Internal Revenue bulletin

Bulletin No. 2004-29
July 19, 2004

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Notice 2004–46, page 46.

This notice requests comments on whether debit cards may be used to provide qualified transportation fringes described under section 132(f) of the Code.

Notice 2004–47, page 48.

This notice relieves health insurance providers from preparing IRS Form 1099–H, "*Health Coverage Tax Credit (HCTC) Advance Payments*," unless they affirmatively retain that obligation. A contractor of the IRS will prepare the form and file it with the Service and furnish copies to taxpayers.

EMPLOYEE PLANS

Announcement 2004–58, page 66.

Relative value regulations; effective dates; notices; qualified joint and survivor annuities. This announcement postpones, in certain circumstances, the effective date of the relative value regulations. In addition, it responds to questions that have been raised in connection with the regulations. Finally, the announcement states the intention of the Treasury and the Service to clarify the interaction between the QJSA requirements and the requirements of section 417(e)(3).

EXCISE TAX

Announcement 2004–61, page 67.

This announcement publishes an advance notice of proposed rulemaking requesting comments and information about current technologies, services, and methods for transmitting voice and data communications for purposes of section 4251 of the Code.

TAX CONVENTIONS

Announcement 2004–60, page 43.

Guidance on effective dates under Japan treaty. A copy of the news release issued by the Director, International (U.S. Competent Authority), on June 23, 2004, is set forth.

ADMINISTRATIVE

Notice 2004–47, page 48.

This notice relieves health insurance providers from preparing IRS Form 1099–H, "*Health Coverage Tax Credit (HCTC) Advance Payments*," unless they affirmatively retain that obligation. A contractor of the IRS will prepare the form and file it with the Service and furnish copies to taxpayers.

Rev. Proc. 2004–39, page 49.

This document sets forth procedures for determining whether a qualified residential rental project is in compliance with the applicable set-aside requirements contained in section 142(d) of the Code during the qualified project period (as defined in section 142(d)(2)(A)).

Rev. Proc. 2004–40, page 50.

This 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. Rev. Proc. 96–53 and Notice 98–65 superseded.

Actions Relating to Court Decisions is on the page following the Introduction.
Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are compiled semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

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Actions Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce at an early date whether it will follow the holdings in certain cases. An Action on Decision is the document making such an announcement. An Action on Decision will be issued at the discretion of the Service only on unappealed issues decided adverse to the government. Generally, an Action on Decision is issued where its guidance would be helpful to Service personnel working with the same or similar issues. Unlike a Treasury Regulation or a Revenue Ruling, an Action on Decision is not an affirmative statement of Service position. It is not intended to serve as public guidance and may not be cited as precedent.

Actions on Decisions shall be relied upon within the Service only as conclusions applying the law to the facts in the particular case at the time the Action on Decision was issued. Caution should be exercised in extending the recommendation of the Action on Decision to similar cases where the facts are different. Moreover, the recommendation in the Action on Decision may be superseded by new legislation, regulations, rulings, cases, or Actions on Decisions.

Prior to 1991, the Service published acquiescence or nonacquiescence only in certain regular Tax Court opinions. The Service has expanded its acquiescence program to include other civil tax cases where guidance is determined to be helpful. Accordingly, the Service now may acquiesce or nonacquiesce in the holdings of memorandum Tax Court opinions, as well as those of the United States District Courts, Claims Court, and Circuit Courts of Appeal. Regardless of the court deciding the case, the recommendation of any Action on Decision will be published in the Internal Revenue Bulletin.

The recommendation in every Action on Decision will be summarized as acquiescence, acquiescence in result only, or nonacquiescence. Both "acquiescence" and "acquiescence in result only" mean that the Service accepts the holding of the court in a case and that the Service will follow it in disposing of cases with the same controlling facts. However, "acquiescence" indicates neither approval nor disapproval of the reasons assigned by the court for its conclusions; whereas, "acquiescence in result only" indicates disagreement or concern with some or all of those reasons. "Nonacquiescence" signifies that, although no further review was sought, the Service does not agree with the holding of the court and, generally, will not follow the decision in disposing of cases involving other taxpayers. In reference to an opinion of a circuit court of appeals, a "nonacquiescence" indicates that the Service will not follow the holding on a nationwide basis. However, the Service will recognize the precedential impact of the opinion on cases arising within the venue of the deciding circuit.

The Actions on Decisions published in the weekly Internal Revenue Bulletin are consolidated semiannually and appear in the first Bulletin for July and the Cumulative Bulletin for the first half of the year. A semiannual consolidation also appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in result only in the following decision:

Tax Analysts v. Internal Revenue Service,[1]
215 F. Supp.2d 192 (D.D.C. 2002),
reversed,
350 F.3d 100 (D.C. Cir. 2003)

[1] Acquiescence in result only relating to whether letter rulings issued by the Service that deny or revoke an organization's tax exempt status are subject to public inspection under I.R.C. section 6110.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 35.—Health Insurance Costs of Eligible Individuals

Health insurance providers need not prepare IRS Form 1099–H, "*Health Coverage Tax Credit (HCTC) Advance Payments*", unless they affirmatively retain that obligation. See Notice 2004-47, page 48.

Section 482.—Allocation of Income and Deductions Among Taxpayers

26 CFR 1.482: Allocations of income and deductions among taxpayers.

A revenue procedure describes 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. See Rev. Proc. 2004-40, page 50.

Section 7527.—Advance Payment of Credit for Health Insurance Costs of Eligible Individuals

Health insurance providers need not prepare IRS Form 1099–H, "*Health Coverage Tax Credit (HCTC) Advance Payments*", unless they affirmatively retain that obligation. See Notice 2004-47, page 48.

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions and Other Related Items

Guidance on Effective Dates Under Japan Treaty

Announcement 2004–60

Following is a copy of the News Release issued by the Director, International (U.S. Competent Authority), on June 23, 2004 (IR–2004–82).

Guidance Relating to July 1st Application of New U.S.-Japan Income Tax Treaty

IR–2004–82, June 23, 2004
WASHINGTON — Today, the Internal Revenue Service and the Japanese National Tax Agency respectively have issued guidance regarding the commencement of application of the new income tax treaty between the United States and Japan in each country.

The United States–Japan tax treaty, which was signed on November 6, 2003, entered into force on March 30, 2004. Pursuant to Article 30, the treaty generally is applicable with respect to withholding taxes on July 1, 2004. In the case of U.S. withholding taxes, the treaty is applicable for amounts paid or credited on or after July 1st. In the case of Japanese withholding taxes, the treaty is applicable for amounts taxable on or after July 1st.

The guidance issued today by the IRS provides illustrative examples regarding the application of the new treaty in the case of U.S. withholding taxes on dividends, interest, and royalties. Incorporated in the guidance is an attachment prepared by the Japanese National Tax Agency providing similar illustrative examples regarding the application of the new treaty in the case of Japanese withholding taxes on dividends, interest, and royalties. The Japanese National Tax Agency also has issued guidance providing these illustrative examples and incorporating the U.S. illustrative examples as an attachment.

The text of the Guidance is as follows:

Guidance regarding the Commencement of Application
of the New Tax Convention between the United States and Japan
June 23, 2004

Internal Revenue Service

In the United States, the provision with respect to taxes withheld at source in paragraph 2 of Article 30 of the Convention between the Government of the United States of America and the Government of Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income ("the Convention"), entered into force on March 30, 2004, for amounts (such as dividends, interest, and royalties) to be paid before, on or after July 1, 2004, provides for the commencement of application of the Convention as indicated in Attachment 1.

In Japan, the commencement of application is as indicated in Attachment 2, which was prepared by the Japanese National Tax Agency.

Note

Paragraph 2 of Article 30 of the Convention states:

2. This Convention shall be applicable:

(a) in Japan

(i) with respect to taxes withheld at source:

(aa) for amounts taxable on or after July 1 of the calendar year in which the Convention enters into force, if the Convention enters into force before April 1 of a calendar year; or

(bb) . . .

(ii) . . . ; and

(b) in the United States:

(i) with respect to taxes withheld at source:

(aa) for amounts paid or credited on or after July 1 of the calendar year in which the Convention enters into force, if the Convention enters into force before April 1 of a calendar year; or

(bb) . . .

(ii) . . . .

Attachment 1

Commencement of Application of the New U.S.-Japan Income Tax Convention in the United States

(With respect to Taxes Withheld at Source regarding Investment Income)

Internal Revenue Service

The Convention shall be applicable with respect to taxes withheld at source for amounts paid or credited on or after July 1, 2004. Therefore, the Convention is applicable to the amount of investment income (dividends, interest, and royalties) paid or, where amounts are credited, credited on or after that date.

Specifically, the date on which an amount is paid or credited for the purposes of the Convention is as follows:

DIVIDENDS

In the case of all dividends (including interim dividends), amounts are paid or credited on the date on which they are paid or, where amounts are credited, on the date on which they are credited.

Interest and Royalties

In the case of interest or royalties, amounts are paid or credited on the date on which they are paid or, where amounts are credited, on the date on which they are credited. When an amount is paid (for example in the case where an amount required to be paid by contract on a specified date actually is paid on a later date) shall be determined on the basis of United States tax law.

Examples:

Dividends

1. U.S. Company A has a fiscal year that ends on March 31, 2004. At a shareholders' meeting on June 25, 2004, Company A declares dividends. Company A pays the dividends on July 5, 2004.

These dividends are paid or credited on July 5, 2004.

Interest

2. U.S. Company B has an obligation to pay to a financial institution interest on a debt-claim. The interest is payable in quarterly installments due at the end of each quarter. In accordance with the terms of the debt-claim, the interest is paid on June 30, 2004.

This interest is paid or credited on June 30, 2004.

3. U.S. Company C has an obligation to pay to a financial institution interest on a debt-claim. The interest is payable in installments three times a year, due at the end of April, August, and December. In accordance with the terms of the debt-claim, the interest is paid on August 31, 2004.

This interest is paid or credited on August 31, 2004.

Royalties

4. U.S. Company D has an obligation to pay royalties to Japanese Company E. Pursuant to a license agreement, the royalties are determined based on sales over six-month periods ending June 30 and December 31, and are payable within 15 days of the end of each six-month period. In accordance with the terms of the license, royalties are paid on July 5, 2004.

These royalties are paid or credited on July 5, 2004.

5. U.S. Company F has an obligation to pay royalties to Japanese Company G. Pursuant to a license agreement, the royalties are determined based on sales over six-month periods ending March 31 and September 30 and are payable within 15 days of the end of each six-month period. In accordance with the terms of the license, royalties are paid on October 5, 2004.

These royalties are paid or credited on October 5, 2004.

(Unofficial Translation)

Attachment 2

Commencement of Application of the New Japan-U.S. Income Tax Convention in Japan
(With respect to Taxes Withheld at Source regarding Investment Income)

National Tax Agency

The Convention shall be applicable with respect to taxes withheld at source for amounts taxable on or after July 1, 2004. Therefore, the Convention is applicable to the amount of investment income (dividends, interest, and royalties) "due to be received" on or after that date.

Specifically, the date on which an amount is due to be received for purposes of the Convention is as follows:

DIVIDENDS

The date of the shareholders' meeting where dividends are declared. (In Japan a company's ordinary shareholders' meeting is held within three months after the end of the fiscal year in accordance with the Commercial Code.)

As for interim dividends, the date of the resolution by the board of directors. If an effective date is specified regarding the resolution, that effective date (which must be a date within three months after the date determined in the company's articles of incorporation).

Interest and Royalties

If the date of payment is stipulated in a contract, that date; if not, the date on which the interest or royalties are actually paid.

Examples:

Dividends

1. Japanese Company A has a fiscal year that ends on March 31, 2004. At a shareholders' meeting on June 25, 2004, Company A declares dividends. Company A pays the dividends on July 5, 2004.

These dividends are taxable on June 25, 2004.

Interest

2. Japanese Company B has an obligation to pay to a financial institution interest on a debt-claim. The interest is payable in quarterly installments due at the end of each quarter. In accordance with the terms of the debt-claim, the interest is paid on June 30, 2004.

This interest is taxable on June 30, 2004.

3. Japanese Company C has an obligation to pay to a financial institution interest on a debt-claim. The interest is payable in installments three times a year, due at the end of April, August, and December. In accordance with the terms of the debt-claim, the interest is paid on August 31, 2004.

This interest is taxable on August 31, 2004.

Royalties

4. Japanese Company D has an obligation to pay royalties to U.S. Company E. Pursuant to a license agreement, the royalties are determined based on sales over six-month periods ending June 30 and December 31, and are payable within 15 days of the end of each six-month period. In accordance with the terms of the license, royalties are paid on July 5, 2004.

These royalties are taxable on July 5, 2004.

5. Japanese Company F has an obligation to pay royalties to U.S. Company G. Pursuant to a license agreement, the royalties are determined based on sales over six-month periods ending March 31 and September 30 and are payable within 15 days of the end of each six-month period. In accordance with the terms of the license, royalties are paid on October 5, 2004.

These royalties are taxable on October 5, 2004.

Part III. Administrative, Procedural, and Miscellaneous

Request for Comments on the Use of Debit Cards to Provide Qualified Transportation Fringes Under Section 132(f)

Notice 2004–46

PURPOSE

Employers and others have asked for clarification of their ability to use debit cards to provide their employees with qualified transportation fringes described under § 132(f). Qualified transportation fringes include transportation in a commuter highway vehicle (vanpooling), any transit pass, and qualified parking (collectively referred to herein as "transit benefits") meeting the requirements of § 132(f). Qualified transportation fringes are excluded from the employee's gross income and from wages for purposes of employment tax.

A qualified transportation fringe includes cash reimbursement for transportation in a commuter highway vehicle and qualified parking. However, under § 132(f)(3), a qualified transportation fringe does not include cash reimbursement for a transit pass if a voucher or similar item that may be exchanged only for a transit pass is readily available for direct distribution by the employer to the employer's employees. Thus, in circumstances where vouchers are readily available, an employer must provide vouchers to its employees in order for a transit pass benefit to be excludable from gross income and wages under § 132(f). If a qualified transportation fringe can be provided through cash reimbursement, the employer must use a *bona fide* reimbursement arrangement. To meet the requirements for such an arrangement, first the payment must be a reimbursement, and not an advance. See § 1.132–9(b) Q/A–16(a). Second, the employee must substantiate to the employer that an expense for a transit benefit was actually incurred. See § 1.132–9(b) Q/A–16(c). There are monthly limits on the dollar value of qualified transportation fringe benefits that an employer may provide to an employee and exclude from the employee's income and wages. The monthly limits vary depending upon the type of benefit, and are currently $195 per month for qualified parking and $100 per month for transit passes.

Treasury and the Service are seeking information about how debit card technology works. The operation of the technology is directly relevant to answering a number of questions that arise when applying the qualified transportation fringe benefit regulations. For example, should a debit card be considered a voucher that may be exchanged exclusively for a transit pass? If so, should employers be barred from using cash reimbursement to provide transit passes to their employees as qualified transportation fringe benefits, even if vouchers are not otherwise readily available? If a debit card can be used to purchase more than one kind of fringe benefit, does an employer provide an advance or a reimbursement when it provides a debit card for use in purchasing various transportation benefits? Can a debit card system be established to keep amounts designated for different types of transit benefits separate to ensure that the statutory monthly limits applicable to the different types of benefits are not exceeded?

The Service and Treasury request comments on the issues described below, and any other comments on the use of a debit card to provide transit benefits, from all persons affected by this issue, including employers, employees, transit operators, voucher providers, debit card providers, and third party administrators.

BACKGROUND

Section 132(a)(5) provides that any fringe benefit that is a qualified transportation fringe is excluded from gross income.

Section 132(f)(1) provides that the term "qualified transportation fringe" means (1) transportation in a commuter highway vehicle between home and work, (2) any transit pass, and (3) qualified parking. The amount of the fringe benefit which may be excluded from gross income and wages is currently limited to $100 per month for the aggregate of transportation in a commuter highway vehicle and transit passes, and $195 per month for qualified parking. See § 132(f)(2); Rev. Proc. 2003–85, 2003–49 I.R.B. 1184.

Section 132(f)(5)(A) provides that a transit pass means any pass, token, farecard, voucher or similar item entitling a person to transportation (or transportation at a reduced price) if such transportation is on mass transit facilities or is provided by any person in the business of transporting persons for compensation or hire in a commuter highway vehicle. See § 132(f)(5)(B) for the definition of a commuter highway vehicle.

Section 132(f)(3) provides that a qualified transportation fringe includes a cash reimbursement by an employer to an employee for transit benefits. However, a qualified transportation fringe includes cash reimbursement by an employer to an employee for a transit pass only if a voucher or similar item which may be exchanged only for a transit pass is not readily available for direct distribution by the employer to the employee.

Income Tax Regulations § 1.132–9(b) Q/A–16(b)(2) provides that a transit system voucher is an instrument that may be purchased by employers from a voucher provider that is accepted by one or more mass transit operators in an area as fare media or in exchange for fare media. Under § 1.132–9(b) Q/A–16(b)(3), a voucher provider is any person in the trade or business of selling transit system vouchers to employers, or any transit system operator that sells vouchers to employers for the purpose of direct distribution to employees.

Section 1.132–9(b) Q/A–16(b)(4) provides that a voucher or similar item is readily available for direct distribution by an employer to employees if and only if the employer can obtain it from a voucher provider who does not impose fare media charges greater than 1 percent of the average annual value of the voucher for a transit system, or does not impose other restrictions causing the voucher not to be considered readily available. See § 1.132–9(b) Q/A–16(b)(5) and (b)(6).

Section 1.132–9(b) Q/A–16(a) provides that the term qualified transportation fringe includes cash reimbursement for transportation in a commuter highway vehicle, transit passes (if permitted),

and qualified parking, provided the reimbursement is made under a *bona fide* reimbursement arrangement. A payment made before the date an expense has been incurred or paid is not a reimbursement, even if the employee certifies in advance that the employee will incur expenses at some future date. Under § 1.132–9(b) Q/A–16(c), a *bona fide* reimbursement arrangement is an arrangement under which the employee must substantiate to the employer within a reasonable period of time that an expense for transit benefits has been paid.

Section 1.132–9(b) Q/A–18 provides that no substantiation is required if the employer distributes a transit pass (including a voucher) in-kind to the employer's employees.

In Rev. Rul. 2003–43, 2003–1 C.B. 935, the Service held that under certain circumstances employer-provided expense reimbursements may be made through a debit or credit card, or certain other electronic media, and be excludable from gross income under § 105. The use of a debit card, by itself, generally was not found to be sufficient to meet the substantiation requirement under § 105(b). Instead, in addition to requiring that the Merchant Codes for the debit cards be restricted, the employee is required to substantiate the expense incurred, albeit after the initial transaction. In addition, under certain circumstances the substantiation requirement can be met without additional substantiation. First, a payment made at a doctor's office in the amount of a copayment is deemed to satisfy the substantiation requirement. Second, recurring expenses that have been previously actually substantiated are deemed to meet the substantiation requirement. Third, real-time verification at the point of sale is deemed to meet the substantiation requirement. Other than copayments, recurring expenses, and real-time substantiation, the revenue ruling requires that expenses paid through a debit card be treated as conditional pending confirmation of the charge.

ISSUES ON WHICH COMMENTS ARE SPECIFICALLY REQUESTED

1. Given existing technology, under what circumstances, if any, should a debit card be considered the equivalent of a voucher or similar item described in § 132(f)(5)(A)? We understand that a debit card may be restricted for use only at merchants with certain Merchant Codes or specific merchant card terminals. Would a rule that required use of a debit card to be limited to merchants with certain Merchant Codes or merchant card terminals be administrable? Would such a rule provide adequate controls consistent with the statutory objective of ensuring that amounts are only used to provide transit pass benefits within the meaning of § 132(f)(5)(A)? For example, under what circumstances could a debit card with Merchant Code restrictions be used to purchase something other than a transit pass within the meaning of § 132(f)(5)(A)? In addition, under what circumstances should a debit card be restricted for use only at a particular merchant card terminal in order to be considered a voucher or similar item for purposes of § 132(f)(3)?

2. If a debit card is a voucher or similar item, should the availability of the debit card in an area in which a voucher or similar item is otherwise not readily available preclude cash reimbursement for a transit pass in that area? For example, in Metropolitan Area A, a voucher or similar item is not considered readily available because fare media charges imposed by voucher providers in A exceed 1 percent of the average annual value of vouchers for a transit system. However, the charges associated with using a debit card in A that is the equivalent of a voucher or similar item are less than 1 percent of the annual value of the debit card for the transit system. Should the debit card be considered a readily available voucher in A for purposes of § 132(f)(3), and thus preclude cash reimbursement for a transit pass in A?

3. Is it appropriate to allow the use of recurring transaction substantiation such as that described in Rev. Rul. 2003–43 to meet the requirement under § 132(f)(3) that a transit pass benefit be provided through distribution of a voucher or similar item instead of cash reimbursement? For example, in circumstances in which fare media may be purchased from a merchant who is not in the trade or business of providing transportation services, and thus does not have a Merchant Category Code indicating that the merchant sells only transit passes, *e.g.*, a convenience store, under what circumstances, if any, should recurring transaction substantiation be deemed to satisfy the requirement that a voucher or similar item be distributed?

4. Under what circumstances should an expense related to transportation in a commuter highway vehicle, a transit pass (assuming cash reimbursement is permitted), or qualified parking paid with a debit card be considered to be a *bona fide* reimbursement (*i.e.*, not an advance), and considered adequately substantiated within the meaning of § 1.132–9(b) Q/A–16(c)?

5. Under what circumstances, if any, could a debit card be used to provide multiple qualified transportation fringes (*e.g.*, qualified parking and a transit pass), and adequately ensure that the respective applicable statutory monthly limits for qualified transportation fringes are not exceeded? Given existing technology (such as multiple purses on a debit card, and Merchant Code technology), is it possible, and, if so, how is it possible, to ensure that amounts designated for a particular benefit are used for the intended benefit, and thus that the separate applicable statutory monthly limits for transportation in a commuter highway vehicle and transit passes, and qualified parking are not exceeded? For example, if an employer provides through the use of a debit card a $150 monthly benefit for parking and a $100 monthly benefit for transit passes, how may use of the debit card be restricted to ensure that the respective applicable statutory monthly limits for qualified parking and other qualified transportation fringes are not exceeded?

DATES: Written and electronic comments must be submitted by October 19, 2004.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (Notice 2004–46), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may also be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to the Courier's Desk at 1111 Constitution Avenue, NW, Washington, DC 20224, Attn: CC:PA:LPD:PR (Notice 2004–46), Room 5203. Alternatively, taxpayers may send submissions electronically directly to the Service at: *Notice.comments@irscounsel.treas.gov*. All materials submitted will be available for public inspection and copying.

FOR FURTHER INFORMATION CONTACT: Concerning submissions, Guy Traynor at (202) 622–7180. Concerning this notice, John Richards of the Office of the Associate Chief Counsel (Tax Exempt & Government Entities) at (202) 622–6040 (not toll-free calls).

Information Reporting for Advance Payments of Health Coverage Tax Credit

Notice 2004–47

PURPOSE

This notice provides that the HCTC Transaction Center (Transaction Center), as an administrator of the Health Coverage Tax Credit (HCTC), will file and furnish the information returns and statements required by § 6050T of the Internal Revenue Code, unless the health insurance provider notifies the Transaction Center that the provider will file and furnish information returns and statements.

BACKGROUND

Health Credit

Section 35 provides that under certain conditions, individuals affected by foreign trade competition or receiving benefits from the Pension Benefit Guaranty Corporation may claim the HCTC for a portion of their health insurance expenses. The credit is 65 percent of the eligible individual's expenses for qualified health insurance coverage.

Advance Payment of the Health Credit

Section 7527 provides for advance payment of the credit, in the form of payments from the Treasury Department to the individual's health insurance provider. Such payments reduce the premiums the individual would otherwise owe the provider and, accordingly, reduce the amount of the HCTC available to be claimed on the eligible individual's income tax return.

Information Reporting of Advance Payments

Section 6050T requires the providers to file information returns with the Service reporting advance payments the providers receive from the Treasury Department, and to furnish the insureds an information statement showing the information filed with the Service. The returns required of providers under § 6050T must contain, among other things, the name, address, and taxpayer identification number of insureds who have been declared eligible to benefit from the advance payments described in § 7527. The information returns and statements required by § 6050T enable the Service and taxpayers to ensure that taxpayers do not claim excessive credits on their income tax returns. Form 1099–H, *Health Coverage Tax Credit (HCTC) Advance Payments*, has been developed for providers to use in meeting this reporting obligation.

ADMINISTRATION OF THE PROGRAM

The Treasury Department is administering the HCTC program by using a HCTC Customer Contact Center and a HCTC Transaction Center to perform various administrative duties relating to the program. The Transaction Center will, among other things, collect the insured's portion of the premium and forward the total premium, which includes the advance payment, to health insurance providers through health plan administrators.

INFORMATION REPORTING OBLIGATIONS OF HEALTH INSURANCE PROVIDERS UNDER THE HCTC PROGRAM

Under the program developed to administer the HCTC advance payment program, the Transaction Center will know the amount of those advance payments, and the identity of the individuals who benefit from the payments. Accordingly, the Transaction Center will have the information that the health insurance provider would otherwise have to file with the Service (and furnish to the insureds) pursuant to § 6050T. The Treasury Department and the Service believe that it is in the interest of sound tax administration to allow health insurance providers to use the Transaction Center to satisfy their information reporting obligations under § 6050T and not require the providers to file information returns with the Service or furnish information statements to the insureds. A health insurance provider receiving advance payments from the Transaction Center will be deemed to have elected to have the Transaction Center file these information returns and furnish these statements unless the provider notifies the Transaction Center that the provider will file Forms 1099–H with the Service and furnish those forms to insured individuals. Therefore, unless the health insurance provider notifies the Transaction Center that the provider will file and furnish information returns and statements under § 6050T, the Transaction Center will take those actions instead. The Transaction Center may be contacted for this purpose by calling 1–866–628–4282.

WAIVER OF PENALTIES

Section 6724(a) authorizes the Service to waive any penalties for failures to comply with § 6050T if such failures resulted from reasonable cause and not willful neglect. The Service will not assert the penalties imposed by §§ 6721 and 6722 for information returns and statements required to be filed and furnished regarding advance payments made to health insurance providers against providers that elect to allow the Transaction Center to file and furnish Forms 1099–H. If a health insurance provider does not elect to allow the Transaction Center to file and furnish Forms 1099–H, the normal rules for seeking a penalty waiver under §6724(a) will apply. (See § 301.6724–1 of the Regulations on Procedure and Administration.)

CONTACT FOR INFORMATION

The principal author of this notice is Nathan Rosen of the Office of the Associate Chief Counsel (Procedure & Administration), Administrative Provisions and Judicial Practice Division. For further information regarding this notice, contact Nathan Rosen at (202) 622–4910 (not a toll-free call).

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26 CFR 1.103–8(b): Qualified residential rental projects.
(Also: sections 142(d) and 145(d).)

Rev. Proc. 2004–39

SECTION 1. PURPOSE

This revenue procedure provides guidance to States and local governments that issue bonds to which section 142(d) of the Internal Revenue Code applies. It sets forth procedures for determining whether a residential rental project is in compliance with the applicable set-aside requirements contained in section 142(d) during the qualified project period (as defined in section 142(d)(2)(A)).

SECTION 2. BACKGROUND

.01 Section 103(a) provides that except as provided in section 103(b), gross income does not include interest on any State or local bond.

.02 Section 103(b)(1) provides that section 103(a) does not apply to any private activity bond that is not a qualified bond (within the meaning of section 141).

.03 Section 141(e)(1)(A) and (G) provides that an exempt facility bond or a qualified 501(c)(3) bond may be a qualified bond.

.04 Section 142(a)(7) provides that the term "exempt facility bond" includes any bond issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide qualified residential rental projects.

.05 Section 142(d)(1) provides that the term "qualified residential rental project" means any project for residential rental property if, at all times during the qualified project period, such project meets the requirements under section 142(d)(1)(A) or (B) (the "set-aside requirements"), whichever is elected by the issuer at the time of the issuance of the issue with respect to such project.

.06 A project meets the requirements of section 142(d)(1)(A) if 20 percent or more of the residential units in the project are occupied by individuals whose income is 50 percent or less of area median gross income.

.07 A project meets the requirements of section 142(d)(1)(B) if 40 percent or more of the residential units in the project are occupied by individuals whose income is 60 percent or less of area median gross income. Under section 142(d)(6), in the case of a project located in a city having 5 boroughs and a population in excess of 5,000,000, section 142(d)(1)(B) is applied by substituting "25 percent" for "40 percent".

.08 Section 142(d)(2)(A) provides that the term "qualified project period" means the period beginning on the first day on which 10 percent of the residential units in the project are occupied and ending on the latest of (i) the date that is 15 years after the date on which 50 percent of the residential units in the project are occupied, (ii) the first day on which no tax-exempt private activity bond issued with respect to the project is outstanding, or (iii) the date on which any assistance provided with respect to the project under section 8 of the United States Housing Act of 1937 terminates.

.09 Section 142(d)(3) contains rules for purposes of determining whether an increase in the income of individuals that occupy a residential unit will cause the individuals to no longer qualify as low-income tenants. For this purpose, section 142(d)(4) contains special rules for deep rent skewed projects. Section 142(d)(4)(B)(i) defines the term deep rent skewed project as a project in which, among other requirements, 15 percent or more of the low-income units in the project are occupied by individuals whose income is 40 percent or less of area median gross income.

.10 In the Tax Reform Act of 1986, 1986–3 (Vol. 1) C.B. 519–575 (the "1986 Act"), Congress reorganized sections 103 and 103A of the Internal Revenue Code of 1954 (the "1954 Code") regarding tax-exempt bonds into sections 103 and 141 through 150 of the Internal Revenue Code of 1986. Congress intended that to the extent not amended by the 1986 Act, all principles of pre-1986 Act law would continue to apply to the reorganized provisions. 2 H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. II–686 (1986), 1986–3 (Vol. 4) C.B. 686. The regulations promulgated pursuant to section 103(b)(4)(A) of the 1954 Code (the predecessor to section 142(d)) continue to apply for purposes of section 142(d) except as otherwise modified by the 1986 Act or subsequent law.

.11 Under § 1.103–8(b)(7)(ii) of the Income Tax Regulations, if the issue date of the bonds occurs after the first day on which at least 10 percent of the residential units in the project are occupied, then the qualified project period begins on the issue date of the bonds.

.12 Under § 1.103–8(b)(6)(i), if a project does not comply with the set-aside requirements continuously during the qualified project period, the project will not be a qualified residential rental project (as of the issue date of the bonds that financed the project), unless the noncompliance is corrected within a reasonable period. Under § 1.103–8(b)(6)(ii), a reasonable period is at least 60 days after the noncompliance is first discovered or would have been discovered by the exercise of reasonable diligence. Section 1.103–8(b)(6)(i) provides that if noncompliance is not corrected within a reasonable period, subsequent compliance does not alter the taxable status of the bonds that financed the project.

.13 Section 145(a) provides, in general, that the term "qualified 501(c)(3) bond" means any private activity bond issued as part of an issue if (1) all property that is to be provided by the net proceeds of the issue is to be owned by a 501(c)(3) organization or a governmental unit, and (2) such bond would not be a private activity bond if (A) 501(c)(3) organizations were treated as governmental units with respect to their activities that do not constitute unrelated trades or businesses, determined by applying section 513(a), and (B) sections 141(b)(1) and (2) were applied by substituting "5 percent" for "10 percent" each place it appears and by substituting "net proceeds" for "proceeds" each place it appears.

.14 Section 145(d)(1) provides, in general, that a bond that is part of an issue is not a qualified 501(c)(3) bond if any portion of the net proceeds of the issue are to be used directly or indirectly to provide residential rental property for family units. Section 145(d)(2) provides, in part, that section 145(d)(1) shall not apply to any bond issued as part of an issue if the portion of such issue that is to be used directly or indirectly to provide residential rental property for family units is to be used to provide qualified residential rental projects (as defined in section 142(d)).

.15 The IRS and Treasury Department have received comments requesting guidance regarding the application of the set-aside requirements during the qualified project period. For example, guidance has been requested regarding whether residential units in a newly-constructed project may only be leased to low-income tenants until low-income tenants occupy the required percentage of all residential units in the project, or whether a project complies with the set-aside requirements if low-income tenants occupy the required percentage of occupied residential units. Moreover, guidance also has been requested regarding whether the set-aside requirements apply when an existing project is acquired, or whether there is a transition period before the project must comply with the set-aside requirements. The comments indicate that the lack of guidance on these questions and the resulting uncertainty may be limiting the development of low-income rental housing.

SECTION 3. DEFINITIONS

.01 *Available units* means residential units in a residential rental project that are actually occupied and residential units in the project that are unoccupied and have been leased at least once after becoming available for occupancy, provided that (a) in the case of an acquisition of an existing residential rental project, a residential unit that is unoccupied on the later of (i) the date the project is acquired or (ii) the issue date of the first bonds is not an available unit and does not become an available unit until it has been leased for the first time after such date, and (b) a residential unit that is not available for occupancy due to renovations is not an available unit and does not become an available unit until it has been leased for the first time after the renovations are completed.

.02 *First bonds* means the first issue of bonds to which section 142(d) applies issued to finance the acquisition of an existing residential rental project.

.03 *Low-income tenants* means individuals occupying a residential unit whose income satisfies the applicable income limit under section 142(d)(1)(A) or (B) and, if applicable, section 142(d)(4)(B)(i).

.04 *Set-aside requirements* is defined in section 2.05 of this revenue procedure.

SECTION 4. SCOPE

This revenue procedure provides guidance to States and local governments that issue bonds to which section 142(d) of the Internal Revenue Code applies. It sets forth procedures for determining whether a residential rental project is in compliance with the applicable set-aside requirements during the qualified project period.

SECTION 5. APPLICATION

.01 *General rule for set-aside requirements*. Beginning on the first day of the qualified project period (*i.e.*, the later of the first day on which at least 10 percent of all of the residential units in the project are occupied or the issue date of the bonds), the set-aside requirements apply to the total number of available units.

.02 *Special rule for certain existing projects*. This section 5.02 applies to the acquisition of an existing residential rental project unless more than 90 percent of the residential units in the project are not available units (for example, because residential units are not available for occupancy due to renovations) at any time within 60 days after the later of (1) the date the project is acquired or (2) the issue date of the first bonds. For a period of 12 months beginning on the issue date of the first bonds (the "transition period"), the failure to satisfy the set-aside requirements as described in section 5.01 will not cause the project to not be a qualified residential rental project. If the set-aside requirements are not satisfied on the last date of the transition period, such failure will cause the project to not be a qualified residential rental project as of the issue date(s) of the bonds issued to finance the project unless all bonds issued to finance the project are redeemed as soon as possible, but in no event later than 18 months after the issue date of the first bonds.

SECTION 6. EFFECTIVE DATE

This revenue procedure is applicable to bonds sold on or after July 19, 2004, that are subject to section 142(d). In addition, subject to the applicable effective dates for the corresponding statutory provisions, an issuer may apply this revenue procedure to any bonds (1) sold before July 19, 2004, that are subject to section 142(d), or (2) subject to section 103(b)(4)(A) of the 1954 Code.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Rose M. Weber, Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury Department participated in the development of this revenue procedure. For further information regarding this revenue procedure, contact Ms. Weber at (202) 622–3980 (not a toll-free call).

Section 482.—Allocation of Income and Deductions Among Taxpayers

Rev. Proc. 2004–40

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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:

	Washington, DC	California
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)–1. 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 re-

quested, 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. Compe-

tent 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 finan-

cial 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).

Part IV. Items of General Interest

Extension of Effective Date of Relative Value Regulations

Announcement 2004–58

The Department of the Treasury and the Internal Revenue Service announce a delay in the effective date of § 1.417(a)(3)–1 of the Income Tax Regulations with respect to qualified joint and survivor (QJSA) explanations relating to certain optional forms of benefit. However, the current effective date of the regulations is retained with respect to QJSA explanations relating to single sum or other optional forms of benefit subject to § 417(e)(3) of the Internal Revenue Code that are less valuable than the QJSA.

Section 1.417(a)(3)–1 requires the disclosure, as part of a QJSA explanation, of the relative value and financial effect of optional forms of benefit available to participants in retirement plans qualified under § 401(a) of the Internal Revenue Code. This announcement also addresses certain questions that have arisen under these regulations.

Extension of Effective Date

Final regulations (T.D. 9099, 2004–2 I.R.B. 255) under § 417(a)(3) of the Code regarding disclosure of the relative value and financial effect of optional forms of benefit as part of QJSA explanations provided to participants receiving qualified retirement plan distributions were published in the Federal Register on December 17, 2003. See § 1.417(a)(3)–1 of the regulations, 68 FR 70141. The final regulations are generally effective for QJSA explanations provided with respect to annuity starting dates beginning on or after October 1, 2004.

The regulations were issued in response to concerns that, in certain cases, the information provided to participants under § 417(a)(3) regarding available distribution forms does not adequately enable them to compare those distribution forms without professional advice. In particular, participants who are eligible for both subsidized annuity distributions and unsubsidized single-sum distributions may be receiving explanations that do not adequately explain the value of the subsidy that is foregone if the single-sum distribution is elected. In such a case, merely disclosing the amount of the single-sum distribution and the amount of the annuity payments would not adequately enable a participant to make an informed comparison of the relative values of those distribution forms. The regulations address this problem, as well as the problem of disclosure in other cases where there are significant differences in value among optional forms, and also clarify the rules regarding the disclosure of the financial effect of benefit payments.

A number of commentators have requested that the effective date of the regulations be postponed. Among the reasons cited is the need in some plans for sponsors to complete an extensive review and analysis of optional forms of benefit in order to prepare proper comparisons of the relative values of those optional forms to the QJSA. They have noted that recently proposed regulations (REG–128309–03, 2004–16 I.R.B. 800) under § 411(d)(6) would permit elimination of certain optional forms of benefit and that many plan sponsors can be expected to engage in a thorough review of all of the optional forms of benefit under their plans following publication of those regulations in final form. See § 1.411(d)–3 of the regulations, 69 FR 13769 (March 24, 2004). These commentators have argued that it would be inefficient for plans to be required to incur the costs of two such extensive analyses in succession, rather than a single analysis of optional forms that might serve to some extent for purposes of both the relative value regulations and the § 411(d)(6) regulations.

After careful consideration of these comments, Treasury and the IRS are postponing the effective date of the final regulations under § 1.417(a)(3)–1 for certain QJSA explanations. The regulations will generally be effective for QJSA explanations provided with respect to annuity starting dates beginning on or after February 1, 2006. In the interim, plans that do not comply with § 1.417(a)(3)–1 will be required to comply with prior guidance regarding disclosure of relative value and financial effect. See §§ 1.401(a)–11(c)(3) and 1.401(a)–20, Q&A–36 as they appeared in the April 1, 2003, edition of the Code of Federal Regulations.

Notwithstanding this extension, the existing effective date under § 1.417(a)(3)–1 of the regulations is retained for explanations with respect to any optional form of benefit that is subject to the requirements of § 417(e)(3) of the Code (*e.g.*, single sums, distributions in the form of partial single sums in combination with annuities, or installment payment options) if the actuarial present value of that optional form is less than the actuarial present value (as determined under § 417(e)(3)) of the QJSA. Thus, for example, a QJSA explanation provided with respect to an annuity starting date beginning on or after October 1, 2004, must comply with § 1.417(a)(3)–1 to the extent that the plan provides for payment to that participant in the form of a single sum that is less valuable than the QJSA.

Reasonable Estimates for Generalized Notice

The final regulations provide two methods for disclosing the relative value and financial effect of the optional forms of benefit presently available to a participant: the "participant-specific" method of § 1.417(a)(3)–1(c) and the "generalized notice" method of § 1.417(a)(3)–1(d). Under the participant-specific method, a plan must provide information on the relative value and financial effect of each optional form of benefit and is permitted to use reasonable estimates for this purpose (*e.g.*, estimates based on data as of an earlier date, a reasonable assumption of the spouse's age, or reasonable estimates of the applicable interest rate under § 417(e)(3)).

Under the generalized notice method, a plan discloses the amount of the participant's benefit payable in the normal form of benefit and provides additional information that is not participant-specific (although participant-specific information must be provided upon request). The additional information may be disclosed in the form of a chart based on computations for hypothetical participants that shows the financial effect of generally available optional forms of benefit in units such as dollars per thousand, and the relative value of those optional forms. The disclosure of

the amount of the individual participant's benefit in combination with the chart allows the individual to estimate the financial effect and relative value of the optional forms of benefit available to that individual.

In response to questions raised, this announcement clarifies that reasonable estimates may be used in determining the amount of the normal form of benefit available to a participant under the generalized notice method of disclosure. In addition, a plan may choose to base the chart or additional information described above in part on participant-specific data so long as the requirements of the generalized notice method are otherwise satisfied.

QJSA as Most Valuable Optional Form of Benefit

Section 1.401(a)–20, Q&A–16, provides that, in the case of a married participant, the QJSA must be at least as valuable as any other optional form of benefit payable under the plan at the same time. Section 417(e)(3) provides that specified mortality and interest rate assumptions apply in determining the minimum present value of certain optional forms of benefit, such as a single sum. Some commentators have expressed concern that, solely as a result of the use of the actuarial assumptions specified in § 417(e)(3), the value of a single-sum distribution may exceed the actuarial present value of a QJSA, especially at younger ages.

The Treasury and the Service intend to issue regulations, effective retroactively, clarifying the interaction between the QJSA requirements and the requirements of § 417(e)(3) to use specified actuarial assumptions. The regulations are expected to provide that a plan will not fail to satisfy the requirements of § 417 merely because the application of § 417(e)(3) causes an optional form of benefit to be more valuable than the QJSA.

Contact Information

For further information regarding this announcement, please contact Diane Bloom at (202) 283–9888, or Linda Marshall at (202) 622–6090. These numbers are not toll-free.

Excise Taxes; Communications Services

Announcement 2004–61

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: This document requests information from the public on issues that the IRS may address in proposed regulations (REG–137076–02) relating to the tax on amounts paid for communications services. All materials submitted will be available for public inspection and copying.

DATES: Written and electronic comments must be received by September 29, 2004.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–137076–02), room 5203, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–137076–02), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC, or sent electronically, via the IRS Internet site at *www.irs.gov/regs* or via the Federal eRulemaking Portal at *www.regulations.gov* (indicate IRS and REG–137076–02).

FOR FURTHER INFORMATION CONTACT: Concerning submissions generally, the Regulations Unit, (202) 622–3628; concerning the proposals, Cynthia McGreevy (202) 622–3130 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

Section 4251 imposes tax on amounts paid for certain communications services, including local and toll telephone service. Section 4252(a) provides that local telephone service means the access to a local telephone system, and the privilege of telephonic quality communication with substantially all persons having telephone or radio telephone stations constituting a part of such local telephone system. Section 4252(b)(1) provides that toll telephone service includes a telephonic quality communication for which there is a toll charge that varies in amount with the distance and elapsed transmission time of each individual communication. Section 4252(b)(2) provides that toll telephone service also includes a service that entitles the subscriber, upon payment of a periodic charge (determined as a flat amount or upon the basis of total elapsed transmission time), to the privilege of an unlimited number of telephonic communications to or from all or a substantial portion of the persons having telephone or radio telephone stations in a specified area which is outside the local telephone system area in which the station provided with this service is located.

A tax on communications services has existed for over 100 years. The communications services that currently are subject to the tax are defined in section 4252, which was enacted in its current form in 1965. That section describes the local and long distance telephone service sold under the 1965 Federal Communications Commission rules. Existing Treasury regulations do not reflect the 1965 statutory change.

Sections 4252(a) and (b) define local and toll telephone service in terms of telephonic or telephonic quality communication, which means voice quality communication. Since 1965, numerous communications services have been developed and marketed, the methods of transmission have expanded, and the industry has been deregulated.

As a result of these changes, questions have arisen concerning the application of section 4251 to certain communications services that were not available in 1965. In response to these questions, Treasury and the IRS are considering proposing regulations that would revise the existing regulations to reflect changes in technology.

The test for taxability under section 4251 is whether a service for which an amount is paid is a communications service described in section 4252. The purpose of this ANPRM is to solicit information from the public on how present technology should be treated within the description of telephonic or telephonic quality communication in the definitions

of local and toll telephone service under section 4252.

To ensure that any new regulations accurately reflect the state of today's communications services industry, Treasury and the IRS request that communications services providers and other interested parties submit comments and suggestions describing the various technologies, services, and methods of transmission currently available for transmitting data and voice communications and how they should be treated under section 4251.

Special Analysis

This advance notice of proposed rulemaking is not a significant regulatory action for purposes of Executive Order 12866, "Regulatory Planning and Review."

Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on July 1, 2004, 8:45 a.m., and published in the issue of the Federal Register for July 2, 2004, 69 F.R. 40345)

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D. —Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z —Corporation.

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[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2004–1 through 2004–26 is in Internal Revenue Bulletin 2004–26, dated June 28, 2004.

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