

Global Transfer Pricing

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## 2014 U.S. Competent Authority Statistics Reveal Significant Increase in Demand and Inventory, More Expected to Come in 2015



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The Internal Revenue Service (IRS) on April 16 released competent authority (CA) statistics for the 12-month period from January 1, 2014, to December 31, 2014.<sup>1</sup> The report contains statistics on cases handled by both the IRS Advance Pricing and Mutual Agreement (APMA) Program and the Treaty Assistance and Interpretation Team (TAIT), and includes information on requests received, cases resolved, and pending cases.<sup>2</sup>

The key trend the IRS CA statistics reveal is the almost 50 percent increase in the number of APMA cases the IRS received in 2014 (286 cases received in 2014, compared to 192 received in 2013).<sup>3</sup> Given the increased foreign and IRS audit activity seen in recent years, and heightened taxpayer awareness and acceptance of the CA process as an effective and practical way to resolve double taxation, this trend is not surprising. In addition, with the issuance of Notice 2013-78,<sup>4</sup> the IRS proposed to allow certain requests for assistance arising from taxpayer-initiated transfer pricing adjustments, which will be helpful to taxpayers that want to address potential foreign transfer pricing adjustments before a foreign audit commences.<sup>5</sup> This expansion of the CA process will likely result in more cases being filed in future years. Further, as countries adopt and companies seek to comply with recent base erosion and profit shifting (BEPS) initiatives by the Organization for Economic Cooperation and Development (OECD), including country-by-country reporting as early as 2016, CA is expected to play an even more important role as both foreign and IRS audit activity is expected to continue to grow.

The IRS CA statistics also show a significant increase in end-of-year inventory of APMA CA cases (37 percent). In addition to the rising number of APMA CA cases received by the IRS, another likely factor in the increased inventory is the historical impasse between the U.S. and Indian competent authorities. During 2014, U.S. taxpayers continued to file requests for relief in U.S.-India double tax cases, but those cases were not actively negotiated or resolved by the two governments. With the historical impasse coming to an end, the 2015 CA statistics should show significant improvement in the number of cases resolved.

Highlights of the 2014 CA statistics include the following:<sup>6</sup>

- In 2014, the number of closed cases that resulted in full relief of double tax was 94 percent (or 88 percent, measured by the dollar amount of the total adjustments at issue).

- APMA and TAIT resolved a welcome 185 cases in 2014; however, they received a combined total of 354 CA requests. If the number of CA cases the IRS receives continues to rise in the future, the IRS will need to significantly increase staffing levels to keep pace with demand.
- The percentage of transfer pricing cases received by the IRS relating to U.S.-initiated adjustments increased in 2014 (30 percent in 2014 compared with 18 percent in 2013). In comparison, the number of non-transfer pricing cases received by the IRS that related to U.S.-initiated cases decreased -- from 56 percent of cases received by the IRS in 2013 to 44 percent of cases received by the IRS in 2014. Of interest, while foreign-initiated adjustments accounted for 56 percent of non-transfer pricing cases received in 2014, only 35 percent of cases resolved in 2014 were foreign initiated.
- The processing time for transfer pricing double tax cases decreased in 2014 (from an average of 26.1 months in 2013 to 21.4 months in 2014). Remarkably, U.S.-initiated transfer pricing double tax cases decreased from 23.8 months in 2013 to 15.0 months in 2014. Non-transfer pricing cases continued to be processed quickly in 2014, with an average processing time of 19.8 months, up slightly from 19.2 in 2013. Interestingly, U.S.-initiated non-transfer pricing cases processing times decreased from 18.4 months in 2013 to 14.3 months in 2014, while foreign-initiated non-transfer pricing cases processing times increased by 51 percent from 20.0 months in 2013 to 30.2 months in 2014. This increase in processing time may be related to some withholding tax cases in which competent authority negotiations continue to proceed slowly as a result of differences in treaty interpretation between the United States and some treaty partners.

Overall, the 2014 CA statistics are very positive for U.S. taxpayers. Looking forward, the number of requests for CA assistance is expected to continue to rise, in light of the foreign and IRS audit environment, the increased emphasis by the IRS on the need to seek CA assistance, the pending finalization of the new revenue procedure governing requests for CA assistance (which may expand the scope of CA assistance to taxpayer-initiated transfer pricing adjustments), and the new BEPS environment.

As the IRS continues to emphasize the need for U.S. taxpayers to pursue effective and practical remedies, including recourse to competent authority, before claiming a foreign tax credit, U.S. taxpayers under foreign audit should take care not to acquiesce to foreign-initiated adjustments. In addition, U.S. taxpayers that are under tax or transfer pricing audit in foreign jurisdictions, or that have a reasonable expectation they may be subject to a foreign tax audit, should be mindful of treaty timelines to request competent authority relief or file notifications, and take all necessary protective measures to preserve their right to seek competent authority relief. Taxpayers do not need to wait until the conclusion of a transfer pricing audit to take such measures. Failure to notify the IRS (or foreign tax authority) within the specified time frames will likely preclude the taxpayer from seeking competent authority relief from double taxation, which could give rise to issues regarding the creditability of foreign taxes.<sup>7</sup>

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<sup>1</sup>From 2013, the Office of the U.S. Competent Authority (USCA) started tracking its statistics on a calendar-year basis. Thus, the 2013 report represents a transition from the historical fiscal-year basis to the calendar year, and includes 15 months of statistics from October 1, 2012, through December 31, 2013.

<sup>2</sup>APMA has primary responsibility for cases arising under the business profits and associated enterprises article of U.S. income tax treaties, and TAIT has primary responsibility for cases arising under all other articles of U.S. income tax treaties.

<sup>3</sup>APMA Director Hareesh Dhawale told reporters that 192 requests for double tax relief had been filed in calendar year 2013. See "IRS Releases MAP Statistics for 2014 Showing Jump in Filings and Inventory," Bloomberg/BNA *Transfer Pricing Report*, April 16, 2015.

<sup>4</sup>Notice 2013-78 on requests for competent authority relief would supersede the current Rev. Proc. 2006-54, once finalized.

<sup>5</sup>In the past, the IRS has generally not accepted such cases, on the basis that double taxation was not the result of government action as predicated in the Mutual Agreement Procedure article of the relevant tax treaty. Under Notice 2013-78, the IRS reserves the right to deny requests for assistance if the taxpayer-initiated positions evince after-the-fact tax planning or fiscal evasion, or are otherwise inconsistent with sound tax administration.

<sup>6</sup>Using data for the 15-month period from October 1, 2012, through December 31, 2013, for 2013.

<sup>7</sup>See *Procter & Gamble Co. v. U.S.*, (S.D. Ohio, Case No. 1:08-cv-00608, defendant's motion for summary judgment granted 7/6/10).

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