

Part III

Administrative, Procedural, and Miscellaneous

[26 CFR 1.482]: Internal Revenue Code §482: Allocation of income and deductions among taxpayers

Rev. Proc. 2004-40

TABLE OF CONTENTS

Section 1: Purpose .....

Section 2: Principles of the APA Program.....

Section 3: Prefiling Conferences.....

Section 4: Content of APA Requests.....

Section 5: Processing of APA Requests .....

Section 6: Competent Authority Consideration .....

Section 7: Rollback of TPM.....

Section 8: Small Business Taxpayer APAs .....

Section 9: Legal Effect of the APA.....

Section 10: Administering the APA .....

Section 11: Renewing the APA .....

Section 12: Disclosure .....

Section 13: Effect on Other Documents .....

Section 14: Effective Date .....

Section 15: Paperwork Reduction Act.....

Drafting Information.....

## SECTION 1: PURPOSE

.01 This revenue procedure explains the manner in which taxpayers may request an advance pricing agreement ("APA") from the APA Program within the Office of the Associate Chief Counsel (International), the manner in which such a request will be processed by the APA Program, and the effect and administration of APAs. This revenue procedure updates and supersedes Revenue Procedure 96-53, 1996-2 C.B. 375, and Notice 98-65, 1998-2 C.B. 803.

## SECTION 2: PRINCIPLES OF THE APA PROGRAM

.01 The APA Program provides a voluntary process whereby the Internal Revenue Service ("Service") and taxpayers may resolve transfer pricing issues under § 482 of the Internal Revenue Code ("Code"), the Income Tax Regulations ("the regulations") thereunder, and relevant income tax treaties to which the United States is a party in a principled and cooperative manner on a prospective basis. The APA process increases the efficiency of tax administration by encouraging taxpayers to come forward and present to the Service all the facts relevant to a proper transfer pricing analysis and to work towards a mutual agreement in a spirit of openness and cooperation. The prospective nature of APAs lessens the burden of compliance by giving taxpayers greater certainty regarding their transfer pricing methods, and promotes the principled resolution of these issues by allowing for their discussion and resolution in advance before the consequences of such resolution are fully known to taxpayers and the Service.

.02 The APA Program's central goal is the prompt, proper, and fair resolution of APA requests and renewals consistent with the principles of sound tax administration.

.03 The APA Program reserves the right not to accept an APA request or to terminate consideration of an APA request if the request or the continued development of the case is contrary to the principles of sound tax administration.

.04 An APA is an agreement between a taxpayer and the Service in which the parties set forth, in advance of controlled transactions, the best transfer pricing method ("TPM") within the meaning of § 482 of the Code and the regulations. The agreement specifies the controlled transactions or transfers ("covered transactions"), TPM, APA term, operational and compliance provisions, appropriate adjustments, critical assumptions regarding future events, required APA records, and annual reporting responsibilities.

- (1) APAs are intended to supplement traditional administrative, judicial, and

treaty mechanisms for resolving transfer pricing issues.

- (2) Taxpayers formally initiate the process for APAs. Thereafter, APAs require discussions among the taxpayer, one or more associated enterprises, and one or more tax administrations, including the Service.
- (3) Ordinarily, an APA is reached only on the proposed covered transactions. In some cases, however, the APA Program may require that the scope of the proposed covered transactions be expanded or contracted, or may determine that the TPM proposed by the taxpayer is not appropriate for some subset of the proposed covered transactions.

.05 The taxpayer's participation in the APA process is entirely voluntary. In some cases, the Service may approach a taxpayer to discuss the advantages of an APA.

.06 The APA Program is under the immediate supervision of a Director (the "APA Director") within the Office of the Associate Chief Counsel (International). The APA Director reports to the Associate Chief Counsel (International) who exercises general oversight over the APA Program. The APA Director, directly or by delegation, may take any action – not contrary to statute, regulation, or treaty – necessary to carry out the provisions of this revenue procedure. The APA Director may modify the provisions contained in this revenue procedure (for example, time limits, or content of an APA request), if that modification would be consistent with sound tax administration.

.07 Under the APA request procedure, the taxpayer proposes a TPM and provides data intended to show that the TPM constitutes the appropriate application of the best method rule under the § 482 regulations. The Service through an APA Team evaluates the APA request by analyzing all relevant data and information submitted with the initial request and at any time thereafter.

.08 Taxpayers may request a bilateral, multilateral, or, if appropriate, a unilateral APA. A bilateral or multilateral APA involves a request for an APA between the taxpayer and the Service, accompanied by a request for a mutual agreement between relevant competent authorities. A unilateral APA involves only an agreement between the taxpayer and the Service. Where possible, in the interest of sound tax administration and to ensure that no potential for double taxation results from an APA, an APA should be concluded on a bilateral or multilateral basis between the competent authorities through the mutual agreement procedure of the relevant treaty.

.09 In a bilateral or multilateral case, the APA Program prepares a recommended negotiating position for the U.S. Competent Authority. The negotiating

position serves as a basis for discussions with the relevant foreign competent authority or authorities under the mutual agreement article of the applicable income tax treaty or treaties. Prior to finalizing its recommendation, the APA Program through the Team Leader (see section 5.03) conveys the substance of the APA Team's position to the taxpayer to provide an opportunity for the taxpayer to comment. The Team Leader, in coordination with other members of the APA Team, considers the merits of the taxpayer's timely received comments in finalizing the recommended position.

.10 If the U.S. Competent Authority and the relevant foreign competent authority or authorities reach a mutual agreement, the taxpayer and the Service may execute one or more APAs consistent with that mutual agreement.

.11 The APA Policy Board establishes policy on matters of substantial general importance pertaining to the APA Program. It consists of the Associate Chief Counsel (International), the APA Director, the Director, International (Large and Mid-Size Business (LMSB) Operating Division), Treasury's International Tax Counsel, and other senior officials.

.12 In appropriate cases, the TPM may be applied to tax years prior to those covered by the APA ("rollback" of the TPM, see section 7). The Service's policy is to use rollbacks whenever feasible based on the consistency of the facts, law, and available records for the prior years. This policy does not apply to unilateral APA requests in which a rollback would decrease taxable income on a return filed for a taxable year not covered by the APA (see § 1.482-1(a)(3)).

.13 Filing an APA request does not suspend any examination or other enforcement proceedings. The APA Program will coordinate its activities with those of other Service proceedings to avoid duplicative information requests to the taxpayer, enhance the efficiency of Service operations, and reduce overall taxpayer compliance burdens.

### SECTION 3: PREFILING CONFERENCES

#### .01 *General Principles*

A taxpayer may request a prefiling conference ("PFC") with the APA Program to discuss informally the suitability of an APA.

#### .02 *Discussion Topics*

The taxpayer may use a PFC to clarify what information, documentation, and analyses are

likely to be necessary for the Service to consider an APA request. Among the areas of discussion are the covered transactions, the potentially applicable TPMs, the probability of agreement among the competent authorities, and the APA Program's schedule and method for coordinating and evaluating the request. To provide for the efficient use of taxpayer resources, PFCs are recommended in order to ensure that the APA request is appropriate and focuses on relevant issues.

*.03 Scheduling*

A taxpayer or its representative may contact the APA Program Office in Washington, D.C. or California to schedule a PFC. The taxpayer or its representative should propose three alternative dates, and should generally allow two weeks before the first proposed date. The telephone and facsimile numbers are:

	<u>Washington, DC</u>	<u>California</u>
voice:	(202) 435-5220	(949) 360-3486
facsimile:	(202) 435-5238	(949) 360-3446

*.04 PFC May be Named or Anonymous*

The taxpayer may request a PFC either on an identified or anonymous basis.

*.05 Participation*

If a taxpayer identifies itself, representatives of the Service Operating Division with responsibility for the taxpayer's return normally will participate in the PFC. Representatives from Appeals and the Division Counsel field offices may also attend. In the case of a PFC regarding a bilateral APA request, a Competent Authority analyst may attend. If a taxpayer initially requests a PFC on an anonymous basis but prior to the meeting chooses to identify itself, the meeting may be rescheduled to permit necessary personnel to attend. When requesting a PFC on an identified basis, the taxpayer must inform the APA Program whether transactions similar or related to those to be covered by the proposed APA are currently under consideration by a Service Operating Division, Appeals, Division Counsel, or Associate Chief Counsel.

*.06 Prefiling Submission*

A taxpayer must send a brief prefiling submission to the relevant APA Program Office in Washington, D.C. or California that lists the persons attending the PFC for the taxpayer (first names only, pseudonyms, or job titles are sufficient if on an anonymous basis) and that outlines and describes the issues to be discussed. This brief submission should be

provided at least one week in advance of the PFC. If the document is twenty pages or less, it may be sent by facsimile; but if it exceeds twenty pages, eight copies (or if anonymous, only three copies) and one original should be delivered.

#### SECTION 4: CONTENT OF APA REQUESTS

##### *.01 General Principles*

- (1) For purposes of requesting an APA, each taxpayer that is a member of a consolidated group (as defined in Treasury Regulations §1.1502-1) must comply with the provisions of § 1.1502-77.
- (2) All materials submitted with the APA request become part of the APA Program's case file and will not be returned. Therefore, the taxpayer's original documents should not be submitted.
- (3) The taxpayer must submit copies of any documents relating to the proposed TPM. All materials submitted must be properly labeled, indexed, and referenced in the request. Any previously submitted documents that the taxpayer wishes to associate with the request must be referenced.
- (4) The APA request must include a comprehensive table of contents.
- (5) If the records or documents to be submitted are too voluminous for transmittal with the request, the taxpayer must describe the contents of such items in the request and confirm that the items will promptly be made available upon request.
- (6) All documents submitted in a foreign language must be accompanied by an accurate English translation.
- (7) All documents in the APA request that are available in electronic format should be submitted, on either a CD-ROM or diskette, along with the paper submission. Suitable formats include Microsoft Word, Excel, PowerPoint, and Adobe Portable Document Format. Other formats may be arranged on a case-by-case basis.
- (8) The user fee should be submitted at the same time as the request, unless previously submitted. The taxpayer should also provide a justification of the user fee amount with a demonstration of its calculation. See sections 4.11 and 4.12.

- (9) The APA request should provide all information reasonably necessary to permit the APA Program to evaluate fully the taxpayer's proposed TPM. Failure by a taxpayer to provide all materials required by this revenue procedure in its APA request, or requested by the APA Program during the negotiation process, may result in rejection of the APA.
- (10) The taxpayer must describe in detail in its APA request the transactions it intends to cover under the APA and, if applicable, how those transactions relate in context to other related party transactions that the taxpayer does not intend to cover.
- (11) If the APA request is unilateral and involves transactions with an entity in a treaty jurisdiction, the taxpayer must provide an explanation of why the request is not bilateral.
- (12) The taxpayer is under a duty to supplement its APA submission to correct and/or to update all material facts and information in its APA submission or in any supporting documentation. This supplemental submission (or submissions) must be made within 30 days of request by the APA Program and, in any event, prior to the commencement of Competent Authority negotiations (in the case of a bilateral or multilateral APA) and execution of the APA (in all cases).

*.02 Explanation of the Proposed TPM*

- (1) The taxpayer must provide a detailed explanation and analysis of why the proposed TPM is the best method within the meaning of § 1.482-1(c).
- (2) The request should illustrate application of each proposed TPM by applying it, in a consistent format, to the prior three taxable years' financial and tax data of the parties to the covered transactions. If historical data cannot be used to illustrate a TPM (for example, when the TPM applies to a new product or business), the request should include an illustration based on projected or hypothetical data, as well as a description of the source of the data. If coverage of three taxable years is inappropriate for any reason, the taxpayer should provide data for an appropriate period and explain why the period was chosen.
- (3) If a taxable year is completed while the APA is pending, the taxpayer must update its APA submission within 120 days following the close of the taxable

year by demonstrating the application of the proposed TPM to its actual financial results for that year.

*.03 Factual and Legal Items for All Proposed APAs*

The detailed information supporting the APA request should be tailored to the specific facts relating to the taxpayer, the proposed covered transactions, and relevant legal authority. It should also take into account discussions with the APA Program in a PFC. Unless otherwise agreed, each request must include, in addition to any other items specified in this revenue procedure, the following items:

- (1) The names, addresses, telephone and facsimile numbers, taxpayer identification numbers (if applicable), and both the Standard Industrial Classification (SIC) and the North American Industry Classification System (NAICS) codes reported on the most recently filed federal tax returns (if applicable) of (a) the organizations, trades, and businesses engaging in the proposed covered transactions, and (b) the controlling taxpayer of the parties, if the controlling taxpayer is not itself engaging in the proposed covered transactions.
- (2) The controlling taxpayer's industry (for example, Heavy Manufacturing and Transportation) within LMSB; or if the taxpayer files its tax returns with the Small Business/Self-Employed (SB/SE) Operating Division, a statement to that effect.
- (3) A properly completed Form 2848 (Power of Attorney and Declaration of Representative) for any person authorized to represent the taxpayer in connection with the request, disregarding if appropriate the line 3 instruction limiting the authorization to three future tax periods. If the taxpayer or the taxpayer's authorized representative retains any other person (for example, a law firm, accounting firm, or economic consulting firm) to assist the taxpayer in pursuing the APA request, such taxpayer must also provide a separate written authorization for disclosures to the person and such person's employees during the APA Team's consideration of the request, according to the instructions in § 301.6103(c)-1T (see also, T.D. 9011, 31 C.F.R. Part 10 (July 26, 2002)). Such written authorization may be made by completing Form 8821 (Tax Information Authorization), disregarding, if appropriate, the line 3 instruction limiting the authorization to three future tax periods.
- (4) A description of the general history of business operations, worldwide organizational structure, ownership, capitalization, financial arrangements,



principal businesses, the place or places where such businesses are conducted, and major transaction flows of the parties to the proposed covered transactions. The description must also identify any branches or entities disregarded for tax purposes (see § 301.7701-3) that are involved in the proposed covered transactions.

- (5) A description and analysis of the transactions covered by the APA request, as well as the estimated dollar value of each of the proposed covered transactions for each year of the proposed term of the APA.
- (6) A statement whether the tested party has commission sales income. If the APA request involves commission income, the taxpayer must propose and analyze whether, under the facts and circumstances, it is appropriate to: (a) cover the commission sales income, but separately test it; (b) segregate the commission sales income and exclude it from the APA; (c) propose a TPM consistent with a sales function; or, (d) adjust the financial statement data and results to account for the functional differences between commission sales transactions and buy-sell transactions.
- (7) For each party to the proposed covered transactions, a detailed analysis of:
  - (a) the functions and economic activities performed;
  - (b) the assets employed;
  - (c) the economic costs incurred;
  - (d) the risks assumed;
  - (e) relevant contractual terms;
  - (f) relevant economic conditions; and
  - (g) relevant non-recognition transactions.
- (8) Representative financial and tax data of the parties to the proposed covered transactions for the last three taxable years (or more years if relevant to the proposed TPM), together with other pertinent data and documents in support of the TPM. This item may include (but need not be limited to) data from the following:
  - (a) Form 5471 (Information Return of U.S. Persons With Respect to

Certain Foreign Corporations);

- (b) Form 5472 (Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business);
  - (c) income tax returns;
  - (d) financial statements;
  - (e) annual reports to stockholders;
  - (f) other pertinent U.S. and foreign government filings (for example, customs reports or SEC filings);
  - (g) existing pricing, distribution, or licensing agreements;
  - (h) marketing and financial studies;
  - (i) documentation prepared in consideration of § 6662(e); and
  - (j) company-wide accounting procedures, budgets, projections, business plans, and worldwide product line or business segment profitability reports.
- (9) The functional currency of the parties to the proposed covered transactions and their foreign currency exchange risk.
- (10) The taxable year of each party to the proposed covered transactions.
- (11) A description of significant financial accounting methods employed by the parties that have a bearing on the proposed TPM.
- (12) An explanation of any relevant financial and tax accounting differences between the U.S. and the foreign countries involved.
- (13) A discussion of any relevant statutory provisions, tax treaties, court decisions, regulations, revenue rulings, or revenue procedures that relate to the appropriateness of the proposed TPM for the requested APA. For cases in which the taxpayer requests a rollback, the discussion should include a statement whether the period of limitations for the rollback years has expired in the U.S. or foreign countries, and if not, when the periods of

limitations do expire.

- (14) (a) A statement describing all previous and current issues at the examination, Appeals, judicial, or competent authority levels that relate to the proposed TPM, including an explanation of the taxpayer's and the government's positions and any resolution of the issues.
- (b) If the taxpayer is requesting a rollback that involves any issues relevant to the proposed covered transactions that are unresolved and still under consideration by Appeals, the taxpayer must include with its APA request a waiver of its right to be present during communications between the Appeals Office and the APA Team members (as described in section 5.04). See Rev. Proc. 2000-43, 2000-2 C.B. 404. The following language satisfies this requirement:

Waiver of Ex Parte Communication: [Name of taxpayer(s)] agrees to the participation of the Appeals Office in the consideration of this APA request, and hereby waives its right to be present during, or participate in, communications related to the APA request or the proposed covered transactions between the Appeals Office and the APA Team members.

- (15) A statement describing any APAs with, or rulings by, foreign tax authorities relating to the proposed covered transactions (or any pending requests for such APAs or rulings) and, if requested, copies of such APAs or rulings.
- (16) An economic analysis or study of the general industry pricing practices and economic functions performed within the markets and geographical areas covered by the APA request.
- (17) A list of the taxpayer's competitors and a discussion of any uncontrolled transactions, lines of business or types of businesses comparable or similar to those addressed in the request.
- (18) A detailed presentation of the research efforts and criteria used to identify and select possible independent comparables. This presentation should include a list of potential comparables and an explanation of why each was either accepted or rejected. The taxpayer may request an APA even though no comparable uncontrolled prices, transactions, or companies can be identified. In such cases, a taxpayer must demonstrate that the proposed TPM otherwise satisfies the requirements of § 482 and this revenue procedure.

- (19) Detailed financial data (and licenses or other agreements, if applicable) on the selected independent comparables in print and electronic formats. For example, if the proposed TPM uses the comparable uncontrolled price (CUP) method, the comparable pricing information should be included; for the comparable uncontrolled transaction (CUT) method, the comparable license agreements should be included; and for the comparable profits method (CPM), the annual and multiple year period results using the selected profit level indicator should be included.
  - (a) The taxpayer should be prepared to update the comparables data, if requested, following 90 days after the close of its fiscal year.
  - (b) In addition, if pertinent, the taxpayer should demonstrate consideration of alternative measurements of profitability and return on investment (for example, gross profit margin or markup, ratio of gross income to total operating expenses, net operating profit margin, or return on assets).
- (20) A detailed explanation of any adjustments to the selected comparables, such as accounting for product line segregations, differences in accounting practices, functional differences relating to activities performed, assets employed, risks assumed, costs incurred, volume or scale differences, and differing economic and market conditions.

#### *.04 Specific Items for a Cost Sharing Arrangement*

In addition to the items in section 4.03, an APA request related to a cost sharing arrangement (“CSA”) must include:

- (1) A copy of the CSA and a statement that the CSA conforms with the requirements of §1.482-7(b).
- (2) A specific description of intangible development costs for all participants under the CSA. Such description should include a description of the costs included and excluded (for example, costs of technology acquired from third parties; the treatment of stock-based compensation under the CSA; non-product specific development costs; costs associated with abandoned projects; costs associated with specific stages of product development; relevant labor, material, and overhead costs; and support and administrative costs); a description of any services performed for participants that will be included in intangible development costs (for example, contract research)

and how those services would be taken into account; and, for a representative period, a breakdown of total costs incurred, and the costs borne by each participant, according to the CSA.

- (3) The basis (as described in § 1.482-7(f)(3)(ii)) used to measure anticipated benefits, the projections used to estimate benefits, and why such basis and projections yield the most reliable estimate of reasonably anticipated benefits.
- (4) The method used to calculate each participant's share of intangible development costs; the reason why that method can reasonably be expected to reflect that participant's share of anticipated benefits; and a statement of the circumstances under which the participants' shares of intangible development costs will be adjusted to account for changes in economic conditions, business operations and practices, and the ongoing development of intangibles under the CSA.
- (5) The accounting method used to determine the costs and benefits of the intangible development (including the method used to translate foreign currencies).
- (6) Each participant's sales, cost of sales, operating expenses, research and development costs, and operating profit (historical for the five most recently completed taxable years and projected for two taxable years) with regard to the product area covered by the CSA.
- (7) A description of any amounts to be received from nonparticipants for the use of covered intangibles (for example, as a royalty pursuant to a license agreement) and how the participants would take into account such amounts.
- (8) Representative internal manuals, directives, guidelines, and similar documents prepared for purposes of implementing or operating the CSA (for example, research and development committee meeting minutes, market studies, economic impact analyses, capital expenditure budgets, engineering studies, reports and studies of trends and profitability in the industry, and financial analyses for financing and cash flow purposes).
- (9) A description of any prior research undertaken in the intangible development area; the amount of any buy-in or buy-out payment (as defined in §1.482-7(g)(2)); a complete economic analysis to support the payment; the method used to determine the amount of the payment (that is, the method used to value the pre-existing intangible property and to calculate any royalty, lump

sum, or installment payments); and an analysis demonstrating that the method used constitutes the best method under §1.482-1(c).

- (10) The treatment of cost sharing and buy-in or buy-out payments for U.S. income tax purposes (for example, the source and character of those payments).
- (11) Evidence of the participants' compliance with the reporting requirements under §1.482-7(j) of the cost sharing regulations.
- (12) Taxpayers requesting an APA that covers a CSA but does not cover the related buy-in transaction, or an APA that covers a buy-in transaction but does not cover the related CSA, must provide the reasons why an APA limited in this manner is consistent with the principles of the APA process, as set forth in this revenue procedure. The APA Program will evaluate the requests to ensure their consistency with the principles of this revenue procedure and sound tax administration. If an APA request is limited to covering only buy-in payments, the APA must include the critical assumption that the CSA to which the buy-in payments relate meets the § 482 regulatory requirements for CSAs.

#### *.05 Critical Assumptions*

The taxpayer should propose and describe any relevant critical assumptions. A critical assumption is any fact the continued existence of which is material to the taxpayer's proposed TPM whether related to the taxpayer, a third party, an industry, or business and economic conditions. Critical assumptions might include, for example, a particular mode of conducting business operations, a particular corporate or business structure, a range of expected business volume, or the relative value of foreign currencies.

#### *.06 Contents of Annual Report*

Section 10.01 provides that the taxpayer must file an annual report for each taxable year covered by the APA. The taxpayer should propose in the request a list of items to be included in each report. Consideration should be given to all items listed in Appendix C to the APA Program's current Model APA (see Announcement 2004-26, 2004-15 I.R.B. 743, 768).

#### *.07 Term*

- (1) The taxpayer must propose a term for the APA appropriate to the industry,

products, and transactions involved. Although the appropriate APA term is determined on a case-by-case basis, a request for an APA should propose an APA term of at least five years unless the taxpayer states a compelling reason for a shorter term. Additionally, the APA Program strives to have at least three prospective years remaining in the term upon the execution of an APA (in the case of a unilateral APA) or completion of the APA Program's recommended negotiating position for Competent Authority (in the case of a bilateral or multilateral APA), except in unusual circumstances. Accordingly, taxpayers should anticipate that the APA Program may require their agreement to extend the proposed term of an APA if necessary to ensure such prospectivity.

- (2) The taxpayer must file its APA request within the time prescribed by statute (including extensions) for filing its Federal income tax return for the first proposed APA year. An APA request will be considered filed on the date the required user fee is paid (within the meaning of § 7502(a)), provided that a substantially complete APA request is filed with the APA Program within 120 days of the return due date (including extensions) for the first proposed APA year. Because of the need to begin the processing of the APA request in a manner that ensures appropriate prospectivity, the APA Director will consider extending the 120 day period pursuant to section 2.06 only in unusual circumstances. In the event the APA Program's evaluation of an APA request is delayed due to a lack of responsiveness or timeliness by the taxpayer subsequent to the filing of its request, the APA Director may deem the taxpayer's APA request to have been filed for purposes of this paragraph on a date subsequent to its actual filing.

#### *.08 Request for Competent Authority Consideration*

- (1) The taxpayer must state whether any of the parties to the proposed covered transactions are residents of or conduct activities in a treaty partner country or U.S. possession, and whether the taxpayer proposes an agreement among competent authorities (see section 6 for guidelines). For purposes of this revenue procedure, "competent authority" includes the Director, International (LMSB) and designated foreign competent authorities under income tax treaties to which the U.S. is a party, and also includes the Director, International (LMSB) acting as the U.S. Competent Authority with respect to a possession tax agency described in Rev. Proc. 89-8, 1989-1 C.B. 778, as well as a designated possession tax official within the meaning of that revenue procedure.

- (2) If the taxpayer requests a bilateral or multilateral APA, the taxpayer's request must include the information described in section 4.05(a) and (b) and, in a separate document, section 4.05(n), of Rev. Proc. 2002-52, 2002-2 C.B. 242 (or its successor), or similar information pursuant to a request for relief under Rev. Proc. 89-8. The following wording satisfies section 4.05(n) of Rev. Proc. 2002-52:

[Name of taxpayer(s)] consents to the disclosure to the competent authority of [name of foreign country] and the competent authority's staff of any or all of the items of information set forth or enclosed in the [bilateral/multilateral] APA request for the taxable year(s) \_\_\_\_\_ [and accompanying rollback request for relief from economic double taxation of income for the taxable years \_\_\_\_\_], and any further submissions, within the limits contained in the [name of treaty].

*.09 Perjury Statement*

- (1) The taxpayer must include in any APA request and supplemental submission a declaration in the following form:

Under penalties of perjury, I declare that I have examined this [APA request] [supplemental submission relating to this APA request] including accompanying documents, and, to the best of my knowledge and belief, the [APA request] [supplemental submission] contains all the relevant facts relating to the [APA request] [supplemental submission], and such facts are true, correct, and complete.

- (2) The declaration must be signed by the person or persons on whose behalf the request is being made and not by the taxpayer's representative. The person signing for a corporate taxpayer must be an authorized officer of the taxpayer who has personal knowledge of the facts, whose duties are not limited to obtaining letter rulings or determination letters from the Service, or negotiating APAs, and who is authorized to sign the taxpayer's income tax return pursuant to § 6062. The person signing for any other person must be an individual who has personal knowledge of the facts, and who is authorized to sign in accordance with §§ 6061 or 6063, as applicable.
- (3) While the APA request is pending and after it is executed, a taxpayer is under a duty to timely supplement its disclosures if the taxpayer discovers that in some material respect the information provided was incomplete, inaccurate, or incorrect, or that the facts or business practices as described



in the materials or statements submitted in support of the APA request have changed or will change. Failure to do so may be considered fraud, malfeasance, or misrepresentation with respect to a material fact, or failure to state a material fact.

*.10 Signatures*

The taxpayer or the taxpayer's authorized representative must sign the APA request. If an authorized representative is to sign, the taxpayer and representative must satisfy the relevant instructions on signatures in Rev. Proc. 2004-1, 2004-1 I.R.B. 1 (or its successor).

*.11 Mailing, Deliveries, Copies, and Office Location*

- (1) User fees (accompanied by an identifying cover letter) must be sent to:

Internal Revenue Service  
Attn: CC:DOM:CORP:T  
P.O. Box 7604  
Ben Franklin Station  
Washington, D.C. 20044

The fee payment may also be hand delivered to the drop box at the 12th Street entrance of 1111 Constitution Avenue, N.W., Washington, DC.

- (2) All other communications must be mailed or delivered as follows (unless arranged otherwise, for example, mailing to the California office):

Office of Associate Chief Counsel (International)  
Advance Pricing Agreement Program  
Attn: CC:INTL:APA; MA2-266  
1111 Constitution Avenue, N.W.  
Washington, D.C. 20224

- (3) The taxpayer must provide the original and eight copies of its APA request and any supplemental materials submitted while the request is pending.

- (4) The APA Program is located at:

799 9th Street, N.W.  
Washington, D.C. 20001

.12 *User Fees.*

- (1) The following general principles apply to user fees for APA requests.
  - (a) A separate user fee is required for each APA request.
  - (b) A separate APA request concerns a specific TPM and distinct facts, such that a review of the facts will determine the suitability of the TPM and all other methodologies under consideration.
  - (c) A single filing may include more than one APA request and may require more than one user fee. A reduced user fee will apply to additional APA requests. The maximum user fee for any filing involving more than one APA request is \$50,000.
  - (d) User fees are made payable to the United States Treasury.
  - (e) For user fee purposes, a multilateral APA request will normally be considered as multiple bilateral APA requests. The user fee for the first bilateral request will be determined under the principles of section 4.12(2). The user fee for the other foreign jurisdictions will be treated as additional bilateral requests to which a reduced user fee will apply.
  - (f) A unilateral APA request will normally be considered as only one APA request even though it may involve a pricing issue in more than one foreign jurisdiction. If separate analyses are required for each foreign jurisdiction, the unilateral APA request may be treated as multiple APA requests for which reduced user fees will apply to the additional requests.
  - (g) For purposes of determining the applicable user fee in accordance with section 4.12(2), the gross income of a taxpayer includes the gross income of all organizations, trades, or businesses owned or controlled directly or indirectly by the same interests controlling the taxpayer. Gross income must be computed for the last full (12 month) taxable year ending before the date the taxpayer filed the APA request. If the information on the taxpayer's gross income for the last full taxable year is not available, the taxpayer must use its projected gross income for the first year of the APA term.
  - (h) The APA Director may request an additional user fee after

submission of an APA request if the request does not meet the criteria for the user fee amount initially paid by the taxpayer. The taxpayer may either pay the additional fee and continue the APA process or withdraw the request.

- (i) If a taxpayer requests substantial changes to the originally proposed TPM or proposed covered transactions during the processing of the APA request, the APA Director may consider the request an entirely new APA request and an additional user fee may be required. Generally, no additional user fee will be imposed if substantial changes are requested by the Service or by a foreign competent authority.
- (2) The following user fees apply to APA requests.
- (a) The user fee for an original APA request or a non-routine renewal from a taxpayer with gross income of \$1 billion or more is \$25,000, and each additional separate request is \$7,500.
  - (b) The user fee for an original APA request or a non-routine renewal from a taxpayer with gross income of at least \$200 million and less than \$1 billion is \$15,000, and each additional separate request is \$7,500.
  - (c) The user fee for each separate APA request or renewal request from a taxpayer with gross income of less than \$200 million is \$5,000.
  - (d) The user fee for the request for a routine APA renewal (that is, where the material facts, critical assumptions, and proposed TPM have not substantially changed) from a taxpayer with gross income of at least \$200 million is \$7,500.
  - (e) If the taxpayer's gross income is at least \$200 million, but the transaction or transactions in the APA request involve either (i) tangible property and/or services with a total annual value not in excess of \$50 million, or (ii) payments for intangible property not in excess of \$10 million annually, the user fee for each separate APA request or renewal is \$5,000 ("small transactions").
  - (f) The following chart summarizes the above user fees:

Taxpayer's Gross Income or Transactions	Original Request or Non-Routine Renewal	Each Additional Separate Request	Routine Renewal
\$1 billion or more	\$25,000	\$7,500	\$7,500
\$200 million to \$1 billion	\$15,000	\$7,500	\$7,500
Less than \$200 million	\$5,000	\$5,000	\$5,000
Small Transactions	\$5,000	\$5,000	\$5,000

## SECTION 5: PROCESSING OF APA REQUESTS

### .01 *General*

The time for processing an APA request follows one of two paths, depending on whether the request is for a bilateral or multilateral APA, or for a unilateral APA. The scheduling of due diligence, analysis, discussion, agreement, and drafting is designed to complete the recommended U.S. negotiating position (bilateral or multilateral APA request), or a unilateral APA, within 12 months from the date the full request was filed. The filing of a full APA request includes not only the payment of a user fee, but also the receipt by the APA Program of the materials specified in sections 4.01 through 4.10. Significant factual analysis of the APA request will not begin until a full request has been filed.

### .02 *Initial Contact*

After receiving an APA request, a representative of the APA Program will contact the taxpayer or representative to discuss any preliminary questions the APA Program may have, or to ask for any additional information or documents necessary in order to initiate processing of the request. Additional information and documents must be supplied by the date specified by the APA Program, as extended for good cause, accompanied by the perjury statement as set forth in section 4.09.

### .03 *Designation of Team Leader*

Shortly after receiving the taxpayer's APA request and any required user fees, the APA Director will appoint a Team Leader to review the request. If a prefiling conference was held with the taxpayer, the Team Leader generally will be appointed from among the APA Program staff attending the prefiling conference. The Team Leader will oversee the APA Team's activities in processing the APA request.

#### *.04 Formation of APA Team*

The Team Leader will organize the APA Team, which normally consists of the following personnel: the Team Leader, an APA Program economist and/or a Service Operating Division economist, an LMSB international examiner, a Division Counsel attorney, and a competent authority analyst in bilateral cases. In appropriate cases, the international examiner's manager and other Service Operating Division personnel familiar with the taxpayer may participate in the APA Team. If the APA may affect taxable years in Appeals, the appropriate Appeals Officer will be invited to participate. The APA Team Leader will assure that copies of the APA request are distributed to all Team members for review.

#### *.05 Function of APA Team*

The function of the APA Team is the following: (1) for a bilateral or multilateral APA, to develop, in consultation with the taxpayer and consistent with sound tax administration, a competent authority negotiating position that it can recommend for approval, and (2) for a unilateral APA, to make best efforts, consistent with sound tax administration, to develop an APA that it can recommend for approval by the Associate Chief Counsel (International). The Service Operating Division field office responsible for the taxpayer's income tax return will be provided an opportunity to review and comment on the recommended U.S. competent authority negotiating position in the case of a bilateral or multilateral APA, and the proposed APA in the case of a unilateral APA.

#### *.06 Due Diligence and Analysis*

The APA Team will evaluate the taxpayer's APA request by discussing it with the taxpayer, verifying the data supplied, and requesting additional supporting data if necessary. The evaluation of the request will not constitute an examination or inspection of the taxpayer's books and records under § 7605(b) or other provisions of the Code.

#### *.07 Schedule for Discussion and Drafting*

- (1) The APA Team will arrange with the taxpayer for an initial meeting to take place within 45 days from the assignment of an APA Team Leader (and following receipt of the APA request). The function of the initial meeting is to review the taxpayer's facts, to discuss and clarify issues, and to reach agreement on the scope and nature of the APA Team's due diligence.
- (2) In connection with the initial meeting, the APA Team and the taxpayer will

agree on a Case Plan, to which both Service and taxpayer personnel will be expected to adhere. The Case Plan may identify issues raised by the APA Team's initial review of the APA request. Firm dates should be agreed upon for resolving all outstanding issues, and case milestones should be cited. Case milestones include: (a) submission of any necessary additional information by the taxpayer; (b) any planned site visits or interviews; (c) evaluation of the information by the Service; (d) negotiation dates; and (e) presentation of the competent authority negotiating position or recommended agreement to the APA Director. To minimize delays caused by the need to coordinate different parties' schedules on short notice, the time and place of future meetings required for any steps in the case should be agreed upon at the initial meeting and established in the Case Plan.

- (3) The time scheduled for completion of the case milestones will depend to some extent on the scope and complexity of the particular case. In the case of bilateral or multilateral requests, the Service will seek to work with the competent authority of the treaty partner or the U.S. possession involved to minimize the time needed for competent authority resolution.
- (4) Failures to meet case milestones will be addressed promptly. The APA Director will assist in remedying any difficulties to ensure a course of action to meet case milestones. Substantial or persistent failure by the taxpayer to comply with the Case Plan may be treated by the APA Program as a withdrawal of the APA request. In this event, if the taxpayer wishes to continue to pursue the APA, it must refile the request and pay a new user fee.
- (5) In some circumstances, development of the case will suggest to both the APA Team and the taxpayer that they adjust some milestone dates. To preserve flexibility, the APA Team and the taxpayer may amend the Case Plan by mutual agreement, consistent with the need to complete the case expeditiously.

#### *.08 Execution*

Signature of an APA by the APA Director and the taxpayer will constitute agreement to the APA. For purposes of executing the APA, each taxpayer that is a member of a consolidated group (as defined in § 1.1502-1) must comply with the provisions of § 1.1502-77. The person signing the APA request on behalf of the taxpayer must satisfy the requirements of section 4.09(2).

*.09 Withdrawing the Request*

The taxpayer may withdraw the request at any time before the execution of the APA. The user fee generally will not be refunded if the taxpayer withdraws its APA request after the due diligence process has been initiated.

*.10 Rejecting the Request*

The APA Program may decline either to accept any APA request or to execute any APA after a request has been accepted. If the APA Program declines to execute an APA after the due diligence process has been initiated, the Service normally will retain the user fee, although the fee may be returned if the APA Program determines that such action would be appropriate under the circumstances. If the APA Program proposes to reject an APA request, the taxpayer will be granted one conference of right with the APA Director. Other conferences may be granted at the APA Director's discretion.

**SECTION 6:           COMPETENT AUTHORITY CONSIDERATION**

*.01*           When any of the parties to a request are entitled to obtain assistance under the mutual agreement provision of a tax treaty between a foreign country and the United States, or under Rev. Proc. 89-8, the competent authorities may enter into agreements concerning the APA. Requests similar to APA requests that are initiated through treaty partners or possession tax agencies and submitted to the U.S. competent authority will be processed under this revenue procedure and Rev. Proc. 2002-52, as appropriate. In order to provide timely clarification of factual issues, minimize the potential for miscommunication, and assist in development of a multiple party agreement on a timely basis, the Service will generally initiate coordination among the taxpayer, the Service, and the competent authorities of treaty partners at the earliest possible stage of consideration of an APA request including, where possible, the prefiling stage. In this manner, the U.S. and foreign competent authorities can develop a joint understanding of the case, which should facilitate negotiation and resolution of competent authority issues. The taxpayer should remain available throughout consideration of the request to assist the Service in reaching agreement with the foreign competent authority. Final agreement to the negotiated APA will be sought among the taxpayer, the Service, and the foreign competent authority. As a general matter, the taxpayer should submit APA requests and related correspondence simultaneously to the Service and to foreign competent authorities involved in the requests.

*.02*           The purpose of a competent authority agreement is to avoid double taxation or taxation not in accordance with the relevant income tax treaty. If such an agreement is not acceptable to the taxpayer, the taxpayer may withdraw the APA request (see section

5.09). If the competent authorities are unable to reach an agreement, the taxpayer may withdraw its request or, at its discretion, the Service may negotiate and enter into a unilateral APA with the taxpayer (see section 6.06).

.03 The taxpayer must cooperate with the Service and the U.S. competent authority, pursuant to the standards set forth in Rev. Proc. 2002-52 and any other applicable revenue procedures.

.04 Taxpayers have an affirmative obligation to identify relevant concerns that may impact competent authority negotiation of an APA request. For example, it may be necessary for the Service to request sensitive confidential data (including material that may constitute a trade secret), which if disclosed, could harm the taxpayer's competitive position. If the taxpayer identifies such sensitive information, the Service will work with the taxpayer in developing a mechanism to permit consideration or verification by the treaty partner of the information while still preserving its confidentiality.

.05 When the competent authorities enter into an agreement covering an APA, the Service will, to the extent appropriate, agree to a mutual exchange of information with the foreign competent authority concerning any subsequent modifications, cancellation, revocation, requests to renew, evaluation of annual reports, or examination of the taxpayer's compliance with the terms and conditions of the APA. Bilateral APAs may provide for simultaneous filing of the annual report with the Service and with the foreign tax administration.

.06 To minimize taxpayer and governmental uncertainty and administrative cost, bilateral or multilateral APAs generally are preferable to unilateral APAs when competent authority procedures are available with respect to the foreign country or countries involved. In appropriate circumstances, however, the Service may execute an APA with a taxpayer without reaching a competent authority agreement. The taxpayer must show sufficient justification for a unilateral APA. In some circumstances, procedures agreed upon with particular foreign competent authorities, or the requirements of proper relations with treaty partners, may preclude unilateral APAs.

.07 Section 7.05 of Rev. Proc. 2002-52 provides in part that, if a taxpayer reaches a settlement on an issue pursuant to a written agreement, the U.S. competent authority will endeavor only to obtain a correlative adjustment from a treaty country and will not undertake any actions that would otherwise change such agreement. The restrictions imposed under section 7.05 of Rev. Proc. 2002-52 with respect to the discretion of the U.S. competent authority to negotiate correlative relief will not apply to a unilateral APA. However, a unilateral APA may hinder the ability of the U.S. competent authority to reach a mutual agreement which will provide relief from double taxation, particularly when a



contemporaneous bilateral or multilateral APA request would have been both effective and practical (within the meaning of § 1.901-2(e)(5)(i)) to obtain consistent treatment of the APA matters in a treaty country. If there is a settlement with respect to taxable years prior to the first year subject to a unilateral APA based on rollback of the APA's TPM (as discussed in sections 2.12 and 7 of this revenue procedure), section 7.05 of Rev. Proc. 2002-52 will apply to the rollback years in the regular manner.

## SECTION 7: ROLLBACK OF TPM

.01 Application of the TPM to tax years prior to those covered by the APA ("rollback" of the TPM) may be an effective means of enhancing voluntary compliance and of using available resources to address unresolved transfer pricing issues. The taxpayer may request that the Service consider a rollback (a "rollback request") in connection with a particular APA request. Under regularly applicable procedures, the Service may determine that the same or a similar TPM as that agreed to in an APA should be applied to prior years even in the absence of a rollback request. When applying the TPM to prior years, adjustments may be made to reflect differences in facts, economic conditions, and applicable legal rules. Those adjustments may be made regardless of whether the taxpayer or the Service initiated the rollback request.

.02 The taxpayer may make a rollback request in its APA request or at any time prior to the execution of the APA. The principles set forth in section 2.12 generally will govern the Service's consideration of the request. The balance of prospectivity and retroactivity of the total number of years covered by the proposed overall agreement, and the status of any on-going examination, will also be given consideration in the Service's decision to entertain a rollback request. Rollbacks requested after submission of the APA request must be in writing and addressed to the APA Director.

.03 If a rollback request is submitted in connection with a bilateral or multilateral APA, the rollback request will be deemed to constitute an application for accelerated competent authority consideration as described in section 7.06 of Rev. Proc. 2002-52 (or its successor). The Office of Associate Chief Counsel (International), the Service Operating Division field office involved, and the U.S. Competent Authority will coordinate consideration of the request. The taxpayer's request must include all information required for accelerated competent authority consideration under Rev. Proc. 2002-52 (or its successor), subject to the rules set forth therein. The taxpayer's request can pertain to any years prior to the first year to be covered under the requested APA. As necessary to reach a competent authority agreement, the Service may require that the rollback be applied to one or more specified years if accelerated competent authority is to be granted. In exercising its discretion over the conduct of accelerated competent authority consideration, the U.S. Competent Authority will seek to implement the policy concerning APA rollbacks

stated in section 2.12.

.04 Rollback requests submitted in connection with a bilateral or multilateral APA and involving a taxable year under the jurisdiction of Appeals will be deemed to constitute an application for simultaneous Appeals and competent authority consideration. That application is described in section 8 of Rev. Proc. 2002-52 and is subject to the rules of that section. The Office of Associate Chief Counsel (International), Appeals, and the U.S. Competent Authority will coordinate consideration of the request. In exercising its discretion in a simultaneous Competent Authority-Appeals proceeding, the U.S. Competent Authority will seek to implement the policy concerning APA rollbacks stated in section 2.12. Taxpayers are encouraged to request accelerated competent authority consideration under section 7.03 above, in conjunction with an application for the simultaneous Appeals and competent authority process.

.05 Subject to the policy stated in section 2.12, the Service official with jurisdiction over the taxable year subject to the rollback has discretion as to whether the rollback is applied. That official may be either the Service Operating Division executive responsible for the taxpayer's income tax return, the National Chief of Appeals, the U.S. Competent Authority (for matters subject to competent authority negotiations), or the Division Counsel (for matters pending litigation). Except to the extent inconsistent with this revenue procedure, APA rollbacks will be implemented using regularly applicable procedures for resolving tax issues. Such procedures include but are not limited to closing agreements and other settlement documents and Forms 870 and 870AD.

## SECTION 8: SMALL BUSINESS TAXPAYER APAs

### .01 *Special Provisions Available to Small Business Taxpayers*

At the request of a small business taxpayer ("SBT"), the APA Program may apply any or all of the following provisions in this section. A SBT is any U.S. taxpayer with total gross income of \$200 million or less, as determined under section 4.12(1)(g). In addition, SBT procedures will be available for APAs that cover small transactions described in section 4.12(2)(d). Although transactions involving valuable intangible property or CSAs would not ordinarily be amenable to these SBT procedures due to the complexity of valuing such intangibles, the APA Program will consider employing special procedures for such transactions on a case-by-case basis.

### .02 *PFC Procedures*

- (1) Under ordinary conditions, a taxpayer contemplating an APA may request a PFC with the APA Program. If a PFC is requested, the APA Program

provides informal advice to the taxpayer regarding the taxpayer's proposal, but ordinarily does not begin its due diligence evaluation in earnest until the taxpayer formally files an APA request along with the appropriate user fee. In contrast, the APA Program will commence its due diligence analysis of a SBT at the front end of the process to accelerate the conclusion of the APA negotiations.

- (2) The APA Program and a SBT may hold a PFC to determine as early as possible the best method for the SBT's proposed covered transactions. The APA Program will need a detailed description of the underlying facts and the proposed TPM for the SBT's proposed covered transactions at least 60 days prior to the scheduled conference. The SBT may provide the information it maintains under § 6662(e) to satisfy this requirement. Prior to its prefiling submission, the SBT must consult with the APA Program to determine the information required to evaluate the SBT's covered transactions.
- (3) An APA Team will evaluate the APA prefiling information to determine items of concern and the additional documentation needed to evaluate the request. The SBT will be advised of the APA Team's initial conclusions before the PFC so that it can address these items before or at the conference.
- (4) At the PFC, the SBT and APA Program will agree on a schedule with the objective of finalizing the recommended negotiating position for a bilateral APA, or concluding a unilateral APA, within six months of the date the SBT files its APA request. The APA Program expects that performing this analysis earlier in the process should result in a reduced number of post-filing meetings and supplemental information requests.

### *.03 Items Required for an SBT APA Request*

Before an SBT submits an APA request, the APA Program and the SBT may agree to reduce or eliminate specific items that would otherwise be required by section 4.

### *.04 Locale and Number of Meetings for SBT APA Requests*

The APA Program will endeavor to hold meetings with the SBT at a location convenient to the SBT. To minimize the number of meetings, teleconferences will be employed whenever feasible.

### *.05 Assistance in Economic Analysis*

At the SBT's request, the APA Program will assist the SBT in the selection and evaluation of comparables, as well as the computation of any appropriate adjustments to comparables.

*.06 APA*

For unilateral APA requests, a SBT should submit a proposed draft APA in a form substantially similar to the APA Program's current Model APA (see Announcement 2004-26, 2004-15 I.R.B. 743, 765). The electronic component of the APA request should include a "redline" version showing the differences between the Model APA and the SBT's proposed draft (see section 4.01(7)).

*.07 APA Program's Consideration of Other Alternative Procedures*

The APA Program may consider other procedures suggested by the SBT to reduce the SBT's administrative and financial burden, consistent with the objectives of the APA Program and the requirements of § 482.

SECTION 9: LEGAL EFFECT OF THE APA

*.01* An APA is a binding agreement between the taxpayer and the Service. See sections 2.01 - 2.04.

*.02* If the taxpayer complies with the terms and conditions of the APA, the Service will not contest the application of the TPM to the subject matter of the APA except as provided in this revenue procedure. The taxpayer remains otherwise subject to U.S. income tax laws and applicable income tax conventions.

*.03* An APA shall have no legal effect except with respect to the taxpayer, taxable years, and transactions to which the APA specifically relates.

*.04* Unless provided otherwise by written agreement or regulations, the Service and the taxpayer may not introduce the APA or non-factual oral and written representations made in conjunction with the APA request as evidence in any judicial or administrative proceeding regarding any tax year, transaction, or person not covered by the APA. This paragraph does not preclude the Service and the taxpayer from agreeing to roll back the APA TPM, or the Service's use of any non-factual material otherwise discoverable or obtained other than in the APA process merely because the parties considered the same or similar material in the APA process.

.05 Unless provided otherwise by written agreement or regulations, the Service and the taxpayer may not introduce a proposed, cancelled, or revoked APA, or any non-factual oral or written representations or submissions made during the APA process, as an admission by the other party in any judicial or administrative proceeding regarding any taxable year of the requested APA term. This paragraph does not preclude the Service's use of any non-factual material otherwise discoverable or obtained other than in the APA process merely because the APA Program and the taxpayer considered the same or similar material in the APA process.

## SECTION 10: ADMINISTERING THE APA

### .01 *Annual Reports*

- (1) For each taxable year covered by the APA, the taxpayer must file a timely and complete annual report describing its actual operations for the year and demonstrating compliance with the APA's terms and conditions. The report must include all items required by the APA, describe any pending or contemplated requests to renew, modify or cancel the APA, and report any adjustments made pursuant to section 10.02. Failure to timely file the annual report is grounds for canceling the APA. In appropriate circumstances, the APA Director may extend the time to file the annual report.
- (2) The taxpayer must file an original and four copies of the annual report by the later of (a) 90 days after the time prescribed by statute (including extensions) for filing its federal income tax return for the year covered by the report, or (b) 90 days after the effective date of the APA. The Service and the taxpayer may agree to alternative filing dates. The taxpayer should file the original annual report and copies with the APA Director in Washington, D.C., as indicated in section 4.11. For bilateral or multilateral APAs, the Service may require the taxpayer to file simultaneously a copy of the annual report with the treaty partner or partners.
- (3) The Service Operating Division or the APA Program Office will contact the taxpayer regarding an annual report if it is necessary to clarify or complete the information submitted in the annual report. The taxpayer must supply the additional information by the date specified.
- (4) Any contact between the Service Operating Division, or the APA Program Office, and the taxpayer to clarify the information in an annual report is not an examination or the commencement of an examination of the taxpayer for purposes of § 7605(b) or any other Code provision.

(5) If a filed annual report contains incomplete or incorrect information, or reports an incorrect application of the TPM, the taxpayer must amend it within 45 days after becoming aware of the need to amend the report. The time may be extended for good cause.

(6) An annual report must contain the following declaration:

Under penalties of perjury, I declare that I have examined this annual report including accompanying documents, and, to the best of my knowledge and belief, this annual report contains all the relevant facts relating to the annual reporting requirements pursuant to the APA, and such facts are true, correct, and complete.

[If applicable: An adjustment to conform taxable income and other relevant items to reflect the results reported herein has been reported to the appropriate responsible Service Operating Division personnel.]

[If applicable: An amended income tax return to conform taxable income and other relevant items to reflect the results reported herein [has been] [will be] filed with the appropriate Internal Revenue Service Center.]

(7) The taxpayer must sign the declaration in compliance with sections 4.09 (Perjury Statement) and 4.10 (Signatures).

*.02 APA Primary Adjustments, Secondary Adjustments, and Revenue Procedure Treatment*

(1) **APA Primary Adjustments.** The APA provides the TPM for determining the proper amount of the taxpayer's gross or net income, deductions, credits, or allowances with respect to the APA's covered transactions. Under some TPMs, the taxpayer may have to wait until the close of the taxable year to determine whether the intercompany prices it actually paid or received complied with the TPM (for example, a comparable profits method providing for a particular operating margin range). If the taxpayer's actual transactions do not comply with the TPM, the taxpayer must nonetheless report its taxable income in an amount consistent with the TPM (an "APA primary adjustment"), either on a timely filed original return or on an amended return. The generally applicable Code rules, including additions to tax, penalties and interest, apply with respect to an APA primary adjustment. When the taxpayer makes an APA primary adjustment, an appropriate correlative adjustment will also

be made with respect to the related foreign entity affected by the APA primary adjustment. See § 1.482-1(g)(2). To the extent the APA covers years for which federal income tax returns were filed before the APA was executed, the taxpayer must make any required primary adjustments in an amended return or returns filed within, and pay such primary adjustments within, 90 days of entering into the APA. The generally applicable Code rules will apply with respect to the primary adjustment with respect to the APA years for which federal income tax returns were filed before the APA was executed, except: (a) the computation of any required estimated tax installments for the taxable year will not take into account the primary adjustment and related secondary adjustments (see section 10.02(2)); and (b) the taxpayer will not be subject to the failure to pay penalties under §§ 6651 and 6655, or the failure to make timely deposit of taxes penalty under § 6656, by reason of the primary adjustment and related secondary adjustments.

- (2) **Secondary Adjustments.** Absent an election of the APA revenue procedure treatment described in section 10.02(3), an APA primary adjustment requires a secondary adjustment to conform the taxpayer's accounts. The secondary adjustment may result in tax consequences. See § 1.482-1(g)(3).
- (3) **APA Revenue Procedure Treatment.** If a taxpayer makes an APA primary adjustment, the taxpayer and its related foreign entity may elect APA revenue procedure treatment and avoid the possible adverse tax consequences of a secondary adjustment that would otherwise follow the APA primary adjustment. Under APA revenue procedure treatment, consistent with the principles of Rev. Proc. 99-32, 1999-2 C.B. 296, the taxpayer will be permitted to establish an account receivable from, or payable to, its related foreign entity in the amount of the APA primary adjustment as of the last day of the taxable year to which the APA primary adjustment applies. The account will not bear interest and must be paid within 90 days of the later of (a) the date for timely filing (with extensions) of the federal income tax return for the taxable year to which the APA primary adjustment applies, or (b) the APA's effective date. The account must be paid within the 90 day period to receive revenue procedure treatment. Payment must be in the form of money, a written debt obligation payable at a fixed date and bearing interest at an arm's length rate as provided in § 1.482-2(a)(2), or through an accounting entry offsetting such account against an existing bona fide debt between the U.S. taxpayer and the related foreign entity. The taxpayer must document the payment or offset of the account, and disclose it in the APA annual report for the year of the payment.

- (4) The Service will give effect to an APA primary adjustment, secondary adjustment, and payment under APA revenue procedure treatment, if applicable, for all U.S. income tax purposes. The tax treatment of any such adjustment or payment depends on the facts and circumstances of the adjustment or payment. For example, if a taxpayer's APA primary adjustment involves the reporting of an additional royalty expense for a transaction with a related foreign entity, the Service will deem a payment in the nature of a royalty in the amount of the APA primary adjustment to have been made by the taxpayer to the related foreign entity. This deemed payment may be subject to U.S. withholding tax, and interest would accrue on the tax required to be withheld from the due date of the taxpayer's federal income tax return without regard to extensions. Similarly, a taxpayer's APA revenue procedure treatment may involve the recharacterization of a dividend paid by its foreign subsidiary as a payment of an account receivable established in connection with an APA primary adjustment. Any foreign tax withheld from the payment may be treated as a noncompulsory payment ineligible for the foreign tax credit, unless the taxpayer exhausts all effective and practical remedies, including invocation of competent authority procedures, to obtain consistent treatment that would eliminate the foreign tax liability. See § 1.901-2(e)(5).
- (5) If the Service proposes a tax adjustment or the taxpayer files an amended return that does not require an APA primary adjustment, generally applicable Code rules will apply.
- (6) If the taxpayer requests a bilateral or multilateral APA, the U.S. Competent Authority will discuss the principles of this section with the appropriate foreign competent authority to seek substantially identical treatment of the taxpayer's related foreign entity.

### *.03 Examination*

- (1) With respect to the application of § 482 to the covered transactions, the Service will limit the examination of a taxpayer's income tax return for a tax year covered by an APA to the requirements described in the next paragraph and will not reconsider the TPM.
- (2) For the year under examination, the Service may require the taxpayer to establish: (a) compliance with the APA's terms and conditions; (b) validity and accuracy of the annual report's material representations; (c) correctness of the supporting data and computations used to apply the TPM; (d)



satisfaction of the critical assumptions; and (e) consistent application of the TPM.

- (3) The Service Operating Division must inform the APA Director if the taxpayer has not satisfied any requirement in the prior paragraph. After consulting with the appropriate Service Operating Division personnel, the Associate Chief Counsel (International) may decide to enforce, revise (see section 10.05), cancel (see section 10.06) or revoke (see section 10.07) the APA.
- (4) The Service Operating Division may audit and propose adjustments to the taxpayer's operating results as determined under the TPM without affecting the APA's validity or applicability. The taxpayer may agree with the proposed adjustments in the same manner as any other adjustment, and the Service Operating Division will assess any resulting additional tax or refund any resulting overpayment of tax. If the taxpayer does not agree with the proposed adjustment, the taxpayer may contest it through the normal administrative and judicial procedures. The taxpayer must include the audit adjustments as finally determined for the purpose of applying the TPM and, as necessary, make any APA primary, secondary and correlative adjustments under section 10.02. Revenue procedure treatment under section 10.02(3) is unavailable for audit adjustments.

#### *.04 Record Retention*

- (1) The taxpayer must maintain books and records sufficient to enable the Service Operating Division to examine whether the taxpayer has complied with the APA. The taxpayer's compliance with this paragraph fulfills the record-keeping requirements of §§ 6038A and 6038C as applied to the covered transactions.
- (2) Upon examination, the Service Operating Division may submit a written request to the taxpayer requiring the submission of requested information or the translation of specific documents within 30 days, as extended for good cause. The fact that a foreign jurisdiction may impose a penalty upon the taxpayer or other person for disclosing the material will not constitute reasonable cause for noncompliance with the Service Operating Division's request.

#### *.05 Revising the APA*

- (1) In the event of failure of a critical assumption, or a material change in

governing case law, statute, regulation, or a treaty, as described in section 10.08, the APA Director and the taxpayer will discuss revising the APA. If the APA Director and the taxpayer cannot agree to revise the APA, the Associate Chief Counsel (International) will cancel it as of the beginning of the taxable year in which the failure or change occurred. If the APA Director and the taxpayer agree to revise the APA, the revised APA will indicate its effective date.

- (2) In the event of failure of a critical assumption, the taxpayer must notify the APA Director and provide supporting documentation and a statement as to whether revision appears appropriate. The taxpayer must file the notification before the last date permitted for filing the annual report for the year in which the failure occurred. In providing the notification, the taxpayer must follow the procedures contained in sections 4.09 through 4.11.
- (3) If the APA Director and the taxpayer agree to revise a bilateral or multilateral APA, the Team Leader will submit the revised APA to the U.S. Competent Authority to obtain the consent of the foreign competent authority. If the foreign competent authority refuses to accept the revised APA, or if the competent authorities cannot agree on a revised APA acceptable to all parties, the APA Director and the taxpayer may agree to: (a) apply the existing APA, if appropriate; (b) apply the revised APA or agree to further revisions; or (c) request the Associate Chief Counsel (International) to cancel the APA as of an agreed date. If the APA Director and the taxpayer cannot agree on how to proceed, the Associate Chief Counsel (International) will cancel the APA pursuant to section 10.06(1).

#### *.06 Canceling the APA*

- (1) The Associate Chief Counsel (International) or designee may cancel an APA due to the failure of a critical assumption, or due to the taxpayer's misrepresentation, mistake as to a material fact, failure to state a material fact, failure to file a timely annual report, or lack of good faith compliance with the terms and conditions of the APA. The Associate Chief Counsel (International) will consider facts as material if, for example, knowledge of the facts could reasonably have resulted in an APA with significantly different terms and conditions. In regard to annual reports, the Associate Chief Counsel (International) will consider facts as material if, for example, knowledge of the facts would have resulted in (a) a materially different allocation of income, deductions, or credits than reported in the annual report or (b) the failure to meet a critical assumption.

- (2) The Associate Chief Counsel (International) may waive cancellation if the taxpayer can satisfactorily show good faith and reasonable cause and agrees to make any adjustment proposed to correct for the misrepresentation, mistake as to a material fact, failure to state a material fact, or noncompliance. The Associate Chief Counsel (International) is not required to cancel the APA and may require the taxpayer to continue abiding by it.
- (3) If the Associate Chief Counsel (International) cancels an APA, the cancellation relates back to the beginning of the year in which the critical assumption failed or the beginning of the year to which the misrepresentation, mistake as to a material fact, failure to state a material fact, or noncompliance relates. If, however, the cancellation results from a change in case law, statute, regulation, or treaty, the cancellation normally relates back to the effective date of the change in case law, statute, regulation, or treaty.
- (4) As of the effective date of the cancellation, the APA has no further force and effect with respect to the Service and the taxpayer for U.S. income tax purposes. The Service will seek to coordinate any action concerning the cancellation of a bilateral or multilateral APA with the foreign competent authority.

*.07 Revoking the APA*

- (1) The Associate Chief Counsel (International) may revoke an APA due to fraud or malfeasance (as defined in § 7121), or disregard (as defined in § 6662(b)(1) and (c)) by the taxpayer in connection with the APA, including, but not limited to, fraud, malfeasance, or disregard involving (a) material facts in the request or subsequent submissions (including an annual report) or (b) lack of good faith compliance with the APA's terms and conditions. The Associate Chief Counsel (International) will consider facts as material if, for example, knowledge of the facts could reasonably have resulted in an APA with significantly different terms and conditions. In regard to annual reports, the Associate Chief Counsel (International) will consider facts as material if, for example, knowledge of the facts would have resulted in (a) a materially different allocation of income, deductions, or credits than reported in the annual report or (b) the failure to meet a critical assumption.
- (2) If the Associate Chief Counsel (International) revokes an APA, the revocation

relates back to the first day of the APA's first taxable year.

- (3) If the Associate Chief Counsel (International) revokes an APA, the Service may: (a) determine deficiencies in income taxes and additions thereto; (b) deny relief under Rev. Proc. 99-32, 1999-2 C.B. 296; (c) allow the taxpayer relief under Rev. Proc. 99-32, but determine the interest on any account receivable established under Rev. Proc. 99-32, section 4.01, without mutual agreement or correlative relief; (d) revoke the APA as an "egregious case" under Rev. Rul. 80-231, 1980-2 C.B. 219, so as to deny the taxpayer a foreign tax credit; and (e) not make available the unilateral relief provisions of Rev. Proc. 2002-52 (see section 12.07). The Service will seek to coordinate any action concerning revocation of a bilateral or multilateral APA with the foreign competent authority.

#### *.08 Change in Case Law, Statute, Regulation, or Treaty*

If applicable U.S. case law, statutes, regulations, or treaties change the federal income tax treatment of any matter covered by the APA, the new case law, statute, regulation, or treaty provision supersedes inconsistent terms and conditions of the APA. The APA Director and the taxpayer may revise the APA under section 10.05 to reconcile it with the new law or treaty provision, or agree to cancel the APA.

### SECTION 11: RENEWING THE APA

*.01* A taxpayer may request renewal of an APA using the procedures for initial APA requests. The taxpayer must submit the user fee required under section 4.12 and appropriate supporting documentation. In general, the principles in section 11.02 govern the APA Program's consideration of the renewal request. The renewal request must address changed or anticipated changes in facts and circumstances the APA Team should consider. Taxpayers are encouraged to file the renewal request nine months before the expiration of the APA term.

*.02* The APA Program will expedite the processing of a renewal APA if the following conditions exist: (a) substantially the same law and policy applied to the existing APA; (b) no substantial differences exist between the taxpayer's proposed TPM and the TPM under the existing APA; (c) no material changes occurred in the taxpayer's facts or circumstances since the parties entered into the existing APA; and (d) for a bilateral APA, a rollback or closed year considerations did not influence the TPM in the existing APA.

*.03* If the conditions in the prior paragraph exist, the APA Team begins its evaluation of the renewal APA by considering the continuing applicability of the existing

APA, using updated comparables as appropriate. The APA Team will focus on any changed facts and circumstances. While the APA Team will endeavor to streamline the renewal process, certain cases may require additional analysis. That is, experience and insight gained from applying the TPM to actual data (for example, APA annual reports) may provide insight that indicates the need to modify the TPM.

## SECTION 12: DISCLOSURE

.01 An APA, any background information related to the APA, and the taxpayer's APA request for that APA, are return information and are confidential. See §§ 6103, 6105, 894, and 7852(d).

.02 An APA, any background information related to the APA, and the taxpayer's APA request, are not "written determinations," and they are not open to public inspection. See § 6110.

.03 The Secretary must prepare an annual report for public disclosure. See § 521(b) of the Ticket to Work and Work Incentives Improvement Act of 1999, Pub. L. 106-170, 113 Stat. 1860, 1925. That report includes specifically designated information concerning all APAs, but in a form that does not identify taxpayers or their trade secrets or proprietary or confidential business or financial information.

.04 An APA, any annual reports, and any factual information contained in the background files is subject to exchange of information under income tax treaties or tax information exchange agreements in accordance with the terms of such treaties and agreements (including terms regarding relevancy, confidentiality and the protection of trade secrets). In cases where the exchange of information would be discretionary, information may be exchanged to the extent consistent with sound tax administration and the practices of the relevant foreign competent authority, including where relevant the existence and application by the foreign competent authority of rules similar to those described in sections 9.04 and 9.05.

## SECTION 13: EFFECT ON OTHER DOCUMENTS

Rev. Proc. 96-53, 1996-2 C.B. 375, and Notice 98-65, 1998-2 C.B. 803, are superseded.

## SECTION 14: EFFECTIVE DATE

This revenue procedure will apply to all APA requests, including requests for renewal, received on or after 30 days after publication. By agreement, this revenue procedure may apply to any APA resulting from an APA request pending on such date.

## SECTION 15: PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545 - 1503.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The collections of information are in sections 3.06, 4, 7.03, 10.01, 10.02(1), 10.04, 10.05 and 11.01. This information is required to provide the Service sufficient information to evaluate and process the APA request or request for renewal of an existing APA, or to determine whether the taxpayer is in compliance with the terms and conditions of an APA. This information will be used to evaluate the proposed TPM, and the taxpayer's compliance with the terms and conditions of any APA to which it is a party. The collections of information are required to obtain an APA. The likely respondents are business or other for-profit institutions.

The estimated total annual reporting and/or recordkeeping burden is 8200 hours.

The estimated average burden for an APA prefiling conference is 10 hours; the estimated average burden for an APA request is 50 hours; and the estimated average burden for preparation of an annual report by a party to an APA is 15 hours. The estimated number of respondents and/or recordkeepers is 230.

The estimated annual frequency of responses is one request or report per year per applicant or party to an APA, except that a taxpayer requesting an APA may also request a prefiling conference.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by § 6103.

### DRAFTING INFORMATION

The principal authors of this document are various members of the Advance Pricing Agreement Program of the Office of Associate Chief Counsel (International). For further information regarding this revenue procedure please contact Mr. Peyton Robinson at (202) 435-5220, or Mr. Matthew Kramer at (415) 848-4846 (not toll free numbers).