operating in a country. More details about that policy that should be considered in the context of this analysis will be provided in the next section of this document.

One aspect that should be evaluated and was commented on the above paragraphs is the "ability to comply with international standards". The importance to comply with international standards in this subject lies in the need to harmonize the ability of countries and in particular of tax administrations to access and exchange information.

This aspect is important because in some cases, the lack of "legal reciprocity" between cooperation instruments could prevent achieving "effective exchange of information". To increase "material reciprocity" levels based on practice has also generated standards for ensuring a minimum efficiency level of an information exchange unit. While the aforementioned "material reciprocity" cannot be easily verified and should not be considered as "critical" when negotiating a cooperation instrument or meet a request for information, tax administrations must gradually evolve to harmonize their efficiency levels in this area. In the following sections the aforementioned standards will be detailed.

Finally, it is necessary to highlight the fight against evasion and tax fraud as a critical aspect for many countries that have high risk of tax base loss, as a result of international operations based on harmful international tax planning. As discussed in previous sections, the information exchange does not only benefits countries that adopt world income criteria, but it is also effective in countries that adopt territorial criteria.

There is no doubt that the proper use of this tool should provide greater tax revenue, either by their risk perception or for their effective use.

III. "KEY" ASPECTS TO ACHIEVE EFFECTIVE INFORMATION EXCHANGE

The road to the "effective tax information exchange" between States leads us to review a number of legal and administrative aspects that are considered basic to achieve this purpose. Hereinafter, we will discuss the main points relating to the "domestic legal framework" and "negotiation of instruments for information exchange", as well as the "administrative aspects" for the good performance of the “tax information exchange unit".

a. Domestic legal framework

First of all, it is necessary to verify if the country's Constitution allows or not and refers or not to the information exchange between States. Secondly, it is important to verify if citizens’ rights covered by the data confidentiality principle are so protected that it could be interpreted as a barrier for the exchange of information.

Given the Supreme nature of the Constitution in the legal hierarchy of countries, it will not be possible to move forward on other aspects if the necessary adjustments that allow providing other States with information subject to "tax secrecy” may not be implemented. In line with this, it could be mentioned that in those countries where international treaties have a "supra legal" level, with just their entry into force the Constitution would stop being a problem. However, it is not good that they come into conflict with the Constitution or other similar regulations.

All tax administrations in the world have verification and supervision powers that allow them to control their taxpayers; however these powers can vary significantly from one State to another. This will depend in part on guarantees of taxpayers and the importance tax resources have in a specific State.

What makes essential to review these rules comes mainly from two limitations usually included in the information exchange instruments They would not allow to provide information that cannot be obtained according to the laws and internal regulations and cannot adopt any administrative measures that go against the same laws or regulations (e.g. paragraph 7, subparagraph b) and c) of CIAT - MCIAT tax information exchange agreement model).

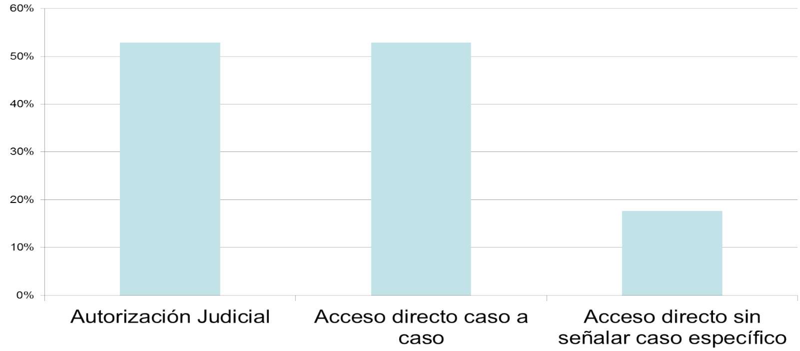
Such limitations may not be absolute, since most of the existing instruments and the most widely used models ensure a minimum of information exchange established by the laws and practices of a requested State should not prevent or affect the actions of the competent authority of the State which receives a request for information and provides information on behalf of financial institutions, parents or persons acting as agents or trustees; regarding the identification of shareholders or members of a legal entity or other collective entity or in the possession of the tax administration (e.g. Article 2 of the MCIAT).

According to "Implementing the tax transparency standards, a Handbook for Assessors and Jurisdictions" published by the OECD in 2011, the transparency and information exchange standard is mainly based on information availability, access to it and the existence of information exchange mechanisms. To do this, in line with the aforementioned in the preceding paragraph, it is necessary for a State or a jurisdiction to access banking information, identities and accounting information of asset owners and where this information is regularly provided by available systems.

Compliance with these standards should not be in conflict with the "tax secrecy" or other secrets in a State. "Tax Secrecy" is never eliminated; it remains when providing the information to another State that has the obligation to provide information confidentiality levels similar to those of the country of origin. Other secrets exist in the country, such as professional secrecy, industrial, trade and business secrets, the privileges of the professionals in law, financial/banking secrecy, among others should not be applied regarding "relevant" information for tax purposes. In this case, such information would be covered anyway by the "tax secret".

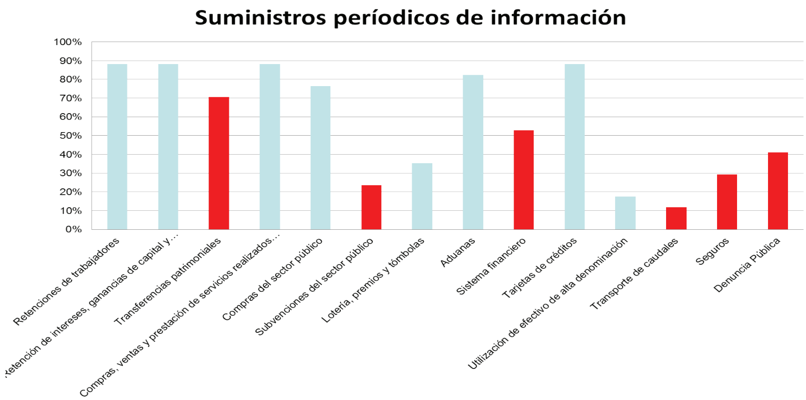
It is important to highlight that the previously mentioned secrets should not be subject to wide interpretations, since this could void the "relevant" information exchange.

The following graphic presents the ability of several Latin American countries to access banking information. As it can be seen, the sum of the three bars exceed 100% and this is so because some countries can use different procedures depending on the type of banking operation and other formal aspects:



Source: State of Tax administration in Latin America BID – CAPTAC-DR - CIAT: 2006-2010

The graphic below shows what information and what percentage is available for Latin American countries and it is obtained by periodical information, the vertical line corresponding to the percentage of countries that have periodic information and the horizontal (abscissa), concerning the classification of the information:



Source: State of Tax administration in Latin America BID – CAPTAC-DR - CIAT: 2006-2010

Although the differences of the verification and supervision powers and the availability of information are relevant between two States; they could mutually benefit from the exchange of information, not being barriers to prevent them from contracting. In short, the most relevant of this process lies in the satisfaction of the Contracting Parties during the implementation of the instrument.

Considering the limitations mentioned above, the internal rules of the countries could become not only a great limitation for the exchange of information, but a barrier to contracting State which intends to implement an internationally accepted model and applies "legal reciprocity" (e.g. MCIAT, MOCDE, Multilateral Convention, etc.).

Another important issue is the rules concerning 'conservation of records'. The tax rules often require taxpayers to keep records (books, supporting documentation of their transactions, etc.) during a given period of time. Some countries set different periods depending on the subjects and transactions, while others only set a period of general application.

This aspect is critical at the time of contracting. For example, in a State where the obligation to keep information is 3 years, by the mere fact that the taxpayer has no obligation to retain documents, a request for information from another State relating to a previous period could not be supported.

Countries usually establish conservation periods of at least 5 years, depending on different factors such as the condition of the taxpayer with the tax administration (registered/not registered).

This is closely related to the prescription rules, since these can also be a barrier in some cases for the effective exchange of information when the deadlines are different between States. This issue is more complex when we refer to concepts such as interruption and suspension, which operate differently between States. For example, there are countries where the debts never prescribe and others where the limitation period is automatically interrupted when a control process begins.

With regard to this last point, perhaps to harmonize these criteria should not be the issue, but it is important to know the limitations that might exist when making a request for information before subscribing or applying an instrument.

For ensuring the effective compliance of the verification and supervision standards with the tax administrations, it is necessary to have rigorous sanctions, but at the same time in accordance to the seriousness of the facts.

For these purposes, sanctions play a key role for formal non-compliance.

Based on international standards, the so-called "domestic interests" should not exist when considering a request for information. It should be treated as if the request was originated within a domestic performance context. This means that any required information from a taxpayer who does not comply with the formal duties, could be liable to a sanction that motivates compliance.

It is necessary to know in detail the "rights and guarantees" when making a request for information, since they directly point out the procedure to be followed. For example, such rights and guarantees may require for the taxpayer to be notified whenever there is information exchanged about him, and he may question or not the procedure. Some countries could eliminate this obligation by notifying the taxpayer in cases of tax fraud or to postpone the notification once the exchange is finished. Similarly, in some countries the obligation to notify could be eliminated when a federal court determines that the notification could harm the investigation.

Given these rights and guarantees, it is necessary to know the respective legislation of the counterparts on information exchange instruments for informing to the taxpayer the reasons for the notification that could hinder a procedure. As a result, a State may refuse a request for information.

An important aspect is the legal and regulatory powers that entitle a State to exchange information.

Many countries have internal rules that allow them to respond to requests for information from other States which have not signed information exchange instruments.

They would also send requests for information and validate documents from abroad to be used in formal procedures.

The existence of these rules allows the use of diplomatic channels to transmit and receive information. Also, if internal rules grant the power to the tax administration, it could sign administrative instruments for the exchange of information.

Although these types of internal rules are useful, they do not annul the convenience of payment instruments for the exchange of information. The "obligation" to respond to requests for information where all the agreed conditions are met is from these same instruments.

b. Negotiation of instruments for information exchange

When a State project to exchange information with another State, there are several valid alternatives to do it. These alternatives include "agreements to avoid double taxation" (DTC) with wide clauses for tax information exchange, either in the OECD, UN, regional or own models. Usually, in this type of instruments, information exchange arises in article 26, which does not present great differences among versions.

Others of the most used instruments are the "specific agreements for tax information exchange", which may have legal or administrative rank according to the possibilities of each State. As a variant to the specific agreements, there are agreements or multilateral agreements that may be signed at the regional or global level. Among them are the Directive 77/799/EEC, its updates and complements; the Nordic Convention on mutual administrative assistance in tax matters, the Convention on mutual assistance and technical cooperation between tax administrations and customs of Central America, and the Multilateral Convention on mutual administrative assistance in tax matters (Multilateral Convention).

The advantage of multilateral instruments is the possibility to access an information exchange network by negotiating a single document. This saves considerable time and money in the negotiation process. It should also be noted that such instruments are multilateral in allowing the information exchange with several countries, but the relationship always remains bilateral in the execution.

A country that only wants to exchange information should not have an Art. 26 of a DTC, since the main objective of this type of instrument is to avoid double taxation. To move forward on this type of agreement implies analyzing several additional factors not mentioned in the present work.

According to the wording of article 26 in the most current versions of the OECD and UN models, there would not be any restriction when exchanging information. For example, in the past this article presented some barriers for information exchange purposes or their use.

In certain cases, at the administrative level, it is necessary to generate "memoranda of understanding", which purpose are to generate greater certainty for the procedures within the cooperation instrument framework. For example, a memorandum of understanding could be generated within an automatic information exchange context, in a simultaneous control or with the aim of developing procedures based on article 26 of a DTC.

In Latin America, on March 2012, 73% of the Latin American countries were applying DTCs and 42% had information exchange agreements[2] in force. To April 2013, 30%[3] of the Latin American countries signed the Multilateral Convention. Given the importance that this matter has, it is estimated that these numbers will grow in the coming years.

To start a negotiation process of information exchange instruments, the following aspects have to be considered:

- **Bilateral/multilateral:** before a bilateral negotiation with one country, it is necessary to verify if it would be more convenient to enter a multilateral convention to which said country is member. By verifying this circumstance, multiple negotiating processes can be avoided.

- **Characteristics of the tax administrations:** many countries have integrated tax administrations (taxes/customs). In many cases, signing agreements that allow the cooperation for exchanging information in the tax field could be also an advantage on customs matters. Obviously, these models would work in those negotiations between States that have integrated tax administrations.

- **Subjective scope:** refers to the entities or individuals on which information can be exchanged. These may be residents of a State, its nationals or other on which there is information.

- **Taxes included:** there should not be any restrictions.

- **Notification of relevant regulatory changes:** even though this aspect is not essential, it could be of great help for the officers of the information exchange unit when assessing whether it is appropriate or not to send or process a request for information, consequently avoiding loss of time and resources.

- **Time:** is very important to define from when an instrument can be applied including the possibility to apply it on non-prescribed periods.

- **Exchange of information for criminal purposes:** it is important to define this aspect in the body of the instrument. If accepted, it is recommended that the so-called "double criminality" should not exist, where a country only exchanges information for criminal cases if there is a domestic case open on the same individual.

2 *Data obtained from the "State of the Tax Administration in Latin America" 2006-2010. IDB - CAPTAC-DR - CIAT.*

3 *Data obtained from the OECD web site: http://www.oecd.org/ctp/exchange-of-tax-information/Status_of_convention.pdf*

- **Cases in which it is not possible to refuse a request for information:** this clause ensures a minimum of transparency in the Contracting States. Usually it refers to financial information on ownership of assets, etc.

- **Obligation to use all available resources:** this clause ensures that a State uses all its powers and resources to meet a request for information, as if it was for its own interest. However, it should be limited by the "proportionality principle" mentioned before.

- **Limitations:** restrictions on the exchange of information should apply only in exceptional cases, in which the Contracting Parties would not be obliged to exchange information. It is important to know at the time of the negotiation what cases should be raised as a limitation and which not. For example, among the aspects that should not be a limitation we could mention the tax secret, banking/financial secret, the fact that the information is maintained by attorneys, agents and Trustees, the "domestic interests". If the limitations would affect public policy or public order, they involve providing information that cannot be obtained according to domestic laws. In other cases, the MCIAT has some differences with the MOCDE, since the MCIAT does not admits as limitation reciprocity, industrial, commercial and business secrecy and privilege of reservation of law professionals. The limitations are not bans, because they exempt the parties from the obligation to exchange information under certain circumstances. In these cases, the possibility of co-operating or not would be discretionary.

- **People to whom information can be disclosed:** it is necessary to review this clause carefully to avoid inconvenience when the instrument is used. In general, in different models, this clause is similar and has a great level of detail on who can access the information.

- **Disclosure of information in public court proceedings or in judicial decisions:** it is important to provide this aspect explicitly in the instrument´s body.

- **Confidentiality:** there should be a clause that defines the confidentiality level that will be granted to the information exchanged. For example: information deemed secret according to the norms of the State which provided it, if they are more restrictive.

- **Rights and guarantees for taxpayers:** as much as possible, it is important to capture in the instrument the scope of these rights/ guarantees and procedures to follow.

- **Admitted procedures for exchanging information:** the instrument should expressly consider procedures or methodologies that can be applied in the Contracting States for information exchange. For example: spontaneous, automatic, on-demand simultaneous audits, audits abroad, among others. Also, some instruments have other additional cooperation procedures such as assistance on enforced collection or on notification of performances.

- **Reservations:** multilateral instruments must have certain flexibility that motivates their accession by States with different interests and tax systems. In this sense, it is important to define on what aspects it is possible to oppose reservations.

The following table compares the main characteristics of the CIAT Tax Information Exchange Agreement Model (MCIAT - published in 1999), OECD Tax Information Exchange Agreement Model (MOCDE - published in 2002), of the Mutual Assistance and Technical Cooperation Convention between tax administrations and customs of Central America (published in 2006) and the Multilateral Convention on mutual assistance in tax matters and its Protocol (published in 2010):

Concept	MCIAT	MOCDE	Central American Convention	Multilateral Convention
Multilateral	YES	YES	YES	YES
Was it adopted by countries?	YES	YES	YES	YES
Does it incorporate customs cooperation procedures?	NO	NO	YES	NO
Scope of Application: resident, national, and other.	YES	YES	N/I	YES
Taxes included - are there any restrictions?	NO	NO	NO	NO
Notification of relevant legal changes	YES	YES	N/I	YES
Temporary Scope	N/I	N/I	YES	YES Criminal, retroactive
Does it accept information exchange for criminal purposes?	YES	YES	N/I	YES. Only upon agreement
Unable to deny requests: Financial institutions / agents / trustees / shareholders / partners / legal / domestic interest	YES	YES	YES	YES
Obligation to use all means available	YES	YES	YES	YES

Concept	MCIAT	MOCDE	Central American Convention	Multilateral Convention
Limitations: -Public policy -Administrative Measures contrary to the law -Information not obtainable under the laws - Discrimination	YES	YES + industrial, commercial, professional secrecy	NO + reciprocity and constitutionality	YES + industrial, commercial, professional secrecy, taxation contrary to PGA / + DTC + subsidiarity disproportionate administrative burden
The information will be disclosed to persons involved in the determination, assessment, collection, collection of tax credits, tax enforcement, prosecution of tax crimes, resolution of administrative and oversight of the above	YES	YES + prior consent, information may communicate to other persons, authorities or jurisdictions	NO. Compliance with the functions and powers of the TA	YES + previous consent and if allowed by law, the information could be used for other purposes
Ability to disclose the information in public court proceedings or tax judgments	YES	YES	YES. It does not specify the type of process	YES
The information is considered secret according to state standards that provides it, if these are more restrictive	YES	YES	N/I	YES
Guarantees	N/I	N/I	N/I	YES
Spontaneous	YES	NO	N/I	YES
Automatic	YES	NO	N/I	YES
Simultaneous Control	YES	YES	N/I	YES + joint authorities
Control abroad	YES	YES	YES	YES
Industries	SI	NO	NO	NO
coercive collection Assistance	NO	NO	NO	YES
performances notification assistance	NO	NO	NO	YES
Specialized technical cooperation	NO	NO	YES	NO
Reservations	N/I	N/I	NO	YES

N / I: the instrument does not expressly include clauses dealing with this matter.
Prepared by the author

c. Administrative aspects

Here it is necessary to distinguish between those specific aspects that are directly linked to the information exchange unit and the others that have to do with structural issues of the tax administration or a given State that directly impact on the process under analysis.

With regard to the specific operation aspects information exchange unit, the following are highlighted:

Competent authority for the exchange of information

Historically, the relations between States have been channeled through the Ministry of Foreign Affairs, which is the environment for managing these issues. However, when we refer to specific instruments for the exchange of information, or even the DTCs; they are negotiated and implemented in another scope. This does not prevent the Ministry of Foreign Affairs to be involved, but our experience shows that these effects involve the Ministry of finance and the tax administration.

To manage the exchange of information it is necessary to define a "competent authority". This issue is not handled in the same way in every country, many factors influence, among them the structure for the information exchange unit and procedures to implement this exchange. For example, if we refer to the DTCs, the competent authority is usually at ministerial level (e.g. Ministry of Finance), and the Ministry delegates this function to the tax administration. Internal rules usually grant this authority to tax administrations. The same happens for specific information exchange agreements.

It is consistent for the competent authority to be part of the tax administration, since it is the one which will identify when it is necessary to process a request for information, will collect information as a result of its verification and control powers, and will coordinate the simultaneous audits or automatic exchanges.

If the exchange of information is performed at the highest level or in another public entity the process time will considerable increase as well as their associated costs. This recommendation should be considered by the tax administrations when defining the competent authority, since it is more convenient to delegate the function to a no very high level officer, who is able to handle all documentation received in the framework of this process.

The competent authority is usually one person or many people, depending on the adopted structure. For example, France adopted a decentralized structure that provides competent authorities in their different tax regions and the United States have offices classified according to the region with which they exchange information. Most countries, particularly in Latin America, have centralized information exchange units.

The changes on competent authority must be reported immediately to the respective counterpart of instruments for information exchange. It is recommended that the competent authority to be defined in a function or position within the tax administration, and not on a specific person, since this facilitates the changes that may occur.

It is also necessary to define a "direct contact" for each generated exchange in order to have a more fluid communications and therefore progress with the procedures.

Information exchange Unit

In recent years, Latin American countries have established information exchange units (hereinafter, the unit). Currently, 47% of countries have these units.

In general terms, the resources needed to create an Office for the exchange of information are not many in relation to the potential benefit brought by the "effective exchange". Nor it is necessary to begin activities with a big structure. For example, most of Latin America and the Caribbean offices work with an average of three officers (with the exception of Argentina and Mexico). Obviously, the size of the unit depends on the level of priority that the authorities assign to the topic, on the existing instruments network and on the tax administration´s resources.

As mentioned before, when talking about the "competent authority", the structure to be adopted by the tax administrations for exchanging information can be centralized or decentralized. This will depend on the particular characteristics of each country. In Latin America and the Caribbean, the information exchange units are centralized.

First, it is necessary to define which functions the unit will assume. For example, under certain circumstances, Mexico´s SAT has given the possibility to carry out audits. It is also necessary to define the unit´s role within the control context or in the so-called "audits abroad". In addition, some units are able to intervene in the negotiation of memorandum of understanding and specific agreements on information exchange. The functions of the unit must be defined in the tax administration´s internal regulations.

Another important aspect is to delimit the responsibilities. For example, the AEAT unit is responsible for each of the information exchange methodologies (e.g. upon request, automatic, etc.). In small units, it is obvious that there is not much where to delimit the scope.

In order to establish more accurately the functions of the area and the responsibilities of its members, it is essential to develop a manual that defines the procedures to be followed by the unit. In this manual, it is important that aspects relating to language, feedback treatment, costs distribution, deadlines and internal procedures, sources to be used to process an information request (internal/external), update of counterparts regarding the competent authority and relevant standards and forms or standard formats are defined (request for information, feedback, etc.).

The aforementioned issues should be considered within the framework of a series of basic procedures as those mentioned below:

- Sending/receiving applications
- Registration of a request
- Sending/receiving information
- Sending/receiving information under the "spontaneous" procedure
- Coordination of the automatic exchange. In general, the procedures to be followed will depend on what was agreed with the respective counterpart regarding its implementation.
- Coordination of visits by foreign officials and; simultaneous and joint audits.
- The competent authority functions
- Direct communication management
- Management control of the information exchanged

Many of these procedures could be part of a memorandum of understanding if for some reason, as a result of the negotiation, it is necessary to provide special treatment to the exchange of information with a specific State. However, the importance of manuals, forms, etc., ensures a minimum quality standard to the unit. For example, the forms may not be used in all cases, but they provide a guideline on the information field that should be considered for making an information request based on the best international standards.

Regarding the deadlines, the general rule is to always provide a response as soon as possible. However, based on the international experience the following are considered reasonable periods:

Procedure	Term
Acknowledgement of receipt	1 month and 7 days if it is sent by electronic means
Invalid or incomplete application	2 months
Information held by the tax administration	2 months or 1 month if information must not be processed
Information that is not in the possession of the tax administration	6 months
Cases where the deadline may not be fulfilled	This situation and the period in which the request may be answered will be notified. Always before the expiration date or within three months of its receipt.

Elaborated by the Author

Once the previous aspects are determined, it is necessary to analyze the characteristics that the human resources should have and the material resources required.

It is important that human resources to affect the area have several years of experience in different tasks within the tax administration. The unit being a cross-sectional area within the Organization; it relates to areas of audit and investigation, legal authorities, among others. It requires officials who know very well the structure of the tax administration, its partners and processes. Profile of officials will depend on the functions of the area. An area that is dedicated only to exchange information between two States, one which implements controls, advises, negotiates, or monitors is not the same.

Considering a unit that has broad functions, officials should have the following competences:

- Extensive knowledge of internal rules and of the relevant parts of the counterpart standards, as well as the information exchange instruments network.
- Skills for resolving conflicts, with counterparts and internal.
- Ability to understand and process information from the outside and databases.
- Knowledge of internal administrative procedures
- Knowledge of the standards used for the automatic information exchange. In relation to this aspect it may be necessary for the computer Department to give support to the unit when trying to exchange computerized data on a routine basis.
- Ability to identify faults in the internal procedures relating to information exchange and propose adjustments
- Knowledge of at least one additional language
- Experience in the research and control areas.

The Unit presents no particular requirements when we refer to material resources. In general it needs the same resources that are used in any modern office (communication systems - phone, Internet, Fax, etc.-, furniture, overhead costs, etc.). Among the specific resources that the area requires, are the costs for translation of documents, correspondence, travel abroad in order to carry out procedures if necessary, participate in international forums on the topic, take training, negotiate procedures with partners, etc.

Once the unit is in operation, it is recommended to define performance indicators, feed and evaluate them. It is important to value these indicators from the beginning in order to compare the results on different years and take relevant decisions (e.g. expand the capacity of the unit, negotiate new instruments or renegotiate the existing ones, change procedures, forms, etc.). To define these indicators, it is important to keep the following records: date of receipt of a request, date of notification about invalid or incomplete requirements, date of notification of requirements that cannot be addressed in the pre-established term, exceptional claims (deadlines, certifications, etc.), date in which the information was provided, date in which the procedure ends, date when the feedback was sent. It is also important to keep a record of procedural aspects that have generated problems and other quality aspects that allow interpreting the results of the indicators that will be generated.

With this information, it is possible to work on indicators. Examples of indicators are the following:

- No. of attended /received requests
- No. acknowledgments of receipt/Total requests
- No. on time responses/Total responses
- No. of requests sent or received where the information requested or received is incomplete/Total requirements sent or received.

It is important to also know the indicators of other units in order to evaluate the efficiency of the area based on a "benchmarking" and thus to implement improvements in the future.

The relationship of the unit with other areas is an important issue to watch, since the unit would mainly perform management issues, mainly users and providers of information and audit areas.

For example, it is possible for a unit to be responsible for gathering information available in the tax administration databases in order to respond to requests for information.

However, in case it is not possible to use these rules or apply the verification and supervision powers, it should coordinate with audit areas, which have access to these databases, files and processes for functional reasons. For example, it is not common for a unit to request information from a taxpayer, impose sanctions in case of non-compliance or order search warrant. In these cases it will depend on other areas to comply with the commitment to apply all means available to deal with a request.

The unit is related to auditing areas when processing a request for internal information, receive and respond to requests from abroad, sending information abroad, receive and use information from abroad, provide feedback, receive and give treatment to the feedback from abroad. The unit also is related to audit areas when assisting in information exchange processes (in some countries the Unit advises on cases on which it can request information abroad or for example identify and send information spontaneously) and it feedbacks from the abroad information received.

Regarding the relationship Unit – Auditors, it is important to prevent conflicts or to manage them in the best possible way. Conflicts might occur when there are differences on the treatment of certain information or request and when the unit has the ability to monitor or engage in auditing procedures. Therefore, it is important that the unit properly justifies all its actions (for example if it is decided to refuse a request for information or engaging in a process), since the relationship with Auditors is key for success.

Another task that usually handle units, is the "awareness and training" of Auditors.

As discussed at the beginning of this document, information exchange implies a major change in the form of the Auditors work. It is not easy for them to incorporate using information from abroad in their usual processes. It is even more difficult to identify information that might be useful for other tax authorities or promote simultaneous audits.

For this, it is necessary to carry out strategies that motivate the use of tools, such as rewards, training, etc.

For the purpose of knowing through a practical example the use of information exchange in Latin America, the following table shows those countries that frequently use this tool to transfer pricing cases and those who tend not to use it:

Criteria applied	Country
Usually send requests	Argentina, Chile, Colombia, Costa Rica, Mexico y Peru
Do not usually send requests	El Salvador , Ecuador[1/], Guatemala[2/], Honduras, Panama, Uruguay, Venezuela

1 / In some circumstances they have requested information to other tax authorities but it is not a common practice.

2 / Do not make exchanges of information, because they have not initiated the control procedures, however already has seven (7) signed information exchange agreements with the Nordic countries.

Source: Consulted tax administrations.

Source: Study on the Control of the handling of the transfer pricing in Latin America and the Caribbean. ITC-GIZ-CIAT. December 2012.

For example, between the aforementioned rewards, the following are highlighted: travel abroad to participate in international events that allow exchanging experiences between auditors, to obtain better qualifications, access to language courses, among others.

It is important that the unit, independently or in coordination with other areas, design national training programs which will allow to present the existing tools, explain in detail the procedures for exchanging information, addressing questions based on real cases and in general, to encourage the information exchange.

An advisable practice is to design a site within the tax administration "Intranet" that allow to download all the existing instruments, allows to know about the negotiations in process, consult the relevant internal rules relating to the exchange of information, download manuals and forms, documents presenting good practices and recent international developments, make consultations on issues, among others.

The highest authority of the tax administration must accompany the message to promote the information exchange.

General aspects

There are two major issues which are essential for the tax administrations and which are closely related to information exchange processes. One of them has to do with ensuring confidentiality[4] standards and the other has to do with the availability of information.

Since the tax administration must ensure the fulfillment of the "tax secrecy", it is relevant to take all necessary measures to prevent leaks of information and misbehaviors of their officials, whether voluntary or involuntary. While the filtering of internal information can generate great disadvantages for the tax administration, misleading disclosure of information subject to "tax secrecy" in other States can generate responsibilities in terms that could also affect the reputation of a State as information is exchanged.

There fore, it is important to make officers aware of the importance of following the rules that ensure information confidentiality information and the sanctions that could be given in the event of failure to comply, setting up controls, solve problems in an Executive way trying to minimize the negative effects, document all processes, maintain information in secure sites, among others.

4 *It is recommended to consult the "guide of the OECD on the protection of the information subject to Exchange tax purposes"*

For this purpose, the internal5[5] control area plays an essential role and must control not only the internal standards for confidentiality, but also those included in the respective instruments for the exchange of information (for example, applications that can be given to the information may not be the same in all cases).

For example, a comprehensive protection to the confidentiality policy must be reviewed and approved by the highest authority and consider at least the following aspects: classification of information and secure files, appoint officials, establish safe procedures for sending information (physical/electronic) and a series of basic actions:

- Verification of the Staff background and security controls for employees
- Detailed evaluation of employment contracts (e.g. confidentiality clauses)
- Criteria of access to premises and electronic and physical records.
- Staffs dismissal policies
- Elimination of information policies
- Unauthorized disclosures

When sending information abroad, the documents that have to be protected are: the request for information, correspondence and information itself. Both the request for information and correspondence may contain valuable information. For this reason it is usual for many tax administrations to use these documents to feed their tax intelligence databases.

When sending information it is important to include the data from the competent authority, to give validity to it; tag all information that is considered confidential, include integrated notices on information confidentiality, and send it by secure electronic media or through emails that have international records that allow their tracking. In all cases, the correspondence must be received by the competent authority, which stores it in secure files.

When sending computerized information electronically, it is important to know that it will have a confidential character throughout the process. Only authorized persons may check the competent authority´s mail. The sender is responsible for the information until it is received by the respective competent authority. To manage this process, it is necessary to have a secure platform or encrypted emails.

5 *On this point the manual on Internal Control of the tax authorities and the regulated system of Internal Control, developed by CIAT, the AEAT, AECI and the IDB can be consulted. www.ciat.org*

To automatically exchange information, it is important that records are coded to prevent leaks. Exchanges may occur through optical media, secure platforms or encrypted files sent via email. Regarding this last mechanism, it is important to consider the size of the files to ensure that the information is actually received.

In the process for receiving information it is important, first, to classify the information received, then store it in a safe place, such as in a physical file, a special database or a general database with limited access. To access this information, security measures such as the use of electronic fingerprints to control access to the information, defining authorized officials are required, and printing only if it is necessary to restrict the access to the physical file, access to information based on the "need to know" principle.

It is also useful to keep a record of people who received the information and who made copies.

It is recommended for the competent authority to include warnings of the information in the transmitted letter and not to transmit the information received, but the relevant parts that are presumably useful to everyone who receives them. For example, the correspondence is not revealed to the Auditors.

The second essential aspect mentioned at the beginning of this section is related to the "availability of information". This issue is closely linked to the laws of a country, the powers of the tax administration, their level of development, the development level of other governmental institutions that handle information of tax interest and relations with other government institutions.

It takes time and many resources for the tax administration to develop information systems and generate new sources. It is also complex to adopt measures that would allow providing maximum reliability to the information that is uploaded into the databases.

Currently there are many technological developments that facilitate the massive access to reliable information, such as the "electronic invoice", the presentation of returns via the web, using geo-reference data, etc.

The evolution of tax administrations, along with the availability of more and better tools, have allowed keeping a large amount of data that can be obtained and exchanged with other States in the tax administrations systems immediately or in a relatively short period of time. However, some tax administrations that have not yet reached an average development level will have to go to the taxpayers more frequently and probably take more time to fulfill a simple information request.

For example, the information that is usually most requested at the international level is the following:

- Information about payments and withholdings
- Balance Statements
- Bank accounts: ownership, movements, payments and collections
- Ownership of real estate
- Declaration of payments to non-resident, non-resident identification
- Taxpayer identification data
- Information on legal entities
- Financial statements
- Supporting documentation for significant operations
- Statements by the taxpayer or third parties

It is important to determine what information is public, since it could be obtained by other means than the formal channels.

Based on the "State of the Tax Administration in Latin America" 2006 - 2010. IDB - CAPTAC-DR - CIAT", 100% of the Latin American countries establish in their regulations the obligation of taxpayers, responsible third parties and third parties unrelated to the legal relationship to provide tax information and have a computer database for the support of tax control tasks and select taxpayers to be audited based on information crosses.

Also, 23% of these countries assign a tax identification number to non-resident taxpayers, 70% can get information about whether a company is a subsidiary of a non-resident matrix and 53% has implemented a Declaration on international operations.

To ensure minimum quality standards of information, tax administrations should have a permanent, complete, correct and updated registry of taxpayers. The following table shows the percentage of Latin American countries whose taxpayer's number have a series of "key" characteristics in order to fulfill the quality standards:

	YES	NO
Obligation of all taxpayers to be registered	82%	18%
Registration and incorporation of the information to the registry of taxpayers in real time	82%	18%
NIT derives from the CI or registry of companies	88%	12%
Public/private agencies to record the financial	94%	6%
TA modifies ex officio the taxpayers registration transactions using NIT	76%	24%
There are automatic updating mechanisms based on third party information or from the TA	41%	53%

These data shows the need to identify non-residents in the region and to generate information about international operations, being this information very important for international information exchange purposes.

If we only focus on the table´s data, we could confirm that in Latin America there are no major problems to manage the taxpayers' registry. However, there are other factors that affect its management and make the efficient and effective management of the registry a challenge for tax administrations in the world.

Based on the aforementioned study, 100% of the tax administrations in Latin American countries can get information regularly, without the need of a special requirement.

However, slightly more than 50% receive information from the financial system and less than 20% can access this way to information on bank accounts.

On the other hand, 59% of the Latin American countries have external audit reports from taxpayers to identify risks and 76% carried out studies on the functioning of the economic sectors. This last aspect is relevant for the exchange of information on industries or branches of the economic activity.

For strengthening the available information levels for internal use and for exchanging with other tax authorities, it is recommended to observe the following:

- Assess the legal capabilities
- Develop studies to identify informants and sources of information
- Promote and arrange partnerships with public institutions, the private sector and other States
- To develop capabilities to automatically validate the information received and consolidating information reported by informant
- Develop differentiated purging processes and quality control
- Evaluate in detail the cost/benefit ratio of information regimes
- Try to contribute with other public institutions to improve the quality of information and its availability.
- Investing in information technology.

FINAL CONSIDERATIONS

FINAL CONSIDERATIONS

Dr. Carlos Maria Folco
General Attorney, Tax Prosecutor
(Argentina)

Carlos María Folco

We would like to congratulate CIAT authorities for the choice of this essential topic for this 47th General Assembly program, highlighted by various speakers.

We also congratulate the Federal Administrator of the AFIP and all who have helped in hosting all participating foreign delegations, offering technical and organizational support to make possible this successful event, as well as the excellent service provided to participants.

The great Attorney Tucumano Juan Alberdi Baptist has written in his famous "The Economic and Income System of the Argentinian Confederation" that "Wealth and the existence of the power are essential for the nation. With no income there is no government; with no government, no population, no capital, there is no State".

Alberdi had a direct influence in the Argentinian Constitution of 1853, which doctrine is in the "Bases and Starting Points for the Political Organization of the Argentine Republic".

After establishing the type of government, he drafted the National Treasury, understanding that the Treasury and the Government were tied.

No government planning is possible with high tax fraud indices. The States make great efforts to fight it, at international levels. Greater transparency of financial activities is needed at worldwide level, as well as a greater collaboration between countries.

The efficiency and the effectiveness in tax collection is a constitutional mandate for protecting, strengthening and satisfying human rights, in this sense its final mission, as stated in the Argentinian's Magna Carta, is "to promote the general welfare".

We will summarize the most important aspects in the discussed topics:

1) The international economic arena has greatly expanded, creating a significant economic interdependence between nations, increasing goods, services and capitals flows, as well as the globalization of technology and information.

To answer this complex reality, the States have structured and developed the international trade, but at the same time they have realized the need to strengthen international tax policies.

Therefore, the guidelines for international trade are provided by an important set of treaties and international agreements.

In that context, the international taxation plays an important role.

It is important to remember that DTCs´ purpose is to avoid double international taxation, but beyond this intention, they don't prevent sophisticated fraudulent maneuvers.

Here is the first significant contribution to this Assembly. The AFIP Federal Administrator (Argentina) claims the need to eliminate “double non taxation” in international taxation, which can take place, for example, through treaty abuse or treaty shopping, when an individual or a legal entity uses the provisions of a DTC for the single purpose of evading the tax burden, even if they are not resident in any of the contracting States, so the purpose of the treaty is mocked.

From the above mentioned, Dr. Michel states that with aggressive fiscal planning, certain taxpayers with global level operations try to have tax benefits, from the low taxation levels at source and the deferral (or nonpayment) of taxes in the residence jurisdiction, resulting in what we know as double non-taxation.

This double non-taxation phenomenon derives from deceptive returns or the abusive use of legal structures or commercial practices, with the purpose to hide or to distort the reality or economic objective of businesses, relations or situations that affect the tax determination, which represents an international tax evasion.

He also confirms the Tax Administration participation in the evaluation and negotiation of DTCs.

He states that Argentina has decided to create a Commission to evaluate and review agreements to avoid Double Taxation, with the purpose of performing a periodic review of the tax consequences of the mentioned agreements, as well as to make a multidisciplinary analysis and evaluation of the agreements in force or in process, adopting integral and coordinated evaluation mechanisms to determine if the tax sacrifice imposed by the application the agreements to avoid the double taxation is justified. The work of this Commission will mainly come from AFIP data bases, sectorial crossings of information, research by sectors and complete regimes of information established by the AFIP.

Similarly, within the new tax agreements negotiation guidelines, Argentina promotes a new vision which gives the possibility to carry out regular inspections to the tax treaties, verifying the effects of their application by comparing them with the expected results at the moment of negotiation.

This is the approach to a “Dynamic Agreement”, i.e. not tied to a rigid interpretation, but placed under scheduled inspection - previously agreed - and versus results.

Similarly, Dr. Beatriz Gloria Viana Miguel’s (Spain) presentation discusses the double no-taxation, confirming this reality in international initiatives such as the OECD’s and the European Union, which approach the topic in different manners.

Spain has made a reform, maintaining the legal system at the forefront of the fight against fraud, in which I would highlight four remarkable measures.

The first three are material and the fourth is organizational.

First: the obligation to provide information on assets and rights located abroad. There is now a regulation in force to present an annual information statement on accounts, values and buildings located abroad for resident individuals and entities in the Spanish territory.

This provision is to effectively fight against the fraudster who obtained income from abroad, did not declare them and waited for the prescription in order to get the benefits on accounts or assets out of the Spanish Treasury’s information scope. This measure is reinforced by the tax information that the administration hopes to obtain thanks to bilateral cooperation instruments.

The legal framework is established by recently signed tax information exchange agreements, along with the renegotiation of the information exchange clause in some other previous agreements.

Failure to inform is considered a very serious infraction, with high financial sanctions. The inclusion of undeclared goods or assets in the income taxation bases from individuals and enterprises is another consequence. Finally, the non-declared goods or assets are now considered in the income tax and in the corporate tax as unfair patrimonial gain.

Second: The limitation of the financial expenses deduction in the tax on corporate profits.

Financial expenses generated by a commercial entity for certain operations between organizations that belong to a same group are not deductible (acquisition of participation in the capital or funds of any type to other entities of the same group and contributions in capital or funds from other organizations of the same group). The possibility that those financial expenses are deductible exists only if the taxpayer provides valid economic reasons for performing these operations.

Third: cash payments are limited. Operations to be paid in cash will not be allowed above a certain amount. For operations that cannot be paid in cash, the parties will have to keep payment vouchers, during a five years period, to prove that the payment was not in cash. The purpose of this provision is to make difficult money laundering or benefits from irregular capital in Spain or abroad.

Fourth. The creation of a highly specialized tax office for international operations; the National Office of International Taxation has competence on management, planning, and operative coordination. The office´s main focuses are international operations and transfer pricing analysis as well as non-residents taxation.

The effective answer to international taxation cannot be solved by each country in an isolated manner. It is based on three great axes, information, legislation and enforcement.

Without information it is impossible to manage the taxes and in case of international operations, this information comes from third parties.

Tax administrations must support international initiatives and be better organized for an effective tax information exchange.

Finally, various agreement models to avoid double taxation (the OECD; The UN; the Andean pact), have been described, and a recent example is the signature of the agreement between the Argentinian Republic and the Eastern Republic of Uruguay for tax information exchange and a method to avoid the double taxation, which Dr. Michel called as the “Rio de la Plata Model” due to its specific characteristics.

This agreement includes regulations to avoid double taxation as well as effective information exchange aspects for international tax cooperation.

We consider that as a result of negotiations, there is a trend towards a "Hybrid Model", i.e. a bilateral framework for international tax relations, which can include different clauses from other referred Models adapted to the domestic legislations and interests.

Even for countries that have adopted the "territoriality criterion" – which links tax regulation with political sovereignty - CIAT has rightly pointed out the benefits that could be obtained from the effective implementation of information exchange and international taxation units, which are as follows:

- Control of transfer pricing abusive manipulation;
- Control of consumption taxes such as VAT;
- To control "treaty abuse" schemes;
- To detect unjustified patrimonial increases;
- To avoid double taxation;
- Assistance in coactive collection;
- If the instrument allows it, it could be used for other purposes such as the fulfillment of the convention against the bribing of Public Foreign Officials, reports of financial crimes, etc.

2) Prof. Heleno Taveira Torres, in his opening presentation, showed us an innovative perspective on the Legal Security Principle; universally recognized, based on legal certainty.

He states that it should be applied also in favor of the State and not only in favor of the taxpayer, clearly identifying it as a two-ways road.

He emphasizes that legal certainty, stability of the norms, good faith and transparency must coexist in a Democratic Rule of Law.

We could add that the balanced use of Clause XXXVI of the American Declaration on the Rights and Duties of Man, which states that: "It is the duty of every person to pay the taxes established by law for the support of public services."

3) Another interesting aspect against harmful tax practices is the creation and development of the "global taxpayer" concept, highlighted by the AFIP Federal Administrator and by Dr. Guillermo Michel (Argentina) in their presentations.

This innovating concept helps the tax Administration to be aware of the integral tax situation of taxpayers and executives, at national or international level.

In line with this concept, new measures have been implemented, such as the new return for the profit tax, specially related to international taxation.

4) Another question discussed in the Assembly, with high expectations, was the BEPS project (Base Erosion and Profit Shifting) of the Organization for the Economic Cooperation and Development.

On the matter, Lionel Testevuide, Official from the French DGFiP, showed that during the summit held on June 18 and 19 in Los Cabos, the G 20 countries heads of States and Governments, along with France and the United States, requested the OECD to present an action plan against the bases erosion in the corporate taxes and transfers of profits (Base Erosion and Profit Shifting - BEPS). In Moscow, on February 14 and 15, the OECD has presented a document on this topic to the Ministers of Finances, and in June of 2013, a road map on the possible options will be submitted.

The referred works organized by the OECD consist of three groups:

The first group specifically examines topics on anti-abuses, packages of measures based on different qualifications between States (hybrid), abuses of agreements, deducible payments and preferential regimes.

The second group analyzes the territoriality rules and specifically the permanent establishment concept, withholding, the residence concept, and the tax regimes for enterprises controlled by foreign companies.

Finally, the third group focuses on transfer pricing.

The speaker approaches the debate related to intangible goods, stating that France wishes to complete the work on the intangible goods, but in accordance with the arm length´s principle.

The OECD’s secretary, in preparatory documents, suggests a wider definition and evolution of the profits derived from intangible goods according to transfer pricing (to share the economic property within the group).

Finally, France supports a rule that would be technically strong, to avoid any arbitrary and unilateral state approach, adding that the existence of an intangible good could be based on a legal analysis of the goods concept that would benefit from some legal protection (intellectual, commercial property laws or competition laws).

He concludes that the income derived from them would have to be taxed in the state where the legal property is registered, except for abusive use cases.

5) In relation to transfer pricing control methods, the Federal revenue of Brazil's presentation refers to the transfer pricing model adopted in their country, which is not a model imported from other countries.

Under such circumstances, Brazil has decided not to adopt the APA.

6) We selected to discuss another important topic, relating to the "Global Forum on Information Transfer and exchange - Global Forum Argentina".

As mentioned before, the 2009 international financial crisis has dimmed the tax transparency and consequently brought changes in the international cooperation.

Even if transparency has been internally improved, by multiplying international information exchange agreements, there are still some weaknesses in member administrations' internal systems, which limit their effectiveness.

Indeed, all Global Forum activities aim to ensure the effective implementation of the international transparency rule and information exchange for tax purposes.

Regulations are mainly based on information exchange instruments models related to assets and accounts transfers, the lifting of banking secret, etc.

This regulation must be considered as a triangle (transparency triangulation), which center it is the information.

Information is essential for the tax system management.

In each angle of this triangle there are three pillars on which the rule is based: access, availability and information exchange.

Finally, the international regulation requires the information to be available, accessible by competent authorities and to have a legal framework to respond the requests for information exchange.

7) In relation to the transfer pricing control, the CIAT presentation underlines the existing disparity in the evolution in Latin America and the Caribbean countries.

Gonzalo Arias has classified the countries in five groups, considering a series of indicators, such as the date of their legislations, the progresses in control or audits and the human resources aspects.

Thus, he identifies a first group integrated by those countries that have been implementing norms for more than a decade, as Argentina, Brazil and Mexico.

A second group of countries have implemented legislations later, but have made notable progresses, as Chile, Ecuador, Dominican Republic and Venezuela.

In both groups, regulations cover all or most of the aspects that allow the transfer pricing control and there are specialized units for it, as well as mandatory documentation; audit and judicial cases are processed.

A third group includes countries that have strengthened the transfer pricing regulations and have created or are in process of creating specialized units, as Colombia, Peru and Uruguay.

In the fourth group of countries (El Salvador, Guatemala, Honduras and Panama), regulations are in a more premature stage, they just have entered or are still waiting to enter into force.

Their transfer pricing units are also in formation process.

The fifth group of countries has not yet introduced regulations (Bolivia, Costa Rica, Jamaica, Nicaragua, Paraguay and Trinidad and Tobago).

However, all of them (except for Jamaica and Bolivia) are in process of creating legal regimes for transfer pricing control.

Similarly, it was noted that the region uses the method described in Argentina´s law specially designed for exporting “agricultural commodities” (sixth paragraph, art. 8 of the simplified Profit Tax Law), all inclusive hotels pricing methods and automatic determinations in Dominican Republic, “protection regimes” or “safe harbors” for “maquiladoras” in Mexico and simplified Brazilian methods that have generated many debates in international tax forums.

The CIAT chart below schematically shows these developments:

Countries	Projected legislation	Regulations before 2002	Control in process	Cases in Courts	Use of data base	Transfer Pricing units in the Tax Adm.	Groups
Argentina	Yes	If your card's	Yes	Yes	Yes	Yes	I
Bolivia	No	No	No	No	No	No	V
Brazil	Yes	Yes	Yes	Yes	Yes	Yes	I
Chile	Yes	Yes	Yes	No	Yes	Yes	II
Colombia	Yes	Yes	No	No	Yes	Yes	III
Costa Rica	No	No	No	No	No	Yes	V
Ecuador	Yes	No	Yes	Yes	Yes	Yes	II
El Salvador	Yes	No	No	No	No	Yes	IV
Guatemala	Yes	No	No	No	No	Yes	IV
Honduras	Yes	No	No	No	No	No	IV
Jamaica	No	No	No	No	No	No	V
Mexico	Yes	Yes	Yes	Yes	Yes	Yes	I
Panama	Yes	No	No	No	No	Yes	IV
Nicaragua	No	No	No	No	No	No	V
Paraguay	No	No	No	No	No	No	V
Peru	Yes	Yes	Yes	No	Yes	Yes	III
Dominican republic	Yes	No	Yes	Yes	Yes	Yes	II
Trinidad and Tobago	No	No	No	No	No	No	V
Uruguay	Yes	No	Yes	No	No	Yes	III
Venezuela	Yes	Yes	Yes	No	Yes	Yes	II

Source: ITC-GIZ-CIAT study on "Control of Transfer pricing manipulation in Latin America and the Caribbean" CIAT. December 2012.

8) We reserve a space for court issues

Various cases have been through judicial processes: Argentina (29); Costa Rica (3); Ecuador (22); Mexico (80) and Dominican Republic (22).

There are specialized courts in Argentina, Chile, Colombia, Ecuador (judicial), Guatemala, Mexico, Peru, Dominican Republic and Panama (Administrative).

It is worth noting that even in countries where there are specialized courts; very few have knowledge on transfer pricing issues.

We have to add that there is a significant delay to resolve judicial cases.

We conclude with a thought of Couture, a famous Uruguayan practicing lawyer, who stated that in law, time is more than money: It is justice.

We agree with Couture, even more when this is related to public income, which guarantees the welfare of our nations.

DAILY SCHEDULE OF ACTIVITIES

47TH GENERAL ASSEMBLY
Buenos Aires, Argentina
April 22-25, 2013

DAILY SCHEDULE OF ACTIVITIES

MAIN TOPIC: **"INTERNATIONAL TAXATION ASPECTS THAT AFFECT MANAGEMENT OF THE TAX ADMINISTRATIONS"**

Monday, April 22

09:00 - 09:40 Inaugural Ceremony
- Statement by the CIAT Executive Secretary
- Statement by the Executive Council President
- Welcome Statement by Mr. Ricardo Echegaray, Federal Administrator of Public Revenues, AFIP, Argentina

09:40 - 10:10 Conference Opening Presentation: Prof. Heleno Taveira Torres

10:10 - 10:40 Official photograph, coffee and integration

TOPIC 1: **DOUBLE TAXATION, INTERNATIONAL TAX EVASION AND TREATIES FOR THE AVOIDANCE OF DOUBLE TAXATION**

Moderator: Julio Pereira, Director; Internal Revenue Service, Chile

10:40 - 11:10 **Speaker:** Guillermo Michel, Deputy General Director, Institutional Technical Coordination, Federal Administration of Public Revenues, Argentina (30´)

11:10 - 11:30 **Speaker:** Lionel Testevuide, Deputy Director of Large Taxpayers, General Directorate of Public Finances, France (20´)

11:30 - 11:45 **Commentator:** Márcio Ferreira Verdi, Executive Secretary, CIAT (15´)

11:45 - 12:00 Discussion (15´)

Subtopic 1.1: Domestic regulations to prevent international tax evasion

Moderator: John Njiraini, Commissioner General, Kenya Revenue Authority.

12:00 - 12:20 **Speaker:** Rosario Massino, Head of the International Cooperation Office, Finance Guard, Italy (20´)

12:20 - 12:40 **Speaker:** Beatriz Gloria Miguel, General Director, State Agency of Tax Administration, Spain (20´)

12:40 - 12:55 Discussion (15´)

12:55 - 02:00 Lunch

Subtopic 1.2: Effective implementation of anti-abuse provisions in Tax Treaties for the Avoidance of Double Taxation

Moderator: Gilles Berteau, Executive Secretary, CREDAF

02:00 - 02:20 **Speaker:** Grace Pérez Navarro, Deputy Director, Centre for Tax Policy &, OECD (20´)

02:20 - 02:40 **Speaker:** Carlos Alberto Barreto, Secretary of Federal Revenues, Brazil (20´)

02:40 - 03:00 **Speaker:** Sudha Sharma, Member / Special Secretary to Government of India (20´)

03:00 - 03:20 Discussion (20´)

03:20 - 03:40 Coffee & integration

Subtopic 1.3: Assistance in Collection of Taxes Articles in Tax Treaties for the Avoidance of Double Taxation

Moderator: Katherine Baer, Division Chief of Revenue, IMF

03:40 - 04:0	**Speaker:**	Adrián Guarneros, General Planning Manager, Tax Administration Service, Mexico (20´)
04:00 - 04:15	Discussion (15´)	

Panel Discussion – Effective Management Tools for Improving Performance

	Moderator:	Socorro Velazquez, Director, Planning and Institutional Development, CIAT
04:15 - 4:35	**Speaker:**	Miguel Pecho, Director, Tax Studies and Research CIAT (20´)
04:35 - 05:00	**Speaker:**	Arturo Herrera, Sector Manager, World Bank (25´)
05:00 - 05:45	Panel Discussion Panel members: Speakers, IOTA, Audience	

Tuesday, October 16

TOPIC 2: CONTROL OF TRANSFER PRICING

	Moderator:	José Antonio de Azevedo Pereira, General Director, General Directorate of Taxes, Portugal
09:00 - 09:20	**Speaker:**	Wang Wenqin, Deputy Director of the Tax Department, Taxation Department, People’s Republic of China (20´)
09:20 - 09:40	**Speaker:**	Gonzalo Arias, Director, Cooperation and International Taxation, CIAT (20´)
09:40 - 09:50	**Commentator:**	José Daniel Acevedo, Acting Intendant of Examination, Superintendency of Tax Administration, Guatemala (15´)
09:50 - 10:10	Discussion (15´)	

Subtopic 2.1: **Specific methods for the control of transfer pricing**

Moderator: Carlos Carrasco, General Director, Internal Revenue Service, Ecuador

10:10 - 10:30 **Speaker:** Horacio Curien, Deputy General Director, Deputy General Directorate of Examination, Federal Administration of Public Revenues, Argentina (20´)

10:30 - 10:50 **Speaker:** Carlos Alberto Barreto, Secretary of the Federal Revenues, Brazil (20´)

10:50 - 11:05 Discussion (15´)

11:05 - 11:25 Coffee & integration

Subtopic 2.2: **Commercial Sectors of Interest (case studies)**

Moderator: Víctor Manuel Gómez De La Fuente, General Director State Undersecretariat of Taxation,Paraguay

11:25 - 11:45 **Speaker:** Tania Quispe, National Tax Superintendent, National Superintendency of Customs and Tax Administration, Peru (20´)

11:45 - 12:05 **Speaker:** María Eugenia Torres, Sectional Tax Director, Colombia (20´)

12:05 - 12:25 **Speaker:** Sergio Mujica, Deputy Executive Secretary, WCO (20´)

12:25 - 12:40 Discussion (15´)

12:40 - 01:40 Lunch

Subtopic 2.3: **Advance Pricing Agreements (APAs), Bilateral Advance Pricing Agreement, Multilateral Advance Pricing Agreement**

Moderator: María Luisa Carbonell, Director of International Affairs, Federal Administration of Public Revenues, Argentina

01:40 - 02:00 **Speaker:** Esther Hernández, General Directorate of Internal Taxes, Dominican Republic (20´)

02:00 - 02:20 **Speaker:** Pablo Ferreri, General Director of Revenue, Uruguay (20´)

02:20 - 02:40 **Speaker:** Aristóteles Núñez, Head of the Tax Administration Service, Mexico (20´)

02:40 - 02:55 Discussion (15´)

03:00 - 06:00 Administrative Session (CIAT member countries)

Wednesday, April 24

TOPIC 3: **EXCHANGE OF INFORMATION AND MUTUAL ADMINISTRATIVE ASSISTANCE BETWEEN TAX ADMINISTRATIONS**

Moderator: Khurshid Sattaur, Commissioner General, Guyana Revenue Authority.

09:00 - 09:30 **Speaker:** Horacio Curien, Deputy General Director,Deputy General Directorate of Examination, Federal Administration of Public Revenues, Argentina (30´)

09:30 - 09:50 **Commentator:** Bermuda (20´)

09:50 - 10:10 Discussion (20´)

10:10 - 10:40 Coffee & integration (30´)

Subtopic 3.1: Information exchange

Moderator: Carlos Six, General Manager of Tax Administration, Belgium

10:40 - 11:10 **Speaker:** Douglas O'Donnell, Assistant Deputy Commissioner Large Business & International, USA / FATCA (30´)

11:10 - 11:40 **Speaker:** Donal Godfrey, Deputy Head, Global Forum on Transparency and EOI (30´)

11:40 - 12:10 Discussion (30´)

12:10 - 02:00 Lunch

Subtopic 3.2: Examinations and collection abroad

Moderator: Cornelis Van Dijk, Director of Taxes and Customs Directorate of Taxes, Finances, Suriname

02:00 - 02:20 **Speaker:** Marian Bette, Senior Policy Advisor, International Affairs, Netherlands Tax and Customs Organization, The Netherlands (20´)

02:20 - 02:40 **Speaker:** Gunilla Pahlsson Bluhm, International Co- ordinator, Swedish Tax Agency (20´)

02:40 - 03:00 **Speaker:** Brian McCauley, Assistant Commissioner, Legislative Policy and Regulatory Affairs Branch, Canada Revenue Agency (20´)

03:00 - 03:20 Discussion (20´)

03:20 - 03:50 Coffee & integration (30´)

03:50 - 05:30 **Open discussion panel on international taxation**

Countries: Argentina, Brazil, USA, Barbados, Italy, Portugal

Moderator: World Bank-IFC – Rajul Awasthi

Thursday, April 25

Subtopic 3.3: Effective implementation of information exchange and international taxation units

Moderator: Socorro Velazquez, Director, Planning and Institutional Development, CIAT

09:00 - 09:30 **Speaker:** Jenny Patricia Jimenez, Director of International Taxation and Tax Technique, General Directorate of Taxation, Costa Rica (30´)

09:30 - 10:00 **Speaker:** Gonzalo Arias, Director, Cooperation and International Taxation, CIAT (30´)

10:00 - 10:20 **Commentator:** Alberto Barreix, Regional Economist, Inter-American Development Bank, IDB (20´)

10:20 - 10:40 Discussion (20´)

10:40 - 11:10 Coffee & integration

Closing Ceremony

11:10 - 11:20 Event evaluation (10´)

11:20 - 11:50 **Final Assembly theme considerations – Carlos Folco, Federal Fiscal Judge, Argentina (30´)**

11:50 - 12:10 **Other Activities**

- Innovation Award Presentations
- Signing of Agreements
- Invitation to next Technical Conference and General Assembly
- Words of appreciation to AFIP

12:10 - 12:25 **Closing words by the Executive Council President (15´)**

12:25 - 12:40 Lunch

Free afternoon for social activities and integration

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Buenos Aires, Argentina
April 22 to 25, 2013

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