

Notice 2013-79: IRS Proposes Revisions to Advance Pricing Agreement Requests

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On November 22, 2013, the IRS issued Notice 2013-79, which contains draft Revenue Procedures applicable to Advance Pricing Agreements (APAs). The IRS requested comments by March 10, 2014. The Revenue Procedure and the associated requirements will take effect only when the document is issued in final form, which likely will be in the second half of 2014. Importantly, none of the new requirements applies to applications or cases currently pending before the IRS.

Many of the proposals simply memorialize long-standing practices or introduce administrative changes. Other proposals would affect significantly how the government and taxpayers approach APA requests.

Memorialization of Established Practices

Many of the proposed changes in the Revenue Procedure memorialize certain practices that the Advance Pricing & Mutual Agreement Program (APMA) has adopted over several years.

APA terms appropriate to the transaction. The Revenue Procedure states that an APA term should be appropriate to the covered transactions. In the past, taxpayers often were hesitant to request a term longer than five years, even for transactions for which longer terms may be more appropriate, such as certain types of intangibles transactions.

Required bilaterals. The proposed Revenue Procedure is more firm than the current revenue procedure about requiring bilateral APAs instead of unilateral APAs for transactions with treaty countries. The APMA program began restricting unilateral APAs with treaty countries approximately four years ago, and the Revenue Procedure memorializes that trend.

Sharing information with treaty partners. The Revenue Procedure requires taxpayers to provide to all relevant competent authorities any responses, information, documents or analyses that provides to one competent authority. In prior years, the consent to disclosure form included in bilateral APA requests allowed the governments to share information with one another under the exchange of information article in bilateral income tax treaties. The new requirement places the responsibility to share documents directly on taxpayers, and it satisfies a long-standing but unwritten practice that had been inconsistently applied in the APMA program.

Updated financial information. Taxpayers are subject to an affirmative obligation to provide updated financial data for a proposed APA year within 180 days of the close of that year. This rule formalizes the existing practice on the part of many practitioners.

Administrative Changes

Some examples of administrative changes include the following.

Email communications. The Revenue Procedure requires that taxpayers indicate whether they will agree to communicate with APMA personnel via email. Encouraging

email communications should increase the efficiency of communications between APMA personnel and taxpayers and their representatives.

Fulfilling documentation requirements. Filing a complete APA request is “a factor taken into account in determining” whether the taxpayer satisfied the transfer pricing documentation provisions of Treas. Reg. § 1.6662-6(d)(2)(iii) for the proposed APA years. The Revenue Procedure states only that the APA request needs to be filed to be considered a factor in fulfilling the documentation requirements. The APA need not be executed.

In prior years, it was common practice for the APA program to consider the documentation provisions of Treas. Reg. § 1.6662-6(d)(2)(iii) satisfied once an APA request was filed. Formalizing the rule by considering an APA request a “factor” in the fulfillment of those requirements actually could weaken a taxpayer’s penalty protection.

Possible efficiency for APA renewal. Taxpayers filing an APA renewal request must submit a pre-filing memorandum and then follow APMA’s directions regarding whether to submit a normal or abbreviated APA renewal request. Allowing abbreviated renewal requests suggests an emphasis on the part of the IRS on completing renewals with greater speed and efficiency than in the past. It remains to be seen whether treaty partners would be willing to accept such requests for bilateral APAs.

Significant Changes

In addition to the changes mentioned above, the Revenue Procedure includes several proposed changes that could impact taxpayer approaches to an APA. If the changes are implemented, they likely will require more strategic planning on the part of taxpayers in their approaches to the APA process than had been necessary in the past.

Rollbacks. Although Rev. Proc. 2006-9 states that the IRS’s policy is to use rollbacks whenever feasible, rollbacks generally have been at the discretion of taxpayers. Under the Revenue Procedure, APMA may condition acceptance of an APA request on the taxpayer’s agreement to roll back the terms of the proposed APA where APMA has clear interests in doing so and the taxpayer does not offer clear reasons against doing so. The criteria for a rollback would remain as previously: sufficient similarity in relevant facts and circumstances across the taxpayer’s APA and pre-APA years.

Conditioning acceptance of an APA request on taxpayer agreement to a rollback would mean that APMA had examined the facts only briefly before making that determination. It is unclear how such a determination could soundly be made under such circumstances. Moreover, although rollbacks can be beneficial, they also may be disadvantageous. A rollback could have undesired consequences for a taxpayer’s overall tax structure.

Taxpayers considering an APA request will need to be clear at the outset whether a rollback would be desirable and, if not, what arguments might be brought to bear against one.

Coverage of issues relevant to the proposed covered issue. The Revenue Procedure states that APMA has a strong interest in resolving transfer pricing issues “and other coverable issues.” Coverable issues include certain Mutual Agreement Program (MAP) issues, determination of effectively connected income, determination of amounts sourced within and without the U.S., “ancillary issues” (including interest and penalties) and any other issues for which transfer pricing principles may be relevant to their resolution.

Like rollbacks, the scope of APA coverage always has been at the taxpayer's discretion. Also like a rollback, coverage of additional transactions or issues could be beneficial. However, there may be situations in which a taxpayer does not want the IRS examining other transactions. One of the common concerns – and often complaints – of taxpayers in the APA program has been keeping the IRS APA team focused only on the transfer pricing issues requested for coverage. Taxpayers must be clear on whether and how an APA request will open doors for the IRS to examine issues in addition to those for which APA coverage is requested.

Required diagrams. An Appendix in the Revenue Procedure provides detailed guidance concerning the required elements of an APA request, as well as instructions concerning formatting of documents, order of presentation, number of copies, etc. A new requirement is a “covered issue diagram.” Under the Revenue Procedure, APA requests will have to include diagrams, charts or similar representations that depict, among other items, the legal structure, tax structure, business unit structure, intercompany flows of the controlled group and proposed covered group, and the “value chain” of the proposed covered groups.

As stated, it can be a challenge to keep the IRS APA team focused on the transfer pricing issues proposed for APA coverage. The Revenue Procedure is not specific about the amount and type of financial information required to show the value chain. In many instances, such information could raise questions and give rise to assumptions regarding functions, risks, and income among entities that are not relevant to the proposed covered transactions.

Statutes of limitation. The Revenue Procedure requires taxpayers to sign consent agreements to extend the period of limitations for assessment of tax for each proposed APA year and for each proposed rollback year. Consents may be general or restricted.

In the past, the IRS often has been unwilling to issue restricted consents. Under the Revenue Procedure, a taxpayer has no say in determining the type of consent to which it must agree; the Revenue Procedure states that “the taxpayer will be instructed as to the type of consent to execute, viz., general or restricted.”

Restrictions on anonymous prefile meetings. Currently, taxpayers have no restrictions on their ability to conduct a prefile meeting on an anonymous basis. The Revenue Procedure requires a named prefile meeting for certain types of transactions, including requesting unilateral APAs when a bilateral is possible; filing an abbreviated APA request; or requesting an APA that covers intangible transfers, global trading arrangements or unincorporated branches, pass-through entities, hybrid entities, or entities otherwise disregarded for U.S. tax purposes. Under the Revenue Procedure, none of those issues can be discussed anonymously.

Changes to opening conference and case plan procedures. The Revenue Procedure includes two significant changes to how APAs would be processed. First, opening conferences are at the discretion of the IRS. In certain circumstances, opening conferences may indeed not be necessary, particularly for renewals of routine cases. However, taxpayers who believe an opening conference would be beneficial, but who are denied the opportunity, should be prepared to advocate for a conference.

Second, case plans would become optional. The Revenue Procedure states that case plans may be implemented if appropriate, in light of the due diligence and analysis the APA team expects to undertake in the APA process. Many taxpayers may be pleased with the elimination of a case plan requirement. However, eliminating case plans removes from the process a primary vehicle by which

taxpayers can hold the APA team to a timeframe for moving a case forward, and the APA team can hold the taxpayer to a timeframe for providing information and documents.

Where is the IRS Headed?

The stated aim of the APMA program in the Revenue Procedure is to resolve transfer pricing issues and issues for which transfer pricing principles may be relevant in a principled and cooperative manner. Many of the proposals suggest that the APMA Program wants to increase the efficiency with which it processes and completes cases. The Revenue Procedure also contains proposals that, if implemented, may place more discretionary power in the hands of the IRS regarding the issues covered and the procedures followed. APAs will remain a key tool for taxpayers' international tax management. However, if certain proposals are adopted, taxpayers may have to become even more proactive in anticipating certain procedural, administrative and substantive demands from APMA personnel, and may have to incur additional costs in satisfying those demands.