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Tax Treaties

IRS Treaty, Advance Pricing Guidance Reflects OECD Work

BNA Snapshot

Development: IRS issues final versions of revenue procedures for advance pricing agreements and competent authority assistance.

Impact: IRS official says documents reflect interest in ensuring access to both programs, notes coming increases in APA application fees.

By Dolores W. Gregory

Aug. 12 — The IRS finalized a pair of revenue procedures explaining the process for multinational taxpayers seeking advance pricing agreements or treaty assistance from the U.S. competent authority.

The documents, released Aug. 12, were originally issued in draft form in November 2013 (227 DTR G-6, 11/25/13).

“Between notice and finalization we took into account the many public comments we received, but we also took into account the greater global tax administration environment,” said David Varley, acting director of transfer pricing with the IRS’s Large Business & International Division (LB& I).

Varley noted the ongoing work under the Organization for Economic Cooperation and Development’s project on base erosion and profit shifting, in particular BEPS Action 14, which relates to improvements in dispute resolution, as well as the work of the OECD’s Forum on Tax Administration to improve resolution of double tax cases through the mutual agreement procedure (MAP).

“We are looking to improve the practical operations of the MAP programs by providing clear rules and procedures for how MAP and bilateral APA programs work,” Varley said.

“You’ll see reflected in both revenue procedures a greater focus on improving access to MAP and APA,” he added.

Notably, the revenue procedure related to competent authority contains new language urging taxpayers to be more proactive in communicating with the U.S. competent authority; similar language appears in the Forum on Tax Administration's "Multilateral Strategic Plan On Mutual Agreement Procedures: A Vision For Continuous Map Improvement."

The final versions of the documents are:

- Rev. Proc. 2015-40, explaining how to obtain treaty assistance from the U.S. competent authority, through the Advance Pricing and Mutual Agreement (APMA) program and the Treaty Assistance and Interpretation Team within LB& I; and
- Rev. Proc. 2015-41, explaining how to apply for advance pricing agreements.

Structural Changes

The documents reflect structural changes undertaken by the IRS since 2006, including the establishment of LB& I and the creation of APMA, which had formerly been two separate programs dealing with APAs and MAP applications.

Varley noted some of the changes between the proposed procedures and the final versions. Both documents discuss the ability of the IRS to expand the scope of an APA or a MAP case, but the IRS won't make an expansion of scope a condition of competent authority assistance, he said. However, the IRS will ask for more information where necessary, to fully understand the transaction, he said.

There is more discussion in the APA revenue procedure about the circumstances under which the process will continue, he added.

Varley also noted that a taxpayer won't be required to obtain U.S. competent authority agreement before entering into a closing agreement with another jurisdiction.

The agency "reverted to the rule in 2006-54"—the prior revenue procedure on competent authority—"that says if you do that without our prior concurrence, you have the ability to do that, but we will seek only limited correlative relief" from the other competent authority, Varley explained. "We had received some criticism that we were perhaps raising barriers to MAP that we did not have to."

Steven Wrappe of KPMG LLP in Washington, said the two documents draw a clear distinction between the taxpayer's obligation to expand the scope of an APA application and the scope of a competent authority case.

A new section in the APA revenue procedure discusses how "interrelated issues" might affect an application. It states that the agency might determine that it can't reach an effective resolution without also addressing those interrelated matters and "could condition its acceptance, continued consideration or resolution of an APA request upon the agreement of the taxpayer—and, if applicable, of the foreign competent authority—to expand the scope of the APA.

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“It looks like a greater theme is that the IRS views competent authority applications a bit differently from an APA application, in that APA taxpayers are expected to show a bit more flexibility,” Wrappe said, noting that the distinction appears throughout other sections of the revenue procedures.

BEPS Link

Varley also said that the competent authority revenue procedure includes language on limitations on benefits (LOB) that reflects work under BEPS Action 6 regarding treaty abuse as it relates to revised provisions of the U.S. model income tax treaty.

“It more clearly lays out the criteria we look to when deciding to grant discretionary relief,” he said. “The treaty itself will control, but it more thoroughly shows the types of factors we take into consideration.”

Varley also noted that the documents reflect increases in user fees for APAs and discretionary LOB requests. Fees for discretionary LOB requests are increasing from \$27,500 to \$32,500, he said, and will jump to \$37,000 in 2016.

The filing fee for an APA, formerly \$50,000, increases to \$60,000 under the new revenue procedure. Fees for renewals and multiple requests may be lower.

Over time, the APA fee will increase even further, Varley said.

In the past, fees have reflected roughly half the cost of processing an APA, he explained. Thus, a \$60,000 fee covers about 54 percent of the total cost of \$112,000, he said.

The IRS plans to increase the APA fees gradually over the next five years, so that by 2020, taxpayers will be paying the full cost of the APA, he said.

The change is part of “a general initiative within the IRS to begin to charge full user fees where ever possible,” he said. When asked whether the jump in fees was related to the IRS's ongoing budget cuts, Varley declined to comment.

Increasing Costs

Richard McAlonan, former director of APMA, said that compared to the existing revenue procedure, the new requirements for the APAs ask for more information from taxpayers, which will increase the time and cost of seeking an APA.

“That getting an APA appears to contain more requirements and hurdles for taxpayers and is more bureaucratic is probably inevitable given how long APAs have been around,” said McAlonan, who is now with EY LLP in Washington.

But the jump in APA fees may be a bigger problem than the documentation requirements, he said. “A

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\$100,00 fee will scare a lot of taxpayers away, particularly when audits are still free.”

McAlonan noted that the APA revenue procedure requires a standard format for applications—which will make reviewing requests easier for APMA and may speed up the evaluation of requests.

“So that's good for taxpayers and IRS,” he said. “The encouraging of informal discussions outside the APA process, and the willingness to address issues in an anonymous pre-filing memorandum are both very positive signs.”

However, he said, “the real impact of the rev proc won't be apparent until we get to see how it is administered and is applied in practice.”

Step Back

Patricia Lewis of Caplin & Drysdale in Washington, told Bloomberg BNA that the competent authority revenue procedure indicates that the IRS has taken a step back from its earlier proposal to be more involved in the examination process.

“One must presume this was driven by resource constraints (and possibly jurisdictional tensions) even though it held the potential to better focus competent authority issues sooner,” she said in an e-mail. “There will surely be a range of reactions to this change.”

In the same vein, she said, the U.S. competent authority dropped the proposal to participate in the fast track procedure at the exam level.

“Personally, I had been quite intrigued by this concept and saw it as a really attractive option for taxpayers; too bad it's gone,” she said, noting that “a small window” remains open in that the competent authority won't decline assistance to a case that has been through fast track, “but that is a more muted and less constructive role.”

It also appears, she said, that competent authority hasn't retreated from its proposed enhanced role at the Appeals stage, where the taxpayer choice remains the simultaneous audit process or “a quick-step to Appeals.”

“This feature will present challenging strategic considerations for taxpayers and is clearly designed to move cases more quickly and limit taxpayers’ ‘bites at the apple,’ ” she said.

Rev. Proc. 2015-40 supersedes Rev. Proc. 2006-54, 2006-C.B. 1035 and is effective for competent authority requests filed on or after Oct. 30, 2015.

Rev. Proc. 2015-41 supersedes 2006-9, 2006-1 C.B. 278, and Rev. Proc. 2008-31, 2008-1133 and applies to all APAs filed after Dec. 29, 2015. Some APAs filed before that date may be filed under the prior procedure.

Both revenue procedures are scheduled for publication Aug. 31 in Internal Revenue Bulletin 2015-35.

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For More Information

Texts of Rev. Proc. 2015-40 and Rev. Proc. 2015-41 are in TaxCore.

The Forum on Tax Administration's strategic plan for improving MAP is at <http://www.oecd.org/tax/forum-on-tax-administration/map-strategic-plan.pdf>.