

## 4 Tips For Negotiating IRS Advance Pricing Agreements

By Ama Sarfo

*Law360, New York (March 27, 2015, 6:18 PM ET)* -- While U.S.-based multinationals can use the Internal Revenue Service's advance pricing agreement program to predetermine the tax treatment of their intercompany transactions, the time and expense involved means taxpayers need a game plan before approaching the IRS. Here, experts share tips on best practices for negotiating an advance pricing agreement.

### Know Your Strategy Before the Prefiling Conference

Taxpayers can request a prefilling conference where the corporation and IRS personnel discuss the taxpayer's transactions, proposed tax positions and economics before the taxpayer decides to submit an APA application and pay a \$50,000 filing fee. Taxpayers aren't obligated to follow through with an APA if they're unhappy with the prefilling conference or determine that an APA clashes with their needs. However, attorneys stress that corporations need to have a game plan before they schedule the conference.

One downside to entering a prefilling conference is that the process could expose a taxpayer's financials and tax positions to IRS scrutiny if the taxpayer ultimately declines to enter the APA process. Taxpayers do have the option to enter prefilling agreements anonymously, but the IRS recently limited the availability of that option.

"A lot of the strategic thought occurs in the decision to pursue an APA or resolve a transfer pricing issue in another way," Crowell & Moring LLP tax partner David Fischer told Law360. "You have to think about the likelihood of succeeding with an APA and whether you're willing to take a somewhat less aggressive position. Most APAs involve transactions with affiliates in jurisdictions with tax rates similar to the U.S. rate, so the IRS's tendency to push of the results toward the middle has less impact on the overall effective tax rate."

Kerwin Chung, managing principal of Deloitte Tax LLP's Washington national tax transfer pricing team, adds that it is crucial for corporate tax departments to brief key stakeholders on potential APA plans and obtain their support and approval before moving forward.

"The tax department needs to manage expectations within the organization," explained Chung, who is also the leader of Deloitte Tax's U.S. advance pricing agreement and mutual agreement procedure team. "Oftentimes, the tax department already has an idea in mind as to what they want to do, and they don't always coordinate with the rest of the organization. But the tax department needs to know what the

CFO or others will be happy with."

### **Leave Your Aggression at the Door**

Multinationals like APAs because of the program's collaborative, nonadversarial nature. However, the application process is long, and even the best intentioned taxpayers can occasionally become impatient. But if companies want to secure the best outcome possible, they need to keep a level head at all times, experts say.

Budget cuts and staff attrition have cast a pall over the entire IRS, although the agency's advance pricing and mutual agreement office is doing its best to complete APA applications. Additionally, tax authorities in other jurisdictions have resource issues in their transfer pricing offices, says David Canale, the Americas leader for Ernst & Young LLP's transfer pricing controversy services group. These wrinkles mean that taxpayers need to keep tabs on their cases, albeit in a diplomatic and respectful way.

"It's important to keep an active dialogue with the IRS and ask for status and timing updates, but you don't want to be a nag," Canale said. "Rather, you should ask how you can assist and facilitate the movement of the case."

"Taxpayers really need to establish a culture of trust and have as many touch points as possible. However, they need to have these dialogues without being overbearing," he added. "It's a process, but it's one that should be actively managed — not passively managed."

This balance between collaboration and assertiveness is one that must be constantly monitored, especially considering that taxpayers and the IRS ultimately have competing interests, says Baker Tilly Virchow Krause LLP principal Mark Heroux.

"Keep in mind this is not supposed to be an adversarial procedure ... however, the taxpayer's interests are adverse to the IRS and the foreign authority and the tax authorities are adverse to each other," he said. "The process requires maximum influence from the taxpayer without that influence becoming adversarial."

### **Treat All Authorities Equally**

APAs often involve the IRS and another foreign authority, and it's key that multinationals share the exact same information with both sides in order to hasten the process and stay in both authorities' good graces.

Taxpayers can enter an APA with the IRS alone, known as a unilateral APA. However, the very nature of transfer pricing dictates that most APAs involve two or more tax authorities. Although the authorities stay in touch, they don't share everything, and it's the multinational's responsibility to make sure that both sides are on the same page.

"Otherwise, when they get to the negotiation table, it looks like you're playing games," Canale said. "It's not necessarily intentional — a multinational could be scrambling to get information to one authority and forget to give to the other."

Mismatched information will certainly irritate the IRS and other authorities involved and cause delays, according to Chung.

"Tax authorities around the world are short-staffed — they have a lot of competing priorities — and to have an efficient process, you need to be in constant contact and keep both governments apprised as to what's going on," he said. "If you don't do that, cases tend to languish."

As part of this process, it's important to establish tentative milestones with the authorities involved, Fischer said.

### **Get Into the Nitty Gritty**

In the IRS' words, transfer pricing cases are won and lost on the facts. Therefore, the level of detail that taxpayers provide in their APA package has a significant bearing on their level of success in the process.

Taxpayers need to provide detailed information from the outset, even in their prefiling conferences, as they work to determine whether an APA is right for them. The better the information, the better the feedback from the IRS. And that feedback is critical for taxpayers, because if they have a strong idea of what the IRS is looking for, and can issue as much information in their application as possible, they can avoid dealing with information document requests later in the process, Canale said.

Multinationals also need to be prepared to give the IRS a broad overview of their financial picture, Chung says.

"You can't just go in and ask the IRS to give you an APA on a specific isolated transaction without the IRS asking about the big picture," Chung said. "The tax authority wants to know how that transaction fits within the big picture, the entire supply chain, and your group transactions. The impact of surrounding transactions could have an impact on the covered transactions."

Heroux also stresses that taxpayers need to have a tight grasp on their realistic economic data before entering the process.

"A lot of taxpayers have unreasonable expectations and projections in their economic data, so it's important to be reasonable," he said. "It's going to be tough to build a great relationship with the IRS otherwise."

--Editing by Katherine Rautenberg and Philip Shea.