

Rev. Proc. 96--53

Section 482 -- Allocations Between Related Parties

1996-2 C.B. 375; 1996 IRB LEXIS 321; 1996-49 I.R.B. 9; REV. PROC. 96-53

December 2, 1996

[*1]

SECTION 1. PURPOSE

This revenue procedure updates and supersedes Revenue Procedure 91--22, 1991--1 C.B. 526, and informs taxpayers how to secure an advance pricing agreement ("APA") from the Office of the Associate Chief Counsel (International) covering the prospective determination and application of transfer pricing methodologies ("TPMs") for international transactions. An APA is an agreement between the Service and the taxpayer on the TPM to be applied to any apportionment or allocation of income, deductions, credits, or allowances between or among two or more organizations, trades, or businesses owned or controlled, directly or indirectly, by the same interests. The TPM thus represents the application to the taxpayer's specific facts and circumstances of the best method within the meaning of the income tax regulations under § 482 of the Internal Revenue Code ("the regulations"), as agreed pursuant to negotiations between the Service and the taxpayer.

SEC. 2. OVERVIEW

Under the APA request procedure, the taxpayer proposes a TPM and provides data intended to show that the TPM is the appropriate application of the[*2] best method within the meaning of the regulations for determining arm's length results between the taxpayer and specified affiliates with respect to specified intercompany transactions. The Service evaluates the APA request by analyzing the data submitted and any other relevant information. After discussion, if the taxpayer's proposal is acceptable, the parties execute an APA covering the proposed TPM. APAs often involve agreements with foreign competent authorities under income tax conventions.

SEC. 3. PRINCIPLES OF THE APA PROCESS

.01 The APA process is designed to be a flexible problem-solving process, based on cooperative and principled negotiations between taxpayers and the Service.

.02 APAs are intended to reflect agreement between the taxpayer and the Service on the best method, within the meaning of the regulations, for determining arm's length prices, and the proper application of the best method to the taxpayer's specific facts and circumstances (that is, the TPM). In negotiations for APAs involving one or more foreign competent authorities ("bilateral" and "multilateral" APAs), the initial negotiating position of the U.S. competent authority will reflect the Service's[*3] opinion, based on consultation with the taxpayer, of the best method within the meaning of the regulations and the appropriate TPM.

.03 The taxpayer must, to the extent feasible, secure relevant pricing data from closely comparable uncontrolled transactions. If this information cannot be obtained, the taxpayer must identify any transactions it believes may be comparable, but for which reliable data is unavailable. Where such transactions cannot be identified, the taxpayer must, to the extent possible, secure relevant pricing data from uncontrolled transactions that are similar, even though not closely comparable, and propose adjustments to account for differences between such uncontrolled transactions and its own operations. The APA process may apply notwithstanding that no comparable uncontrolled transactions can be identified. In such cases, a taxpayer must demonstrate that the proposed TPM otherwise satisfies the requirements of § 482 and this revenue procedure.

.04 The APA Policy Board (the "Policy Board") consists of the Associate Chief Counsel (International), the Assistant Commissioner (International), and the Assistant Commissioner (Examination). The Policy Board establishes[*4] Service policy on matters of substantial general importance pertaining to the APA Program.

.05 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 shall, directly or by delegation, take any actions necessary for carrying out the provisions of this revenue procedure.

.06 Application of the TPM to tax years prior to those covered by the APA ("rollback" of the TPM) is an effective means of enhancing voluntary compliance and an effective use of resources in addressing unresolved transfer pricing issues. It is Service policy that, whenever feasible (based, for example, on consistency of facts, law, and available records in the prior years), the TPM should be used for resolving such issues for prior taxable years. As provided in section 8 of this revenue procedure, the taxpayer may request that the Service consider a rollback in connection with a particular request. Taxpayers should recognize that, even absent a request for a rollback, the Service may, under regularly applicable procedures, determine that the TPM agreed to in an APA should be applied to prior years. When[*5] applying the TPM to prior years, whether or not at the request of the taxpayer, adjustments may be made to reflect differences in facts, economic conditions, and applicable legal rules.

.07 The filing of an APA request does not put into abeyance any examination or other enforcement proceeding. Service personnel responsible for APAs and for enforcement proceedings involving the taxpayer shall, to the extent feasible, coordinate their activities so as to avoid duplicative information requests to the taxpayer, to enhance the efficiency of Service operations and to reduce overall taxpayer compliance burdens.

.08 Prompt and fair resolution of APA requests and renewals, in keeping with the demands of the multinational economic environment, are central goals of the APA process.

.09 The Service intends that the APA process will retain the flexibility to address the needs of particular taxpayers. To this end, the Service and the taxpayer may, by agreement, adopt special procedures, including simplified procedures, that depart from those set forth in this revenue procedure. Such special procedures might be warranted, for example, in order to meet the needs of small business taxpayers, or[*6] in order to facilitate simultaneous negotiation of APAs by the taxpayer, the Service, and foreign competent authorities.

SEC. 4. PREFILING CONFERENCES

.01 Some cases are not suitable for APAs. Even in suitable cases, the extent of information needed and scope of the necessary written request will vary from case to case. Therefore, the taxpayer may request one or more prefiling conferences to explore informally the suitability of an APA and to clarify what data, documentation, and analyses are likely to be necessary in order for the Service to be able to consider a request; the need for an independent expert; potentially applicable TPMs; the possibility of an agreement among competent authorities; and the Service's schedule and method for coordinating and evaluating the request.

.02 To schedule a prefiling conference, the taxpayer or its representative should contact the APA Office with three alternative dates for the prefiling conference. The taxpayer may request a prefiling conference either on the basis that its identity will be made known in connection with the conference, or that it will participate in the conference on an anonymous basis. If the taxpayer chooses to make[*7] its identity known in the conference, representatives of the District and of any Appeals or District Counsel Office with responsibility for the taxpayer's returns normally will participate in the prefiling conference. If the taxpayer initially requests a prefiling conference on an anonymous basis, then chooses to identify itself, the conference may be rescheduled to permit necessary personnel to participate. When requesting a prefiling conference on an identified basis, the taxpayer must inform the APA Office whether transactions similar or related to those to be covered by the proposed APA are currently under consideration by Examination, Appeals or Counsel. Taxpayers should, at least one week prior to a prefiling conference, send a brief prefiling submission to the APA Office that confirms the date, time and place of the prefiling conference; lists the persons attending the prefiling conference for the taxpayer; and outlines the issues to be discussed at the prefiling conference. If the prefiling submission is ten pages or less, it may be sent by facsimile; if the prefiling submission exceeds ten pages, seven copies and one original should be delivered pursuant to the instructions[*8] contained in section 5.13 of this revenue procedure.

SEC. 5. CONTENT OF APA REQUESTS

.01 General.

(1) All materials submitted with the request become part of the Service's file and will not be returned. Therefore, original documents should not be submitted.

(2) The taxpayer must submit copies of any documents relating to the proposed TPM and must ensure that all submitted information is properly labeled, indexed, and referenced in the request. Any previously-submitted documents that the taxpayer wishes to associate with the request must be referenced in the request. 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, certify that the items exist at the time the request is submitted, state where the items are located, state whom the Service can contact to secure the items, and confirm that the items will promptly be made available upon request.

(3) All documents submitted in a foreign language must be accompanied by an English translation.

(4) The user fee should be submitted with the request, unless previously submitted.

.02 Explanation of the Proposed [*9] TPM.

The taxpayer must provide a detailed explanation and analysis of each proposed TPM based on the principles discussed in sections 3.02 and 3.03 of this revenue procedure. The request should illustrate each proposed TPM by applying it, in a consistent format, to the prior three taxable years' financial and tax data of the parties. When 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. If coverage of three taxable years is inappropriate for any reason, the taxpayer should provide data for an appropriate date range and explain why this range was chosen.

.03 General Factual and Legal Items for All Proposed TPMs.

Unless otherwise agreed in a prefiling conference, each request must include, in addition to any other items specified in this revenue procedure, the following items:

(1) The organizations, trades, businesses, and transactions that will be subject to the APA.

(2) The names, addresses, telephone numbers, and taxpayer identification numbers of the controlled taxpayers that are parties to the requested APA (the parties). [*10]

(3) A properly completed Form 2848 for any persons authorized to represent the parties in connection with the request. If the taxpayer or the taxpayer's authorized representative has retained any other person or persons (including, but not limited to, a law firm, accounting firm, or economic consulting firm) to assist the taxpayer in pursuing the APA request, the taxpayer must also provide a separate written authorization for disclosures to such person or persons and their employees during the Service's consideration of the request, pursuant to the instructions in § 301.6103(c)--1 of the Income Tax Regulations.

(4) A brief description of the general history of business operations, worldwide organizational structure, ownership, capitalization, financial arrangements, principal businesses, and the place or places where such businesses are conducted, and major transaction flows of the parties.

(5) Representative financial and tax data of the parties for the last three taxable years, together with other relevant data and documents in support of the proposed TPM. This item includes, but need not be limited to, data contained in Form 5471 (Information Report with Respect to a Foreign[*11] Corporation); Form 5472 (Information Report of a Foreign Owned Corporation); income tax returns; financial statements; annual reports; other pertinent U.S. and foreign government filings (for example, customs reports or SEC filings); existing pricing, distribution, or licensing

agreements; marketing and financial studies; and company-wide accounting procedures, business segment reports, budgets, projections, business plans, and worldwide product line or business segment profitability reports.

(6) The functional currency of each party and the currency in which payment between parties is made for the transactions that will be covered by the APA.

(7) The taxable year of each party.

(8) A description of significant financial accounting methods employed by the parties that have a direct bearing on the proposed TPM.

(9) An explanation of significant financial and tax accounting differences, if any, between the U.S. and the foreign countries involved that have a bearing on the proposed TPM.

(10) A discussion of any relevant statutory provisions, tax treaties, court decisions, regulations, revenue rulings, or revenue procedures that relate to the proposed TPM.

(11) A statement describing[*12] 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 any such issues. The same information may also be required for similar issues involving foreign tax authorities.

.04 Specific Factual Items for a Proposed TPM other than a Cost Sharing Arrangement.

The following information may be appropriate to establish the arm's length basis of the proposed TPM under § 482:

(1) Pertinent measurements of profitability and return on investment (for example, gross profit margin or markup, gross income/total operating expenses, net operating profit margin, or return on assets).

(2) A functional analysis of each party setting forth the economic activities performed, the assets employed, the economic costs incurred, and the risks assumed.

(3) An economic analysis or study of the general industry pricing practices and economic functions performed within the markets and geographical areas to be covered by the APA.

(4) A list of the taxpayer's competitors and a discussion of any uncontrolled transactions, lines of business[*13] or types of businesses that may be comparable or similar to those addressed in the request.

(5) A detailed presentation of the research efforts and criteria used to identify and select possible independent comparables and of the application of the criteria to the potential comparables. This presentation should include a list of potential comparables and an explanation of why each was either accepted or rejected.

(6) A detailed explanation of the selection and application of the factors used to adjust the activities of selected independent comparables for purposes of devising the proposed TPM. Examples of possible adjustments include adjustments to accord with product line segregations; for functional differences relating to activities performed, assets employed, risks and costs incurred; for volume or scale differences; and for differing economic and market conditions.

.05 Specific Factual Items for a Cost Sharing Arrangement.

The taxpayer must apply the cost sharing regulations under § 482 in developing the cost sharing arrangement proposed in the request. The following illustrates information that may be appropriate to establish that the proposed arrangement is a qualified[*14] cost sharing arrangement:

(1) The history of the business operations, the geographic locations, and principal business activities (for example, manufacturing or marketing) of each of the participants.

(2) Documentation of the arrangement and any changes made to it, along with an explanation and the dates thereof.

(3) The participants, their dates of entry, each participant's contribution to the arrangement, each participant's interest in any covered intangibles, and how each participant reasonably anticipates that it will derive benefits from the use of covered intangibles; a statement whether there has been or will be any transfer by any participant of covered intangibles to another taxpayer under common control and, if so, how benefits will be reflected under those circumstances; and evidence of participants' compliance with the reporting requirements under the cost sharing regulations.

(4) The method for calculating each participant's share of intangible development costs and the reason why such method can reasonably be expected to reflect that participant's share of anticipated benefits; and a statement whether and how the participants' shares of intangible development costs [*15] will be adjusted to account for changes in economic conditions, the business operations and practices of the participants, and the ongoing development of intangibles under the arrangement.

(5) The scope of the research and development to be undertaken, including the intangible or class of intangibles intended to be developed.

(6) The duration of the arrangement; the conditions under which the arrangement may be modified or terminated; and the consequences of such modification or termination, such as the interest that each participant will receive in any covered intangibles.

(7) The scope of intangible development costs, and which costs are included and which are excluded (for example, costs of technology acquired from third parties; non-product specific development costs; costs associated with abandoned projects; costs associated with specific stages of product development; and relevant labor, material, and overhead costs); a description of any services performed for participants to 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, [*16] and the costs borne by each participant, pursuant to the arrangement.

(8) The basis used for measuring benefits, the projections used to estimate benefits, and why such basis and projections yield the most reliable estimate of reasonably anticipated benefits; 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 such amounts would be taken into account; and, for a representative period, a comparison of projected and actual benefit shares.

(9) The accounting method used to determine the cost and benefits of the intangible development (including the method used to translate foreign currencies), and to the extent that the accounting method differs materially from U.S. generally accepted accounting principles, an explanation of any material differences.

(10) Prior research, if any, undertaken in the intangible development area; any tangible or intangible property made available for use in the arrangement and any compensation paid for that property (specifying the amount, payor and payee, and how such compensation is determined); and any other information used to establish[*17] the value of preexisting and covered intangibles.

(11) Whether and how participants may join or leave the arrangement (or otherwise change their interests in covered intangibles); any adjustments that will be made to the participants' interests in covered intangibles in such cases; any payments that must be made in such cases, and how such payments will be calculated and made; and whether any changes in the participants' interests in covered intangibles have already occurred, any compensation paid for those interests, and any information used to establish the value of such interests.

(12) How cost sharing payments and buy-in or buy-out payments (i.e., payments made when a participant contributes intangibles, or acquires or relinquishes an interest in covered intangibles) made or received have been treated for U.S. income tax purposes.

(13) Representative internal manuals, directives, guidelines, and similar documents prepared for purposes of implementing or operating the cost sharing arrangement (for example, research and development committee meeting

minutes, market studies, economic impact analyses, capital expenditure budgets, engineering studies, reports and studies of trends[*18] and profitability in the industry, and financial analyses for financing and cash flow purposes).

(14) Each participant's gross and net profitability (historical for five taxable years and projected for two taxable years) with regard to the product area covered by the arrangement.

.06 Discussion of Collateral Income Tax Issues.

The taxpayer must discuss any relevant collateral income tax issues (for example, issues relating to foreign tax credits) raised by the proposed TPM under United States law.

.07 Critical Assumptions.

The taxpayer must propose and describe a set of critical assumptions. A critical assumption is any fact (whether or not within control of the taxpayer) related to the taxpayer, a third party, an industry, or business and economic conditions, the continued existence of which is material to the taxpayer's proposed TPM. Critical assumptions might include, for example, a particular mode of conducting business operations, a particular corporate or business structure or a range of expected business volume.

.08 Contents of Annual Report.

Section 11.01 of this revenue procedure provides that the taxpayer must file an annual report for each taxable year[*19] covered by the APA. The taxpayer should propose in the request a list of items to be included in each report. For example, the report should generally include the following items: (a) the application of the TPM to the actual operations for the year; (b) a description of any material lack of conformity with critical assumption and the reasons therefor (or, if there has been no material lack of conformity with critical assumptions, a statement to that effect); and (c) an analysis of any compensating adjustments to be paid by one entity to the other, and the manner in which the payments are to be made. Other items may be appropriate to the taxpayer's particular circumstances.

.09 Term.

(1) The taxpayer must propose an initial term for the APA. For example, the APA could take effect at the beginning of the taxable year during which it was requested or signed, and last for three taxable years. The term should be appropriate to the industry, product, or transaction involved.

(2) The APA request must be filed no later than the time prescribed by law (including extensions) for filing the taxpayer's Federal income tax return for the first taxable year to be covered by the APA. For purposes[*20] of the preceding sentence, an APA request will be considered filed on the date payment of the required user fee is made (within the meaning of § 7502(a)), provided that a substantially complete APA request is filed with the Service within 120 days thereafter, subject to extension by the Service based on a showing of substantial unforeseen circumstances.

.10 Request for Competent Authority Consideration.

The taxpayer must state whether any of the parties to a request are residents of or conduct activities in a foreign country that has a tax treaty with the United States or in a possession of the United States, and whether the taxpayer proposes an agreement among competent authorities or an agreement described in Rev. Proc. 89--8, 1989--1 C.B. 778 (see section 7 of this revenue procedure for guidelines). For purposes of this revenue procedure, "competent authority" includes the U.S. and foreign competent authorities under income tax treaties to which the U.S. is a party, and also includes the Assistant Commissioner (International) acting with respect to a possession tax agency described in Rev. Proc. 89[*21] --8, as well as a designated possession tax official within the meaning of that revenue procedure. If the taxpayer proposes an agreement among competent authorities for the initial term of the APA, the taxpayer's request must include the information described in sections 4.05(a) and (b) and, in a separate document, section 4.05(m), of Rev. Proc. 96--13, 1996--3 I.R.B. 31, or similar information pursuant to a request for relief under Rev. Proc. 89--8.

.11 Perjury Statement.

The taxpayer must include in any request for an APA, and any supplemental submission, a declaration in the following form:

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

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[*22] personal knowledge of the facts and whose duties are not limited to obtaining letter rulings or determination letters from the Service, or negotiating APAs. The person signing for a trust or a partnership must be a trustee or a partner who has personal knowledge of the facts.

.12 Signatures.

The taxpayer or the taxpayer's authorized representative must sign the request. If an authorized representative is to sign, the taxpayer and representative must conform to the rules of Rev. Proc. 96--1, 1996--1 I.R.B. 8 (or its successor).

.13 Copies and Mailing.

(1) Requests or other documents containing user fees must be mailed or delivered to
Internal Revenue Service
Attn: CC:DOM:CORP:T
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044,

or 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 may either be mailed to
Advance Pricing Agreement Program
Internal Revenue Service
Attn: CC:INTL
Room 3501, 1111 Constitution Ave., N.W.
Washington, DC 20224

or may be delivered[*23] to
Advance Pricing Agreement Program
Internal Revenue Service
Attn: CC:INTL
5th Floor, 950 L'Enfant Plaza, S.W.
Washington, DC 20024.

The taxpayer should provide the original and seven copies of its APA request and of all supplemental materials submitted while the request is pending.

.14 User Fees.

(1) The user fee for each separate request for an advance pricing agreement is \$25,000 except as provided below in this section 5.14 of this revenue procedure.

(2) The user fee for each separate request for an advance pricing agreement from a taxpayer with gross income (as determined in section 5.14(7) of this revenue procedure) of at least \$100,000,000 and less than \$1,000,000,000 is \$15,000.

(3) The user fee for each separate request for an advance pricing agreement or renewal from a taxpayer with gross income (as determined in section 5.14(7) of this revenue procedure) of less than \$100,000,000 is \$5,000.

(4) Notwithstanding sections 5.14(1) and (2) of this revenue procedure, if it is apparent on the face of the APA request that the transaction or transactions subject to the request involve tangible property and/or services the total annual[*24] value of which is not in excess of \$50,000,000, or payments for intangible property (such as royalties) not in excess of \$10,000,000 annually, the user fee for each separate request shall not be more than \$7,500.

(5) As explained in section 5.14(8) of this revenue procedure, an APA request that involves pricing issues in more than one foreign jurisdiction will normally be considered to constitute multiple bilateral requests. The user fee for the first such request shall be determined under sections 5.14(1), (2), (3), (4), or (6) of this revenue procedure as applicable. The user fee for each subsequent bilateral request, however, shall be not more than \$7,500, if such subsequent bilateral request (a) involves the same product line, goods, services, or intangibles, and the same issues, as involved in the first request; (b) covers the same taxable years as covered by the first request; and (c) proposes the same TPM as the first request.

(6) Notwithstanding sections 5.14(1) and (2) of this revenue procedure, the user fee for a request for renewal of an APA, when the material facts, critical assumptions and proposed TPM have not substantially changed, shall not be more than \$7,500. [*25]

(7) For purposes of sections 5.14(2) and 5.14(3) of this revenue procedure, gross income of a U.S. person (or non-U.S. person filing a federal income tax return with respect to all such person's income) is equal to "total income" as reported on the last federal income tax return for such person (as amended) filed for a full (12 month) taxable year ending before the date the request was filed, plus "cost of goods sold" as reported on that federal income tax return, plus any income not subject to tax under section 103 for that period; and gross income of all other persons shall be computed on an equivalent basis (that is, gross receipts or economic income plus cost of goods sold) for such person's most recently completed 12-month year. For purposes of sections 5.14(2) and (3) of this revenue procedure, gross income of a taxpayer shall include the gross income (determined pursuant to the preceding sentence) of all organizations, trades or businesses (whether or not incorporated, whether or not resident or organized in the U.S., and whether or not affiliated for tax purposes) owned or controlled directly or indirectly by the same interests controlling the taxpayer.

(8) For purposes [*26] of this section 5.14 of this revenue procedure, a separate request constitutes a request for agreement on a transfer pricing methodology or methodologies comprising a closely related set of facts, such that review of the single set of facts will suffice to determine the suitability of all the methodologies involved in the separate request. For example, an APA submission involving the pricing of tangible products and the manufacturing services provided by a parent to a subsidiary with respect to those products usually would constitute one separate request. Similarly, a submission involving separate product lines manufactured in the same location by substantially similar processes usually would constitute one separate request. However, a submission involving product lines manufactured at different locations, or by manufacturing processes that are not substantially similar, usually would constitute more than one request. The fact that an APA submission involves pricing issues related to more than one foreign jurisdiction, and thus requires analyses of separate factual or economic issues, as well as negotiations between the U.S. and more than one foreign competent authority, will normally[*27] result in treatment of the submission as more than one request. However, such separate requests may be eligible for reduced user fees under paragraph (5) of this section 5.14 of this revenue procedure.

(9) If an APA request is submitted or processed under paragraphs (2), (3), (4), (5), or (6) of this section 5.14 of this revenue procedure, and it later becomes apparent that the request does not meet the criteria for application of such paragraphs, the Service will request an additional user fee to conform the request to the proper amount under this revenue procedure, as appropriate. The taxpayer may either pay such additional fee and continue the APA process or may withdraw the request. If the taxpayer withdraws the request, the Service may return the user fee to the taxpayer if the Service determines that such action would be appropriate under the circumstances. Except to the extent inconsistent with this revenue procedure, the principles of Rev. Proc. 96--1 (or its successor), including but not limited to section 14 thereof, shall apply to all questions related to user fees in connection with APAs. The APA Team Leader described in section 6.04 of this[*28] revenue procedure, prior to the initial meeting with the taxpayer on a filed APA, will make a determination regarding the correctness of the taxpayer's initial payment of user fees and request any necessary corrections.

(10) The chart below summarizes the foregoing user fee provisions:

Taxpayer Gross Income	Each Additional			
	Original Request	Multilateral Request n1	Routine Renewal n2	Small Transactions n3
\$ 1 billion or more	\$ 25,000	\$ 7,500	\$ 7,500	\$ 7,500
less than \$ 1 billion and greater than or equal to \$ 100 million	15,000	\$ 7,500	\$ 7,500	\$ 7,500
less than \$ 100 million	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000

n1 Only if such additional request involves the same issues, covers the same years, and proposes the same TPM as the first request; see section 5.14(5).

n2 Only if the material facts, critical assumptions, and proposed TPM have not substantially changed; see section 5.14(6).

n3 Regardless of taxpayer size, applies to transactions that involve (i) tangible property or services valued at no more than \$ 50 million annually, or (ii) payments for intangible property not in excess of \$ 10 million annually; see section 5.14(4).

SEC. 6. PROCESSING [*29] OF APA REQUESTS

.01 Initial Contact.

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

.02 Coordination with Other IRS Offices.

Upon receipt of a request, the APA Director will coordinate the evaluation of the request with other Service officials, such as the District Director, Regional Director of Appeals and District Counsel. In appropriate cases, such as where a request proposes an agreement between competent authorities, the APA Director will coordinate with the U.S. competent authority.

.03 Evaluation Process.

The Office of Associate Chief Counsel (International), in coordination with the appropriate District Director and other appropriate Service officials, 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[*30] evaluation of the request will not constitute an examination or inspection of the taxpayer's books and records under § 7605(b) or any other provision of the Code.

.04 Formation of the APA Team and Designation of Team Leader.

Within 45 days of receiving the taxpayer's APA request and any required user fees, the APA Director will appoint an APA Team to review the request. The APA Team normally will consist of at least one representative of the Office of Associate Chief Counsel (International), as well as representatives of the appropriate District and District Counsel and, when appropriate, Appeals and the U.S. competent authority. The APA Director will appoint a Team Leader to oversee

the APA Team's activities. Whenever reasonably feasible, if a prefiling conference has been held with the taxpayer, the Team Leader will be appointed from among the IRS representatives at the prefiling conference.

.05 Negotiation and Drafting.

(1) The APA Team shall arrange with the taxpayer for an initial meeting to take place within 60 days of receiving the taxpayer's APA request and required user fee. In connection with the initial meeting, the APA Team and the taxpayer shall agree on a[*31] Case Plan and Schedule, to which everyone involved in the APA--both government and taxpayer personnel--will be expected to adhere. The Case Plan and Schedule should list each question raised by the initial Service review of the APA request and should include a schedule for seeking to resolve each. The Case Plan and Schedule generally should reflect agreement between the APA Team and the taxpayer on the scope and nature of any additional information that will be required to resolve these questions in order to negotiate an APA. Firm dates should be agreed upon for case milestones, including: (a) submission of any necessary additional information by the taxpayer; (b) evaluation of the information by the government; (c) negotiation of a recommended agreement or competent authority negotiating position; and (d) presentation of the recommended agreement or competent authority negotiating position in writing to the Associate Chief Counsel (International).

(2) 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[*32] authority of the treaty partner or U.S. possession involved to minimize the time needed for competent authority resolution.

(3) To minimize delays caused by the need to coordinate different parties' schedules on short notice, the time and place of meetings required for any steps in the case should be determined in the Case Plan and Schedule.

(4) Failures by either the taxpayer or the APA Team to meet case milestones will be addressed promptly, normally in a meeting or telephone conference involving the APA Director, members of the Service APA Team, and the taxpayer. If a taxpayer has failed to meet one of the case milestones, the APA Director will assist the taxpayer in remedying any difficulties and will propose a course of action to ensure that milestones can be met. Substantial and consistent failure by the taxpayer to comply with the Case Plan and Schedule will be treated by the Service as a withdrawal of the APA request. In this event, if the taxpayer wishes to continue to pursue the APA, the taxpayer will be required to refile the request and pay a new user fee. If the Service fails to meet a case milestone, the APA Director, the Service APA Team, and supervisors in the District[*33] and Region, as appropriate, shall work together promptly to remedy the situation.

(5) In some circumstances, development of the case after agreement on the Case Plan and Schedule will suggest, to both the APA Team and the taxpayer, that some milestone dates should be adjusted. To preserve flexibility, the APA Team and the taxpayer may amend the Case Plan and Schedule by mutual agreement, consistent with the need to maintain progress toward completion of the case as expeditiously as feasible.

(6) The function of the APA Team is to negotiate and recommend an agreement, and if applicable to recommend in consultation with the taxpayer a competent authority negotiating position, to the Associate Chief Counsel (International). Negotiations between taxpayers and the APA Team should be documented by means agreed between the parties. The District Director with responsibility for the taxpayer's returns shall be provided an opportunity to review and comment on the draft APA in the case of a unilateral APA, and the proposed initial US competent authority negotiating position in the case of a bilateral or multilateral APA. Signature of an APA by the Associate Chief Counsel (International) and[*34] the taxpayer will constitute agreement to the APA.

.06 Withdrawing the Request.

The taxpayer may withdraw the request at any time before the execution of the APA. Pursuant to the principles of Rev. Proc. 96--1 (or its successors), including but not limited to section 14.09 thereof, the user fee generally will not be refunded if the taxpayer withdraws its request for an APA.

.07 Rejecting the Request.

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

SEC. 7. COMPETENT AUTHORITY CONSIDERATION

.01 When any of the parties to a request are entitled to seek relief under the mutual agreement provision of a tax treaty between a foreign country and the United[*35] 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. 96--13, 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[*36] APA will be sought among the taxpayer, the Service, and the foreign competent authority. As a general matter, the taxpayer is encouraged to submit APA requests and related correspondence simultaneously to the Service and to foreign competent authorities involved in the requests.

.02 The purpose of the competent authority agreement is to avoid double taxation. If such an agreement is not acceptable to the taxpayer, the taxpayer may withdraw the APA request (see section 6.06 of this revenue procedure). If the competent authorities are unable to reach an agreement or the taxpayer does not accept the competent authority agreement, the Service will attempt to negotiate a unilateral APA with the taxpayer (see section 7.07 of this revenue procedure).

.03 The taxpayer must cooperate with the Service and the U.S. competent authority, pursuant to the standards set forth in Rev. Proc. 96--13 and any other applicable revenue procedures. Any information received or prepared by the Service, including information furnished by the taxpayer or the related foreign entity, will be subject to the restrictions on disclosure of tax related information provided by U.S. law and[*37] the applicable income tax convention.

.04 It may be necessary to request sensitive confidential data (such as trade secrets) which, if disclosed, could harm the taxpayer's competitive position. In such cases, the parties will attempt to negotiate a mechanism to permit verification by a foreign competent authority without disclosing such information.

.05 When the competent authorities enter into an agreement covering an APA, the Service will, to the extent practicable, 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 The U.S. competent authority will seek to persuade the foreign competent authority to use APA data only on terms similar to those described in sections 10.04 and 10.05 of this revenue procedure.

.07 To minimize taxpayer and governmental uncertainty and administrative cost, bilateral or multilateral APAs generally[*38] 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. When a unilateral APA request involves taxpayers operating in a country that is a treaty partner, the Service may notify the treaty partner of the filing of the request and provide the treaty partner with other information related to the request, under normal rules governing the exchange of information under income tax treaties. In some circumstances, procedures agreed upon with particular foreign competent authorities, or the requirements of proper relations with treaty partners, may preclude unilateral APAs.

.08 Section 7.05 of Rev. Proc. 96--13 provides in part that, if a taxpayer reaches a settlement on an issue with Counsel 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[*39] change such agreement. The restrictions imposed under section 7.05 of Rev. Proc. 96--13 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 such APA's TPM (as discussed in sections 3.06 and 8 of this revenue procedure), section 7.05 of Rev. Proc. 96--13 will apply to such rollback years in the regular manner.)

SEC. 8. ROLLBACKS

.01 The taxpayer may indicate in its APA request, or at any time prior to the completion of APA negotiations, that it desires for the Service to consider using the TPM of the APA to resolve transfer pricing issues[*40] for years prior to the earliest year covered by the APA. In general, the principles set forth in section 3.06 of this revenue procedure will govern the Service's consideration of this request (the "rollback request"). When a rollback request is made after submission of the APA request, the taxpayer must provide the request to the APA Director at the address indicated in section 5.13(2) of this revenue procedure.

.02 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. 96--13. The Office of Associate Chief Counsel (International), the District Director, and the U.S. competent authority will coordinate consideration of the request. The taxpayer's request must include all information required for accelerated competent authority consideration under Rev. Proc. 96--13, 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, except that, in order to facilitate[*41] effective competent authority negotiations, the Service may require that, if accelerated competent authority consideration is to be granted, it will apply to one or more specified years. In exercising their regular discretion over the conduct of accelerated competent authority consideration, Service officials shall seek to implement the policy concerning APA rollbacks stated in section 3.06 of this revenue procedure.

.03 If a rollback request is submitted in connection with a bilateral or multilateral APA and involves a taxable year that is under the jurisdiction of Appeals, the rollback request will be deemed to constitute an application for simultaneous Appeals and competent authority consideration as described in section 8 of Rev. Proc. 96--13 and will be subject to the rules set forth therein. The Office of Associate Chief Counsel (International), the Regional Director of Appeals, and the U.S. competent authority will coordinate consideration of the request. In exercising their regular discretion over the conduct of simultaneous Appeals and competent authority consideration, Service officials shall seek to implement the policy concerning APA rollbacks[*42] stated in section 3.06 of this revenue procedure.

.04 Subject to the policy set forth in section 3.06 of this revenue procedure, the determination whether a rollback shall be granted with respect to a taxable year is within the discretion of the Service official with jurisdiction over the taxable year subject to the rollback--typically, either the District Director, the Regional Director of Appeals, the Assistant Commissioner (International) (for matters subject to competent authority negotiations), or the District Counsel (for matters under litigation). Except to the extent inconsistent with this revenue procedure, normal procedures for resolving tax issues, including but not limited to closing agreements and other settlement documents and Forms 870 and 870AD, shall be used to implement APA rollbacks.

SEC. 9. INDEPENDENT EXPERT OPINION

.01 The taxpayer may be required to provide at its own expense an independent expert, acceptable to both the taxpayer and the Service (and, in a bilateral or multilateral proceeding, the foreign competent authority or authorities) to review and opine on the proposed TPM. The taxpayer may suggest in its APA request whether an independent expert[*43] is needed, or the Service (or, if applicable, the foreign competent authority) may determine that an independent expert is needed for the evaluation of the taxpayer's request.

.02 For purposes of this revenue procedure, an expert is any person who, by agreement between the taxpayer and the Service (and, if involved, the foreign competent authority), possesses expert education or experience in a field of study, industry or geographic area that is relevant to the subject matter of the taxpayer's APA request.

.03 For purposes of this revenue procedure, an expert is independent if the expert has not participated to any material extent in the development of the request and has not in the past assisted either the Service or the taxpayer in matters substantially related to the request.

.04 If an expert is necessary, the expert will critically analyze the taxpayer's proposed TPM and render a written opinion. The opinion will address any questions and concerns raised by the Service or the taxpayer (and, if involved, the foreign competent authority); conclude whether the proposed TPM or a revised version fairly supports and produces an arm's length approach; and provide the basis for this[*44] opinion. However, the expert's opinion will not be binding on any of the parties. The taxpayer and the Service (and, if involved, the foreign competent authority) will have access to the expert's report and supporting documentation. The Service and the taxpayer shall both be kept fully informed of any communications between the other party and the independent expert, and receive copies of all information provided by such other party to the expert.

.05 If an independent expert is necessary, the taxpayer must provide a waiver under § 6103(c) to the Service for purposes of discussing returns or return information with the expert. The taxpayer must also ensure that the expert is familiar with the provisions of this revenue procedure and that any opinion rendered by the expert complies with those provisions.

SEC. 10. LEGAL EFFECT

.01 An APA is a binding agreement between the taxpayer and the Service.

.02 If the taxpayer complies with the terms and conditions of the APA, the Service will regard the results of applying the TPM as satisfying the arm's length standard, and, except as provided in this revenue procedure, will not contest the application of the TPM to the subject matter[*45] of the APA. The taxpayer remains otherwise subject to U.S. income tax laws and is entitled to any benefits otherwise available under U.S. income tax laws.

.03 Except to the extent provided by regulations, an APA shall have no legal effect except with respect to the taxpayer, taxable years and transactions to which the APA specifically relates.

.04 Except as otherwise provided by written agreement, regulations, or this revenue procedure, neither the APA nor any non-factual oral or written representations or submissions made in conjunction therewith may be introduced by the taxpayer or the Service as evidence in any judicial or administrative proceeding in relation to any tax year, transaction, or person not covered by the APA. However, taxpayers should recognize that the preceding sentence does not preclude rollback of the APA TPM, nor the discovery, use, or admissibility of non-factual material otherwise discoverable or obtained other than in the APA process merely because the same or similar material was also included in the APA or representations or submissions made in connection with the APA or presented during the APA process.

.05 Except as otherwise provided by written agreement[*46] or regulations, if an APA is not executed or if an executed APA is later revoked or canceled, neither the APA or the proposal to use a particular TPM, nor any non-factual oral or written representations or submissions made during the APA process, may be introduced by the taxpayer or the Service as an admission by the other party in any administrative or judicial proceeding for the taxable years for which the APA was requested or executed. However, taxpayers should recognize that the preceding sentence does not preclude the discovery, use, or admissibility of non-factual material otherwise discoverable or obtained other than in the APA process merely because the same or similar material was also included in the APA or representations or submissions made in connection with the APA or presented during the APA process.

SEC. 11. 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 the taxpayer's actual operations for the year and demonstrating good faith compliance with the terms and conditions of the APA. The report must include all items called for by the APA, must describe [*47]any pending or contemplated requests to renew, modify or cancel the APA, and must describe any compensating adjustments made pursuant to section 11.02 of this revenue procedure.

(2) The taxpayer shall file an original and four copies of each report, no later than 90 days after the time prescribed by law (including extensions) for filing the taxpayer's Federal income tax return for the year covered by the report, or by such other date as is specified in the APA, with the APA Director at the address indicated in section 5.13(2) of this revenue procedure. The taxpayer may also be required to file a copy of the annual report with the treaty partner or partners with respect to a bilateral or multilateral APA. The report must comply with sections 5.11 and 5.12 of this revenue procedure.

(3) The Service will contact the taxpayer regarding an annual report only if it is necessary to clarify or complete the information contained in the annual report. Additional information must be supplied by the date specified by the Service, as extended for good cause. Any contact between the taxpayer and the Service for the purpose of clarifying the information contained in the annual report will not [*48] constitute an examination, or the commencement of any examination, of the taxpayer for purposes of § 7605(b) or any other provision of the Code.

.02 Compensating Adjustments.

(1) If the results of applying the TPM differ from those contemplated by the APA, the APA may permit the taxpayer and its related foreign entity to make a compensating adjustment. For example, if the APA provides for a range of expected operating results, and the actual operating results are outside that range (but within any limits specified in the APA), the APA may permit the parties to make a compensating adjustment to bring the results to an agreed upon point within the described range. Such compensating adjustment should be reflected on the taxpayer's timely filed (with extensions) federal income tax return; if the taxpayer is not able to make such adjustments in its original return, the required compensating adjustment must in any event be made and paid within 90 days of the date prescribed for filing such return (with extensions), and reflected on an amended return filed within such period and the timely filed annual report required by section 11.01 of this revenue procedure. To the extent the APA[*49] covers years for which federal income tax returns were filed before the APA was executed, the taxpayer must make any required compensating adjustments in an amended return or returns filed within, and pay such compensating adjustments within, 90 days of entering into such APA.

(2) The taxable income and earnings and profits of both the taxpayer and its related foreign entity for a taxable year covered by an APA will include all income generated as a result of the TPM as increased or decreased by any compensating adjustment for that year. A compensating adjustment will be deemed to have been made as of the last day of the taxable year to which it applies. For all U.S. income tax purposes, after taking into consideration any compensating adjustment, the adjusted figures will be used. Provided that the taxpayer has made a good faith effort to comply with the TPM in such manner as to avoid the need for compensating adjustments, and payments of compensating adjustments are made within the time specified in section 11.02(1) of this revenue procedure, (i) the compensating adjustment will not be taken into account in the computation of any required estimated tax installments for such year, [*50] (ii) the taxpayer will not be subject to the failure to pay penalties under §§ 6651 and 6655 by reason of the compensating adjustment, and (iii) no interest will accrue on any receivable or payable established to settle such compensating adjustment. A compensating adjustment may, however, be taken into account for purposes of redetermining any foreign tax credits in accordance with § 901. Subject, where applicable, to agreement between competent authorities, the taxpayer or the related foreign entity may employ any method that accords with section 4 of Rev. Proc. 65--17, 1965--1 C.B. 833 (as modified), or any successor, for paying compensating adjustments, including checks, wire transfers, offsets through intercompany accounts, or recharacterized dividends. All actions taken with respect to such compensating adjustments must be documented and disclosed in the annual report.

(3) A "subsequent compensating adjustment" arises when the taxpayer or the Service makes normal and routine adjustments (for example, correction of computational errors) to the determination and computation of the taxpayer's TPM during the taxable year or years[*51] under the APA, as determined in accordance with the TPM. The generally applicable Code rules relating to assessment, collection and refund of tax and the principles of Rev. Proc. 65--17 (as

modified), or any successor, apply to any resulting change in Federal income tax liability because of a subsequent compensating adjustment.

(4) When an agreement between competent authorities is sought as part of the APA request, the principles stated in this section will be discussed with the appropriate foreign competent authority to seek to ensure substantially identical treatment of the taxpayer's related foreign entity.

(5) The Service and the taxpayer may agree in an APA to modify the foregoing provisions relating to compensating adjustments.

.03 Examination.

(1) If the District Director examines a tax year covered by an APA, the examination of matters covered by the APA will be limited to the factors in section 11.03(2) of this revenue procedure. The District Director will not re-evaluate the TPM itself.

(2) The District Director may require the taxpayer to establish that (a) the taxpayer has complied in good faith with the terms and conditions of the [*52]APA; (b) the material representations in the APA and the annual reports remain valid and accurately describe the taxpayer's operations; (c) the supporting data and computations used in applying the TPM were correct in all material respects; (d) the critical assumptions underlying the APA remain valid; and (e) the taxpayer has consistently applied the TPM and met the critical assumptions.

(3) If the District Director determines that any requirement in section 11.03(2) of this revenue procedure has not been satisfied, the issue will be submitted to the Associate Chief Counsel (International) for resolution. The Associate Chief Counsel (International) will decide either to continue to apply the APA; revoke the APA (see section 11.05 of this revenue procedure); cancel the APA (see section 11.06); or revise the APA (see section 11.07).

(4) The District Director may, without securing the consent of the Associate Chief Counsel (International), propose normal and routine audit adjustments, which are not related to interpretation of the TPM, to the determination and computation of the operating results of the taxpayer's TPM during the taxable year or years under examination (as determined[*53] in accordance with the TPM) without affecting the continued validity or applicability of the APA. If the taxpayer agrees with the proposed adjustments, they will be given effect through payment of additional compensating adjustments. If the taxpayer does not agree, the taxpayer may contest the proposed adjustments through normal administrative and judicial proceedings. Any changes to compensating adjustments previously made by the taxpayer, in respect of the taxable year or years under examination, that arise as a result of the audit adjustments made by the District Director will be made within ninety days of a final determination of the audit adjustments. Any compensating adjustments and changes to compensating adjustments described in this section 11.03(4) will be treated as subsequent compensating adjustments for purposes of section 11.02 of this revenue procedure.

.04 Record Retention.

(1) The taxpayer must maintain books and records sufficient to enable the Service to examine the taxpayer's compliance with the APA. The APA may specify the books and records that are necessary to fulfill this objective and may specify that compliance with the applicable provisions of the [*54] APA will constitute compliance with the provisions of §§ 6038A and 6038C with respect to transactions covered by the APA.

(2) Upon examination, information requested by the Service must be made available to the Service upon written request within 30 days, and translations must be provided within 30 days of a request for translation of specific documents, both 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's request.

.05 Revoking the APA.

(1) The Associate Chief Counsel (International) may revoke the APA if there has been 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 any of the following: the material facts set forth in the request or subsequent submissions (including the annual report), or lack of good faith compliance with the terms and conditions of the APA. Material facts are those that, if known by the Service, could reasonably have resulted[*55] in a significantly different APA (or no APA at all). The Associate Chief Counsel (International) is not required to revoke the APA and may require the taxpayer to continue to abide by it.

(2) If the APA is revoked for any reason, the revocation may be retroactive to the first day of the first taxable year for which the APA was effective.

(3) If the APA is revoked for any reason, the Service may determine deficiencies in income taxes and additions thereto in accordance with applicable provisions of the Code. In addition, (a) relief under Rev. Proc. 65--17 may be denied; (b) if the Service determines that the taxpayer may avail itself of the relief under Rev. Proc. 65--17, interest on any account receivable established under section 4.03 of that revenue procedure may be determined not to be subject to mutual agreement or correlative relief; (c) the revocation of the APA may be treated as an "egregious case" under Rev. Rul. 80--231, 1980--2 C.B. 219, with the result that the taxpayer may be denied a foreign tax credit in accordance with that ruling; and (d) the unilateral relief[*56] provisions of Rev. Proc. 96--14, 1996--3 I.R.B. 41, may not be available. When an APA has been the subject of negotiation with a foreign competent authority, the Service will seek to coordinate any action concerning revocation of the APA with the foreign competent authority.

.06 Cancelling the APA.

(1) The Associate Chief Counsel (International) may cancel the APA if the District Director, with the concurrence of the Associate Chief Counsel (International), determines that there was a misrepresentation, mistake as to a material fact, failure to state a material fact, or lack of good faith compliance with the terms and conditions of the APA (but not fraud, malfeasance or disregard) in connection with the request for the APA, or in any subsequent submissions (including the annual report). Material facts are those that, if known by the Service, would have resulted in a significantly different APA (or no APA at all).

(2) The Associate Chief Counsel (International) may waive cancellation if the taxpayer can show good faith and reasonable cause to the satisfaction of the Associate Chief Counsel (International), and if the taxpayer[*57] agrees to make any adjustment proposed by the Associate Chief Counsel (International) 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 to abide by it.

(3) If the APA is cancelled under section 11.06(1) of this revenue procedure, the cancellation will be effective as of the beginning of the year in respect of which the misrepresentation, mistake as to a material fact, failure to state a material fact, or noncompliance occurs. If, however, the cancellation results from a change in law or treaty, as provided in section 11.07(1) of this revenue procedure, the cancellation normally will be effective as of the effective date of the change in law or treaty.

(4) If the APA is cancelled for any reason, then as of the effective date of the cancellation the APA will cease to be of any further force and effect with respect to the taxpayer and the Service for U.S. income tax purposes. After the effective date of the cancellation, the tax treatment of the transactions covered by the APA will be subject to[*58] all U.S. tax rules (including treaty rules) that otherwise apply. When an APA has been the subject of negotiation with a foreign competent authority, the Service will seek to coordinate any action concerning cancellation of the APA with the foreign competent authority.

.07 Revising the APA.

(1) If a critical assumption has not been met, or there has been a change in law or treaty as described in section 11.09 of this revenue procedure, the APA may be revised by agreement of the parties. If such agreement cannot be achieved, the APA will be cancelled.

(2) If a critical assumption has not been met, the taxpayer must notify the APA Director, including with the notification supporting documentation and a statement whether a revision appears appropriate. The taxpayer shall file the notification at any time prior to the last date permitted for filing the annual report for the year in which the failure to

meet a critical assumption occurred. In providing the notification, the taxpayer must follow the procedures contained in sections 5.11 through 5.13 of this revenue procedure.

(3) If a critical assumption has not been met, the taxpayer and the Service will discuss how to revise the[*59] APA. If the taxpayer and the Service cannot execute a revised agreement, the APA will be cancelled as of the beginning of the taxable year in which the failure to meet a critical assumption occurred. If the Service and the taxpayer can agree on a revised APA, the effective date of the revised APA will be stated in the new APA.

(4) If the Service and the taxpayer agree to revise an APA that has been subject to competent authority agreement, the revised APA will be submitted to the U.S. competent authority in order to seek the consent of the foreign competent authority to the revised APA. If the foreign competent authority refuses to accept the revised APA, or if the competent authorities cannot agree on a revised APA agreeable to all parties, the taxpayer and the Service may: (a) agree to continue to apply the existing APA, (b) agree to apply the revised APA or agree to further revision thereof, or (c) agree to cancel the APA as of an agreed date. If such agreement cannot be achieved, the APA will be cancelled pursuant to section 11.07(1) of this revenue procedure.

.08 Renewing the APA.

A taxpayer may request renewal by following the form and procedures that apply to initial[*60] APA requests. The taxpayer must submit the user fee as required under section 5.14 of this revenue procedure, and must provide appropriate supporting documentation with the request. Unless otherwise agreed by the Service, the taxpayer should file the request to renew no later than nine months before the expiration of the initial term or any renewal term.

.09 Change in Law or Treaty.

If there is a change in any applicable U.S. law or treaty that changes the Federal income tax treatment of any matter covered by the APA, the new law or treaty provision supersedes the APA to the extent the APA is inconsistent therewith. The parties may revise the APA under section 11.07 of this revenue procedure to reconcile it with the new law or treaty provision.

SEC. 12. DISCLOSURE

The information received or generated by the Service during the APA process relates directly to the existence and amount of tax liability of the taxpayer under the Internal Revenue Code. Therefore, the APA and such information are subject to the confidentiality requirements of § 6103. In addition, the APA and such information may be confidential pursuant to the provisions of income tax conventions, or other[*61] rules applicable to communications with foreign governments.

SEC. 13. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 91--22, 1991--1 C.B. 526, is superseded. Rev. Proc. 96--13 is modified. Rev. Proc. 96--1 is modified.

SEC. 14. EFFECTIVE DATE

This revenue procedure will apply to all APA requests, including requests for renewal, received on or after December 31, 1996, except that (i) section 7.08 shall apply to all such APA requests and APA requests that have been filed on or after the effective date of Rev. Proc. 96--13, (ii) section 8.02 and/or section 8.03 may at the taxpayer's request apply to an APA request filed prior to such date and with respect to which an APA has not been concluded, and (iii) any provision of section 5.14 may apply to a request filed prior to such date and with respect to which an APA has not been concluded, if the taxpayer demonstrates that such application is necessary to avoid unfairness to the taxpayer.

SEC. 15. PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have [*62]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 in this revenue procedure are in sections 4.02, 5, 8.02, 9, 11.01, 11.02(1), 11.04, 11.07, and 11.08. 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 5,250 hours.

The estimated average burden for an APA prefiling conference [*63] 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 160.

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 Office of the Office of the Associate Chief Counsel (International). For further information regarding this revenue procedure contact Ms. Carolyn Fanaroff or Ms. Sherri New at (202) 874--4360 (not a toll-free number).

Rev. Proc. 96--53

Section 482 -- Allocations Between Related Parties

1996-2 C.B. 375; 1996 IRB LEXIS 321; 1996-49 I.R.B. 9; REV. PROC. 96-53

December 2, 1996

[*1]

SECTION 1. PURPOSE

This revenue procedure updates and supersedes Revenue Procedure 91--22, 1991--1 C.B. 526, and informs taxpayers how to secure an advance pricing agreement ("APA") from the Office of the Associate Chief Counsel (International) covering the prospective determination and application of transfer pricing methodologies ("TPMs") for international transactions. An APA is an agreement between the Service and the taxpayer on the TPM to be applied to any apportionment or allocation of income, deductions, credits, or allowances between or among two or more organizations, trades, or businesses owned or controlled, directly or indirectly, by the same interests. The TPM thus represents the application to the taxpayer's specific facts and circumstances of the best method within the meaning of the income tax regulations under § 482 of the Internal Revenue Code ("the regulations"), as agreed pursuant to negotiations between the Service and the taxpayer.

SEC. 2. OVERVIEW

Under the APA request procedure, the taxpayer proposes a TPM and provides data intended to show that the TPM is the appropriate application of the[*2] best method within the meaning of the regulations for determining arm's length results between the taxpayer and specified affiliates with respect to specified intercompany transactions. The Service evaluates the APA request by analyzing the data submitted and any other relevant information. After discussion, if the taxpayer's proposal is acceptable, the parties execute an APA covering the proposed TPM. APAs often involve agreements with foreign competent authorities under income tax conventions.

SEC. 3. PRINCIPLES OF THE APA PROCESS

.01 The APA process is designed to be a flexible problem-solving process, based on cooperative and principled negotiations between taxpayers and the Service.

.02 APAs are intended to reflect agreement between the taxpayer and the Service on the best method, within the meaning of the regulations, for determining arm's length prices, and the proper application of the best method to the taxpayer's specific facts and circumstances (that is, the TPM). In negotiations for APAs involving one or more foreign competent authorities ("bilateral" and "multilateral" APAs), the initial negotiating position of the U.S. competent authority will reflect the Service's[*3] opinion, based on consultation with the taxpayer, of the best method within the meaning of the regulations and the appropriate TPM.

.03 The taxpayer must, to the extent feasible, secure relevant pricing data from closely comparable uncontrolled transactions. If this information cannot be obtained, the taxpayer must identify any transactions it believes may be comparable, but for which reliable data is unavailable. Where such transactions cannot be identified, the taxpayer must, to the extent possible, secure relevant pricing data from uncontrolled transactions that are similar, even though not closely comparable, and propose adjustments to account for differences between such uncontrolled transactions and its own operations. The APA process may apply notwithstanding that no comparable uncontrolled transactions can be identified. In such cases, a taxpayer must demonstrate that the proposed TPM otherwise satisfies the requirements of § 482 and this revenue procedure.

.04 The APA Policy Board (the "Policy Board") consists of the Associate Chief Counsel (International), the Assistant Commissioner (International), and the Assistant Commissioner (Examination). The Policy Board establishes[*4] Service policy on matters of substantial general importance pertaining to the APA Program.

.05 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 shall, directly or by delegation, take any actions necessary for carrying out the provisions of this revenue procedure.

.06 Application of the TPM to tax years prior to those covered by the APA ("rollback" of the TPM) is an effective means of enhancing voluntary compliance and an effective use of resources in addressing unresolved transfer pricing issues. It is Service policy that, whenever feasible (based, for example, on consistency of facts, law, and available records in the prior years), the TPM should be used for resolving such issues for prior taxable years. As provided in section 8 of this revenue procedure, the taxpayer may request that the Service consider a rollback in connection with a particular request. Taxpayers should recognize that, even absent a request for a rollback, the Service may, under regularly applicable procedures, determine that the TPM agreed to in an APA should be applied to prior years. When[*5] applying the TPM to prior years, whether or not at the request of the taxpayer, adjustments may be made to reflect differences in facts, economic conditions, and applicable legal rules.

.07 The filing of an APA request does not put into abeyance any examination or other enforcement proceeding. Service personnel responsible for APAs and for enforcement proceedings involving the taxpayer shall, to the extent feasible, coordinate their activities so as to avoid duplicative information requests to the taxpayer, to enhance the efficiency of Service operations and to reduce overall taxpayer compliance burdens.

.08 Prompt and fair resolution of APA requests and renewals, in keeping with the demands of the multinational economic environment, are central goals of the APA process.

.09 The Service intends that the APA process will retain the flexibility to address the needs of particular taxpayers. To this end, the Service and the taxpayer may, by agreement, adopt special procedures, including simplified procedures, that depart from those set forth in this revenue procedure. Such special procedures might be warranted, for example, in order to meet the needs of small business taxpayers, or[*6] in order to facilitate simultaneous negotiation of APAs by the taxpayer, the Service, and foreign competent authorities.

SEC. 4. PREFILING CONFERENCES

.01 Some cases are not suitable for APAs. Even in suitable cases, the extent of information needed and scope of the necessary written request will vary from case to case. Therefore, the taxpayer may request one or more prefiling conferences to explore informally the suitability of an APA and to clarify what data, documentation, and analyses are likely to be necessary in order for the Service to be able to consider a request; the need for an independent expert; potentially applicable TPMs; the possibility of an agreement among competent authorities; and the Service's schedule and method for coordinating and evaluating the request.

.02 To schedule a prefiling conference, the taxpayer or its representative should contact the APA Office with three alternative dates for the prefiling conference. The taxpayer may request a prefiling conference either on the basis that its identity will be made known in connection with the conference, or that it will participate in the conference on an anonymous basis. If the taxpayer chooses to make[*7] its identity known in the conference, representatives of the District and of any Appeals or District Counsel Office with responsibility for the taxpayer's returns normally will participate in the prefiling conference. If the taxpayer initially requests a prefiling conference on an anonymous basis, then chooses to identify itself, the conference may be rescheduled to permit necessary personnel to participate. When requesting a prefiling conference on an identified basis, the taxpayer must inform the APA Office whether transactions similar or related to those to be covered by the proposed APA are currently under consideration by Examination, Appeals or Counsel. Taxpayers should, at least one week prior to a prefiling conference, send a brief prefiling submission to the APA Office that confirms the date, time and place of the prefiling conference; lists the persons attending the prefiling conference for the taxpayer; and outlines the issues to be discussed at the prefiling conference. If the prefiling submission is ten pages or less, it may be sent by facsimile; if the prefiling submission exceeds ten pages, seven copies and one original should be delivered pursuant to the instructions[*8] contained in section 5.13 of this revenue procedure.

SEC. 5. CONTENT OF APA REQUESTS

.01 General.

(1) All materials submitted with the request become part of the Service's file and will not be returned. Therefore, original documents should not be submitted.

(2) The taxpayer must submit copies of any documents relating to the proposed TPM and must ensure that all submitted information is properly labeled, indexed, and referenced in the request. Any previously-submitted documents that the taxpayer wishes to associate with the request must be referenced in the request. 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, certify that the items exist at the time the request is submitted, state where the items are located, state whom the Service can contact to secure the items, and confirm that the items will promptly be made available upon request.

(3) All documents submitted in a foreign language must be accompanied by an English translation.

(4) The user fee should be submitted with the request, unless previously submitted.

.02 Explanation of the Proposed [*9] TPM.

The taxpayer must provide a detailed explanation and analysis of each proposed TPM based on the principles discussed in sections 3.02 and 3.03 of this revenue procedure. The request should illustrate each proposed TPM by applying it, in a consistent format, to the prior three taxable years' financial and tax data of the parties. When 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. If coverage of three taxable years is inappropriate for any reason, the taxpayer should provide data for an appropriate date range and explain why this range was chosen.

.03 General Factual and Legal Items for All Proposed TPMs.

Unless otherwise agreed in a prefiling conference, each request must include, in addition to any other items specified in this revenue procedure, the following items:

(1) The organizations, trades, businesses, and transactions that will be subject to the APA.

(2) The names, addresses, telephone numbers, and taxpayer identification numbers of the controlled taxpayers that are parties to the requested APA (the parties). [*10]

(3) A properly completed Form 2848 for any persons authorized to represent the parties in connection with the request. If the taxpayer or the taxpayer's authorized representative has retained any other person or persons (including, but not limited to, a law firm, accounting firm, or economic consulting firm) to assist the taxpayer in pursuing the APA request, the taxpayer must also provide a separate written authorization for disclosures to such person or persons and their employees during the Service's consideration of the request, pursuant to the instructions in § 301.6103(c)--1 of the Income Tax Regulations.

(4) A brief description of the general history of business operations, worldwide organizational structure, ownership, capitalization, financial arrangements, principal businesses, and the place or places where such businesses are conducted, and major transaction flows of the parties.

(5) Representative financial and tax data of the parties for the last three taxable years, together with other relevant data and documents in support of the proposed TPM. This item includes, but need not be limited to, data contained in Form 5471 (Information Report with Respect to a Foreign[*11] Corporation); Form 5472 (Information Report of a Foreign Owned Corporation); income tax returns; financial statements; annual reports; other pertinent U.S. and foreign government filings (for example, customs reports or SEC filings); existing pricing, distribution, or licensing

agreements; marketing and financial studies; and company-wide accounting procedures, business segment reports, budgets, projections, business plans, and worldwide product line or business segment profitability reports.

(6) The functional currency of each party and the currency in which payment between parties is made for the transactions that will be covered by the APA.

(7) The taxable year of each party.

(8) A description of significant financial accounting methods employed by the parties that have a direct bearing on the proposed TPM.

(9) An explanation of significant financial and tax accounting differences, if any, between the U.S. and the foreign countries involved that have a bearing on the proposed TPM.

(10) A discussion of any relevant statutory provisions, tax treaties, court decisions, regulations, revenue rulings, or revenue procedures that relate to the proposed TPM.

(11) A statement describing[*12] 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 any such issues. The same information may also be required for similar issues involving foreign tax authorities.

.04 Specific Factual Items for a Proposed TPM other than a Cost Sharing Arrangement.

The following information may be appropriate to establish the arm's length basis of the proposed TPM under § 482:

(1) Pertinent measurements of profitability and return on investment (for example, gross profit margin or markup, gross income/total operating expenses, net operating profit margin, or return on assets).

(2) A functional analysis of each party setting forth the economic activities performed, the assets employed, the economic costs incurred, and the risks assumed.

(3) An economic analysis or study of the general industry pricing practices and economic functions performed within the markets and geographical areas to be covered by the APA.

(4) A list of the taxpayer's competitors and a discussion of any uncontrolled transactions, lines of business[*13] or types of businesses that may be comparable or similar to those addressed in the request.

(5) A detailed presentation of the research efforts and criteria used to identify and select possible independent comparables and of the application of the criteria to the potential comparables. This presentation should include a list of potential comparables and an explanation of why each was either accepted or rejected.

(6) A detailed explanation of the selection and application of the factors used to adjust the activities of selected independent comparables for purposes of devising the proposed TPM. Examples of possible adjustments include adjustments to accord with product line segregations; for functional differences relating to activities performed, assets employed, risks and costs incurred; for volume or scale differences; and for differing economic and market conditions.

.05 Specific Factual Items for a Cost Sharing Arrangement.

The taxpayer must apply the cost sharing regulations under § 482 in developing the cost sharing arrangement proposed in the request. The following illustrates information that may be appropriate to establish that the proposed arrangement is a qualified[*14] cost sharing arrangement:

(1) The history of the business operations, the geographic locations, and principal business activities (for example, manufacturing or marketing) of each of the participants.

(2) Documentation of the arrangement and any changes made to it, along with an explanation and the dates thereof.

(3) The participants, their dates of entry, each participant's contribution to the arrangement, each participant's interest in any covered intangibles, and how each participant reasonably anticipates that it will derive benefits from the use of covered intangibles; a statement whether there has been or will be any transfer by any participant of covered intangibles to another taxpayer under common control and, if so, how benefits will be reflected under those circumstances; and evidence of participants' compliance with the reporting requirements under the cost sharing regulations.

(4) The method for calculating each participant's share of intangible development costs and the reason why such method can reasonably be expected to reflect that participant's share of anticipated benefits; and a statement whether and how the participants' shares of intangible development costs [*15] will be adjusted to account for changes in economic conditions, the business operations and practices of the participants, and the ongoing development of intangibles under the arrangement.

(5) The scope of the research and development to be undertaken, including the intangible or class of intangibles intended to be developed.

(6) The duration of the arrangement; the conditions under which the arrangement may be modified or terminated; and the consequences of such modification or termination, such as the interest that each participant will receive in any covered intangibles.

(7) The scope of intangible development costs, and which costs are included and which are excluded (for example, costs of technology acquired from third parties; non-product specific development costs; costs associated with abandoned projects; costs associated with specific stages of product development; and relevant labor, material, and overhead costs); a description of any services performed for participants to 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, [*16] and the costs borne by each participant, pursuant to the arrangement.

(8) The basis used for measuring benefits, the projections used to estimate benefits, and why such basis and projections yield the most reliable estimate of reasonably anticipated benefits; 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 such amounts would be taken into account; and, for a representative period, a comparison of projected and actual benefit shares.

(9) The accounting method used to determine the cost and benefits of the intangible development (including the method used to translate foreign currencies), and to the extent that the accounting method differs materially from U.S. generally accepted accounting principles, an explanation of any material differences.

(10) Prior research, if any, undertaken in the intangible development area; any tangible or intangible property made available for use in the arrangement and any compensation paid for that property (specifying the amount, payor and payee, and how such compensation is determined); and any other information used to establish[*17] the value of preexisting and covered intangibles.

(11) Whether and how participants may join or leave the arrangement (or otherwise change their interests in covered intangibles); any adjustments that will be made to the participants' interests in covered intangibles in such cases; any payments that must be made in such cases, and how such payments will be calculated and made; and whether any changes in the participants' interests in covered intangibles have already occurred, any compensation paid for those interests, and any information used to establish the value of such interests.

(12) How cost sharing payments and buy-in or buy-out payments (i.e., payments made when a participant contributes intangibles, or acquires or relinquishes an interest in covered intangibles) made or received have been treated for U.S. income tax purposes.

(13) Representative internal manuals, directives, guidelines, and similar documents prepared for purposes of implementing or operating the cost sharing arrangement (for example, research and development committee meeting

minutes, market studies, economic impact analyses, capital expenditure budgets, engineering studies, reports and studies of trends[*18] and profitability in the industry, and financial analyses for financing and cash flow purposes).

(14) Each participant's gross and net profitability (historical for five taxable years and projected for two taxable years) with regard to the product area covered by the arrangement.

.06 Discussion of Collateral Income Tax Issues.

The taxpayer must discuss any relevant collateral income tax issues (for example, issues relating to foreign tax credits) raised by the proposed TPM under United States law.

.07 Critical Assumptions.

The taxpayer must propose and describe a set of critical assumptions. A critical assumption is any fact (whether or not within control of the taxpayer) related to the taxpayer, a third party, an industry, or business and economic conditions, the continued existence of which is material to the taxpayer's proposed TPM. Critical assumptions might include, for example, a particular mode of conducting business operations, a particular corporate or business structure or a range of expected business volume.

.08 Contents of Annual Report.

Section 11.01 of this revenue procedure provides that the taxpayer must file an annual report for each taxable year[*19] covered by the APA. The taxpayer should propose in the request a list of items to be included in each report. For example, the report should generally include the following items: (a) the application of the TPM to the actual operations for the year; (b) a description of any material lack of conformity with critical assumption and the reasons therefor (or, if there has been no material lack of conformity with critical assumptions, a statement to that effect); and (c) an analysis of any compensating adjustments to be paid by one entity to the other, and the manner in which the payments are to be made. Other items may be appropriate to the taxpayer's particular circumstances.

.09 Term.

(1) The taxpayer must propose an initial term for the APA. For example, the APA could take effect at the beginning of the taxable year during which it was requested or signed, and last for three taxable years. The term should be appropriate to the industry, product, or transaction involved.

(2) The APA request must be filed no later than the time prescribed by law (including extensions) for filing the taxpayer's Federal income tax return for the first taxable year to be covered by the APA. For purposes[*20] of the preceding sentence, an APA request will be considered filed on the date payment of the required user fee is made (within the meaning of § 7502(a)), provided that a substantially complete APA request is filed with the Service within 120 days thereafter, subject to extension by the Service based on a showing of substantial unforeseen circumstances.

.10 Request for Competent Authority Consideration.

The taxpayer must state whether any of the parties to a request are residents of or conduct activities in a foreign country that has a tax treaty with the United States or in a possession of the United States, and whether the taxpayer proposes an agreement among competent authorities or an agreement described in Rev. Proc. 89--8, 1989--1 C.B. 778 (see section 7 of this revenue procedure for guidelines). For purposes of this revenue procedure, "competent authority" includes the U.S. and foreign competent authorities under income tax treaties to which the U.S. is a party, and also includes the Assistant Commissioner (International) acting with respect to a possession tax agency described in Rev. Proc. 89[*21] --8, as well as a designated possession tax official within the meaning of that revenue procedure. If the taxpayer proposes an agreement among competent authorities for the initial term of the APA, the taxpayer's request must include the information described in sections 4.05(a) and (b) and, in a separate document, section 4.05(m), of Rev. Proc. 96--13, 1996--3 I.R.B. 31, or similar information pursuant to a request for relief under Rev. Proc. 89--8.

.11 Perjury Statement.

The taxpayer must include in any request for an APA, and any supplemental submission, a declaration in the following form:

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

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[*22] personal knowledge of the facts and whose duties are not limited to obtaining letter rulings or determination letters from the Service, or negotiating APAs. The person signing for a trust or a partnership must be a trustee or a partner who has personal knowledge of the facts.

.12 Signatures.

The taxpayer or the taxpayer's authorized representative must sign the request. If an authorized representative is to sign, the taxpayer and representative must conform to the rules of Rev. Proc. 96--1, 1996--1 I.R.B. 8 (or its successor).

.13 Copies and Mailing.

(1) Requests or other documents containing user fees must be mailed or delivered to
Internal Revenue Service
Attn: CC:DOM:CORP:T
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044,

or 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 may either be mailed to
Advance Pricing Agreement Program
Internal Revenue Service
Attn: CC:INTL
Room 3501, 1111 Constitution Ave., N.W.
Washington, DC 20224

or may be delivered[*23] to
Advance Pricing Agreement Program
Internal Revenue Service
Attn: CC:INTL
5th Floor, 950 L'Enfant Plaza, S.W.
Washington, DC 20024.

The taxpayer should provide the original and seven copies of its APA request and of all supplemental materials submitted while the request is pending.

.14 User Fees.

(1) The user fee for each separate request for an advance pricing agreement is \$25,000 except as provided below in this section 5.14 of this revenue procedure.

(2) The user fee for each separate request for an advance pricing agreement from a taxpayer with gross income (as determined in section 5.14(7) of this revenue procedure) of at least \$100,000,000 and less than \$1,000,000,000 is \$15,000.

(3) The user fee for each separate request for an advance pricing agreement or renewal from a taxpayer with gross income (as determined in section 5.14(7) of this revenue procedure) of less than \$100,000,000 is \$5,000.

(4) Notwithstanding sections 5.14(1) and (2) of this revenue procedure, if it is apparent on the face of the APA request that the transaction or transactions subject to the request involve tangible property and/or services the total annual[*24] value of which is not in excess of \$50,000,000, or payments for intangible property (such as royalties) not in excess of \$10,000,000 annually, the user fee for each separate request shall not be more than \$7,500.

(5) As explained in section 5.14(8) of this revenue procedure, an APA request that involves pricing issues in more than one foreign jurisdiction will normally be considered to constitute multiple bilateral requests. The user fee for the first such request shall be determined under sections 5.14(1), (2), (3), (4), or (6) of this revenue procedure as applicable. The user fee for each subsequent bilateral request, however, shall be not more than \$7,500, if such subsequent bilateral request (a) involves the same product line, goods, services, or intangibles, and the same issues, as involved in the first request; (b) covers the same taxable years as covered by the first request; and (c) proposes the same TPM as the first request.

(6) Notwithstanding sections 5.14(1) and (2) of this revenue procedure, the user fee for a request for renewal of an APA, when the material facts, critical assumptions and proposed TPM have not substantially changed, shall not be more than \$7,500. [*25]

(7) For purposes of sections 5.14(2) and 5.14(3) of this revenue procedure, gross income of a U.S. person (or non-U.S. person filing a federal income tax return with respect to all such person's income) is equal to "total income" as reported on the last federal income tax return for such person (as amended) filed for a full (12 month) taxable year ending before the date the request was filed, plus "cost of goods sold" as reported on that federal income tax return, plus any income not subject to tax under section 103 for that period; and gross income of all other persons shall be computed on an equivalent basis (that is, gross receipts or economic income plus cost of goods sold) for such person's most recently completed 12-month year. For purposes of sections 5.14(2) and (3) of this revenue procedure, gross income of a taxpayer shall include the gross income (determined pursuant to the preceding sentence) of all organizations, trades or businesses (whether or not incorporated, whether or not resident or organized in the U.S., and whether or not affiliated for tax purposes) owned or controlled directly or indirectly by the same interests controlling the taxpayer.

(8) For purposes [*26] of this section 5.14 of this revenue procedure, a separate request constitutes a request for agreement on a transfer pricing methodology or methodologies comprising a closely related set of facts, such that review of the single set of facts will suffice to determine the suitability of all the methodologies involved in the separate request. For example, an APA submission involving the pricing of tangible products and the manufacturing services provided by a parent to a subsidiary with respect to those products usually would constitute one separate request. Similarly, a submission involving separate product lines manufactured in the same location by substantially similar processes usually would constitute one separate request. However, a submission involving product lines manufactured at different locations, or by manufacturing processes that are not substantially similar, usually would constitute more than one request. The fact that an APA submission involves pricing issues related to more than one foreign jurisdiction, and thus requires analyses of separate factual or economic issues, as well as negotiations between the U.S. and more than one foreign competent authority, will normally[*27] result in treatment of the submission as more than one request. However, such separate requests may be eligible for reduced user fees under paragraph (5) of this section 5.14 of this revenue procedure.

(9) If an APA request is submitted or processed under paragraphs (2), (3), (4), (5), or (6) of this section 5.14 of this revenue procedure, and it later becomes apparent that the request does not meet the criteria for application of such paragraphs, the Service will request an additional user fee to conform the request to the proper amount under this revenue procedure, as appropriate. The taxpayer may either pay such additional fee and continue the APA process or may withdraw the request. If the taxpayer withdraws the request, the Service may return the user fee to the taxpayer if the Service determines that such action would be appropriate under the circumstances. Except to the extent inconsistent with this revenue procedure, the principles of Rev. Proc. 96--1 (or its successor), including but not limited to section 14 thereof, shall apply to all questions related to user fees in connection with APAs. The APA Team Leader described in section 6.04 of this[*28] revenue procedure, prior to the initial meeting with the taxpayer on a filed APA, will make a determination regarding the correctness of the taxpayer's initial payment of user fees and request any necessary corrections.

(10) The chart below summarizes the foregoing user fee provisions:

Taxpayer Gross Income	Each Additional			
	Original Request	Multilateral Request n1	Routine Renewal n2	Small Transactions n3
\$ 1 billion or more	\$ 25,000	\$ 7,500	\$ 7,500	\$ 7,500
less than \$ 1 billion and greater than or equal to \$ 100 million	15,000	\$ 7,500	\$ 7,500	\$ 7,500
less than \$ 100 million	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000

n1 Only if such additional request involves the same issues, covers the same years, and proposes the same TPM as the first request; see section 5.14(5).

n2 Only if the material facts, critical assumptions, and proposed TPM have not substantially changed; see section 5.14(6).

n3 Regardless of taxpayer size, applies to transactions that involve (i) tangible property or services valued at no more than \$ 50 million annually, or (ii) payments for intangible property not in excess of \$ 10 million annually; see section 5.14(4).

SEC. 6. PROCESSING [*29] OF APA REQUESTS

.01 Initial Contact.

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

.02 Coordination with Other IRS Offices.

Upon receipt of a request, the APA Director will coordinate the evaluation of the request with other Service officials, such as the District Director, Regional Director of Appeals and District Counsel. In appropriate cases, such as where a request proposes an agreement between competent authorities, the APA Director will coordinate with the U.S. competent authority.

.03 Evaluation Process.

The Office of Associate Chief Counsel (International), in coordination with the appropriate District Director and other appropriate Service officials, 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[*30] evaluation of the request will not constitute an examination or inspection of the taxpayer's books and records under § 7605(b) or any other provision of the Code.

.04 Formation of the APA Team and Designation of Team Leader.

Within 45 days of receiving the taxpayer's APA request and any required user fees, the APA Director will appoint an APA Team to review the request. The APA Team normally will consist of at least one representative of the Office of Associate Chief Counsel (International), as well as representatives of the appropriate District and District Counsel and, when appropriate, Appeals and the U.S. competent authority. The APA Director will appoint a Team Leader to oversee

the APA Team's activities. Whenever reasonably feasible, if a prefiling conference has been held with the taxpayer, the Team Leader will be appointed from among the IRS representatives at the prefiling conference.

.05 Negotiation and Drafting.

(1) The APA Team shall arrange with the taxpayer for an initial meeting to take place within 60 days of receiving the taxpayer's APA request and required user fee. In connection with the initial meeting, the APA Team and the taxpayer shall agree on a[*31] Case Plan and Schedule, to which everyone involved in the APA--both government and taxpayer personnel--will be expected to adhere. The Case Plan and Schedule should list each question raised by the initial Service review of the APA request and should include a schedule for seeking to resolve each. The Case Plan and Schedule generally should reflect agreement between the APA Team and the taxpayer on the scope and nature of any additional information that will be required to resolve these questions in order to negotiate an APA. Firm dates should be agreed upon for case milestones, including: (a) submission of any necessary additional information by the taxpayer; (b) evaluation of the information by the government; (c) negotiation of a recommended agreement or competent authority negotiating position; and (d) presentation of the recommended agreement or competent authority negotiating position in writing to the Associate Chief Counsel (International).

(2) 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[*32] authority of the treaty partner or U.S. possession involved to minimize the time needed for competent authority resolution.

(3) To minimize delays caused by the need to coordinate different parties' schedules on short notice, the time and place of meetings required for any steps in the case should be determined in the Case Plan and Schedule.

(4) Failures by either the taxpayer or the APA Team to meet case milestones will be addressed promptly, normally in a meeting or telephone conference involving the APA Director, members of the Service APA Team, and the taxpayer. If a taxpayer has failed to meet one of the case milestones, the APA Director will assist the taxpayer in remedying any difficulties and will propose a course of action to ensure that milestones can be met. Substantial and consistent failure by the taxpayer to comply with the Case Plan and Schedule will be treated by the Service as a withdrawal of the APA request. In this event, if the taxpayer wishes to continue to pursue the APA, the taxpayer will be required to refile the request and pay a new user fee. If the Service fails to meet a case milestone, the APA Director, the Service APA Team, and supervisors in the District[*33] and Region, as appropriate, shall work together promptly to remedy the situation.

(5) In some circumstances, development of the case after agreement on the Case Plan and Schedule will suggest, to both the APA Team and the taxpayer, that some milestone dates should be adjusted. To preserve flexibility, the APA Team and the taxpayer may amend the Case Plan and Schedule by mutual agreement, consistent with the need to maintain progress toward completion of the case as expeditiously as feasible.

(6) The function of the APA Team is to negotiate and recommend an agreement, and if applicable to recommend in consultation with the taxpayer a competent authority negotiating position, to the Associate Chief Counsel (International). Negotiations between taxpayers and the APA Team should be documented by means agreed between the parties. The District Director with responsibility for the taxpayer's returns shall be provided an opportunity to review and comment on the draft APA in the case of a unilateral APA, and the proposed initial US competent authority negotiating position in the case of a bilateral or multilateral APA. Signature of an APA by the Associate Chief Counsel (International) and[*34] the taxpayer will constitute agreement to the APA.

.06 Withdrawing the Request.

The taxpayer may withdraw the request at any time before the execution of the APA. Pursuant to the principles of Rev. Proc. 96--1 (or its successors), including but not limited to section 14.09 thereof, the user fee generally will not be refunded if the taxpayer withdraws its request for an APA.

.07 Rejecting the Request.

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

SEC. 7. COMPETENT AUTHORITY CONSIDERATION

.01 When any of the parties to a request are entitled to seek relief under the mutual agreement provision of a tax treaty between a foreign country and the United[*35] 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. 96--13, 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[*36] APA will be sought among the taxpayer, the Service, and the foreign competent authority. As a general matter, the taxpayer is encouraged to submit APA requests and related correspondence simultaneously to the Service and to foreign competent authorities involved in the requests.

.02 The purpose of the competent authority agreement is to avoid double taxation. If such an agreement is not acceptable to the taxpayer, the taxpayer may withdraw the APA request (see section 6.06 of this revenue procedure). If the competent authorities are unable to reach an agreement or the taxpayer does not accept the competent authority agreement, the Service will attempt to negotiate a unilateral APA with the taxpayer (see section 7.07 of this revenue procedure).

.03 The taxpayer must cooperate with the Service and the U.S. competent authority, pursuant to the standards set forth in Rev. Proc. 96--13 and any other applicable revenue procedures. Any information received or prepared by the Service, including information furnished by the taxpayer or the related foreign entity, will be subject to the restrictions on disclosure of tax related information provided by U.S. law and[*37] the applicable income tax convention.

.04 It may be necessary to request sensitive confidential data (such as trade secrets) which, if disclosed, could harm the taxpayer's competitive position. In such cases, the parties will attempt to negotiate a mechanism to permit verification by a foreign competent authority without disclosing such information.

.05 When the competent authorities enter into an agreement covering an APA, the Service will, to the extent practicable, 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 The U.S. competent authority will seek to persuade the foreign competent authority to use APA data only on terms similar to those described in sections 10.04 and 10.05 of this revenue procedure.

.07 To minimize taxpayer and governmental uncertainty and administrative cost, bilateral or multilateral APAs generally[*38] 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. When a unilateral APA request involves taxpayers operating in a country that is a treaty partner, the Service may notify the treaty partner of the filing of the request and provide the treaty partner with other information related to the request, under normal rules governing the exchange of information under income tax treaties. In some circumstances, procedures agreed upon with particular foreign competent authorities, or the requirements of proper relations with treaty partners, may preclude unilateral APAs.

.08 Section 7.05 of Rev. Proc. 96--13 provides in part that, if a taxpayer reaches a settlement on an issue with Counsel 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[*39] change such agreement. The restrictions imposed under section 7.05 of Rev. Proc. 96--13 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 such APA's TPM (as discussed in sections 3.06 and 8 of this revenue procedure), section 7.05 of Rev. Proc. 96--13 will apply to such rollback years in the regular manner.)

SEC. 8. ROLLBACKS

.01 The taxpayer may indicate in its APA request, or at any time prior to the completion of APA negotiations, that it desires for the Service to consider using the TPM of the APA to resolve transfer pricing issues[*40] for years prior to the earliest year covered by the APA. In general, the principles set forth in section 3.06 of this revenue procedure will govern the Service's consideration of this request (the "rollback request"). When a rollback request is made after submission of the APA request, the taxpayer must provide the request to the APA Director at the address indicated in section 5.13(2) of this revenue procedure.

.02 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. 96--13. The Office of Associate Chief Counsel (International), the District Director, and the U.S. competent authority will coordinate consideration of the request. The taxpayer's request must include all information required for accelerated competent authority consideration under Rev. Proc. 96--13, 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, except that, in order to facilitate[*41] effective competent authority negotiations, the Service may require that, if accelerated competent authority consideration is to be granted, it will apply to one or more specified years. In exercising their regular discretion over the conduct of accelerated competent authority consideration, Service officials shall seek to implement the policy concerning APA rollbacks stated in section 3.06 of this revenue procedure.

.03 If a rollback request is submitted in connection with a bilateral or multilateral APA and involves a taxable year that is under the jurisdiction of Appeals, the rollback request will be deemed to constitute an application for simultaneous Appeals and competent authority consideration as described in section 8 of Rev. Proc. 96--13 and will be subject to the rules set forth therein. The Office of Associate Chief Counsel (International), the Regional Director of Appeals, and the U.S. competent authority will coordinate consideration of the request. In exercising their regular discretion over the conduct of simultaneous Appeals and competent authority consideration, Service officials shall seek to implement the policy concerning APA rollbacks[*42] stated in section 3.06 of this revenue procedure.

.04 Subject to the policy set forth in section 3.06 of this revenue procedure, the determination whether a rollback shall be granted with respect to a taxable year is within the discretion of the Service official with jurisdiction over the taxable year subject to the rollback--typically, either the District Director, the Regional Director of Appeals, the Assistant Commissioner (International) (for matters subject to competent authority negotiations), or the District Counsel (for matters under litigation). Except to the extent inconsistent with this revenue procedure, normal procedures for resolving tax issues, including but not limited to closing agreements and other settlement documents and Forms 870 and 870AD, shall be used to implement APA rollbacks.

SEC. 9. INDEPENDENT EXPERT OPINION

.01 The taxpayer may be required to provide at its own expense an independent expert, acceptable to both the taxpayer and the Service (and, in a bilateral or multilateral proceeding, the foreign competent authority or authorities) to review and opine on the proposed TPM. The taxpayer may suggest in its APA request whether an independent expert[*43] is needed, or the Service (or, if applicable, the foreign competent authority) may determine that an independent expert is needed for the evaluation of the taxpayer's request.

.02 For purposes of this revenue procedure, an expert is any person who, by agreement between the taxpayer and the Service (and, if involved, the foreign competent authority), possesses expert education or experience in a field of study, industry or geographic area that is relevant to the subject matter of the taxpayer's APA request.

.03 For purposes of this revenue procedure, an expert is independent if the expert has not participated to any material extent in the development of the request and has not in the past assisted either the Service or the taxpayer in matters substantially related to the request.

.04 If an expert is necessary, the expert will critically analyze the taxpayer's proposed TPM and render a written opinion. The opinion will address any questions and concerns raised by the Service or the taxpayer (and, if involved, the foreign competent authority); conclude whether the proposed TPM or a revised version fairly supports and produces an arm's length approach; and provide the basis for this[*44] opinion. However, the expert's opinion will not be binding on any of the parties. The taxpayer and the Service (and, if involved, the foreign competent authority) will have access to the expert's report and supporting documentation. The Service and the taxpayer shall both be kept fully informed of any communications between the other party and the independent expert, and receive copies of all information provided by such other party to the expert.

.05 If an independent expert is necessary, the taxpayer must provide a waiver under § 6103(c) to the Service for purposes of discussing returns or return information with the expert. The taxpayer must also ensure that the expert is familiar with the provisions of this revenue procedure and that any opinion rendered by the expert complies with those provisions.

SEC. 10. LEGAL EFFECT

.01 An APA is a binding agreement between the taxpayer and the Service.

.02 If the taxpayer complies with the terms and conditions of the APA, the Service will regard the results of applying the TPM as satisfying the arm's length standard, and, except as provided in this revenue procedure, will not contest the application of the TPM to the subject matter[*45] of the APA. The taxpayer remains otherwise subject to U.S. income tax laws and is entitled to any benefits otherwise available under U.S. income tax laws.

.03 Except to the extent provided by regulations, an APA shall have no legal effect except with respect to the taxpayer, taxable years and transactions to which the APA specifically relates.

.04 Except as otherwise provided by written agreement, regulations, or this revenue procedure, neither the APA nor any non-factual oral or written representations or submissions made in conjunction therewith may be introduced by the taxpayer or the Service as evidence in any judicial or administrative proceeding in relation to any tax year, transaction, or person not covered by the APA. However, taxpayers should recognize that the preceding sentence does not preclude rollback of the APA TPM, nor the discovery, use, or admissibility of non-factual material otherwise discoverable or obtained other than in the APA process merely because the same or similar material was also included in the APA or representations or submissions made in connection with the APA or presented during the APA process.

.05 Except as otherwise provided by written agreement[*46] or regulations, if an APA is not executed or if an executed APA is later revoked or canceled, neither the APA or the proposal to use a particular TPM, nor any non-factual oral or written representations or submissions made during the APA process, may be introduced by the taxpayer or the Service as an admission by the other party in any administrative or judicial proceeding for the taxable years for which the APA was requested or executed. However, taxpayers should recognize that the preceding sentence does not preclude the discovery, use, or admissibility of non-factual material otherwise discoverable or obtained other than in the APA process merely because the same or similar material was also included in the APA or representations or submissions made in connection with the APA or presented during the APA process.

SEC. 11. 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 the taxpayer's actual operations for the year and demonstrating good faith compliance with the terms and conditions of the APA. The report must include all items called for by the APA, must describe [*47]any pending or contemplated requests to renew, modify or cancel the APA, and must describe any compensating adjustments made pursuant to section 11.02 of this revenue procedure.

(2) The taxpayer shall file an original and four copies of each report, no later than 90 days after the time prescribed by law (including extensions) for filing the taxpayer's Federal income tax return for the year covered by the report, or by such other date as is specified in the APA, with the APA Director at the address indicated in section 5.13(2) of this revenue procedure. The taxpayer may also be required to file a copy of the annual report with the treaty partner or partners with respect to a bilateral or multilateral APA. The report must comply with sections 5.11 and 5.12 of this revenue procedure.

(3) The Service will contact the taxpayer regarding an annual report only if it is necessary to clarify or complete the information contained in the annual report. Additional information must be supplied by the date specified by the Service, as extended for good cause. Any contact between the taxpayer and the Service for the purpose of clarifying the information contained in the annual report will not [*48] constitute an examination, or the commencement of any examination, of the taxpayer for purposes of § 7605(b) or any other provision of the Code.

.02 Compensating Adjustments.

(1) If the results of applying the TPM differ from those contemplated by the APA, the APA may permit the taxpayer and its related foreign entity to make a compensating adjustment. For example, if the APA provides for a range of expected operating results, and the actual operating results are outside that range (but within any limits specified in the APA), the APA may permit the parties to make a compensating adjustment to bring the results to an agreed upon point within the described range. Such compensating adjustment should be reflected on the taxpayer's timely filed (with extensions) federal income tax return; if the taxpayer is not able to make such adjustments in its original return, the required compensating adjustment must in any event be made and paid within 90 days of the date prescribed for filing such return (with extensions), and reflected on an amended return filed within such period and the timely filed annual report required by section 11.01 of this revenue procedure. To the extent the APA[*49] covers years for which federal income tax returns were filed before the APA was executed, the taxpayer must make any required compensating adjustments in an amended return or returns filed within, and pay such compensating adjustments within, 90 days of entering into such APA.

(2) The taxable income and earnings and profits of both the taxpayer and its related foreign entity for a taxable year covered by an APA will include all income generated as a result of the TPM as increased or decreased by any compensating adjustment for that year. A compensating adjustment will be deemed to have been made as of the last day of the taxable year to which it applies. For all U.S. income tax purposes, after taking into consideration any compensating adjustment, the adjusted figures will be used. Provided that the taxpayer has made a good faith effort to comply with the TPM in such manner as to avoid the need for compensating adjustments, and payments of compensating adjustments are made within the time specified in section 11.02(1) of this revenue procedure, (i) the compensating adjustment will not be taken into account in the computation of any required estimated tax installments for such year, [*50] (ii) the taxpayer will not be subject to the failure to pay penalties under §§ 6651 and 6655 by reason of the compensating adjustment, and (iii) no interest will accrue on any receivable or payable established to settle such compensating adjustment. A compensating adjustment may, however, be taken into account for purposes of redetermining any foreign tax credits in accordance with § 901. Subject, where applicable, to agreement between competent authorities, the taxpayer or the related foreign entity may employ any method that accords with section 4 of Rev. Proc. 65--17, 1965--1 C.B. 833 (as modified), or any successor, for paying compensating adjustments, including checks, wire transfers, offsets through intercompany accounts, or recharacterized dividends. All actions taken with respect to such compensating adjustments must be documented and disclosed in the annual report.

(3) A "subsequent compensating adjustment" arises when the taxpayer or the Service makes normal and routine adjustments (for example, correction of computational errors) to the determination and computation of the taxpayer's TPM during the taxable year or years[*51] under the APA, as determined in accordance with the TPM. The generally applicable Code rules relating to assessment, collection and refund of tax and the principles of Rev. Proc. 65--17 (as

modified), or any successor, apply to any resulting change in Federal income tax liability because of a subsequent compensating adjustment.

(4) When an agreement between competent authorities is sought as part of the APA request, the principles stated in this section will be discussed with the appropriate foreign competent authority to seek to ensure substantially identical treatment of the taxpayer's related foreign entity.

(5) The Service and the taxpayer may agree in an APA to modify the foregoing provisions relating to compensating adjustments.

.03 Examination.

(1) If the District Director examines a tax year covered by an APA, the examination of matters covered by the APA will be limited to the factors in section 11.03(2) of this revenue procedure. The District Director will not re-evaluate the TPM itself.

(2) The District Director may require the taxpayer to establish that (a) the taxpayer has complied in good faith with the terms and conditions of the [*52]APA; (b) the material representations in the APA and the annual reports remain valid and accurately describe the taxpayer's operations; (c) the supporting data and computations used in applying the TPM were correct in all material respects; (d) the critical assumptions underlying the APA remain valid; and (e) the taxpayer has consistently applied the TPM and met the critical assumptions.

(3) If the District Director determines that any requirement in section 11.03(2) of this revenue procedure has not been satisfied, the issue will be submitted to the Associate Chief Counsel (International) for resolution. The Associate Chief Counsel (International) will decide either to continue to apply the APA; revoke the APA (see section 11.05 of this revenue procedure); cancel the APA (see section 11.06); or revise the APA (see section 11.07).

(4) The District Director may, without securing the consent of the Associate Chief Counsel (International), propose normal and routine audit adjustments, which are not related to interpretation of the TPM, to the determination and computation of the operating results of the taxpayer's TPM during the taxable year or years under examination (as determined[*53] in accordance with the TPM) without affecting the continued validity or applicability of the APA. If the taxpayer agrees with the proposed adjustments, they will be given effect through payment of additional compensating adjustments. If the taxpayer does not agree, the taxpayer may contest the proposed adjustments through normal administrative and judicial proceedings. Any changes to compensating adjustments previously made by the taxpayer, in respect of the taxable year or years under examination, that arise as a result of the audit adjustments made by the District Director will be made within ninety days of a final determination of the audit adjustments. Any compensating adjustments and changes to compensating adjustments described in this section 11.03(4) will be treated as subsequent compensating adjustments for purposes of section 11.02 of this revenue procedure.

.04 Record Retention.

(1) The taxpayer must maintain books and records sufficient to enable the Service to examine the taxpayer's compliance with the APA. The APA may specify the books and records that are necessary to fulfill this objective and may specify that compliance with the applicable provisions of the [*54] APA will constitute compliance with the provisions of §§ 6038A and 6038C with respect to transactions covered by the APA.

(2) Upon examination, information requested by the Service must be made available to the Service upon written request within 30 days, and translations must be provided within 30 days of a request for translation of specific documents, both 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's request.

.05 Revoking the APA.

(1) The Associate Chief Counsel (International) may revoke the APA if there has been 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 any of the following: the material facts set forth in the request or subsequent submissions (including the annual report), or lack of good faith compliance with the terms and conditions of the APA. Material facts are those that, if known by the Service, could reasonably have resulted[*55] in a significantly different APA (or no APA at all). The Associate Chief Counsel (International) is not required to revoke the APA and may require the taxpayer to continue to abide by it.

(2) If the APA is revoked for any reason, the revocation may be retroactive to the first day of the first taxable year for which the APA was effective.

(3) If the APA is revoked for any reason, the Service may determine deficiencies in income taxes and additions thereto in accordance with applicable provisions of the Code. In addition, (a) relief under Rev. Proc. 65--17 may be denied; (b) if the Service determines that the taxpayer may avail itself of the relief under Rev. Proc. 65--17, interest on any account receivable established under section 4.03 of that revenue procedure may be determined not to be subject to mutual agreement or correlative relief; (c) the revocation of the APA may be treated as an "egregious case" under Rev. Rul. 80--231, 1980--2 C.B. 219, with the result that the taxpayer may be denied a foreign tax credit in accordance with that ruling; and (d) the unilateral relief[*56] provisions of Rev. Proc. 96--14, 1996--3 I.R.B. 41, may not be available. When an APA has been the subject of negotiation with a foreign competent authority, the Service will seek to coordinate any action concerning revocation of the APA with the foreign competent authority.

.06 Cancelling the APA.

(1) The Associate Chief Counsel (International) may cancel the APA if the District Director, with the concurrence of the Associate Chief Counsel (International), determines that there was a misrepresentation, mistake as to a material fact, failure to state a material fact, or lack of good faith compliance with the terms and conditions of the APA (but not fraud, malfeasance or disregard) in connection with the request for the APA, or in any subsequent submissions (including the annual report). Material facts are those that, if known by the Service, would have resulted in a significantly different APA (or no APA at all).

(2) The Associate Chief Counsel (International) may waive cancellation if the taxpayer can show good faith and reasonable cause to the satisfaction of the Associate Chief Counsel (International), and if the taxpayer[*57] agrees to make any adjustment proposed by the Associate Chief Counsel (International) 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 to abide by it.

(3) If the APA is cancelled under section 11.06(1) of this revenue procedure, the cancellation will be effective as of the beginning of the year in respect of which the misrepresentation, mistake as to a material fact, failure to state a material fact, or noncompliance occurs. If, however, the cancellation results from a change in law or treaty, as provided in section 11.07(1) of this revenue procedure, the cancellation normally will be effective as of the effective date of the change in law or treaty.

(4) If the APA is cancelled for any reason, then as of the effective date of the cancellation the APA will cease to be of any further force and effect with respect to the taxpayer and the Service for U.S. income tax purposes. After the effective date of the cancellation, the tax treatment of the transactions covered by the APA will be subject to[*58] all U.S. tax rules (including treaty rules) that otherwise apply. When an APA has been the subject of negotiation with a foreign competent authority, the Service will seek to coordinate any action concerning cancellation of the APA with the foreign competent authority.

.07 Revising the APA.

(1) If a critical assumption has not been met, or there has been a change in law or treaty as described in section 11.09 of this revenue procedure, the APA may be revised by agreement of the parties. If such agreement cannot be achieved, the APA will be cancelled.

(2) If a critical assumption has not been met, the taxpayer must notify the APA Director, including with the notification supporting documentation and a statement whether a revision appears appropriate. The taxpayer shall file the notification at any time prior to the last date permitted for filing the annual report for the year in which the failure to

meet a critical assumption occurred. In providing the notification, the taxpayer must follow the procedures contained in sections 5.11 through 5.13 of this revenue procedure.

(3) If a critical assumption has not been met, the taxpayer and the Service will discuss how to revise the[*59] APA. If the taxpayer and the Service cannot execute a revised agreement, the APA will be cancelled as of the beginning of the taxable year in which the failure to meet a critical assumption occurred. If the Service and the taxpayer can agree on a revised APA, the effective date of the revised APA will be stated in the new APA.

(4) If the Service and the taxpayer agree to revise an APA that has been subject to competent authority agreement, the revised APA will be submitted to the U.S. competent authority in order to seek the consent of the foreign competent authority to the revised APA. If the foreign competent authority refuses to accept the revised APA, or if the competent authorities cannot agree on a revised APA agreeable to all parties, the taxpayer and the Service may: (a) agree to continue to apply the existing APA, (b) agree to apply the revised APA or agree to further revision thereof, or (c) agree to cancel the APA as of an agreed date. If such agreement cannot be achieved, the APA will be cancelled pursuant to section 11.07(1) of this revenue procedure.

.08 Renewing the APA.

A taxpayer may request renewal by following the form and procedures that apply to initial[*60] APA requests. The taxpayer must submit the user fee as required under section 5.14 of this revenue procedure, and must provide appropriate supporting documentation with the request. Unless otherwise agreed by the Service, the taxpayer should file the request to renew no later than nine months before the expiration of the initial term or any renewal term.

.09 Change in Law or Treaty.

If there is a change in any applicable U.S. law or treaty that changes the Federal income tax treatment of any matter covered by the APA, the new law or treaty provision supersedes the APA to the extent the APA is inconsistent therewith. The parties may revise the APA under section 11.07 of this revenue procedure to reconcile it with the new law or treaty provision.

SEC. 12. DISCLOSURE

The information received or generated by the Service during the APA process relates directly to the existence and amount of tax liability of the taxpayer under the Internal Revenue Code. Therefore, the APA and such information are subject to the confidentiality requirements of § 6103. In addition, the APA and such information may be confidential pursuant to the provisions of income tax conventions, or other[*61] rules applicable to communications with foreign governments.

SEC. 13. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 91--22, 1991--1 C.B. 526, is superseded. Rev. Proc. 96--13 is modified. Rev. Proc. 96--1 is modified.

SEC. 14. EFFECTIVE DATE

This revenue procedure will apply to all APA requests, including requests for renewal, received on or after December 31, 1996, except that (i) section 7.08 shall apply to all such APA requests and APA requests that have been filed on or after the effective date of Rev. Proc. 96--13, (ii) section 8.02 and/or section 8.03 may at the taxpayer's request apply to an APA request filed prior to such date and with respect to which an APA has not been concluded, and (iii) any provision of section 5.14 may apply to a request filed prior to such date and with respect to which an APA has not been concluded, if the taxpayer demonstrates that such application is necessary to avoid unfairness to the taxpayer.

SEC. 15. PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have [*62]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 in this revenue procedure are in sections 4.02, 5, 8.02, 9, 11.01, 11.02(1), 11.04, 11.07, and 11.08. 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 5,250 hours.

The estimated average burden for an APA prefiling conference [*63] 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 160.

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 Office of the Office of the Associate Chief Counsel (International). For further information regarding this revenue procedure contact Ms. Carolyn Fanaroff or Ms. Sherri New at (202) 874--4360 (not a toll-free number).

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