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OECD releases Brazil Stage 1 peer review report on implementation of BEPS Action 14 minimum standard

Executive summary

On 28 November 2019, the Organisation for Economic Co-operation and Development (OECD) released the seventh batch of peer review reports relating to the implementation of the Base Erosion and Profit Shifting (BEPS) minimum standard under Action 14 on improving tax dispute resolution mechanisms.[1] Brazil was among the assessed jurisdictions in the seventh batch.[2]

Overall the report concludes that Brazil meets most of the elements of the Action 14 minimum standard. In the next stage of the peer review process, Brazil's efforts to address any shortcomings identified in its Stage 1 peer review report will be monitored.

Detailed discussion

Background

In October 2016, the OECD released the peer review documents (i.e., the Terms of Reference and Assessment Methodology) on Action 14 on *Making Dispute Resolution Mechanisms More Effective*.[3] The Terms of Reference translated the Action 14 minimum standard into 21 elements and the best practices into 12 items. The Assessment Methodology provided procedures for undertaking a peer review and monitoring in two stages. In Stage 1, a review is conducted

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of how a member of the Inclusive Framework (IF) on BEPS implements the minimum standard based on its legal framework for Mutual Agreement Procedure (MAP) and how it applies the framework in practice. In Stage 2, a review is conducted of the measures the member of the IF on BEPS takes to address any shortcomings identified in Stage 1 of the peer review.

Both of these stages are desk-based and are coordinated by the Secretariat of the Forum on Tax Administration's (FTA) MAP Forum.[4] In summary, Stage 1 consists of three steps or phases:

(i) Obtaining inputs for the Stage 1 peer review

(ii) Drafting and approval of a Stage 1 peer review report

(iii) Publication of Stage 1 peer review reports

Input is provided through questionnaires completed by the assessed jurisdiction, peers (i.e., other members of the FTA MAP Forum) and taxpayers. Once the input has been gathered, the Secretariat prepares a draft Stage 1 peer review report of the assessed jurisdiction and sends it to the assessed jurisdiction for its written comments on the draft report. When a peer review report is finalized, it is sent for approval of the FTA MAP Forum and later to the OECD Committee on Fiscal Affairs' to adopt the report for publication.

Minimum standard peer review reports

The report is divided into four parts, namely:

(i) Preventing disputes

(ii) Availability and access to MAP

(iii) Resolution of MAP cases

(iv) Implementation of MAP agreements

Each part addresses a different component of the minimum standard.

The report includes 22 recommendations relating to the minimum standard. In general, the performance of Brazil with regard to MAP has proven to be satisfactory in their respective reports. Overall, Brazil meets most of the elements of the Action 14 minimum standard.

Preventing disputes

- Article 25(3), first sentence, of the OECD Model Tax Convention (OECD MTC) in tax treaties:
  - Brazil has a tax treaty network of 35 tax treaties, of which 33 contain a provision equivalent to Article 25(3) first sentence of OECD MTC requiring their competent authority to endeavor to resolve by mutual agreement any difficulties or doubt arising from the interpretation or application of the tax treaty.
  - In the two remaining treaties, the sentence only relates to difficulties or doubts arising from the *application* of the treaty, but not related to the *interpretation* of the treaty. Brazil has reported that its competent authority would be allowed to enter into a MAP with respect to the *interpretation* of tax treaty for those cases.
  - Also, for the two treaties that do not contain the provision equivalent to Article 25(3), first sentence, of the OECD MTC, Brazil reported it will strive to update them via bilateral negotiations. Brazil also reported that it intends to include the required provision in all future tax treaties. One relevant peer reported that it received a draft protocol from Brazil which contains a new provision regarding the MAP.
- Brazil's current legal framework does not provide for entering into Advanced Pricing Agreements (APAs).

Availability and access to MAP

- In all of Brazil's tax treaties, taxpayers can file a MAP request irrespective of domestic remedies.
- With respect to Article 25(1), first sentence, of the OECD MTC:
  - Of Brazil's 35 tax treaties, 8 contain a provision equivalent to Article 25(1), first sentence, of the OECD MTC, which allows taxpayers to submit a MAP request to the competent authority of their state of residence when it is considered that the actions of one or both of the treaty partners result or will result for the taxpayer in taxation not in accordance with the provisions of the tax treaty. In addition, two of Brazil's tax treaties contain a provision equivalent to the Article 25(1) as changed by the *Making Dispute Resolution Mechanisms More Effective*, first sentence, of the OECD MTC.
  - The other 25 tax treaties are considered not to have the full equivalent of Article 25(1), first sentence, of the OECD MTC, as it read prior to the adoption of the Action 14 final report, whereby taxpayers can only submit a MAP request to the competent authority of the Contracting State of which they are resident.

- One of the tax treaties does not contain such provision and it is recommended by the OECD that Brazil should follow up on its request for the inclusion of that provision via bilateral negotiation.

- With respect to Article 25(1), second sentence, of the OECD MTC:
  - Six of Brazil's tax treaties contain a provision equivalent to Article 25(1), second sentence, of the OECD MTC allowing taxpayers to submit a MAP request within a period of no less than three years from the fist notification of the action resulting in taxation not in accordance with the provisions of the particular tax treaty.
  - Twenty tax treaties do not contain a filling period for MAP requests and for the four treaties that refer to the domestic time limits as a filing period, Brazil reported that the filling period would be five years, starting as from the first notification to the taxpayer of the actions taken by one or both of the Contracting States resulting in taxation not in accordance with the tax treaty.
  - Seven of the tax treaties do not contain such provision, as the timeline to file a MAP request is shorter than three years. It is recommended by the OECD that Brazil should follow up on its requests for the inclusion of the required provision via bilateral negotiations.
- Input of peers
  - Three peers provided input relating to similar experiences of cases where a MAP case could not be initiated further to the expiration of Brazil's domestic time limits. All three MAP cases were closed without any ability to find a solution for the relevant cases.
  - Brazil responded that the cases concerned are "pre-2016" cases and, at that time, it was not possible to reach an ideal solution. Currently, the Brazilian competent authority is communicating with the competent authority of the other Contracting State about the need to file a return request within the domestic statute of limitations to ensure the effective implementation of a refund after reaching the MAP agreement.
- The OECD recommended that Brazil document its notification process as soon as possible and provide information on how that process should be applied in practice.
- Brazil intends to update the tax treaties that do not contain the equivalent of Article 25(1) of the OECD MTC via bilateral negotiations and to include that provision in all future tax treaties.
- MAP in transfer pricing cases:
  - Brazilian tax treaties do not contain a provision equivalent to Article 9(2) of the OECD MTC, by requiring their state to make a correlative adjustment in the case of a transfer pricing adjustment imposed by the treaty partner.
  - Access to MAP should be available for transfer pricing cases regardless of whether the equivalent of Article 9(2) is contained in Brazil's tax treaties and irrespective of its domestic legislation.
  - Brazil's MAP guidance refers to transfer pricing cases as typical cases for MAP and the relevant MAP guidance also recommends that the other associated company submit a MAP request in the other country of residence.
  - Since January 2016, Brazil has received several MAP requests from taxpayers relating to transfer pricing cases.
- MAP in relation to the application of anti-abuse provisions are not included in the Brazilian tax treaties.
- Audit settlements are not possible in accordance with domestic law.
- Article 25(3), second sentence, of the OECD MTC:
  - Eighteen of the Brazilian tax treaties contain a provision of equivalent to Article 25(3), second sentence, of the OECD MTC allowing their competent authorities to consult together for the elimination of double taxation.
  - Brazil intends to update the tax treaties with an equivalent provision via bilateral negotiations.

Resolution of MAP cases

- Article 25(2), first sentence, of the OECD MTC:
  - All of Brazil's 35 tax treaties contain a provision equivalent to Article 25(2), first sentence, of the OECD MTC requiring its competent authority to endeavor, when considered as justified and no unilateral solution is possible, to resolve by mutual agreement with the competent authority of the other treaty partner the MAP case with a view to the avoidance of the double-taxation.
- Brazil's MAP caseload increased by 125% from January 2016 to December 2018, which may indicate that the Brazilian competent authority is not adequately resourced.
  - On January 2016, Brazil had 12 pending MAP cases: 5 related to attribution/allocation cases, and 7 related to other MAP cases.

- By the end of December 2018, Brazil had 27 MAP cases in its inventory: 15 related to attribution/allocation cases, and 12 related to other MAP cases.
- From 2016 to 2018, Brazil closed a total of six MAP cases. Two of those MAP cases were closed through an agreement that fully eliminated double taxation.
- The average time needed to close a MAP case was 26.43 months, which represents two cases of attribution/allocation cases in a period of 23.28 months, and six other cases in a period of 28.01 months.
- The MAP cases can be divided among "pre-2016 cases" and "post-2015 cases":
  - For the pre-2016, Brazil reported that on average it needed 34.16 months to close attribution/allocation cases and 44.34 months to close other cases.
  - For the post-2015 cases, Brazil reported on average it needed 12.40 months to close attribution/allocation cases and 11.67 months to close other cases.
- MAP arbitration is not a mechanism currently available within any of Brazil's tax treaties.

Implementation of MAP agreements

- Brazil reported that, given its domestic legislation, implementation of MAP agreements can only be made within its domestic statute of limitations, meaning five years after the date of payment of the relevant taxes. It is applicable both when the MAP request was submitted to the Brazilian competent authority and when it was submitted to the competent authority of the treaty partner. Hence, there would be a risk that not all MAP agreements would be implemented due to the five-year time limitation in Brazil's domestic law. The OECD has recommended that Brazil continue to notify the treaty partner without delay, as they recently started to do, and that Brazil follow its stated intention and introduce a tracking mechanism to ensure that all MAP agreements are implemented in the future.
- Brazil reported it has reached one MAP agreement since January 2016 that needed to be implemented in Brazil, and that it was implemented.
- Brazil also reported that to mitigate the risk of non-implementation of MAP agreements associated with the expiration of the statute of limitations, its competent authority now informs its treaty partner of the need to submit a refund request and does so immediately after being notified of the existence of a filed MAP request in the other jurisdiction.
- Taxpayers are invited to provide their acceptance of the solution found within 30 days after being notified of the outcome of their MAP cases.

Next steps

Brazil is already working to address deficiencies identified in its peer review and will now move on to Stage 2 of the process, where Brazil's efforts to address any shortcomings identified in its Stage 1 peer review report will be monitored. Under the peer review program methodology, Brazil shall submit an update report to the Forum on Tax Administration's MAP Forum within one year of the OECD Committee on Fiscal Affairs' adoption of the Stage 1 peer review report.

Implications

In a post-BEPS world, where multinational enterprises (MNEs) face tremendous pressures and scrutiny from tax authorities, the release of Brazil's peer review report represents the continued recognition and importance of the need to achieve tax certainty for cross-border transactions for MNEs. While increased scrutiny is expected to significantly increase the risk of double taxation, the fact that tax authorities may be subject to review by their peers should be seen by MNEs as a positive step to best ensure access to an effective and timely mutual agreement process.

Furthermore, the peer review for Brazil provides insights to taxpayers on the availability and efficacy of MAP. With additional countries continuing to be reviewed, the OECD has made it known that taxpayer input continues to be welcomed on an ongoing basis.

With stakeholder feedback in mind, businesses are encouraged to share their views with the OECD on the peer review for Brazil and any other jurisdictions, and to comment on whether the next iteration of the OECD's assessment of tax administration's MAP performance warrants greater feedback from taxpayers as the primary source. Feedback from the international tax community is the logical next step after peer review, which may help to further validate the current favorable result.

Endnotes

1. See EY Global Tax Alert, *OECD releases seventh batch of Stage 1 peer review reports on BEPS Action 14*, dated 3 December 2019.
2. https://read.oecd-ilibrary.org/taxation/making-dispute-resolution-more-effective-map-peer-review-report-brazil-stage-1_12acb5ea-en#page1.
3. See EY Global Tax Alert, *OECD releases BEPS Action 14 on More Effective Dispute Resolution Mechanisms, Peer Review*, dated 31 October 2016.
4. http://www.oecd.org/tax/forum-on-tax-administration/about/.

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