

The 10th SGATAR Joint Training Program

Mutual Agreement Procedure (MAP) and Advance Pricing Agreement (APA) : Implementation and Application (Working Paper)

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1. Introduction

1.1 Tax System at a glance

The tax system of Macao Special Administrative Region (hereafter abbreviated as “MSAR”) is one originated from Portugal. The system and its regulations had been reformed in numerous occasions over the years to accommodate to the changing business environment in the region but it has always been, and still is, a tax regime with a simple tax structure and relatively low tax rate (Tax rates for Profits Tax: 3 – 12%). The Financial Services Bureau (hereafter abbreviated as DSF) is a multi-functional government body. It acts as an executive arm of the Government of the Macao Special Administrative Region (MSAR), providing services of public asset management, public finance, as well as tax administration. To abide by the Decree No. 30/99/M, which governs its constitution and function, DSF plays an important role in the following taxation activities:

- Managing the tax administration of the MSAR to ensure its compliance with the laws concerned and to maintain public interest when it is offended;
- Implementing tax policies of MSAR, evaluating the policies effectiveness on different aspects such as the public finance, the economy and the society;
- Inspecting taxation and public finance activities, preventing and correcting anomalies;
- Assisting in the participation of the negotiation of international treaties concerning tax affairs, and implementing its follow-up actions.

In respect of the tax administration and collection, DSF is responsible for seven types of taxes in MSAR, namely Business Registration Tax, Profits Tax, Tourism tax, Motor-Vehicle Tax, Salaries Tax, Stamp Duty and Property Tax.

1.2 Recent Development on Transfer Pricing Policy, MAP and APA

It is essential to note that there is no specific legislation, nor guidelines regarding dealings with transfer pricing issues within our tax legislation. Conventional wisdom would dictate that should transfer pricing occur, the logical and usual flow of profits would be from a higher to a lower tax rate regime. It is therefore not uncommon to find MSAR at the receiving end of such profits, rather than the other way round because of its relatively low tax rates. Moreover, most of the businesses in MSAR are of small and medium sized capacity, transaction values of these small and medium enterprises are relatively small and thus may not provide much indication of the existence of transfer pricing practices.

After the liberalisation of gaming industry in 2002, the economy of Macao grew dramatically with significant investment inflows associated with the gaming industry. With the rapid economic development, double taxation cases, as a result, increased and became more complicated. As the world economy has become increasingly globalised in recent years, it is evident that multinational corporations pose challenges to tax administrations and bilateral tax cooperation becomes a major concern of tax authorities.

The concept of international double taxation where both contracting parties impose tax on the same income can often be mitigated by double taxation agreements between countries. These agreements remove impediments to international trade and investment by abating the risk of double taxation and help contain issues concerning with tax fraud as well as tax evasion.

1.2.1 Organizational Structure in relation to MAP and APA

To establish a positive business environment, Macao has signed Double Taxation Agreements with its close business partners for the purpose of relieving double taxation and fighting against fiscal evasion and tax avoidance. At the time of writing, “*Arrangement/Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income*” have been signed with Mainland China¹, Portugal, Mozambique, Belgium and Cape Verde. Further talks with several countries, particularly Portuguese speaking countries are underway. The above mentioned agreements are, in principle, of similar structure. Macao has neither adopted the UN nor the OECD model. The agreements are combination of both the aforementioned models, with modification to suit Macao’s situation.

The competent authority of Macao referred in the Double Taxation Agreement is the Chief Executive, Secretary of Economy and Finance or his authorised representative. Day-to-day functions regarding the implementation of the Double Taxation Agreements are carried out by Double Taxation Working Group under Macao Financial Services Bureau (DSF).

¹ Being a special administrative region of China, DTA concluded with Mainland China is an “Arrangement”, while others are “Agreements”. (*Arrangement/Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income*)

1.3 Related Legislation

When a taxpayer is taxed not in accordance with the Double Taxation Agreement, he may elect to seek domestic recourse. Under Article 44 of Complementary Tax Regulation (CTR) enacted by Law No. 21/78/M and Article 79 of Professional Tax Regulation (PTR) enacted by Law No. 2/78/M, the taxpayer may lodge a tax appeal with the Commission of Revision under DSF within 20 days of receipt of notification of result of assessment. Collection of tax is suspended until decision has been made by the Commission of Revision regarding the appeal. For any tax appeal lodged after the 20 days mentioned above, no suspension of collection will be granted and its eligibility will be determined by the Commission of Revision.

Under Article 82, 84 of CTR and Article 84, 86 of PTR, if the taxpayer loses the tax appeal in the Commission of Revision, he may lodge an appeal with the Administrative Tribunal with 30 days (for Complementary Tax) and 45 days (for Professional Tax) after receipt of notification. Under Article 85 of CTR and Article 87 of PTR, lodging an appeal with Administrative Tribunal against the decision of Commission of Revision does not create effect of suspension of collection of tax.

2. Implementation of MAP

Macao's Experience on MAP

Up to the present, three Double Taxation Agreements that were signed with Mainland China, Portugal and Mozambique are effective. However, implementation of MAP in Macao are still in its infancy. Macao has not received any MAP request from taxpayers.

Types of MAP Cases

In the aspect of FDI flows, Mainland China and Portugal have close connection with Macao. As the transactions with these countries become greater in size and in number, the risks of double taxation get bigger. The types of MAP cases anticipated are likely to be transfer pricing cases in which profits are shifted to Macao due to Macao's low tax rate. Competent authority of the other country may make a transfer pricing adjustment to the price of goods or services provided to Macao. Macao may consider allowing a corresponding adjustment to relieve double taxation.

Name of Tax	Tax Rate (Year 2011)	Annual Tax Allowance (Year 2011)
Complementary Tax	Progressive tax rate ranging from 9% to 12%	Macau Patacas \$200,000 (or USD \$25,100).
Professional Tax	Progressive tax rate ranging from 7% to 12%	Macau Patacas \$192,000 (or USD \$24,000).

2.1.2 Current Procedures

As there have not been any MAP cases, they are likely to be treated on an ad hoc basis by Double Taxation Working Group when they are initiated. There is no prescribed form for MAP application. Requests are required to be submitted in form of letter. There are no existing formal procedures for MAP in Macao. Much work has yet to be done in order to establish a systematic mechanism for MAP. Any MAP cases initiated in the future will first be treated in the following procedures, with ideas adopted from the “Manual on Effective Mutual Agreement Procedures” published by OECD. After gaining experience in the future implementation, Macao will develop its own sets of formal MAP procedures taking in account of the actual situation.

First Stage	1	Receive MAP request from taxpayer
	2	Confirm receipt of MAP request
	3	Preliminary review of case
	4	Request for additional information, if necessary
	5	Determine eligibility for MAP
	6	Notify taxpayer whether request is accepted or not
	7	Propose to other competent authority to start discussion
	8	Receive confirmation from other competent authority
Second Stage	9	Analyse the initial adjustment
	10	Issue/receive position paper
	11	Issue/receive response to position paper
	12	Negotiate with other competent authority
Third Stage	13	Reach mutual agreement
	14	Tapayer agrees with mutual agreement
	15	Confirm mutual agreement by exchange of letter
	16	Implement the mutual agreement

2.1.3 Strengths and Weaknesses of MAP Implementation

Since the organization structure of the competent authority of Macao is relatively simple, this shortens the time required for communication and approval. Having a small working group on the double taxation matters ensures the consistency in treatment of cases. The other side of the coin is that the limited number of cases and limitation of human resources create difficulty in accumulating knowledge of market and industry. Moreover, staff finds it hard to build up expertise without specialization.

Another potential weakness is lack of segregation of duties. The general responsibility of Tax Inspection Department is to conduct desk audit and field audit, and make adjustments on tax returns. The members of Double Taxation Working Group are drawn from the Tax Inspection Department. Aside from tax inspection, they also play a major role in implementing the Double Taxation Agreements. MAP cases will be handled by Double Taxation Working Group members who are directly or indirectly involved with the initial tax assessment and adjustment. The level of objectivity may be affected without proper segregation of duties.

Language barrier is also one of the weaknesses for Macao in implementing MAP as the official languages are Traditional Chinese and Portuguese. Tax laws and related documents are all written and recorded either in both languages or either language. If there is a MAP, all information related to the case have to be translated into a common language before communicating with the other competent authority, i.e. English, in which it could be time consuming and in turn, will prolong the MAP.

A potential area of improvement in the MAP implementation is publicity. To increase taxpayer's awareness of MAP, DSF considers making its MAP information available on the OECD website and its official website, with profile of the competent authority, procedures concerning use of MAP, related domestic laws, etc.

2.1.4 Relationship between Dispute Resolution under MAP and Domestic Laws

Notwithstanding the domestic recourse mentioned in Section 1.2, the taxpayer can initiate a MAP request under Article 25 of the Double Taxation Agreement. It overrides the domestic laws where there is conflict between them. For Macao, its wording of Article 25 is similar to that of OCED Model of 2005 with 4 paragraphs, which does not include arbitration process.

Under Article 25 of the Double Taxation Agreements signed, the last sentence indicates that the MAP case must be presented within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Agreement. Therefore, the 20-days appeal lodgment period requirement of domestic laws does not restrict the taxpayers' right to initiate a MAP, but it does affect the suspension of collection of tax.

Improving Efficiency of MAP Implementation

Macao has not received any MAP cases from taxpayers. In the future, more Double Taxation Agreements will be signed. DSF considers developing a set of

formal procedures for MAP implementation. The “Manual on Effective Mutual Agreement Procedures” (MEMAP) published by OECD will serve as a useful reference. Allowing early resolution of cases is one of the Best Practices suggested by MEMAP. Article 25 of OECD Model Tax Convention and its Commentary indicate that taxpayers are entitled to initiate a MAP request even before an audit is completed or they have received formal notification of an assessment. Early involvement, for example, prior to conclusion of audit, shortens the processing time of the MAP case.

3. Implementation of APA

As for APA cases, APAs are generally bi- or multilateral agreements between the taxpayer and one or more foreign tax administrations under the authority of the MAP specified in income tax treaties. APA provides greater certainty on the transfer pricing method adopted, mitigating the possibility of disputes and facilitating the financial reporting of potential tax liabilities, as well as, reduces the incidence of double taxation. Even though DSF acknowledges the benefits for both taxpayers and tax authorities from an effective APA programme as this is evidenced by the number of jurisdictions that already have well functioning APA programmes as well as a number of jurisdictions within the Asia Pacific region currently in the process of establishing a programme. However,

Future development in the implementation of APA

As previously mentioned, MSAR has only five DTAs signed and which only three of them are currently effective. The implementation of MAP is definitely still in its infancy, much work has to be done in order to establish a systematic mechanism for MAP. Hence, due to resource constraints, DSF aims to focus on

the expansion of our DTA network and the development of MAP implementation at this current stage. In the future, after gaining experience in the implementation of MAP, DSF will head to develop its own mechanism for the implementation of APA. According to the organization structure of DSF, APA are likely to be treated on an ad hoc basis by Double Taxation Working Group. To establish a systematic mechanism for APA, the “Guidelines for Conducting Advance Pricing Arrangements Under the Mutual Agreement Procedure (“MAP APAs”) published by OECD will serve as a useful reference.

4. Conclusion

As Macao is at the beginning stage of expanding its tax treaty network, there are no mechanisms or formal procedures in place for MAP and APA at the time of writing. And it has not received any MAP or APA request from taxpayer. If MAP and APA are implemented in the future, its structure will face the challenge of lack of segregation of duties though it has the advantage of close communication and consistency in treatment. Moreover, much work has to be done on publicity.

In the future, after gaining experience from practical implementation, Macao will develop its own sets of formal MAP and APA procedures with principles adopted from MEMAP. With their completion and subsequent effective implementation, would allow MSAR to further enhance its status as a co-operating jurisdiction within the international community.

References

Manual on Effective Mutual Agreement Procedures - Index. "OECD" [Cited 2012/9/3]. Available from World Wide Web: <<http://www.oecd.org/ctp/transferpricing/manualoneffectivemutualagreementprocedures-index.htm>>