



**Ad hoc Group of Experts on International Cooperation  
in Tax Matters**

**Ninth meeting**

New York, 3–7 May 1999

**Draft report**

**Contents**

	<i>Paragraphs</i>	<i>Page</i>
I. Opening of the meeting .....	1–2	2
II. Election of officers .....	3	2
III. Adoption of the agenda .....	4	2
IV. Exchange of information .....	5–13	2
V. Transfer pricing .....	14–20	4

## I. Opening of the meeting

1. The ninth meeting of the Ad Hoc Group of Experts on International Cooperation in Tax Matters was opened on behalf of the Under-Secretary-General for Economic and Social Affairs, by the Director of the Division for Public Economics and Public Administration of the United Nations Secretariat. He noted that the contribution made by the focus group has facilitated the work of revision and update of the United Nations Model Double Taxation Convention between Developed and Developing Countries. Taxation is an important component of the process of economic development and is in the forefront of the social and economic agenda of the United Nations. In 2000, the General Assembly will take stock of the implementation of recommendations made at the World Summit for Social Development, when the recent advances in matters connected with international taxation and international cooperation in taxation policies to contain tax competition will be examined. He commended the work done by the focus group at two meetings, in New York in December 1998 and at Amsterdam in March 1999. He also referred to the implications of globalization for tax policy and the unfair tax competition to which it may lead. He made reference to Tobin's tax on foreign exchange transactions as a potent source of revenue, and remarked that the Group of Experts might wish to examine closely the implications of tax sparing for promoting the economic growth of developing and transitional economy countries.

2. The Secretary of the Group referred to the consensus arrived at by the focus group in connection with the amendment of articles and the modification of the commentaries on the United Nations Model Convention. He referred to the structural changes proposed in the form of bringing out loose-leaf editions of the United Nations Model Convention in the future for facilitating additions and deletions, as required. He mentioned some significant changes made to the text of articles 5, 9 and 14. He pointed out that agenda item 2, "Transfer pricing", creates an artificial basis for the determination of taxable profits resulting in distortions of market mechanisms. There is a need for the United Nations and other multilateral organisations, such as the Organisation for Economic Cooperation and Development (OECD), to adopt a consensual approach and provide guidelines and strategies for dealing with these practices. As regards agenda item 3, "Exchange of information", he observed that tax administrations can no longer rely only on information available within their national jurisdiction to combat tax evasion. In order to face the challenges posed by tax havens, it is necessary to facilitate access to tax information through bilateral tax treaties with provision for exchange of

information or separate international agreements on information exchanges.

## II. Election of officers

3. The Group elected Antonio Hugo Figueroa (Argentina) as Chairman, and Hillel Skurnik (Finland) as Rapporteur. Abdel Hamid Bouab served as Secretary, and was assisted by Suresh Shende (Assistant Secretary), and Paul McDaniels as resource person.

## III. Adoption of the agenda

4. The Group adopted the following agenda for the ninth meeting:

1. Revision and updating of the United Nations Model Double Taxation Convention between Developed and Developing Countries and the Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries.
2. Transfer pricing.
3. Exchange of information.
4. Other matters.
5. Arrangements for the tenth meeting.

## IV. Exchange of information

5. The subject of exchange of information was initiated with a presentation of papers on the subject by two participants. The first participant observed that exchange of information which has treaty implications is relevant to United Nations member countries in various dimensions. Studies on this subject have been done in economic, legal and anthropological contexts. Studies are under way in the state of California relating to a technology gap involving ownership structures and the means employed to avoiding reporting allocation of income appropriately. A new framework has been developed to utilize databases to disaggregate ownership for affixing income. Tax information exchange is a successful part of exchange of information. Tax costs are not a significant part of business equations when disparities are acknowledged. Technology has an important function in exchange of information and may provide practical solutions.

6. Another participant observed that article 26 of the United Nations Model Convention relating to exchange of information establishes a legal basis for access to information. Exchange of information is appropriate to deal with fiscal fraud. The United Nations Model Convention may intensify inter-administration cooperation among the signatories of conventions. First, the expansion of the international economy has resulted in the greater use of double taxation conventions, which have established and strengthened control mechanisms to ensure equitable tax payments by all taxpayers. This has also helped to limit the scope for treaty shopping. Second, new opportunities have been provided by harmful tax competition, and the situation is further complicated by a lack of political will. There are also limitations on exchange of information as a result of each country's perception of its fiscal sovereignty as well as a lack of mutual interest in disclosing tax information. The intentional refusal or lack of positive action to provide legal mechanisms to other States in exchange of information is not conducive to the channelling of international capital movements.

7. The representative of OECD reviewed that organization's recent efforts with respect to harmful tax competition, and stressed the role of effective exchange of information procedures in that context. Harmful tax competition is a global problem which requires multilateral cooperation. The OECD report is primarily directed to issues raised by the financial services sector since companies in these businesses can readily transfer profits to low tax jurisdictions without changing the location of their real activities. The OECD project will identify countries engaged in harmful tax competition, particularly those used for money-laundering purposes. But its primary emphasis is on securing cooperation so that tax havens can develop effective fiscal sovereignty systems that do not rely on bank secrecy practices with little or no taxation. It was emphasized that the OECD project is not intended to set minimum acceptable tax rates nor to bring about harmonization of taxes across countries. The factors employed by OECD to identify countries potentially engaged in harmful tax competition were reviewed, and it was emphasized that all factors — not just one — must be examined. The process and time-table for action by OECD countries to remove harmful tax regimes was reviewed. OECD also desires to solicit the views of non-member countries in the process.

8. One member from a developing country stated that the core of the problem is the lack of administrative and legal structures which will permit exchanges of information. He felt that it is time to implement the last sentence of article 26, paragraph 1, relating to the development of appropriate conditions, methods and techniques concerning matters for

exchange of information. He emphasized the need for a central organization to develop exchanges of information procedures, and desired that the limits in article 26, paragraph 2, be relaxed. Another member, however, cautioned against making any change in this provision since multinational corporations view the limits as important protection, especially as regards confidentiality.

9. Some members asserted that there were legitimate reasons for developing countries not to agree to full exchange of information treaty articles. Among other things, the language tends to assume the equality of resources of developing and developed countries, which is demonstrably not the case. It was observed that tax evasion is equally harmful to both developing and developed countries. Similarly, an OECD representative noted that tax havens are harmful to all countries. Another member further commented that the bank secrecy issue must be seen as a continuum. Every country has some bank secrecy rules. But countries cannot operate tax systems effectively without some access to bank records.

10. Several participants stressed the importance of utilizing new technologies to make the exchange of information process more effective. But one member from a developed country noted that tax officials in his country often do not even know that the process is available. A member from a developing country emphasized that OECD countries need to develop effective exchange of information techniques and then share those with developing countries.

11. A member from a developed country expressed the view that exchange of information articles in bilateral tax treaties do not function simply as anti-abuse rules; they are necessary to implement the application of a country's tax system to cross-border transactions. Moreover, he stated that exchange of information articles are not a solution to problems caused by tax havens, especially since most tax haven countries do not enter into tax treaties.

12. One observer raised the question whether the focus group had addressed the issue of tax collection in the context of exchange of information. A member stated that the focus group had discussed the issue in conjunction with its consideration of article 25. A representative of OECD noted that OECD is working to develop a provision in bilateral tax treaty providing assistance in matters of tax collection.

13. In conclusion, the process of globalization of the world economies has made the provisions relating to exchange of information more necessary than before. But there is a growing disparity between the ability of developed and developing countries to obtain and provide the required information to a treaty partner. The developed countries need

to provide information and assistance to developing countries to enable them to carry out exchange of information procedures at an acceptable cost. These procedures will also lead to effective control of harmful tax competition.

## V. Transfer pricing

14. The initial discussion revealed that a consideration of transfer pricing issues necessarily also involves, for developing countries, the provision of technical training for their tax administrators in transfer pricing methodologies and techniques, as well as the issue of improving tax collections from multinational companies, and for all countries the implementation of effective mutual agreement and exchange of information procedures. In addition, there is also the question of whether an international framework to facilitate arbitration of transfer pricing disputes should be established.<sup>1</sup>

15. There was a consensus that training of tax administrators in the methodologies and approaches to resolution of transfer pricing was of the utmost importance. The first workshop to begin this process was successfully held, under United Nations auspices in association with the International Bureau of Fiscal Documentation, at Amsterdam in March 1999.

16. A representative of OECD reviewed the recent developments on transfer pricing in OECD, including monitoring of the use of the OECD guidelines by member countries, studying the application of the guidelines to permanent establishments situations, publishing guidelines for advance pricing agreements (APAs), and studying the question of inclusion of dispute resolution procedures in tax treaties. The OECD transfer pricing guidelines have been expanded by examples showing how these guidelines should be applied, particularly with respect to the profit-split methods and intangibles. A glossary of terms has also been prepared.

17. The use of and experience with APAs was extensively discussed. One observer noted that his country had found the APA process to be cheaper, quicker and a less confrontational approach to transfer pricing issues than the audit process. It was generally agreed that bilateral and multilateral APAs represent the preferred approach. Several participants opposed the use of unilateral APAs. But some participants reported that unilateral APAs had proved valuable in their experience, particularly for establishing a basis in mutual agreement procedures.

18. It was noted that there is general agreement on the basic methodologies to be applied by countries in determining

appropriate transfer prices. But it was noted that some countries use safe harbours. While safe harbours provide some simplification, it was also observed that they may depart from the arm's length principle, and may also lead to double taxation and opportunities for tax arbitrage. OECD has recommended that countries not employ safe harbours.

19. One member stated that the transfer pricing issue was of great importance for both developing and developed countries. He recommended that the Group endorse the creation of a structure for arbitration of transfer pricing disputes. In his view, this would be of great assistance to developing countries. Some participants observed that since the European Union has an arbitration convention and a few tax treaties include provisions on arbitration, it would be desirable to wait for more experience under those treaties. Others emphasized that an arbitration procedure should not be a substitute for developing expertise in transfer pricing issues. It was made clear, however, that the arbitration procedure being proposed was not a substitute for training or mutual agreement procedures; it would be a procedure of last resort to resolve transfer pricing disputes. There was general agreement that if arbitration procedures were adopted, they should be the result of multi-country agreements, perhaps on a regional basis. One member stressed the need for developing procedures that lead to quick resolution of transfer pricing disputes.

20. In short, the members agreed that training of tax administrators in developing countries in transfer pricing methodologies and procedures is of the utmost importance and should be pursued by the United Nations. In addition, to assist developing countries in addressing transfer pricing issues effectively, a framework should be established under the auspices of the United Nations to provide a mechanism for the resolution of disputes by an arbitration procedure. Arbitration would be seen as a measure of last resort in the mutual agreement procedure. Such an institution could develop a cadre of arbitrators and other experts to assist developing countries in presenting their cases to the arbitrators. This procedural arrangement could accelerate the resolution of disputes in transfer pricing cases.

*Notes*

<sup>1</sup> These issues are discussed in detail in *International Cooperation in Tax Matters* (United Nations publication, Sales No. E.98.XVI.1), part one, chap. IV, and part two, paper entitled “The taxation of international income in developing countries”.

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