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Memorandum

The APA Program's Experience with Rev. Proc. 2008-31: Increased Opportunities For Certainty

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The jurisdiction of the IRS Advance Pricing Agreement Program (the APA Program) was ''clarified'' in early 2008 with the issuance of Rev. Proc. 2008-31 (the ''Rev. Proc.'').[2] The APA Program's reach previously was limited to issues arising under §482 [3] of the Internal Revenue Code [4] and the Proposed Global Dealing Regulations.[5] The Rev. Proc. expands APA Program coverage to include:

> other issues arising under certain income tax treaties, the Code, or the Income Tax Regulations, *for which transfer pricing principles may be relevant*, such as attribution of profits to a permanent establishment under an income tax treaty, determining the amount of income effectively connected with the conduct by the taxpayer of a trade or business within the United States, and determining the amounts of income derived from sources partly within and partly without the United States, as well as related subsidiary issues.[6]

This article explains why the Rev. Proc. was issued and identifies the kinds of cases that have been deemed to fall within the purview of the Rev. Proc.[7] If there is a guiding principle, it is as follows: If the applicable legal test resolves an issue by reference to economic principles, rather than by a formulaic or other predetermined rule, the APA Program *may* have jurisdiction under the Rev. Proc. to enter into an APA on the issue. Whether or not the APA Program will, in fact, accept jurisdiction when economic principles appear to apply depends on a number of additional factors, such as (i) the consent of the Associate Chief Counsel (International) (ACCI), (ii) when a U.S. tax treaty is involved, the language in Article 7 of the treaty dealing with the attribution of profits to permanent establishments (PEs), (iii) in ''old'' U.S. tax treaties (vs. ''new'' U.S. treaties, which contain revised Article 7 language, as described below), the relationship between the U.S. competent authority and the relevant foreign tax authority; and (iv) the extent to which the issue requires a determination of value, as

[1] When Rev. Proc. 2008-31 was issued in May 2008, Craig Sharon was the APA Director, Clark Armitage was the APA Deputy Director, and Richard Osborne was an APA Branch Chief. Clark Armitage, until March 2010, and then Richard Osborne, until he retired from the IRS in August 2011, were primarily responsible for overseeing and coordinating the application of Rev. Proc. 2008-31 within the APA Program during their respective tenures.

[2] 2008-1 C.B. 1133.

[3] Historically, the APA Program has also had jurisdiction over income inclusions under §367(d). Because such coverage is quite similar to the Program's core coverage under §482, APA coverage of §367(d) issues is not further discussed in this memorandum.

[4] Unless otherwise specified, all section references are to the Internal Revenue Code of 1986, as amended (the ''Code''), and the regulations promulgated thereunder.

[5] Prop. Regs. §§1.482-8, 1.863-3(h).

[6] Rev. Proc. 2008-31 (emphasis added).

[7] This article does not generally describe how transfer pricing principles have, in fact, been applied when deemed relevant.

opposed to a conclusion of law. Outside the new U.S. treaties, whether or not an issue is resolvable by economic analysis, and therefore analyzed using "transfer pricing principles," is not always obvious from the language of the relevant statute or regulations. The Rev. Proc., like the primary APA Program revenue procedure (Rev. Proc. 2006-09),[8] covers both domestic and international issues, but virtually all inquiries to date have involved international matters.

INTRODUCTION

In 2002, then ACCI John Staples curtailed APA Program jurisdiction by limiting coverage to intercompany transactions and allocations covered by the Proposed Global Dealing Regulations.[9] Non-global dealing cases involving attribution of profits to a PE (or to a branch in a non-treaty APA), which had been a fixture of the APA Program since its inception in 1991 (and included principally headquarters expense allocation cases and some royalty cases), would no longer be accepted. The stated rationale for this change was that "there is no current doctrine that applies §482 to attribution of profit to PEs." [10] Mr. Staples added that "[w]e have a great deal of concern about putting the APA Program in the position of leading the policy charge on how to determine the attribution of profit to PEs." [11] More specifically, there were concerns within the Office of the ACCI that APA Program staff did not have the expertise to address PE/branch attribution and were in fact incorrectly applying transfer pricing principles to make PE allocations, or at least did not understand the limited effect of an APA on collateral issues, such as whether or not a PE exists [12] and foreign tax credits.

Given this history, why did the ACCI re-introduce some of these cases to the APA Program? The reversal coincides with the increased application by the United States of transfer pricing principles to determine branch and PE income. Most significantly, since March 2003, the U.S. Senate has ratified seven tax treaties — those with Belgium, Bulgaria, Canada, Germany, Iceland, Japan, and the United Kingdom [13] — that apply transfer pricing principles to determine PE profits. Consistent with these treaty changes, the United States changed its Model Tax Treaty in 2006 to incorporate transfer pricing principles in Article 7.[14] The United States also endorsed the OECD's 2008 Report on the Attribution of Profits to Permanent Establishments [15] (the "2008 OECD PE Report") and the OECD's 2010 Model Tax Treaty Article 7,[16] which similarly apply transfer pricing principles to attribute profits to PEs.

In addition, over roughly the same period, the ACCI had indicated informally on different occasions that in certain instances U.S. domestic law applies transfer pricing principles to determine the profits of U.S. branches of foreign corporations and to determine the foreign source income of foreign branches of U.S. corporations. Among other things, these determinations created potential jurisdictional conflicts with the IRS Pre-Filing Agreement Program, which has concurrent authority with the Office of the ACCI on PE attribution and most other international issues, but no jurisdiction over transfer pricing issues.[17] The Rev. Proc. ensured that the APA Program would retain exclusive jurisdiction for advance rulings on transfer pricing matters and that taxpayers would have an effective advance issue resolution forum available to them on PE attribution and other transfer pricing issues outside §482.

Given the evolving nature of the substantive law, it is not surprising that the APA Program has proceeded cautiously with accepting applications under the Rev. Proc. Since the Rev. Proc. was issued, the APA Program has evaluated each case one at a time, required prefiling conferences, and involved, to the extent possible, the appropriate ACCI technical branch to help determine which substantive rules will or should apply to a potential case.[18] Putting the ACCI technical branches in the center of decisions about APA Program jurisdiction over branch and PE cases addressed concerns about the appropriateness of the APA Pro-

[8] 2006-1 C.B. 278.

[9] Molly Moses, "Staples Responds to Charges That IRS Cutting APA Scope: Says Program Should Not Lead Policy Charge in PE Area," 11 *Tax Mgmt. Transfer Pricing Rpt.* (BNA) 23 (5/1/02) (interview with John Staples).

[10] *Id.*

[11] *Id.*

[12] The determination of whether a PE exists is not based on transfer pricing principles. Accordingly, the APA Program generally lacks authority to make such a determination. In practice, if a taxpayer contests the existence of a PE in an APA submission requesting coverage of the attribution issue, the APA Program will reject the taxpayer's request on administrative grounds. A taxpayer may obtain an advance ruling on the PE issue from the Pre-Filing Agreement Program. Rev. Proc. 2009-14, 2009-1 C.B. 324, at §3.06(2) and (3) (branch determinations), (5) (PE determinations).

[13] These treaties undoubtedly account for a very significant portion of U.S. APA and double-tax cases (although the United States does not publish per-country inventory or completion data).

[14] United States Model Income Tax Convention, Nov. 15, 2006.

[15] OECD Centre for Tax Policy and Administration, Report on the Attribution of Profits to Permanent Establishments, July 17, 2008.

[16] OECD Model Tax Convention on Income and on Capital, July 22, 2010.

[17] *See, e.g.,* Rev. Proc. 2009-14, 2009-1 C.B. 324, at ¶3.06, 3.08(1).

[18] Lisa M. Nadal, "New Director Shares Goals and Expectations for APA Program," 119 *Tax Notes* 901 (6/2/08).

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gram handling these cases and has allowed the Office of the ACCI to speak with a single voice regarding the circumstances in which transfer pricing principles will be applied outside §482.

With several years of applications under its belt, the APA Program now has some experience with how the Rev. Proc. is working. In summary, although there has been a considerable volume of inquiries, only a handful of APA applications under the Rev. Proc. have been submitted and accepted. This result is somewhat disappointing, but not surprising. The caution with which the APA Program has addressed these cases — the prefiling process has typically been long and its outcome uncertain — has undoubtedly discouraged taxpayers from seeking an APA under the Rev. Proc. In addition, many of the submitted cases have required the application of both transfer pricing principles and the allocation and apportionment methods of the Code and Treasury regulations (''regulations''). This complicates the process by requiring the involvement, throughout the APA process, of personnel from the ACCI technical branches to interpret and apply domestic allocation and apportionment rules and to address collateral issues. Also, for bilateral and multilateral APAs, such partial applications of transfer pricing principles do not bode well for avoidance of double tax where the foreign competent authority (CA) likely will be confused about or unreceptive to the application of U.S. domestic rules, especially those that are formulary in nature, such as the allocation and apportionment of research and experimentation expenses under Regs. §1.861-17.

Notwithstanding the small number of applications, there have been several useful developments stemming from proceedings under the Rev. Proc. First, in non-global dealing cases involving one of the seven new treaties identified above, it is reasonably clear that the APA Program will apply transfer pricing principles to reach an operating profit result for both unilateral and bilateral APAs and for both inbound and outbound situations, thereby defining the taxing jurisdiction of the host country. For outbound situations, however, there is an additional wrinkle. That is, the APA will not govern the sourcing of expenses for purposes of calculating the §904 foreign tax credit limitation.[19] That determination remains subject to the U.S. allocation and apportionment rules, which may limit to some extent the utility of an outbound APA, especially a unilateral APA. Second, the APA Program has refined its thinking about the global dealing area in ways that helpfully expand the scope of APA coverage (i.e., covering commodities transactions and other ''securities'' and the allocation of interest expense). Finally, the ACCI has identified several circumstances in which it views the Code and regulations as calling for the application of transfer pricing principles on an implied basis. Examples are identified below.

There is reason to believe that the APA Program, after it merges into the new Advance Pricing and Mutual Agreement (APMA) Program,[20] will improve as a forum for addressing PE allocations. First, U.S. treaty negotiators presumably will continue to pursue treaty language requiring the application of transfer pricing principles to determine PE profits. Application of transfer pricing principles may eventually become the de facto standard, at least for bilateral and multilateral APA negotiations. Second, the U.S. competent authority has long applied transfer pricing principles to resolve potential double taxation situations under non-APA mutual agreement procedures (i.e., double tax cases) involving PE allocations. That experience will accelerate the learning of APA Program staff when the two functions are combined in the APMA Program. Finally, the ongoing shift in U.S. international tax enforcement away from confrontation to cooperation will emphasize the importance of early-issue resolution and should only heighten the role of the APA Program in IRS enforcement going forward.

It is important to note that the ACCI will likely continue to be involved in cases arising under the Rev. Proc. because these cases will likely be considered ''strategic'' — presumably, cases involving novel fact situations or the application of legal principles for which there is little authority or precedent — under relevant APMA procedures:

> ACCI will continue to provide legal advice and support to LB&I on all transfer pricing matters. With respect to APAs, early in the process, the APMA team will recommend whether an APA should be treated as a non-strategic APA (i.e., an APA requiring a determination of facts or the application of well-established legal principles to known facts) or as a strategic APA. In APAs determined to be strategic, an ACCI attorney will be assigned to assist the team, and the initial APA position paper (the U.S. position developed for pur-

[19] As discussed below, the seven new treaties and many other treaties as a general rule deem gross income that is taxable consistent with the treaty by the foreign country to be income from sources in that country.

[20] On July 27, 2011, the IRS announced that the APA Program and the part of the U.S. Tax Treaty Office that deals with double-tax allocation cases would be merged into a new office within the LB&I Transfer Pricing Practice and renamed the APMA Program. For additional information about the APMA Program, see the APA and Mutual Agreement Program Realignment questions and answers posted on the IRS website on July 27, 2011, at http://www.irs.gov/businesses/article/0,,id=242980,00.html.

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poses of beginning bilateral negotiations) or the APA itself (in unilateral cases) will be subject to the concurrence of the ACCI.[21]

U.S. APPLICATION OF TRANSFER PRICING PRINCIPLES TO PE/BRANCH CASES

In Income Tax Treaties

U.S. income tax treaties can and often do abrogate the Code and regulations. Before 2001, the United States sought in treaty negotiations to retain, at least in part, its ability to apply the Code and regulations to determine the income of a PE. Treasury's Technical Explanation for the United States Model Income Tax Convention of 1996 states in part:

> [Paragraph 3 of Article 7] specifies that the expenses that may be considered to be incurred for the purposes of the permanent establishment are expenses for research and development, interest and other similar expenses, as well as a reasonable amount of executive and general administrative expenses. *This rule permits (but does not require) each Contracting State to apply the type of expense allocation rules provided by U.S. law (such as in Treas. Reg. sections 1.861-8 and 1.882-5).*[22]

The Technical Explanation offered the following rationale for U.S. retention of this authority:

> Paragraph 3 does not permit a deduction for expenses charged to a permanent establishment by another unit of the enterprise. Thus, a permanent establishment may not deduct a royalty deemed paid to the head office. Similarly, a permanent establishment may not increase its business profits by the amount of any notional fees for ancillary services performed for another unit of the enterprise, but also should not receive a deduction for the expense of providing such services, since those expenses would be incurred for purposes of a business unit other than the permanent establishment.[23]

In other words, the United States viewed inter-branch ''transactions'' as tax nothings that should be ignored.[24] Under this view, when a PE acts, the corporation as a whole is acting, and not merely the PE. Profits attributable to the PE must therefore be a ratable portion of the corporation's income, rather than a portion determined by an artificial ''separate-entity'' structure that the corporation imposes on its constituent parts.

The IRS pursued this view in *National Westminster Bank, PLC v. U.S.*,[25] where the United States asserted that U.S. rules for apportioning interest expense between a foreign corporation and its U.S. PE (Regs. §1.882-5) applied under Article 7 of the 1975 U.S.-U.K. Tax Treaty.[26] The court disagreed[27] and found that the application of Regs. §1.882-5 impermissibly disregarded an intra-corporate allocation of capital from the bank's home office to its U.S. PE:

> [W]e do not read the separate enterprise language of Article 7, P 2 — requiring that the U.S. Branch's business profits be determined as ''if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment'' — as permitting transactions between the permanent establishment and the enterprise to be disregarded.[28]

The court concluded instead that an appropriate analysis to determine the interest expense of the U.S. PE of National Westminster Bank, PLC, would start with the books and records of the PE:

> [W]e uphold the trial court's decision in *NatWest II*. ''[B]ranch profits must be based

[21] *Id.*

[22] Technical Explanation, United States Model Income Tax Convention, art. 7, ¶3, Sept. 20, 1996 (emphasis added).

[23] *Id.*

[24] *See also* Regs. §1.446-3(c)(1)(i) (explaining that ''a taxpayer cannot enter into a contract with itself'' as the basis for not allowing inter-branch dealings to constitute notional principal contracts).

[25] 512 F.3d 1347 (Fed. Cir. 2008). The IRS has not issued an action on decision with respect to the case.

[26] Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-U.K., Dec. 31, 1975, 31 U.S.T. 5668.

[27] The IRS made a similar losing argument in an earlier case, *North West Life Assurance Company of Canada v. Comr.*, 107 T.C. 363 (1996), arguing that a statutory formula in §842(b) should determine the minimum amount of investment income effectively connected to the taxpayer's U.S. PE. The taxpayer argued that the PE did not have to follow the regulations, but instead should be treated as if it was a separate entity for purposes of determining the PE's effectively connected U.S. insurance income under Article 7 of the then-effective (1980) U.S.-Canada treaty. The Tax Court found for the taxpayer.

[28] *National Westminster Bank, PLC v. U.S.*, 512 F.3d 1347, at 1354–55 (Fed. Cir. 2008).

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on the properly maintained books of the branch,'' subject to examination and adjustment where: ''(1) an interest expense was deducted for advances to the branch that were not used in the ordinary course of its banking business; (2) an interest expense was deducted on amounts designated as capital on its books or on amounts that were in fact allotted to it for capital purposes, such as funding capital infrastructure; and (3) interest paid on interbranch borrowing [that] was not at arms' length.'' [29]

In the early 2000s (and possibly earlier), the United States began to change its treaty position that intracorporate transactions should be ignored in all circumstances and that Code and regulations allocation and apportionment rules should be applied exclusively to allocate interest and other expenses. Article 7 of the 2001 U.S.-U.K. tax treaty restated the last sentence of Article 7, paragraph 2, to incorporate ''risks assumed'' terminology: ''For this purpose, the business profits to be attributed to the permanent establishment shall include only the profits derived from the assets used, risks assumed and activities performed by the permanent establishment.'' [30] The treaty also amended paragraph 3, which provides for the deduction of expenses in calculating a PE's business profits, to eliminate the reference in the predecessor U.S.-U.K. treaty to ''a reasonable allocation of . . . expenses incurred for the purposes of the enterprise as a whole.'' [31] The Exchange of Notes to the new U.S.-U.K. treaty make clear that, as a result of these changes, transfer pricing principles apply: ''OECD Transfer Pricing Guidelines will apply, by analogy, for the purposes of determining the profits attributable to a permanent establishment.'' [32]

To amplify what it means to apply transfer pricing principles specifically with respect to interest expense, the Exchange of Notes states:

In particular, in determining the amount of attributable profits, the permanent establishment shall be treated as having the same amount of capital that it would need to support its activities if it were a distinct and separate enterprise engaged in the same or similar activities. With respect to financial institutions other than insurance companies, a Contracting State may determine the amount of capital to be attributed to a permanent establishment by allocating the institution's total equity between its various offices on the basis of the proportion of the financial institution's risk-weighted assets attributable to each of them.[33]

The United States thus agreed to apply transfer pricing principles to determine the profits of a PE. It subsequently expressly acknowledged, through separate advice, that Regs. §1.882-5 is inconsistent with transfer pricing principles because it fails to risk-weight assets, as unrelated parties would.[34] But the United States arguably won the war on allocation of interest expense by ensuring that it could effectively ignore a PE's documented capital and apportion interest based on risk-weighted assets. National Westminster Bank undoubtedly would obtain a very different result under the 2001 treaty than under the 1975 treaty.

The United States has since agreed to similar Article 7 transfer pricing language in six other ratified [35] treaties:

Treaty Country	Relevant Document	Execution Date	Entry into Force	Effective in United States for Tax Years . . .
Belgium	2006 Treaty and 2006 Protocol	November 27, 2006	December 28, 2007	Beginning Jan. 1, 2008 (except for withholding)
Bulgaria	2007 Treaty	February 23, 2007	December 15, 2008	Beginning Jan. 1, 2009

[29] *Id.* at 1362 (internal citation omitted).

[30] Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-U.K., July 24, 2001, T.I.A.S. 13161.

[31] Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-U.K., Dec. 31, 1975, 31 U.S.T. 5668.

[32] Exchange of Notes, Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-U.K., July 24, 2001, T.I.A.S. 13161.

[33] *Id.*

[34] Notice 2005-53, 2005-2 C.B. 263; *see also* Technical Explanation, United States Model Income Tax Convention, art. 7, ¶3, Nov. 15, 2006 (''[Regs. §] 1.882-5 does not take into account the fact that some assets create more risk for the enterprise than do other assets. An independent enterprise would need less capital to support a perfectly-hedged U.S. Treasury security than it would need to support an equity security or other asset with significant market and/or credit risk.'').

[35] In addition to these Senate-ratified treaties, the United States has agreed to apply arm's-length principles in other, pending treaties, including those with Luxembourg and Switzerland, which were approved by the Senate Foreign Relations Committee in August 2011.

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Canada	2007 Protocol	September 21, 2007	December 15, 2008	Beginning Jan. 1, 2009 (except for withholding)
Germany	2006 Protocol	June 1, 2006	December 28, 2007	Beginning Jan. 1, 2008 (except for withholding)
Iceland	2007 Treaty and Exchange of Notes	October 23, 2007	December 15, 2008	Beginning Jan. 1, 2009
Japan	2003 Treaty and Exchange of Notes	November 6, 2003	March 30, 2004	Beginning Jan. 1, 2005 (except for withholding)
United Kingdom	2001 Treaty and Exchange of Notes	July 24, 2001	March 31, 2003	Beginning Jan. 1, 2004 (except for withholding)

The new language eventually made its way into the U.S. model treaty, with the 2006 U.S. Model Income Tax Convention including the "risks assumed" language in Article 7, paragraph 2: "For this purpose, the profits to be attributed to the permanent establishment shall include only the profits derived from the assets used, risks assumed and activities performed by the permanent establishment." [36] As noted in the 2006 U.S. Model Treaty Technical Explanation: "The language of paragraph 2, when combined with paragraph 3 dealing with the allowance of deductions for expenses incurred for the purposes of earning the profits, incorporates the arm's-length standard for purposes of determining the profits attributable to a permanent establishment." [37]

The 2006 U.S. Model Treaty Technical Explanation envisions that in future treaties the United States will continue to seek language in the Exchange of Notes providing for the special interest allocation rule:

> [T]he notes allow a taxpayer to apply a more flexible approach [to allocate interest expense] that takes into account the relative risk of its assets in the various jurisdictions in which it does business. In particular, in the case of financial institutions other than insurance companies, the amount of capital attributable to a permanent establishment is determined by allocating the institution's total equity between its various offices on the basis of the proportion of the financial institution's risk-weighted assets attributable to each of them.[38]

While the new treaties anticipate the application of transfer pricing principles to determine the taxable income of a PE, the new treaties do not embrace transfer pricing principles for purposes of calculating a U.S. corporation's foreign tax credit limitation. The seven new treaties (like other U.S. treaties) include two provisions relevant to determining the amount of creditable taxes paid by a U.S. corporation to a foreign host country. First, the United States is required, subject to the limitations of U.S. law, to allow a credit for income taxes paid to the host country. For example, Article 24, paragraph 1 of the new U.S.-U.K. treaty provides:

> In accordance with the provisions and *subject to the limitations of the law of the United States*, . . . the United States shall allow to a resident [defined in Treaty Article 4 to include corporate residents] . . . of the United States as a credit against the United States tax on income a) the income tax paid or accrued to the United Kingdom by or on behalf of such . . . resident.[39]

Because transfer pricing principles apply to determine the amount of income that the United Kingdom and other new-treaty countries may tax, transfer pricing principles are in effect used to determine whether a foreign income tax is creditable under §901; i.e., that the foreign tax in question was imposed on the net income properly taxable by the treaty jurisdiction. As the emphasized language makes clear, however, the U.S. foreign tax credit limitation in §904 continues to apply, so that the foreign taxes, while creditable, may not be usable in a particular year if the U.S. corporation is in an excess foreign tax credit position with respect to those foreign taxes.

A second provision of the typical U.S. tax treaty, including the new treaties, lessens to an extent the implications of the continuing application of §904. Under treaty "re-sourcing" provisions, "gross income" that is properly subject to tax by the foreign host country (i.e., applying transfer pricing principles) is deemed to be from sources in the foreign host country, even if it would be U.S. source under the Code

[36] United States Model Income Tax Convention, art. 7, ¶2, Nov. 15, 2006.

[37] Technical Explanation, United States Model Income Tax Convention, art. 7, ¶2, Nov. 15, 2006.

[38] *Id.* at art. 7, ¶3.

[39] Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-U.K., art. 24, ¶1, July 24, 2001, T.I.A.S. 13161 (emphasis added).

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and regulations. For example, the new U.S.-Japan treaty provides: ''For the purposes of this paragraph, an item of gross income as determined under the laws of the United States, derived by a resident of the United States that, under this Convention, may be taxed in Japan shall be deemed to be income from sources in Japan.'' [40] Under the new treaties, transfer pricing principles thus also determine the portion of a U.S. corporation's gross income that is properly treated as foreign source gross income for purposes of the foreign tax credit limitation of §904. The new treaties, like other U.S. tax treaties, do not, however, provide for the re-sourcing of expenses. The Code and regulations apply in this area and, where those rules are not based on transfer pricing principles, may thus produce an amount of net foreign source income that differs from maximum taxable income determined under the treaty.

In OECD Guidance

Consistent with the change in its treaty negotiating position, the United States endorsed the application of transfer pricing principles in the 2008 OECD PE Report and the 2010 OECD Model Tax Treaty. Both OECD documents generally employ transfer pricing principles to determine the profits attributable to a PE.

The OECD Model Tax Treaty incorporates the ''risks assumed'' language discussed above.[41] The Commentary to the OECD Model Tax Treaty Article 7 explains that the revised language is intended to be consistent with the approach authorized by the OECD in the 2008 OECD PE Report (the ''Authorized OECD Approach'' or ''AOA'').[42]

The AOA first hypothesizes the PE as a distinct and separate enterprise, then attributes profits to that PE under transfer pricing principles:

> [T]he authorised OECD approach is that the profits to be attributed to a PE are the profits that the PE would have earned at arm's length if it were a legally distinct and separate enterprise performing the same or similar functions under the same or similar conditions, determined by applying the arm's length principle.[43]

In hypothesizing the PE as a distinct and separate enterprise, the AOA analyzes the ''significant people functions'' [44] performed by the PE and then attributes assets and risks based on the results of that functional analysis:

> [T]he authorized OECD approach attributes to the PE those risks for which the significant functions relevant to the assumption and/or management (subsequent to the transfer) of the risks are performed by people in the PE and also attributes to the PE economic ownership of assets for which the significant functions relevant to the economic ownership of assets are performed by people in the PE.[45]

In evaluating economic ownership of assets and attribution of risks, the AOA indicates that intra-corporate dealings will be recognized, provided any such dealing is ''equivalent to a transaction that would have taken place between independent enterprises acting at arm's length.'' [46] A key exception to the AOA's general recognition of intra-corporate dealings is for guarantees, which are not recognized.[47] The effect of disregarding intra-corporate guarantees, along with treating a PE as having the same creditworthiness as the enterprise of which it is part,[48] is to allow for the allocation of ''free'' capital (i.e., equity from a U.S. standpoint) and interest expense based on ''the arm's length principle.'' [49] The AOA provides details on the methods for allocating free capital and interest expense and indicates that there is a range of permissible capital and allocable interest that may be attributed in any particular situation.[50]

Once the PE is hypothesized as a distinct and separate enterprise (with functions, assets, and risks attributed to it), the OECD Transfer Pricing Guidelines [51] are used ''by analogy'' to determine the PE's attributable income.[52] It is worth noting that the AOA does not dictate the specifics or mechanics of domestic law, but only sets the maximum ''limit on the amount of attributable profit that may be taxed in the host country of the PE.'' [53] Thus, for example, the AOA determines which expenses should be attributed to the PE,

[40] Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.-Japan, art. 23, ¶1, Nov. 26, 2003.

[41] OECD Model Tax Convention on Income and on Capital, art. 7, ¶2, July 22, 2010.

[42] Commentary, OECD Model Tax Convention on Income and on Capital, art. 7, Part I, ¶9.

[43] 2008 OECD PE Report, Part I, ¶10.

[44] *Id.*, at ¶19.

[45] *Id.*, at ¶18.

[46] *Id.*, at ¶38.

[47] *Id.*, at ¶¶32, 36.

[48] *Id.*, at ¶¶33, 130.

[49] *Id.*, at ¶33.

[50] *Id.*, at ¶¶34, 35.

[51] OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, July 22, 2010.

[52] 2008 OECD PE Report, Part I, ¶12.

[53] *Id.*

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but it does not go on to determine whether those expenses, once attributed, are deductible when computing the net profit of the PE.[54] As a consequence, the AOA does not determine, on its own, either the creditability of foreign taxes or the source of PE profits for U.S. foreign tax credit limitation purposes.

The AOA has four parts. Part I, cited above, provides rules of general application, while Parts II, III, and IV provide rules for banking, global trading, and insurance, respectively. The general guidelines discussed above generally apply to the other Parts of the AOA.

In APA Program Practice Under the Code and Regulations

When the Rev. Proc. was issued, the APA Program had virtually no experience applying transfer pricing principles to branches and PEs under the Code and regulations outside the global dealing context. Presumably, that was because few people understood that transfer pricing principles might apply to certain technical aspects of the determination of net income attributable to a PE or that the APA Program would accept such cases. There may have been APAs, especially before 2002, covering transactions governed in whole or in part by the allocation and apportionment principles of the Code and regulations, but it seems clear that the APA Program was applying transfer pricing principles (i.e., the Treasury regulations under §482) to all aspects of these cases rather than basing its analysis on a specific application of the allocation and apportionment rules of the Code and regulations. Regardless, the ACCI and the APA Program learned quickly after the Rev. Proc. was issued that the interplay between the technical rules and the application of transfer pricing principles was more complicated than expected and that they were working mostly from a blank slate.

APA PROGRAM EXPERIENCE UNDER REV. PROC. 2008-31

The principal driver behind the change in APA Program jurisdiction set forth in the Rev. Proc. was the change in U.S. treaty language under Article 7 and the accompanying adoption by the OECD of the AOA. In addition to re-introducing cases that were part of APA Program inventory before the 2002 decision to curtail APA Program jurisdiction (such as headquarters expense allocation cases involving PEs), the new treaty language and the AOA have changed the way the APA Program handles global dealing cases. A handful of other cases under the Rev. Proc. have involved non-new-treaty, non-global-dealing situations where the Code and regulations require or permit the application of transfer pricing principles in determining the income that is attributable to a PE or branch.

Cases Arising Under New Treaties and the AOA

As noted above, seven U.S. treaties ratified after 2000 adopt transfer pricing principles in Article 7 to determine the income that may be attributed to a PE and thus taxed by the host country. The APA Program interprets these treaties as requiring the use of the AOA to determine the taxable income of the PE. In inbound cases, the AOA is used to determine the maximum U.S. taxable income. In outbound cases, the AOA is used to determine (i) the maximum income that the host country may tax and therefore the maximum amount of creditable tax imposed on such income by the host country and (ii) the source of the gross income of the PE, but not the source of associated expenses, for purposes of the foreign tax credit limitation calculation in §904. The key cases, or groups of cases, accepted to date by the APA Program under the Rev. Proc. are described below.

Several new-treaty applications under the Rev. Proc. have requested APA coverage of headquarters expense allocations from a U.S. multinational to its foreign PEs. As many of the PE cases handled prior to 2002 involved headquarters allocations, it makes sense that these cases would be the first to return to the APA Program. The cases are covered by the Rev. Proc. because they involve allocations from a U.S. multinational to one or more PEs located in one or more new-treaty countries. The challenge for these cases is that U.S. multinationals seldom limit their operations to countries that have negotiated new Article 7 language with the United States. The cases thus involve application of both U.S. domestic allocation and apportionment rules and transfer pricing principles under the AOA. The domestic rules may or may not employ transfer pricing principles, so the question becomes how to reconcile the two regimes in an APA to avoid double taxation or an outcome where income is not taxed anywhere.

In at least one unilateral APA involving headquarters expense allocations, the APA Program has applied transfer pricing principles to the allocation of a U.S. corporation's headquarters expenses to both new-treaty countries and old-treaty countries. The APA Program recognized that if transfer pricing principles were used to determine the portion of the expense pool allocated to new-treaty country operations, but U.S. domestic principles were used to determine the

[54] *Id.*, at ¶¶12, 290. For example, if charitable expenses are not deductible under applicable domestic law of the PE, the AOA will not make them deductible.

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portion of the pool allocated to old-treaty or non-treaty country operations, there might be an inconsistency between the two sets of allocations that produced double taxation or untaxed income. To avoid this result, the APA Program agreed to apply transfer pricing principles for the allocations to all affected countries.

In at least one other outbound case, the APA Program allowed the allocation of interest expense based on transfer pricing principles, rather than under the Code and regulations (i.e., Regs. §§1.861-9T through 1.861-13T). This treatment is significant because the case did not involve a global dealing operation where allocation of interest expense based on transfer pricing principles is more established (see discussion below). It is also important to note that the relevant treaty partners were amenable to a transfer pricing analysis, so the decision to apply the AOA to allocate the taxpayer's interest expense was as much practical as it was technical.

This last point — i.e., the need for pragmatism — is a recurring consideration in Rev. Proc. cases, especially when a foreign treaty partner is involved. For example, even in old-treaty countries, if the U.S. competent authority and the foreign tax authority have historically resolved PE attribution cases based on transfer pricing principles, the APA Program has been willing, in at least one case, to apply the AOA to a new APA request notwithstanding the old Article 7 language. Similarly, when an APA request spans one or two old-treaty years and several new-treaty years, the APA Program has agreed to apply transfer pricing principles to the old-treaty years to allow for a single transfer pricing method for all APA years.

As discussed above, in cases involving U.S. corporation PEs in new-treaty countries, the APA Program will apply transfer pricing principles to determine the maximum taxable income of the PE, but will apply the allocation and apportionment rules in the Code and regulations for sourcing expenses for purposes of determining the §904 foreign tax credit limitation fraction. This is a very significant exception to the application of transfer pricing principles in outbound cases where certain expenses are sourced based on rules from the Code and regulations that do not apply transfer pricing principles (e.g., interest, foreign taxes, and research and experimentation expenditures). If these expenses are material, a unilateral APA covering such an outbound situation would be of limited utility since sourcing is a key U.S. question and, unlike in a bilateral APA, the foreign treaty country would not be bound by the transfer pricing outcome (because the foreign country is not a party to a unilateral APA). Also, such an APA, even if bilateral, could produce some strange results. If a significant portion of the transfer pricing net income of a foreign branch or PE is treated as U.S. source income (because, for example, the allocation and apportionment regulations allocate significant research and experimentation expenses to the foreign branch or PE), this would reduce the corporation's §904 limitation and could prevent the utilization of foreign taxes paid on the PE's transfer pricing net income.

The AOA permits the host country to apply its domestic rules regarding whether and when gross income and expenses allocated to a PE under transfer pricing principles, are to be included and deducted from income, respectively. For example, U.S. accelerated depreciation rules may not apply to determine the ''transfer pricing'' income of a U.S. PE of a foreign corporation, but would apply to determine the taxable income of the PE. Similarly, U.S. mark-to-market rules apply to determine the U.S. taxable income of a U.S. securities dealer PE. The foreign corporation's home country might have different base and timing rules for including gross income and deducting expenses. The variance in the two countries rules could result, for a particular year, in income being double taxed or not taxed at all. Over time, however, most of these differences will reverse because the rules typically affect only timing and do not permanently change net income amounts.

Global Dealing Cases

The Rev. Proc. did not newly confer APA Program jurisdiction over global dealing cases that involve PEs. As noted earlier, such cases were not proscribed in 2002 when Mr. Staples limited APA Program coverage of branch and PE cases. These cases are now some of the oldest in the APA Program (on their third or fourth renewals). The Rev. Proc. did, however, expand APA Program jurisdiction over global dealing cases in two important ways: (1) by adding commodities transactions to the coverable pool of global dealing transactions; and (2) by permitting coverage of the allocation of interest expense.[55] For both items, the APA Program's jurisdiction is dependent on the applicability of the new treaties and the AOA. For example, if the global dealing participants of a single corporation are located in New York, London, and Tokyo, the APA Program has jurisdiction because transfer pricing principles apply under the new U.S.-U.K. and U.S.-Japan treaties.

The basis for generally permitting the APA Program to cover global dealing PE cases is that the Proposed Global Dealing Regulations apply transfer pricing

[55] The APA Program started addressing these issues when the 2001 U.S.-U.K. treaty went into force and before issuance of the Rev. Proc. The Rev. Proc. clarified that the APA Program had authority to do so.

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methods to allocate profit among the controlled participants in a global dealing operation. Prop. Regs. §1.482-8(a)(1) allocates ''income, gains, losses, deductions, credits and allowances'' between the controlled participants, and one of the methods used is the profit split method under Prop. Regs. §1.482-8(e)(1), which allocates ''operating profit.''

Prop. Regs. §1.863-3(h), which addresses sourcing of income from global dealing transactions, makes clear that the transfer pricing principles of Prop. Regs. §1.482-8 apply to determine the source of income of a global dealing PE. Each qualified business unit (QBU) of a global dealing operation (i.e., each PE) is considered to be a separate participant for purposes of applying the rules of Regs. §1.482-8.[56] Any ''income, gain or loss'' from global dealing that is thus allocated to a QBU/PE is sourced to the residence of the QBU/PE under Prop. Regs. §1.863-3(h)(2). It is expected that the final regulations (if they are ever issued) will clarify that only gross income will be so sourced (rather than gross income net of deductions for operating expenses), and that deductions will be allocated and apportioned for foreign tax credit limitation purposes under the normal rules of the Code and regulations. This mirrors the resourcing provisions of the typical U.S. treaty, as discussed above.

The APA Program historically did not cover commodities books in global dealing cases because commodities are not ''securities'' within the meaning of §475(c)(2) and so are not covered by the Proposed Global Dealing Regulations.[57] The exclusion of commodity book cases from the APA Program has now changed in part. Where the principal dealing operations are located in new-treaty countries, such as Japan and the United Kingdom, the APA Program has covered commodity transactions in global dealing APAs. This has several benefits for both the IRS and taxpayers. Interest and back-office expenses for books that involve securities and books that involve other transactions (such as commodities) may now be covered in a single analysis, which helps to ensure that the expenses for all books are allocated on a consistent basis. It also allows for the use of a consistent profit split formula for allocating profits for all books among the global dealing participants.

Since the Rev. Proc. was issued, the APA Program has also changed the way it handles the allocation of interest expense within a single-entity global dealing operation. The APA Program views the seven new treaties and the AOA as permitting inbound taxpayers (i.e., foreign corporations with a U.S. PE) to apply either a risk-adjusted asset allocation method or Regs. §1.882-5 to allocate interest expense to the U.S. PE. The foreign corporation must select a single method for all of its U.S. PE operations (i.e., the IRS view is understood to be that taxpayers may not pick and choose methods within a single company for a single year). If the taxpayer elects to apply Regs. §1.882-5, the APA Program will not provide for a detailed application of the regulation, but will simply recommend that the APA specify that the regulation will govern for U.S. purposes (and, for bilateral APAs, that applicable foreign rules will govern to allocate interest expense to the foreign operation). This is largely a continuation of pre-Rev. Proc. APA Program practice. If the taxpayer elects instead to apply a risk-adjusted asset allocation method, the APA Program will then engage the taxpayer and eventually the foreign competent authority in a discussion of:

1. How much total capital the U.S. PE needs to conduct its business;
2. How much free capital/equity the U.S. PE needs;
3. The arm's length return on the capital (i.e., since the provision of capital is viewed as routine, a routine return to capital is typically awarded or recommended by the APA Program);
4. The appropriate interest rate on the portion of the company's third-party debt that should be borne by the U.S. PE; and
5. The total interest expense to be borne by the U.S. PE (i.e., total capital less free capital times the third-party interest rate).

In contrast to the inbound situation, the new treaties provide no safe harbor to use the Code and regulations (i.e., Regs. §§1.861-9T through 1.861-13T) to allocate interest expense to a foreign PE of a U.S. company. This is so because the AOA permits the PE's host country, but not the home country, to apply local rules for determining the PE's attributable interest expense.[58] Given the pragmatism exhibited by the APA Program to date in implementing the Rev. Proc., it is possible that the APA Program would consider a Code- and regulations-based approach for allocating interest expense in outbound new-treaty situations if the normal AOA analysis is difficult. In a bilateral APA, the U.S. and host country competent authorities would presumably agree to a single formula for allo-

[56] The rules here for ''hypothesizing'' the separate QBUs (or PEs) are similar to those provided by the AOA. For example, ''since the entire capital of a corporation supports all of the entity's transactions, regardless of where those transactions may be booked, the payment of a guarantee fee within the entity is inappropriate and will be disregarded.'' Prop. Regs. §1.863-3(h)(3)(ii). Also, certain agreements between the QBUs will be recognized. Prop. Regs. §1.863-3(h)(3)(iii).

[57] *See* Prop. Regs. §1.482-8(a)(2).

[58] 2008 OECD PE Report, Part III, ¶242, Part II, ¶128.

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cating interest expense (whether Code- and regulations-based or otherwise). In a unilateral APA, the taxpayer would have to accept the risk that the host country might allocate interest expense on some other basis. The taxpayer presumably would do so only if it believed that the foreign country would accept an allocation based on the principles of the Code and regulations or because applicable local rules would allocate more interest expense to the PE and so in effect produce double deductions.

Cases Arising Under Old Treaty and Non-Treaty Situations

In addition to providing for APA Program jurisdiction to determine PE income under a treaty that invokes transfer pricing principles, the Rev. Proc. permits the APA Program to accept cases that involve ''determining the amount of income effectively connected with the conduct by the taxpayer of a trade or business within the United States, and determining the amounts of income derived from sources partly within and partly without the United States.''[59] In several specific circumstances, the APA Program has been permitted to handle such non-new-treaty, inbound and outbound cases, respectively, because the applicable rules of the Code and regulations have been deemed to require or permit the application of transfer pricing principles.

The ACCI technical branches have been heavily involved in evaluating whether transfer pricing principles apply in a particular setting and so in determining whether APA Program jurisdiction exists. The process has revealed a surprising amount of uncertainty about the interplay between the U.S. domestic rules and transfer pricing principles and about the scope and effect of an APA to PE situations involving non-treaty and old-treaty countries. Still, the process has produced a number of helpful technical clarifications, led to a few unanticipated outcomes, and produced a few noteworthy early precedents.

Some old treaties (e.g., with Switzerland) have language in the technical notes or other commentary that suggests that transfer pricing principles could be applied to determine the income of PEs. Indeed, more than one taxpayer has pointed to such language and cited *National Westminster* and *North West Assurance*, among other authorities, to argue that the APA Program should have jurisdiction under the Rev. Proc. to attribute net profit to PEs in some (if not all) old treaties. The IRS has not so interpreted such treaties based in part on historic practice and in part because the treaties do not mention ''risks and assets'' in the Article 7 text or commentary. Notwithstanding this longstanding IRS view, a taxpayer could seemingly take a filing position applying transfer pricing principles under Article 7 in an old treaty, but such a taxpayer should be prepared for the IRS to challenge that position in a mutual agreement proceeding, administrative proceedings, and litigation. The APA Program would almost certainly reject an APA request based on such a position.

On the favorable side, one or more prefile meetings under the Rev. Proc. have involved the method for sourcing income from services that are performed partly within and partly without the United States. Under the Code and regulations, gross income from performing services is sourced as U.S. or foreign according to whether the services are performed within or without the United States. Gross income from services performed partly within and partly without the United States is sourced ''on the basis that most correctly reflects the proper source of the income under the facts and circumstances of the particular case.''[60] The ACCI has interpreted this standard as invoking transfer pricing principles.

While services gross income is sourced by applying transfer pricing principles, the associated deductions are apportioned between U.S. and foreign sources under rules of the Code and regulations that do not necessarily apply transfer pricing principles. Thus, net foreign source income will not always correspond to the transfer pricing concept of net (or operating) profit. The APA Program may accept a services case where less than all relevant deductions are sourced based on transfer pricing principles and the taxpayer will have to decide whether it wishes to obtain ACCI technical branch determinations on the sourcing of expenses.

The APA Program's working assumption in these cases is that the Code and regulations allocate most expenses based on transfer pricing principles. The most common exceptions are research and experimentation expenses, interest expense, and taxes. Because, of these three items, only research and experimentation expenses are typically operating expenses, the APA Program likely can, in many of these cases, provide or recommend a TPM that derives operating profit both for transfer pricing and for Code and regulations purposes.

Another group of applications under the Rev. Proc. involves gross income earned by foreign corporations that manufacture goods outside the United States and sell them using an office or other fixed place of business in the United States. Regs. §1.863-3(b)(3) provides that under certain circumstances, a taxpayer

[59] Rev. Proc. 2008-31, 2008-1 C.B. 1133.

[60] Regs. §1.861-4(b).

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may elect to allocate income to manufacturing and sales, respectively, according to a ''books and records'' method,[61] which requires the taxpayer to maintain regular ''books of account'' that clearly reflect ''the amount of the taxpayer's income from production and sales activities.'' Historically, there was an issue as to how this regulation should be applied to situations where products manufactured abroad were sold in the United States through a U.S. sales office. Section 865(e)(2) provides (subject to certain exceptions) that ''income from any sale of personal property (including inventory property) attributable to such office or other fixed place of business shall be sourced in the United States.'' Under the ACCI's interpretation of this provision for the books and records method — a position that has engendered considerable internal debate over the years — only income from the sales function, and not income from the manufacturing function, is treated as U.S. source — i.e., the word ''attributable'' modifies the word ''income'' and not the word ''sale.'' Section 864(c)(5)(C) limits the income attributable to such office or other fixed place of business ''to the income . . . properly allocable thereto,'' which is interpreted as distinguishing manufacturing income, which will be foreign source, from sales income, which will be U.S. source. This requirement is understood to invoke transfer pricing principles, for items of gross income. In other words, a taxpayer choosing the books and records method may apply transfer pricing principles to determine U.S. source gross sales income. Expenses associated with the activities are then allocated based on the Code and regulation provisions that govern this situation.[62]

A final line of cases involves hybrid entities in old-treaty countries. In these cases, the United States sees a foreign PE, while the foreign tax authority sees a foreign corporation. In reverse hybrid cases, the reverse is true — the United States sees a U.S. corporation, while the foreign tax authority sees a U.S. PE. The question in both situations is whether Article 7 (PE attribution) or Article 9 (associated enterprises) of the applicable treaty applies. The general answer is that the United States will apply Article 9 (i.e., transfer pricing principles under §482), provided the foreign tax authority is also willing to apply Article 9 transfer pricing principles in both hybrid and reverse hybrid situations. In situations where the countries agree to apply Article 9, the APA Program has been advised by ACCI technical staff that treaty resourcing provisions do apply, even though, by their terms, such provisions arguably are limited to Article 7 cases.

By no means do the foregoing cases exhaust the kinds of old-treaty and Code and regulations cases that could fall within the Rev. Proc. Other possible cases include Subpart F determinations under §954(d)(2), which treats a low-taxed purchase and sales branch carrying on activities outside the country of incorporation of the enterprise of which the branch is part as a separate entity and thus requires an allocation of income and expenses to the branch. Because Regs. §1.954-3 provides little guidance on how the branch's taxable income is to be determined, it is possible that the ACCI and APA Program would apply transfer pricing principles. On the other hand, the APA Program declined at least one request to apply transfer pricing principles to the new ''substantial contribution'' test in the recently revised Subpart F manufacturing rules in Regs. §1.954-3(a)(4)(iv) on the ground that the issue, even if based in whole or part on economic principles, was too remotely related to the APA Program's bread-and-butter valuation expertise.

In sum, the application of economic principles to resolve an issue is a necessary, but not sufficient, condition to APA Program jurisdiction under the Rev. Proc. The consent of the ACCI has been critical, with such consent hinging on the language of the specific legal rule, historic interpretation and practice, competent authority relationships, and various other practical considerations. Taxpayers are well advised to seek an APA prefiling conference before they begin to apply transfer pricing principles to any issue potentially falling within the purview of the Rev. Proc.

CONCLUSION

The APA Program has had only limited experience to date applying the Rev. Proc. Cases arising under new treaties that apply transfer pricing principles to determine PE profits are relatively straightforward because the APA Program can develop a pricing method for both gross income and expenses that is based solely on transfer pricing principles. For outbound situations, the APA will not necessarily be determinative of the §904 foreign tax credit limitation calculation.

Global dealing APAs have benefited from the Rev. Proc., which clarifies that such APAs may cover commodities transactions and provide specific methods for allocating interest expense and return on capital. Both additions make global dealing APAs more comprehensive and more valuable to both the APA Program and taxpayers.

[61] The other two methods for sourcing such gross income are the 50/50 method, which splits gross income evenly between manufacturing and sales, and the independent factory price (IFP) method, which treats the portion of the gross income equal to the IFP as manufacturing gross income and the remainder as sales gross income. Regs. §1.863-3(b)(1), (2). Neither of these tests applies transfer pricing principles.

[62] Regs. §1.863-3(d).

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For PE situations involving non-treaty and old-treaty countries, the Rev. Proc. has revealed to APA Program staff some of the challenges of applying Code and regulations allocation and apportionment rules and transfer pricing rules side by side to the same transactions. The few Rev. Proc. cases involving these situations have provided some clarity on the circumstances in which the APA Program and the ACCI view the Code and regulations allocation and apportionment rules as incorporating transfer pricing principles. Given the novelty of these issues, the ACCI may need to consider issuing public guidance at some point.

Regardless, use of the Rev. Proc. should expand after the anticipated merger of the APA Program into the APMA Program. The U.S. competent authority staff has significant, longstanding experience applying allocation and apportionment rules to PE situations, which will help with the training of APA Program staff. In addition, U.S. treaty negotiators likely will continue to enter into and the U.S. Senate likely will continue to ratify new treaties that provide for the application of transfer pricing principles to determine PE profits. This bodes well for the use of the APA Program as a forum for cases involving the determination of PE profits.

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