

Israel

# Tax Authority Issues Updated Mutual Agreement Procedures

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The Israeli Tax Authority (ITA) has published the Income Tax Circular on Mutual Agreement Procedures (MAPs) in Treaties for the Prevention of Double Taxation (the new circular). The new circular deals with the way of submitting applications for MAPs and regulates the treatment of such applications. The new circular replaces an Execution Order published over 20 years ago.

## General instructions regarding MAPs as stated in the new circular

A taxpayer that believes that an action by one or both of the contracting states to a tax treaty causes, or may cause, it to be taxed contrary to the provisions of the tax treaty, may ask the competent authority of the contracting state of which it is a resident to initiate a MAP. The competent authority in Israel is the International Taxation Department of the Professional Division of the ITA, which is an independent body. Accordingly, the competent authority is not dependent on the assessing officer who conducted the assessment within the framework of the MAP. However, in appropriate cases, additional ITA representatives may be included in the review of the MAP application and the MAP itself.

According to the new circular, cases and issues in which a MAP may be relevant include the following:

- cases in which questions arise regarding applicable transfer pricing provisions and the way in which income must be allocated between the two contracting states;
- the existence of a permanent establishment in a contracting state and the allocation of income and expenses from the permanent establishment determination;
- decisions regarding residency in cases where a taxpayer is defined as a resident of both contracting states;
- different classifications of income in the contracting states; and
- double taxation arising as a result of the application of exit tax provisions.

The new circular also clarifies cases in which a MAP is not relevant, emphasizing that the procedure is not suitable for cases regulated by domestic tax law.

A MAP can be initiated simultaneously with other procedures, such as assessment procedures, administrative appeals or court appeals. According to the ITA, submitting an application to initiate a MAP or its actual initiation does not affect the statutory statute of limitations. However, most of Israel's tax treaties state that the decision of the competent authority within the framework of the MAP prevails over the statute of limitations period in domestic tax law.

According to the new circular, a competent authority's decision cannot prevail over a ruling issued by an Israeli court.

## Procedure for submitting the application to initiate a MAP

The taxpayer must submit an application to initiate a MAP within the period specified in the relevant tax treaty (usually 3 years), or within a reasonable time if no such period is specified, from the date of the first notification of the expected double taxation issue. In accordance with the new circular, an assessment issued to the taxpayer in Stage A, or a demand for tax withholding, constitutes a "first notice" in this respect, even though there may be ways to appeal or challenge these notices under domestic tax law.

Unlike the previous Execution Order, the new circular details the documents that must be submitted together with the MAP application, and requires the applicant to provide these documents to the competent authority. The new circular also determines the application's language (Hebrew and English) and lists the obligations that the applicant must meet (including the obligation to transfer additional documents as required by the competent authority).

## Processing the application

Upon receiving the application to initiate the MAP, the competent authority will examine the application. Once the competent authority has decided to conduct the MAP, it will do so independently and detached from the applicant. However, the Israeli competent authority may allow the applicant to present its arguments to both competent authorities at its discretion and in collaboration with the competent authority of the other contracting state.

After examining the MAP issue, the competent authority will inform the applicant and the assessment office of the results of the MAP. The new circular clarifies that if the competent authorities do not reach an agreement and the Israeli competent authority believes that the taxation in Israel is in compliance with the provisions of Israeli tax law and the relevant tax treaty, Israel need not prevent double taxation unilaterally. In the case where the competent authorities have reached an agreement, the applicant will be asked to notify them within 30 days (or within such time that was determined in the competent authority's notice) whether it consents to the results of the MAP or whether it disputes them. Failure to respond will be considered a rejection of the agreements between the competent authorities. If the applicant agrees to the agreement reached, the aforementioned agreement will be final, with no right to challenge or appeal. If it does not agree, the agreement between the competent authorities will not bind the states.

The new circular authorizes the competent authority to agree to apply the agreement between the competent authorities to the years beyond the scope of the MAP. Namely, the competent authorities can turn the MAP into a kind of advance pricing agreement (APA). Such an agreement can improve the taxpayer's situation and create certainty regarding its tax liability in the years to come, as long as it complies with the principles of the agreement.

# The MAP effect on assessment, administrative appeals, court appeals and collection procedures

A significant issue in the context of the MAP is the relationship between the MAP and the other assessment and appeal procedures. According to the ITA, the MAP is independent of the assessment. Therefore, the assessing officer can continue the assessment procedures simultaneously with the MAP. Administrative appeal procedures can also continue as usual, although, in some cases, the assessing officer will be required to coordinate its actions with the competent authority.

The new circular states that the existence of an assessment agreement does not negate the right of a taxpayer to request the opening of a MAP. However, it clarifies that, within the framework of the MAP, the existence of such an agreement will be taken into consideration.

The new circular also clarifies that a MAP will not take place simultaneously with an active court appeal. In some cases, the competent authority will recommend staying the court appeal proceedings, given an active MAP. However, the ITA reflects its position that the court appeal procedures must be stayed before the submission of the Arguments of Assessment by the ITA or after the submission of the arguments of appeal by the taxpayer, but not in the period between the submission of these two documents. In this context, it should be noted that, according to the new circular, the Israeli competent authority is not allowed to deviate from the rulings of the Israeli court in the case insofar as such rulings were given.

In addition, according to the new circular, the existence of a MAP does not detract from the authority of the ITA to initiate collection procedures in accordance with Israeli domestic law. In some cases, the ITA is authorized to demand guarantees for the payment of the disputed tax from the applicant before the MAP initiates and, in appropriate circumstances, even as the MAP is undergoing.

The new circular (Income Tax Circular No. 01/2023 on MAPs in the Treaties for the Prevention of Double Taxation) was published on 18 August 2023 and is available [here](#) (in Hebrew).

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