International Overview Training – Post 2017 Tax Reform

Topic V
IRS Treaty Administration:
Post Tax Cuts and Jobs Act of 2017
IRS Front Matters

- The IRS Mission Statement
- 14 General Principles of Ethical Conduct for Federal Employees
- Your Rights as a Taxpayer
Learning Objectives

At the end of this lesson, you will be able to:

A. Describe the basic purpose of tax treaties

B. Identify a few key provisions of tax treaties and the Competent Authority’s (“CA”) role and assistance

C. Explain how tax treaties may affect examinations
A. Basic Purpose of Tax Treaties
Purpose of Tax Treaties

- Avoid double taxation:
  - Allocate taxing rights among the source and residence countries
  - Resolve transfer pricing disputes
  - Credit/exemption mechanisms
  - Allow CAs to agree to provide relief in cases of taxation not in accordance with the treaty

- Prevent fiscal evasion through exchange of information and mutual collection assistance
## US Tax Treaties

### Countries with a US tax treaty in force:

<table>
<thead>
<tr>
<th>Armenia*</th>
<th>Hungary</th>
<th>Pakistan</th>
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<tbody>
<tr>
<td>Australia</td>
<td>Iceland</td>
<td>Philippines</td>
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<tr>
<td>Austria</td>
<td>India</td>
<td>Poland</td>
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<td>Azerbaijan*</td>
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<td>Portugal</td>
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<td>Korea</td>
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<td>Kyrgyzstan*</td>
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<td>Tajikistan*</td>
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<td>Luxembourg</td>
<td>Thailand</td>
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<tr>
<td>Egypt</td>
<td>Malta</td>
<td>Trinidad and Tobago</td>
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<tr>
<td>Estonia</td>
<td>Mexico</td>
<td>Tunisia</td>
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<tr>
<td>Finland</td>
<td>Moldova*</td>
<td>Turkey</td>
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<td>France</td>
<td>Morocco</td>
<td>Turkmenistan*</td>
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<td>Georgia*</td>
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<td>Ukraine</td>
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<td>Germany</td>
<td>New Zealand</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Greece</td>
<td>Norway</td>
<td>Uzbekistan*</td>
</tr>
</tbody>
</table>

General Operation of Tax Treaties

- Tax Treaty Interpretation:
  - Every treaty contains different language and needs to be independently analyzed
  - Treaties do not impose tax or provide a basis for taxation independent of domestic law
  - First, analyze the transaction under the Internal Revenue Code ("IRC"). Then, consider how a treaty might alter the result
  - Treaties, like the IRC, have the force and effect of law and should be read harmoniously with the IRC to the extent possible. But, if there is a direct conflict, the more recently-enacted provision controls
  - Characterization
US treaty provisions can be viewed as serving one of the following roles:

- Scope
- Definitions
- Operation
- Administration
B. Key Provisions of Tax Treaties
Key Provisions of Tax Treaties: Scope

- Eligibility for Treaty Benefits
  - In order to claim treaty benefits, a person must:
    - Be a resident of one of the Contracting States ("CS") to the treaty, and
    - If the treaty has a Limitation on Benefits ("LOB") article, meet one of the tests set forth in the LOB article
Key Provisions of Tax Treaties: Scope (Cont’d)

- Covered taxes generally only include income taxes in effect as of the signature date of the treaty
  - The treaty generally will also apply to any identical or substantially similar income taxes imposed after the signature date of the treaty
- Taxes covered by US totalization agreements (e.g., FICA taxes) as well as estate and gift taxes generally are not covered
Key Provisions of Tax Treaties: Definitions

- Definitions
  - Throughout treaty (e.g., Article 12 (Royalties), US Model Treaty (2006))

- Undefined terms
  - Generally, look to US domestic law when US tax is at issue.

- CA agreements
### Key Provisions of Tax Treaties: Operation

#### Income From

<table>
<thead>
<tr>
<th>Real property</th>
<th>Dividends</th>
<th>Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property gains</td>
<td>Business profits</td>
<td>Interest</td>
</tr>
<tr>
<td>Directors’ Fees</td>
<td>Gov’t service</td>
<td>Royalties</td>
</tr>
</tbody>
</table>

- Shipping and air transport
- Students & trainees
- Entertainers & athletes
- Associated enterprises
- Pensions, social security, annuities, alimony & child support
- Other income
Business Profits & Permanent Establishment Articles

- Business profits of an enterprise of one CS may be taxed by that CS
- Business profits of an enterprise of one CS may not be taxed by the other CS unless the enterprise carries on business in that other CS through a permanent establishment ("PE") situated therein
- When the enterprise of one CS carries on business in the other CS through a PE, the CS in which the PE is situated may tax the enterprise on the net income that is “attributable” to the PE
- E.g., see US Model Treaty (2006):
  - Article 7 (Business Profits)
  - Article 5 (Permanent Establishment)
Key Provisions of Tax Treaties: Operation (Cont’d)

- The Associated Enterprises article permits each country to assert transfer pricing adjustments on intercompany transactions based on arm’s-length principles under IRC 482.

- If the CA agrees to a foreign-initiated transfer pricing adjustment, the Associated Enterprises article allows the CA to provide a correlative adjustment to reflect the foreign-initiated adjustment to mitigate double taxation.
Key Provisions of Tax Treaties: Administration

- Relief from Double Taxation

- Mutual Agreement Procedure

- Exchange of Information ("EOI")
Key Provisions of Tax Treaties: Administration (Cont’d)

- Treaty Assistance and Interpretation (“TAIT”)
  - Non-allocation provisions and PE

- Advanced Pricing and Mutual Agreement Program (“APMA”)
  - Allocation provisions and PE

- Exchange of Information (“EOI”)
  - Exchange of information provisions (and for some treaties, collection assistance provisions)
Key Provisions of Tax Treaties: Administration (Cont’d)

Commissioner
Large Business & International

Deputy Commissioner

Treaty and Transfer Pricing Operations

- DFO Transfer Pricing Practice
- Practice Networks

Office of Assistant Deputy Commissioner International

- Director APMA
- Director Treaty Administration

JITSIC

TAIT

EOI
Mutual Agreement Procedure

- **US Model Treaty (2006), Article 25**

  - When a taxpayer is subject to double taxation or taxation not in accordance with a tax treaty, the taxpayer may request CA assistance under the Mutual Agreement Procedure (“MAP”) article

  - The process of applying for CA assistance differs in each country (see Revenue Procedure 2015-40 for procedures governing requests for US CA assistance)
Advance Pricing Agreements (APAs)

- An APA may be concluded on a bilateral or multilateral basis between CAs through the mutual agreement procedure of the relevant treaty.

- A bilateral APA is an agreement between tax administrations and a Taxpayer on the proper transfer pricing of related party cross-border transactions for a term of years, which often include prior years as well as future years.
Key Provisions of Tax Treaties: Administration (Cont’d)

EOI – US Model Treaty (2006), Article 26

- Treaty Partners may exchange information foreseeably relevant for carrying out provisions of the treaty or of domestic laws.

- Use and disclosure of information exchanged must be in accordance with the provisions of the specific treaty. Unless otherwise provided under the terms of the treaty:
  - May only be used for tax administration and tax enforcement purposes, and
  - Subject to same disclosure restrictions as information obtained under our domestic laws.

- US initiated requests may be sent to #LBI.Intl.Exchange.of.Information@irs.gov#

Any line marked with # is for OFFICIAL USE ONLY.
Specific Information Exchanged

- Tax return information, including:
  - Filing status and address
  - Income and expenses
  - Information returns
- Business records, invoices, contracts, agreements
- Bank, brokerage, and other financial records

Automatic Exchanges of Information

- Fixed, Determinable, Annual, and Periodic

Spontaneous Exchanges of Information

- Information suggesting non-compliance with tax laws of a foreign jurisdiction
Joint International Taskforce on Shared Intelligence and Collaboration (“JITSIC”) also assists with exchanges of information

- The EOI Program manages almost all exchange of information requests, outgoing and incoming
- JITSIC performs a relatively small number of requests. JITSIC exchanges involve: i) JITSIC Network project exchanges, ii) joint audits or joint collaborations with JITSIC Network member countries, or iii) complex, cross-border tax avoidance schemes involving JITSIC Network member countries (http://www.oecd.org/tax/forum-on-tax-administration/jitsic/)

Both programs adhere to Internal Revenue Manual 4.60.1, Exchange of Information procedures
C. How Tax Treaties May Affect Tax Examinations
Compliance Role

- Have a general familiarity with how a treaty applies and affects US tax
- Consider the potential impact of a transfer pricing issue to the foreign related party
- Notify US Taxpayer of MAP rights when double tax/tax inconsistent with treaty
- Know when to consider EOI procedures
- Evaluate foreign-initiated adjustments
When an examination involves a transfer pricing issue, the Issue Team will be expected to follow the memorandum from LB&I Commissioner on “Interim Guidance on Mandatory Issue Team Consultations with APMA for Examination of Transfer Pricing Issues Involving Treaty Countries” (dated February 19, 2019)
Compliance role when MAP may arise:

- Notify US Taxpayer of MAP rights
- Protect US statute of limitations
- Suspend US administrative action (e.g., assessments, collection procedures) on CA issues; and
- Prepare Issue Team and MAP Reports
Compliance Role: Global Awareness

- Building a clear picture of the global business

- Working with the taxpayer:
  - Encourage a collaborative approach,
  - Face-to-face dialogue can be more effective than lengthy exchanges of correspondence in developing an understanding of the business, and
  - Advocate direct interaction with key personnel of the taxpayer
Compliance Role: Global Awareness (Cont’d)

- The Issue Team is an active participant in global tax administration.

- The Issue Team understands how proposed adjustments will impact multinational taxpayers by understanding:
  - Taxpayer’s global business model and practices, and
  - Taxpayer’s transfer pricing methods
Compliance and CA

Country A C.A. <-> Country B C.A.

Communication and Collaboration

GLOBAL TAX ADMINISTRATION

Exam function <-> Exam function
What Did We Learn?
What did we learn?

You should now be able to:

A. Describe the basic purpose of tax treaties

B. Identify a few key provisions of tax treaties and the CA’s role and assistance

C. Explain how tax treaties may affect examinations
Appendix
Resources

- **IRM 4.60.2** - Mutual Agreement Procedures and Report Guidelines

- [#LBI.Treaties.IPN@irs.gov#](#) - Treaties Practice Network

- [Treaties Practice Units](#)

- **APMA**

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Resources (Cont’d)

- #LBI.Exchange.of.Information.PN@irs.gov# - EOI Practice Network
- EOI Practice Units
- Exchange of Information (EOI) Program

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Resources (Cont’d)

- **US Model Treaty (2006) and Technical Explanations**
- **US Income Tax Treaties/Model Treaties, TIEAs, and Technical Explanations**
- **OECD Model Treaty Convention on Income and Capital**
- **OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MAAC)**
Resources (Cont’d)

- LB&I International Practice Units
- Information Gathering Practice Units
- Information Gathering Contacts
# Glossary of Terms

<table>
<thead>
<tr>
<th>Acronym/Terms</th>
<th>Definition</th>
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<tbody>
<tr>
<td>APA</td>
<td>Advance Pricing Agreement</td>
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<tr>
<td>APMA</td>
<td>Advanced Pricing and Mutual Agreement</td>
</tr>
<tr>
<td>CA</td>
<td>Competent Authority</td>
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<tr>
<td>CS</td>
<td>Contracting State</td>
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<tr>
<td>EOI</td>
<td>Exchange of Information</td>
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<tr>
<td>IRC</td>
<td>Internal Revenue Code</td>
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<td>LB&amp;I</td>
<td>Large Business &amp; International</td>
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<tr>
<td>LOB</td>
<td>Limitation on Benefits</td>
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