

# **Mutual Agreement Procedure (MAP) and Advance Pricing Arrangement (APA): Implementation and Application**

## 1. Mutual Agreement Procedure

When fiscal dispute inevitably occurs, a court is certainly the traditional arena for solution. However, is this method always the best solution corresponding to our needs? The answer seems to be negative. Alternative dispute resolutions in tax conflicts have been continuously developing throughout time. Not only is substance taken to heart in public law theory in order to clarify its legal feasibility, but the form is also examined through real practices as a means to test its compatibility with the socioeconomic environment. This way of resolution accepted by legal theoreticians and practitioners is actually mastered by several administrative organisms.

According to OECD guideline, Mutual Agreement Procedure (MAP) in tax conventions allows designated representatives (“competent authorities”) from the governments of Contracting States to interact with the intent to resolve international tax disputes. These disputes involve cases of double taxation (juridical and economic) as well as inconsistencies in the interpretation and application of a convention. However, by virtue of article 3 of OECD Model Tax Convention, it implies that the term of competent authorities depends on Contracting States. Competent authorities are possibly the highest hierarchies, delegates or other key persons of Ministry of Finance. This flexibility permits each State to design independently the competent authorities being capable to find the most suitable solution for the parties as well as the best answer for technical issues.

Designation of competent authority can be different corresponding to the domestic law of some Contracting States. The signing authority in an

international convention is able to be transferred to other public agencies namely Minister of Foreign Affairs, or even Tribunal<sup>1</sup>. In all hypotheses, the competent authorities shall have rights to make decision and sign agreement. Also, the most important principle of competent authorities is independence which means the authorities should not be involved in issues already treated before MAP.

The competent authorities can be expert in varied domains:

1. Juridical domain - some legal issues have to be examined by skilled lawyer being able to master interpretation and application of Double tax agreement, including lack of provision concerned, even inconsistency of legal provision. By this reason, a good knowledge of national and international law, jurisprudence as well as administrative practice.

2. Economic or Financial Domain - the knowledge of market mechanism, even international commerce and industrial experience will mostly help to settle the tax dispute.

3. Accounting expert - accounting skill will facilitate balance sheet analysis and transactional control especially Transfer Pricing and Advance Pricing Arrangements issues.

Cases submitted to MAP are usually difficult either technical issues particularly some terms of DTA<sup>2</sup> or application issues. However, in principle, more the monetary value of conflict, more complicated the case will be. Compared with article 3 of Convention [90/436/EEC](#) on the elimination of double taxation in connection with the adjustment of profits of associated enterprises 1990 (the EU Arbitration Convention 1990), the competent authority can be separated into 2 types : Minister of Finance or Economic Affairs or an

---

<sup>1</sup> Comité des affaires fiscales OCDE, **Modèle de Convention fiscale concernant le revenu et la fortune**, Paris, publication OCDE, 2003, p. 322

<sup>2</sup> In case of Thailand e.g. Royalty, Pension, APA, PE, Resident, etc.

authorized representative and Commissioner of Inland Revenue or an authorized representative<sup>3</sup>.

**Table : Competent authority of member countries of the EU Arbitration Convention 1990 shall mean :**

| <b>Countries</b>                       | <b>Competent authority</b>   |
|--|--|
| <b>Belgium</b>                         | De Minister van Financiën or an authorized representative          |
| <b>Denmark</b>                         | Skatteministeren or an authorized representative                   |
| <b>The Federal Republic of Germany</b> | Der Bundesminister der Finanzen or an authorized representative    |
| <b>Greece</b>                          | O Ypoyrgos ton Oikonomikon or an authorized representative         |
| <b>Spain</b>                           | El Ministro de Economía y Hacienda or an authorized representative |
| <b>France</b>                          | Le Ministre chargé du budget or an authorized representative       |
| <b>Ireland</b>                         | The Revenue Commissioners or an authorized representative          |
| <b>Italy</b>                           | Il Ministro delle Finanze or an authorized representative          |
| <b>Luxembourg</b>                      | Le Ministre des Finances or an authorized representative           |
| <b>The Netherlands</b>                 | De Minister van Financiën or an authorized representative          |

---

<sup>3</sup> In general, the competent authority of civil law countries like France, Germany, Belgium, Denmark, Greece, Spain, Italy, Luxembourg, The Netherlands and Portugal is Minister of Finance or Economic Affairs or an authorized representative while in common law countries like England and Ireland, competent authority is Commissioner of Inland Revenue or an authorized representative

| Countries                 | Competent authority   |
|---------------------------|---|
| <b>Portugal</b>           | O Ministro das Finanças or an authorized representative             |
| <b>The United Kingdom</b> | The Commissioners of Inland Revenue or an authorized representative |

### **1.1 Recent Development on MAP: DTA**

Thailand first concluded the Double Tax Agreement (DTA) with Sweden in 1963. The Thai DTA network continues to be expanded and updated. So far Thailand has concluded DTAs with 55 countries (as of August 2011) with 10 countries listed for non entered into force status.

According to competent authority for MAP, Thailand designates the Minister of Finance or an authorized representative as competent authority. In practice, the Director- General of the Revenue Department or a delegate will act as competent authority.

#### **1.1.1 Tax position on Royalties**

Withholding Tax Rates for Royalties, under Thailand's DTAs if the recipient of royalties does not have a P.E. or fixed base in the source country, are between 5 - 25 percent.

#### **1.1.2 Tax position on Interest**

Withholding Tax Rates for Interest, under Thailand's DTAs if the recipient of interest does not have a P.E. or fixed base in the source country, are between 3 - 25 percent.

## **1.2 Regulations concerning MAP : National Law**

### **Constitution of The Kingdom of Thailand B.E. 2550 (2007)**

**Section 190** The King has the prerogative to conclude a peace treaty, armistice and other treaties with other countries or international organisations.

A treaty which provides for a change in the Thai territories or the Thai external territories that Thailand has sovereign right or jurisdiction over such territories under any treaty or an international law or requires the enactment of an Act for its implementation or affects immensely to economic or social security of the country or results in the binding of trade, investment budget of the country significantly must be approved by the National Assembly. In such case, the National Assembly must complete its consideration within sixty days as from the date of receipt of such matter.

Before the conclusion of a treaty with other countries or international organisations under paragraph two, the Council of Ministers must provide information thereon to the public, conduct public consultation and state information in relevant thereto to the National Assembly. In such case, the Council of Ministers must submit negotiation framework to the National Assembly for approval.

Upon giving signature to the treaty under paragraph two, the Council of Ministers shall, prior to give consent to be bound, facilitate the public to get access to the details of such treaty. In the case where the application of such treaty has affected the public or small and medium entrepreneurs, the Council of Ministers must revise or render remedy to such effects rapidly, expediently and fairly.

There shall be a law determining measure and procedure for the conclusion of a treaty having immense effects to economic or social security of

the country or resulting in the binding of trade or investment of the country significantly and the revision or rendering of remedy to the effects of such treaty with due regard to the fairness among the beneficiaries, the affected persons and the general public.

A matter arising from the provisions of paragraph two falls within the jurisdiction of the Constitutional Court and the provisions of section 154 (1) shall apply mutatis mutandis to the referring of the matter to the Constitutional Court.

### **1.3 Capacity building on MAP: Leaning from the negative**

#### **1.3.1 MAP: Effectiveness is doubtful**

In case C-311/08 of Court of Justice of the European Union, Mme KOKOTT, the General Attorney, mentioned that (...) the ARD occasionally makes additional charges to administrator on one hand. On the other hand, the taxpayer itself has to pay the debt without exception during the MAP procedure and this situation may lead to double tax payment. Due to the arbitration, the procedure could be extended for many years if the period of time issued in DTA was entirely used.

A question posed again when the collaboration is held between competent authority, how to be ensure that the procedure will be conducted in the same direction. Each member country has different juridical background and administrative norms especially it seem to be difficult to settle the dispute with the countries where the tax sovereignty shall be strictly respected.

Concerning the study, the interpretation of domestic law in some countries takes side with government. That is why the local remedy fails. Also, the domestic law probably reduces submission period prescribed on article 25 of the DTA. By this reason, if the taxpayer neglects this period, the reclamations will be

rejected by domestic authority and a corresponding adjustment of benefit in other Contracting State will not be held.

### **1.3.2 MAP and negotiation power**

In negotiation process, the bargaining power between Contracting States is not equal. The developed countries often have certain advantages over developing countries or third world countries. So that, filing case to the local court is not the worst alternative in this situation.

Lack of juridical and administrative protection is the critical problem of MAP which leads to the decline of trust and confidence vis à vis the taxpayer e.g. MAP does not offer participation rights to the taxpayer due to its change to the international affair that why the taxpayer sometime refuses to proceed MAP.

Also, lack of Convention on the recognition and enforcement of judgments or administrative decision in fiscal matter could lead to complicate the taxpayer's situation. It will be impossible to proceed MAP if MAP is unrecognized and inaccessible for the other Contracting State. MAP just works well in theory, however, in practice MAP cannot guarantee any tax relief especially in cases of ;

1. Being interrupted by prescription of one Contracting State.
2. Result of MAP is rejected by other party
  - 2.1 Lack of domestic law enforcement
  - 2.2 Violation of national legislation
3. For sensitive issues like PE, Royalty, Resident, the authorities hardly find a proper solution caused by difference of interpretation, including administrative norms
4. Lack of necessary information and collaboration of taxpayer
5. Belated submission of taxpayer's reclamation
6. Impossibility of MAP process in case of non Contracting State, etc.

### **1.3.3 MAP and Corresponding Adjustment**

The Thai Revenue Department has begun its first transfer pricing MAP discussions with the National Tax Agency (NTA) of Japan in February 2011. And up to 2012 the Revenue Department has received 5 MAP cases which are in the process of negotiation (4 with Japan, 1 with U.S.A.).

Although the Tax treaty between Thailand and Japan provides for MAP corresponding adjustment, the Revenue Department has its limitation presented by the domestic tax provision which do not cater for corresponding adjustment. Hence, the Thai Revenue Department is on the process of amending the law to resolve such problem.

### **1.4 MAP: Conclusion**

In dialogue, other issues could be simultaneously raised. Not only the main issues like interpretation, application, inconsistencies of legal provision, but similar issues have to be dealt also: penal liabilities, interest, payment order, tax elimination or relief method, etc. Moreover, the Contracting states shall focus on main factors leading MAP become more effective namely competent authority, national legislation and administrative practice which are the keys to bring success to MAP finally.



## 2. Advance Pricing Arrangement

Generally, transfer pricing is related to the activities or transactions between the members of multinational companies. Whether they intend to transfer profit within the group, the related tax authorities still pay their attention that the price transferred is according to the arm's length principle or not. Therefore, the transfer pricing regulations are established in many countries and, also, in Thailand. For transfer pricing consideration, the Revenue Department of Thailand has issued Departmental Instruction No. 113/2545 by adopting the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

Transfer pricing audit is the mechanism to prevent the tax evasion but it may cause the double taxation. To cope with the double taxation, advance pricing agreement is introduced for transfer pricing disputes between taxpayers and tax authorities.

### **2.1 Tax Policy and Legislation on Transfer Pricing**

Over the past two decades Transfer Pricing cases in Thailand has increased considerably in both domestic and international transactions. To curb with these activities, the Revenue Department released Departmental Instructions concerning transfer pricing guideline known as Departmental Instructions No. 113 in 2002.

This guideline provides information that is applicable to, documentation required, how to derive market price and methodologies used to determine market price of the transactions by adopting arm's length principle of the OECD guidelines. The following methods are acceptable by the Revenue Department; comparable uncontrolled price, resale price method, cost plus method, transactional net margin method, and profit split method. The comparable uncontrolled price method, the resale price method, or the cost plus method are preferred over the transactional net margin method and the profit

split method. However there is no hierarchy over these three methods. In event where the three traditional transaction methods were found to be inappropriate, other methods may be applied. Other methods in this case refer to methods that are internationally accepted and are commercially appropriate to the facts and circumstances in respect of the transfer of property, provision of service or lending of fund. The Departmental Instruction is divided into the following sections:

1. Criteria for the Calculation of Net Profits of Juristic Partnerships or Corporations for Income Tax Purposes
2. Assessment of Revenue and Expenses Based on the Market Price
3. Methodologies in Determining the Market Price
4. Documentation that should be prepared
5. Advance Pricing Arrangements (APAs)

Not only the Departmental Instruction No. 113 was adopted for transfer pricing cases, there are other general provisions under the Revenue Code designed to prevent tax avoidance arising from transactions between related parties conducted at lower than market price. In order to prevent the evasion of taxation caused by manipulated transfer pricing within the MNEs, tax authorities can price goods and services by applying the provisions of Sections under the Revenue Code as follows:

- Sec. 65 bis (4) In the case of transfer of assets, provision of service or lending of money, fee or interest without remuneration that is lower than the market price without reasonable cause, an assessment official shall have the power to assess such remuneration, fee or interest in accordance with the market price on the date of transfer, provision or lending.
- Sec. 65 bis (7) In calculating the cost of goods imported from abroad, the assessment official shall have the power to assess by comparing with the cost of the same type and kind of goods imported into other countries.

- Sec. 65 ter :disallowed expenditures
  - (13) Expense which is not for the purpose of making profits or for the business
  - (14) Expense which is not for the purpose of business in Thailand
  - (15) Cost of purchase of asset and expense related to the purchase or sale of asset, but only the amount in excess of normal cost and expense without reasonable cause.

Moreover, Double Tax Agreements between Thailand and other countries, as well as Standard Accounting No. 37 and 47 are applied.

## **2.2 Tax position on APA**

Whereby if a taxpayer considers that the tax assessment of one or both of the contracting states results or will result in taxpayer being taxed that is not in accordance with the provisions of the tax conventions, the taxpayer may present the case to the competent authority of the contracting state. The competent authorities shall endeavour to resolve any difficulties or doubts arising by mutual agreement. According to the conventions, the Advance Pricing Arrangement provision was put into the Departmental Instruction No.113/2002.

The rule of "Advance Pricing Arrangement" or APA is available for taxpayers. APA is an agreement between taxpayers and the Revenue Department of the pricing methodologies, terms, and others conditions (see Thai APA guidance) that would be used in future transactions between related parties. Thai position on APA today is to accept bilateral APA.

Due to related company wishing to submit APA, a company or juristic partnership incorporated under Thai law that enters into related party transactions with affiliates who are residents of Thailand's tax treaty partners may apply for APA. However, in principle, a Thai branch (i.e. PE) of a foreign company is unqualified to request APA.

To comply with the double taxation conventions, Thailand started its first APA negotiation in 2005 with Japan and the case was concluded in August 2008. Up to 2012, 17 APA applications have been submitted to the Revenue Department and five of them are on the negotiation process. Our negotiating partners include: 12 cases with Japan, 2 cases with Singapore, 1 with U.S.A., 1 with Switzerland and 1 with South Korea. In order to enter into an APA program, company must submit its application to the Director- General within the first year of APA and pre-filing meeting within 6 months prior to the last day of the first year of APA.

### **2.3 APA : Domestic regulation**

While we have learnt that APA is the process to resolve the double taxation between related companies, some issues have been realized. After the APA negotiation is finished and the agreement is concluded, the results will consequently be applied to the calculation of profit between covered parties in the APA. Unlike other countries, Thailand has provided certain businesses a tax privilege, therefore, the question is how the APA will be implemented.

Most foreign subsidiaries established in Thailand have obtained the tax exemption at least eight years from the Board of Investment (BOI). After their tax privilege is expired, they can request for extension if they invest in a new project. Therefore, some taxpayers may have both businesses which are under BOI and are not under BOI (NON BOI). For tax return filing, they have to calculate the taxable income separately according to their businesses.

In case there is the compensating adjustment resulted from APA, if the covered transaction is either under BOI or NONBOI business, the adjustment will be made in that business simply. However, if the APA covered transactions are under both businesses, the question is how to allocate the adjusted profit to both businesses. Assuming the natures of BOI and NON BOI

businesses are the same but their operating margins are different. For example, BOI earns 20 percent profit whereby NON BOI earns 2 percent profit and the overall profit is 5 percent. If the target profit rate is 10 percent, two methods of adjustment are considered. Firstly, the adjustment is made to each business with the proportion of the business income. Secondly, the adjustment is made only to NON BOI business.

In case the first method is selected, each business's profit may be not in accordance with the ALP's profit that is 5 percent. BOI's profit is higher than ALP's profit while NON BOI's is lower. Therefore, the adjustment will be unfair to the country, if APA is employed for tax planning within the multinational companies.

## BIBLIOGRAPHY

Comité des affaires fiscales OCDE, **Modèle de Convention fiscale concernant le revenu et la fortune**, Paris, publication OCDE, 2003, 2008, 2010

Wuttipong SIRICHANTRANON, **Les modes alternatifs de règlement des litiges fiscaux**, Thèse de l'Université Paris II Panthéon –Assas, Paris, 2010

Constitution of the Kingdom of Thailand 2007

The Revenue Code B.E. 2481 (updated B.E. 2554)

Departmental Instruction No. Paw 113/2545

Guidelines on the Determination of market price

Guidance on APA Process

The Revenue Department of Thailand's website: [www.rd.go.th](http://www.rd.go.th) (visited September 2012)