



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 26.2.2007  
SEC(2007) 246

**COMMISSION STAFF WORKING DOCUMENT**

**Report prepared by the EU Joint Transfer Pricing Forum**

**accompanying document to the  
COMMUNICATION FROM THE COMMISSION TO THE COUNCIL, THE  
EUROPEAN PARLIAMENT AND THE EUROPEAN ECONOMIC AND SOCIAL  
COMMITTEE  
on the work of the EU Joint Transfer Pricing Forum in the field of dispute avoidance  
and resolution procedures and on Guidelines for Advance Pricing Agreements within  
the EU**

{COM(2007) 71 final}

## TABLE OF CONTENTS

1.	Introduction and general considerations .....	4
1.1.	Background – what is dispute avoidance and resolution? .....	4
1.2.	What is the purpose of the Forum's work on dispute avoidance and supplementary dispute resolution? .....	5
2.	Possible forms of dispute avoidance or alternative dispute resolution procedures considered by the Forum.....	5
3.	APAs – General considerations .....	6
3.1.	APA Definitions and analysis carried out by the Forum into the current position and practices regarding APAs.....	6
3.2.	APAs – Advantages .....	7
3.3.	APAs – Possible disadvantages for tax administrations .....	8
3.4.	APAs –Possible disadvantages for taxpayers .....	9
4.	Bilateral/Multilateral APAs – the suggestions of the Forum .....	9
4.1.	APAs Best practice – legal framework .....	10
4.2.	APAs Best practice – organisation of APA procedures in Member States.....	11
4.3.	APAs Best Practice: Entry to the APA programme.....	12
4.3.1.	Entry to the APA programme, general considerations.....	12
4.3.2.	Fees .....	13
4.3.3.	Complexity thresholds .....	13
4.4.	APAs Best practice - Documentation .....	14
4.5.	APAs Best Practice-Conduct of the APA process .....	15
4.5.1.	Pre-filing/Informal application stage.....	15
4.5.2.	Formal application for APA.....	17
4.5.3.	Content of the formal application .....	18
4.5.4.	Evaluation and negotiation of the APA .....	18
4.5.5.	Contents of CA position papers .....	22
4.5.6.	Formal agreement of APA .....	23
4.6.	APAs Best Practice: Specific areas.....	23
4.6.1.	Transactions and Participants in the APA.....	24
4.6.2.	Critical Assumptions.....	24

4.6.3.	Rollback .....	25
4.6.4.	Publication of statistics .....	26
4.7.	APAs Best Practice: Unilateral APAs.....	27
4.8.	APAs Best Practice: Facilitating APAs for SMEs.....	28
5.	Simultaneous tax examinations.....	30
6.	Voluntary or mandatory prior consultation or agreement.....	31
7.	Expert opinion or mediation.....	32
8.	Final conclusions of the Forum.....	33

## **1. INTRODUCTION AND GENERAL CONSIDERATIONS**

1. This document reports on the activities of the EU Joint Transfer Pricing Forum (JTPF or Forum) in the fields of alternative dispute avoidance and resolution. The specific conclusions reached by the Forum for Advance Pricing Agreements are in bold type in section 4 of this report.
2. Under the Chairmanship of Mr. Bruno GIBERT, partner of CMS Bureau Francis Lefebvre and the Vice-Chairmanship of Mr. Guy KERSCH, Tax Counsel - Europe, Pfizer Enterprises SARL, for Business and Mrs. Montserrat TRAPE VILADOMAT, Deputy Head of the International Taxation Unit from Spain for tax administrations, meetings of the JTPF were held in Brussels on the 16 and 17 March, 21 June, 27 September, the 12 and 13 of December 2005, 21 March, 20 June and 14 September 2006.
3. In the work programme for 2005/2006 (document JTPF/008/REV4/2004) the JTPF had identified Dispute Avoidance as a worthwhile area of work. Work on Dispute Avoidance would seek to formulate means by which double taxation could be prevented from arising. This theme was developed from previous work carried out by the JTPF in the field of Dispute Resolution.

### **1.1. Background – what is dispute avoidance and resolution?**

4. The Commission study “Company taxation in the internal market” SEC (01) 1681 of 23 October 2001 identified high compliance costs and potential double taxation for intra-group transactions as a major tax obstacle to cross-border economic activities in the internal market. International Double taxation (or multiple taxation) occurs where the same item of income is taxed by more than one tax administration. Paragraph 4 of the OECD transfer pricing guidelines for Multinational Enterprises and tax administrations (OECD guidelines) states: "Such double or multiple taxation can create an impediment to cross border transactions in goods and services and the movement of capital."
5. Double taxation may arise as result of a dispute between tax administrations over which tax administration should tax certain income. In those cases, the taxpayer frequently feels that he is in a period of uncertainty in such a dispute until it is resolved and that the outcome is a "black box".
6. A Multi National Enterprise group (MNE) makes tax returns for every tax administration where the group has a taxable presence (either a subsidiary or a permanent establishment) on the basis of singular taxation. According to the tax returns, each item of income is subject to corporation tax only once. Hence the MNE files tax returns on a tax singular basis. However, individual tax administrations might conduct an audit and form a different view on the taxation of that part of the MNE under the jurisdiction of that tax administration; they might conclude that the arm's length principle had been incorrectly applied. This action can lead to double taxation. Hence, disputes between tax administrations often arise after an audit has lead to a transfer pricing adjustment by one or more tax administrations. A dispute then follows between tax administrations over which will tax the income.

7. Traditionally, double taxation is resolved under the Mutual Agreement Procedure article of taxation conventions between countries. However there is no guarantee that double taxation will be eliminated. Within the EU, the Arbitration Convention goes one step further than the MAP article by guaranteeing the elimination of double taxation: if after two years of a Mutual Agreement Procedure the double taxation still remains then the matter is resolved by an Arbitration Panel. The Forum's previous work has concentrated on how MAPs could work better and how the AC should work in practice - better dispute resolution. The current work of the Forum has concentrated on how disputes can be prevented from arising in the first place – dispute avoidance -and has also considered supplementary or alternative ways of resolving disputes once they have arisen.

**1.2. What is the purpose of the Forum's work on dispute avoidance and supplementary dispute resolution?**

8. Double taxation is a real cost to taxpayers and dealing with either double taxation or the threat of double taxation uses considerable taxpayer resources. Tax administrations too recognise that double taxation has considerable disadvantages and dealing with issues of double taxation requires considerable tax administration resources.

9. Preventing disputes from arising removes significant levels of the economic costs which arise from double taxation or the threat of double taxation.

**2. POSSIBLE FORMS OF DISPUTE AVOIDANCE OR ALTERNATIVE DISPUTE RESOLUTION PROCEDURES CONSIDERED BY THE FORUM.**

10. The following broad areas were initially identified as worthy of prolonged consideration and discussion:

1. Advance Pricing Agreements (APAs)
2. Simultaneous tax examinations
3. Voluntary or mandatory prior consultation or agreement.
4. Expert opinion or mediation

11. In the initial examination of the potential solutions for dispute avoidance and better dispute resolution the Forum felt that each of the above topics might have the potential to improve the status quo. Ultimately, simultaneous tax examinations, voluntary or mandatory prior consultation and expert opinion or mediation were not considered promising avenues at this stage for improving existing methods for the better elimination of double taxation. However, the Forum considered that developing better practice on APAs in the EU would be most worthwhile.

### **3. APAS – GENERAL CONSIDERATIONS**

#### **3.1. APA Definitions and analysis carried out by the Forum into the current position and practices regarding APAs.**

12. APAs are a concept recognised and elaborated on in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax administrations ("OECD guidelines"). APAs are discussed in Chapter 4 F and AN 19+ of the OECD guidelines.
13. In the OECD guidelines, an APA is defined in 4.124. "An APA is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time."
14. The Pacific Association of Tax Administrators (PATA) has also issued internal operational guidance covering mutual agreement procedures (MAPs) and bilateral advance pricing arrangements (BAPAs) amongst its member countries.
15. An APA is initiated by a taxpayer and requires discussions between one or more associated enterprises, and one or more tax administrations.
16. Businesses argue that the different sets of rules governing the various APA procedures in Member States are time consuming and burdensome for businesses. Because bilateral and multilateral APAs require two or more tax administrations to agree on a transfer pricing methodology, it is much easier if the various jurisdictions use a similar approach. The absence of a common approach can sometimes make it difficult for the tax administrations to reach agreement. Differences in approach can sometimes lead to contentious negotiations that ultimately may fail to produce an APA agreement and can be costly for all involved and fail to avoid double taxation. Common approaches providing clarity for both enterprises and tax administrations will help.
17. APAs can be unilateral (an agreement between an enterprise and one tax administration), bilateral (an agreement involving connected enterprises and two countries where they conduct business) or multilateral (where more than two tax jurisdictions are involved). Agreements involving more than one country are usually conducted under the Mutual Agreement Procedure (MAP) article of the tax treaty between the countries involved. In some countries, domestic provisions do not permit the tax administrations to enter into binding agreements directly with the taxpayers, so that APAs about the taxpayer can be concluded with the competent authority of a treaty partner only under the mutual agreement procedure.
18. Some countries allow unilateral agreements without the involvement of other interested tax administrations. Member States have committed themselves to exchanging information about unilateral APAs – see paragraph 106.
19. A unilateral APA does not systematically avoid the problem of double taxation. The OECD Transfer Pricing guidelines strongly recommend that "wherever possible, an APA should be concluded on a bilateral or multilateral basis." (Paragraph 4.163.)

However, a unilateral APA might still be preferable to a taxpayer than no APA of any kind.

20. Because of the concerns of most Member States over double taxation, most countries prefer bilateral or multilateral APAs. However, in many countries unilateral APAs are more numerous than bilateral/multilateral APAs, not least because unilateral APAs can be concluded faster and with lower costs. But the bilateral (or multilateral) approach is more likely to reduce the risk of double taxation, to be equitable to all tax administrations and enterprises involved, and to provide greater certainty.
21. APAs, including unilateral ones, differ in some ways from private rulings that some tax administrations issue to taxpayers. An APA generally deals with factual issues and methodology, whereas more traditional private rulings tend to be limited to addressing questions of a legal nature based on facts presented by a taxpayer. The facts underlying a private ruling request may not be questioned by the tax administration, whereas in an APA the facts are likely to be thoroughly analysed and investigated. In addition, an APA usually covers several transactions, several types of transactions on a continuing basis, or all of a taxpayer's international transactions for a given period of time. In contrast, a private ruling request usually is binding only for a particular transaction
22. An APA may cover all of the transfer pricing issues of a taxpayer (as is preferred by some countries) or may be limited to specified transactions.
23. An APA can provide an opportunity to apply the agreed transfer pricing methodology to resolve similar transfer pricing issues in open prior years. However, this application would require the agreement of the tax administration, the taxpayer, and, where appropriate, the treaty partner.

### **3.2. APAs – Advantages**

24. APAs provide various advantages for both taxpayers and tax administrations. Taxpayers benefit foremost from the certainty concerning the agreed transfer pricing methodology. Because of the certainty provided by an APA, an enterprise may be in a better position to predict its tax liabilities, thus helping to provide a tax environment that is favourable for investment. When the term of an APA expires, the opportunity may also exist for the relevant tax administrations and enterprises to renew the APA, thus prolonging the advantages.
25. In addition, the taxpayer participates in an APA by presenting and discussing its case with tax administrations to a greater degree than in the conventional mutual agreement procedure (MAP). Due to this participation, there is an opportunity for taxpayers and tax administrations to consult and cooperate in a non adversarial spirit and environment.
26. The opportunity to discuss complex tax issues in a less confrontational atmosphere than in a transfer pricing examination can stimulate a free flow of information and agreement between all parties. This cooperative environment may also result in a more flexible review of the facts than in a more adversarial context.

27. Since in an APA discussion future events have yet to take place due to the prospective nature of the APA, there is more flexibility than in a transfer pricing examination or MAP. This increased flexibility can only help secure an outcome beneficial to all parties.
28. An APA may prevent costly and time-consuming examinations and litigation of major transfer pricing issues for taxpayers and tax administrations and thus reduce the exposure to interest payments and penalties. Once an APA has been agreed, fewer resources may be needed for subsequent examination of the taxpayer's return. It is still necessary however, to monitor the application of the agreement and this right is maintained by the tax administration. The APA process itself may also present time savings for both enterprises and tax administrations over the time that would be spent in a conventional tax examination and subsequent MAP.
29. A bilateral or multilateral APA, which agrees the tax treatment between a taxpayer and more than one tax administration, also averts the risk of double taxation. This too will encourage agreement.
30. Increased flexibility in an APA procedure might also help to provide solutions to more traditional transfer pricing problems. For instance, a lack of data on comparable companies does not necessarily need to be an insurmountable problem in bilateral negotiations between tax administrations. If the taxpayers and the tax administrations can agree on an outcome which would be expected at arm's length – perhaps through a profit split based on the added value of the performed functions, it might not prove necessary to complete a database search.
31. In addition, a tax administration can enjoy the benefit of enhanced taxpayer compliance which will result from an APA.
32. APAs therefore have many advantages. However, APAs cannot be a cure for all transfer pricing problems and cross-border disputes. Even if an APA procedure is organised as efficiently as possible, APAs might still prove time consuming and resource intensive due to the complexity of the issues under review, even if over-all there is a resource saving compared to an audit and MAP. But these limitations or disadvantages of an APA become less serious when an APA procedure is organised and conducted more efficiently.

### **3.3. APAs – Possible disadvantages for tax administrations**

33. An APA may initially place a strain on transfer pricing resources, as tax administrations will generally have to divert resources earmarked for other purposes (e.g. examination, advising, litigation, etc.). Demands may be made on the resources of a tax administration by taxpayers seeking the earliest possible conclusion to an APA request, keeping in mind their business objectives and time scales. These demands may not coincide with the resource planning of the tax administrations, thereby making it difficult to process efficiently both the APAs and other equally important work.
34. The balance of compliance between APA work and other tax work may be particularly difficult to achieve since APAs tend to require highly experienced and often specialised staff. Requests for APAs may be concentrated in particular areas or



sectors, e.g. global trading, and this can overstretch the specialist resources already allocated to those areas by the authorities. Tax administrations require time to train experts in specialist fields in order to meet unforeseeable demands from taxpayers for APAs in those areas.

### **3.4. APAs –Possible disadvantages for taxpayers**

35. Some businesses expressed concern that an APA may allow the tax administration to make a closer study of the transactions at issue than would occur in the context of a transfer pricing examination, depending on the facts and circumstances. The taxpayer must provide detailed information relating to its transfer pricing and satisfy any other requirements imposed for the verification of compliance with the terms and conditions of the APA. At the same time, the taxpayer is not sheltered from normal and routine examinations by the tax administration on other issues. An APA also does not shelter a taxpayer from examination of its transfer pricing activities. The taxpayer will still have to be ready to establish that it has complied in good faith with the terms and conditions of the APA, that the material representations in the APA remain valid, that the supporting data used in applying the methodology were correct, that the critical assumptions underlying the APA are still valid and are applied consistently, and that the methodology is applied consistently.
36. APAs are not used by all taxpayers because the procedure can be expensive and time-consuming and small taxpayers generally may not be able to afford it. This is especially true if independent experts are involved. In addition, the resource implications of APAs may limit the number of requests a tax administration can entertain. In some countries APAs therefore may mainly only assist in resolving large transfer pricing cases.
37. In evaluating APAs, tax administrations can alleviate these potential disadvantages by ensuring that the level of enquiry is adjusted to the size and complexity of the international transactions involved.

## **4. BILATERAL/MULTILATERAL APAS – THE SUGGESTIONS OF THE FORUM<sup>1</sup>**

38. The advantages of APAs can be maximised and the disadvantages minimised by encouraging more efficient APA procedures. This could be done by establishing best practices within the EU for taxpayers and tax administrations to follow where they could do so. The over-all aim of the Forum's work on APAs is to encourage the use of APAs where they are appropriate tools for dispute avoidance.
39. It is recognised that not all Member States are always able to carry out this best practice because of domestic law constraints. This is not to say that any practice that is not described here is bad practice. Best practice remains a goal and an aspiration that should be carried out where relevant and where a Member State is able to do this.

---

<sup>1</sup> **Observations by Germany:** *Germany* believes that this report does not fully reflect the drafting amendments that Germany thought the Forum agreed upon at its meetings. Although Germany does not enter reservations concerning the wording of the respective paragraphs, this cannot be construed as full consent.

40. It is also recognised that taxpayers too should adopt best practices where they can do so. Taxpayers are jointly responsible along with tax administrations for ensuring that an APA application is dealt with efficiently.
41. These suggestions for best practices augment the practices recommended by the OECD Guidelines, particularly within the context of the internal market. The Forum's reasoning and suggestions for best practice are explained hereafter. The suggested best practice is presented in bold text. The best practice in sections 4.1 to 4.6.4 applies to bi and multilateral APAs, unless expressly stated to also apply to unilateral APAs.

#### **4.1. APAs Best practice – legal framework**

42. Article 25 (3) of the OECD Model Tax Convention allows Competent Authorities (CAs) to consult together for the elimination of double taxation. The CAs shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation of the relevant tax Convention.

#### **Article 25 (3) of the OECD Model Tax Convention permits countries to enter into APAs.**

43. An APA is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time. If an APA goes beyond this, the result might be mere prediction and be contrary to the OECD Guidelines. Paragraph 4.125 of the OCED guidelines states "In general, great care must be taken if the APA goes beyond the methodology, the way it will be applied, and the critical assumptions, because more specific conclusions rely on predictions about future events."

**An APA is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time.**

**The APA should not agree precisely the actual profit which should be taxed in the future.**

**The APA should fix according to the arm's length principle arrangements for the determining the transfer pricing for the future transactions in the APA.**

44. Agreed APAs need to provide certainty for both taxpayers and tax administrations. How this certainty can be provided by tax administrations will vary depending on domestic laws. But both tax administrations and taxpayers need to be confident that, provided the terms of the APA are adhered to, the tax treatment of the transactions covered in the APA will be as agreed in the APA.

**APAs must provide certainty for taxpayers and tax administrations. The precise way this can be done can vary depending on the law of the Member State in which the taxpayer is resident.**

45. Under an APA, a tax administration does not give up the right to audit. Transactions not included in the APA will be subject to the usual scrutiny. For transactions included in the APA, the tax administration still has the right to conduct an audit to check that the terms of the APA are being adhered to and that the critical assumptions underlying the APA are correct. But the taxpayer has the certainty that provided the APA terms remain adhered to and the actual facts are in accordance with the critical assumptions presented in the APA, then the transactions will be taxed according to the APA. Hence under normal circumstances an audit of transactions in an APA is concerned with checking and monitoring the terms and the critical assumptions of the APA. However, being part of an APA procedure does not absolve the taxpayer from the usual rules of the tax administration since the taxpayer is still subject to the laws of the country of residence.

**At all times, the taxpayer is subject to the usual rules of the tax administration. Where there is an APA, a tax administration still has the right to conduct an audit. However, under normal circumstances, the audit is carried out only to check and monitor the APA by reviewing the terms and critical assumptions underlying the APA.**

46. Both taxpayers and tax administrations are involved in the APA. To provide the 1 certainty, formal agreements will need to be drawn up between the tax administrations involved in the APA. And the taxpayers involved will need to accept these agreements if the APA is to proceed since they will dictate how the taxpayers in each country will be taxed in the future.

**Bilateral and multilateral APAs will require agreements between tax administrations and understandings between each tax administration and the taxpayer concerned. Unilateral APAs will only require understandings between a tax administration and the taxpayer concerned.**

#### **4.2. APAs Best practice – organisation of APA procedures in Member States**

47. Valid domestic considerations dictate that tax administrations are organised in many different ways. There is no requirement for a tax administration to be organised in one particular way to deal with APAs but it is sensible if tax administrations are able to use their skills appropriately.

**Tax administrations should be able to draw upon all of their skill and adequate resources to conduct an APA.**

48. However, there are clear benefits if an APA programme can be co-ordinated centrally. This is likely to allow a greater efficiency and a greater consistency of treatment for tax payers.

**APA programmes should be centrally co-ordinated.**

49. The key for organizing an APA programme is to have a flexible approach to enable APA applications to be dealt with quickly and efficiently. Specialists will be best placed to deal with APAs. The specialists will need to carry out two broad roles: firstly, checking and evaluating the APA application and, secondly, negotiating the APA with other countries.

**Tax administrations should carry out two broad roles to deal with an APA application: firstly, evaluating the application and secondly negotiating an agreement with the other tax administration.**

50. The negotiations between tax administrations are conducted under the treaty and are CA negotiations and the responsibility of the CA. It is the responsibility of the CA to ensure that the roles of checking and evaluating the APA application and negotiating with other countries are carried out. Where in the organisation both roles are split between CA and other parts of the tax administration, it will be better for both to work together to establish a position before CA negotiations commence, while keeping in mind their respective roles.

**The negotiations between tax administrations should be conducted by the CA. It is the CA's responsibility to ensure that the roles of checking and evaluating the APA and negotiating with other countries are carried out. This applies even if the CA calls upon other parts of the tax administration to provide specialist knowledge.**

### **4.3. APAs Best Practice: Entry to the APA programme**

#### *4.3.1. Entry to the APA programme, general considerations.*

51. The Forum also considered some of the possible obstacles that dissuade taxpayers from entering the APA process and how these obstacles could be ameliorated to encourage the use of APAs where they are appropriate.
52. It is up to the taxpayer to initially decide which transactions it would like included in an APA. After the taxpayer files its APA application, the tax administration can review the application and decide to modify or reject it altogether. In practice, taxpayer and tax administration should work together to establish mutually acceptable terms and conditions for an APA. Taxpayers are free to accept the modification or withdraw the application. Taxpayers should not be penalised if they withdraw an application.

**It is up to the taxpayer to initially decide which transactions should be included in an APA application.**

**The tax administration can review the application and modify or reject it.**

**The tax administration should accept the application where all requirements have been met.**

**In practice, taxpayer and tax administration should work together to establish mutually acceptable terms and conditions for an APA.**

**A withdrawal of an APA application should not automatically trigger an audit**

53. Different laws in different tax administrations affect how an APA programme is conducted and this is completely legitimate. Some countries automatically accept an APA application where a taxpayer requests one. This starting point means that where a taxpayer legitimately requests an APA, the application for an APA will be considered by the tax administration. However, other countries apply rules to restrict

APAs to cases considered to be appropriate by those countries. Typically, two procedural rules can be used to manage the number of APAs in a programme to prevent applications for APAs considered inappropriate: rules on fees and complexity thresholds.

**Domestic considerations will legitimately affect how a tax administration runs its APA programme.**

**Rules on fees and complexity thresholds can be used by tax administrations to ensure APAs are only made available where they are considered appropriate by those tax administrations.**

#### 4.3.2. *Fees*

54. Some countries use fees as a legitimate gauge of the taxpayer's desire for an APA and to expedite the country's ability to address the application. Whether a fee is charged for an APA is up to a Member state. It is not necessary for a tax administration to charge a fee in order for the tax administration to provide a good service to the taxpayer. Fees are typically of two general types: a lump sum figure as an entry fee to the APA programme and/or a fee linked in some way to the extra costs incurred by a tax administration in providing the APA for the taxpayer.

**It is for Member States to decide if a fee system is appropriate.**

**A fee should not be a precondition for an efficient service which should be provided as a matter of course.**

**If they are used, fees should be charged by reference to a lump sum amount as a pure entry fee and/or linked to the extra costs incurred by the tax administration as a result of the APA.**

**Fees are particularly appropriate where without a fee a tax administration would be unable to have an APA programme. But they should not be set so high so as to be a disincentive to apply for an APA.**

#### 4.3.3. *Complexity thresholds*

55. If there is little uncertainty over transfer pricing, then an APA is unlikely to be appropriate. This is because one of the main benefits of an APA is the provision of certainty by an agreement between taxpayer and tax administration. If there is relative certainty already, then there is little benefit to gain in the request for agreement. A complexity threshold could therefore operate in such a way as to only allow taxpayers into an APA negotiation where there is significant doubt as to the transfer pricing.

56. If applied, complexity thresholds could be written in many ways because of the wide number of situations they might have to cover. To avoid being too prescriptive, complexity thresholds have to be dependent on the facts and circumstances of the case but taxpayers are entitled to be treated consistently. One element of complexity will be how other tax administrations potentially involved view the transactions potentially in the APA. The complexity threshold could be lowered where other tax administrations are willing to accept an APA application. It is to the advantage of all

parties to know as soon as possible if the APA application can proceed, so discussing complexity thresholds as soon as possible will save spending resources where an application will not be accepted into an APA programme.

**If complexity thresholds are to be used, they should be used as a guide to whether an APA is appropriate.**

**Complexity thresholds should be operated consistently for all taxpayers.**

**If complexity thresholds are to be used they should be dependent on the facts and circumstances of the case so not to be too prescriptive.**

**The likely attitude of other tax administrations directly involved in any APA should also be a factor in the operation of any complexity threshold: a threshold could be lowered where other tax administrations are willing to accept an APA application.**

**Whether a complexity threshold will operate to deny a taxpayer entry into an APA programme should be discussed at any pre-filing meeting.**

57. The number or size of transactions is not an infallible guide to uncertainty or transfer pricing risk. However, if there are very significant amounts of transactions, this in itself can give rise to uncertainty. Conversely, small transactions may give rise to considerable uncertainty but, because of the small amounts of tax at stake, the transactions might not be appropriate for an APA. Complexity thresholds should be flexible to take these factors into account.

**The number or size of transactions should not constitute an infallible guide to uncertainty or transfer pricing risk. Complexity thresholds should take into account the relative size and transfer pricing risk (to the taxpayer) of the transactions.**

#### **4.4. APAs Best practice - Documentation**

58. The documentation necessary for any APA will vary depending on the particular case. Certain documentation will be necessary for the pre-filing and formal application; this will allow the tax administration to consider the application quickly and efficiently. Supplementary information may have to be produced during the evaluation. The taxpayer will have to maintain certain documentation during the term of the APA as agreed between the tax administration and the taxpayer; this will allow the tax administration to monitor the way the APA is applied. The EUTPD is likely to be a useful basis for the application.

**The taxpayer must maintain documentation throughout the APA so that the tax administration can monitor the way the APA is applied. Where a MNE uses the EU Transfer Pricing Documentation (EUTPD), this will serve as a useful basis for any APA application.**

**Useful additions can be any transfer pricing policy documentation on which the application is based and any reports received on which the application relies. Documentation requirements should not be unduly onerous for taxpayers but the tax administration must be given the opportunity to fully evaluate the transactions included in the APA.**

59. Appendices A & B of this report provide a list of documentation that tax administrations will often find useful in any APA application. Further information might be necessary depending on the circumstances of a particular APA application.

**Appendices A&B provide a list of documentation that is likely to be of use for any APA application. What is actually required in the formal application should be agreed at the pre-filing stage. The specific information necessary to monitor the application of the APA should always be agreed upon as part of the APA negotiation.**

60. During the APA application the tax administration and the taxpayer should work together to determine what documentation is necessary to maintain the co-operative spirit of the APA since this will be advantageous for all parties.

#### **4.5. APAs Best Practice-Conduct of the APA process**

61. The aim of an efficient APA process is to encourage more taxpayers to request APAs where they are appropriate. To achieve this aim, APA negotiations need to be conducted as efficiently and as quickly as possible.

**Tax administrations and taxpayers should work together in as cooperative a manner as possible to ensure that the APA is conducted as efficiently as possible.**

62. APA programmes can be organised in many different ways but there are common stages present in most APAs that form a useful basis for any application. And these common stages should feature in nearly all APA applications. In a particular case the distinctions between the evaluation and the negotiation parts of the process may become blurred to reflect the facts and circumstances of that case; best practice as described below relates to what might happen during the course of the APA application. The best practice suggested for one stage may also apply at a different stage of the application.

**An APA application should typically have four distinct stages:**

- (a) Pre-filing stage/Informal application
- (b) Formal application
- (c) Evaluation and negotiation of the APA
- (d) Formal agreement

##### *4.5.1. Pre-filing/Informal application stage.*

63. The idea of the pre-filing meeting is to allow an informal approach to establish whether an APA is appropriate, what information might be needed for the formal application and to assess the potential benefits and costs. It is not helpful if an onerous amount of information is required at this early stage. It is recognised that every case will be different and will require information of a different type and quantity. The information provided at the pre-filing stage should of course be sufficient to allow the tax administration to give an indication of whether the APA application is likely to be accepted when the formal application is received. The information will have to provide sufficient detail to permit this analysis and should at

least describe the activity and transactions to be covered, the taxpayers affected, the preferred methodology, desired length of the APA, any rollback and the countries to be involved. A pre-filing meeting could also be conducted on a bi or multi-lateral basis.

**The pre-filing meeting should allow all parties to assess the likely success of the APA. The tax administration should be provided with sufficient information to permit this assessment. This information should at least describe the activity and transactions to be covered, the taxpayers concerned, the preferred methodology, desired length of the APA, any rollback and the countries to be involved.**

64. The Pre-filing/Informal application stage is an opportunity for the taxpayer and tax administration to discuss the details of the future formal APA application. Enough detail will need to be available for the tax administration to give an indication of whether the APA application might be acceptable. This stage should give an early opportunity for the taxpayer and the tax administration to think about an APA methodology and terms and conditions that might be mutually acceptable.

**The pre-filing stage must allow the tax administration to make a reasoned judgement on whether the application will be acceptable.**

65. If taxpayers approach the tax administrations as early as possible when applying for an APA, then the advance nature of the APA remains as distant as possible in the future. This will give a greater chance that negotiations can be completed either before the years the APA will cover are reached or as soon into that period as possible. This will maintain flexibility since it will allow taxpayers to behave according to any agreement reached with the tax administration. If no agreement is reached before tax returns have to be made then the taxpayer will be uncertain as to the basis on which the tax returns should be filed. However, taxpayers must have a clear idea of their intentions in the future, so the proposed term the APA is to cover cannot be so far into the future as to preclude this certainty of intention.

**Taxpayers should approach the tax administrations as early as possible once they are clear about their intended actions when considering an APA.**

66. Sometimes, an anonymous approach might be useful although nothing binding could be agreed on an anonymous basis. The anonymous approach might usefully allow the exploration of the benefits, costs, requirements and methodology for the APA. **N.B. Nothing in this paragraph compels tax administrations to accept anonymous approaches from taxpayers** but it is a fact that Business representatives and some tax administrations find anonymous approaches useful.

**Tax administrations might consider anonymous approaches from taxpayers but nothing binding can be agreed on an anonymous basis. At any rate, the taxpayer's intentions should be relatively fixed for the anonymous meeting and as such an anonymous approach should not be a protracted process.**

67. If the tax administration can give a clear indication as early as possible whether a taxpayer's application will be accepted, this will save the taxpayer the often considerable expense of a formal application if no APA is to be permitted. Expense will also be saved if a tax administration can indicate in the pre-filing meeting what it



would and would not accept within an application so that a taxpayer will not have to spend resources developing a transfer pricing methodology that will not prove acceptable to a tax administration.

**The tax administration should give a clear indication as soon as possible whether a taxpayer's subsequent formal application is likely to be accepted and also indicate, where possible, which aspects might be more controversial.**

68. To enable all parties to make an informed judgement over the potential for an APA, all tax administrations involved in the envisaged APA should be approached by the taxpayers. There may be situations where a taxpayer prefers to approach one tax administration first to gauge its view; if this is the case then other tax administrations would need to be approached as soon as possible afterwards if the application is to go ahead.

**The taxpayer should approach all of the Member States directly involved in the envisaged APA. Where more than one tax administration is consulted, the same information should be provided to each (this should apply throughout the APA process)**

69. It might be necessary for CAs to consult between themselves as part of the pre-filing stage if a tax administration considers that it will only accept a request for an APA if the relevant treaty partner will do likewise. An early consultation will expedite a common treatment of the request for an APA.

**As part of the pre-filing stage, CAs should consult with one another where necessary. Where such a consultation is deemed necessary, it should take place as quickly as possible**

70. The pre-filing stage is a good opportunity to discuss what information will be required with the formal application. It will often also be an opportunity for the tax administration to influence the nature of the APA by stating where possible broad details of what will be acceptable. Where a tax administration operates a complexity threshold, this should be discussed at the pre-filing stage.

**In the pre-filing stage, the taxpayer and tax administration should discuss what documentation should be included with the formal application. Any complexity threshold should also be discussed. The tax administration should also use the pre-filing stage to influence the content of the application where this will aid an efficient outcome of the application.**

#### *4.5.2. Formal application for APA*

71. The APA can be conducted more efficiently if the formal application is as complete as possible and is made as early as possible. All parties should be involved. Both taxpayers and tax administrations need to fulfil their obligations if the application is to succeed.

**Formal application for an APA should be made as early as possible in relation to the years to be covered by the APA and in particular soon after any informal approach. The taxpayer should make the formal application to the tax administration of its country of residence and at the same time to all countries. Where Member States have different administrative or legal procedures concerning APAs, it is the taxpayer's responsibility to**

**ensure that all applications are made in time. The tax administration should endeavour to tell the taxpayer as soon as possible whether the application for an APA has been formally accepted for processing and to request as soon as possible any further documentation necessary to evaluate the APA and to formulate a position.**

#### *4.5.3. Content of the formal application*

72. Every APA case will be different and there is no ideal form for any application. The application should be evaluated by the tax administration in a measured and timely fashion. So that this can happen, the application must contain certain information. What is necessary will vary between cases. The aim is to provide as much necessary information as possible as soon as possible without unnecessarily onerous resource implications for the taxpayer.

**In the initial formal application, the taxpayer should try to enclose all relevant information necessary for the tax administration to evaluate the application and to come to a view about the methodology that will be used later to calculate the arm's length price. Appendices A and B contain details of the type of information that might often be necessary in all instances but is not necessarily a minimum and is not the maximum. The precise information necessary for the formal application should be tailored to the specific case.**

73. It is of course unlikely that all the information necessary for the APA can be included in the formal application since the taxpayer is unlikely to be able to predict precisely what the tax administration will require. Further facts might need clarifying during the evaluation. This may mean that more information becomes necessary.

**A tax administration has the right to ask for supplementary information to check and evaluate the APA application.**

#### *4.5.4. Evaluation and negotiation of the APA*

74. The aims of evaluation and negotiation phases are distinct (even if on occasion the phases are being conducted in part at the same time.) The evaluation is to allow each tax administration to formulate its view of the correct arm's length transfer pricing and its most desirable set of terms and conditions for the APA. The negotiation is to allow all the tax administrations to resolve any differences resulting from different evaluations and to formulate one APA methodology for all the taxpayers involved.

**In the evaluation, the tax administration should formulate its preferred terms and conditions for the APA. The negotiation with the other tax administrations concerned should resolve any differences which arise between tax administrations so that one set of terms and conditions can be provided to all the taxpayers involved.**

75. The taxpayer needs to be closely involved in the evaluation of the APA by the tax administration because it is the taxpayer who is in possession of the facts of the case. Once the tax administration is satisfied with the explanation of the facts and circumstances of the case then the negotiation with the other tax administrations involved can begin. The aim is to begin the negotiation as soon as possible after the application has been received (even if in practice the evaluation can take a significant period of time).

**The taxpayer should help the tax administration to evaluate the application through the provision of information. The evaluation should be completed as soon as possible to allow negotiation to be started.**

76. Depending on the circumstances of a particular case, negotiations could begin between tax administrations while the application is still being evaluated if the tax administrations agree and this would aid the application.

**If it would aid the APA procedure, preliminary negotiations should begin before the evaluation is finalised but this should not permit tax administrations to inappropriately postpone finalizing the evaluation.**

77. It will help the timely completion of an APA if contact between CAs takes place as early as possible to establish a timetable. The taxpayer should be involved in this discussion because the taxpayer will be required to produce any further information to allow the tax administrations to evaluate and negotiate the APA. Appendix C of this report contains a model timeline for a typical APA but the timeline in actual cases will derive from the facts and circumstances of the particular case.

**As soon as possible after a formal application is received, the CAs of the tax administrations concerned should contact one another and establish a timetable for the APA.**

**The taxpayer should be involved in the creation of the timetable.**

**In multilateral APAs, the CAs could agree that one CA takes the lead in organising the procedure.**

**A model timetable is contained in Appendix C.**

78. Before entering into negotiations with another country a tax administration must have its own position in mind, even if this is not fully formulated. To reach this position the tax administration will have to evaluate all relevant information and the taxpayer must cooperate in the provision of this information. However, since the final APA will always involve inter-action with another country it will often be appropriate for all the CAs to consult with one another as early as possible in the process and not merely at the end. This will allow them to exchange preliminary views and perhaps issue joint information requests or more tailored requests. This consultation between CAs could range from a face to face meeting to an exchange of emails or a telephone conversation. This inter-action between CAs can be an ongoing process or could only happen at the start of the application and then after both country positions have been established. In some cases, it may not be necessary for CAs to consult periodically before country positions are established. But in most cases it will probably be more effective for CAs to reach provisional agreements together as early as possible even if the agreements have to be revised in the light of subsequent facts.

**The evaluation stage should involve CA inter-action where this will aid reaching an APA. Provisional agreement should be reached where possible. However, it is preferable that a tax administration has in mind at least a preliminary evaluation before actual CA negotiations begin.**

79. However, where a tax administration deems it unnecessary to consult in depth with another tax administration before establishing its own position, they should endeavour to finalise their evaluations as early as possible in the APA process so that full CA negotiations can be opened as soon as possible.
80. Because an APA will require reaching a mutual understanding, it is unlikely to be wise for a tax administration to formulate its position without any consultation between CAs at all. At the very least, CAs should consult very soon after an application is received to establish a timetable for the APA. Likewise it will often be better for CAs to consult throughout the time their respective country positions are being established. However, the over-all approach should be balanced: it may also be unwise in some cases for the CA negotiation to run in parallel to the evaluation and information seeking stage of the APA since this might actively work against each country finalising its position as efficiently as possible.

**The aims of the evaluation and negotiation are distinct even if it might sometimes be appropriate to carry out these tasks partly together. A balanced approach should be adopted to ensure that the evaluation takes place as quickly as possible and the negotiation begins as soon as possible.**

81. The evaluation of an APA application will often be a lengthy process since it involves the gathering and evaluation of considerable amounts of information, possibly from a number of sources. It is important to act efficiently to minimise this period. Taxpayer and tax administration working together will help to do this, as might tax administrations making joint requests for information.

**Tax administrations and taxpayers should work together in an APA to minimise any delay, in particular by making timely requests for necessary information and supplying information in a timely manner. Tax administrations should always consider making joint/common requests for information when this will further minimise delays.**

82. It might well be that, after examining the information provided, the tax administration agrees completely with the application submitted by the taxpayer. In this case, the tax administration's position will be the same as the position of the taxpayer submitted in the original application and the tax administration should be ready to begin negotiations. In any case, a tax administration should push for negotiation to begin as soon as its evaluation is complete.

**As soon as its evaluation is complete, a tax administration should endeavour to begin negotiations and, if necessary, the other tax administration involved should endeavour to complete its own evaluation so that negotiations can begin.**

83. However, where the Member State does not agree with everything in the taxpayer's application it will be necessary to discuss a different position between taxpayer and tax administration. It is to be expected that this exchange of views and information will take time.

**Where a tax administration forms an evaluation different from the taxpayer's application, then its evaluation should be discussed with the taxpayer.**

84. Since an APA is not a traditional audit, nothing can be imposed without the taxpayer's agreement. If the tax administration forms a view completely different from the view of the taxpayer, the taxpayer would have the option of withdrawing the APA request; in this case both the taxpayer and the tax administration may have wasted resources. Whether a taxpayer will finally agree to the APA will depend on the result of the negotiations between the CAs but obtaining the taxpayer's agreement at every stage of the proceedings will minimise the risk of failing to agree at the end.

**As part of the evaluation process, the tax administration should try to obtain the taxpayer's agreement with the position of the tax administration. It is advantageous for tax administration and taxpayer to work together to keep the proceedings on track to a mutually acceptable conclusion.**

85. It is always possible that a significant amount of time in the APA process can pass during the period when a tax administration is seeking information to evaluate the APA but the tax administration and taxpayer are jointly responsible for this.

**Tax administrations should make every effort to keep the evaluation to a minimum by requiring only pertinent information; taxpayers must in turn provide any information requested as quickly as possible. It should be possible to agree what information is relevant.**

86. Openness between all parties will add to the cooperative spirit of the APA and, by establishing trust between all the parties, help find a mutually acceptable conclusion.

**All information provided to one tax administration should also be provided to the other tax administrations involved. Details of what information has been requested should also be exchanged. A convention should be established for each APA to say whether the taxpayer or, exceptionally, the tax administration through exchange of information will do this.**

87. The formal exchange of tax administration evaluations is most often done by an exchange of position papers. CAs should seek to exchange position papers as soon as possible after the formal application for an APA is received. For this target to be met, the co-operation of the taxpayer in providing information and replying to questions quickly is essential. Each CA will need to produce a position paper at the start of the final CA negotiations. Final negotiations can only begin when all tax administrations involved have developed their position. The existence of position papers from each tax administration involved will help to clarify the differences between CAs.

**For most APAs, each CA should produce a position paper containing the tax administration's evaluation. The formal exchange of positions should take place with an exchange of CA position papers. This should be done as soon as possible after the application is received.**

88. The requirement for an exchange of position papers might exceptionally delay the start of full CA negotiations, however. Where this will be the case then it would not be necessary for both CAs to provide position papers. However, it is common practice that position papers are used in the majority of APAs conducted under Article 25(3) of the OECD Model Tax Convention. Some countries have experience with a successful APA negotiation without the formal exchange of position papers.

This absence of a formal exchange of position papers might have the advantage in particular cases of allowing CAs to maintain flexibility and in an open discussion to find common ground to agree. But it is only the exceptional case where full negotiations can properly start without at least one position paper being available.

**Where appropriate, CAs do not need to exchange position papers if this makes the APA process more efficient and faster. But in most cases having all CAs prepare position papers before full negotiations begin will help to identify and thus resolve any disputes quickly and efficiently. Where one CA has prepared a position paper, any other CA involved in the negotiation should at least set out what disagreement exists.**

#### 4.5.5. *Contents of CA position papers*

89. The preparation of a position paper by a CA is a vital event in any APA since it is where each tax administration outlines its evaluation. Appendix D of this report contains suggestions for the contents which are likely to prove necessary for any CA position paper. As every APA will be different the contents of the actual position papers will vary depending on the facts of the case. These will often involve the emphasis of particularly important facts, argument in favour of a particular outcome and perhaps argument rejecting other proposed criteria (e.g methodologies, comparables, critical assumptions) which the tax administration considers inappropriate.

**The contents of a position paper should set out the view of the tax administration involved in the APA. Appendix D lists some of the details that are likely to be necessary in a CA position paper.**

90. Negotiations are most often started with the exchange of CA papers; to keep negotiations on track it is likely to be useful if the CAs agree a timetable to resolve any outstanding issues. If more than one meeting is necessary – as is often necessary in more complex cases – then the taxpayers should be kept informed of any significant developments. This will enable them to make suggestions or provide information quickly to resolve any dispute between CAs.

**Negotiations should be started by the sending of CA papers. A timetable should be agreed for the negotiations. Taxpayers should be kept informed of all significant developments.**

91. It might be beneficial to have taxpayers attend CA meetings to enable factual matters to be addressed efficiently. It may also be beneficial for CAs to arrange regular meetings between themselves where all outstanding APAs are discussed but it would not be beneficial to wait until the next such regular meeting to discuss a particular APA if all parties were ready for discussions before hand.

**If the CAs agree, taxpayers should be allowed to attend CA meetings to address factual matters by making a presentation.**

**If beneficial, CAs should arrange regular meetings to keep the whole APA programme up-to-date but this should not impede arranging and conducting meetings on individual cases.**

#### 4.5.6. Formal agreement of APA

92. The final APA between tax administrations and between a tax administrations and taxpayers governs the behaviour of everyone involved in the APA. There are likely to be a number of separate agreements which together constitute the APA. The taxpayers will require certainty that, provided the relevant terms of the APA are met, then the transfer pricing for the transactions will be as determined in the APA and that the transactions will not be subject to a different interpretation by the tax administration. Equally, tax administrations may require certainty that the tax treatment of the transactions covered by the APA will be accepted by the taxpayers provided it is consistent with the APA. For the APA to become effective, tax administrations may therefore require a taxpayer to submit a binding declaration that any legal remedies (i.e. judicial and administrative appeals) will be waived in respect of tax assessments that correctly implement the APA.

**The formal APA should be given effect by formal agreements between the tax administrations involved (in a multi-lateral APA there could be one agreement between all tax administrations or a series of bilateral agreements between each tax administration.)**

**All agreements should detail the terms and conditions of the APA.**

**These agreements should give certainty to those involved in the APA. Tax administrations should ensure that they are able to provide this certainty.<sup>2</sup>**

**The agreements should provide certainty that provided the relevant terms of the APA are met, then the transfer pricing for the transactions will be as determined in the APA and that the transactions will not be subject to a different interpretation by the tax administration.**

93. Every APA agreement will depend on the facts and circumstances of the case. However, it is likely that all agreements will have to contain certain information.

**Appendix E contains information which is likely to be necessary for all APA formal agreements.**

#### 4.6. APAs Best Practice: Specific areas.

94. The Forum also discussed possible best practices in the following specific areas: transactions and participants in the APA, critical assumptions, rollback. These specific areas had been identified as most deserving of the development of best practice. In addition, the Forum was asked by some Business members to consider the question of tax administrations publishing some statistics on APAs.

---

<sup>2</sup> Germany's reservation: For an APA to become effective, *Germany* reserves the right to require a taxpayer to submit a binding declaration that any legal remedies (i.e. judicial and administrative appeals) will be waived in respect of tax assessments that correctly implement the APA

#### 4.6.1. *Transactions and Participants in the APA.*

95. In general, the more transactions and members of the MNE group that are included in the APA, the greater the certainty offered by the APA. Including all controlled transactions between all associated enterprises in an APA would guarantee that economic double taxation would not arise. Whilst it is the ideal that all inter-company transactions could be included, in practice this can rarely be done, especially if an MNE is very diversified or complex. Since there are inevitably two tax administrations concerned with every cross border inter-company transaction, the view of other tax administrations directly involved might help inform the ideal approach.

**It is up to the taxpayer to initially decide which transactions and which group entities he wants to have included in the APA. But it is the decision of the tax administration whether it accepts the taxpayer's application.**

**It is important that tax administrations are as flexible as possible in allowing the taxpayer to include what he wishes in the APA. It is recommended that the taxpayer's logic for excluding as well as including companies and transactions is explained in the application.**

**A tax administration should exchange information (EOI) spontaneously (subject to any domestic law limitations) with another tax administration which the first tax administration feels should be included in the APA. The taxpayer would need to be consulted about which tax administrations to involve in the APA since the taxpayer's agreement to the terms and conditions of the APA needs to be obtained.**

#### 4.6.2. *Critical Assumptions*

96. The critical assumptions are integral to the APA and provided they are adhered to the transfer pricing consequences of the transactions entered into will be as agreed in the APA. A critical assumption is any fact, the continued existence of which is material to the reliability of the APA transfer pricing methodology whether in respect of the taxpayer, a third party, and industry, or business or economic condition. The breach of a critical assumption is very likely to trigger the renegotiation or cancellation of the APA even though the critical assumption may or may not be within the control of the taxpayer. Critical assumptions within the control of the taxpayer could include, for example, a particular mode of conducting business operations, or a particular corporate or business structure. Critical assumptions not within the control of a taxpayer include, for example, a range of expected business volume.
97. Because APAs are concerned with transactions yet to take place, certain assumptions must be made about the operational and economic conditions that will affect those transactions when they take place. The assumptions are defined as "critical" if the actual conditions existing at the time the transactions occur could diverge from those that were assumed to exist, to the extent that the ability of the methodology reliably reflect arm's length pricing is undermined.

**The taxpayer should describe in the application the assumptions on which the ability of the methodology to accurately reflect the arm's length pricing of future transactions is based.**



98. Critical assumptions cannot be so widely drawn as to permit any behaviour since this would mean that the methodology agreed in the APA would not be commensurate with the arm's length standard. Critical assumptions which are so widely drawn to permit any behaviour would mean that the pricing methodology would not reflect the arm's length principle since many circumstances could apply: a methodology is only likely to provide the arm's length pricing of future transactions when linked to a specific series of facts and events. However, if the critical assumptions are drafted too tightly this might compromise the ability of the APA to provide certainty. Examples of areas that might need to be covered by critical assumptions are included in Appendix F.

**Critical assumptions are by their nature vital to the APA and should be drafted carefully to ensure the capability of the APA to reflect arm's length pricing.**

**Taxpayers and tax administrations should attempt to identify critical assumptions that are based where possible on observable, reliable and independent data.**

**Critical assumptions should be tailored to the individual circumstances of the taxpayer, the particular commercial environment, the methodology and the type of transactions covered.**

**Critical assumptions should not be drawn so tightly that that certainty provided by the APA is jeopardised but should encompass as wide a variation of the underlying facts as those involved in the APA feel comfortable with.**

99. If a critical assumption of an APA has substantially changed then the APA may no longer be valid. However, an automatic, complete end to the agreement would mean that all of the resources spent by all parties involved would be wasted for the remaining intended term of the APA. Keeping the APA in place for the original agreed period would maximise the return from the resources spent. A consultation between all of the parties to the APA could see if it is appropriate to keep the APA. It is possible that the terms and conditions of the APA could be altered to do this. Even if a critical assumption is not met, the methodology agreed in the APA may still be appropriate and this possibility should be explored.

**Taxpayers should inform their tax administrations if critical assumptions are not met.**

**All those involved in the APA should consult with each other to examine the reasons why a critical assumption has not been met and to see if the APA methodology is still appropriate.**

**An attempt should be made renegotiate the APA if at all possible**

**The APA agreement should include parameters for an acceptable level of divergence for some assumptions in advance and only if these parameters are exceeded should a renegotiation become necessary.**

#### *4.6.3. Rollback*

100. Rollback is a term used to describe any retrospective element of an APA where the methodology agreed in an APA for the future is also used for past periods. The main point of an APA is to provide certainty for the future. Despite this, incidental benefits

may arise from the APA application which could permit an avoidance of potential disputes or a resolution of existing disputes for earlier periods. For instance, if the facts merit it, it may be appropriate to apply the methodology in the APA to earlier periods to resolve open audit issues.

101. Different practices regarding rollback exist but rollback of an APA can be a useful tool for resolving existing transfer pricing disputes or avoiding disputes for previous periods.
102. However, rollback must be appropriate to the facts of a particular case. Similar facts and circumstances to those in the APA should have existed for previous periods in order for rollback to be appropriate. It will not be appropriate for a tax administration to apply rollback without this similarity or without the consent of the taxpayer. Rollback cannot be applied automatically but only on a case by case basis when agreement between taxpayer and tax administration is reached.

**Rollback should be a secondary result of the APA.**

**Rollback – when provided for in domestic legislation –can be considered where it will resolve disputes or remove the possibility of disputes in earlier periods.**

**Rollback should only be carried out where it is appropriate to the facts of the case. Similar facts and circumstances to those in the APA should have existed for previous periods in order for rollback to be appropriate.**

**Rollback of the APA should only be applied with the taxpayer's consent.<sup>3</sup>**

**A tax administration has recourse to the usual domestic measures if, as part of the APA process, it discovers information which would affect the taxation of earlier periods. But tax administrations should advise the taxpayer of any such intended action to give the taxpayer the opportunity of explaining any apparent inconsistency before making a tax re-assessment concerning previous periods.**

#### 4.6.4. *Publication of statistics*

103. The Forum was asked to examine the usefulness of publishing some statistical information about APAs. The amount of information published could range from minimal details of APAs concluded to greater amounts of information about the types of APAs and the general trading activities included in the APAs. For reference, the Japanese and US tax administrations currently publish APA information: the US approach is to publish a large amount of detail, the Japanese substantially less. Tax administrations are always bound by confidentiality and cannot provide details about individual taxpayers but nevertheless there may be advantages in publishing

---

<sup>3</sup> Germany's reservation: For reason of clarification, *Germany* notes that it agrees with the best practice proposal to apply rollback of the APA only with the taxpayer's consent only insofar as rollback is meant to be a specific mutual agreement procedure of retroactively applying the terms and conditions of the APA to previous periods. However, where an APA indicates that a tax assessment for a previous period is incorrect, *Germany* cannot refrain from making a tax re-assessment according to its domestic legislation, even without the taxpayer's consent

statistical information since this would help to publicise the APA process and encourage the use of APAs by taxpayers.

**The Forum agreed that in principle the publication of APA statistics would be useful.**

#### **4.7. APAs Best Practice: Unilateral APAs<sup>4 5</sup>**

- 104.** In a situation of a cross border transfer price, a unilateral APA gives certainty in advance in one country and thus reduces the risk of double taxation to some degree. For the country providing the unilateral APA, the essence of the unilateral APA is not different from the regular tax audit which reviews whether transfer pricing is arm's length. Because of this arm's length requirement, most countries have documentation rules requiring evidence that the arm's length standard has been met. A unilateral APA is only different from this regular tax audit to the degree that the review of the arm's length character of the transfer pricing is conducted in advance and not afterwards but is not different in terms of documentation requirements or acceptability of arm's length prices. In this sense, a unilateral APA may effectively replace the domestic requirements.
- 105.** Bilateral APA's give more certainty than unilateral APA's and therefore are generally preferred. However, there may be legitimate reasons for the taxpayer to request a unilateral APA. For example, a unilateral APA may be faster to conclude because bilateral APA procedures can be time consuming and costly. There are also other cases where unilateral APAs may be helpful or even the only possibility. For example, where an enterprise trades with an affiliate in a country that does not have an APA programme, or in cases where many countries are involved, a unilateral APA may be the only pragmatic solution. The same may be true for Small and Medium sized enterprises (SMEs) and in cases where only a small amount of tax is at stake or where the tax issue is not difficult and does not require the heavier process of a bilateral or multilateral APA.

---

<sup>4</sup> *Germany's* reservation on the headline: *Germany* does not consider unilateral APAs as best practice and, according to its domestic legislation, cannot conclude unilateral APAs.

<sup>5</sup> *Germany's* reservation on paragraphs 104-108: *Germany* does not agree with the statement in paragraph 104 that a unilateral APA reduces the risk of double taxation. *Germany* also observes that its domestic legislation does not allow unilateral APAs and that it is not prepared to enter into APA negotiations with another Member State when the other Member State has already concluded a unilateral APA concerning the same transactions and taxpayers. In these cases and with regard to the best practice proposal that when a unilateral APA is concluded, a MAP should not be excluded afterwards, *Germany* is only prepared to enter into a MAP following a tax examination.

With regard to the best practice proposal that taxpayers should not be forced into a bilateral APA, *Germany* observes that its domestic legislation does not allow unilateral APAs.

Furthermore, *Germany* is of the opinion that the statement in paragraph 104 that a unilateral APA is not different from a regular tax audit in terms of documentation requirements is incorrect, because it does not conform with reality. In *Germany*, like in most Member States, the information necessary for an APA is different from the regular transfer pricing documentation requirements for an audit.

*Germany* also cannot share the view that a unilateral APA can be used to effectively replace the domestic tax assessment. In *Germany's* view, it is inconceivable that any APA can be used to effectively replace the domestic tax assessment.

106. A report of the Code of Conduct (Business taxation) Group specifically mentions unilateral APAs. Member States have agreed to spontaneously exchange details of unilateral APAs.

**With the "Code of Conduct" (Business Taxation), Member States have committed themselves to spontaneously exchange details of concluded unilateral APAs. The Exchange of Information (EOI) should be made to any other tax administration directly concerned by the unilateral APA and should be done as swiftly as possible after the conclusion of the APA.**

107. The reasoning behind the decision to ask for a unilateral APA might be considered by the tax administration. It might seem to the tax administration that the APA should be bilateral. The tax administration is entitled to come to this conclusion based on the facts of a particular case. One reason for this conclusion might be that a unilateral APA will not provide sufficient certainty for the tax administration. A unilateral APA, even if it avoids the necessity of conducting an audit, might still involve the tax administration in a subsequent MAP.

108. With particular regard to unilateral APAs it is important that the rights of the other tax administrations and taxpayers are not affected by a unilateral APA because this might lead to double taxation not being avoided. In this case a MAP (either under a Treaty or the Arbitration Convention) would be necessary to resolve any double taxation where another tax administration makes an adjustment which might require a corresponding adjustment for the taxpayer enjoying the unilateral APA.

**Unilateral APA's reduce the risk of double taxation to some degree and can be used to effectively replace the domestic tax assessment.**

**Although bilateral APAs are preferred over unilateral APAs, there may be circumstances where the taxpayer has good reasons to believe that a unilateral APA is more appropriate than a bilateral. In the first instance the taxpayer has the right to decide whether a unilateral or bilateral APA is required.**

**Care must be taken that unilateral APAs are consistent with the arm's length principle in the same way as bilateral or multilateral APAs.**

**The option of including another Member State in the APA could be considered by the Member State preparing for a unilateral APA. Taxpayers however should not be forced into a bilateral APA.**

**Tax administrations are entitled to turn down requests for unilateral APAs where the tax administration feels that a bilateral or multi-lateral APA is more appropriate, or feels that no APA at all is appropriate.**

**The rights of other tax administrations and taxpayers should not be affected by the existence of a unilateral APA. When a unilateral APA is concluded, a MAP should not be excluded afterwards.**

#### **4.8. APAs Best Practice: Facilitating APAs for SMEs**

109. The Forum considered the question of whether APA procedures should be adapted for SMEs to reflect the differences between SMEs and MNEs in terms of resource

availability. It was generally agreed that SMEs were more likely to suffer than MNEs from a lack of resources and knowledge available for negotiating APAs. Some Business Members felt that under some circumstances this might amount to discrimination which could deny SMEs access to APAs.

110. Some tax administrations said that they had already adapted their APA procedures to try and reflect the problems suffered by some SMEs. One tax administration would perform searches for comparable transactions on behalf of the SME. Another tax administration had published guidance for SMEs and APAs. One tax administration exempted SMEs from transfer pricing rules altogether except under certain specific circumstances.
111. Other tax administrations felt that it was wrong to discriminate in favour of SMEs; two tax administrations felt there would be administrative costs arising from any simplification. Business Members of the Forum were also divided over the need or the desirability of different APA procedures for SMEs. Some Business Members felt that this would give an unfair advantage to SMEs over MNEs and might amount to unfair discrimination against MNEs. In any case, arm's length standards should not be disregarded in the view of facilitating APAs for SMEs.
112. The Forum concluded that the APA procedure in all tax administrations should be flexible enough to encourage both SMEs and MNEs to use the procedure but that the Forum's time would be better spent developing best practices for the APA procedures to be used by all companies. This would include facilitating access for all companies including SMEs.
113. When special rules for SMEs are considered, they should address those areas where SMEs are in effect put to extra expense because of a lack of internal resource. Possible approaches that could be considered by tax administrations are outlined below in paragraphs 115-123.
114. Applications could be accepted with a functional analysis but without any transfer pricing methodology analysis or even no preferred transfer pricing method. This will be the area where most SMEs lack expertise and hence have to purchase it and incur a high monetary cost or else develop expertise at a high resource cost. Hence the tax administration can apply its resources and expertise to choose the best methodology to produce the arm's length price.
115. If a fee is to be charged, it could be less than the usual fee. The fee should perhaps compensate the tax administration for any extra work it had to carry out but be less than it would cost the SME to pay outside advisors for the work.
116. Any complexity threshold could be reduced or, within specific circumstances, removed.
117. All questions relating to the pricing of intangible property, or relating to the pricing of non routine services and complex financial instruments could be excluded from the scope of a simplified APA procedure for SMEs. This would mean, for instance, that a simplified APA procedure for intangible property, non-routine services and complex financial instruments would not be available.

118. Given the relative lack of tax risk, the tax administration could adapt its due diligence accordingly. For instance, actual site visits might not be necessary. The level of detail in the functional analysis could reflect the relative lack of risk. This would of course be subject to future discoveries arising from audits.
119. Any reporting requirements throughout the APA could be limited to an annual statement from the taxpayer that all of the critical assumptions in the APA had been adhered to and that the APA was still relevant.
120. Again to aid simplicity and to remove the possibility of roll back leading to unresolved double taxation, rollback considerations could be excluded from APAs for SMEs.
121. It is possible that APAs for SMEs could be unilateral only.

**Tax administrations could use their experience of the problems faced by SMEs to facilitate access to APAs for SMEs where APAs are useful for dispute avoidance or resolution.**

## **5. SIMULTANEOUS TAX EXAMINATIONS**

122. In addition to APAs, the Forum decided to examine whether simultaneous tax examinations could serve as a useful tool for dispute avoidance or resolution. Some members felt that simultaneous examinations had similarities to APAs since they were aimed at establishing individual tax administrations positions but not finalizing them until discussions between tax administrations had taken place.
123. A simultaneous tax examination, as defined in Part A of the OECD Model Agreement for the Undertaking of Simultaneous Tax Examinations, means an "arrangement between two or more parties to examine simultaneously and independently, each on its own territory, the tax affairs of (a) taxpayer(s) in which they have a common or related interest with a view to exchanging any relevant information which they so obtain". Usually simultaneous tax examinations take place into past events.
124. Cooperation and mutual assistance between tax administrations in the EU with regard to transfer pricing has been intensified in recent years. This enhanced cooperation has been made possible by means of different mechanisms such as, for example, the exchange of information and, to a lesser degree, simultaneous tax examinations and the visits of tax auditors of a Member State in another Member State. In this context, the EC Directive 77/799/EC on the exchange of information in direct and indirect taxes has recently been modified in order to implement a procedure for "simultaneous tax inspections" (Article 8.3 of Directive 2004/56/EC).
125. However, simultaneous tax examinations are primarily tools for calculating the tax payable by a taxpayer. Simultaneous examinations are not a substitute for resolving double taxation – in particular they must not be used to replace MAPs; they are mainly used as an audit related tool by tax administrations, often where it is necessary for tax administrations to jointly obtain the same information for a specific purpose.

126. Furthermore, simultaneous examinations are not designed only for transfer pricing problems. They are often used in cases where other tax problems, unconnected with transfer pricing, have arisen. It would be improper to attempt to use simultaneous examinations which are an audit-related activity to avoid problems of double taxation, particularly when simultaneous examination, by adjusting the singular taxation on which a MNE has already made tax returns, can sometimes result in double taxation. This would require an inappropriate blurring of the audit and Competent Authority activity.

## **6. VOLUNTARY OR MANDATORY PRIOR CONSULTATION OR AGREEMENT.**

127. The Forum next considered the idea of voluntary or mandatory prior consultation or agreement as a means of dispute avoidance or dispute resolution.

128. The European Commission staff working paper "Company taxation in the internal market" of 23 October 2001 suggests one possible way to improve the practical application of the EU Arbitration Convention: a framework for prior agreement or consultation before tax administrations make transfer pricing adjustments.

129. The typical time line of events for a Mutual Agreement Procedure (MAP) or Arbitration Convention (AC) process runs as follows: transfer pricing adjustment, MAP/AC claim and Competent Authority discussions, MAP/AC resolution, corresponding adjustment and possible reduction of original adjustment.

130. Under existing procedures in Member States, each event needs to take place before the next event can happen. Some parts in the process require lengthy amounts of time to resolve what sometimes very complicated issues are. The Forum considered various forms of contact between tax administrations which could potentially speed up this process of dispute resolution.

131. The possibilities considered were: Early Notification (under which tax administrations would initiate MAP/AC claims proactively but with the permission of the taxpayer), Prior Notification (under which a tax administration would notify the other tax administration concerned before making the transfer pricing adjustment), Prior Consultation (under which a tax administration would consult with the other tax administration before making the transfer pricing adjustment) and Prior Agreement (under which the other tax administration would have to give a corresponding adjustment before the first tax administration made the transfer pricing adjustment.)

132. Procedures along these lines would to varying degrees address most of the business concerns; i.e. the double taxation itself, the costs of temporarily having to finance the same tax burden twice, business costs of seeking double tax relief etc.

133. However, the Forum felt that these business concerns could be most easily addressed by a suspension of tax until the dispute resolution procedure was finished; Business members also felt that parity in interest and penalty rules for transfer pricing adjustments would be necessary. The tax administrations had already agreed to the suspension of tax in the previous Code of Conduct on the Arbitration Convention, agreed by Member States in December 2004.

134. In particular, the tax administration members of the Forum felt that it was not practical to attempt to change the legal framework in which dispute resolution or avoidance was carried out. The Arbitration Convention and bilateral double tax treaties do not oblige a tax administration to even notify another tax administration in advance of making a transfer pricing adjustment with the tax administration of the affiliated company before a transfer pricing adjustment is made; Early Notification, Prior Notification, Prior Consultation and Prior Agreement are possible under existing tax conventions but they are not obligatory.
135. Under the umbrella of Prior Consultation/Prior Agreement, the Forum also considered a draft proposal from one tax administration described as a "high level functional analysis." In essence, the proposal suggested that before a full transfer pricing audit took place into a taxpayer's affairs, the CA of the tax administration, armed with only basic facts, could seek to agree a common tax treatment with another tax administration potentially involved. The facts available would be restricted to obtaining a high level functional analysis of the taxpayers. A procedure along these lines would, it was proposed, possibly remove the need for a full transfer pricing audit and subsequent MAP.
136. However, the Forum found that in general it would be unwise for tax administrations to agree a tax treatment of transactions between related parties without being in possession of all of the facts of the case.
137. As a conclusion to the Forum's deliberations on voluntary or mandatory prior consultation or agreement, it was acknowledged that for special cases where it was warranted it might be possible and desirable for CAs to consult before a transfer pricing adjustment was made. But this should be the exception and not the norm and could only be done with the agreement of both CAs involved. If CAs were to consult before an audit had been finalised the role of the CA might become confused with that of the auditor.

## **7. EXPERT OPINION OR MEDIATION**

138. Obtaining an expert opinion or mediation was considered by the Forum as a possible means for a speedier and more streamlined dispute resolution procedure. The current Commentary to Article 25 (paragraph 46) of the OECD Model Tax Convention on Income and on Capital discusses the possibility of CAs obtaining an "advisory opinion" from an impartial expert to help them reach a decision. In addition, the Commentary (paragraph 47) foresees the possibility of the parties obtaining an "opinion" on the "correct understanding" of a treaty provision from the OECD's Committee on Fiscal Affairs. Further, paragraph 4 of Article 25 of the OECD Model Tax Convention and paragraphs 4 and 41 of the Commentary on that Article foresee the possible formation of a "joint commission" to deal with some issues. Another possibility might be to have a third party evaluate the strengths and weaknesses of positions taken by the CA. These techniques are forms of "mediation" in which a third party assists the CAs in reaching a decision but generally does not have any independent decision making power.
139. This range of possibilities was considered by the Forum. However, the Forum felt that whatever the merits of the over-all idea of expert opinion or mediation within the



context of the OECD, the situation in the EU was different because of the AC. The AC, inter-alia, provides for a binding expert opinion in all cases where the CAs are unable to agree after a period of two years, unless the taxpayers agree to extending this period. But ultimately if the CAs cannot agree then the case will be subject to binding arbitration by a panel of independent experts. Hence there was little advantage in the Forum discussing the concept of expert opinion or mediation any further because in essence it had already been adopted by the tax administrations.

## **8. FINAL CONCLUSIONS OF THE FORUM**

140. Dispute Avoidance and improved Dispute Resolution are important areas of work in the field of transfer pricing. Some of the costs associated with transfer pricing in the internal market can be mitigated by efficient and transparent Dispute Avoidance and Resolution procedures. In particular, the Forum resources have been used to develop some best practices for APAs because the Forum felt that this was an area where the greatest advances could be made in the time available and to suit the format of the Forum itself, taking into account the Forum's remit to suggest practical non legislative changes and to make best use of the combined presence and expertise of both tax administration and Business Members.
141. The Forum has suggested some best practices for APAs. The Forum has not proposed any best practices so far for the other areas examined for Dispute Avoidance and Resolution – voluntary or mandatory consultation, simultaneous tax examinations and expert opinion or mediation. This lack of proposals for these areas does not necessarily mean that the ideas do not possess any merit at all but more that the Forum considered that developing best practices for APAs would be most beneficial for taxpayers and tax administrations in the internal market.

**APPENDIX A – A LIST OF THE TYPE OF INFORMATION THAT IS LIKELY TO BE NECESSARY WITH THE FORMAL APPLICATION FOR A BILATERAL OR MULTILATERAL APA. THE ACTUAL INFORMATION WILL VARY DEPENDING ON THE FACTS OF THE CASE AND WOULD NEED TO BE DISCUSSED BETWEEN THE TAXPAYERS AND TAX ADMINISTRATIONS, IDEALLY AT THE PRE-FILING MEETING**

This information can be considered as two broad types: information about the past – historical information – which might already exist in some format but will need to be compiled for the APA and information that may need to be created specifically for the APA.

When considering historical information, Member States should keep in mind that APAs concern the future and that historical information may have less relevance for future periods. That said, historical information will be necessary to place the APA in perspective and to allow better judgements about the future to be made.

The pre-filing stage is a useful time for tax administration and taxpayer to decide what information should accompany the formal application. The aim should be to strike a balance between the tax administration having enough information to consider the application properly and the taxpayer not being required to produce unnecessarily onerous amounts of information.

In all cases the tax administration has the right to require further information and the taxpayer has the right to submit further information.

- (1) Name and address of all associated enterprises (including all permanent establishments) in the APA.
- (2) A group structure showing all entities involved in the trade of the enterprises in the APA.
- (3) An analysis of industry and market trends which are expected to affect the business. Any marketing or financial studies for the business which lead to this expectation should also be provided where relevant. An outline should be provided of the business strategy expected to be used for the period of the APA and, where different, of the strategy employed for previous periods. This might include projections used in the plan for the future, management budgets, information on expected business trends and competition, future marketing, production or R&D strategy. Details of who has the power and responsibility of developing and dictating business strategy could be provided.
- (4) The years the APA is to cover, including any request for rollback, and the period for which the taxpayer desires that the APA should apply.
- (5) A functional analysis (see Appendix B) of the parties and transactions to be covered by the APA

- (6) The reason why the taxpayer feels an APA is appropriate for these particular transactions.
- (7) The critical assumptions integral to the APA
- (8) Details of the proposed methodology for the covered transactions and evidence for the view that this produces results consistent with the arm's length principle. Depending on the methodology and how it is to be applied, this evidence could include:
  - (e) A review of the five OECD comparability factors including comparables and any adjustments made to achieve comparability.
  - (f) Reasons why the method in the APA application was selected
  - (g) A demonstration by reference to financial information of how the proposed methodology is to be implemented.
- (9) A list of any APAs already entered into by any of the associated enterprises involved in the APA which relate to the same or similar transactions if not already available to the tax authorities.
- (10) Details of financial information of the entities in the APA for the three years previous to the APA. This could embody:
  - (h) the prior three years statutory accounts
  - (i) an analysis of product/service lines showing gross and net margins with associated costs for the products/services to be included in the APA, if available and useful.
- (11) A list of any legal agreements between any associated enterprises which affect the transactions in the APA. For example, licence agreements, purchase agreements, distribution agreements, R&D service agreements.
- (12) For any years where a rollback is requested – where possible in domestic law - details of the tax position of each entity involved for these years, e.g. tax return agreed, submitted but not agreed, submitted and under audit etc., together with details of any MAP process still open and an analysis of the time limits laws in place in each relevant jurisdiction to show whether years of assessment are capable of being adjusted.

## **APPENDIX B: FUNCTIONAL ANALYSIS**

The functional analysis is the key tool for any transfer pricing work. The contents should be tailored to the specific taxpayer and the transactions in the APA. Dependant on the situation, the APA application should also show to a certain extent which entity carries out what functions in the overall business of the MNE. Tax administrations however should keep in mind that they are not evaluating transactions which are not in the APA. This information will have to be sufficient for them to understand both ends of the transactions under review.

### Activities and Functions

All the activities relating to the transactions covered by the APA should be described (Research and development, manufacturing, distribution, marketing, the type of service activity carried out, etc.) The economic and entrepreneurial worth of these activities should be made clear along with details of how these activities inter-act with those carried out by other group entities. The market and the level in the market place of the entity should be described, along with the type of customer, what product is sold, how it is developed or acquired, who it is acquired from and sold to.

### Risks

The risks assumed by the entity with regard to the transactions in the APA should be described and assessed. Typical risks might include product, technological, obsolescence, market, credit, foreign exchange and legal.

### Assets employed

The amount and type of working capital, tangible and intangible assets utilised in the APA should be described. Again the relative importance of these in the trade should be analysed if possible.

There will be further details necessary if intellectual property right (IPR) is used in the transactions in the APA. Information should be provided on how the IPR was created within the group or acquired by the group. It should be made clear which entity now owns the IPR and how it came to do so, how it is utilised and what value it adds to the business.

## **APPENDIX C: TENTATIVE TIME FRAME FOR CONCLUDING AN APA**

Every APA is different; therefore, there are inherent dangers in stipulating a common timetable for every APA. Best practice is for all parties to formulate a timetable as early as possible once the APA application has been received. Tax administrations can help keep the time to negotiate an APA as short as possible by examining information quickly and efficiently; taxpayers can help to keep the time to negotiate an APA as short as possible by providing complete information quickly. The timetable below is illustrative. But the timetable below contains all the stages typically found in APAs.

### Pre-filing stage – informal application – month 0

An informal approach is made by a taxpayer to two tax administrations, requesting an APA. The tax administrations listen to the statements made and indicate whether the particular case merits an APA. The tax administrations consult with one another to ensure both will agree. Each has brief discussions with the taxpayer over what information should be provided in the first instance and explores what methodology will be appropriate.

### Months 1-3

The formal application is received by each tax administration. The CAs establish in month 1 a timetable to evaluate the APA. Both tax administrations conduct an initial review independently and issue information requests if necessary.

### Months 4-12

Tax administrations continue to evaluate independently with the full cooperation of the taxpayer(s). A first full face to face meeting could take place with a presentation to all involved parties by the taxpayer. The CAs consult as appropriate. The taxpayer is involved in this evaluation and is consulted. By the end of this period each tax administration has formulated its position. The CAs are able to exchange position papers. They agree to meet to discuss these in Month 14.

### Month 13

Each CA evaluates the other CA's position paper and obtains further information where necessary. (Alternatively, in month 12 one CA issues a position paper and in month 13 the other CA issues a position paper rebutting the position and suggesting alternatives.)

### Months 14-16

The first full face to face discussions occur between CAs. Further clarifications are obtained from the taxpayer who is kept informed of the CA negotiations.

### Month 17

The CAs reach agreement. The taxpayers are consulted and indicate their agreement.

### Month 18

The APA is formally agreed between the CAs. Formal documents are exchanged. The taxpayers receive assurances that the APA is acceptable.

More complex cases may take longer, but, with the cooperation and planning of all parties, the time taken to conclude an APA should be kept to a minimum.

## **APPENDIX D: CONTENTS OF THE CA POSITION PAPER**

Since every case will be different position papers will vary. But there is general guidance which should be applicable for the contents of all position papers. The key to concluding an APA procedure without unnecessary delay will always be to commence CA negotiations most often through a position paper as soon as possible after the application is received.

It will often be appropriate for a position paper to contain:

- (1) The conclusion of the CA together with a rationale. This should include details of the preferred methodology and the reasoning for this.
- (2) Reasons for any rejection or modification of the taxpayer's initially preferred method.
- (3) Details of the facts considered as most relevant in forming the above conclusion. If relevant, special consideration should be given to any facts which came to light during the APA process as opposed to in the original application.
- (4) Details of the critical assumptions that the APA will be dependent on.
- (5) A position on any retrospective element and on the future length of the APA.
- (6) Suggestions on how the APA should be monitored.
- (7) A description of the Treaty law and domestic law that will govern the APA and provide certainty for the taxpayer.

## **APPENDIX E: DETAILS LIKELY TO BE NECESSARY IN AN APA AGREEMENT**

- (1) The duration of the APA and day of entry into force.
- (2) Details of the methodology acceptable for determining transfer pricing and the critical assumptions (see appendix F) that must be followed for the APA to apply.
- (3) An agreement that the APA will be binding on the tax administrations involved
- (4) An agreement of how the APA is to be monitored
- (5) An agreement of what documentation is to be maintained throughout the APA to allow monitoring to take place, for example an annual report.
- (6) Any agreement on any retrospective treatment.
- (7) Any circumstances which will require the APA to be revised.
- (8) Any circumstances which will result in the APA being rescinded prospectively or even retrospectively (for instance if false information has been provided.)



## **APPENDIX F – Critical assumptions**

Critical assumptions will vary depending on the APA itself but it is possible that assumptions will need to be made about some of the following areas:

- (1) the relevant domestic tax law and treaty provisions;
- (2) the tariffs, duties, import restrictions and government regulations;
- (3) the economic conditions, market share, market conditions, end-selling price, and sales volume
- (4) the nature of the functions and risks of the enterprises involved in the transactions;
- (5) the exchange rates, interest rates, credit rating and capital structure;
- (6) the management or financial accounting and classification of income and expenses;
- (7) the enterprises that will operate in each jurisdiction and the form in which they will do so.