APMA Key to Resolving BEPS Transfer Pricing Disputes

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The IRS advance pricing and mutual agreement program will become key to maintaining a healthy transfer pricing operation as double taxation disputes increase in the wake of the OECD’s base erosion and profit-shifting initiative, according to J. David Varley, acting director of transfer pricing operations (TPO), IRS Large Business and International Division.

Speaking April 23 at the annual transfer pricing symposium hosted by the University of San Diego School of Law, Varley noted that recent competent authority statistics revealed an increase in mutual agreement procedure (MAP) requests and time to resolve MAP cases, some of which could be attributable to BEPS-oriented foreign-initiated adjustments. “We’re certainly seeing more deviation from the arm’s-length principle, and there’s a good chance that that will increase,” he said. (Prior coverage: Tax Notes Int’l, Apr. 20, 2015, p. 239.)

As some foreign tax authorities become more aggressive about auditing multinationals, APMA will become a crucial program for helping U.S. companies resolve disputes, said Varley. He noted that most taxpayers strive to be compliant. APMA should hold itself out as “the honest broker” when representing U.S. taxpayers before foreign competent authorities, some of whom may not be interested in finding the “true” transfer price, he said.

Competent authority negotiations show that the idea that “transfer pricing is sometimes more art than science” is true, said Varley. OECD Working Party 6 delegates may reach consensus on what the arm’s-length principle means, but “we’ll find when we get in the nitty-gritty of negotiations that maybe the OECD guidelines aren’t always adhered to so closely by all parties,” he said. “That’s why we also need to be able to be practical and sometimes deviate in order to reach what our goal is under the treaty, which is to resolve double tax cases,” he added.

Asked by David Bowen of Grant Thornton LLP whether the India-U.S. treaty relationship is now “open for business,” Varley noted that Indian and U.S. competent authorities recently agreed on a framework to resolve a large backlog of transfer-pricing-related MAP cases. He said he thinks about 20 cases, which translates to maybe five or six taxpayers, have been agreed on. “We’re now working to finalize the paperwork on that,” he said. “Since both competent authorities are more comfortable with the actual implementation of the framework, I would hope that the pace will pick up.”

Varley also noted that the IRS recently announced that it will accept requests for prefiling conferences for Indian bilateral APAs. While some observers have expressed hope that the Indian and U.S. competent authorities could apply the agreed MAP framework to develop the bilateral APA process, Varley said it’s clear that that framework will not and cannot be used to develop the APA process. He added that he hopes India “will at least again come to a common understanding of how those cases should be worked, even if it’s not the framework that was developed for MAP cases.”

(Bowen asked Varley how he would respond to observers who have said that Varley’s recent predecessors were more litigation-oriented than prior regimes that encouraged alternative methods to resolving transfer pricing disputes. Varley said he didn’t want to dwell on the past and reiterated that one of the TPO’s goals continues to be to find good, strategic cases so it can win. The IRS’s transfer pricing practice will therefore “continue to search for, identify, and develop significant cases so we can get some victories for the U.S. government and the IRS in the transfer pricing area,” he said.

Nevertheless, the TPO will still try to resolve disputes at the lowest level possible, said Varley, adding that that goal isn’t necessarily inconsistent with finding winnable cases. “If we’re putting the proper amount of resources and care in case development, and we’re developing cases so that any particular one could be litigation-ready, all of our cases in theory should be litigation-ready,” he said. “At that point, you can have
a very frank conversation at the exam level between the representative for the taxpayer and the U.S. government.” Litigation-ready cases that can’t be resolved at the exam level will give IRS Appeals the facts it needs to make a good decision, Varley said. “And if we can’t resolve it there and we think it’s a good case, we will litigate,” he added.

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