Global Tax Dispute Resolution and Controversy Services

Tax Dispute and Controversy Update – Alternative Dispute Resolution

Wednesday 11 June 2014
ANY TAX ADVICE IN THIS COMMUNICATION IS NOT INTENDED OR WRITTEN BY KPMG TO BE USED, AND CANNOT BE USED, BY A CLIENT OR ANY OTHER PERSON OR ENTITY FOR THE PURPOSE OF (i) AVOIDING PENALTIES THAT MAY BE IMPOSED ON ANY TAXPAYER OR (ii) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY MATTERS ADDRESSED HEREIN.

You (and your employees, representatives, or agents) may disclose to any and all persons, without limitation, the tax treatment or tax structure, or both, of any transaction described in the associated materials we provide to you, including, but not limited to, any tax opinions, memoranda, or other tax analyses contained in those materials.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.
Welcome

Alternative Dispute Resolution

Speaker:

Sharon Katz Pearlman
Global Head, Tax Dispute Resolution & Controversy
KPMG International
National Principal in Charge
Tax Controversy Services
KPMG LLP (US)
Polling Question #1

In how many countries do you do file tax returns?

a) 1-10
b) 11-20
c) 21-35
d) Over 35
Polling Question #2

In how many countries are you currently involved in a tax examination or other dispute with a revenue authority?

a) 1-5
b) 6-10
c) 11-20
d) Over 20
United Kingdom

Tax Dispute and Controversy Update – Alternative Dispute Resolution

Speaker:

Kevin Elliott
Director, Tax Investigations & Dispute Resolution
KPMG in the UK
Alternative Dispute Resolution in the UK

Significant developments

2009: Tax Tribunal Rules
- The Tribunal should seek where appropriate to bring to the attention of the parties the availability of any appropriate alternative procedure for the resolution of the dispute

2010: HMRC Dispute Resolution Unit
- Created to co-ordinate HMRC’s developing approach to dispute resolution

2011: Litigation & Settlement Strategy
- Refreshed to include a new provision:
  “In certain cases ADR can be used to support the resolution of disputes either by facilitating agreement between the parties or by helping the parties prepare for litigation”
- Specific guidance on new ADR procedures

2011 to 2013: ADR pilot
- HMRC piloted the use of mediation to resolve tax disputes

2013: Business as usual
- ADR established a formal procedure for resolving tax disputes
Alternative Dispute Resolution in the UK

What is ADR & how does it work?

Mediation
- ADR involves the use of mediators / mediation techniques to resolve tax disputes
- Initial cases in the pilot engaged external mediators completely independent of the parties

Suitable cases
- Appropriate when cases reach impasse and litigation might have to be considered
- Not suitable for avoidance schemes or issues where HMRC has a clear policy position
- Suitable for cases with a range of possible outcomes but also ‘all or nothing cases’

The process
- Taxpayer applies for ADR to their HMRC relationship manager and the Dispute Resolution Unit
- Any rejections are considered by an ADR Panel and reasons for rejection are provided to the taxpayer
- CEDR accredited facilitators are appointed
- Parties sign an ADR agreement – discussions are on a without prejudice basis
- Position papers are exchanged
- Facilitated mediation held – decision makers present – break out sessions – agreement on the day
Alternative Dispute Resolution in the UK

Findings / results to date

Mediation
- Mediation greatly increases the prospect of the parties reaching negotiated settlement
- HMRC and professional advisers have invested in their people gaining CEDR accreditation

Acceptances
- Early rejection rate was as high as 65% which fell to 20%
- Indirect tax disputes most common 33% followed by corporate income tax 28%

Success rate
- 5% of cases entered into the pilot failed to reach settlement - HMRC ‘win’ rate similar to litigation

Time commitment
- The average elapsed time from application to resolution was 24 weeks compared to 70 weeks average time from making an appeal to the Tribunal Service and having that appeal heard

Cost
- HMRC estimate there are significant cost savings compared to an appeal at First Tier Tribunal

Feedback
- 93% approval rating
Alternative Dispute Resolution in the UK

ADR in action

Client position

- Forthcoming third party disposal of a business
- Significant shareholder is a high net worth individual
- Tax implications of the disposal are dependent on the individual’s domicile status and materially affect the way the transactions can be structured
- Individuals domicile status has been in dispute for 5 years

ADR

- Application accepted by HMRC even though domicile is an ‘all or nothing’ issue and a current hot topic with any settlement requiring sign off by senior HMRC governance board
- HMRC facilitator appointed and senior Specialist Personal Tax officers attend the mediation
- Thorough mediation with client in attendance
- Breakthrough point identified and follow up evidence provided

Outcome

- HMRC team presented evidence to Contentious Issues Panel which accepted the clients position
- Disposal transacted with certainty of tax consequences
Polling Question #3

Are you currently involved in an alternative dispute resolution in any jurisdiction?

a) Yes  
b) No  
c) Don’t know
United States

Tax Dispute and Controversy
Update – Alternative Dispute Resolution

Speaker:

Victoria Sherlock
Managing Director & Southwest Area
Tax Controversy Practice Leader

KPMG LLP in the US
Federal Tax Dispute Resolution Techniques

- Fast Track Settlement
- Traditional Appeals
- Early Referral to Appeals
- Post-Appeals Mediation
- Post-Appeals Arbitration
- Competent Authority/Mutual Agreement Procedure
Fast Track Settlement (FTS) – Part 1

- Available in LB&I cases – as well as other operating divisions by agreement with IRS.
- Resolution target: 120 days from acceptance.
- May be initiated once issue is fully developed – normally after Form 5701 or Notice of Proposed Adjustment issued but before issuance of 30-day letter.
- No “hot interest” (IRC 6621) runs during FTS.
- Taxpayer may withdraw at any time and retain all traditional appeal rights.
Fast Track Settlement – Part 2

FTS may be initiated by either party and must be agreed to by both IRS and taxpayer.

An FTS Appeals Official will serve as a neutral and use various dispute resolution techniques to facilitate settlement.

Settlements available to the parties include those based on the hazards of litigation.

Closing agreement is executed setting forth resolution of issue.

If any issue remains unresolved at conclusion of FTS process, taxpayer retains all of its otherwise applicable appeal rights.
Traditional Appeals

IRS Office of Appeals provides an independent review of all proposed adjustments and denials of claims for refund.

Appeals officer attempts to effect a settlement or resolution based on the perceived hazards of litigation for both parties.

Appeals will not raise new issues and for the most part will evaluate the case as it has been developed.

Appeals can however return a case to exam for further development.

Appeals will not consider “new” information that has not bee presented to the Examination Team.

This rule can be problematical if you plan on bringing company “witnesses” to the conference.

Appeals settles > 80% of cases considered.
(Source: http://www.irs.gov/pub/foia/ig/spder/AP-08-0713-03.pdf)
Post-Appeals Mediation


Nonbinding process in which mediator does not have settlement authority to force a resolution, nor will mediator render a decision.

Appeals Officer becomes advocate for the government and can invite the Exam Team and/or IRS Counsel to participate.

Appeals mediator reviews issue and seeks to effect resolution.

Taxpayer must sign a conflict waiver acknowledging that mediator is an appeals officer.

Non-IRS co-mediator may be jointly selected; taxpayer bears the cost.

If agreement is reached, Form 906 Closing Agreement, is executed.
Post-Appeals Arbitration

Procedures found in Rev. Proc. 2006-44

Arbitration can be requested for issues in the Appeals administrative process after settlement negotiations are unsuccessful

The IRS and the taxpayer agree to be bound by the decision of a third party decision maker

There is no appeal from the decision of the arbitrator

Taxpayer must first attempt in good faith to negotiate a settlement with Appeals before requesting arbitration

An arbitrator is selected from Appeals or from an outside organization. Sometimes there will be more than one arbitrator

Arbitration is optional and has been used infrequently

Initiated by Competent Authorities of the treaty partners, or upon request of the taxpayer.

Taxpayer rights designed to protect against international double taxation (e.g., transfer pricing).

Some new treaties include arbitration provision (for example, U.S. - Canada Treaty).

Proposed revisions to Rev. Proc. 2006-54 to require a more formalized submission and increased taxpayer involvement.
Polling Question #4

If you are participating in an alternative dispute resolution program, how would you describe your experience?

a) Negative; I see little benefit to engaging this way

b) Somewhat positive; the process has made our dealings with the revenue authorities easier and more productive

c) Very positive; the program has truly enhanced our ability to communicate with the revenue authority and has streamlined the process

a) None of the above; as I’m currently not participating in any of these programs
Australia

Tax Dispute and Controversy Update – Alternative Dispute Resolution

Speaker:

Jeremy Geale, Partner of KPMG Tax Law, Tax Partner

KPMG in Australia
Australia – Alternative Dispute Resolution

Context – the Australian Dispute Continuum

- **Audit**
  - Risk Review
    - 230 adjustments
  - Audit
    - 26,500 objections
  - 470,000 adjustments

- **Objection to Revenue Authority**
  - Independent Review by Revenue Authority
    - 130 objections
  - 26,500 objections

- **Appeal**
  - Administrative or Judicial Review (Tribunal or Court)
    - 77 cases
  - 675 cases / 115 judgements

- **Large business**
  - 16.2 million returns

© 2014 KPMG International Cooperative (“KPMG International”), a Swiss entity. Member firms of the KPMG network of independent firms are affiliated with KPMG International. KPMG International provides no client services. No member firm has any authority to obligate or bind KPMG International or any other member firm third parties, nor does KPMG International have any such authority to obligate or bind any member firm. All rights reserved.
Australia – Alternative Dispute Resolution

Legislative context

Use or at least consideration of ADR is entrenched by legislation.

Good Management Rule / Model Litigant Rule (introduced in 2005):

‘requires agencies [ATO] to endeavour where possible to avoid, prevent and limit the scope of legal proceedings by considering ADR before initiating legal proceedings and by participating in ADR where appropriate’

Genuine Steps Statement - prior to commencement of any legal proceedings taxpayer and revenue both required to file ‘genuine steps’ statement outlining what steps they have taken to resolve the dispute prior to commencing legal proceedings (introduced in 2011)
New Commissioner of Taxation appointed January 2013 (ex-chairperson of KPMG NSW Office) – one of three key priorities was the quicker resolution of technical issues and disputes

Introduction of independent review function which sits outside compliance / audit function – applies to large business clients

Greater use of direct and open contact with taxpayers, use of in-house facilitators and third parties such as former Federal Court and High Court judges for early neutral evaluation or mediation.

Results to date:

- 2011 – 31% of all settlements at audit or pre-audit; 47% at litigation;
- 2013 – 49% of all settlements at audit or pre-audit; 28% at litigation

Number of settlements increased by 1/3rd
Australia – Alternative Dispute Resolution

PS LA /2013/3 – public policy instructing ATO as guidelines that must be followed when attempting to resolve a dispute

Code of Settlement Practice (PS LA 2007/5)

Require ATO to adopt a principal based approach to settlement

- Will not forgo tax that is properly payable
- Can not, generally, depart from ‘precedential ATO view’
- Requires settlements to be structured, such that align, with stated technical positions

When will ATO consider ADR to be appropriate

- Cost of litigation outweigh tax in dispute
- Opportunity to narrow facts or issues in dispute
- Achieve certain or early payment
- Maintain or improve relationship between ATO and taxpayer / community
Australia – Alternative Dispute Resolution

Options and when used

Direct engagement with ATO
- Audit or Objection
- Critical to have key stakeholders in room
- Need to have something to give negotiate

Conciliation
- Conciliator (mediator) plays active role, advising parties on their positions
- Conciliator typically a retired judge
- Works best where no precedential view on technical issue or significant dispute as to facts (i.e. there is significant litigation risk)
- Used at objection stage or litigation

Mediation
- Mediator does not advise parties but seeks to encourage resolution
- Used in litigation

Neutral case evaluation
- Retire judge or expert provides opinion on case, or part of case
- Can be binding
PS LA /2013/3 – public policy instructing ATO as guidelines that must be followed when attempting to resolve a dispute

Code of Settlement Practice (PS LA 2007/5)

Require ATO to adopt a principal based approach to settlement

- Will not forgo tax that is properly payable
- Can not, generally, depart from ‘precedential ATO view’
- Requires settlements to be structured, such that align, with stated technical positions

When will ATO consider ADR to be appropriate

- Cost of litigation outweigh tax in dispute
- Opportunity to narrow facts or issues in dispute
- Achieve certain or early payment
- Maintain or improve relationship between ATO and taxpayer / community
Australia – Alternative Dispute Resolution

The results - The amount of variance in ATO original position and the final settled position

Source: Australian Taxation Office
Polling Question #5

Which attribute of alternative dispute resolution is most attractive to you?

a) Reaching earlier certainty

b) Limiting the focus to significant/material positions

c) Improved relationships with the tax administrator

d) More efficient use of resources
Germany

Tax Dispute and Controversy Update – Alternative Dispute Resolution

Speaker:

Jan Uterhark, Partner, National Tax

KPMG in Germany
Agenda

1. Legal framework
2. Legal implementation
3. Content of mediation
4. Experiences/Prospects
1. Legal framework

- Law on the promotion of mediation and other methods of alternative dispute resolution (Mediation Act) of 21 July 2012
1. Legal framework

Although the Directive applies expressly not for tax, customs or administrative court matters (Art. 1 (2) Directive), the German legislator has taken it as an opportunity to introduce mediation in the public jurisdiction as the financial jurisdiction conducted by the Mediation Act.
1. Legal framework

- **§ 278 (5) Code of Civil Procedure**: "The court may order the parties to the conciliation hearing and other quality tests before a particular purpose and non-decision competent court (judge quality). The judge quality can judge all methods of dispute resolution, including mediation."

- **§ 155 Tax Court Code**: "… As far as this law does not contain any other provisions ... the Code of Civil Procedure including sec 278 (5) apply mutatis mutandis ..."
2. Legal implementation

- As is clear from the wording of § 278 of the Civil Procedure Code, the establishment of a judicial mediation is not mandatory, but left to the discretion of the courts.

- The courts must therefore decide by their councils as part of their court administration, whether mediation should be made possible and which judges colleague is determined as a mediator (quality judges).
2. Legal implementation

Of the 18 German fiscal courts currently allow 15 courts a mediation procedure.
(In the course of the deliberations of the Mediation Act, there has been criticism of the tax law and also from the judges as to whether the tax law is open as a public right of intervention of a solution by negotiation).
3. Content of mediation

Mediation is a structured, non-public process in which the participants work out using the quality judge voluntarily and autonomously a satisfactory solution for all parties themselves.
3. Content of mediation

- Only certified mediators may act as quality judges.

- The training to become a certified mediator comprises approximately 200 hours over a period of 12-18 months.

- The quality judge only mediates in the conflict; he is
  - not entitled to a decision,
  - is neutral and
  - gives basically no advice.
3. Content of mediation

A mediation comes into consideration, if

- conflicts that go beyond the actual legal problem;
- in emotional and deadlocked disputes the use of specific conflict resolution methods is required;
- a judgment can not afford the desired holistic solution;
- the parties wish to make their own responsibility a solution;
- the balance of interests is more important than being right;
- the parties wish a rapid and flexible handling of the conflict.
3. Content of mediation

In a mediation no tax claims can be negotiated in and placed in the parties' agreement!

(Tax law is not open as a public right of intervention of a solution by negotiation)
3. Content of mediation

- Mediation can therefore only be practiced at the Tax Courts as courts of first instance.

- There can therefore be no mediation at the Federal Fiscal Court, which is a pure Court of Appeals in legal matters.
3. Content of mediation

The mediation has the following implications for the legal process:

- For the duration of a mediation the court proceedings rest.
- Through the mediation proceedings are no additional court fees.
- A mediation agreement is recorded in court with the agreement of the parties.
- The logged mediation agreement has a title function and binds the parties.
- A mediation agreement resolves the conflict, so that the legal process can be explained by the parties to be settled.
4. Experiences/Prospects

- There is still no statistical data to the mediation process at the German fiscal courts.

- It is questionable whether the mediation process is more effective than the "ordinary" method of amicable dispute resolution, as set out in § 364a Tax Code and in § 79 Tax Court Code.
Polling Question #6

If you do not currently participate in one of these programs, would you choose to participate, given the opportunity?

a) Yes

b) No

c) Not sure
Thank You

If you are interested in speaking with a KPMG professional, please feel free to contact us at:
go-fmglobaltaxdisput@kpmg.com