

AN EVALUATION OF THE NEW ZEALAND
ADVANCE PRICING AGREEMENT PROCESS

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Abstract

Transfer pricing (the pricing of cross border transactions between controlled or related parties) is an important tax issue faced by multinational enterprises (MNEs). The Inland Revenue Department (IRD) initiated the Advance Pricing Agreement (APA) program in 1999/2000 as a more co-operative approach for MNEs to addressing transfer pricing compliance. An APA is an agreement negotiated in advance between a taxpayer and a tax authority that sets the price of cross border intra-firm transactions between related parties over a fixed period of time. This study evaluates the New Zealand APA process with a main focus of gaining an insight of how the program operates. Eight interviews comprising three participants from the IRD and five tax practitioners from the 'Big 4' accounting firms were conducted, in order to gain an insight into the New Zealand APA process. This was supplemented beforehand by documentary analysis of the New Zealand APA process and other sources of data. Further, the study reviews the APA processes of other tax jurisdictions, namely Australia, the United Kingdom, and the United States. A comparative case study analysis approach is utilised to see how these tax jurisdictions' APA processes compare to New Zealand's APA process.

The findings of this research reveal that New Zealand has maintained an informal APA process, where all MNE applicants are welcome to apply regardless of complexity, size or degree of risk involved in any of their transactions proposed to be covered under the APA. This was also seen as a key difference in the approach the IRD maintains towards APAs compared to the APA processes of other comparative tax jurisdictions' considered in this study. All interviewees perceived the New Zealand APA process well in terms of how it works and what it achieves. It was believed to be an attractive solution for all MNEs operating in New Zealand wanting to gain certainty around their transfer pricing tax affairs. An opportunity for New Zealand Customs to incorporate APAs as an acceptable valuation method for MNEs to price

their imports is also identified in this study. However, many obstacles are identified as to why this may prove to be a challenge for New Zealand Customs to implement.

All information mentioned in this thesis is up-to-date as at August 2016.

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Glossary of Acronyms

Acronym	Full Word
AMPA	Advance Pricing and Mutual Agreement
APA	Advance Pricing Agreement
ATO	Australian Tax Office
BEPS	Base Erosion and Profit Shifting
CUP	Comparable Uncontrolled Prices
DTAs	Double Tax Agreements
HMRC	Her Majesty's Revenue & Customs
INTM	International Manual
IRC	Internal Revenue Code
IRD	Inland Revenue Department
IRS	Internal Revenue Service
ITAA	Income Tax Assessment Act
MAP	Mutual Agreement Procedure
MNE	Multinational Enterprise
OECD	Organisation for Economic Co-operation and Development
PATA	Pacific Association of Tax Administrators
PFC	Pre-filing Conference
PSLA	Practice Statement Law Administration
SOX	Sarbanes-Oxley Act
SP	Statement of Practice
TAA	Tax Administration Act
TIOPA	Taxation (International and Other Provisions) Act
TNMM	Transactional Net Margin Method

Chapter 1: Introduction

1.1 Introduction

Transfer pricing remains a major concern for both the world's tax authorities and multinational enterprises (MNEs) and a source of continuous controversy between them. According to the Organisation for Economic Co-operation and Development (OECD), "around 60% of world trade actually takes place within multinational enterprises" (OECD, 2013). MNEs are subject to transfer pricing examinations and enquiries on a much broader scale nowadays (Ernst & Young, 2013). A 2013 global transfer pricing survey revealed that "risk management" is a top priority for 66 percent of respondents; a 32 percent increase over the prior surveys conducted in 2007 and 2010 (Ernst & Young, 2013).

Transfer pricing in its simplest terms can be thought of as the set prices of transactions between associated entities (Willendorf, 2010). Borkowski (1997b) provides an in depth explanation of 'transfer pricing'. Borkowski (1997b, p.322) explained that "transfer pricing is a strategy for pricing goods and intangible services transferred between parent and subsidiaries, or between subsidiaries, to maximize profits, minimize taxes, maintain goal congruence, and/or evaluate managerial performance". Thus it can be said that transfer pricing enables taxpayers to engage in transactions whereby profits from subsidiaries are shifted between tax jurisdictions to maximize global profits and/or minimise taxes.

Many tax jurisdictions have broadened the scope of what is deemed to be tax avoidance under their international tax regimes (Zhang, 2012). Supranational organisations, most prominently the OECD, have an increasing focus on work addressing transfer pricing. The OECD's current project on Base Erosion and Profit Shifting (BEPS) is the leading example of this increased

focus (OECD, 2016). The BEPS Action Plan details the OECD's areas of focus.¹ Three of the fifteen action areas directly apply to transfer pricing, namely, intangibles, risk and overcapitalization (OECD, 2016).

It is evident that MNEs are constantly seeking to achieve certainty in an uncertain global transfer pricing environment (Avoseh, 2014). Advance Pricing Agreements (APAs) have become a prominent management controversy tool to achieve certainty in the transfer pricing arena of many jurisdictions (Ernst & Young, 2010; Ernst & Young, 2013; Markham, 2012). This includes the USA, UK and Australia, all being members of the OECD which have highly developed APA programs. New Zealand has a relatively mature APA program in place, which has seen rising participation rates from MNEs in the past few years (Inland Revenue, 2015a). However, New Zealand's Inland Revenue Department (IRD) has "not established any formal processes for obtaining an APA" (Inland Revenue, 2015a).

Evaluating the New Zealand APA program and the processes involved in obtaining an APA will hopefully shed light in the future on how various parties involved can interact to better develop the overall program to serve as an efficient and effective controversy risk management tool for transfer pricing in the future. Looking at the potential advantages and disadvantages of pursuing an APA, as well as critically evaluating certain aspects of the process itself, will be part of the evaluation. In analysing the process, it is important to take into account the views of the revenue authority offering the program – the IRD – and the views of transfer pricing practitioners who deal with the realities of transfer pricing as part of their clients' daily cross-border operations. The practicalities of how APAs work can be reflected through both parties' points-of-view.

¹ Refer to <http://www.oecd.org/tax/beps/beps-actions.htm> for detail on the OECD's BEPS Action Plan.

1.2 The Need for Certainty in Today's Global Transfer Pricing Environment

Transfer pricing is not a matter that a tax authority or MNE can choose to opt out of in today's global economic environment. Transfer pricing was predominantly employed as a profiting mechanism by which MNEs would shift their profits cross-border in order to obtain a tax benefit. Tax authorities have become increasingly rigorous in terms of assessing each MNEs tax liability to make sure each authority obtains its fair share of tax.

Authorities view transfer pricing as a "soft target" whereby MNEs can increase their "tax revenues" (PwC, 2011). An International Transfer Pricing report mentions that there is no "absolute rule" for determining the right transfer price on a cross border transaction (PwC, 2015). Whether the transaction that is being priced involves tangibles, intangibles, specialised services, financing or cost allocation/sharing arrangements, disagreement between parties involved as to how the transaction is priced is never far away (PwC, 2015).

Most of the jurisdictions in the developed world have detailed transfer pricing documentation requirements in place (Markham, 2012). However, even those nations without detailed requirements expect taxpayers to provide some form of support to justify the transfer pricing position they have adopted (PwC, 2016).

As a result of the enactment of the Sarbanes-Oxley Act (SOX) in 2002 in the United States which came about from the various accounting scandals committed by corporates such as Enron and WorldCom, MNEs have been compelled to be increasingly transparent in relation to the tax and transfer pricing positions adopted in their financial reporting. According to Markham (2012), many governments around the world have reformed their accounting standards in line with SOX. As a transfer pricing report summarises, the impact of SOX requires the "aligning [of] a company's business, accounting, IT, legal, and tax functions to implement and monitor transfer pricing policies and procedures more effectively" (PwC, 2011,

p.20). Further, the 2008 financial crises has been a major source of uncertainty on an international scale for MNEs, with many still ‘sobering up’ from its effects up until today (Markham, 2012).

The OECD Transfer Pricing Guidelines give a particular focus on the arm’s length principle and wheatear MNEs’ cross border transactions are in line with consistent with the principle (OCED, 2010). The arm’s length principle is defined as a condition where all parties to a transaction are independent (OECD, 2010). The OECD Guidelines contain rules and methods which are intended to create a uniform application of the arm’s length principle across the globe. The methodologies used to interpret the arm’s length principle, and how it is to be applied in practice to reach a transfer pricing agreement between a MNE and a tax authority, differ from one jurisdiction to another. MNEs continue to find it difficult to operate in an unstable and uncertain environment of transfer pricing, and thus are looking for ways to achieve increased certainty and less risk (Ernst & Young, 2013). APAs may prove to be an effective controversy management tool by which MNEs are able to secure a safer transfer pricing position.

1.3 Advance Pricing Agreements

A marked increase in the worldwide use of APAs as a controversy risk management tool by MNEs is notable in the twenty first century (Vögele & Brem, 2003). A 2013 Global Transfer Pricing Survey, involving 878 interviews with tax directors and senior tax professionals in parent companies (global headquarters) across 26 countries, reported that 26% of parent companies surveyed are using the APA process in 2012, up from 21% in 2007 (Ernst & Young, 2013). The same survey reports that 30% of New Zealand parent companies have used APAs as a controversy management tool, compared to 26% globally. The global increase in the use

of APAs has been described as a governance change from ‘bureaucracy’ to ‘cooperation’ (Vögele & Brem, 2003a).

The OECD defines an APA “as 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” (OECD, 2010, p.336). APAs may be issued in a unilateral form which involves one tax administration and a taxpayer. Bilateral and multilateral APAs involve two or more tax administrations (Vögele & Brem, 2003). The OECD mentions that this presents a divergence from ‘traditional audit techniques’, which seek to affirm whether tax positions already taken comply with the arm’s length transaction (OECD, 2010).

Markham (2006) observes that transfer pricing audit activity is on the rise globally. Two thirds of respondents (855 respondents) in a global transfer pricing survey in 2010 reported that they had experienced a transfer pricing audit, compared with only 52% in 2007 (Ernst & Young, 2010). Judicial mechanisms such as litigation are also not favoured by MNEs and revenue authorities as a method of disputes (Markham, 2012). Litigating transfer pricing disputes is costly and time consuming. One of the advantages of obtaining APAs listed by the OECD is that they “may prevent costly and time-consuming examinations and litigation of major transfer pricing issues for taxpayers and tax administrations”.²

The New Zealand IRD claim that APAs present a more co-operative approach for MNEs to address transfer pricing compliance. As mentioned previously, the New Zealand revenue authority has not established any formal processes for MNE applicants wanting to obtain an APA.

² OECD Transfer Pricing Guidelines, paragraph 4.144.

1.4 Research Aims and Objectives

This study aimed to provide an evaluation of the New Zealand APA process. As it is exploratory in nature, several other aims also exist, with several other areas investigated within the process itself. These included New Zealand tax practitioners' experience with the APA program, and recommendations by both the IRD and transfer pricing tax practitioners on how certain aspects of the New Zealand APA process can be improved. The research statement explored in this research is presented as "An evaluation of the New Zealand Advance Pricing Agreement Process." The word 'process' has been used by the researcher instead of 'program' as it is a broader concept covering more aspects rather than simply the APA process itself.

The New Zealand APA process was undertaken with the following objectives. These are:

- Outline how a New Zealand APA can be obtained and the steps involved in obtaining one;
- Obtain various key parties' critical evaluations of the New Zealand APA process;
- Define and evaluate the New Zealand tax authority – tax practitioner relationship under the APA process; and
- Examine how the New Zealand APA process compares to those of overseas' APA processes; namely those of Australia, the United States (US), and the United Kingdom (UK) and what lessons, if any, could be learned from these countries.

1.5 Contribution to Knowledge

It is intended that this research will enable for a better overall understanding of the New Zealand APA process. To the researcher's knowledge, there is no existing academic study on the topic of New Zealand APAs, which also forms part of a motivation for the researcher to undertake this research. Further, there is a lack of governmental or professional reports on the

topic as well. It is hoped that this research will form the foundation for further academic study on APAs in a New Zealand context and that further evaluations will be undertaken of the New Advance Pricing Agreement process.

As mentioned above, the evaluation of the New Zealand APA process will be compared to those of other jurisdictions and may also provide useful insights to these jurisdictions on certain aspects of their APA processes in place. Lessons can be learnt from the New Zealand APA process experience. Also, other jurisdictions with a ‘young and developing’ process or that are considering adopting a similar tax product – APAs – can benefit from this study as well. The overall relationship of the parties involved in the APA process can be enhanced by using the findings of this research. Some of the critical aspects of the New Zealand APA process this research wanted to focus on are, the advantages and disadvantages of obtaining an NZ APA, and the practicality and potential benefits of New Zealand Customs using APAs as part of their valuation practice.

1.6 Structure of Thesis

The remainder of this thesis is arranged as follows: Chapter 2: Literature Review, starts with a brief review of the prior research surrounding transfer pricing and APAs. Next, Chapter 2 reviews the APA processes of New Zealand and those of three overseas’ tax jurisdictions, namely, Australia, the UK and the US. This review will shed some light on how each country’s APA process operates. The main purpose of Chapter 2 is to be able to identify the gap in literature on the New Zealand APA process.

Chapter 3: Research Questions, Methods and Methodology, outlines the research questions, research methods and research approach undertaken in this study. This chapter will introduce the qualitative methodology used in this thesis. The research methods for undertaking this research include a comparative case study analysis, documentary analysis and several semi-

structured interviews. The main theoretical framework used in this study is institutional theory. The theoretical framework will assist the researcher in evaluating the New Zealand APA process.

Chapter 4: Research Findings and Discussion, contains the researcher's findings and discussion on the topic. The chapter follows this structure:

- A critical evaluation of the New Zealand APA process following a thematic order deemed logical by the researcher;
- Presenting the steps involved in obtaining a New Zealand APA; and
- A brief comparative analysis of selected APA processes, including the New Zealand one.

The above structure aims to answer the research questions presented in this thesis:

RQ1: What are the steps involved in obtaining a NZ APA?

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

RQ3: How does the NZ APA process compare to selected overseas' APA processes?

Chapter 5: Conclusions, Limitations and Future Research, provides the conclusions, key limitations and areas of future research. The conclusions of the research presented and discussed under Chapter 4, Research Findings and Discussion, are outlined under this chapter. Key limitations of this study, which also inform future research areas are outlined.

Chapter 2: Literature Review

2.1 Introduction

Establishing acceptable transfer prices is possibly the accounting topic that most consumes the time and energy of multinational enterprises (McAulay & Tomkins, 1992). Avoseh (2014) states that this may be due to the fact that transfer pricing is ‘grappled’ with many other topics and disciplines, the most common which are economics, accounting, international business, law, and public policy. As noted in Chapter 1: Introduction, section 1.1 “around 60% of world trade actually takes place within multinational enterprises” (OECD, 2013). By that, the topic of transfer pricing has clearly become important in present day international accounting and tax matters. Several studies have already shown this, for example, in a comparative study carried out by Sand and Pragasam (1997), the researchers found that transfer pricing was perceived as one of the most important topics in international accounting. Surveys such as Ernst & Young’s ‘Global Transfer Pricing Surveys’ (1995-2010) are another example of how important transfer pricing is globally.

This chapter is set out in two main parts. The first part covers a generic review of transfer pricing literature. In addition, literature on Advance Pricing Agreements (APAs) and the Organisation for Economic Co-operation and Development (OECD) are considered in the first part of this chapter as well. This will assist in justifying the under researched area of APAs. Due to the scope of this thesis, this will only present a minor part of the literature review and will not be discussed in detail. Instead, any relevant literature will be addressed directly in Chapter 4 and Chapter 5 of this thesis. The second part covers a review of the existing literature surrounding the APA processes of each of New Zealand, Australia, the United Kingdom (UK), and the United States (US). The main purpose of this review is to answer the third research question, *RQ3*, of this thesis:

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

This part of this chapter considers empirical studies on the specific area of APAs for each of the comparative tax jurisdictions considered in this thesis. More information as to why these tax jurisdictions were chosen as part of the comparative study is explained in Chapter 3 of this thesis (refer section 3.5.1 'Case Study'). Existing literature on the New Zealand APA process is reviewed first in the hope of identifying the gap in literature on the topic – the New Zealand APA process – and clarifying the need to examine the research questions proposed in this thesis.

Information about the APA processes' of the tax jurisdictions considered in this study (Australia, the UK, and the US) were directly sourced from each of their respective revenue authorities (Australian Tax Office (ATO), Her Majesty's Revenue & Customs (HMRC), and the Internal Revenue Service (IRS)) that manage each of the tax jurisdictions' APA process(es). This will be expanded on in Chapter 3 of this thesis (refer section 3.5.2 'Documentary Analysis'). In relation to academic literature, this study heavily relies on the works of Markham (2012) and Avoseh (2014). These two pieces of academic literature combined provide a comprehensive evaluation of the three comparative tax jurisdictions' APA processes considered in this study. Further, to the author's knowledge, no other recent academic studies exist out there that provide such a comprehensive review of a tax jurisdiction's APA process.³ Other documents published by professional service firms are considered as well (for example, Ernst & Young's Global Transfer Pricing Surveys 1995-2013). These are considered throughout this thesis.

The next two sections, section 2.2 and section 2.3 set out an overview of the literature on transfer pricing and APAs. Section 2.4 follows with a brief overview of the OECD. Section 2.5

³ At least for those APA processes considered in this study.

reviews the existing literature surrounding the APA processes of each of New Zealand, Australia, the United Kingdom (UK), and the United States (US).

2.2 Overview of Transfer Pricing Literature

Hirshleifer (1964) identifies two main shortcomings of both empirical and theoretical transfer pricing studies. The first being that literature does not recognise that transfer pricing is the by-product of an organization decentralizing their operations. The second being that transfer pricing is a multi-disciplinary exercise. On the second shortcoming identified by Hirshleifer (1964), Mehafdi (1990) further argues that transfer pricing does require explanations from various disciplines such as marketing, management accounting and economics in order to formulate a combined accounting solution. A wide variety of transfer pricing studies have emerged as a result of the multidisciplinary nature of transfer pricing (Mehafdi, 1990).

The study of Hirshleifer (1956) has been the foundation for many transfer pricing studies examining transfer pricing from an economics point of view (Solomons; 1965; Kanodia, 1979). His study observed the exchange of goods and services between autonomous 'profit centres' within a firm and to observe how the prices set between these divisions contribute to the overall profitability of the firm. Hirshleifer (1956) suggested that the behaviour of the division managers were influenced to supply information that is not truthful or relevant when the prices of the goods and services provided are specified. This model holds only when in a perfectly competitive market. Otherwise, prices would fall along the marginal cost for transfers within the same firm (Hirshleifer, 1956).

Another interesting study on transfer pricing is that of Cravens (1997) where she examined the survey responses of US-based multinational enterprises (MNEs) describing their overall strategic objectives of international transfer pricing. Three areas were identified in relation to the strategic objectives of international transfer pricing: (1) taxation-related objectives; (2)

internal management-oriented objectives; and (3) international or operational objectives (Cravens, 1997). The main takeaway from Cravens (1997) study is that transfer pricing is beyond the idea of complying with the tax law burdens faced by MNEs. It was found that transfer pricing can be used to influence the behaviour and performance of organizations and contribute towards their corporate objectives.

The studies of Ciric and Gracanin (2010) and Klassen, Lisowsky and Mescall (2013) also sought to examine the motives behind the use transfer pricing by an organization. Ciric & Gracanin (2010) concluded that transfer pricing is an important tool used to reduce costs and better allocate limited resources throughout an organization. Further, transfer pricing can drive competition in an organization. Thus, the transfer pricing method used is really important and is given much consideration by managers. On the other hand, Klassen et al. (2013) investigated the use of transfer pricing as a tax minimization tool by MNEs. Through a multivariate analysis, their study showed that transfer pricing is a material tool used for the purpose of minimizing tax among many MNEs. Many MNEs measure the success of their transfer pricing function based on tax minimization (Klassen et al., 2013).

2.3 Overview of APA Literature

The studies of Borkowski (1993; 1996b) examined MNEs' view around the use of APAs. Her first study explored why US based MNEs' would not pursue an APA as an alternative method of resolving transfer pricing disputes with the IRS (Borkowski, 1993).⁴ Three main deterrents were identified as to why MNEs would not consider APAs as an alternative option: (1) the "volume of information and documentation" required to obtain an APA; (2) the "costs of obtaining" an APA; and (3) the risk of an APA triggering an audit of prior years (Borkowski,

⁴ 340 US based MNEs were sampled from the Fortune 500. The response rate was 43% (146 MNEs) with an end result of 140 useable surveys.

1993, p.7). Borkowski (1993) found that only very few MNEs considered the APA option (5.9%) compared to a much larger number preferring litigation to resolve transfer pricing disputes (30%).

Borkowski's (1996b) study extends on her 1993 study by way of examining MNEs' view on APAs from both host countries (inside and outside the US).⁵ Her study found MNEs that had or planned to have APAs with the US or the other country only ranged from 5% to 29%. Deterrents similar to those found in her 1993 study were attributed to why MNEs would not pursue an alternative APA. The most important deterrent ranked by MNEs in Borkowski's (1996b) study was the cost of the APA.

A study conducted by Elliott and Emmanuel (2000), which mainly looked at transfer pricing from a management accounting point of view, attempted to examine 12 MNEs perception about APAs. The tax managers of the MNEs were interviewed face to face. Divergent views were expressed by the participants about APAs. It was found that the divergence of views was mainly due to each tax manager's experience with the APA process.

2.4 Organisation for Economic Co-operation and Development (OECD)

The OECD is a supranational organisation consisting of 34 member countries of which the G20 are all members of.⁶ All of these member countries have come together in a collaborative matter in an effort to effectively enforce their transfer pricing laws. In an attempt to bring all tax authorities and MNEs globally at a fair playing field, the OECD have issued a set of transfer pricing guidelines. The 2010 "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" (referred to as the 2010 OECD Guidelines) are the most recent transfer

⁵ Borkowski's survey sample was made up of 1,363 MNEs based in Canada, Germany, Japan and the UK, all with US subsidiaries. The survey sample also included US based MNEs with subsidiaries based in the countries considered in the study.

⁶ Refer to the OECD's 'Members and partners' webpage for an overview of the OECD:
<http://www.oecd.org/about/membersandpartners/>

pricing guidelines issued by the OECD.⁷ The guidelines provide both tax administrations and MNEs guidance on how the ‘arm’s length principle’ should be applied. Paragraph 1 of Article 9 of the OECD Model Tax Convention⁸ contains the authoritative statement of the arm’s length principle:

“[Where] conditions are made or imposed between the two [associated] enterprises in their commercial or financial relations which differ from those which would, but for those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly” (p.5 Chapter 1 OECD 2010 Guidelines).

The OECD define the ‘arm’s length principle’ as a valuation principle where transactions should be valued as if they had occurred between unrelated parties, “each acting in his own best interest (OECD, 2010).

Avoseh (2014) mentions that the 2010 OECD Guidelines are generally considered to act as a political mediator among the transfer pricing regimes of the OECD members. However the efforts of the OECD in relation to the ALP are respected by both OECD and many of the non-OECD members, especially in regards to the definition and interpretation of the principle under the OECD Guidelines. Avoseh (2014) further mentions that the issue of ‘comparability’ is at the heart of the arm’s length. In order to make accurate adjustments on a transaction to satisfy the arm’s length principle, judgement needs to be exercised to determine the comparability of that certain transaction (Adams and Coombs, 2003).

⁷ Refer to the OECD’s website for more information on the history of development of the OECD’s Transfer Pricing Guidelines.

⁸ ... which forms the basis of bilateral tax treaties involving OECD member countries and an increasing number of non-member countries: (p.5 Chapter 1).

The 2010 OECD Guidelines explain five factors in order to determine ‘comparability’. These factors are: Characteristics of the property and services; functional analysis; contractual terms; economic circumstances; and business strategies. Functional analysis is looked at in detail below as per the 2010 OECD Transfer Pricing Guidelines:

Functional analysis: this analysis mainly seeks to identify and compare the extent to which each associated or independent entity undertakes economically significant activities and responsibilities on its behalf.

Some useful indications outlined by the OECD Guidelines include paying close attention to and examining the MNEs organisational structure. Compensation can also be a useful indicator that reflects the extent of functions performed by each party. “Design manufacturing, assembling, research and development, servicing, purchasing, distribution, marketing, advertising, transportation, financing, and management” are some functions taxpayers and tax authorities should consider when undertaking a functional analysis. The OECD Guidelines stipulate that, regardless of whether one party provides a large number of functions, the economic significance of each function is what matters.⁹ Another factor to consider is the allocation of risks (for example, exchange rate risks) between parties involved. Also the risk allocation needs to be in line with the economic substance of the transaction.¹⁰ Overall, in the absence of robust functional analysis procedures, tax administrations may suffer revenue losses

⁹ “For example, when a distributor takes on responsibility for marketing and advertising by risking its own resources in these activities, it would be entitled to a commensurately higher anticipated return from the activity and the conditions of the transaction would be different from when the distributor acts merely as an agent, being reimbursed for its costs and receiving the income appropriate to that activity. Similarly, a contract manufacturer or a contract research provider that takes on no meaningful risk would be entitled to only a limited return” (OECD Chapter I: The Arm’s Length Principle p. 34).

¹⁰ “If, for example, a manufacturer sells property to a related distributor in another country and the distributor is claimed to assume all exchange rate risks, but the transfer price appears in fact to be adjusted so as to insulate the distributor from the effects of exchange rate movements, then the tax administrations may wish to challenge the purported allocation of exchange rate risk” (OECD Chapter I: The Arm’s Length Principle p. 34).

where sizable profits and losses can be allocated in the most advantageous place to the group of associated parties involved (OECD, 2010).

The international tax landscape is changing rapidly due to governments' efforts to better administer their local systems and tackle the perceived tax avoidance undertaken by MNEs by way of shifting their profits globally. In an attempt to address existing flaws in the international tax rules, the OECD published its BEPS project in July 2013 which consists of 15 action plans. As mentioned previously in Chapter 1, section 1.1, three of the fifteen action areas directly apply to transfer pricing, namely, intangibles, risk and overcapitalization (OECD, 2016).

2.5 Review of Tax Jurisdictions' APA Processes

2.5.1 New Zealand

2.5.1.1 Introduction

MNEs continue to be a significant force in driving New Zealand economic activity (Edwards and Nash, 2009). Many of these MNEs are involved in associated party transactions, which need to be transfer priced for taxation purposes. The New Zealand tax authority – Inland Revenue Department (IRD) – has identified transfer pricing as a current focus area in 2015 and 2016 (Inland Revenue, 2015c). The IRD has been among those who have been responding the global political pressure concerning BEPS. According to a transfer guide published by PwC, IRD has been responding to global political pressure concerning the OECD's BEPS Action Plan (PwC, 2016). New Zealand's Minister of Finance welcomed the OECD's full release of the BEPS Action Plan stating that "New Zealand is becoming more and more attractive as a place to do business and invest in, so it is critical the we [New Zealand] continue to strengthen our tax rules to ensure overseas companies pay their fair share" (Inland Revenue, 2015g).

Section 2.5.1.2 provides an overview of New Zealand transfer pricing landscape. Subsequently, the New Zealand APA process is reviewed under section 2.5.1.3.

2.5.1.2 Transfer Pricing Landscape in New Zealand

Transfer pricing legislation was first introduced in New Zealand on 12 December 1995.¹¹ The transfer pricing guidelines were issued in their final form by IRD in October 2000 (Inland Revenue, 2015d). The IRD have no further intentions to update the issued guidelines (Inland Revenue, 2015d).¹² The latest 2010 OECD Guidelines are being applied instead (Inland Revenue, 2015d). The IRD claim that the 2010 OECD Transfer Pricing Guidelines are consistent with New Zealand's current transfer pricing legislation and double taxation treaties in place (Inland Revenue, 2015d). The IRD has a Transfer Pricing enforcement program in place with an overall goal to maintain New Zealand's fair share of multinational tax (Inland Revenue, 2009). The program takes into account compliance costs borne by MNEs to comply with transfer pricing rules by placing the burden of proof on the Commissioner to demonstrate a more reliable arm's length amount, provided the MNE demonstrates a reasonable level of cooperation with the IRD. The IRD states that the lack of any specific rules in relation to maintaining transfer pricing documentation means that the costs of compliance with New Zealand's transfer pricing rules are not as onerous as they are in other jurisdictions (Inland Revenue, 2009).

Transfer pricing questionnaires are central to IRD's monitoring of compliance with transfer pricing rules (PwC, 2016; Edwards and Nash, 2009). There are three questionnaires in place: one for New Zealand owned multinationals, one for New Zealand branches and one for foreign

¹¹ Transfer Pricing legislation had not come into effect until the income year ending 31 March 1997.

¹² There has been two minor revisions to IRD's administrative practice for services where the threshold has been lifted from \$100,000 to \$600,000 and more recently to \$1,000,000.

owned-multinationals (Inland Revenue, 2008b; Inland Revenue, 2008c; Inland Revenue, 2008a). The three questionnaires are similar in the main questions they ask. “The questionnaire requires taxpayers to provide details of, among other things: their financial performance; the worldwide group’s financial performance; the type and amounts of cross-border, associated-party transactions; the method or methods used to test the transactions; and whether documentation exists to substantiate the transfer prices” (PwC, 2016, p.768). The one designed for foreign owned multinationals, further assesses the MNE’s compliance with thin capitalisation rules. These questionnaires remain to serve as a main tool to the IRD’s effective and efficient scoping of risks (Edwards & Nash, 2009).

There are no specific statutory requirements in New Zealand for MNEs to maintain transfer pricing documentation (Inland Revenue, 2012). However, such documentation is considered centric in justifying the transfer prices the MNE has applied in relation to its cross-border transactions (Inland Revenue, 2015b). In relation to transfer pricing documentation, sections GC6 to GC14 of the Income Tax Act (ITA) 2007 require taxpayers to determine the transfer prices on their cross-border transactions in accordance with the arm’s length principle. Section GC13(1) states that:

*“An arm’s length amount of consideration must be determined by applying whichever 1 or a combination of the methods listed in subsection (2) produces the most reliable measure of the amount that completely independent parties would have agreed upon after real and fully adequate bargaining”.*¹³

As mentioned previously, the burden of proof in demonstrating a more reliable arm’s length transfer price falls on the Commissioner; this burden of proof is contained under section

¹³ Methods listed under Section GC13(2) Income Tax Act are (a) the comparable uncontrolled price method; (b) the resale price method; (c) the cost plus method; (d) the profit split method; (e) the comparable profits methods.

GC13(4) of the ITA 2007. To show compliance with the above legislative requirements, the IRD considers adequate transfer pricing documentation necessary for a MNE to explain and justify its transfer pricing methodologies used to derive its transfer prices. The IRD explains that lack or non-existence of adequate documentation may have implications on the taxable positions taken by MNEs (Inland Revenue, 2012). The IRD will more likely audit a MNE's transfer pricing matters in detail if there is a lack of adequate transfer pricing documentation. Secondly, in the case of the IRD proposing an alternative arm's length transfer price on a cross-border transaction, it will be difficult for the MNE to rebut the adjustment being proposed by the IRD, and is likely to result in significant levels of interest and penalties payable in addition to the adjustment(s) being made. The IRD constantly emphasises the importance of adequate transfer pricing documentation and that it is the company's local management responsibility to ensure it is in place (Inland Revenue, 2015c).

“If we [the IRD] make transfer pricing adjustments, the quality of supporting documentation will be a key factor in determining the extent to which penalties might apply. A failure to prepare adequate transfer pricing documentation or acceptance of pricing that is clearly inappropriate could result in a 40% shortfall penalty for gross carelessness if apparent problems involving material associated party transaction are simply brushed over lightly or even ignored” (Inland Revenue, 2012).

The IRD provides a view on what it believes is adequate transfer pricing documentation. The first matter is the extent of maintaining detailed documentation and how feasible it is from a cost-benefit point of view (PwC, 2016). For MNEs with small cross-border transactions, a transfer pricing questionnaire may suffice. A reasonable explanation as to how the cost-benefit analysis conclusion is reached would be expected. An international transfer pricing guide suggests all the following documentation at a minimum:

- “An identification of the cross-border transactions for which the taxpayer has a T[ransfer] P[ricing] exposure.
- A broad functional analysis of the taxpayer’s operations to identify the critical functions being performed.
- An estimate of the business risk of not undertaking and documenting a more detailed T[ransfer] P[ricing] analysis.
- An estimate of the costs of complying with the T[ransfer] P[ricing] rules” (PwC, 2016, p. 768).

Where a cost-benefit analysis shows that full analysis is needed for a MNE’s transfer pricing matters, the IRD would expect more detailed documentation. Functional analysis is considered to be heart of the documentation in explaining and justifying how the arm’s length principle has been applied (Inland Revenue, 2015b). The 2010 OECD Transfer Pricing Guidelines provide guidance on what is to be included under a functional analysis (discussed previously under section 2.4). Other matters MNEs should be aware of are that relying on earlier documentation is not acceptable (Inland Revenue, 2012). “Transfer pricing is an ongoing process not a one time documentation exercise. The [taxpayer needs] to ensure associated party transactions are identified and accurate disclosures are made (including notes to the annual financial statements)” (Inland Revenue, 2012). Also a MNE should be wary of using transfer pricing documentation that has been prepared by its parent company.¹⁴ The parent company may not always be reflective of its overseas’ related parties, which may in turn result in the transfer pricing documentation not reflecting an appropriate arm’s length price (Inland Revenue, 2012).

¹⁴ For more details on what best practice guidelines the IRD provides in relation to transfer pricing documentation refer to the IRD’s Transfer Pricing Documentation online webpage <http://www.ird.govt.nz/transfer-pricing/practice/transfer-pricing-practice-documentation.html>.

New Zealand's transfer pricing environment is managed by a small team of transfer pricing specialists – the Specialist Advice Unit. The team consists of an International Revenue Strategy Manager, Investigations and Advice Manager, four Principal Advisors and an Economist (Inland Revenue, 2015h). This small team of highly experienced personnel provide a stream of 'principled, practical, coordinated and consistent solutions to problems arising' (Inland Revenue, 2015h). Their main functions include:

- Maintaining a multinational enterprise database
- Monitoring taxpayers;
- identifying and scoping risks;
- advising and assisting Inland Revenue Assurance staff;
- industry analyses and special projects;
- training;
- advance pricing agreements;
- mutual agreement cases; and
- exchange of information from and to treaty partners (Inland Revenue, 2015h).

It is worth noting that other IRD tax inspectors and investigators are capable of handling transfer pricing issues, and usually perform them alongside with the assistance of the small team of specialists (PwC, 2016).

The IRD will perform transfer pricing tax audits or investigations where necessary. Commencing to investigate a MNE's transfer pricing practices depends on a wide range of factors where one or more of these factors may trigger an audit.

There have been no specific court cases in relation to New Zealand's transfer pricing legislation. One main reasons attributed to this is that most transfer pricing disputes were

resolved by way of negotiation, thus no need to proceed to court (PwC, 2016). The most significant case on transfer pricing was the Court of Appeal decision in the case of *CIR v Squibb*.¹⁵ The case concerned a taxpayer challenging the Inland Revenue's use of secret comparables in deriving its tax assessments. It was held that the revenue authority has the right to access all information, including secret comparables, in order to exercise its statutory duty to collect the correct amount of tax (Quantera, 2015).

Double taxation issues may arise where adjustments are made by either the IRD or an overseas tax authority. A provision called the Mutual Agreement Procedure (MAP) is contained under the Double Tax Agreements (DTAs) New Zealand has concluded with overseas tax jurisdictions. MAP, also referred to as a request for Competent Authority assistance, allows taxpayers to present their cases to the tax administration, called the 'Competent Authority' (Inland Revenue, 2015f). Most double taxation issues and requests for Competent Authority assistance involve transfer pricing issues. The IRD may provide assistance by way of executing a downwards adjustment if it agrees with the overseas adjustment made, or communicate with the treaty partner and persuade it to 'reduce or withdraw' their adjustment (Inland Revenue, 2015f). The IRD claims that resolution of double taxation is successful in most cases.

2.5.1.3 New Zealand APA Process

New Zealand taxpayers can apply for a binding ruling with the IRD, which assists taxpayers to meet their obligations under the law. A binding ruling is the IRD's interpretation as to how a certain tax law applies (Inland Revenue, 2013a). There are four types of binding rulings, with private rulings being the most relevant to transfer pricing.¹⁶ A private ruling is a confidential

¹⁵ *CIR v E R Squibb & Sons (NZ) Limited* (1992) 14 NZTC 9,146.

¹⁶ The other three types of binding rulings are public rulings, product rulings and status rulings. Refer to IRD's IR715 Binding Rulings document for more information on these types of rulings.

ruling, which provides a taxpayer or group of taxpayers with an interpretation of how the law applies to a particular arrangement (Inland Revenue, 2013c).

New Zealand taxpayers may address transfer pricing compliance by way of entering into an APA with the IRD. One hundred and twenty nine APAs have been concluded as at 30 June 2015, up from 45 APAs completed in 2009 (Inland Revenue, 2015a; Edwards & Nash, 2009). New Zealand's domestic legislation allows unilateral APAs to be issued in the form of binding rulings. Bilateral/multilateral APAs may be entered into pursuant to the DTA applicable. IRD defines a unilateral APA as a "ruling binding on the Commissioner of Inland Revenue on an appropriate transfer pricing methodology to be applied to the taxpayer's specified international related-party transactions over a fixed period" (Inland Revenue, 2012). The IRD states that in both inbound and outbound transfer pricing scenarios, unilateral APAs have proven to be successful (Inland Revenue, 2015a).

The majority of bilateral APAs have been concluded with Australia (Inland Revenue, 2015a). Other APAs have been concluded with Belgium, Canada, Japan, Korea, Switzerland and the United States (Inland Revenue, 2015a). APAs represent a more co-operative approach as to how MNEs can manage their transfer pricing affairs (Inland Revenue, 2015a). A considerable amount of time and costs are saved when entering an APA by both IRD and a MNE, especially when compared to adversarial transfer pricing audits (Inland Revenue, 2015a). The IRD's Specialist Advice Unit are responsible for considering and issuing APAs (Inland Revenue, 2015h). A minimal application fee applies to a unilateral APA, while the IRD usually does not charge for entering into bilateral/multilateral APAs.¹⁷ The following forms need to be completed as part of an APA application: *Application for private ruling* (IR713) as well as the

¹⁷ The minimal application fee for a unilateral APA is a legislative requirement as it is a private ruling. IRD will seek to recover "out of pocket" travel costs in the completion of any of the APAs.

Application for private ruling on transfer pricing arrangement – additional declaration (IR713A). The IR713 and IR713A application forms are set out in Appendices 1 and 2.

The IRD has not established a formal process to obtain an APA. The IRD considers that each taxpayer's case will be different, thus a less formal process better addresses the different facts and circumstances (Inland Revenue, 2015a). The IRD aims to complete unilateral APAs and bilateral APAs with Australia within six months of when the APA application is accepted (Inland Revenue, 2015a). Negotiating an APA with other jurisdictions other than Australia generally take considerably longer to conclude (Inland Revenue, 2015a). The informal process usually involves the following steps for potential applicants:

- A written proposal is submitted by the applicant briefly outlining the entity's business activities, associated party transactions involved and what methodologies are to be applied to price these transactions.
- A pre-application meeting follows with a Principal Advisor to informally discuss the submitted proposal.
- The APA application is then formalised and submitted for consideration. The application will include transfer pricing documentation, full functional analysis, methodologies and comparables used, and other matters discussed in the pre-application meeting.
- The IRD may request site visits to examine the actual operation, especially where valuable intangibles are involved.
- A review of comparables will be performed by the IRD to assess the appropriateness of the ones proposed.
- Once the review is completed, the IRD will sit down with the taxpayer (unilateral situation) or with the officers of the other jurisdiction (bilateral situation) to discuss any

differences of opinion. Once agreement is reached, an APA is concluded (Inland Revenue, 2015a)

As mentioned previously, an APA application must consist of an IR713 Form and an additional declaration Form (IR713A). The additional declaration is part of a legislative requirement under section 91ED(1B) of the Tax Administration Act 1994 (TAA 1994), which is specific to transfer pricing. Section 91ED(1B) of the TAA 1994 states that:

“In the case of an application for a private ruling that relates to how either sections GC 6 to GC 14 or YD 5 of the ITA 2007 applies, or would apply, the applicant must state in a notice, signed by them and sent to the Commissioner at the same time as the application described in subsection (1), that—

(a) they have examined the application; and

(b) to the best of their knowledge and belief, the information disclosed for the application is comprehensive”.

This legislative requirement simply requires applicants to be more involved in the process of obtaining an APA in comparison with other private ruling applications (Inland Revenue, 2012a). The additional declaration ensures that the person concluding the APA on behalf of the business and holds sufficient knowledge of the applicant’s cross border transactions and transfer pricing affairs, is able to declare to the IRD that the information provided is full and complete.

It is worth noting that the IRD’s online public database on transfer pricing practice issues, the revenue authority consistently turns taxpayers’ minds towards considering APAs by asking if ‘due consideration’ to an APA has been given, and if not, why not. Also all three of the transfer pricing questionnaires ask the question, “Are you giving consideration to applying for an

advance pricing agreement in New Zealand?” (Inland Revenue 2008b; Inland Revenue 2008c; Inland Revenue 2008a).

The above sections set out an overview of the New Zealand transfer pricing environment and the New Zealand APA process. Section 2.5.2 reviews Australia’s transfer pricing environment and the jurisdiction’s APA process in detail.

2.5.2 Australia

2.5.2.1 Introduction

According to Markham (2012), transfer pricing remains to be a focus area receiving the greatest scrutiny by the Australian Tax Office (ATO). In Australia, as in New Zealand, the accepted basis for placing a transfer price on a cross border transaction is the arm’s length principle (Markham, 2012). Division 13 of the Australian *Income Tax Assessment Act* (ITAA) 1936 applies to both residents and non-residents and includes the arm’s length consideration by the Commissioner as one of its provisions. Section 136AD of the ITAA 1936, which includes the key provisions of Division 13, provides the basis as to whether the Commissioner may substitute a non-arm’s length transaction with a more appropriate one.

The Australian transfer pricing landscape has seen a tremendous amount of change and reform in the past decade. One of the most important aspects of reform was shown in the court case, *Commissioner of Taxation versus SNF (Australia) Pty Limited [2011] FCAFC 74*. In this case, the Federal Court of Australia rejected the Commissioner’s attempt to use profit based methodologies, namely the transactional net margin method (TNMM), and the OECD Transfer Pricing Guidelines in interpreting Division 13, as both the OECD Guidelines and the legislation are not consistent (Ernst & Young, 2014). As a result, new transfer pricing provisions directly referring to the OECD Transfer Pricing Guidelines and the methods described under the Guidelines as relevant and appropriate, were drafted by the Treasury.

Advance Pricing Arrangements¹⁸ (APAs) have found their way in Australia as a popular transfer pricing management controversy tool among MNEs. The use of APAs as a management controversy tool by parent companies in Australia is higher than the Asia-Pacific and global average (Ernst & Young, 2013). It is worthy to mention that the world's first bilateral APA was signed between the United States Internal Revenue Service (IRS), the ATO and the Apple Computer Company in 1991 (Markham 2012). Since then, Australia's APA program has been continuously evolving (Markham, 2012).

In February 2001, the first report on APAs was issued by the ATO (Markham, 2012). The report was brief and contained information about the program and how it performed since its commencement in 1991. Up until 2007, the ATO had issued various guides and reports on transfer pricing and APAs; the APA program had been experiencing difficulty. By 2007, concerns over inconsistencies of APAs and the sustainability of the program itself were arising. As a result the ATO had commissioned PwC Legal in 2007 to undertake an independent third party review and evaluate the APA program. The purpose of the review was to layout recommendations to improve the effectiveness and efficiency of the existing program at the time. Many stakeholders, including taxpayers, tax advisors, industry groups and ATO personnel were involved in the review. The PwC Legal report identified 14 key recommendations to be considered by the ATO to improve the effectiveness and efficiency of the APA program.¹⁹ The recommendations fell into six main themes: Transparency and governance; Efficiency and Project Management; Sustainability/People; Relationship/Trust; Fitness for Purpose; and Balanced Score Card Evaluation (Markham 2012). Markham (2012)

¹⁸ Markham (2011) explains that "Australia refers to advance pricing 'arrangements' rather than 'agreements', giving Australian APAs less of a contractual flavour than US APAs" (p.157).

¹⁹ "...PwC Legal submitted its report to the ATO's APA program in April 2008, ..." (Markham, 2012, p.190).

described the independent review as perhaps being “the most significant development in relation to the Australian APA program to date” (p.189).

There were delays in introducing the new APA program. Eventually, in 2011 the ATO released a new Practice Statement on APAs, PS LA 2011/1. “At first glance the Practice Statement contained a number of innovations which would broaden the options available to MNE taxpayers in the transfer pricing dispute resolution context. The changes instituted indicated an awareness of taxpayer criticisms levelled against the former APA system, and demonstrated a commitment to the success of the APA program in years to come” (Markham, 2012, p.217).

As part of the ATO’s reinvention agenda, a new Law Administration Practice Statement PSLA 2015/4 was introduced outlining the Commissioner’s practice and procedures and provides guidance to ATO staff on how to deal with APA requests (Australian Taxation Office, 2015b).²⁰ The ATO states that the new Practice Statement reflects a “principle-based approach; streamlined process and practices to improve timelines; [and a] reduction in red tape” (Australian Taxation Office, 2015). The Practice Statement is an internal ATO document, and does not provide full protection for taxpayers in relation to their taxable position.

Under the revised guidance, the ATO’s APA process is divided into three phases: Early engagement; APA application; and monitoring compliance (PwC, 2015). The early engagement phase has changed significantly than what it was previously. “The early engagement process brings forward a greater amount of work to be completed before a formal APA application is submitted to the ATO” (PwC, 2015). This stage has a set time limit of six months. An internal ‘triage’ workshop is arranged to decide whether a taxpayers request will

²⁰ “If taxpayers rely on this practice statement [PSLA 2015/4], they will be protected from interest and penalties in the following way. If a statement turns out to be incorrect and taxpayers underpay their tax as a result, they will not have to pay a penalty. Nor will they have to pay interest on the underpayment provided they reasonably relied on this practice statement in good faith. However, even if they don’t have to pay a penalty or interest, taxpayers will have to pay the correct amount of tax provided the time limits under the law allow it”.

proceed, to the next phase or not. Various factors are considered in deciding whether a request will proceed such as the complexity of the transactions involved, collateral tax issues that may need to be considered as part of the APA, taxpayer history and taxpayer's previous APA history.

Once the request is accepted under the early engagement phase, the taxpayer is invited to lodge a formal APA application which is subject to a maximum timeframe of 18 months for completion. The final stage, which is the monitoring stage involves an Annual Compliance Report. The ATO monitors a taxpayer's performance under the APA entered into in this final stage.

2.5.2.2 Evaluation of the ATO APAs program

2.5.2.2.1 Certainty

PS LA 2015/4 states the purpose of entering into an APA is "primarily to mitigate risk" "[They] give taxpayers the opportunity to reach agreement with the ATO on the method of application of the arm's length principle to their covered cross-border dealings on a prospective bases" (Australian Taxation Office, 2015b). According to Markham (2012), many benefits are realised by the ATO and taxpayers entering into an APA. Agreeing on appropriate transfer pricing methodologies used to price inter-affiliate cross border transactions, MNEs increased accuracy in predicting tax liabilities, and the substantial elimination of the risk of double taxation are some of the major benefits that can be realised. Another point Markham (2012) points out is the ATO's increased emphasis on MNEs maintaining a 'high standard' of corporate governance and tax risk management of its uncertain tax positions. APAs prove to be an attractive solution for MNEs to maintain such 'high standard'.

2.5.2.2.2 Cooperation and Flexibility

The ATO places emphasis on the cooperative and flexible nature of its APA program. The ATO's latest PS LA 2015/4 mentions that the authority will commit to fostering constructive working relationships with mutual trust by way of full disclosure in a cooperative manner. The ATO does have mutual expectations from taxpayers to reach an effective outcome. 'Open and ongoing dialogue' in the development of an APA is a must. Full transparency in disclosing all relevant material facts is expected. Markham (2012) mentions that revenue authorities, including the ATO, need to differentiate the APA process's cooperative nature from a normal audit activity. It is worthy to note that although the ATO strongly encourages taxpayers to obtain APAs, it does make it clear that it is not appropriate for all taxpayers as a higher level of due diligence than before is undertaken in concluding an APA (Australian Taxation Office, 2015x; Ernst & Young, 2015).

2.5.2.2.3 Rollbacks

The ATO's approach with APAs has been forward-looking; however, looking at previous years (i.e. roll-backs) is not ruled out (Markham, 2012). Transfer pricing issues arising from prior years are treated as collateral issues by the ATO. Applying the same methodology used in the APA to prior years can be a way to deal with such issues. Issues relating to prior years are to be dealt with using an active compliance product. The ATO will consider to roll-backs on a risk-assessment basis (Ernst & Young, 2015). Rolling back for a lesser amount of years in the case of a voluntary APA request, or issues rated as high risk will more likely have the ATO consider such request (Australian Taxation Office, 2015b).

2.5.2.2.4 Renewals

One of the benefits this transfer pricing controversy management tool is the ability to renew the arrangement, thus offering continued certainty and as well cost savings (Markham, 2011). The ATO offers a streamlined renewal process as part of its program. The new PS LA 2015/4 outlines the circumstances where it may be appropriate to streamline an APA renewal request. The circumstances include, where there have been no material changes to the applicant's cross border transactions, no new terms are being proposed, and that there will unlikely be any material changes to the dealings over the renewed term of the APA. "It is implied that the ATO may be less receptive to renewing APAs with taxpayers who have consistently returned results at the bottom end of the range agreed in an APA" (PwC, 2015, p.2).

2.5.2.2.5 Time and Cost of Filing an APA

"The ATO needs to monitor the cost of keeping APAs up-to-date in the face of company, product and time specific changes, which make the parameters of the APA obsolete" (Markham, 2012, p. 257). As mentioned previously, the revised ATO guidance on the APA process (PS LA 2015/4) aims to streamline the process and practices to improve timeliness and reduce 'red tape'. The ATO has placed maximum timeframes for the early engagement phase and APA application phase of six months and eighteen months, respectively.

There has been some criticism from tax advisors that tax authorities themselves cause further delay to the process. "The ATO has itself been criticized for having insufficient resources to adequately administer its APA program" (Markham, 2012, p. 258). Markham (2012) states that recently tax advisors have seen increased confidence in relation to timelessness with the ATO's commitment to having been actively recruiting more appropriately skilled staff to deal with APA requests.

The new Practice Statement which provides guidance to ATO staff on APAs and how to deal with taxpayer requests shows the authority's awareness of the program's various parameters, including cost and timeliness. 'Paragraph 4' of the Practice Statement highlights the cost savings achieved by entering into an APA (Australian Taxation Office, 2015b). APAs represent a preventative mechanism unlike audits which are reactive, thus providing cost savings to the tax system. Also, APAs contribute to government's efforts to reduce 'red tape' as a result of reduced compliance costs over the term of an APA once entered into. The Annual Compliance Report under the final monitoring stage should also provide cost savings to taxpayers as the level of documentation required under the duration of an APA is less than if a taxpayer had to prepare adequate transfer pricing documentation without an APA in place.²¹

A discussion paper published by Ernst & Young (2015) commenting on the ATO's revised APA program, states that the overall timeframe for concluding a complex APA has not changed and that a lot of upfront work and documentation is required before being accepted into the program. A further transfer pricing discussion paper on the matter issued by PwC (2015) mentions that the objectives of the new program to improve timeliness, streamline the process, and reduce red tape may take some time before they are realised. To ensure an APA progresses in a timely manner, the discussion paper recommends that identifying key ATO stakeholders and establishing good working relationships with them is important (PwC, 2015).

2.5.2.2.6 An APA Could Trigger a Transfer Pricing Investigation

The new PS LA 2015/04 outlines the interactions between APAs and ATO audits.²² Linked to the issue of the cost of an APA, (Markham, 2012) mentions that taxpayers often require top level external advice to negotiate an APA with one or more tax authorities to reach agreement.

²¹ Paragraph 21, PS LA 2015/4.

²² Paragraph 25 of the PS LA 2015/4.

As part of the negotiation process, taxpayers need to keep in mind the amount of information they reveal. Revealing too much may pose severe risks in relation to the ATO proceeding to auditing the applicants' TP affairs.

“An APA does not preclude a taxpayer from a risk review or audit (active compliance product) of its business overall”.²³ Cross-border transactions already covered under an APA will not be subject to active compliance unless the applicant has omitted information or provided incorrect information that is material and relevant. The ATO has emphasised the importance of its staff to treat active compliance products and APA developments separately. In relation to rollbacks and their interaction with audits, as mentioned previously (under Rollbacks) the methodology used in an APA may be applied to prior years under active compliance given the taxpayers circumstances are sufficiently similar (Australian Taxation Office, 2015b; Ernst & Young, 2015). APAs appeal to taxpayers desiring certainty; however, proceeding to audit tremendously hinders timeliness and can be costly (PwC, 2015).

2.5.2.2.7 Relevance of APAs to SMEs

Under the previous PS LA 2011/1, the ATO had streamlined the APA process for SMEs by introducing a simplified APAs for businesses with a turnover less than \$250 AUD million (Markham, 2012). APAs for SMEs are usually unilateral (Feinschreiber & Kent, 2008). SMEs wanting to enter a bilateral APA will need to go through the standard process (Markham, 2012).

The new PS LA 2015/4 does not mention anything regarding APAs for SMEs or even that of a simplified version. However, the Practice Statement does explicitly mention that ‘ATO staff are to tailor an APA to address the taxpayer’s circumstances.’²⁴ An interesting point raised by the Practice Statement is in regards to taxpayers who qualify for and opt to apply the

²³ Paragraph 25, 25A of the PS LA 2015/4.

²⁴ Paragraph 4, 4G of the PS LA 2015/4.

‘Simplifying transfer pricing record keeping’ online guidance. While the ATO has said it will still consider applicants who have applied the simplified record keeping, it considers that such taxpayers may be less likely to request an APA in respect of the cross border transactions covered by the simplified record keeping online guidance.²⁵

2.5.2.3 The Alternatives to using an APA

The alternatives available to using an APA in Australia are to either maintain transfer pricing documentation, undergo a transfer pricing audit, arbitration via Mutual Agreement Procedure (MAP), or undergo TP litigation.

Apart from the Annual Compliance Report that is required, no other documentation is required with the duration of an APA (Markham, 2012). Transfer pricing audits have been discussed in the previous section. Taxpayers need to be careful when they approach the ATO for an APA; in the case of a request proceeding to audit, it can be costly and hinder timeliness. In the incident of double taxation, taxpayers have access to the MAP program, where an agreement is reached between the relevant competent authorities.

There is a lot of reluctance in undergoing litigation to resolve transfer pricing disputes. This reluctance is mainly attributed to the high legal costs involved in a litigation process, the ATOs success in resolving disputes, and the uncertainty of the litigation process outcome (Markham, 2012). Some of the most prominent transfer pricing litigation cases in Australia are the *Roche* case,²⁶ *SNF*,²⁷ and more recently the *Chevron* case²⁸ decision in 2015.

²⁵ Paragraph 7, 7B of the PS LA 2015/4.

²⁶ *Roche Products Pty Ltd v. Commissioner of Taxation* [2008] AATA 639.

²⁷ *SNF (Australia) Pty Ltd v. Commissioner of Taxation* [2010] FCA 635.

²⁸ *Chevron Australia Holdings Pty Ltd v FC of T* [2015] ATC 20-535.

2.5.2.3.1 The Roche Case

“This is a novel case which considers the circumstances in which transfer prices, paid for acquisition of property by subsidiaries of multinational corporations, can be adjusted for income tax purposes” - ROCHE PRODUCTS PTY LTD v FC of T 2008 ATC 10-036

The Roche case is one of the most recent cases showing taxpayers’ willingness to litigate their transfer pricing disputes with the ATO (Markham, 2012). The case concerned the Roche Group’s transfer prices paid from its Australian subsidiary to its parent company, which is a resident of Switzerland. The Roche Group is a major pharmaceutical corporation with various business functions performed by the Group. Roche Australia carried on the business of marketing, selling and distributing Roche products in Australia.

The ATO reviewed the transfer pricing affairs of three of the subsidiary’s divisions: the Prescription Division, the Consumer Health Division and Diagnostic Products. The Commissioner audited the transfer prices of the Roche products acquired by Roche Australia from the related companies located in Switzerland and Singapore. The Commissioner viewed these prices as excessive. The Commissioner used the TNMM using net profit comparables in deriving his assessment. The ATO increased Roche’s taxable income for the years in consideration (1993-2003) by approximately AUD 126 million. The Applicant - Roche Australia - used a comparable uncontrolled price (CUP)²⁹ and gross margin analysis to demonstrate the prices paid were arm’s length.

²⁹ Refer to the OECD’s ‘Review of Comparability and of Profit Methods’ report issued 22 July 2010 for further information on any transfer pricing methodologies mentioned throughout this thesis. Can be accessed from <http://www.oecd.org/ctp/transfer-pricing/45765701.pdf>.

“A number of expert opinions were heard, but each was in some way found wanting by the Tribunal” (Markham, 2011, p.269). The use of the Transactional Net Margin Method (TNMM) by the ATO was rejected by the judge.

On 2 April 2008, Downes J gave his decision. The judge had found that the Applicant’s prescription divisions had overpaid AUD 58.7 million and that the taxable income should be adjusted accordingly. The other divisions were found to have paid prices that were in line with the arm’s length principle. On 22 July 2008, based on a revised gross margin analysis Downes J further reduced the assessments to AUD 42.55 million.

“The case raised many issues. The judge gave some support to the view that the Associated Enterprises article of the DTAs is not a source of taxing power and that the focus of Division 13 is on transactional rather than on profit-based methods” (Markham, 2012, pp. 269-270).

2.5.2.3.2 SNF Australia

The decision on this case had been decided on 25 June 2010, two years after the *Roche* decision.³⁰ The case concerned whether *SNF Australia* had paid prices more than the arm’s length price for products it had acquired from overseas related entities so that the Commissioner could apply transfer pricing adjustment to adjust the purchase prices accordingly.

The taxpayer was part of a global group with the parent company being a resident in France. SNF Australia would buy chemicals from overseas related entities and sell them to non-related end users in Australia. The taxpayer consistently returned losses from the date of incorporation in 1990 until 2004. The taxpayer’s transfer pricing affairs were subject to an audit.

³⁰ [2010] FCA 635 (25 Jun. 2010).

Determinations were made under Division 13 of Part III of the Income Tax Assessment Act 1936 to adjust the purchase prices to reflect an arm's length purchase price of the chemicals.

“The taxpayer produced evidence of sales by the overseas suppliers to third party purchasers, which it submitted established comparable uncontrolled prices (CUP) that were as high as or higher than the prices paid by the taxpayer” (Australian Taxation Office, 2011). The Commissioner rejected the taxpayer's evidence. The ATO relied on a TNMM in determining the arm's length price.

Middleton J, held that the taxpayer could rely on the CUP analysis transfer pricing methodology. The decision was a major win for the taxpayer (Markham, 2012).

“The judge expressed similar concerns to those expressed in the *Roche* case ...and reiterated Justice Downes' point that the TNMM inevitably attributed any loss to the pricing, while there may well be other legitimate reasons for losses to occur” (Markham, 2012, p.272).

The Commissioner appealed the case, however the Full Federal Court upheld the earlier decision made by the Federal Court. The ATO had referred to paragraph 1.6 of the OECD Guidelines to support its submission; the submission was regarded as deeply impractical as the OECD guidelines were not consistent with the current legislation (Ernst & Young, 2014).

On 7 November 2011 the ATO released a Decision Impact Statement on the Full Federal Court's decision in *Commissioner of Taxation v. SNF Australia Pty Ltd*. The Statement referred to the Government announcing substantial reforms to the transfer pricing provisions. Markham (2011, p. 273) states that the “SNF case has promoted an overhaul of Australia's transfer pricing legislation to incorporate the OECD's view on transfer pricing methodologies and provide taxpayers with greater certainty”.

2.5.2.3.3 Chevron Case

This is one of the recent cases around the financing aspect of transfer pricing. This case saw a win to the ATO and has presented the Australian transfer pricing landscape with a landmark case. The case concerned interest payments made by Chevron Australia Holdings Pty Ltd (CAHPL) to its US subsidiary Chevron Texaco Funding Corporation (CFC) and whether the base interest rate used for the intercompany loan in question was at arm's length under the ITAA 1997.

*“Central to the proceedings is a Credit Facility Agreement [CFA] dated 06 June 2003 between CAHPL and CFC under which CFC agreed to make advances from time to time to CAHPL in the aggregate the equivalent in Australian Dollars ...of Two Billion Five Hundred Million United States Dollars”.*³¹

The interest rate was payable monthly at a rate equal to the 1-month AUD-LIBOR as determined with respect to each Interest Period +4.14% per annum, which gave an effective interest rate ranging from 8.8% to 10.5%. The final maturity date of the CFA was 30 June 2008. Some of the features of the loan were the CAHPL provided no guarantee or security over its assets to CFC. CFC was entitled to terminate the CFA at any time with no cause. Further, CAHPL was able to repay any of the advances made to it. CFC had initially raised the funds at a rate equivalent to or under the US LIBOR rate (approx. 1 to 2%).

CAHPL claimed deductions at 30% for the repayments it made to CFC at interest rates up to 10.5% while the initial funds were raised at under 2%. These interest rates were exempt from withholding tax. CFC was able to pay back the sums as tax free dividends to CAHPL as these were not subject to withholding tax in the US, nor were they assessable income in Australia.

³¹ *Chevron Australia Holdings Pty Ltd v FC of T* [2015] ATC 20-535: Introduction, Paragraph 2.

The end result was that CAHPL claimed interest deductions charged as high as 10.5% at the Australian company tax rate, despite the funds being raised by CFC at a much lower rate.

“The [Federal] Court held that CAHPL had not shown that the interest paid under the CFA was equal to or less than arm’s length” (Deloitte, 2015a). A report issued by Deloitte (2015a) described the case as being ‘extremely complex’. The case was heard over more than 20 court days and involved more than 20 witnesses.

The above sections set out an overview of the Australia’s transfer pricing environment and the Australian APA process. Australian transfer pricing case law was reviewed as well.

2.5.3 United Kingdom (UK)

2.5.3.1 Introduction

Section 2.5.3.2 provides an overview of the UK’s APA process with all the stages involved to obtain an APA. Avoseh’s (2014) evaluation of the UK’s APA process is reviewed under section 2.5.3.3. Section 2.5.3.4 concludes the overview of the UK’s APA process.

2.5.3.2 The UK APA Process

Before a statutory framework for an APA program existed in 1999, APAs were agreed using the mutual agreement procedure of the relevant authority. Formerly found at Section 85, Finance Act 1999, the legislation that relates to APAs now appears at *Sections 218-230 of the Taxation (International and Other Provisions) Act 2010 (TIOPA 2010)*. HMRC has published a practice statement, Statement of Practice 2(2010) (SP02/10), which provides detailed guidance about HMRC’s practice in reaching advance agreements. HMRC also maintains an ‘International Manual’ (INTM) which contains up to date guidance on key international tax issues including practical guidance on working transfer pricing and thin capitalisation cases.³²

³² HMRC INTM can be accessed from <https://www.gov.uk/government/publications/statement-of-practice-2-2010/statement-of-practice-2-2010>.

HMRC INTM422000, ‘Transfer pricing methodologies: Advance Pricing Agreements: contents’, reproduces the content of SP02/10 throughout the manual.

According to HMRC International Manual (INTM422020):

“An APA enables businesses to achieve certainty that the transfer pricing issues covered by the agreement will not be part of any enquiry into their self-assessment tax returns for the relevant period and so provides greater certainty over their tax liabilities. HMRC has also found that where there is considerable difficulty or doubt in determining the method by which the arm’s length principle should be applied, the transfer pricing issues can be more efficiently dealt with in real time ...”

Statement of practice SP02/10, paragraph 13 states that an APA may be requested by any:

- UK business, including a partnership, with transactions to which the provisions of Part 4 TIOPA 2010 apply (the UK transfer pricing rules);
- Any non-resident trading in the UK through a permanent establishment; and
- Any UK resident trading through a permanent establishment outside the UK.

Every APA request will be considered by HMRC, but generally, the authority closely considers cases where the transfer pricing issues are complex and rather than straightforward.³³ Also, where the transfer pricing policies or issues would not be regarded as ‘low risk’ and/or the likelihood of double taxation is high. Further, a taxpayer seeking to implement a method which is highly tailored to their own circumstances, is another situation HMRC would consider closely. HMRC will not decline a request solely in reference to the size of transactions giving

³³ Complex means there is a doubt as to how the arm’s length standard should be applied – SP 02/10 Paragraph 13.

rise to transfer pricing issues because the authority does recognise that complex transfer pricing issues can be encountered by smaller businesses.³⁴

A Guide to APAs published by Ernst & Young (2012) outlines the stages of the UK APA process that passes through. The UK APA process stages:

a) Pre-filing Conferences

This stage is referred to as the ‘Expression of Interest’ process under the UK framework. HMRC strongly recommends that taxpayers informally discuss their plans first before presenting a formal application. This is to ensure that resources are not wasted on an unsuitable application. Further that the detailed work undertaken by the taxpayer in submitting the formal application is focused on the relevant issues. Some of the issues the ‘Expression of Interest’ should cover are, the nature of the transfer pricing issues intended to be covered by an APA, the details of the tax residence of the parties involved and the importance to the wider business of the transactions intended to be covered.³⁵

In the event that HMRC considers the application should not be admitted into the APA program, HMRC will explain the reasons to the business, and will allow the business to make further representations.

b) Formal APA Request

At this stage, a formal application is submitted if HMRC give an indication that they are willing to accept the APA proposal and the business wishes to proceed. SP02/10 ‘Annex 1’ sets out the requirements of TIOPA10/S223 and states these requirements

³⁴ HMRC International Manual INTM422040: Many small and medium enterprises are exempt from the UK transfer pricing legislation by virtue of TIOPA10/S166 and so there may be limited occasions where the APA process will be appropriate for smaller businesses.

³⁵ Refer to HMRC INTM422050 for further information on what the ‘Expression of Interest’ stage of the UK’s APA process should cover.

are in place to ensure that any agreement about the practical treatment of specified transfer pricing issues is formed from a proper understanding of the relevant principles of the 'Taxes Acts'.³⁶

Evaluation and Negotiation

Once the formal application is received, HMRC will evaluate its contents and will request any additional information from the applicant as necessary. HMRC expect that the transfer pricing issues be discussed openly and access to any relevant information is made available by the business. Lack of co-operation may result in HMRC giving no further consideration to the APA applied for by the business.

Once final agreement is reached, HMRC and the taxpayer will be made subject to the terms being observed. The terms are outlined by INTM422090 and include:

- "A commitment from the business to demonstrate adherence to the agreed method for dealing with the transfer pricing issues during the term of the APA in the form of a regular compliance report (an "Annual Report") as required by TIOPA10/S228 and
- The identification of Critical Assumptions bearing materially on the reliability of the method and which, if subject to change, may render the agreement invalid."

From the date of the formal submission, HMRC aims to complete the APA process within 18-21 months.³⁷

³⁶ The list of requirements set out in TIOPA 10/S223 are also listed in HMRC International Manual INTM422130: 'SP2/10 Annex 1'.

³⁷ HMRC INTM422140: 'SP2/10 Annex 2'.

c) The APA Annual Report³⁸

The requirements of the final report will be set out in the finalised agreement and will focus narrowly on the issue covered by the APA. The APA annual report usually is filed with the business' tax return. The purpose of the annual report is to determine whether the business has complied with the terms of the APA or not.

2.5.3.2.1 Revising and renewing APAs

Paragraphs 46-48 of SP 2/10 set out in detail what HMRC considers when revising and renewing APAs. In respect to revising an APA, HMRC states that specific circumstances may allow for an APA to be revised. For example, where there has been a change that results in an agreed transfer pricing methodology to become difficult to apply, however, not to the extent that the change invalidates the underlying critical assumption of the APA, HMRC will consider revising the APA.

Some of things HMRC will consider when renewing an APA are if there has been a material change in the facts over the term of the APA. In cases where the transfer pricing issues have changed significantly and a new transfer pricing methodology is being proposed, HMRC will require the taxpayer to make a 'fresh' application.³⁹

2.5.3.2.2 Term of agreement and roll-back

Typically the term of an APA under HMRC's program is from three to five years.⁴⁰ In some situations, a chargeable period to which the APA relates may have ended before agreement is

³⁸ HMRC INTM422100: 'Annual reports'.

³⁹ Refer to HMRC' SP 2/10, Paragraphs 46-48, for detail on what HMRC considers when revising and renewing APAs.

⁴⁰ HMRC INTM422060: 'Term of agreement and roll-back'.

reached. TIOPA10/S224 allows the APA to be effective for that chargeable period and any adjustments to be made for tax purposes as a consequence of the agreement.

Statement of Practice (SP 2/10) states the following in relation to roll-backs:

“The agreed transfer pricing methodology may be relevant for an earlier period and to the resolution of any transfer pricing enquiries raised for earlier periods if the particular facts and circumstances surrounding those years are substantially the same. Consequently, in such circumstances, the business may wish to consider using the agreement as a basis for amending a self-assessment return or to request that the method for dealing with transfer pricing issues contained in the APA should be considered for resolving any transfer pricing enquiries to which it is relevant for earlier years. HMRC may also suggest that the ‘roll-back’ of the APA is an appropriate means of resolving a transfer pricing issue in earlier years although, in bilateral or multilateral cases, the possibility of doing so will also be dependent on the ability or willingness of the administration of the other country or countries involved to do so” (Paragraph 26).

2.5.3.2.3 Nullifying and revoking APAs and penalties

In accordance with TIOPA/S225, an APA may be revoked by HMRC in accordance with its terms, where the business does not comply with the terms and conditions of the agreement, or where the identified critical assumptions cease to be valid.⁴¹

Where false or misleading or misleading information is supplied fraudulently, or negligently, in connection with an application for, or in the process of monitoring, an APA, penalties may be applied, and the APA might be nullified.⁴²

⁴¹ HMRC INTM422110: ‘Revocation and penalties’.

⁴² See TIOPA10/S226 and TIOPA10/S227.

2.5.3.3 Avoseh (2014)⁴³

Avoseh's (2014) study, *An empirical evaluation of the advance pricing agreement process in the UK*, which examines the UK's APA process provides insight on various aspects of the process. The author states that recent statistics in the UK, where HMRC has operated the APA program since 1999, the APA program has not been popular among MNE taxpayers. Avoseh (2014) adopts a mixed-method approach to examine HMRC's APA process. "A sample of MNEs based in the UK was investigated and also their reasons for applying or not applying for an APA, particularly with HMRC in the UK". The study concludes with three key themes that are critical to MNEs' when deciding on whether or not to apply for APAs. The three key themes concluded are: (1) Cost and Benefit of an APA, (2) Clarification of APA Guidelines and (3) Generic APA Process. Avoseh's (2014) study proves to be highly beneficial in reviewing HMRC's APA process as a comparative for the purposes of this research.

2.5.3.3.1 Findings and Discussions

Three thematic issues emerged through the data analyses as ultimately relevant to the decisions of MNEs on whether or not to consider an APA. These include the issue of the 'Cost and Benefit of an APA to the MNE'; 'The Clarification of the APA Guidelines to the MNE' and; finally the desire and usefulness of having a 'Generic APA' in place as a channel for improving APA submissions.

'Cost and Benefit of an APA to the MNE'

"Respondents rated the 'Cost of APA' as the most important primary rationale working against their interest in the APA process" (Avoseh, 2014, p.213). Avoseh (2014) mentions that this did

⁴³ Avoseh, O. O. (2014). *An empirical evaluation of the advance pricing agreement process in the UK. PhD thesis*. (Doctoral thesis, University of Glasgow, Scotland, United Kingdom). Retrieved December 13, 2015 from <http://theses.gla.ac.uk/5182/1/2014Avosehphd.pdf>.

not come as a surprise as prior research in the same area has reported similar claims by MNEs in the past (Borkowski, 1993; 1996b; 2008). The cost of an APA was recognized as relatively significant when the transactions are large. This included the cost of hiring advisors. In addition, the costs involved in sustaining applications over the long duration of negotiations, especially in the case of bilateral APAs. The benefits of concluding an APA for MNEs were seen in terms of the amount of transactions under focus.

The 'Cost and Benefit of an APA' theme for MNEs not regarded as large enough to consider an APA was interpreted in terms of the time involved in putting documentation together for an APA application as compared with that of preparing documentation for defence in a transfer pricing audit. Also, the materiality of transactions involved was a factor further reflected in the findings. Avoseh (2014) explains in this situation, an APA would only be given consideration if the volume of transactions involved is significant in order to cover the cost associated with the APA application. Otherwise, there was the notion of undergoing an audit for internal transactions is always generally less costly when compared with an APA.

The study recommends a greater pursuit of collective commitment on the part of HMRC should be exercised across jurisdictions as a means of speeding up the process of concluding bilateral APAs. Greater harmonization may need to be pursued by HMRC with that of tax authorities of other UK treaty partners.

'Clarification of APA Guidelines'

APA guidelines mainly constitute of HMRC's Statement of Practice (currently SP 2/10) and the OECD Guidelines on transfer pricing which HMRC follow. In Avoseh's (2014) study, the idea of how clear these guidelines are was largely expressed by MNEs in terms of acceptable methods of pricing intangibles as well as new inter-company transactions.

“ ... MNEs’ perception of the level of certainty that can be obtained from the UK APA process is influenced by their inability to clearly determine from the guidelines available, which T[ransfer] P[ricing] methodology is acceptable to HMRC on their class of transactions and subsequently, whether or not the eventual T[ransfer] P[ricing] methodology to be imposed by HMRC will be suitable for the company” (Avoseh, 2014, p.215).

The study evidenced that HMRC’s SP 2/10 is regarded as generic and not helpful enough. Also, the author mentions that there may be a need for HMRC and the OECD to further clarify their guidance on intangibles – a main concern expressed by MNEs. Overall, clearer guidance is needed to better reflect the business realities of MNEs.

‘Generic APAs’

The desire to have more generic APAs was noted by the sample MNEs in the study in cases where the APA is typically bilateral or multilateral in nature. MNEs expressed the concept of ‘Generic APAs’ in two ways. First, it was expressed as having more simplified APA regulatory requirements in place. The second expression was in relation to the positive impact that uniform transfer pricing documentation requirements (rather than a uniform transfer pricing audit exercise) could have on APA application submissions with HMRC.

MNEs welcomed the idea of having a unified documentation requirement that could suffice for different tax authorities involved in an APA application. Avoseh (2014) refers to the workings of the Pacific Association of Tax Administrators (PATA) which is an inter-country affiliation between Australia, USA, Canada, and Japan. Taxpayers’ resident within any of these jurisdictions can produce uniform transfer pricing documentation. Under the PATA agreement, MNEs are not subject to legal requirements which are greater than those imposed under the local laws of the PATA member. The PATA agreement is aimed at responding to difficulties

MNEs face in complying with the laws and administrative requirements of multiple tax jurisdictions.

Borkowski's (2008) survey (mentioned in Avoseh's (2014) study) showed that the number of APAs did not increase, neither did the process become more efficient as a result of PATA. Borkowski believed that PATA would need to reach higher global awareness among MNEs for it to have any significant effect on MNEs' transfer pricing related practices. Avoseh (2014), in addition to Borkowski's recommendation, provided an alternative explanation for the lack of evidence for an increase in APA usage after the introduction PATA transfer pricing documentation. The lack of increase "could be related to how cost effective MNEs find their adherence to the documentation package" (Avoseh, 2014, p. 219).

"HMRC can make their APA process more attractive to MNEs through a consistent and standardised harmonization of their APA rules, procedures, documentation requirements and penalties vis-à-vis their major treaty partners" (Avoseh, 2014, p.220).

2.5.3.4 Conclusion

A review of the HMRC's APA process and the stages involved in obtaining an APA were looked at in this section. Further, Avoseh's (2014) evaluation of the UK's APA process was reviewed.

Avoseh's (2014) study has shown that other themes are relevant to MNEs decision on whether or not to consider an APA, besides 'the cost of an APA'. The 'clarification of APA guidelines' as well as whether or not such an APA arrangement will be easily acceptable to other tax authorities (in reference to the desire of a 'generic APA arrangement) are additional factors that MNEs consider in their APA decision.

2.5.4 United States (US)

2.5.4.1 Introduction

In the US, the arm's length principle is the accepted basis for determining an appropriate transfer price (Markham, 2012). The arm's length principle has been incorporated in regulations under section 482 of the Internal Revenue Code (IRC). It is a requirement under Section 482 of the IRC for related parties to reflect the arm's length principle on their tax returns. Transfer pricing disputes may take years to resolve and sometimes more than a decade if the case proceeds to litigation (PwC, 2013). The IRS has been increasing its transfer pricing audit activity in recent years (Markham, 2012). A 2013 global transfer pricing survey shows the scope of the IRS's transfer pricing audit activity with 91% of US parent companies having their transfer pricing policy examined since 2009. Against the widening scope of the IRS's transfer pricing audit activity, it is not a surprise that MNEs are showing a greater interest in APAs. By pursuing an APA, a taxpayer has the ability to work in a collaborative manner with the IRS and (in the case of bilateral/multilateral APAs) with one or more tax authorities to agree on an appropriate transfer price and/or resolve transfer pricing matters (PwC, 2013).

Many studies stipulate that the US's APA process is perhaps one of the most advanced and detailed in the world (See: Avoseh, 2014; Calderon, 1998; Markham, 2012). Since the inception of the US's APA program in 1991, taxpayers are able to conclude an APA with the IRS to agree on an appropriate transfer price that reflects the arm's length principle.⁴⁴ The Advance Pricing and Mutual Agreement (AMPA) Program are responsible for managing the

⁴⁴ The procedures for obtaining an APA were first published in 1991. See Rev. proc. 91-22, 1991-1 C.B. 526.

US's APA process.⁴⁵ The Revenue Procedure (Rev. Proc.) 2015-41⁴⁶ was released on August 12 (Deloitte, 2015). Rev. Proc. 2015-41 “provides guidance on the process of requesting and obtaining advance pricing agreements from”⁴⁷ APMA.

As a general note, APMA has a particular preference to conclude bilateral and multilateral APAs⁴⁸ over unilateral APAs.⁴⁹ The IRS claim that bilateral and multilateral APAs minimize taxpayer and governmental uncertainty and administrative cost. Where a taxpayer requests a unilateral APA to cover issues that could be covered under a bilateral or multilateral APA, the taxpayer must explain their reasoning for why a unilateral APA is more appropriate to cover those issues.⁵⁰

Due to the scope of this thesis, the literature on the US APA process is not reviewed in detail. Any literature that is relevant in assisting to answer the research questions proposed in this study will be addressed directly in Chapter 4, ‘Research Findings and Discussion’. Other literature on the US transfer pricing regime and APA program have been considered previously under section 2.3, ‘Overview of APA Literature’. The remainder sections in relation to the US's APA process are set out as follows: section 2.5.4.2 sets out the phases of the APA process. Section 2.5.4.3 gives a brief overview of the IRS's approach to APA renewals and rollbacks.

⁴⁵ “In early 2012, the Advance Pricing Agreement (APA) Program merged with that portion of the Office of the U.S. Competent Authority (USCA) that resolves transfer pricing cases under the mutual agreement procedures of the United States’ bilateral income tax conventions to form the Advance Pricing and Mutual Agreement (APMA) Program. APMA’s mission is to resolve actual or potential transfer pricing disputes in a timely, principled, and cooperative manner”. See <https://www.irs.gov/businesses/corporations/apma>.

⁴⁶ This revenue procedure updates and supersedes *Rev. Proc.* 2015-40, 2006-1 C.B. 278, as modified by *Rev. Proc.* 2008-31, 2008-1 C.B. 1133 which is also superseded. *Rev. Proc.* 2015-41 can be viewed from <https://www.irs.gov/pub/irs-drop/rp-15-41.pdf>.

⁴⁷ *Rev. Proc.* 2015-41, section 1.01, p.2.

⁴⁸ *Rev. Proc.* 2015-41, section 2.02(4)(d), ‘Preference for Bilateral and Multilateral APAs’.

⁴⁹ This is evident from the number of bilateral APAs executed by the IRS compared to the number of executed unilateral APAs. Out of the 1511 APAs executed 1991-2015, 958 were bilateral APAs. Refer to the ‘[2015 APMA Statutory Report](#)’.

⁵⁰ Refer to section 2.02(4)(d) for more information on the IRS's preference for bilateral and multilateral APAs.

2.5.4.2 Phases of the US APA process

The 2010 IRS annual report⁵¹ divides the APA process into five phases: (1) application; (due diligence; (3) analysis; (4) discussion and agreement; and (5) drafting, review, and execution. Markham's (2012) overview of the US APA process considered a sixth phase: 'Ongoing APA Compliance – Annual Reports'. The US APA process in this thesis is considered using the six phases, consistent with Markham's (2012) review. The six phases are set out below:

2.5.4.2.1 Phase 1: APA Application, including the Pre-Filing Conference

Usually a taxpayer signals their intent to pursue an APA through a pre-filing conference (PFC). PFCs are informal and may not always be conducted. The purpose of the pre-filing conference is to informally explore the suitability and appropriateness of the APA being proposed by the taxpayer.⁵² Potential applicants may seek clarification about the IRS's functional analysis requirements for the APA and informally discuss the transfer pricing methods and any potential issues at PFCs (PwC, 2013).

Once the taxpayer decides to pursue an APA, the next step is to apply for an APA. The IRS charges a user fee for APA applications.⁵³ Section 3 of the 'Rev. Proc 2015-41 Appendix' sets out in detail information about 'User Fees'. In general, the user fee amount for an APA request is \$60,000 unless it is a small business APA request⁵⁴, in which case it is \$30,000. Paying the user fee is a general requirement in order for the APA process to initiate and progress (Rev. Proc. 2015-41, Section 2.03).

Rev. Proc. 2015-41 (refer Section 3.04) details the required components of a formal APA request. An essential component of an APA application is the 'functional analysis' which

⁵¹ 2010 IRS annual report can be viewed from <https://www.irs.gov/pub/irs-utl/2010statutoryreport.pdf>.

⁵² See Rev. Proc. 2015-41, section 3.02, for detail on PFCs.

⁵³ Markham (2012, p.68) mentions that it is unusual for revenue authorities to charge for an APA application.

⁵⁴ Refer Rev. Proc. 2015-41, section 3.04, for details on what constitutes a 'Small business APA request'.

should detail the analysis performed by the taxpayer in determining an arm's length price (PwC, 2013). This should address all the functions of the taxpayer, the risks borne by parties in any contemplated transactions and any other relevant economic conditions and contractual terms (4). Certain other information will need to be provided to the IRS as part of the formal APA application such as the group structure, financial and administrative data, company annual reports and any other similar data.

Once the application has been received by the IRS, it is assigned to an APA Team leader who is responsible for the case. Generally, if a PFC was held with the taxpayer, an attending APA Team Leader will be assigned to process the APA request (PwC, 2013). AMPA will notify the taxpayer that the APA request has been received. Refer to Rev. Proc 2015-41, section 4: 'Actions on APA request', for detail on the steps taken by AMPA when an APA request is received.

2.5.4.2.2 Phases 2 and 3: 'Due Diligence' and 'Analysis'

The due diligence and analysis aspects of the IRS's APA process is 'vital' (Markham, 2012). "Broadly, the APMA Team conducts due diligence and analysis of the APA request by discussing it with the taxpayer, verifying the data supplied, investigating the facts, and requesting and analysing additional information if necessary" (PwC, 2013, p.5). Rev. Proc 2015-41, section 4.07: 'Not an Examination', makes it clear that the due diligence and analysis aspects of the APA process will not constitute an audit.

2.5.4.2.3 Phases 4 and 5: 'Discussion and Agreement' and 'Drafting, Review, and Execution'

Phases 2 and 3 above lead to 'discussion' between the relevant parties. In the case of a unilateral, the discussion is between the taxpayer and the IRS's APA Team and agreement has

to occur before the APA can be concluded. In the case of a bilateral APA, a US Competent Authority analyst leads discussions with the treaty partner until agreement is reached among all relevant parties. Upon agreement by all relevant parties, the APA is executed by the IRS and the taxpayer. The length of time from the taxpayer submitting a formal APA application and execution of the APA usually depends on the complexity of the transactions involved and of the workload and resources of the APMA Program at the time (PwC, 2013).

2.5.4.2.4 Phase 6: Ongoing APA Compliance – Annual Reports

“An APA annual report must be filed for each APA year. The report must demonstrate the taxpayer’s compliance with the APA terms and conditions ...”⁵⁵ The IRS maintains the power to cancel or revoke an APA for failure to file an annual report that is timely, complete and accurate.⁵⁶ Rev. Proc 2015-41, section 7.02: ‘Annual Reports’, sets out in detail the requirements in relation to the APA annual report that must be filed for each APA year. The nature of documentation required in an annual report are listed in Appendix 3.

2.5.4.3 Renewals and Rollback

Under Rev. Proc. 2015-41, renewal APA requests with substantial changes in the facts will require a substantial effort to conclude. However, renewal APA requests with no material changes to the facts can be concluded with an APA procedure called an ‘abbreviated APA request’. An abbreviated APA request is defined as “an APA request in which information, documents, or content required for a complete APA request has been truncated or omitted, per explicit authorization from APMA”.⁵⁷ New APA requests with similar facts and issues currently under the IRS’s consideration may also be concluded with the same procedure

⁵⁵ Rev. Proc 2015-41, section 7.02: ‘Annual Reports’, pp.51-52.

⁵⁶ Rev. Proc 2015-41, section 7.06, ‘Revoking or Cancelling the APA’.

⁵⁷ See Rev. Proc. 2015-41, section 3.04(2), for detail on abbreviated APA requests.

(Deloitte, 2015). Taxpayers wanting to file an abbreviated APA request must obtain prior permission from AMPA in order to do so.⁵⁸

One of the significant changes under Rev. Proc. 2015-41 is in relation to rollbacks. (Deloitte, 2015). Section 5.02(1), 'Rollbacks', of the Rev. Proc 2015-41 states that "an APA is primarily a means to resolve coverable issues for prospective years. However, an APA may apply the covered methods (with appropriate modifications, if necessary) to one or more earlier, rollback years". AMPA can request to include rollback years on any APA request. Taxpayers considering an APA must now think about any open tax years on which the IRS might impose a rollback (Deloitte, 2015).

2.6 Gap in Literature

Avoseh (2014) mentions that there is lack within mainstream academic literature looking at APA processes in an empirical way. Some revenue authorities have attempted to evaluate their APA processes on consistent basis, for example, the IRS's Annual Statutory Reports on APAs. Other publications are made available by professional service firms such as Ernst & Young's Global Transfer Pricing Surveys (1995:2013).

Revenue authorities are usually a wealth of information in regards to their APA processes. However, these documents do not serve the purpose of an evaluation. The studies of Markham (2011) and Avoseh (2014) are examples of comprehensive evaluations of tax jurisdictions' APA processes. These two studies collectively review and evaluate the APA processes of Australia, the UK, and the US. No academic literature has been identified in relation to New Zealand's APA process. Moreover, the informal nature of the New Zealand APA process and

⁵⁸ Rev. Proc 2015-41, section 3.04(2): 'Abbreviated APA Requests'.

the lack of any publicly available information on the process make an attempt to evaluate the New Zealand APA process warranted.

2.7 Conclusions

This Chapter set out in two main parts. The first part sought to briefly review the literature on transfer pricing and APAs. A brief overview of the OECD and BEPS Action Plan were looked at too. The second part of this chapter reviewed the APA processes of New Zealand, Australia, the UK, and the US. Revenue authority documents were mainly used to explain the phases of each of the mentioned APA processes. Other literature, including empirical studies on these APA processes were reviewed to set out the evaluations obtained in relation to the APA processes, where applicable.

The literature review identifies a lack within mainstream academic literature looking at APA processes in an empirical way. Further, no academic literature on New Zealand's APA process has been identified. These factors all justify the research questions proposed in this thesis:

RQ1: What are the steps involved in obtaining a New Zealand APA?

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

Chapter 3: Research Questions, Methods and Methodology

3.1 Introduction

This chapter introduces the research questions and the theoretical framework, methodology and research methods utilised to answer these research questions. As mentioned previously, to the researcher's knowledge, there is no existing academic study on the subject of New Zealand Advance Pricing Agreements (APAs), a fact which also forms a motivation for the researcher to undertake this research. Section 3.2 of this chapter introduces the research questions to be investigated in in this study. Section 3.3 outlines the theoretical framework which provides guidance to the research project. Section 3.4 introduces the qualitative methodology used to answer the research questions. A discussion of the research methods employed to undertake this research project is provided under Section 3.5. Section 3.6 summarises the chapter.

3.2 Research Questions

This project seeks to evaluate the New Zealand APA process initiated by the Inland Revenue Department (IRD). This evaluation will consist of three main parts:

- documentation of the New Zealand APA process itself;
- a critical evaluation of certain aspects of the process from various parties' points-of-view; and
- a comparative analysis of selected overseas' APA processes relative to the New Zealand APA process.

The research project proposes three research questions:

RQ1: What are the steps involved in obtaining a New Zealand APA?

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

To answer *RQ1*, a literature review is conducted to document the steps involved in obtaining a New Zealand APA. The process is further documented through conducting semi-structured interviews with both personnel from the IRD and tax practitioners from the Big 4 accounting firms.⁵⁹ Critical comments regarding certain aspects of the process are to be gathered through the interviews to reflect on the various critical aspects of the process, which will in turn answer *RQ2*. *RQ3* will be answered by conducting a comparative analysis with a number of selected tax jurisdictions' APA processes. The selected tax jurisdictions are Australia, the United Kingdom (UK) and the United States (US). Further explanations as to how and why these methods are used will be provided throughout the remainder of this chapter. Also, the reasons why the previously mentioned tax jurisdictions were chosen as comparatives will be explained under section 3.5.1, 'Case Study', of this chapter.

3.3 Theoretical Framework

The theoretical framework used in the thesis is institutional theory. This theoretical framework is further supplemented by using agency theory. These theories are explained later in this section. Gernon and Olusegun Wallace (1995) explain the concept of 'theory' as a system which provides for the orderly arrangement and examination of data. Reference to the theoretical framework in this study facilitates the evaluation of the New Zealand APA process. It should be noted that other theoretical frameworks have the potential to provide insights and assist in evaluating the New Zealand APA process. As a priori interpretation, the researcher

⁵⁹ Deloitte, PwC, Ernst & Young and KPMG.

anticipates that there will be a difference between the interpretations made by the IRD on certain aspects of the APA process, compared to those interpretations made by tax practitioners.

Scott (1987) mentions that it is important to recognise that there is not one definition of institutional theory and that several variants exist. Selznick (1996) explains that institutional theory seeks to understand patterns of organizational interaction and adaptation in order to explain environmental responses. “Institutions may adopt a number of forms including formal government structures, legal institutions or social institutions” (Marriott, 2008, p.39). For the purposes of this research, the IRD can be thought of as a ‘formal institution’ and tax practitioners collectively as a ‘social institution’.

Two main approaches define the field of institutional theory: ‘new institutionalism’ and ‘old institutionalism’ (Marriott, 2008). Peter (1993) mentions that the approach followed by old institutionalism required political institutions to be formed in order to structure and influence the behaviour of individuals towards a better end. “However, old institutionalism did not encourage the development of concepts that would facilitate comparative research and advance explanatory theory” (Marriott, 2008, p.44). ‘New institutionalism’ emerged in response. New institutionalism looked at the role of institutions within society (Hall, 1986). There are a number of variants of new institutionalism.⁶⁰ This thesis’s theoretical framework will draw from rational choice institutionalism. Other variants of new institutionalism are not considered in this thesis.

Marriott (2008) mentions that formal institutions, which are viewed as constraining the behaviour of actors, is the primary focus of rational choice institutionalism. This sub theory was largely inspired by rational choice analysts seeking to examine how the rules of the US Congress affect the behaviour of legislators (Hall & Taylor, 1996). Analysts turned to

⁶⁰ Peters (1999) identifies six approaches. These are: normative institutionalism, rational choice institutionalism, historical institutionalism, empirical institutionalism, international institutionalism and societal institutionalism.

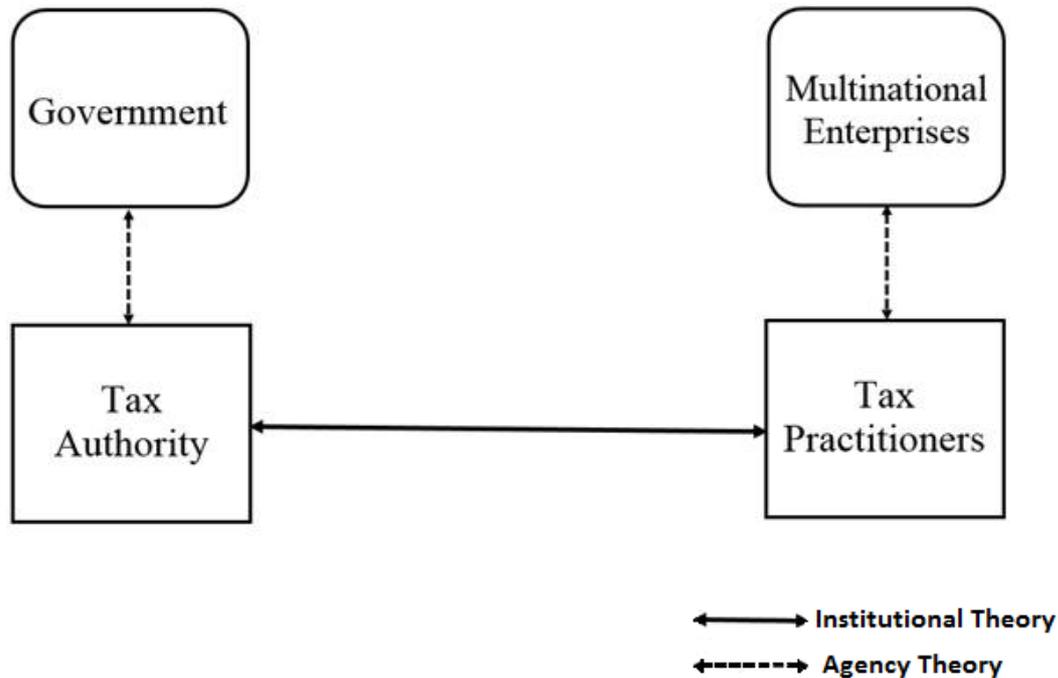
institutions to examine this affect. Possible answers emerged as a result of examining Congressional institutions and how they were structured and how Congress designs institutional arrangements to achieve favoured outcomes (Hall & Taylor, 1996). This approach of analysing how a formal institution structures its institutions and policies which accordingly affects the behaviours of involved actors, is a key reason for the adoption of this theory in the thesis.

The previously mentioned approach allows the researcher to evaluate the relationship between the New Zealand Government (the formal institution) and how the laws and policies in place affect the behaviour of MNEs (the actors). To put this statement into the context of evaluating the relationship between the IRD and tax practitioners, agency theory is used.

Agency theory “is directed at the ubiquitous agency relationship, in which one party (the principal) delegates work to another (the agent), who performs that work” (Eisenhardt, 1989). Jensen and Meckling (1976) use the metaphor of a contract to explain the relationship described by agency theory. Mehafdi (1990) argues that undertaking transfer pricing studies requires the researcher to look at accounting solutions with explanations from behavioural science (which includes agency theory). In summary, agency theory is concerned with resolving issues that can exist between principals (for example MNEs) and agents of the principal (for example tax practitioners representing the MNE).

This theory is not the focus of this study; however it complements the primary theoretical framework used to facilitate the evaluation of the New Zealand APA process – rational choice institutionalism. It is assumed that the IRD (the agent) work for the best interest of the New Zealand Government (the principal) in administering the tax laws passed by the government. Also, it is assumed that tax practitioners (the agent) work for the best interest of MNEs (the principal) in managing their tax affairs.

Figure 3.1 Theoretical Framework



(Source: Author)

Thus, it can be concluded that rational choice institutionalism allows the researcher to evaluate the relationship between the IRD (the formal institution) and how the APA process (institutional arrangement) affects the behaviour of tax practitioners (actors). Figure 3.1 above illustrates the theoretical framework of this thesis. In short, the theoretical framework will allow the researcher to observe critical evaluations of the New Zealand APA process from the perspectives of the IRD and tax practitioners.

3.4 Methodology

The researcher's ontological viewpoint in this thesis is that of a critical realist. The intention of this viewpoint is to provide an understanding of reality based on the subjective interpretations made by the researcher. Critical realism seeks to understand the social world, while still recognising that reality exists (Bryman & Bell, 2011). Researchers with a critical realist ontological viewpoint, usually have an epistemological position that lays between

positivism and interpretivism; sometimes referred to as 'post-positivism' (McKerchar, 2010). McKerchar (2010) mentions that such epistemological position allows for the 'real' reality to be explored by seeking to answer the "how" and "why" questions in order to understand the complex arrangements underlying the researcher's study.

The unpublished thesis of Moll (2003) is an example where critical realism can be seen in the context of accounting. Moll (2003) employed existing theories in her thesis that allowed her to tailor a unique framework to the aims and objectives of her research. A similar approach was used by the researcher in order to explore the New Zealand APA process.

Choosing a methodological approach is appropriate once the researcher has identified the appropriate research framework, and the aims and context of the research, alongside the researcher's ontological and epistemological beliefs (McKerchar, 2010). McKerchar (2010, p.90) describes methodology as the "overall guide to how you are going to go about your research and the platform from which you will choose your method(s)". In other words, the choice of the methodology will influence the choice of the method(s) to be employed to answer the three research questions. The methodology employed in this research project is qualitative.

McKerchar (2010 p.94), stipulates that qualitative research "focuses on the building of theories, the identification of patterns, and the making of both meaningful and analytical generalisations that are limited in context to the population studied". Such methodology seeks to build theories using inductive reasoning, rather than disapproving theory by deductive reasoning and empirical means (McKerchar, 2010). Thus, it can be said that the reality is always subjective, rather than objective.

This research project is exploratory in nature, so using qualitative information is better suited in developing a foundation than quantitative data. An exploratory study will allow the researcher to examine the New Zealand APA process in depth. King and Harrocks (2010)

explain that in qualitative research, meaningful differences and experiences can be captured by using a variety of participants who are selected on the basis of their relation to the research topic. Unlike quantitative research, generalizability is established when a sample that is statistically representative of the population to be studied has been obtained (McKerchar, 2010). Further, the objective nature of quantitative research is not suitable for the purposes of this research project.

In order to capture the perceptions' of tax practitioners and the tax authority, a qualitative methodology is the most appropriate. This also allows for an inductive approach to evaluate the subject matters involved. Statistical analysis of the data obtained from the interviewees would undermine the understanding of why and how the interviewees responded. Further, exploring other tax jurisdictions' APA processes is best undertaken using qualitative research methods.

3.5 Research Methods

The research questions used in this study are answered using the following research methods and approaches.

3.5.1 Case Study

The study utilises a comparative case study analysis of three selected tax jurisdictions' APA processes, alongside the New Zealand APA process being the focus of attention. McKerchar (2010, p.102), states that a case study "generally involves a researcher undertaking an in-depth exploration of a program, an event, an activity, or a process concerning one or more individuals". Yin (2009, p.13) describes a case study as an empirical inquiry that investigates a contemporary phenomenon within its real-life context.

The subjects of the comparative case study have been carefully selected through a process of preliminary research. The process involved finding tax jurisdictions with developed and mature APA processes. The tax jurisdictions identified were further filtered by their comparability to New Zealand's APA process. Determining if information was publicly available and able to be obtained in relation to the tax jurisdictions' APA processes was a major consideration in selecting tax jurisdictions as comparatives. Another major consideration was the jurisdictions' rankings in terms of the amount of trade with New Zealand.⁶¹ The preliminary research yielded three countries: Australia, the UK and the US. As a precautionary note, this is not an exhaustive list of tax jurisdictions, and there are other countries that could have been studied and potentially added new insights for future research. However, as the research is in its exploratory stage, what is currently being proposed should be sufficient in promoting New Zealand's APA process as a comparative for future research.

A literature review was conducted on each of the tax jurisdictions' APA processes identified above and is outlined in Chapter 2, Literature Review, of this thesis. The literature review of these tax jurisdictions' APA processes is also used to formulate many of the interview questions for the interviews conducted as part of this study.

Comparisons of different legal systems of the world can be sought by way of comparative law studies (Zweigert & Kotz, 1998). Furthermore, a country's tax policy can benefit from comparative analysis (Thuronyi, 2003). A country can learn from different countries' experiences with a certain program. Once the literature review was complete, a comparative case study was undertaken to draw out and aggregate various critical aspects of each tax jurisdictions' APA process in a table. This table (Table 4.2) is presented in Chapter 4, 'Research Findings and Discussion', of this thesis. The primary purpose of the table is to provide an

⁶¹ This consideration was deemed important by the researcher as it was assumed that APAs (bilateral APAs and multilateral APAs in this case) would be more popular with New Zealand's major trading partners.

overview of how the New Zealand APA process compares to those other processes selected as part of this comparative study.

As mentioned previously, a case study approach is preferred in examining contemporary events. Although a focus has been given to the comparative analysis part of this research, the study as a whole can be further classified as a case study. Yin (2009) points out a unique strength to case studies being able to deal with a full variety of evidence (documents, artefacts, interviews, and observations).

3.5.2 Documentary Analysis

Documentary analysis was used as a primary research method in this study. This method was greatly beneficial in providing information about the New Zealand APA process and the APA processes of those jurisdictions used as comparatives in this study. Furthermore, it assisted in formulating the interview questions used as part of this study (explained under section 3.5.3, ‘Interviews’).

Scott (1990, p.12) describes a document in its most general sense as a “written text”. He argues that the quality of the evidence available for analysis is the foundation of scientific research and can be achieved by using a simple set of criteria. The author sets out four criteria (Scott, 1990, p.6):

1. Authenticity. Is the evidence genuine and of unquestionable origin?
2. Credibility. Is the evidence free from error and distortion?
3. Representativeness. Is the evidence typical of its kind, and, if not, is the extent of its untypicality known?
4. Meaning. Is the evidence clear and comprehensible?

This study investigated published materials from various government agencies, including the IRD, the Australian Taxation Office (ATO), the UK’s Her Majesty’s Revenue & Customs

(HMRC), and the US's Internal Revenue Service (IRS). These documents provide some of the best sources to understand and gain insight of the APA process of each of the comparative jurisdictions considered in this study. Other sources looked at included publications by the accounting profession and existing academic literature on APAs. Documents published by the various government agencies can be seen as organisational documents. Bryman and Bell (2011) observed that such documents are heterogeneous; although they are still important in informing researchers on certain organisations when examined.

The organisational documents used in this study were set against the four criteria argued by Scott (1990). They were directly sourced from each organisation to ensure authenticity. These documents are perceived as having issues with their credibility. Whilst these documents may have been free of error, they have been written by the tax agencies of each jurisdiction and may contain their biases as a result. Therefore, it is not possible to accept that the organisational documents are necessarily completely credible as distortions to information about each APA process may exist.

The representativeness of the data was closely considered as most information about any APA process came from one source (for example, information about the UK's APA process mainly came from publications by the HMRC). Bryman and Bell (2011, p.560) note that organisational documents may not provide an "... accurate representation of how different organisational actors perceive the situations in which they are involved". The documents produced by these tax agencies were 'typical' in nature. They provide one of the best sources of data, and to contain information that may have been hard, if not impossible, to replicate elsewhere. Finally, the organisational documents analysed are perceived as being clear and comprehensible.

Scott's (1990) four criteria were used against other documents analysed as part of this study. Documents made available to the researcher were only analysed in this study.

It is important to note that the documents were analysed through one interpretation, which may have led to the results being influenced by the researcher's own views and subjective biases. Much of the information provided in these documents was central to the research questions asked in the interviews with both IRD personnel and New Zealand tax practitioners. The researcher examines the IRD staff and Big 4 tax practitioners' views, which in turn limits any subjective biases.

3.5.3 Interviews

The last (and main) research method utilised in this study was semi-structured interviews. Due to the exploratory nature of this project, semi-structured interviews were believed to be the most appropriate method to provide the researcher with more in depth answers and a greater exploration of the subject matter. A greater emphasis can be placed on the interviewees' points-of-view and opinions on the subject matter when conducting interviews (Bryman & Bell, 2011). Liamputtong (2009) observed that the main strength of conducting in-depth interviews is the opportunity given to the researcher to probe and clarify meanings relevant to the research project. King and Harrocks (2010, p.53) state that 'probing' seeks to add depth to interview data. It is important however, to note that probing to obtain real depth in interview data can be overdone (King & Harrocks, 2010). This may result in obtaining a large amount of detail in an area which is of limited relevance to the research question(s).

Mason (2010) and Dworkin (2012) state that the saturation point is reached when no new relevant data should be obtained by conducting a further interview. Interview based research should have a minimum of twelve participants; however if the participant interviewees are highly homogenous then six participants would be sufficient (Guest, Bunce & Johnson, 2006). The total number of interviews conducted with IRD staff and tax practitioners was eight for this study. By the eighth interview, it was believed that the saturation point had been reached. No new knowledge or insights is expected be obtained from conducting any further interviews.

Section 3.5.3.1, 'Participants', provides a background of the participants who partook in this study.

3.5.3.1 Participants

Whilst the APA program is used by taxpayers, specifically Multinational Enterprises (MNEs) and their tax agents, it was considered appropriate to interview IRD staff and tax practitioners for the purposes of this research. The eight participants were made up of three IRD staff and five tax practitioners from the Big 4 accounting firms.⁶² It was considered appropriate to interview the IRD as the APA program had been initiated by the tax authority itself. The three IRD staff interviewed were all senior transfer pricing personnel with extensive experience in dealing with the IRD's APA program.

Tax practitioners from the Big 4 firms were ideally placed to evaluate the APA program, being the main representatives for MNEs in their transfer pricing affairs. Tax practitioners were only chosen from the Big 4 accounting firms as it was believed that these firms captured the majority of the MNE market in New Zealand. This was confirmed by the IRD prior to commencing any interviews. One participant from each of the Big 4 accounting firms was interviewed. The researcher was also presented with an opportunity to interview a second tax practitioner, thus a total of five participants from the Big 4 accounting firms. All five tax practitioners were of either a 'Partner' or 'Tax Director' job title at their firm. They all had extensive experience in transfer pricing and dealing with the New Zealand APA program.

The practitioners were sourced after searching the websites of the Big 4 accounting firms. Direct contact with intended participants was made by way of email. Seven out of the eight participants agreed to have the interview conducted face-to-face at their workplace. One of the interviews was conducted by way of remote video interviewing via Skype. This was due to the

⁶² Deloitte, PwC, Ernst & Young and KPMG.

participant's location and other resource constraints (time and expense). King and Horrocks (2010, p.80) state that "the most obvious advantage of remote interviewing is that it can facilitate the inclusion of participants who are geographically distant from the interviewer ...".

These interviews were all audio recorded and transcribed afterwards. The transcribed data was coded thematically in order to explore any themes and allow them to be analysed in detail (McKerchar, 2010). Boyatzis (1998) stipulates that thematic analysis can be used with any form of qualitative study. Thematic analysis seeks to search for themes or patterns in a data set (Braun & Clarke, 2006).

Braun & Clarke (2006) provide a step-by step guide on how to conduct a thematic analysis:

1. Familiarise yourself with your data: as the data had been collected by the researcher, it is recommended that the entire set of data is read through at least once after it has been transcribed in order to search for patterns and themes.
2. Generate initial codes: this is where a generic list of ideas and codes is generated from reading and becoming familiar with the data set on hand. Each generic code identified is copied from the transcribed data set and placed in a separate document with a unique title or identifying code.
3. Search for themes: This step involves analysing the data in a much broader manner where themes and patterns are identified, instead of just codes. The relationships between the codes are examined and then labelled as either themes or sub-themes.
4. Review the themes: The themes identified need to be refined. The researcher needs to ensure they are presented in a coherent manner. Some themes at this stage may be removed if deemed not suitable, and others may be added. At this stage, the researcher needs to have a good understanding of all the themes identified and how they fit in the overall study they are conducting.

5. Define and name the themes: Here, the scope of each individual theme needs to be defined, including what sub-themes that will be presented under each theme. A written detailed analysis is essential in defining the theme and what it does not include; each theme needs to be given a name too. “Names need to be concise, punchy, and immediately give the reader a sense of what the theme is about” (Braun & Clarke, 2006, p.23).
6. Produce the report: This involves the write-up of the final report where the themes are presented, alongside data-extracts from the original data set. The themes need to be written-up in a logical and coherent manner to convince the reader of the validity of the analysis undertaken. Further, the data-extracts chosen need to relate directly to the theme being presented. Enough data extracts should be included in the write-up to prove the prevalence of the theme.

The themes and data extracts obtained from the interview data are presented throughout Chapter 4, ‘Research Findings and Discussion’, of this thesis in a logical and coherent manner as determined by the researcher. The research questions asked in the interviews were based on the research questions of this study. The research questions looked to evaluate the New Zealand APA process. The literature set out in Chapter 2 assisted the researcher in formulating many of the questions asked in the interviews (especially those studies of Markham (2012) and Avoseh (2014)). The questions were asked in a thematic order. This allowed the researcher to facilitate the interviews and provided a point of reference (McKerchar, 2010).

The interviews conducted in this study have been granted ethics approval by the Human Ethics Committee of the University of Canterbury. The approval letter is set out in Appendix 4. All participants were provided with an information sheet and consent form before commencing the interview. The information sheet and consent form are set out in Appendices 5 and 6.

Confidentiality has been granted to all participants involved in the interviews. No information mentioned in this research identifies a person by their name. Also, in relation to interviewees from the Big 4, no information identifies any of the interviewees' accounting firm.

3.6 Summary and Conclusions

The New Zealand APA process offered a great opportunity to research. In order to evaluate the New Zealand APA process, it was decided to conduct eight interviews with professionals from the IRD (3 participants) and tax practitioners from the Big 4 accounting firms (5 participants). It was considered appropriate to interview the IRD as the APA program had been initiated by the tax authority itself. Tax practitioners were only chosen from the Big 4 accounting firms as these firms captured the majority of the MNE market in New Zealand. This was confirmed by the IRD prior to conducting any interviews.

The overall theoretical framework used in this thesis was chosen so as to assist the researcher in evaluating New Zealand's APA process. Rational choice institutionalism and agency theory will allow the researcher to observe critical evaluations of the APA process from the perspectives of the IRD and tax practitioners from the Big 4 accounting firms. Documentary analysis was used as a primary analysis method in this study. This enabled information to be obtained from various sources about the New Zealand APA process and the APA processes of those jurisdictions used as comparatives in this study. Australia, the UK, and the US were selected to be the comparative tax jurisdictions in this study. Documentary analysis also assisted the researcher in formulating the interview questions used in the interviews. The evaluations gathered throughout this study, alongside with the comparative case study are presented in Chapter 4, 'Research Findings and Discussion'.

Chapter 4: Research Findings and Discussion

4.1 Introduction

This chapter presents the interview findings conducted with eight tax professionals and practitioners from the Inland Revenue Department (IRD) and the Big 4 accounting firms⁶³ in New Zealand. The main purpose of the interviews, as explained in Chapter 3, was to evaluate the New Zealand Advance Pricing Agreement (APA) process and gain an in depth understanding on certain aspects of it from interviewees' perspective. The interview findings are presented in this Chapter, under section 4.2 'Interview Findings', to mainly answer the second research question:

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

Section 4.3 of this chapter presents a summary table and a brief discussion to answer this thesis's third research question:

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

Table 4.1 on the next page provides an overview of the interviewees who participated in this study.

⁶³ Deloitte, PwC, Ernst & Young and KPMG.

Table 4.1 Overview of the interviewees

Type of Tax Professional	Interview Method	Reference in the Thesis
IRD	Face-to-Face	Tax Professional A
IRD	Face-to-Face	Tax Professional B
IRD	Remote Video Interview	Tax Professional C
Big 4	Face-to-Face	Tax Professional D
Big 4	Face-to-Face	Tax Professional E
Big 4	Face-to-Face	Tax Professional F
Big 4	Face-to-Face	Tax Professional G
Big 4	Face-to-Face	Tax Professional H

4.2 Interview Findings

Several themes emerged from the interviews. The following sections analyse the information under each of these identified themes to provide insights about the New Zealand APA process. The themes are placed in a logical order as determined by the researcher.

4.2.1 New Zealand Transfer Pricing Environment

All interviewees were initially asked to provide an overview of the New Zealand transfer pricing environment and comment on how robust the rules in place are in terms of preventing revenue leakage. As a whole, the transfer pricing rules in place were perceived as being robust and has served New Zealand well in protecting its Multinational Enterprise (MNE) tax base. Most Big 4 tax practitioners mentioned that the IRD's transfer pricing focus has always been on the 'top-end' MNEs.

Interviewees compared the New Zealand transfer pricing landscape to other tax jurisdictions' landscapes and how it operates differently. Many of the tax practitioners believed that Australia was most relevant to New Zealand's transfer pricing landscape:

"... in terms of the New Zealand environment, about 50% of our trade investment is in Australia ...in terms of action or activity, it is very much Trans-Tasman".

(Tax Professional A, IRD)

While all interviewees agreed on the robustness of the rules in place, one Big 4 tax practitioner believed that there may be a future risk of greater leakage of tax revenue to the Australian side "given how strong Australia is in terms of enforcement" (Tax Professional E, Big 4). The practitioner believed it is a matter the IRD is looking to address.

All IRD staff commented about the revenue authority's generic approach to transfer pricing and how compliance is being addressed in today's environment. One IRD practitioner raised the point on how New Zealand businesses that are part of a global group can often be influenced by the parent's group policies:

"We have seen a great bigger change in the way companies are operating here ...they are no longer left alone. They are part of a group. If there are certain [tax] policies, maybe not intentionally that they are aggressive, but whatever stance they are taking at the head level is coming down to the [New Zealand] subsidiary as well".

(Tax Professional B, IRD)

Perhaps the most important point made under this theme was in relation to the OECD's Base Erosion and Profiting Shifting (BEPS) project. All interviewees made reference to the project and the uncertainty it has created in the New Zealand and global transfer pricing environment. Many Big 4 tax practitioners saw the need for the IRD to revisit the transfer pricing rules in

place to better align with the interpretations made by the revenue authority itself, especially in the light of BEPS. Practitioners were uncertain of the IRD's intention to change existing laws or adopt any new ones, as one interviewee commented:

“We have seen a bit of a change from an advisor point of view ...in the last twelve to eighteen months particularly around ...the OECD's work around BEPS ...where other jurisdictions are legislating for needing to have contemporaneous documentation ...the IRD are signalling that they are not going to go down that path”.

(Tax Professional D, Big 4)

From the IRD's point of view, one practitioner mentioned that the revenue authority views the OECD as the standard setter and especially in terms of transfer pricing. The practitioner further commented on New Zealand's current approach and the OECD stating:

“ ...what we are seeing is the OECD catching up with where we have gone in relation to our emphasis on commercial reality and substance over form”.

(Tax Professional A, IRD)

Overall, New Zealand's transfer pricing rules in place were perceived by the interviewees from the IRD and Big 4 accounting firms as being robust in protecting New Zealand's MNE tax base and in preventing tax revenue leakage. However, there were uncertainties, especially by the Big 4 tax practitioners interviewed, about the transfer pricing environment with the OECD's current BEPS Action Plan. Also, tax practitioners from the Big 4 accounting firms have expressed concerns over the IRD's approach on addressing future changes to transfer pricing practices and how some of the interpretations made fit within the current laws in place. The BEPS Action Plan, proposed by the OECD, inherently provides uncertainties, not just to the New Zealand transfer pricing environment, but to the global environment as a whole. These observations suggest that the IRD should engage with tax practitioners from the Big 4

accounting firms and address any issues or interpretations they see not aligning with the current laws in place.

4.2.2 Purpose of an APA

4.2.2.1 Certainty

All participants agreed that certainty was the main purpose for an MNE to conclude an APA. Many of the participants raised further points beyond certainty as to why interested parties may want to conclude an APA. One point that was raised by a tax practitioner from a Big 4 accounting firm was credibility. The tax practitioner saw the benefit of a MNE holding an APA with the IRD is that it increases its global credibility overall:

“It is certainty, but also I think if talking about New Zealand owned groups it is sort of a quality mark on the global position as well. They [MNEs] go to overseas offices and actually say we have had this reviewed by IRD and I think it is a good reputation internationally”.

(Tax Professional E, Big 4)

Professionals from the IRD mentioned benefits unique to the revenue authority itself by having a number of APAs concluded with MNEs. It was seen as a more efficient way to manage compliance among MNEs given the IRD’s limited resources. One IRD professional commented that compliance levels are being increased by having more MNEs enter into the APA program. MNEs that complete an APA are required to submit annual reports – annual compliance report - and supporting evidence to confirm adherence to the agreed terms and conditions (Woodhouse, 2016). The annual compliance report allows the IRD to monitor MNEs and ensure they are complying with the terms of their APA in an effective and efficient manner. In addition, interviewees agreed that APAs are a better way to address risk areas and issues, rather than going through a transfer pricing audit:

“...APAs are usually for five years ...once you have looked at a company that has entered into an APA, it reduces the number of cases you [the IRD] have to look at ...our [the IRD’s] review time is saved”. “Second thing ...going through a dispute is a very long process and very costly for both parties; we are saving time as well”.

(Tax Professional B, IRD)

Many of the interviewees praised the way the APA program looks at addressing issues in a cooperative manner. All interviewees agreed that APAs predominantly look at complex transactions. Reaching upfront agreement on the treatment of these complex transactions from a transfer pricing perspective, feeds into the benefit of certainty that is provided by an APA. In respect of the fact that a unilateral APA is binding on the Commissioner and not the taxpayer, one tax practitioner from a Big 4 firm described the unilateral APA as an insurance policy:

“I think it is a good thing ...to be able to go along and get agreement with a tax authority and know that you kind of have an insurance policy that you are not going to be disrupted for months by an audit”.

(Tax Professional F, Big 4)

4.2.3 Can an APA trigger a Transfer Pricing Audit?

As evident from the literature examined about the Australian, the United Kingdom (UK) and the United States’ (US) APA processes,⁶⁴ MNEs and their tax practitioners in those jurisdictions have raised concerns about the possibility of an APA triggering a transfer pricing audit (Avoseh, 2014; Markham, 2012). Interviewees were asked to comment about the APA process serving as a ‘carrot-and-stick’⁶⁵ policy when a MNE applies for an APA. Concluding

⁶⁴ Refer Chapter 2: ‘Literature Review’ of this thesis.

⁶⁵ Fran, Seeberger and O’Reilly (2004, p.1940) note that this approach “...refers to the use of a combination of positive and negative reinforcement: One can persuade a donkey to move either by dangling a carrot in front of it or by striking it with a stick”.

an APA represents the ‘carrot’ and not reaching agreement results in a transfer pricing audit which is the ‘stick’. All Big 4 tax practitioners interviewed agreed that an APA request may result in a transfer pricing audit. Likewise, the IRD professionals interviewed confirmed that some APA requests may proceed to a transfer pricing audit.

None of the Big 4 tax practitioners interviewed expressed direct concern over the IRD being aggressive in terms of having their APA requests turn into transfer pricing audits. One interviewee from a Big 4 accounting firm explained:

“[An APA request turning into a transfer pricing audit] has happened. I would say perhaps justifiably so. So I don’t think it was like being bullied into it, I do not think the IRD does that.”

(Tax Professional G, Big 4)

Four out of the five tax practitioners from the Big 4 firms interviewed affirmed the degree of involvement required with the revenue authority in order to conclude an APA. Because it is an ‘all-cards-on-the-table’ approach, the four tax practitioners mentioned that they are upfront with their clients before negotiating an APA with the tax authority about the risk of having their prior years open for a transfer pricing audit. One Big 4 tax practitioner further commented about when advising clients to consider an APA:

“... if you did not give them [MNE clients] a heads up telling them what we are doing is pretty aggressive ...one of the potential outcomes might be an audit. You would be a poor advisor if you fooled your client to enter one ...as an advisor if you are too aggressive and your clients are too aggressive and you are not upfront with the revenue, you run the risk of ruining your personal brand with the revenue”.

(Tax Professional E, Big 4)

The IRD professionals interviewed believed APA requests containing aggressive proposals would result in a transfer pricing audit as a consequence. One IRD professional raised a point about transfer pricing audits in the context of APAs as a way for encouraging engagement:

“[The APA process] require[s] them [MNEs] to actually engage and to be prepared to provide us [the revenue authority] with information that is obviously necessary to get that APA”.

(Tax Professional A, IRD).

This approach also reinforces the legislative requirement under Section 91ED(1B) of the Tax Administration Act 1994, which requires applicants to be more involved in the process of obtaining an APA in comparison to other private ruling applications.⁶⁶

Overall, the IRD has its APA program operating in a manner where a transfer pricing audit will usually be the result of no agreement being reached on any certain APA. The primary theoretical framework used in this thesis, rational choice institutionalism, assists in examining the ‘carrot and stick’ policy used by the IRD and how it effects the behaviours of applicant MNEs in the New Zealand transfer pricing landscape. The IRD believe it is necessary that aggressive APA proposals proceed to a transfer pricing audit. Tax practitioners seem to be more concerned about their reputation with their clients and the revenue authority in some instances. In the context of a ‘carrot-and-stick’ approach, the IRD appear to be successful in influencing tax practitioners’ behaviour, and consequently MNEs’ behaviour, requiring them to be fully involved throughout the APA process until agreement is reached. This fits well with this thesis’s theoretical framework. The IRD (the formal institution) have embedded the ‘carrot

⁶⁶ Discussed in more detail in Chapter 2: Literature Review, section 2.5.1.3, ‘New Zealand APA Process’.

and stick' policy within their APA process (institutional arrangement), which in turn influences the behaviour of MNEs (actors).

4.2.4 Time and Cost of Filing an APA

Two aspects of filing an APA are discussed further, time and cost. The first aspect to be discussed is the timing of the APA process. The IRD aims to complete unilateral APAs within six months from the date a formal application is lodged (Inland Revenue, 2015a). The six month timeframe is not a legislative timeframe, meaning the IRD is not bound to complete any unilateral APAs within that timeframe. All tax practitioners from the Big 4 accounting firms interviewed had no concerns regarding unilateral APAs not having a legislative timeframe that binds the IRD. Further none of Big 4 interviewees blamed the IRD for not being able to give an indication on when a bilateral or multilateral APA will be completed. This was due to the nature of such APAs where another tax authority is involved and the IRD does not have any control over the process as a whole. Some other interesting points were made by interviewees from the Big 4 accounting firms in relation to the time aspect of the APA process. Some of the comments made were:

“Six months is seen as a pretty good standard ...for me the timing is what indication I have given my client and how urgent they want it and how I can impress them ...they [the IRD] are pretty good with meeting the timeline”.

(Tax Professional F, Big 4)

“All unilaterals I have done except one have been settled within six months. The one that was not... no agreement [was] reached because the issues were very complex, but I think the IRD do try and stick to their six month timeline. Obviously with a bilateral it is different because you have another authority on the other side. They do try and

keep it with Australia under six months and if it does not there usually is a reason for it. It does not worry me that it [the timeframe] is not binding.

(Tax Professional D, Big 4)

The IRD professionals interviewed likewise agreed that they have been able to meet the six month timeframe for all unilateral APAs. One of the IRD professionals said it is mainly due to the pre-lodgement phase where a lot of the work is done upfront. The six month deadline starts once the MNE lodges a formal application. One Big 4 tax practitioner, despite praising the IRD for being able to meet the six month timeline, criticised the revenue authority for being under resourced which has caused some time issues. The practitioner mentioned that sometimes you are not able to have a pre application meeting with the IRD until three or four months from the time you ask for one. The Big 4 practitioner stated that “maybe having a binding time would force the IRD to put more resourcing” (Tax Professional E, Big 4).

The same reasons were mentioned by the IRD professionals interviewed in relation to bilateral and multilateral APAs. One IRD professional elaborated on bilaterals concluded with Australia, commenting:

“Most of our bilaterals are with Australia because they are our [New Zealand’s] major trading partner. [Bilaterals with Australia are] not usually concluded within six months, they usually take between twelve to fourteen months ...they have much different processes than us and that is why it takes much longer, especially with their governance processes ...the reason being they are much bigger than us and they operate under a different model. We [the IRD] have kept it centralised”.

(Tax Professional B, IRD)

In respect of the second aspect discussed under this theme is the cost associated with filing an APA. All interviewees agreed there are material costs involved in obtaining APAs, however in

their view, it is still worth obtaining one. The IRD only charge a minimal application fee to apply for an APA; no other fees are charged. All IRD professionals interviewed mentioned that unilateral APAs should not cost much more than what it costs to prepare ‘adequate’ transfer pricing documentation from the IRD’s perspective. Although the requirement to keep transfer pricing documentation is not legislated for in New Zealand, one IRD professional stated that “they [MNEs] have to be able to support the tax position in their tax return” (Tax Professional B, IRD). Therefore, transfer pricing documentation is the most essential component of any APA application. As one Big 4 tax practitioner commented:

“The transfer pricing documentation is an essential component of an APA application because it actually tells you the story and tells you what the IRD needs to test”.

(Tax Professional G, Big 4)

The same Big 4 tax practitioner further commented that the transfer pricing documentation lodged as part of the APA application affects both the timeliness and cost aspects of the APA process. In their view, turning adequate transfer pricing documentation into an APA should not cost a lot more than the documentation itself. Further, adequate documentation provides the IRD with a better awareness of the MNEs’ business and what it should emphasis on, in the course of an APA, therefore saving time as well. An interesting point in relation to the adequacy of transfer pricing documentation provided by some MNEs was raised by one of the interviewees from the IRD:

“What happens with transfer pricing documentation is that they [MNEs] have pasted a lot of things from their website or when you look at their functional analysis where you talk about risk ...often the CA [Chartered Accountancy] firms use templates so we really need to verify what is happening ...we spend a lot of time asking to gain clarification”.

(Tax Professional B, IRD)

The IRD are required by law to charge a fee of 332 NZD for preparing private rulings, including APAs (Inland Revenue, 2013). The fact that the IRD do not charge anything material for an APA was seen as a selling point by a tax practitioner from a Big 4 accounting firm and an advantage, which increased demand. However, the tax practitioner mentioned that some MNEs still remain resistant to obtaining one, mainly due to the cost of APAs in overseas markets. The tax practitioner commented that “[the] overseas tax man expects an APA to cost him \$250,000 in New Zealand ...it actually does not cost that here but that is their mind set” (Tax Professional E, Big 4).

Although some practitioners raised interesting points about the timing and cost aspects of the APA process, overall both aspects were not a major concern to any of the interviewees. The 6-month timeframe, although not a legislative timeframe (Inland Revenue, 2015a), was not a major concern to any of the tax practitioners from the Big 4 accounting firms interviewed and the IRD were seen as being able to meet that timeframe. Further, the timing of bilateral and multilateral APAs received no criticism as all interviewees agreed that no one party to the APA had control over the process. Transfer pricing documentation that is adequate for revenue authority purposes can save both time and cost for the MNE and the IRD.

The perceptions of the IRD professionals and tax practitioners from the Big 4 accounting firms interviewed were positive overall about the time and cost aspects of the APA process. In the author’s view, the IRD need to consider applying additional resources towards its transfer pricing and APA program. This will allow for MNEs to be able to discuss their APA proposals with the revenue authority in a prompt and efficient manner. MNEs and Big 4 tax practitioners should ensure that all transfer pricing documentation that is provided as part of an APA application is adequate and that all transfer pricing risks are captured within those documents.

This will allow for the IRD to assess any risks and conclude APAs in an efficient and effective manner.

4.2.5 Potential use of APAs to New Zealand Customs

All interviewees, with the exception of one IRD professional, provided input on this theme. The IRD professional had no commentary to provide on the topic. All the interviewees, with the exception of one, are involved in or have had previous experience of dealing with the New Zealand Customs Service (NZ Customs). NZ Customs is a government agency charged with the security of New Zealand's borders, including the collection of GST on imported goods liable for such tax (New Zealand Customs Service, 2016a). Interviewees who commented on the potential use of APAs by NZ Customs saw a great benefit, especially in using the APA as a means to value imports. Where a transfer pricing adjustment results from an increase in the price of goods, in most cases this will result in a customs and GST impact which will need to be disclosed to NZ Customs (Deloitte, 2016).

The main starting point for all interviewees on the potential use of APAs was on how NZ Customs operate. All interviewees suggested the way the organisation works is a major issue when proposing transfer pricing and APAs as potential methods to value imports. Six out of the seven interviewees that responded referred to the Goods and Services Tax (GST) paid on the value of imported goods. The interviewees did not see the point of NZ Customs being overly concerned about the GST charged on these imported goods as it ends up being refunded back to the MNE by the IRD. Another major point made by all interviewees was the differing objectives of the IRD and NZ Customs. One tax practitioner from a Big 4 accounting firm commented:

“We want as a[n accounting] firm to administer customs and revenue without frustrations ...they are separately administered ...customs counts GST as part of their

revenue, yet it is not [revenue] because it goes [back to the MNE in the form of a refund]. I think if it was all aligned under one umbrella, someone can look at this and say why am I chasing a taxpayer for GST when it does not really matter”.

(Tax Professional F, Big 4)

Another tax practitioner from a Big 4 accounting firm summarised the difference in objectives, stating:

“So you have the IRD which wants more profits and you have Customs which wants a higher price ...they will never marry ...I think that is the natural tension. We [New Zealand] actually do not have much duties ...so it makes sense that customs makes sure that it is right. But I cannot understand why Customs get so conscious about it”.

(Tax Professional G, Big 4)

The same tax practitioner mentioned that NZ Customs may get overly concerned with valuation due to the organisation being concerned about statistics and the overall value of imports coming into New Zealand, which plays an essential part in Government reporting. The practitioner still believed that the process can be much quicker.

Three interviewees commented about the culture of NZ Customs and how this can be a difficulty in integrating APAs as part of the organisation’s valuation methods. The three interviewees viewed NZ Customs as a form of ‘police’. One of the interviewees commented:

“The Customs Department are quite different than the IRD ...they still wear uniforms and they think they are police and I think their value is on how many drugs they detect ...they can be quite difficult to deal with”.

(Tax Professional H, Big 4)

Two further differences were pointed out by interviewees that limit NZ Customs' ability to rely on APAs to value imports were, Custom NZ's limited tax knowledge and the legislative environment that the organisation operates in. Four interviewees believed that Customs NZ needs to have as a resource more tax 'savvy' individuals in order for APAs to work and be administered as an accepted valuation method. One tax practitioner from a Big 4 accounting firm concluded their view on NZ Customs using APAs, commenting: "[NZ] Customs are less tax oriented, less professional, a little less technical minded and certainly not commercially minded, so I think it is muddy" (Tax Professional F, Big 4).

The conservative legislative environment that NZ Customs operates in was viewed as a major constraint by six of the interviewees. The Customs and Excise Act 1996 is a principal legislation under which NZ Customs operate (New Zealand Customs Service, 2016). Interviewees mentioned that the prescriptive nature of the legislation does not allow for wide interpretation by NZ Customs, contrary to the Revenue Acts (e.g. Income Tax Act 2007) administered by the IRD. One Big 4 tax practitioner commented that transfer pricing requires a holistic approach and is not a 'black and white' matter.

Another interviewee from the IRD mentioned that with transfer pricing, five methods are used, whereas NZ Customs use seven. The issue raised was that NZ Customs is more restricted to the methods they can use. The IRD professional commented that following the OECD's Transfer Pricing Guidelines for transfer pricing allows for more freedom. "Whereas with [NZ] Customs it is bible" (Tax Professional B, IRD). Three interviewees believed that the OECD Transfer Pricing Guidelines, which New Zealand adopts, adds to the challenge of incorporating APAs into NZ Customs' day-to-day valuation practice. Some of the comments made were:

“It is a basic premise of the law ...our customs law is based on General Agreement Trade,⁶⁷ which New Zealand is signatory to. We [New Zealand] are also a signatory to the OECD and the two are inconsistent ...the whole basic principal legislation is different”.

(Tax Professional E, Big 4)

“APAs would absolutely be an attractive solution ...[however] the short answer is that you cannot align, it is impossible, the valuation rules that customs are subject to [with the ones the IRD use to conclude APAs]. They cannot be changed, they are subject to international agreements ...equally we [the IRD] cannot turn our backs someway to the OECD guidelines ...we [the IRD] are equally bound”.

(Tax Professional A, IRD)

All seven of the interviewees who commented on the potential use of APAs by NZ Customs saw potential benefits for all parties involved in terms of saving time and cost. Only one of the tax practitioners from a Big 4 accounting firm interviewed has used APAs as a means to value their MNE clients' imported goods and was successful in doing so with NZ Customs. This tax practitioner said that no formalised process exists to obtain valuations using APAs.

Throughout the interviews, two of the IRD professionals and one of the tax practitioners from a Big 4 accounting firm, raised an interesting point as to why NZ Customs should not be overly anxious in relying on valuations derived from the back of APAs. The interviewees mentioned that APAs provide a really strong indication that a certain MNE is compliant with their transfer pricing affairs. Therefore, their risk assessment by NZ Customs as an importer, and how their imported goods are being valued, should not be given great emphasis. One of the IRD

⁶⁷ General Agreement on Tariffs and Trade.

professionals interviewed made an interesting comment about MNEs that have an APA in place with the IRD:

“... we [the IRD] have graded them as low risk because they are being compliant. If we are doing that, we cannot enforce them [NZ Customs], but we encourage them to serious taxpayers in a different way that they are not that risky ...what happens is interesting, you know how we are saying [Base Erosion and Profit Shifting]BEPS or for transfer pricing we cannot see a fair amount of profit here [in New Zealand]. If they [NZ Customs] increase the value of goods, the cost of sales increases and because of that the profit reduces”.

(Tax Professional B, IRD)

This thesis’s theoretical framework (specifically agency theory) assumes that the IRD represents the New Zealand government to its best interests. As mentioned previously, NZ Customs is a government agency charged with the security of New Zealand’s borders, including the collection of GST on imported goods liable for such tax (New Zealand Customs Service, 2016a). Under this theme, the role and objectives of NZ Customs seem to not align well with those of the IRD. A natural tension exists between both organisations’ objectives. Incorporating APAs as an accepted valuation method by NZ Customs is not practical given the way the organisation currently works and the legislative environment it operates under. One Big 4 tax practitioner commented that it “is a dream to have [NZ] Customs incorporate APAs in their practice ...it is a global dream” (Tax Professional E, Big 4).

Perhaps, the New Zealand government needs to revisit the roles and objectives of both organisations to achieve better harmony between both, and ultimately a chance for APAs to be incorporated as part of NZ Customs’ valuation practice. According to rational choice institutionalism, government as a formal institution, would be able to achieve better outcomes

this way by positively influencing MNEs (the actors). Four of the interviewees saw hope in incorporating APAs into NZ Customs practice in light of the organisation's principal legislation, the Customs and Excise Act 1996, currently going through a major rewrite. The 'Customs and Excise Bill' is being drafted and is expected to be introduced in to New Zealand Parliament in October 2016 (New Zealand Customs Service, 2016b). A comment made by a tax practitioner sums up the views made by all four tax practitioners interviewed:

"The whole Customs [and Excise 1996] Act is going through rewrite and a reasonable chunk of that is coming around the valuation piece ...when they [NZ Customs] have their ability to give valuation rulings, then you could take an APA and potentially get a ruling on the back of that. [NZ] Customs do that have the legislative power yet [to give out such rulings]".

(Tax Professional E, Big 4)

An interesting point was raised by a tax practitioner about the transactions covered under APAs. They mentioned that most APAs cover transactions concerning intellectual property and related-party loans, which are not the type of imported goods NZ Customs deals with at borders. The point made by the tax practitioner was intended to highlight the limitations of applying all APAs to NZ Customs' valuation practice. The tax practitioner, however, mentioned that APAs could still be beneficial as NZ Customs should view those MNEs with APAs more favourably as they have a reduced risk factor.

Overall, the seven interviewees commenting on the potential use of APAs by NZ Customs saw benefits in using APAs as an accepted method to value imports by MNEs. The rewrite of the Customs and Excise Act 1996 may represent a major change on how NZ Customs work and operate. Further, it may remove many of the restrictions faced by NZ Customs in incorporating transfer pricing and APAs as part of its standard valuation practice. The rewrite may signify a

positive change to MNEs seeking to price their imports based on an APA held by that MNE. It is hoped the rewrite will allow NZ Customs to be more ‘liberal’ on how they can allocate their resources and be able to issue valuation rulings based on APAs. This will allow for better alignment between the IRD and NZ Customs’ overall objectives.

The IRD and tax practitioners seriously need to consider working closely with NZ Customs at the rewrite stage, and afterwards to ensure APAs can be incorporated as part of NZ Customs’ standard valuation practice. NZ Customs should also work on changing its stringent approach towards GST. Further, the organisation should utilise the resources spent by the IRD on concluding APAs with MNEs. These MNEs should be viewed as taxpayers with a low risk factor.

4.2.6 Are APAs Relevant to SMEs?

This study considered companies with a turnover under \$80million as SMEs.⁶⁸ All interviewees agreed that APAs are and can be relevant to SMEs with cross border related party transactions. All Big 4 tax practitioners agreed that the IRD are open to negotiate APAs with SME taxpayers. Five out of the eight interviewees mentioned that APAs are not popular among SMEs, mainly due to the cost of entering an APA. The complexity and risk involved with a transaction needs to justify entering one. One interviewee commented about the cost of APAs to SMEs:

“It is generally because of the cost of obtaining [an APA] ...the cost is actually out of whack compared to the adjustment to be made. Most SMEs would

⁶⁸ As part of the IRD’s Transfer Pricing focus for 2015 and 2016, the revenue authority’s top priority are ‘Large Enterprises’. ‘Large Enterprises’ comprise some 560 taxpayer groups with turnover in excess of NZD80 million (Inland Revenue, 2015e). The researcher considered the relevance of APAs to taxpayers outside this group (i.e. SMEs). All interviewees believed it was appropriate to classify taxpayers with a turnover of under NZD80 million as SMEs.

have straight forward transfer pricing documentation, with an exception to few industries”.

(Tax Professional H, Big 4)

Another Big 4 tax practitioner mentioned the following in relation to the type of APAs entered by SMEs:

“Usually they come in the form of unilateral APAs because bilaterals come too expensive ...the potential tax risk in the other jurisdiction is not necessarily worth it”.

(Tax Professional D, Big 4)

The same interviewee raised an interesting point about the complexity of cross border transactions among SMEs. The transactions dealt with can be more complex as these SMEs have not necessarily turned their mind to the treatment of the transaction upfront from a transfer pricing point of view. The tax practitioner believed that is was mainly due to the fact that they are dealing with people who are ‘more general finance [oriented] people, so they do not think about transfer pricing’.

One IRD professional mentioned that some MNEs have a group policy to conclude APAs in every country they operate in. Such policies explain why sometimes MNEs with a low turnover and sometimes even a low transfer pricing risk have APAs concluded with the IRD. One tax practitioner from a Big 4 accounting firm commented that from a governance perspective some of these SMEs ‘have ticked a box’ by concluding an APA with the IRD, regardless of their turnover.

Overall, SMEs have a place within New Zealand’s APA program. The main concern faced by such taxpayers is the cost of entering into an APA. As mentioned above, Big 4 tax practitioners would recommend APAs to such clients only where the transaction(s) in place are complex and are of a high risk. It is a positive aspect of the New Zealand APA program to accommodate for SMEs wanting to achieve certainty on their cross border transactions. Following the

recommendation of one interviewee from a Big 4 accounting firm who thought that no need exists for the IRD to initiate a separate APA process for SMEs. The interviewee believed that the IRD were efficient and able to tailor their questions to taxpayers' circumstances in cases of SME applicants wanting an APA.

4.2.7 The IRD – Tax Practitioner Relationship

This theme seeks to examine the relationship between the IRD and tax practitioners when interacting with one another throughout the APA process. Many critical evaluations were expressed throughout the interviews around the nature of the New Zealand APA process and the steps involved in obtaining one.

As previously mentioned in the introduction of this Chapter, the Interview Findings are presented in this Chapter to answer the second research question:

RQ2: Through interviews, what are various parties' critical evaluation of certain aspects of the New Zealand APA process?

The next section will add to the critical evaluations presented in this Chapter and will also seek to supplement answering the first research question of this thesis:

RQ1: What are the steps involved in obtaining a NZ APA?

4.2.7.1 Steps involved in obtaining a New Zealand APA

The IRD have not established any formal processes for obtaining an APA (Inland Revenue, 2015a). The informality of the process will be explored under this subtheme. Interviewees' views on the nature of the New Zealand APA process will be expressed throughout the subtheme.

As mentioned previously in Chapter 2, 'Literature Review', under section 2.4, the steps involved in obtaining a New Zealand APA are as follows:

- A written proposal is submitted by the applicant briefly outlining the entity's business activities, associated party transactions involved and what methodologies are to be applied to price these transactions.
- A pre-application meeting follows with a Principal Advisor to informally discuss the submitted proposal.
- The APA application is then formalised and submitted for consideration. The application will include transfer pricing documentation, full functional analysis, methodologies and comparables used, and other matters discussed in the pre-application meeting.
- The IRD may request site visits to examine the actual operation, especially where valuable intangibles are involved.
- A review of comparables will be performed by the IRD to assess the appropriateness of the ones proposed.
- Once the review is completed, the IRD will sit down with the taxpayer (unilateral situation) or with the officers of the other jurisdiction (bilateral situation) to discuss any differences of opinion. Once agreement is reached, an APA is concluded (Inland Revenue, 2015a)

All interviewees agreed with the above steps including the sequence when involved in the APA process. There was much discussion concerning specific areas within the process, mainly the IRD's overall approach towards transfer pricing and APAs and also the functional analysis stage of the process.

The overall process was viewed by all interviewees as one of an informal and cooperative nature. All interviewees felt that the overall relationship between the IRD and applicants

throughout their dealings with the New Zealand APA process was positive. One tax practitioner from a Big 4 accounting firm commented:

“We know the Principal Advisors very well, you deal with them all the time ...the IRD have always been reasonable and they do want to see an outcome ...we are both working towards the same cause, but they are not going to agree at any cost and we certainly are not going to agree at any cost. They [the IRD] still follow their principal approach. Sometimes I think you walk out of these things [and] think we did really well. We are surprised we did really well. Sometimes we think clientshave been ripped off. But end of the day I think if my client is happy, it is a win”.

(Tax Professional F, Big 4)

One interviewee from the IRD praised the nature of relationships maintained here in New Zealand stating, “the New Zealand environment is based on relationship building because you see the same people over and over again” (Tax Professional B, IRD). The same interviewee mentioned that disagreements are always possible, however all parties involved are mindful of doing it professionally.

Throughout the interviews, all participants commented on the functional analysis stage of the process. More recently, a lot more functional analysis has been required for an APA to be appropriately considered by the IRD. The IRD are requiring an increased amount of functional analysis to be included as part of the APA application. Also, the tax authority is now performing its own functional analysis on potential applicants.

“Nowadays we [the IRD] do a lot of interviews with the [applicant] company. For example, [a distributor with a] marketing and sales arm ...we would go and talk to the people in the sales and marketing area to see what they are actually doing ...we want to talk to these people and get their job descriptions ...site visits are important as well”.

(Tax Professional B, IRD)

Ultimately, the informal nature of the New Zealand APA process was viewed positively by all interviewees in the light of the New Zealand transfer pricing environment. However, all interviewees from the Big 4 accounting firms criticised the lack of any guidelines or standard practice statements issued by the IRD around transfer pricing and APAs. This criticism will be expanded on under section 4.2.7.2 ‘Transparency and Consistency’.

4.2.7.1.1 Renewals and Rollbacks

An APA is due for renewal when the duration of the APA has expired. Rollbacks are where an agreed transfer pricing methodology is applied to previous years. No information has been published on renewals or rollbacks on the IRD’s website.

It seems logical to assume that an MNE wanting to renew its existing APA should take less effort than a new applicant MNE wanting to obtain one for the first time. Contrary, all interviewees agreed that many current renewals follow the same process as if the MNE is applying for an APA for the first time. This is mainly attributed to the significant changes in a MNE’s cross border transactions over the five year period of an APA’s term. As noted already, all interviewees mentioned that the IRD as part of the APA process are requiring more functional analysis nowadays and are doing much more verification work than they used to. This also affects APA renewals making the review process more comprehensive. Four of the interviewees from the Big 4 accounting firms also mentioned that at the time of renewal, in most cases they are dealing with a new advisor from the IRD which adds to the renewal process.

“A renewal used to be quite easy and straightforward ...back in the days you would sit down for a coffee with one of the [Principal] Advisors andtalk about what has changed in the [MNE’s] business. Then you need to update the comparables, then just

rollover. You cannot do that anymore. It is a more comprehensive review now ...it is like going through the process again, particularly if you are with a new advisor”.

(Tax Professional E, IRD)

The OECD’s BEPS action plan was also seen as a contributing factor to the increased comprehensiveness of the renewal process. In cases where a MNE’s business has not changed significantly, interviewees mentioned that a renewal should be straightforward. The above is all relevant for the case of a unilateral APA. Renewals for bilateral and multilateral APAs, which involve more than one tax authority, are similar to applying for such an APA for the first time. This was accepted among all interviewees as the IRD has no control over the process.

Rollbacks present a retrospective application to APAs, where the terms of the APA are applied to previous years instead of future ones. New Zealand APAs are mainly forward looking, however rollbacks are not ruled out. Limited information was obtained in this research about APA rollbacks. However, it was believed that the IRD was prepared to apply the terms of an APA to previous years on some APAs given certain conditions are met.

4.2.7.2 Transparency and Consistency

Two main sub themes that emerged from the interviews were in relation to the transparency and consistency of the New Zealand APA process. Interviewees expressed their opinions about transparency and consistency in various ways. These two sub themes will be discussed together in this section.

Six of the interviewees brought up the moderation process when discussing the transparency and consistency of the New Zealand APA process. Moderation is the process of the IRD’s Principal Advisors sharing their workings and the outcomes of each APA with each other in order to improve the consistency of their decisions about APA outcomes. Further, each APA

draft is reviewed by the IRD's Specialist Advice Unit⁶⁹ Manager, who also ensures consistency is achieved among the Principal Advisors decisions regarding APAs. No information is available on the moderation process on the IRD's website. However, all six interviewees knew about the process.⁷⁰

The moderation process was viewed positively by five of the interviewees and perceived as effective in achieving a consistent and transparent outcome for APAs. One Big 4 tax practitioner criticised the moderation process from a transparency point of view, stating that no independent internal review exists. The practitioner commented:

“If theoretically you did have a concern, it is very difficult to escalate that concern to get a second opinionall four of them [Principal Advisors] are peers. If I had a concern about someone handling something, there is no clear process to say I actually have a concern with this and how it is being handled ...I do not feel there is that internal review and that is a weakness of their system ...there is no one above to give a second opinion”.

(Tax Professional E, Big 4)

The tax practitioner praised the APA process overall for what it offers. However, the practitioner believed that, as transfer pricing becomes more sophisticated, the IRD will need to adopt such processes (independent internal reviews).

None of the tax practitioners from the Big 4 accounting firms interviewed had concerns over the consistency of the APA process. All practitioners interviewed believed the IRD were consistent in their decision outcomes. This was regardless of the MNE or the tax advisor involved in assisting the MNE to achieve an APA. Three tax practitioners from the Big 4

⁶⁹ The IRD's Specialist Advice Unit is responsible for managing the APA program (Inland Revenue, 2012).

⁷⁰ The other two participants interviewed in this research study may have knowledge about the moderation process. However, it was not brought up by them in the duration of their interviews.

accounting firms raised an interesting point about the consistency of the New Zealand APA process. Although, they believed the outcome of each APA was consistent throughout all their dealings with the IRD, they also observed that the time and effort involved in reaching an outcome varied depending on the Principal Advisor the tax practitioner is dealing with. One interviewee from a Big 4 accounting firm commented:

“The process is different depending on the Principal Advisor ...you might get a Principal Advisor who might be more thorough and comprehensive. All that means, it is going to be a longer process ...the outcome should be consistent ...I say should because all the Principal Advisors have ensured me that there is a robust review process that happens internally and whereby the Principal Advisors present to the group [of Principal Advisors] ...the group will go through it and then reach agreement about how the APA should be signed”.

(Tax Professional H, Big 4)

The moderation process, discussed previously, assured interviewees from the Big 4 accounting firms that APA outcomes were consistent, regardless of the IRD Principal Advisor involved. All tax practitioners interviewed expressed a desire of being selective as to which Principal Advisor they would like to deal with on any certain APA. However, none of the tax practitioners said they would enforce this view upon the IRD. One tax practitioner explained that the IRD do need to maintain their probity and independence, and enforcing it upon them may compromise the revenue authority’s position.

The responses around the transparency of the New Zealand APA process varied across the interviewees. As noted previously, one matter all Big 4 tax practitioners interviewed criticised was the lack of any guidelines around transfer pricing in general and APAs. One interviewee from the Big 4 accounting firms mentioned, while praising the New Zealand APA process for

its flexibility and informality, that the process should be more structured around what the IRD expect from MNEs and tax practitioners in terms of benchmarking and comparables. One other interviewee commented:

“...for benchmarking purposes, there is not a lot that is publicly available ...we [tax practitioners] just know through ...word of mouth and industry information ...it can be more helpful to have them [benchmarks] available. We suffer from the less availability of guidance”.

(Tax Professional E, Big 4)

The IRD as a whole is restricted under the current secrecy provision in Section 81 of the Tax Administration Act 1994. One interviewee from the IRD mentioned about the ‘secrecy vs transparency’ argument that MNEs can play a big role in enhancing the transparency of the tax system in the area of transfer pricing.

“With the emphasis on transparency, there is a lot more a big business can do in relation to discussing publicly their tax governance, and secondly, actually giving a lot more context and detail around the tax they do pay”.

(Tax Professional H, Big 4).

Another IRD professional believed that increased transparency around the APA process can be achieved by way of producing APAs to the public in a redacted form.

Markham (2012, p.42) mentions that secrecy around the United States’ (U.S.) APA procedures was originally one of the main sources of controversy. In response to this controversy and in order to enhance transparency, in the late 1990s the U.S.’s Internal Revenue Service (IRS) proposed to publish individual APAs in a redacted form (Markham, 2012). Identifying information was removed so that the document could be available for public inspection under

the federal laws of the US. Markham (2012) stated that the IRS's proposal raised issues regarding confidentiality and that sensitive information was becoming available to the public. Further, redacting individual APAs would require immense resources to administer. In another attempt to embrace the transparency of the IRS's APA process, in December 1999, new laws were introduced requiring "the U.S. Treasury Department to publish an extensive annual report on the status of APAs, containing statistical information on APAs and the APA program" (Markham, 2012, p.44). Other features the annual report would cover were critical assumptions, transfer pricing methodologies and taxpayer characteristics. The information contained in the annual report⁷¹ was perceived as useful by the tax community (Markham, 2012). Markham (2012) mentioned that the IRS had demonstrated a greater awareness for the need to address the transparency of the tax system and the APA process with this annual report.

Perhaps redacting APAs in an attempt by the IRD to enhance transparency may not be a wise decision. Redacting individual APAs requires immense administrative resources. As believed by the tax practitioners from the Big 4 accounting firms interviewed, the revenue authority already suffers from lack of resourcing. The other issue is the small size of the New Zealand transfer pricing market. Redacted individual APAs may pose a risk around confidentiality and commercially sensitive information being available to the public. As an alternative, and consistent with Markham's (2012) review on the transparency of the IRS's APA process, the IRD could learn from the IRS's approach in demonstrating greater transparency of its APA process by way of publishing extensive annual reports. This may also serve as a positive response by the IRD to the New Zealand transfer pricing community criticising the IRD for the lack of guidance available on transfer pricing and APAs.

⁷¹ Refer to the IRS's website for all APA statutory reports 1999-2015
<https://www.irs.gov/businesses/corporations/annual-apa-statutory-reports>.

The overall findings around the consistency of the New Zealand APA process supports that the IRD are consistent in their outcomes. However, as expressed by tax practitioners interviewed, the process in reaching these outcomes is not consistent.

A major area the IRD must consider is the guidelines and practice statements available on transfer pricing and APAs. This matter was brought up by all tax practitioners interviewed and was believed to be a major weakness of the revenue authority's overall transfer pricing and APA program. One practitioner preferred the flexible nature of the New Zealand APA process over those processes where extensive guidelines exist like the US's. However, the tax practitioner still believed that some form of guidance around standard practice, benchmarking and comparables would be greatly beneficial in New Zealand.

4.3. How does the New Zealand APA Process compare to that of other Jurisdictions?

This section presents a summary table and a brief discussion to answer this thesis's third research question:

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

Avoseh (2014, p.34) states that "in general, the differing transfer pricing agenda of a tax authority is reflected in the way it conducts its APA process". The tax jurisdictions selected as part of the summary table – Table 4.2 - are Australia, the UK and the US. These tax jurisdictions all have developed and mature APA processes in place. The APA processes of these tax jurisdictions have already been reviewed in Chapter 2, 'Literature review', of this thesis.

An additional brief discussion will be provided about Australia's ATO APA process under section 4.3.1. Much of this discussion will be provided from the interviews conducted as part of this research. Many of the interviewees commented about the Australian APA process and

used it as a comparison to New Zealand's APA process in many instances. Discussion about the ATO and their APA process came as no surprise to the author. Over 60% of bilateral APAs concluded up until 30 June 2015 were with the ATO (J. Nash, personal communication, January 28, 2016). Moreover, Australia continues to be New Zealand's major trading partner (Edwards & Nash, 2009), which reflects the scale of economic activity between both jurisdictions.

Table 4.2⁷² is set out on the next page to give some brief comparisons of the APA process in New Zealand, Australia, the UK and the US. The information summarised in this table is as made available publicly for the APA process as operated by each tax authority.

⁷² This table draws upon the work of Avoseh (2014, p.35).

Table 4.2 Comparison of the APA Process in New Zealand, Australia, the UK and the US

	New Zealand	Australia	UK	US
APA Legislation	<i>Section 91E: Commissioner to make private rulings on application</i>	<i>Practice Statement Law Administration PS LA 2015/4⁷³</i>	<i>Section 218-230 of the Taxation (International and Other Provisions) Act 2010 (TIOPA 2010)</i>	<i>Rev. Proc. 2015-41⁷⁴</i>
Nomenclature	Advance Pricing Agreement (APA)	Advance Pricing Arrangement (APA)	Advance Pricing Agreement (APA)	Advance Pricing Agreement (APA)
Year of Establishment	1999/2000	1995	1999	1991
APA User Fee⁷⁵	No user fee	No user fee	No user fee	\$30,000- \$60,000
APA Application Phases	(1) Written proposal (2) Pre-application meeting (3) APA application formalised and lodged (4) Review of application (5) Discussion/Agreement	(1) Early engagement (2) APA application (3) Monitoring compliance	(1) Expression of interest (2) Formal submission of APA application (3) Evaluation of proposed methodology and critical assumption (4) Drawing up agreements (5) Annual report	(1) Application (2) Due diligence (3) Analysis (4) Discussion and agreement (5) Drafting, review, and execution (6) Ongoing APA compliance – annual reports
Approach to APA Application	No formal approach established: depending on taxpayer’s specific facts and circumstances. All MNE applicants are considered	Is the APA a practical and commercial outcome to both the MNE and the ATO	Complex transactions vs. Non-complex transaction	Strategic transactions vs. Non-strategic Transactions

It is evident from the table that there are differences between each tax administration’s APA processes. A noticeable difference, which fits within the ‘critical evaluation’ aspect of this research, is the divergence of each tax administration’s approach to APA applications by MNE taxpayers. With the ATO, all MNEs are to refer to section 6, 7 and 12 of the Practice Statement Law Administration (PS LA) 2015/4 for details as to what the ATO considers when determining whether to enter into an APA. The PS LA 2015/4 “sets out the Commissioner’s practice and procedures and provides guidance to ATO staff in dealing with requests from

⁷³ Replaces PS LA 2011/1.

⁷⁴ This revenue procedure updates and supersedes *Rev. Proc. 2015-40*, 2006-1 C.B. 278, as modified by *Rev. Proc. 2008-31*, 2008-1 C.B. 1133 which is also superseded.

⁷⁵ Note: A minimal application fee may apply to those jurisdictions’ APA processes that have a ‘no user fee’. For example, the IRD are required to charge 332 NZD by law for preparing private rulings, including APAs (Inland Revenue, 2013).

taxpayers to enter into an advance pricing arrangement (APA)”. Sections 6, 7 and 12 of the PS LA 2015/4 outline the indicators as what makes the ATO more or less likely enter into an APA and when the ATO will invite a MNE applicant to lodge a formal APA application. For example, some of the indicators set out under section 6 ‘*What makes the ATO more likely to enter into an APA?*’ of the PS LA 2015/4 are:

- “the transfer pricing methodology proposed best achieves consistency with the OECD guidelines as at 22 July 2010
- the transfer pricing issues are complex and there is uncertainty as to how the transfer pricing rules apply
- without an APA, the probability of economic double taxation is high”.

The full sections are set out in Appendix 7. The ATO needs to be convinced the outcome is both practical and commercial for both itself and the MNE applicant before a formal application can be lodged.

As stated by Avoseh (2014, p.35) when comparing the US APA process to those of the UK and Australia, “the US IRS will consider and accept APA applications into its process upon the due payment of the necessary application fees by the MNE applicant”. Once an application has been advanced into the procedural stages of the process, any necessary evaluations are then carried out. This comparison is also relevant to New Zealand.

For the UK’s Her Majesty’s Revenue & Customs (HMRC), every APA request will be considered by the tax authority, but generally, the authority closely considers cases where the transfer pricing issues are complex and rather than straightforward. Complex means there is a

doubt as to how the arm's length standard should be applied.⁷⁶ Instances where there is a high chance of double taxation is also taken into consideration by the HMRC.

Relating the research findings and discussion of this thesis to Avoseh's (2014) study, which examined UK based MNEs' reason for applying or not applying for an APA, can provide further comparisons between the New Zealand APA process and that of the UK's. Avoseh (2014) concludes with three key themes that are critical to MNEs' when deciding on whether or not to apply for APAs. The three key themes concluded were: (1) Cost and Benefit of an APA, (2) Clarification of APA Guidelines and (3) Generic APA Process. These three themes are set against the research findings and discussion of this thesis.

In relation to the 'Cost and benefit of an APA', this theme is consistent with the views expressed by the Big 4 tax practitioners in this study. Respondents in Avoseh's (2014) study expressed that the cost of an APA was a significant factor when considering to pursue one. Further, an APA would only be considered if the transactions involved are large enough to cover the cost of the APA. This holds true for the New Zealand APA process as well. Although interviewees believed that the cost of a unilateral APA in New Zealand should not cost much more than it does to maintain adequate transfer pricing documentation, if the transactions involved are not material enough in terms of risk and monetary value, an APA would not be worth pursuing (also the case for bilateral and multilateral APAs).

In relation to the second theme, 'Clarification of APA Guidelines', UK based MNEs thought that the HMRC's current guidance on APAs and transfer pricing is "generic and not helpful enough" (Avoseh, 2014, p. 215). The MNEs stated that in many instances it was difficult to determine what the HMRC regarded as an acceptable transfer pricing methodology. Likewise, this theme is consistent with the findings of this research. In this study, all tax practitioners from the Big 4 accounting firms criticized the lack of any guidelines or practice statements on

⁷⁶ Refer to HMRC's Statement of Practice 2 (2010) (SP 02/10), Paragraph 13.

transfer pricing and APAs in New Zealand. While all tax practitioners interviewed praised the New Zealand APA process for its flexibility and informality, many expressed that the process should be more structured around what the IRD expect from MNEs and tax practitioners in terms of benchmarking and comparables.

In relation to the third theme, UK based MNEs expressed a desire for a more ‘generic APA process’, especially for bilateral and multilateral APAs. Having more simplified APA regulatory requirements in place was seen as a way for a more ‘generic APA policy’ to be achieved. In the author’s view, this theme is not of much relevance to this thesis given the findings of the research. None of the interviewees expressed the need for the New Zealand APA process to become more ‘generic’. However, this theme should not be ruled out as it was not explored in this study.

Although a noticeable divergence is noted between the IRD and HMRC’s approaches to APAs, similar findings were found above in relation to certain aspects of the two revenue authorities’ APA processes.

The New Zealand IRD have maintained an APA approach where all MNE applicants are welcome to apply regardless of complexity, size or degree of risk involved in any of their transactions to be covered under the APA. What stands out about the New Zealand APA process, in comparison to the other tax jurisdictions, is that the process itself has not experienced any ‘formal’ reform or revisions. Instead, as observed by the author from the interviewees conducted as part of this study, the IRD are able to tailor the APA process and allow it to address the revenue authority’s needs in relation to transfer pricing on an ongoing basis when needed. This may be feasible to the IRD given the size of the transfer pricing market in New Zealand, in comparison with other tax jurisdictions, for example, the US. Another factor may be due to the informality of the New Zealand APA process since the program’s inception. No formal guidelines have been issued, which assists the IRD in being able to

address the needs of the process upfront on an ongoing basis, without the need for major reform. In the end, each tax administration's approach to its APA process reflects the differing transfer pricing agenda that tax administration has.

Table 4.3 on the next page sets out the number of unilateral, bilateral and multilateral APAs completed by the IRD as at 31 December 2015.

Table 4.3 Number of APAs completed by the IRD as at 31 December 2015⁷⁷

APA Type	Number Completed
Unilateral	101 APAs
Bilateral	36 APAs <u>Breakdown</u> Australia – 24 Belgium – 1 Japan – 2 Korea – 1 Switzerland – 2 USA - 6
Multilateral	2 APAs*
Total	139 APAs

*Canada were part of these two multilateral APAs

The above table reflects the extent of APA activity the IRD has with the ATO with 24 of the 36 bilateral APAs completed being with Australia.

4.3.1 The New Zealand APA Program and the Australian Tax Office

Two main topics risen from the interviews about the ATO and their APA process. The first topic is in relation to the overall relationship between New Zealand and Australia from a transfer pricing perspective. None of the interviewees thought that the relationship between the IRD and the ATO was unique or special. This was mainly due to the differing transfer pricing governance processes the ATO maintains. The IRD mention that they aim to complete bilateral APAs with Australia within six months from the date a formal application is lodged (Inland Revenue, 2015a). As mentioned previously, under ‘section 4.2.4’ Time and Cost of Filing an APA, an interviewee from the IRD commented that it takes twelve to fourteen months to complete bilateral APAs nowadays due to the different governance model Australia operates under.

⁷⁷ (J. Nash, personal communication, January 28, 2016).

One interviewee from the IRD raised an interesting point about transfer pricing comparables in Australia. The interviewee commented:

“ ...the market place [between New Zealand and Australia] is not a lot different[it is] often been said, it is a single market ...when it comes to comparables searches, we tend to come up with similar ones”.

(Tax Professional B, IRD)

All interviewees from the Big 4 accounting firms mentioned that they have close relationships with the transfer pricing practitioners from their counter Big 4 firms located in Australia. The interviewees mentioned that in cases where a bilateral APA with the ATO consists of complex issues, the Australian tax practitioners are involved to manage the ATO's side of the bilateral APA.

The second topic that had risen from discussion about the ATO was in relation to the recent Australian transfer pricing case law and its relevance to New Zealand. As explained in Chapter 2, 'Literature Review', some of the most prominent transfer pricing litigation cases in Australia are the *Roche* case,⁷⁸ *SNF*,⁷⁹ and more recently the *Chevron* case⁸⁰ decision in 2015.⁸¹ Both the *Roche* and *SNF* cases were in relation to the Australian transfer pricing rules at the time and the rules divergence from the OECD guidelines. As one interviewee from the IRD explained both cases:

⁷⁸ *Roche Products Pty Ltd v. Commissioner of Taxation* [2008] AATA 639(22 July 2008); 2008 ATC 10-036; 2008 AATA 639; 70 ATR 703, 268.

⁷⁹ *SNF (Australia) Pty Ltd v. Commissioner of Taxation* [2010] FCA 635, 270.

⁸⁰ *Chevron Australia Holdings Pty Ltd v FC of T* [2015] ATC 20-535.

⁸¹ Decision made in the Federal Court; subject to appeal by Chevron.

“The ATO legislation was substantially different from both OECD and the New Zealand legislation and in fact those cases dealt not so much with transfer pricing ...but whether the legislation they had allowed them to take the position that they had taken”.

(Tax Professional C, IRD)

The *Chevron* case mainly dealt with an issue in the financing area of transfer pricing, which saw a win to the ATO. Comments from interviewees indicated that Australian transfer pricing case law has not much relevance to New Zealand. Interviewees believed so mainly due to the fact that many of the litigation focuses on how the Australian transfer pricing rules have been written.

New Zealand has not had any transfer pricing litigation, except for the case of *Squibb*,⁸² where it was held that Inland Revenue has the right to use secret comparables in order to exercise its statutory duty to collect the correct amount of tax. Many of the interviewees believed that the New Zealand courts are not equipped to deal with transfer pricing litigation.

An interesting point was made by two interviewees from the Big 4 accounting firms about the current New Zealand transfer pricing legislation. The interviewees believed that the changing transfer pricing environment as a result of the OECD’s BEPS Action Plan and the lack of any guidance or interpretation statements from the IRD, is making the current legislation increasingly obsolete. The practitioners believed that many of the outcomes the IRD are achieving as part of their transfer pricing program may be overturned if challenged in court.

4.4 Summary

The interview findings conducted with eight tax professionals and practitioners from the IRD and the Big 4 accounting firms in New Zealand were presented in this chapter. This chapter

⁸² *CIR v E R Squibb & Sons (NZ) Limited* (1992) 14 NZTC 9,146.

sought to mainly evaluate the New Zealand APA process, and more importantly, answer the second research question:

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

Overall, the New Zealand APA process was perceived positively by all interviewees. Certainty on the cross-border tax positions taken was seen as the primary purpose for a MNE to obtain an APA. It was confirmed that negotiating an APA with the IRD may result in a transfer pricing audit in some circumstances. Various evaluations around the time and cost involved in obtaining an APA were explained by the interviewees. Interviewees saw great potential in NZ Customs incorporating APAs as part of their valuation practice. However, many obstacles stand in the way of NZ Customs implementing such changes; this is explained in this chapter under section 4.2.5 'Potential use of APA to New Zealand Customs'.

The IRD have maintained an informal APA process where all MNE applicants are welcome to apply regardless of complexity, size or degree of risk involved in any of their transactions to be covered under the APA. This chapter presented a summary table and a brief discussion to answer the third research question of this thesis:

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

The informal nature of the New Zealand APA process is a main unique point of difference compared to the APA processes of Australia, the UK and the US.

Chapter 5: Conclusions, Limitations and Future Research

5.1 Introduction

The New Zealand Advance Pricing Agreement (APA) program was initiated by the Inland Revenue Department (IRD) as a way for multinational enterprises (MNEs) to address transfer pricing compliance in a co-operative manner (Inland Revenue, 2015a). This thesis set out to evaluate the New Zealand APA process. Interviews were conducted with eight participants, with three from the IRD and five from the Big 4 accounting firms in New Zealand. Several themes emerged from the interviews and are presented and discussed in Chapter 4, 'Research Findings and Discussion', of this thesis. The conclusions of the research are presented under section 5.2, 'Conclusions'. Section 5.3, 'Limitations', sets out the limitations of the research. Proposed directions for future research follow under section 5.4, 'Recommendations for Future Research'.

5.2 Conclusions

This research study sought to answer the following research questions:

RQ1: What are the steps involved in obtaining a New Zealand APA?

RQ2: Through interviews, what are various parties' critical evaluation of the New Zealand APA process?

RQ3: How does the New Zealand APA process compare to selected overseas' APA processes?

In relation to *RQ1*, the research introduced the New Zealand APA process and the steps involved in obtaining an APA following a literature review on the topic. Further information on the New Zealand APA process was obtained throughout the interviews. In the author's view,

limited information is available on the IRD's website about transfer pricing and the APA process. The aim was to confirm whether the interviewees agreed with the content already published on the topic, and to observe whether any other information would further supplement the literature review.

All interviewees believed the New Zealand APA process follows an informal approach and requires a high degree of mutual cooperation to operate effectively. One common theme across all interviewees was in relation to the degree of functional analysis required by a MNE applicant for its APA application to be appropriately considered by the IRD. From the interviews conducted, it is evident that the IRD are requiring an increased amount of functional analysis to be performed by applicant MNEs in order to justify their transfer pricing positions brought forward as part of their APA application.

In relation to *RQ2*, this thesis attempted to critically evaluate the New Zealand APA process. This was undertaken through a series of semi-structured interviews conducted with a total of eight participants from the IRD (3 participants) and the Big 4 accounting firms (5 participants) in New Zealand. It was considered appropriate to interview the IRD as the APA program had been initiated by the revenue authority itself. Tax practitioners from the Big 4 accounting firms were ideally placed to evaluate the APA program, being the representatives of many MNE applicants throughout the APA process. All tax practitioner participants were senior transfer pricing personnel within their organisations and had extensive experience in dealing with the New Zealand APA program.

The New Zealand transfer pricing rules were perceived by all interviewees as being robust in protecting the New Zealand MNE tax base and in preventing any tax revenue leakage. However, increased uncertainty around future changes to the transfer pricing rules in New Zealand was expressed by interviewees from the Big 4 accounting firms, especially in the light

of the Organisation for Economic Co-operation and Development (OECD)'s Base Erosion and Profiting Shifting (BEPS) Action Plan. In the light of such uncertainties in the New Zealand transfer pricing environment, all interviewees believed APAs were an attractive solution for MNEs wanting to achieve certainty on their cross border transactions. This solution was also believed to be the main purpose for an MNE to obtain an APA.

All interviewees believed an APA may trigger a transfer pricing audit. In the context of a 'carrot-and-stick' approach, concluding an APA represents the 'carrot' and not reaching agreement resulting in a transfer pricing audit, is the 'stick'. From the comments made throughout the interviews, it was believed that APA requests containing aggressive proposals would result in a transfer pricing audit as a consequence. The IRD was well perceived in terms of being able to complete unilateral APAs within the six month timeframe, as indicated by the revenue authority, from the day a formal application is lodged. The timing around bilateral and multilateral APAs received no criticism, as no one party had absolute control over the process.

It was believed among all interviewees that the cost of obtaining a unilateral APA should not be much more than the cost to prepare adequate transfer pricing documentation. Adequate transfer documentation from the IRD's perspective can save both time and cost for MNEs and the IRD when going through the APA process. It allows the IRD to assess any risks and conclude APAs in an efficient and effective manner. Much of the information the revenue authority 'needs to test' would be contained in the transfer pricing documentation provided from the start by the applicant. This in turn minimises the amount of any further information the IRD will need to request, if any, to verify risks.

The potential use of APAs by New Zealand Customs (NZ Customs) was the subject of critical comments throughout the interviews. The results from this interview theme also presents a major contribution to knowledge. Seven out of the eight interviewees provided specific

commentary on this theme. Interviewees believed that APAs can provide great benefits to NZ Customs and MNE importers as an accepted method to value a MNE's imports. These benefits are translated into time and cost saved for both parties. However, many obstacles were identified by the interviewees as to why incorporating APAs into NZ Customs' valuation practice may prove to be a challenge. Some of the obstacles identified were, the rigid legislative environment NZ Customs operates in, and the differing objectives the organisation has, in comparison to the IRD who conclude APAs with MNEs. The current rewrite of NZ Customs' principal legislation, the Customs and Excise Act 1996, signifies a positive change, where MNEs would be allowed to price their imports based on an APA that MNE holds.

Small to Medium Enterprises (SMEs) with cross border transactions have the opportunity to obtain APAs in New Zealand. The IRD was believed to be very open about negotiating any APA requests, regardless of the size or complexity of the transactions involved. An APA is due for renewal before the duration of the APA has expired. It is evident from the interviews conducted that the renewal process for many of the current unilateral APAs follows the same process as if the MNE was a first time applicant. The review process is becoming increasingly comprehensive, even for those MNEs wanting to renew their existing APAs. All interviewees believed it was mainly due to the increased functional analysis and verification work performed by the IRD nowadays. Interviewees from the Big 4 accounting firms accepted that the review process in the case of renewals needed to become increasingly comprehensive. In cases where a MNE's business has not changed significantly, interviewees mentioned that an APA renewal is straightforward. Limited information was obtained in this research about APA rollbacks. However, it was believed that the IRD was prepared to apply the terms of an APA to previous years on some APAs given certain conditions are met.

It is evident from this study that the IRD are consistent with all their decision outcomes regarding APA applications. This is mainly supported by the moderation process in place by

the IRD, which assures MNEs that APA outcomes are consistent throughout the process regardless of the IRD Principal Advisor involved. Various views were expressed around the transparency of the New Zealand APA process. All tax practitioners interviewed from the Big 4 accounting firms agreed that there was a lack of guidelines around transfer pricing and APAs. Also, concerns were expressed that the IRD need to be more structured around what it expects from MNEs and tax practitioners in terms of benchmarking and comparables for transfer pricing purposes.

In relation to *RQ3*, this study sought information about the APA processes of Australia, the UK and the US. A literature review was conducted on each of the countries' APA processes. The information was then presented in a table (Table 4.2) used to give a brief comparison between the APA processes in each of these countries and New Zealand. The IRD have maintained an APA approach where all MNE applicants are welcome to apply regardless of complexity, size or degree of risk involved in any of their transactions proposed to be covered under the APA. The New Zealand APA process has not experienced any 'formal' reform since its inception in 1999/2000. Instead, the process changes and evolves, on an ongoing basis, as the IRD sees fit.

In relation to Australia, none of the interviewees thought that the relationship between the IRD and the Australian Tax Office (ATO) was unique or special. The differing transfer pricing governance processes the ATO maintains, compared to those of the IRD, were believed to be the main reason in preventing a unique relationship. Recent Australian transfer pricing case law was not believed to be relevant to New Zealand. Many of the interviewees believed that New Zealand courts are not equipped to deal with transfer pricing litigation. Concerns over that New Zealand's changing transfer pricing environment was making New Zealand's legislation increasingly obsolete was expressed by two of the interviewees from the Big 4 accounting firms.

This study sought to evaluate the current New Zealand APA process. Overall, the APA process was perceived well in terms of how it works and what it achieves. It is evident from the opinions expressed by interviewees that the process's ultimate aim is for MNEs to achieve certainty on their future transfer pricing tax affairs.

5.3 Limitations

There are several limitations to this research. The limitations are mainly due to the scope of this thesis and the research methods used. The researcher had to ensure the thesis was completed in time and with the available resources provided. The research methods used in this study, documentary analysis and semi-structured interviews, were all qualitative in nature. These qualitative methods require more time spent on collecting information, compared to quantitative methods. With the timeframe allocated for this study, this resulted in a fewer number of subjects being studied.

Semi-structured interviews were mainly used to evaluate the New Zealand APA process. As mentioned previously, this resulted in a fewer number of interviewees being able to be studied. This study involved eight participants from the IRD and the Big 4 accounting firms, all with extensive experience in transfer pricing and the New Zealand APA process. As mentioned in Chapter 3 (section 3.5.3) Mason (2010) and Dworkin (2012) state that when the saturation point is reached, no new relevant data should be obtained by conducting a further interview. By the eighth interview, it was believed that the saturation point would be reached. No new knowledge or insights is expected to be obtained from conducting any further interviews.

The interviews only studied the opinions of tax professionals from the IRD and tax practitioners from the Big 4 accounting firms, and not MNEs themselves, whom are arguably the users of the APA process. This study excluded MNEs from being studied mainly due to time constraints. Further, the secrecy provisions under Section 81 of the Tax Administration Act

1994 create challenges and would lead to a less convenient route for the researcher to identify those MNEs, who hold or have previously held an APA, in order to be studied. The studies of Borkowski (1993; 1996b; 2008), Elliott and Emmanuel (2000) and Avoseh (2014) are all examples of studies on APAs that have incorporated MNEs' view on APAs as part of their research. Studying the opinions of NZ Customs on the potential use of APAs may have added great value to the findings of this research. Again, this was not practicable due to time and scope constraints.

Documentary analysis was used to collect information about transfer pricing and the APA process of New Zealand and those of other overseas tax jurisdictions. A limitation of this study is that the research could not include every document about transfer pricing and APAs, as there is too much information on the topic. To mitigate these limitations, the researcher ensured that all useful and relevant information was revisited and is up-to-date.

As a consequence of scope constraint, the number of tax jurisdictions' whose APA processes were used as comparatives in this thesis was limited to three. The tax jurisdictions were selected by undertaking a preliminary study. Tax jurisdictions with developed and mature APA processes were identified and further filtered by their comparability to New Zealand's APA process. The level of availability of public information to the researcher about the overseas tax jurisdictions' APA processes was also a consideration. Another major consideration was the jurisdictions' rankings in terms of the amount of trade with New Zealand. The preliminary research yielded three countries: Australia, the UK and the US. This preliminary study was primarily undertaken to answer *RQ3* of this thesis and was presented as a minor part of the 'Research Findings and Discussion'. Further, information obtained about these APA processes throughout this study assisted the researcher in formulating many of the questions asked in the interviews. The APA processes of other tax jurisdictions could have been studied, and potentially added new insights for future research.

5.4 Recommendations for Future Research

The evaluation of the New Zealand APA process undertaken in this thesis provides a foundation for future research and policy development on the NZ APA process. The limitations and contributions of this study also present opportunities for future research.

One of the main themes that emerged from the interviews undertaken as part of this study was the 'Potential use of APAs to New Zealand Customs'. Future studies could incorporate the opinions of interviewees from NZ Customs. Studying the current rewrite of NZ Customs' principal legislation and its effect on transfer pricing and APAs is another area yet to be explored. These potential studies would address the current lack of academic literature on the topic as well.

A major limitation of this study was that only interviewees from the IRD and Big 4 accounting firms were only studied, and not MNEs. This presents an opportunity to study MNEs' opinions on the New Zealand APA process in the future. Surveys and questionnaires designed to collect quantitative data can be used to identify and explain MNEs' behaviour on certain aspects of the New Zealand APA process. This approach has been used in previous studies (Borkowski, 1993; Borkowski, 1996b; Borkowski, 2008; Avoseh, 2014).

Tax practitioner interviewees were only chosen from the Big 4 accounting firms as the researcher believed that these firms captured the majority of the MNE market in New Zealand. This was confirmed by the IRD prior to conducting the interviews. Future research could incorporate the opinions of tax practitioners from mid-tier accounting firms who have experience in transfer pricing and dealings with the New Zealand APA process. It is unclear how beneficial this would be as anecdotally it appears APAs are only negotiated by the Big 4 accounting firms due to the complexity of transfer pricing and another relevant factors. This is an area yet to be explored from a New Zealand context in terms of how useful it would be to

consider mid-tier accounting firms for the purpose of APAs. Other potential areas of future research this thesis has identified are examining the New Zealand-Australian relationship in relation to transfer pricing and APAs. Further, evaluating the New Zealand APA process in light of the OECD's BEPS Action Plan is another area that could be explored in the future.

This thesis set out to provide an insight into the New Zealand APA process, form a foundation of literature for future study on the process, and promote the APA process as a comparative for future studies. This study presents a much clearer understanding of how the New Zealand APA process works. It shed some light on the informal nature aspect of the process and how the IRD and tax practitioners interact with each other. Other aspects of the New Zealand APA process were explored, such as the IRD's internal moderation process, the process's applicability to SMEs, and the potential use of APAs by NZ Customs as means for MNEs to value their imports based on an APA that MNE holds. Other lessons can be learnt from the APA processes of other tax jurisdictions. For example, the US's APA program's experience with redacting APAs can assist the IRD in addressing any potential future issues around the transparency of its APA program the right way. A foundation of literature now exists for further future research to be carried out on the New Zealand APA process. The informal nature of the New Zealand APA process explored in this study may provide useful insights to other tax jurisdictions with developing APA processes or tax jurisdictions that are considering initiating an APA program.

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Appendices

Appendix 1: Application for Private Ruling (IR713)



Inland Revenue
Te Tari Taake

Application for private ruling

IR 713
June 2015

- This form is for use by all taxpayers, either personally or by their authorised agent, applying for a ruling on a proposed, current, or completed arrangement.
- Please read the IR 715 Binding Rulings Booklet for information about the binding rulings process, including when we can and can't give rulings.
- If you need further assistance, or to arrange a pre-lodgement meeting, please contact us at rulings@ird.govt.nz

Applicants details

Complete the details of the persons to whom this ruling will apply. If there are not enough spaces, use a separate sheet of paper and attach it to this form.

Full name of applicant

IRD number of applicant (8 digit numbers start in the second box. 7 2 3 4 5 6 7 8)

Full name of applicant

IRD number of applicant

Agent details

If this application is made on behalf of an applicant(s), the agent must have written consent from the applicant(s). The written consent must be supplied on request to Inland Revenue.

Full name of agent

Agents business name

Agents IRD number

Contact person for enquiries

Full name

Daytime phone number

Email address

Postal address

Street address/PO Box number

Town/city

General questions

If you have previously applied for a ruling in respect of this transaction, please advise the reference number or final ruling number:

PRI or BR Prv /

Have you previously received any other advice from Inland Revenue on this transaction?
If yes, please provide details in your application.

Yes No

Is this an application for a ruling on a transfer pricing arrangement?
If yes, please ensure an IR 713A additional declaration is also completed.

Yes No

Application fee

An initial application fee of \$322.00 (including GST) is payable at the time that the application is lodged. Inland Revenue is not able to begin processing your application until the initial application fee is received.

The application fee can be paid electronically or by cheque. If you want to pay electronically, please contact us at rulings@ird.govt.nz for details. Please confirm your method of payment:

Electronically

Date of payment

/ /
Day Month Year

Reference

Cheque

Agreement to Communicate with Inland Revenue via Email

In order for us to email you about your application, please list all persons (including any support personnel) who are authorised to communicate with us about this application (in addition to the contact person named on page one).

If there are not enough spaces, please use a separate sheet of paper and attach it to this form.

Full name

Email address

Full name

Email address

Full name

Email address

Declarations

I consent to communicate with Inland Revenue via email. I accept that Inland Revenue will communicate via email where appropriate in relation to the above application; understanding that at times these emails will contain confidential and or commercially sensitive information. Inland Revenue will take all reasonable steps to mitigate any risk of unauthorised access or disclosure of confidential information, but cannot guarantee that emails will not be intercepted or read by an unintended recipient.

The details contained in this application are true and correct. I hold the written consent of the applicant(s).

/ /

Signature of agent/applicant

Date

Checklist

This checklist is a prompt to help you provide the best application for a private ruling possible which will minimise processing delays.

- Have you had a pre-lodgement meeting? A pre-lodgement meeting is a requirement if you want a draft ruling within three months. Yes No
- Have you identified the applicants and all parties to the arrangement, including counter-parties? Yes No
- Have you fully explained the arrangement, including all transactions, steps and intentions? Yes No
- Have you stated all the tax laws and propositions of law applicable to the arrangement? Yes No
- Have you included a draft ruling, and all other relevant documents? Yes No
- Have you paid the application fee electronically? (If paying by cheque, post to address below) Yes No
- Have you attached a completed IR 713A additional declaration if the application is for a private ruling on a transfer pricing arrangement? Yes No

Email this form with your supporting documentation to rulings@ird.govt.nz or

Post to: Team Secretary, Taxpayer Rulings Unit, Office of the Chief Tax Counsel,
Inland Revenue National Office, PO Box 2198, Wellington 6140

RESET FORM

Appendix 2: Application for Private Ruling on Transfer Pricing Arrangement – Additional Declaration (IR713A)



Application for private ruling on transfer pricing arrangement – additional declaration

IR 713A
November 2012

- This declaration is for completion by all taxpayers applying for a ruling on a proposed, current or completed transfer pricing arrangement, and should be completed by the applicant, NOT a tax agent or accountant outside the applicant's business.
- This form should always be completed in conjunction with and accompany the IR713 Application for Private Ruling form.
- Please ensure you have contacted a Principal Advisor (Transfer Pricing) of the Specialist Advice Unit to discuss the requirements and necessary information for the advanced pricing agreement process before completing the application and this form.
- Please read the information on the back before completing this form.

Applicant details

Complete the details of the person to whom this ruling will apply.

If this is a joint application, please ensure each applicant has completed a separate additional declaration form.

IRD number of applicant	(8 digit numbers start in the second box. 1 2 3 4 5 6 7 8)	<input type="text"/>
Full name of applicant	<input type="text"/>	
Address of applicant	<input type="text"/>	
	Street address/PO Box number	
	<input type="text"/>	
	Town/city	
Name of person signing this declaration	<input type="text"/>	
Position/role held in applicant's business	<input type="text"/>	
Daytime phone number	(<input type="text"/>)	<input type="text"/>

Declaration

The person signing this declaration should be fully aware of the applicant's transfer pricing arrangement, and hold a role in the applicant's business with sufficient authority to make the declaration.

I have fully examined the attached application and information and documents provided in connection with the application. To the best of my knowledge and belief, the information disclosed for the application is comprehensive.

Signature of applicant(s)

Date

Transfer pricing agreement information

Introduction:

Transfer pricing is the setting of prices for the international transfer of goods, services and intangibles between associated parties [one of whom is a New Zealand taxpayer]. If these are manipulated profits may be shifted out of New Zealand.

The purpose of New Zealand's transfer pricing tax rules is to ensure that for tax purposes taxpayers price their international related-party dealings as truly independent parties would have done in the same situation, i.e. on an arm's length basis.

To provide certainty for taxpayers in relation to these international related-party dealings, New Zealand's tax law provides for the issuing, upon application, of unilateral Advance Pricing Agreements ("APAs") in the form of binding rulings. Bilateral and multilateral APAs may also be entered into in line with New Zealand's double tax treaties. A unilateral APA is a ruling binding the Commissioner of Inland Revenue on an appropriate transfer pricing methodology to be applied to the taxpayer's specified international related-party transactions over a fixed period.

The legislation governing the transfer pricing rules is contained in sections GC 6 to GC 14 of the Income Tax Act 2007. In respect of Branches any allocations of income and expenditure are made in terms of section YD 5 of the Act.

Issuing an APA:

Inland Revenue will issue an APA when it is satisfied that the transfer pricing methodology to be used by the taxpayer results in an arm's length price for the international related-party transactions. APAs are considered and issued by Inland Revenue's Specialist Advice Unit whose contact details are set out below.

Applying for an APA:

The transfer pricing documentation and information provided by a taxpayer in connection with its application for a unilateral APA is central to the process of explaining and justifying the pricing methodology for its cross-border transactions. A taxpayer should be able to readily demonstrate to Inland Revenue that its transfer prices are consistent with the arm's length principle.

For this reason a taxpayer considering an application for an APA should contact a Principal Advisor (Transfer Pricing) of the Specialist Advice Unit to discuss the requirements and necessary information for the advanced pricing agreement process before making the application.

An application for an APA is made on Form IR 713 and is to be accompanied by this additional declaration.

Additional declaration:

Section 91ED(1B) of the Tax Administration Act 1994 requires an applicant for a private ruling on how sections GC 6 to GC 14 or YD 5 of the Income Tax Act 2007 applies, to state, in a notice signed by them and sent to the Commissioner at the same time as the application, that they have examined the application and to the best of their knowledge and belief the information disclosed for the application is comprehensive.

Declaration explained:

The additional declaration requires applicants for private rulings relating to advance pricing agreements to be more explicitly involved in the application process compared with other private ruling applications. This additional declaration is to ensure that a person holding a role in the applicant's business with sufficient knowledge of the applicant's international related-party transactions and transfer pricing methodology and having the necessary authority to make the declaration, is able to declare that the information provided to Inland Revenue in connection with the application is sufficiently expansive and complete.

Specialist Advice contact details:

The contact details for the Principal Advisors (Transfer Pricing) can be found on our website:
<http://www.ird.govt.nz/transfer-pricing/about/transfer-pricing-about-team.html>

Appendix 3: Nature of Documentation Required in an Annual Report⁸³

Nature of Documentation Required in Annual Report

§ 521(b)(2)(D)(xi)

APAs executed in 2015 required taxpayers to provide various documents with their annual reports, depending on the specific facts of the case. While not every annual report will include each of the documents listed below the documents listed below are required where the facts demonstrate a need for such documentation.

1.	Statement identifying all material differences between Taxpayer's business operations during APA year and description of Taxpayer's business operations contained in Taxpayer's request for APA. If there have been no such material differences, a statement to that effect.
2.	Statement of all material changes in the Taxpayer's accounting methods and classifications, and methods of estimation, from those described or used in Taxpayer's request for the APA. If there has been no material change in accounting methods and classifications or methods of estimation, a statement to that effect.
3.	Description of any failure to meet critical assumptions. If there has been none, a statement to that effect.
4.	Copy of the APA.
5.	Financial analysis demonstrating Taxpayer's compliance with TPM.
6.	Organizational chart.
7.	Any change to the taxpayer notice information in section 14 of the APA.
8.	The amount, reason for, and financial analysis of any compensating adjustment, for the APA year, including but not limited to: the amounts paid or received by each affected entity; the character (such as capital or ordinary expense) and country source of the funds transferred, and the specific line item(s) of any affected U.S. tax return; and any change to any entity classification for federal income tax purposes of any member of Taxpayer's group that is relevant to the APA.
9.	The amounts, description, reason for, and financial analysis of any book-tax difference relevant to the TPM for the APA year, as reflected on Schedule M-1 or Schedule M-3 of the U.S. return for the APA year.
10.	Financial statements and any necessary account detail to show compliance with the TPM, with a copy of the opinion from an independent certified public accountant or other documentation required by paragraph 5(f) of the APA.
11.	Where required by paragraph 5(f) of the APA, certified public accountant's opinion that financial statements present fairly the financial position of Taxpayer and the results of its operations, in accordance with a foreign GAAP.
12.	Where applicable, financial statements as prepared in accordance with a foreign GAAP.
13.	Various work papers.
14.	Where applicable, a review of the financial statements by a certified public accountant.

⁸³ 2015 APMA Statutory Report. Retrieved from <https://www.irs.gov/pub/irs-utl/2015apmastatutoryreport.pdf>.

Appendix 4: Human Ethics Approval Letter



HUMAN ETHICS COMMITTEE

Secretary, Lynda Griffioen
Email: human-ethics@canterbury.ac.nz

Ref: HEC 2015/108

23 September 2015

Mohammad Abu-Hijleh
Department of Accounting & Information Systems
UNIVERSITY OF CANTERBURY

Dear Mohammad

The Human Ethics Committee advises that your research proposal "An evaluation of the New Zealand advance pricing agreement process" has been considered and approved.

Please note that this approval is subject to the incorporation of the amendments you have provided in your email of 22 September 2015.

Best wishes for your project.

Yours sincerely

A handwritten signature in black ink, appearing to read 'L. MacDonal'.

Lindsey MacDonal
Chair
University of Canterbury Human Ethics Committee

Appendix 5: Information Sheet for Interviews

Information Sheet

University of Canterbury

Department of Accounting and Information Systems

Email: [mab284@uclive.ac.nz]

Date: / /



“An evaluation of the New Zealand Advance Pricing Agreement Process”

I, Mohammed Abu-Hijleh invite you to participate as an interviewee in the research project: “An evaluation of the New Zealand Advance Pricing Agreement Process.” This project seeks to evaluate the NZ Advance Pricing Agreement (APA) process initiated by the IRD. This evaluation will consist of three main parts:

- documentation of the NZ process itself;
- a critical evaluation of certain aspects of the process from various parties’ points-of-view; and
- a comparative analysis of selected overseas’ APA processes relative to the NZ process.

Your participation in this research will be in the form of a semi-structured interview regarding the NZ APA process. You have the right to withdraw at any stage of this interview, including the withdrawal of information without penalty. This interview will take 45 minutes – 60 minutes. If you agree to participate, an electronic copy of the consent form will be emailed to you; signed consent forms must be returned by email to the researcher for your data to be used.

A follow up enquiry might be needed in the form of an email or quick phone-call; you will be asked to comment on further matters arising from other interviews. Participation at the follow up stage is also voluntary. A copy of the research summary can be requested at the conclusion of the project by mid-2016.

The results of the project may be published, but you may be assured of the complete confidentiality of data gathered in this interview: your identity will not be made public without prior consent. Any data I or my supervisors assess as being sensitive will be sent back to you for approval. To ensure anonymity and confidentiality, all data gathered will be securely and safely stored at the University of Canterbury’s database servers. Only the researcher and his two supervisors will have access to the data. A thesis is a public document and will be available through the UC Library.

The project is being carried out as a requirement for the Master of Commerce Degree by Mohammed Abu-Hijleh under the supervision of Professor Adrian Sawyer and Associate Professor Andrew Maples, who can be contacted at **+64 3 364 2617**, or **+64 3 364 2636**, respectively. They will be pleased to discuss any concerns you may have about participation in the project.

This project has been reviewed and approved by the University of Canterbury Human Ethics Committee, and participants should address any complaints to the Chair, Human Ethics Committee, University of Canterbury, Private Bag 4800, Christchurch (human-ethics@canterbury.ac.nz).

If you agree to participate in the study, you are asked to complete a consent form.

Appendix 6: Consent Form for Interviews

Consent Form

University of Canterbury

Department of Accounting and Information Systems

Email: [mab284@uclive.ac.nz]

Date: / /



Consent Form

“An evaluation of the New Zealand Advance Pricing Agreement Process”

I have been given a full explanation of this project and have had the opportunity to ask questions.

I understand what is required of me if I agree to take part in the research. I understand that participation is voluntary and I may withdraw at any time without penalty.

Withdrawal of participation will also include the withdrawal of any information I have provided should this remain practically achievable.

I understand that any information or opinions I provide will be kept confidential to the researcher and his two supervisors and that any published or reported results will not identify the participants or their institution.

I understand that a thesis is a public document and will be available through the UC Library.

I understand that all data collected for the study will be kept in locked and secure facilities and in password protected electronic form and will be destroyed after five years.

I understand the risks associated with taking part and how they will be managed.

I understand that I am able to receive a report on the findings of the study by contacting the researcher at the conclusion of the project by mid-2016.

I understand that I can contact the researcher Mohammed Abu-Hijleh at **+64 220 34 8387** or his supervisors, Professor Adrian Sawyer and Associate Professor Andrew Maples, who can be contacted at **+64 3 364 2617**, or **+64 3 364 2636** for further information. If I have any complaints, I can contact the Chair of the University of Canterbury Human Ethics Committee, Private Bag 4800, Christchurch (humanethics@canterbury.ac.nz)

NAME (please print):

Signature:

Date:

Please tick this box if you would like to receive a copy of the report of the project

Please return consent form via email: mab284@uclive.ac.nz

Appendix 7: Sections 6, 7 and 12 of the Practice Statement Law Administration (PS LA) 2015/4

6. What makes the ATO more likely to enter into an APA?

6A. While single indicators may point in one direction or the other, ATO staff are to consider each APA request on balance having regard to all the relevant facts and circumstances in the context described in section 3. No one indicator is, of itself, determinative. However, transparency as to the material facts is essential.

6B. The ATO may be more likely to enter into an APA where one or more of the indicators set out below are present:

- the transfer pricing methodology proposed best achieves consistency with the OECD guidelines as at 22 July 2010
- the cross border conditions between entities (actual conditions) that are the subject of the proposed APA have already been entered into and the actual conditions are unlikely to change significantly in the period of the APA
- a proposed arrangement is under serious contemplation² and the proposed actual conditions are unlikely to change significantly in the period of the APA
- the transfer pricing issues are complex and there is uncertainty as to how the transfer pricing rules apply
- without an APA, the probability of economic double taxation is high.

7. What makes the ATO less likely to enter into an APA?

7A. Following on from section 6, the ATO may be less likely to enter into an APA where one or more of the indicators set out below are present:

- the actual conditions are simple or routine with arm's length conditions being relatively certain
- the value of the cross border dealings is not material³
- the cross border dealings to be covered by the APA are only a small portion in terms of value of the total cross border dealings
- the proposed APA would not ensure there is alignment between true economic activity and profit outcomes in Australia (refer to section 4)
- collateral issues that affect the ATO's ability to enter into the proposed APA
- the arrangements that are the subject of the proposed APA appear to lack commerciality or be primarily tax driven, for example, the proposed APA covers activities which involve structures, restructuring or greenfields arrangements⁴ where the commercial benefits to the Australian entity are questionable.

7B. The availability of carried-forward losses and meeting the eligibility criteria for the 'Simplifying transfer pricing record keeping' online guidance do not preclude the ATO and the taxpayer from entering into an APA. However, in instances where a taxpayer has opted to apply the 'Simplifying transfer pricing record keeping' online guidance to some or all of its activities, the ATO considers that the taxpayer may be less likely to request an APA in respect of the cross border dealings covered by the on-line guidance.

7C. Where carried forward losses are available to a taxpayer, the APA team are to treat this aspect as a collateral issue (refer to section 22) and understand the reasons behind those losses being incurred.

12. What does the APA team leader consider when deciding whether the ATO will invite the taxpayer to lodge a formal APA application?

12A. In determining whether the ATO will invite the taxpayer to lodge a formal APA application, the APA team leader should consider the taxpayer's relevant facts and circumstances in the context of the global value chain and other steps or arrangements with which they might be linked.

12B. The APA team leader should also consider these facts and circumstances against the matters listed below and any other relevant matters, rather than restrict their analysis only to the actual cross border conditions between entities ('actual conditions') that are the subject of the proposed APA.

12C. In addition to the indicators in sections 6 and 7, the matters the APA team leader is to consider can include whether:

- the information provided allows for a full and proper consideration by the ATO of the APA request
- there is an explanation that demonstrates that the actual conditions are relevant and material to the taxpayer's business¹²
- the transfer pricing risks and issues arising from the actual conditions warrant the allocation of resources required for an APA
- an APA is a suitable product for the taxpayer, given their classification in the Risk Differentiation Framework (RDF), the taxpayer's compliance history (locally and globally) and its performance under any previous APA
- one of the parties to the cross border dealings or an associate is likely to get a tax benefit from the structures, transactions or actual conditions that are the subject of the proposed APA and that tax benefit may be obtained to the detriment of another party to the dealings
- the transfer pricing method (TPM) proposed under the APA is unlikely to result in the taxpayer getting a transfer pricing benefit and the TPM best achieves consistency with the guidance material for the purposes of section 815-135 of the ITAA 1997
- in the absence of an APA, there is a likelihood that the actual conditions may result in double taxation or in a dispute
- a significant part of a limited life project has not yet been completed
- the ATO anticipates that the parties will agree all aspects of the APA in a timely manner
- collateral issues are capable of being resolved prior to or in parallel with the APA (refer to section 22).

12D. This list is not exhaustive. No one matter is determinative. Rather, any decision is to be made on balance after considering all relevant circumstances. Furthermore, one matter does not necessarily have any greater weighting relative to another.

12E. Such decisions involve the APA team leader using professional judgment in light of the APA team's analysis of these matters in relation to each taxpayer's facts and circumstances.