

DRAFT FOR PUBLIC DISCUSSION

TEMPLATE FOR ADVANCE PRICING AGREEMENT TO BE ISSUED UNDER REVENUE PROCEDURE 2015-41

The Advance Pricing and Mutual Agreement Program (“APMA”) of the Internal Revenue Service (“IRS”) is providing this template for use in drafting advance pricing agreements (“APAs”) issued under IRS Revenue Procedure 2015-41, 2015-35 I.R.B. 263 (“Rev. Proc. 2015-41”). This template is designed to systematize how taxpayers propose terms for their APAs and standardize language used in executed APAs. It will improve efficiency in the APA process and enhance consistency in the administration of the APA program.

Rev. Proc. 2015-41 requires that taxpayers include as part of a complete APA request a draft APA and a “redline” comparison of the proposed draft APA against the current model APA. See section 2.03, exhibit 15, of the Appendix to Rev. Proc. 2015-41. This template serves as the model APA. A taxpayer is required to produce the “redline” comparison by following the instructions below to edit this template with tracked changes. The draft APA and “redline” comparison are then to be included in Word format in the complete APA request.

The assigned APMA team will review the APA’s terms proposed in the draft APA. If the APMA team accepts the proposed terms in light of its review of the taxpayer’s complete APA request and other information obtained during the APA process, then the text of the draft APA, edited as needed to fill in any information not available at the time of the APA Request, will be adopted as the text of a finally executed APA. If the APMA team does not accept the proposed terms, it will discuss modifications to the draft APA with the taxpayer during the APA process. For bilateral and multilateral APAs, the terms of the executed APA will of necessity be consistent with the terms of the underlying Mutual Agreement between the United States and one or more treaty partners.

GENERAL INSTRUCTIONS

The template is designed to minimize editing by using an options-based format for selecting from terms presented in certain sections of the model APA. The options presented are those which APMA considers standard and which in appropriate cases APMA has accepted, or is willing to accept, in final APAs. APMA reserves the right to modify the option selections, the specific option language used, or any other terms, in specific cases if APMA decides that the draft APA proposed by the taxpayer is not acceptable in light of the APMA team’s due diligence during the APA process.

Options are indicated by square brackets (“[]”). An “x” should be inserted between the brackets to indicate the selected option (“[x]”). Options that are not selected should not be deleted, but instead should be left in the text of the draft APA. The options to which APMA and the taxpayer ultimately agree for the final APA will be indicated by the presence or absence of an “x”. The term associated with the “x” will be given operative effect in the executed APA.

Certain options are flagged with an asterisk after the square brackets (“[*]”). To facilitate the APMA team’s subsequent review of the draft APA, the asterisks should not be deleted. Taxpayers that select flagged options are required to specifically provide justification for the selection in the APA request. See section 1.02, Part 5, of the Appendix to Rev. Proc. 2015-41.

The template contains placeholder phrases consisting of a hashtag followed by one or more words in block capital letters (e.g., “#COUNTRY”). Generally, the taxpayer should replace a placeholder phrase with appropriate text, subject to the following conventions:

- If a placeholder phrase occurs within an option that the taxpayer has rejected, the taxpayer should change the hashtag to a caret (e.g., change “#COUNTRY” to “^COUNTRY”) but otherwise leave the phrase intact.¹ The caret indicates that the Taxpayer has rejected this option. For example, for a bilateral APA with Japan, the lines on the first page just below the title would read:

[x] Bilateral with Japan
[] Multilateral with ^COUNTRIES
[] Unilateral

- The placeholder phrase “#CURRENCY” should be replaced, for example, with “U.S. dollars,” “Euros,” or “Japanese yen.”
- The placeholder phrase “#DATE” should be replaced with a date in the format of “December 31, 2020.”

The APA Term will be expressed as dates certain, e.g., “January 1, 2017 to December 31, 2022, inclusive”, rather than as particular tax years.

Taxpayers may need to draft text for situations or options not included in the template, such as additional critical assumptions.

¹ As a result, almost all occurrences of the hashtag in the template will be replaced with a caret or other text in the taxpayer’s draft APA. The few remaining occurrences of the hashtag will mark a placeholder phrase that cannot yet be replaced with appropriate text (see, for example, the placeholder phrase in paragraph 6(e) for a date that cannot be determined until the APA nears execution). Searching the draft APA for the hashtag will locate all placeholder phrases that still need replacement.

INSTRUCTIONS ON TABLES

The template contains certain tables that the taxpayer should edit. Entries in the tables will not contain hashtags, but taxpayers nevertheless should fill in the information and add additional rows to the tables if needed. Taxpayers also should fill in the “APA Information” in the table in Appendix D, to the extent available or proposed.

INSTRUCTIONS ON APPENDIX A

Appendix A of this template contains the description of the APA’s covered issue(s) and covered method(s). Taxpayers should note the following points in completing Appendix A:

- The template includes just one covered issue with one corresponding covered method. If there is more than one covered Issue proposed for the APA, the taxpayer should add additional covered issues in Appendix A, section 3, with tracked changes.
- If there is more than one covered method, the taxpayer should first replicate the template’s entire text for Covered Method 1 in Appendix A, section 4, without tracked changes, to provide template text for each additional covered method, and then edit the text for each covered method with tracked changes.
- Normally, each covered issue will have its own corresponding covered method. However, in some cases, a covered method may apply at once to more than one covered issue. For example, covered issues may be proposed to be aggregated and tested by a single covered method. In such cases, the heading for that covered method could read, for example, “Covered Method for Covered Issues 1-3”.
- Any interaction between different covered methods should be adequately explained in the text, and in an appropriate manner. For example, an explanation might be provided in an introduction at the start of section 4 of Appendix A, preceding the description of the respective covered methods.

Appendix A uses the term “Tested Party.” When applied in the context of methods that consider, or test, data from only one party to a transaction, this term is similar in concept to the term “tested party” as defined in the OECD Guidelines paragraphs 3.18 and 3.19, and in the U.S. Treasury Regulations section 1.482-5(b)(2). However, some methods consider, or test, data from both parties to a transaction, where there is no singular “tested” party. Even in applying such methods, however, it is typically the case that one particular party’s results are formally tested for compliance with the method. For purposes of this template, in such circumstances, the party whose results are formally tested in applying any particular method is the “Tested Party”, even

if that party is not strictly a “tested party” as defined in the OECD Guidelines paragraphs 3.18 and 3.19, and in the U.S. Treasury Regulations section 1.482-5(b)(2).

DRAFT for Public Discussion

ADVANCE PRICING AGREEMENT
between
ACME US, INC.
and
THE INTERNAL REVENUE SERVICE

Deleted: #SIGNATORY

- Bilateral with Japan
 Multilateral with COUNTRIES
 Unilateral

Deleted: #COUNTRY

Deleted: #

Term: January 1, 2016 to December 31, 2020, inclusive

Deleted: #DATE to #DATE

This APA is commonly referred to as the Acme Example APA.

Deleted: #APA NAME

PARTIES

The Parties to this APA are the Internal Revenue Service ("IRS") and Acme US, Inc., EIN: 99-1111111.

Deleted: #NAME OF EACH NON-IRS SIGNATORY, WITH EIN

Acme US, Inc. will be referred to as "U.S. Taxpayer."

Deleted: #SIGNATORY

SIGNATORY is the common parent of an affiliated group filing consolidated U.S. tax returns, and is entering into this APA on behalf of both itself and the following members of its consolidated group:

Deleted: #

MEMBERS OF GROUP. All members of this consolidated group will be referred to collectively as "U.S. Taxpayer."

Deleted: #

RECITALS

This APA is a renewal of one or more prior APAs, which are listed below in reverse chronological order:

Party(ies)	Execution Date	Term

Key:

- **Party(ies)**: The signatory(ies) to the prior APA, other than the IRS, with each signatory's taxpayer identification number;
- **Execution Date**: The date, or the later of the dates, on which the prior APA was executed;
- **Term**: The term of the prior APA.

This is a bilateral APA within the meaning of Rev. Proc. 2015-41 and implements the terms of a mutual agreement reached between the United States and Japan.

Deleted: #COUNTRY

This is a multilateral APA within the meaning of Rev. Proc. 2015-41 and implements the terms of a mutual agreement reached among the United States, COUNTRIES.

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This APA is a unilateral APA within the meaning of Rev. Proc. 2015-41 and is not based on any mutual agreement.

The Parties to this APA are defined in the "Parties" section above. Regarding the Party(ies) to this APA other than the IRS:

No such Party has an immediate parent or owner that is not a U.S. entity.

One or more such Parties has an immediate parent or owner that is not a U.S. entity, as follows:

Party	Parent's or Owner's Identifying Information	Parent's or Owner's Contact Information
<u>Acme US, Inc.</u>	<u>Acme Japan, Ltd.</u> <u>Japan Tax ID: 990123456789</u>	<u>1-2-3 Tokyo Street,</u> <u>Tokyo, Japan, 100-100</u> <u>+81-99-999 9999</u>

Key:

- **Party:** Name of the Party having an immediate parent or owner that is not a U.S. entity;
- **Parent's or Owner's Identifying Information:** Name of the immediate parent or owner of such Party, and the taxpayer identification number of that parent or owner for income tax purposes in its country of residence;
- **Parent's or Owner's Contact Information:** The immediate parent's or owner's address and phone number.

The term "Worldwide Group" is defined below in paragraph 12 of this APA. The ultimate parent entity or owner of Worldwide Group is:

Acme Japan, Ltd.
1-2-3 Tokyo Street
Tokyo, Japan, 100-100
+81-99-999 9999,

Deleted: #ENTITY NAME, ADDRESS, AND PHONE

U.S. Taxpayer's principal place of business is Home, State. U.S. Taxpayer is a supplier of Japanese manufactured auto parts to U.S. automakers and original

equipment manufacturers. It also provides research and development and design-in services to the Japan Parent Company. Acme Japan, Ltd. is a global electronics company.

Deleted: #CITY, #STATE. #BRIEF DESCRIPTION OF U.S. TAXPAYER AND NON-U.S. TAXPAYER (DEFINED IN SECTION 1 OF APPENDIX A), AND SPECIFICALLY OF EACH COVERED ENTITY (DEFINED IN SECTION 1 OF APPENDIX A).

This APA contains the Parties' agreement on the Covered Method(s) for resolving the Covered Issue(s) under Code section 482 and any other Code sections that are identified in Appendix A to this APA, the U.S. Treasury Regulations thereunder, and (if applicable):

The income tax convention(s) between the United States and Japan.

Deleted: #COUNTRY(IES).

This APA shall not limit the authority of the IRS to (1) verify compliance with this APA as to the Covered Issue(s), or (2) audit issues other than Covered Issue(s), including issues that arise under Code section 482 and any other Code sections identified in Appendix A to this APA, and the U.S. Treasury Regulations thereunder.

LIMITATION ON ASSISTANCE

The Covered Issue(s) may relate to one or more countries which (i) have an income tax convention with the United States, but (ii) are not a party to a mutual agreement whose terms are implemented by this APA. U.S. Taxpayer acknowledges that the IRS may decline to provide competent authority assistance concerning taxation by such country(ies) that relates to the Covered Issue(s). See section 2.02(4)(d) of Rev. Proc. 2015-41.

AGREEMENT

The Parties agree as follows:

1. *Covered Entities.* This APA's Covered Entities are defined in Appendix A.
2. *Covered Issue(s).* This APA applies to the Covered Issue(s), as defined in Appendix A.
3. *Covered Method(s).* Appendix A sets forth the Covered Method(s) for the Covered Issue(s).
4. *Term.* This APA applies to the APA Term, as defined in Appendix A.
5. *Operation.*
 - a. Rev. Proc. 2015-41 governs the interpretation, legal effect, and administration of this APA.
 - b. The APMA program provides a voluntary process whereby the IRS and taxpayers may resolve transfer pricing issues and issues for which transfer pricing principles may be relevant in a principled and cooperative manner on a prospective basis. As such, the APA process (as defined in Rev. Proc. 2015-41) is an alternative to dispute resolution that benefits both taxpayers and the IRS and that is intended to promote and encourage open communication. Accordingly, the IRS and U.S. Taxpayer agree that neither party will attempt to use nonfactual oral or written representations, within the meaning of sections 6.04 and 6.05 of IRS Revenue Procedure 2015-41 (including any proposals to use particular Covered Method(s)), made in conjunction with the APA Request in any judicial or administrative proceeding. The IRS and U.S. Taxpayer also agree that factual representations made in conjunction with the APA Request may be used in judicial and administrative proceedings.
6. *Compliance.*
 - a. U.S. Taxpayer must report its taxable income in an amount that is consistent with Appendix A and all other requirements of this APA. U.S. Taxpayer must so report its taxable income in the following manner:
 - i. For any APA Tax Year for which U.S. Taxpayer timely files its original U.S. return prior to, or no later than 60 days after, the U.S. Effective Date, U.S. Taxpayer must so report its taxable income for that APA Tax Year in one of the following ways:
 - A. on such original U.S. return;

- B. on an amended U.S. return submitted no later than 120 days after the U.S. Effective Date;
- C. through a means proposed by U.S. Taxpayer and accepted by the applicable IRS field examination group no later than 120 days after the U.S. Effective Date (or by such other deadline as is agreed between U.S. Taxpayer and the applicable IRS field examination group); or
- D. if applicable:
 - [] no later than 120 days after the U.S. Effective Date through the following means: [^]DESCRIPTION OF MEANS.

Deleted: #

- ii. For all other APA Tax Years, U.S. Taxpayer must so report its taxable income on its timely filed original U.S. return.
- iii. The provisions of paragraphs 6(a)(i) and 6(a)(ii) are modified by this paragraph 6(a)(iii). If a Covered Method includes a term test (including the case of an annual test with a supplemental term test) or a subterm test, as described in section 4 of Appendix A, then the APA Covered Year as of which the term test or subterm test applies would change in the event of an Early Termination. Specifically, while in the absence of an Early Termination a term test would apply as of the last APA Covered Year, in the event of an Early Termination the term test would apply as of an earlier APA Covered Year. Similarly, while in the absence of an Early Termination a subterm test would apply as of the last APA Covered Year in the subterm, in the event of an Early Termination the subterm test might apply as of an earlier APA Covered Year. In these situations, the Early Termination might not be established in time for U.S. Taxpayer to know to apply the term test or subterm test as of the earlier APA Covered Year in reporting taxable income as required under paragraphs 6(a)(i) and 6(a)(ii) for the APA Tax Year corresponding to that earlier APA Covered Year. In such cases, U.S. Taxpayer may need to correct its reporting for that APA Tax Year. Specifically, U.S. Taxpayer will need to correct its income reporting for that APA Tax Year if the application of the term test or subterm test in that earlier APA Covered Year changes the existence or amount of an APA Primary Adjustment for the Covered Method for that APA Tax Year. In such cases:
 - A) The resulting incorrectness in the prior reporting for that APA Tax Year is excused; and

- B) U.S. Taxpayer must correct such prior reporting through a means listed in paragraph 6(a)(i) within 120 days of the Early Termination being established.

b. For each Covered Issue, if any, that involves determination of pricing and/or income allocation² under Code section 482 (or Code section 367(d)) as modified by any applicable income tax convention, this APA addresses the pricing and/or income allocation between U.S. Taxpayer and Non-U.S. Taxpayer in the aggregate. Except as explicitly provided, this APA does not address and does not bind the IRS with respect to pricing or income allocation (1) among particular legal entities that are members of U.S. Taxpayer, or (2) among particular legal entities that are members of Non-U.S. Taxpayer. In addition, this APA does not address pricing or income allocation between an entity that is not a Covered Entity, and any entity.

c. For each APA Tax Year, if U.S. Taxpayer complies with the terms and conditions of this APA, then, provided that this APA remains effective for that APA Tax Year for a particular Covered Issue, the IRS will not make or propose any allocation or adjustment that is inconsistent with the application under this APA of the applicable Covered Method to that Covered Issue.

d. If U.S. Taxpayer does not comply with the terms and conditions of this APA, then the IRS may:

- i. enforce the terms and conditions of this APA and make or propose allocations or adjustments based on the application of the Covered Method(s) to the Covered Issue(s) as provided in this APA;
- ii. cancel or revoke this APA under section 7.06 of Rev. Proc. 2015-41; or
- iii. revise this APA, if the Parties agree.

e. U.S. Taxpayer must timely file an Annual Report for each APA Tax Year in accordance with this paragraph 6(e), Appendix C to this APA, and section 7.02 of Rev. Proc. 2015-41. Annual Reports for multiple APA Tax Years may be combined, provided that all required information for each APA Tax Year is clearly presented. For each Annual Report, U.S. Taxpayer must submit an original printed version containing a signed original "penalties of perjury" declaration, one printed copy of the contents of the original printed version, and an electronic copy of the contents of the original printed version. Any exhibits in the printed version must be tabbed, and the electronic copy is subject to the same requirements, as to medium and format, that are specified for APA requests in section 2 of the Appendix to Rev. Proc. 2015-41. Upon request, U.S. Taxpayer must provide additional copies of the printed version, at addresses specified by the IRS. U.S. Taxpayer must file the Annual Report for each APA Tax Year by the later of (i) #DATE CERTAIN, NORMALLY APPROXIMATELY 90 DAYS AFTER THE

² As used in this APA, "income allocation" includes allocation of loss.

U.S. EFFECTIVE DATE, and (ii) the fifteenth day of the twelfth month following the close of the APA Tax Year. The IRS may by notice request additional information reasonably necessary to clarify or complete the Annual Report. (See paragraph 16, and section 3(c) of Appendix C, regarding notices.) U.S. Taxpayer will provide such requested information within 30 days from the date of the notice unless a later date is specified in the notice. Additional time may be allowed for good cause in the discretion of the Director of the Advance Pricing and Mutual Agreement Program.

Comment [A1]: This placeholder phrase cannot be filled in until the APA process nears completion (that is, until the APA is close to being executed).

f. The IRS will determine whether U.S. Taxpayer has complied with this APA based on U.S. Taxpayer's U.S. returns, the Financial Statements and additional statements required under this paragraph 6(f), and other APA Records, for all APA Tax Years and any other tax year necessary to verify compliance. The Financial Statements and additional statements required for a particular tax year are:

Comment [A2]: For example, if a Covered Method uses a three-year rolling average test, then financial data from certain tax years before the APA term will be used in applying the Covered Method.

For every U.S. Covered Entity, the Financial Statements together with the additional statements specified in paragraph 6(f)(i); and for every Non-U.S. Covered Entity, the Financial Statements together with the additional statements specified in paragraph 6(f)(ii).

* For every U.S. Covered Entity, the Financial Statements together with the additional statements specified in paragraph 6(f)(i).

* For every Non-U.S. Covered Entity, the Financial Statements together with the additional statements specified in paragraph 6(f)(ii).

i. For each U.S. Covered Entity, the additional statements consist of the following statement(s):

An audit opinion for that U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

* One or more of the following, as indicated:

An accountant's report for that U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

A self-certification for that U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

A self-certification for that U.S. Covered Entity's Financial Statements, together with a tying certification for that entity's Financial Statements, as defined in paragraph 6(f)(iii).

~~OTHER MEANS OF VERIFYING THE RELIABILITY OF THE U.S. COVERED ENTITY'S FINANCIAL STATEMENTS.~~

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ii. For each Non-U.S. Covered Entity, the additional statements consist of the following statement(s):

An audit opinion for that Non-U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

* One or more of the following, as indicated:

An accountant's report for that Non-U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

A self-certification for that Non-U.S. Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

A self-certification for that Non-U.S. Covered Entity's Financial Statements, together with a tying certification for that Covered Entity's Financial Statements, as defined in paragraph 6(f)(iii).

~~OTHER MEANS OF VERIFYING THE RELIABILITY OF THE NON-U.S. COVERED ENTITY'S FINANCIAL STATEMENTS.~~

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iii. With reference to the Financial Statements for a particular Covered Entity for a particular tax year, certain terms used in paragraphs 6(f)(i) and 6(f)(ii) are defined as follows:

A. An audit opinion is an opinion of an independent certified public or chartered accountant who audited the Financial Statements.

B. An accountant's report is a report of an independent certified public or chartered accountant who is associated with the Financial Statements.

C. A self-certification is an attestation, as defined in paragraph 6(f)(iii)(E), that the Financial Statements have been prepared according to the Applicable Accounting Standard.

D. A tying certification consists of the following:

- (1) An attestation, as defined in paragraph 6(f)(iii)(E), that the Financial Statements can be reconciled to the consolidated Financial Statements for that entity's direct or indirect parent according to workpapers provided with the attestation;
- (2) The workpapers referred to in paragraph 6(f)(iii)(D)(1), which must demonstrate the consolidation of the Covered Entity's Financial Statements into the Financial Statements of the parent referred to in paragraph 6(f)(iii)(D)(1);
- (3) The Financial Statements of the parent referred to in paragraph 6(f)(iii)(D)(1); and
- (4) An audit opinion (as defined in paragraph 6(f)(iii)(A)) for the Financial Statements of the parent referred to in paragraph 6(f)(iii)(D)(1).

E. An attestation is an affirmation by an officer of the Covered Entity in the following form:

I, [Officer's Name and Title], of [Name of Covered Entity] affirm under penalties of perjury that the facts stated below are true. I either have adequate first-hand knowledge to make this affirmation, or have gained adequate knowledge to make this affirmation through diligent consultation(s) with one or more individuals who have first-hand knowledge.

[Facts attested to.]

[Signature]

g. In accordance with section 7.04 of Rev. Proc. 2015-41, U.S. Taxpayer will (1) maintain the APA Records, and (2) make them available to the IRS in connection with an examination under section 7.03 of Rev. Proc. 2015-41. Compliance with this subparagraph constitutes compliance with the record-maintenance provisions of Code sections 6038A and 6038C for the Covered Issue(s) for any APA Covered Year.

h. The "true taxable income" within the meaning of U.S. Treasury Regulations sections 1.482-1(a)(1) and (i)(9) of a member of an affiliated group filing a U.S. consolidated return will be determined under the U.S. Treasury Regulations under Code section 1502.

Comment [A3]: If a tax year is only partly within the APA Term, then compliance with this subparagraph satisfies the record-maintenance provision of Code sections 6038A and 6038C only regarding the portion of that tax year that is within the APA Term. See the definitions of APA Tax Year and APA Covered Year in section 2 of Appendix A.

i. To the extent that U.S. Taxpayer's compliance with this APA depends on certain acts of other members of Worldwide Group, U.S. Taxpayer will ensure that such other members will perform such acts.

7. *Critical Assumptions.* The Critical Assumptions, which are this APA's critical assumptions as defined in Rev. Proc. 2015-41, appear in Appendix B. If any Critical Assumption has not been met, then Rev. Proc. 2015-41, section 7.06, governs, as modified by Appendix B to this APA.

8. *Disclosure.* This APA, and any background information related to this APA or the APA Request, are: (1) considered "return information" under Code section 6103(b)(2)(C); and (2) not subject to public inspection as a "written determination" under Code section 6110(b)(1). Section 521(b) of Pub. L. 106-170 provides that the Secretary of the Treasury must prepare a report for public disclosure that includes certain specifically designated information concerning all APAs, including this APA, in a form that does not reveal taxpayers' identities, trade secrets, and proprietary or confidential business or financial information.

9. *Disputes.* If a dispute arises concerning the interpretation or application of this APA, the Parties will seek a resolution by the Director, Treaty and Transfer Pricing Operations, to the extent reasonably practicable, before seeking alternative remedies.

10. *Materiality.* In this APA the terms "material" and "materially" will be interpreted in a manner consistent with the description of "material facts" in Rev. Proc. 2015-41, section 7.06(4).

11. *Paragraph Captions.* This APA's paragraph captions, which appear in italic type, are for convenience and reference only. The captions do not affect in any way the interpretation or application of this APA.

12. *Terms and Definitions.*

a. Unless otherwise specified, terms in the plural include the singular and vice versa.

b. Appendix A contains definitions for certain terms used in this APA's body and appendices.

c. Certain terms used in this APA's body and appendices are defined as follows:

Comment [A4]: Appendix A contains most of the defined terms. Appendix A could be adapted for use in a Mutual Agreement, and therefore contains terms that would need to be understood by or agreed with treaty partners. Certain terms are defined in the body of the APA instead of Appendix A (see paragraph 12(c) below); the definitions for those terms would not be part of a Mutual Agreement. Those terms are omitted from Appendix A either because they are already well understood by treaty partners (e.g., "APA" or "Critical Assumptions"), and thus do not need to be defined there, or because they concern U.S. domestic enforcement and are not typically of interest to a treaty partner (e.g. "Financial Statements").

The terms "IRS" and "U.S. Taxpayer" are defined both at the start of the APA, and in Appendix A.

The term "U.S. Effective Date" is also defined twice (see the table in paragraph 12(c) below).

Term	Definition
Annual Report	A report within the meaning of Rev. Proc. 2015-41, section 7.02.
Advance Pricing Agreement, or "APA"	An "advance pricing agreement" within the meaning of Rev. Proc. 2015-41, section 2.02. Unless context indicates otherwise, "this APA" or "the APA" denotes the particular APA that is executed below.
APA Records	(Defined in Appendix C.)
APA Request	U.S. Taxpayer's request for this APA, which was dated <u>January 5, 2016</u> , including any amendments or supplemental or additional information thereto (including but not limited to any responses to due diligence questions).
Critical Assumptions	(Defined in paragraph 7.)
Financial Statements	Balance sheet, income statement, statement of cash flow, and explanatory notes, prepared in accordance with the Applicable Accounting Standard as defined in section 8 of Appendix A.
Non-U.S. Group	In any APA Tax Year, Worldwide Group members that are not U.S. persons.
Parties	(Defined in the Recitals near the start of this APA.)
Pub. L. 106-170	The Ticket to Work and Work Incentives Improvement Act of 1999.
U.S. Effective Date	(Defined in paragraph 17 and in section 8 of Appendix A. Those definitions are intended to have the same meaning. In case of conflict, the definition in paragraph 17 controls.)
U.S. Group	In any APA Tax Year, Worldwide Group members that are U.S. persons.
Worldwide Group	In any APA Tax Year, U.S. Taxpayer and all organizations, trades, businesses, entities, or branches (whether or not incorporated, organized in the United States, or affiliated) owned or controlled directly or indirectly by the same interests.

Deleted: #DATE

13. *Deadline References.* If a deadline under this APA falls on a Saturday, Sunday, or a legal holiday in the District of Columbia, the deadline is extended to the next succeeding day that is not a Saturday, Sunday, or legal holiday in the District of Columbia.

14. *Entire Agreement and Severability.* This APA is the complete statement of the Parties' agreement. The Parties will sever, delete, or reform any invalid or unenforceable provision in this APA to approximate the Parties' intent as nearly as possible.

15. *Successor in Interest.* This APA binds, and inures to the benefit of, any successor in interest to U.S. Taxpayer.

16. *Notice.* Any notices required by this APA or Rev. Proc. 2015-41 must be in writing. U.S. Taxpayer will send notices to the IRS at:

Commissioner, Large Business and International Division
Internal Revenue Service
1111 Constitution Avenue, NW
SE:LB:TTPO:APMA:NCA534-01
Washington, DC 20224
(Attention: APMA)

The IRS will send notices to:

Acme US, Inc.
Attn: Joe Doe
1234 Market Street
Home, State, 88888-1111
(999) 123-4567

Deleted: #NAME AND ADDRESS¶
(phone: #PHONE)¶

The IRS also will send notices to, if applicable:

□ Representative
Lawyer
Law Firm Address
(999) 123-4567

Deleted: #REPRESENTATIVE'S
NAME AND ADDRESS¶
- (phone: #PHONE)

provided that a valid IRS Form 2848 "Power of Attorney and Declaration of Representative" for that person was included in the most recent Annual Report (or, if no Annual Report has been filed, was included in the APA Request).

17. *U.S. Effective Date and Counterparts.* This APA is effective starting on the date, or later date of the dates, upon which all Parties execute this APA ("U.S. Effective Date"). The Parties may execute this APA in counterparts, with each counterpart constituting an original.

WITNESS,

The Parties have executed this APA on the dates below.

ACME US, INC.,

Deleted: #SIGNATORY NAME IN BOLD
FACE BLOCK CAPITAL LETTERS

By: _____ Date: _____, 20____

Joe Doe
Vice President Taxes

Deleted: - #NAME¶
#TITLE¶

INTERNAL REVENUE SERVICE

By: _____ Date: _____, 20____
John C. C. Hughes
Director, Advance Pricing and Mutual Agreement Program

DRAFT for Public Discussion

**APPENDIX A
COVERED ENTITIES, TERM, COVERED ISSUE(S), COVERED METHOD(S),
INCOME REPORTING,
CONFORMING ADJUSTMENTS AND REPATRIATION OF FUNDS,
CERTAIN SUBSEQUENT ADJUSTMENTS,
AND DEFINITIONS**

Section 1 of this Appendix lists the Covered Entities. Section 2 defines the APA Term, APA Tax Years, and APA Covered Years. Section 3 describes the Covered Issue(s). Section 4 describes the Covered Method applicable to each Covered Issue.

Section 5 describes the application of the Covered Method(s) to income reporting and the possible need for an APA Primary Adjustment under one or more Covered Methods. Section 6 addresses conforming adjustments and repatriation of funds following APA Primary Adjustments.

Section 7 addresses the effect of certain adjustments by tax authorities and resulting competent authority proceedings.

Section 8 provides definitions that apply both to this Appendix and to the APA as a whole. The definitions table is based on a standard, inclusive model, and thus may include terms not used in this APA.

1. Covered Entities

The U.S. Covered Entity(ies) are:

[Acme US, Inc. \("Acme-US"\)](#)
[1234 Market Street](#)
[Home, State, 88888-1111](#)
[\(803\) 575-4444](#)
[EIN: 99-1111111](#)

The term "U.S. Taxpayer" includes collectively all U.S. Covered Entities and any other entities that are in a consolidated return group with a U.S. Covered Entity.

The Non-U.S. Covered Entity(ies) are:

[Acme Japan, Ltd. \("Acme-Japan"\)](#)
[1-2-3 Tokyo Street](#)
[Tokyo, Japan, 100-100](#)
[+81-99-999 9999](#)

Deleted: #LIST OF EACH U.S. ENTITY INVOLVED IN ONE OR MORE COVERED ISSUE(S), AND ALSO (LISTED FIRST) ANY CONSOLIDATED RETURN PARENT FOR ANY SUCH ENTITY. FOR EACH ENTITY, NAME, ADDRESS, PHONE, AND EIN.¶

Deleted: # LIST OF EACH NON-U.S. ENTITY INVOLVED IN ONE OR MORE COVERED ISSUE(S), AND ALSO (LISTED FIRST) ANY COMMON TAX REPORTING PARENT FOR ANY SUCH ENTITY. FOR EACH ENTITY, NAME, ADDRESS, AND PHONE.¶

The term “Non-U.S. Taxpayer” includes collectively all Non-U.S. Covered Entities and any other entities that are in a common tax reporting group with a Non-U.S. Covered Entity.

The term “Covered Entities” includes both the U.S. Covered Entities and the Non-U.S. Covered Entities.

2. APA Term, APA Tax Years, and APA Covered Years

The APA applies to the period from January 1, 2016 to December 31, 2020, inclusive (the “APA Term”).

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The APA Term does not include a Rollback.

The APA Term includes a Rollback, which covers from DATE to DATE, inclusive (the “Rollback Period”).

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A tax year of U.S. Taxpayer that is wholly or partly contained in the APA Term is called an “APA Tax Year.” For a particular APA Tax Year, the portion of such APA Tax Year that is contained in the APA Term is called an “APA Covered Year.” Such APA Tax Year and APA Covered Year are said to “correspond” to each other or to be “corresponding.”

Comment [A5]: The terms “APA Covered Year” and “APA Tax Year” replace the term “APA Year” in the prior model APA. In most cases, each APA Covered Year and corresponding APA Tax Year are coextensive. However, if the APA Term begins or ends in the middle of a tax year, then such tax year will be an APA Tax Year that is not coextensive with the corresponding APA Covered Year. This situation might arise in the case of a tax year mismatch between U.S. Taxpayer and Non-U.S. Taxpayer, or if after an APA is executed U.S. Taxpayer is acquired by a company with a different tax year.

3. Covered Issue(s)

The Covered Issue(s) are as described below.

Covered Issue 1:

The purchase of finished widgets by Acme US from Acme-Japan for distribution to third parties.

Covered Issue 2:

The provision of research and development (“R&D”) and design-in services by Acme-US to Acme-Japan.

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4. Covered Method(s)

Each Covered Method applies to one or more Covered Issues. A Covered Method and the Covered Issue(s) to which the Covered Method applies are said to “correspond,” or to be “corresponding”.

The Covered Methods are summarized in the following table and are described in detail below. In case of conflict with this table, the detailed descriptions of the

Covered Methods below, and the descriptions in section 3 above of the Covered Issues, control.

Covered Method Number	Applies to Covered Issues Number(s)	Summary Description of Corresponding Covered Issues	Type of Method; Results Tested	Point or Range	Testing Frequency and Periods
1	1	<u>Distribution of goods</u>	<u>Transactional net margin / comparable profits; operating margin profit level indicator</u>	<u>1% to 3%</u>	<u>Annual</u>
2	2	<u>Provision of R&D services</u>	<u>Transactional net margin / comparable profits; markup on total costs profit level indicator</u>	<u>5% to 10%</u>	<u>Annual</u>

Covered Method for Covered Issue 1:

a. Tested Party

The Tested Party is Acme-US.

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b. Financial Results Tested (Type of Method)

[] The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the comparable uncontrolled price method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are:

[] per unit price paid, defined as the total amount paid for
~~DESCRIPTION OF GOODS~~ divided by the number of
~~DESCRIPTION OF A UNIT OF GOODS~~ purchased.

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[] per unit price received, defined as the total amount received for
~~DESCRIPTION OF GOODS~~ divided by the number of
~~DESCRIPTION OF A UNIT OF GOODS~~ sold.

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[] The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the comparable

uncontrolled services price method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are:

[] per unit price paid, defined as the total amount paid for
^DESCRIPTION OF SERVICES divided by the number of
^DESCRIPTION OF A UNIT OF SERVICES received.

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[] per unit price received, defined as the total amount received for
^DESCRIPTION OF SERVICES divided by the number of
^DESCRIPTION OF A UNIT OF SERVICES provided.

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[] The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the comparable uncontrolled transaction method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the royalty rate paid for the license of ^DESCRIPTION OF LICENSED INTANGIBLE PROPERTY divided by the Tested Party's:

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[] sales revenue from sales of ^DESCRIPTION OF GOODS/SERVICES.

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[] ^OTHER ROYALTY BASE.

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[] The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the acquisition price method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

[] The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the market capitalization method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

[] The Covered Method is an implementation of the resale price method under the OECD Guidelines and of the resale price method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross profit margin from the sale of ^DESCRIPTION OF GOODS.

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[] The Covered Method is an implementation of the resale price method under the OECD Guidelines and of the gross services margin method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross services margin from the provision of ^DESCRIPTION OF SERVICES.

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[] The Covered Method is an implementation of the cost plus method under the OECD Guidelines and of the cost plus method under the U.S.

Treasury Regulations. The Tested Party's financial results to be tested are the gross profit markup.

- The Covered Method is an implementation of the cost plus method under the OECD Guidelines and of the cost of services plus method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross services profit markup from the provision of DESCRIPTION OF SERVICES.

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- The Covered Method is based on the principles of the low value-adding intra-group services approach under the OECD Guidelines and of the services cost method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the markup on total costs for providing DESCRIPTION OF SERVICES.

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- The Covered Method is an implementation of the transactional net margin method under the OECD Guidelines and of the comparable profits method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the:

- operating margin.
- markup on total costs.
- Berry ratio.
- return on operating assets.
- return on invested capital.

* OTHER PROFIT LEVEL INDICATOR, WITH DEFINITION.

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- The Covered Method is an implementation of the profit split (residual analysis) method under the OECD Guidelines and of the residual profit split method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is an implementation of the profit split (contribution analysis) method under the OECD Guidelines and of the comparable profit split method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is an implementation of an income based valuation technique as referenced in paragraph 6.153 of the OECD Guidelines and of the income method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

- The Covered Method is an implementation of (i) a sharing of the cost of current contributions in proportion to overall expected benefits, within a cost contribution arrangement under the OECD Guidelines, and (ii) a sharing of intangible development costs in proportion to reasonably anticipated benefits, within a cost sharing arrangement under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is a method that is not specified under the OECD Guidelines and not specified under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

Such financial results are determined according to the Applicable Accounting Standard, with the proviso that in determining such results, accounting principles and conventions that are generally accepted in the trade or industry must be used.

Such financial results are tested against a point or range as described below. The test is carried out with a frequency, and for certain time periods, as described below. If and when these financial results do not satisfy the test, they must be adjusted as described in section 5 of this Appendix A.

Comment [A6]: If the Covered Method involves any special adjustments to the Tested Party's data, those adjustments normally would be specified here.

c. Testing of Financial Results Against a Point or Range

The Tested Party's financial results are tested as follows:

- The financial results must equal ΔX .
- The financial results must be within an Arm's Length Range.
 - The Arm's Length Range is from 1% to 3% inclusive.
 - This Arm's Length Range has an associated Median value of ΔZ .
 - This Arm's Length Range has no associated Median value.
 - Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the annual test described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the term test described in subsection (d) below.
 - The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ .

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These Arm's Length Ranges have no associated Median value.

Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the subterm test described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the annual test described in subsection (d) below.

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The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ .

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These Arm's Length Ranges have no associated Median value.

Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the test for the first subterm described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the test for the second subterm described in subsection (d) below.

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The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ .

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These Arm's Length Ranges have no associated Median value.

OTHER DESCRIPTION, FOR EXAMPLE THE EVALUATION AND TESTING MECHANICS FOR A PROFIT SPLIT, AN INCOME METHOD, AN UNSPECIFIED METHOD, OR A SHARING OF COSTS UNDER A COST CONTRIBUTION ARRANGMENT/COST SHARING ARRANGEMENT.

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d. Testing Frequency and Testing Periods

The Tested Party's financial results are tested as of certain APA Covered Years, and for certain time periods, as follows:

The results are tested annually, meaning that they are tested as of each APA Covered Year, for a period consisting of that APA Covered Year.

There is no additional term test.

- [] There is an additional term test. For this test, the results are tested as of the Last Effective APA Covered Year, for the period consisting of the Last Effective APA Covered Year and all prior APA Covered Years.

The application of the annual test and the application of the additional term test are coordinated as described in section 5 of this Appendix A.

- [] The results are tested on a term basis, meaning that they are tested only once, as of the Last Effective APA Covered Year, for a period consisting of the Last Effective APA Covered Year and all prior APA Covered Years.

- [] The results are tested on the basis of two subterms. For this purpose the APA Term is divided into two subterms. The first subterm consists of all APA Covered Years ending on or before Δ DATE, and the second subterm consists of all other APA Covered Years. For each subterm, the results are tested as of the Last Effective APA Subterm Covered Year, for a period consisting of the Last Effective APA Subterm Covered Year and all prior APA Covered Years in the subterm.

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- [] The results are tested on a subterm basis for all APA Covered Years ending on or before Δ DATE (the "subterm"), and are tested annually for each other APA Covered Year, as follows:

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The results are tested as of the Last Effective APA Subterm Covered Year, for a period consisting of the Last Effective APA Subterm Covered Year and all prior APA Covered Years in the subterm.

The results are tested as of each APA Covered Year that is not in the subterm, for a period consisting of that APA Covered Year.

- [] The results are tested on a cumulative basis, meaning that (except as provided in the following sentence) they are not tested as of the first APA Covered Year but they are tested as of each other particular APA Covered Year for a period consisting of such particular APA Covered Year and all prior APA Covered Years. However, if the Last Effective APA Covered Year is the first APA Covered Year, then the results are tested as of the first APA Covered Year, for a period consisting of such APA Covered Year.

Comment [A7]: For example, if there are five APA Covered Years, then unless the next sentence in the text applies the results are tested (i) as of the second APA Covered Year for the period consisting of the first two APA Covered Years, (ii) as of the third APA Covered Year for the period consisting of the first three APA Covered Years, (iii) as of the fourth APA Covered Year for the period consisting of the first four APA Covered Years, and (iv) as of the fifth and last APA Covered Year for the period consisting of all APA Covered Years.

- [] The results are tested on a three-year rolling average basis, meaning that the results are tested as of each APA Covered Year, for a period consisting of the APA Tax Year corresponding to the APA Covered Year

(but excluding any portion of that APA Tax Year that is after the APA Term), and the Tested Party's two preceding tax years.

e. Other Provisions

The Tested Party's financial results, to be tested as described above, are for:

- The Tested Party as a whole.
- Only a segment of the Tested Party's activity. The segment is the distribution activity, which is the activity carried out in the Distribution Operating Division. The results of the Distribution Operating Division will reflect an allocation of all headquarters expenses to the operating divisions in proportion to each operating division's sales revenue.

When the Tested Party's financial results are tested as of a given APA Covered Year, those results shall reflect, to the extent relevant, any APA Primary Adjustment for this Covered Method made under section 5 of this Appendix A for the APA Tax Year corresponding to any prior APA Covered Year.

For this Covered Method, if applicable:

- * For APA Covered Years ending on or before DATE, it is agreed that this Covered Method, yields financial results as shown below, and that any APA Primary Adjustments under section 5 of this Appendix A are as shown below.

TEXT AND/OR TABLES SHOWING THE FINANCIAL RESULTS, THE TESTING OF THOSE FINANCIAL RESULTS UNDER THE COVERED METHOD, AND ANY RESULTING APA PRIMARY ADJUSTMENTS.

Covered Method for Covered Issue 2:

a. Tested Party

The Tested Party is Acme-US.

b. Financial Results Tested (Type of Method)

- The Covered Method is an implementation of the comparable uncontrolled price method under the OECD Guidelines and of the comparable uncontrolled price method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are:

Comment [A8]: For example, suppose that the Tested Party has a calendar tax year at all relevant times, and the APA Term is from July 1, 2018 through June 30, 2021 inclusive. Then the results will be tested as follows:

As of the APA Covered Year that is the last six months of calendar year 2018, for the period consisting of calendar years 2016-2018.

As of the APA Covered Year that is calendar year 2019, for the period consisting of calendar years 2017-2019.

As of the APA Covered Year that is calendar year 2020, for the period consisting of calendar years 2018-2020.

As of the APA Covered Year that is the first six months of calendar year 2021, for the period consisting of calendar years 2019 and 2020 plus the first six months of calendar year 2021 (the parenthetical in the text excludes the last six months of calendar year 2021).

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Comment [A9]: For example, if there are three APA Covered Years and a cumulative test is used, then the testing as of the third APA Covered Year would take into account any APA Primary Adjustment made for the APA Tax Year corresponding to the second APA Covered Year.

Comment [A10]: In some cases, APMA has agreed with the taxpayer that the covered method(s) as applied to certain years yield specific numerical results. See the corresponding provision in section 6 below.

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Treasury Regulations. The Tested Party's financial results to be tested are the gross profit margin from the sale of DESCRIPTION OF GOODS.

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- The Covered Method is an implementation of the resale price method under the OECD Guidelines and of the gross services margin method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross services margin from the provision of DESCRIPTION OF SERVICES.

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- The Covered Method is an implementation of the cost plus method under the OECD Guidelines and of the cost plus method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross profit markup.

- The Covered Method is an implementation of the cost plus method under the OECD Guidelines and of the cost of services plus method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the gross services profit markup from the provision of DESCRIPTION OF SERVICES.

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- The Covered Method is based on the principles of the low value-adding intra-group services approach under the OECD Guidelines and of the services cost method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the markup on total costs for providing DESCRIPTION OF SERVICES.

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- The Covered Method is an implementation of the transactional net margin method under the OECD Guidelines and of the comparable profits method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are the:

- operating margin.
- markup on total costs.
- Berry ratio.
- return on operating assets.
- return on invested capital.

* OTHER PROFIT LEVEL INDICATOR, WITH DEFINITION.

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- The Covered Method is an implementation of the profit split (residual analysis) method under the OECD Guidelines and of the residual profit

split method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

- The Covered Method is an implementation of the profit split (contribution analysis) method under the OECD Guidelines and of the comparable profit split method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is an implementation of an income based valuation technique as referenced in paragraph 6.153 of the OECD Guidelines and of the income method under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is an implementation of (i) a sharing of the cost of current contributions in proportion to overall expected benefits, within a cost contribution arrangement under the OECD Guidelines, and (ii) a sharing of intangible development costs in proportion to reasonably anticipated benefits, within a cost sharing arrangement under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.
- The Covered Method is a method that is not specified under the OECD Guidelines and not specified under the U.S. Treasury Regulations. The Tested Party's financial results to be tested are described in subsection (c) below.

Such financial results are determined according to the Applicable Accounting Standard, with the proviso that in determining such results, accounting principles and conventions that are generally accepted in the trade or industry must be used.

Such financial results are tested against a point or range as described below. The test is carried out with a frequency, and for certain time periods, as described below. If and when these financial results do not satisfy the test, they must be adjusted as described in section 5 of this Appendix A.

c. Testing of Financial Results Against a Point or Range

The Tested Party's financial results are tested as follows:

- The financial results must equal ~~X~~.
- The financial results must be within an Arm's Length Range.
- The Arm's Length Range is from ~~5%~~ to ~~10%~~ inclusive.

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- This Arm's Length Range has an associated Median value of ΔZ . Deleted: #
- This Arm's Length Range has no associated Median value.
- Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the annual test described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the term test described in subsection (d) below. Deleted: #
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- The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ . Deleted: #
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- These Arm's Length Ranges have no associated Median value.
- Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the subterm test described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the annual test described in subsection (d) below. Deleted: #
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- The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ . Deleted: #
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- These Arm's Length Ranges have no associated Median value.
- Two Arm's Length Ranges apply. The first is from ΔW to ΔX inclusive, and applies to the test for the first subterm described in subsection (d) below. The second is from ΔY to ΔZ inclusive, and applies to the test for the second subterm described in subsection (d) below. Deleted: #
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- The first Arm's Length Range has an associated Median value of ΔP , and the second Arm's Length Range has an associated Median value of ΔQ . Deleted: #
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- These Arm's Length Ranges have no associated Median value.
- Δ OTHER DESCRIPTION, FOR EXAMPLE THE EVALUATION AND TESTING MECHANICS FOR A PROFIT SPLIT, AN INCOME METHOD, AN UNSPECIFIED METHOD, OR A SHARING OF COSTS UNDER A Deleted: #

COST CONTRIBUTION ARRANGMENT/COST SHARING ARRANGEMENT.

d. Testing Frequency and Testing Periods

The Tested Party's financial results are tested as of certain APA Covered Years, and for certain time periods, as follows:

- The results are tested annually, meaning that they are tested as of each APA Covered Year, for a period consisting of that APA Covered Year.
- There is no additional term test.
- There is an additional term test. For this test, the results are tested as of the Last Effective APA Covered Year, for the period consisting of the Last Effective APA Covered Year and all prior APA Covered Years.

The application of the annual test and the application of the additional term test are coordinated as described in section 5 of this Appendix A.

- The results are tested on a term basis, meaning that they are tested only once, as of the Last Effective APA Covered Year, for a period consisting of the Last Effective APA Covered Year and all prior APA Covered Years.
- The results are tested on the basis of two subterms. For this purpose the APA Term is divided into two subterms. The first subterm consists of all APA Covered Years ending on or before DATE, and the second subterm consists of all other APA Covered Years. For each subterm, the results are tested as of the Last Effective APA Subterm Covered Year, for a period consisting of the Last Effective APA Subterm Covered Year and all prior APA Covered Years in the subterm.

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- The results are tested on a subterm basis for all APA Covered Years ending on or before DATE (the "subterm"), and are tested annually for each other APA Covered Year, as follows:

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The results are tested as of the Last Effective APA Subterm Covered Year, for a period consisting of the Last Effective APA Subterm Covered Year and all prior APA Covered Years in the subterm.

The results are tested as of each APA Covered Year that is not in the subterm, for a period consisting of that APA Covered Year.

- The results are tested on a cumulative basis, meaning that (except as provided in the following sentence) they are not tested as of the first APA Covered Year but they are tested as of each other particular APA Covered Year for a period consisting of such particular APA Covered Year and all prior APA Covered Years. However, if the Last Effective APA Covered Year is the first APA Covered Year, then the results are tested as of the first APA Covered Year, for a period consisting of such APA Covered Year.
- The results are tested on a three-year rolling average basis, meaning that the results are tested as of each APA Covered Year, for a period consisting of the APA Tax Year corresponding to the APA Covered Year (but excluding any portion of that APA Tax Year that is after the APA Term), and the Tested Party's two preceding tax years.

e. Other Provisions

The Tested Party's financial results, to be tested as described above, are for:

- The Tested Party as a whole.
- Only a segment of the Tested Party's activity. The segment is the R&D activity, which is the activity carried out in the R&D Operating Division. The results of the R&D Operating Division will reflect an allocation of all headquarters expenses to the operating divisions in proportion to each operating division's sales revenue.

When the Tested Party's financial results are tested as of a given APA Covered Year, those results shall reflect, to the extent relevant, any APA Primary Adjustment for this Covered Method made under section 5 of this Appendix A for the APA Tax Year corresponding to any prior APA Covered Year.

For this Covered Method, if applicable:

- * For APA Covered Years ending on or before [^]DATE, it is agreed that this Covered Method, yields financial results as shown below, and that any APA Primary Adjustments under section 5 of this Appendix A are as shown below.

[^]TEXT AND/OR TABLES SHOWING THE FINANCIAL RESULTS, THE TESTING OF THOSE FINANCIAL RESULTS UNDER THE COVERED METHOD, AND ANY RESULTING APA PRIMARY ADJUSTMENTS.

Deleted: #DETAILED DESCRIPTION OF THE SEGMENT AND OF THE ALLOCATION AND APPORTIONMENT METHODS USED, INCLUDING ANY APPLICABLE FORMULAS AND DEFINITIONS OF QUANTITIES USED IN THOSE FORMULAS. THIS DESCRIPTION SHOULD BE DETAILED ENOUGH TO ENABLE A STRAIGHTFORWARD VERIFICATION OF COMPLIANCE BY THE IRS EXAMINATION TEAM.

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5. Application of Covered Method(s) to Income Reporting

For each APA Tax Year, and for each Covered Method and corresponding Covered Issue(s), the amounts reported by U.S. Taxpayer and Non-U.S. Taxpayer for income tax purposes under the laws of the United States and Japan must clearly reflect the Tested Party's actual transactions, allocations, and/or recordkeeping, as applicable, that relate to such Covered Issue(s). adjusted as necessary to conform with section 4 of this Appendix A. Accordingly, for each particular APA Tax Year and corresponding APA Covered Year, and for each such Covered Method:

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- i. If the Tested Party's financial results are tested as of such APA Covered Year and do not conform with section 4 of this Appendix A, then the tax reporting for such APA Tax Year must clearly reflect an adjustment that brings such results into conformance (an "APA Primary Adjustment"). If section 4 of this Appendix A specifies conformance to an Arm's Length Range, then the adjustment shall be to:

the Median.

* the near edge of the Arm's Length Range.

* the Median for Covered Issues SPECIFY WHICH ONES, and the near edge of the Arm's Length Range for Covered Issues SPECIFY WHICH ONES.

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- ii. If an adjustment is not required under paragraph (i) above, then the tax reporting must clearly reflect the Tested Party's financial results. In this case there is no APA Primary Adjustment.
- iii. If both an annual test and an additional term test apply under such Covered Method, and such APA Covered Year is the Last Effective APA Covered Year, so that as of such APA Covered Year the Tested Party's financial results are tested under both the annual test and the term test, then paragraphs (i) and (ii) above are modified by this paragraph (iii), which coordinates the application of both tests. As explained in more detail below, the annual test is applied first, followed by the term test. Specifically, the need for and amount of any APA Primary Adjustment for such APA Covered Year will be determined as follows:
 - (A) First apply paragraphs (i) and (ii) above under the assumption that only the annual test applies. Any required adjustment will be referred to as the "annual adjustment" rather than an "APA Primary Adjustment." If there is no required adjustment, the annual adjustment is considered to be zero.
 - (B) Next, apply paragraphs (i) and (ii) above to the Tested Party's financial results as adjusted by any nonzero annual adjustment, under the assumption that only the term test applies to those

results. Any required adjustment under this application of paragraphs (i) and (ii) will be referred to as the “term adjustment” rather than an “APA Primary Adjustment.” If there is no such required adjustment, the term adjustment is considered to be zero.

- (C) Add the annual adjustment and term adjustment, taking account of the magnitude and (if nonzero) direction of each. If this sum is zero, there is no APA Primary Adjustment for such APA Covered Year. If this sum is nonzero, this sum gives the magnitude and direction of the APA Primary Adjustment for such APA Covered Year. Any APA Primary Adjustment, or the lack of an APA Primary Adjustment, must be clearly reflected in the tax reporting for such APA Tax Year (see paragraphs (i) and (ii) above).

iv. If this APA is unilateral and such APA Covered Year is within the Rollback Period, then:

- Paragraphs (i)-(iii) above notwithstanding, an APA Primary Adjustment will not be made if that APA Primary Adjustment would decrease the income of U.S. Taxpayer for such APA Tax Year.

- Paragraphs (i)-(iii) above apply without modification.

If indicated, the above provisions on APA Primary Adjustments are modified as follows:

- Any APA Primary Adjustment that would be made under the above provisions for an APA Tax Year ending before Δ DATE will instead be made for the APA Tax Year ending Δ THE SAME DATE (the “Telescoping Year”). For each particular Covered Method, all APA Primary Adjustments that are made for the Telescoping Year (including any APA Primary Adjustments that are moved to the Telescoping Year as just described, as well as any APA Primary Adjustment originally made for the Telescoping Year) are netted.

- However, an APA Primary Adjustment that is thus moved from a particular APA Tax Year (the “Original Year”) to the Telescoping Year shall be increased in amount to reflect the time value of money. That increase will consist of multiplication by a factor that is an annual rate raised to a power. The annual rate is $1.\Delta XY$. The power is the quotient of (i) the average of the number of months by which the end of the Telescoping Year is later than the end of the Original Year, and the number of months by which the start of the Telescoping Year is later than the start of the Original Year (with any fractions of months rounded to whole months), (ii) divided by twelve.

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For U.S. tax purposes, the generally applicable Code rules will apply with respect to APA Primary Adjustments, except as otherwise provided in Rev. Proc. 2015-41 or in this APA.

6. Conforming Adjustments and Repatriation of Funds

The provisions in this section 6 apply to “Repatriable Issues,” which are Covered Issues that concern transactions between associated enterprises that fall under Article 9 of the OECD Model Tax Convention. Such transactions correspond to transactions that under U.S. law are subject to application of Code section 482, as modified by any applicable treaty provision.

If the application of a Covered Method to a Repatriable Issue requires an APA Primary Adjustment under section 5 of this Appendix A for a given APA Tax Year, then for U.S. tax purposes there generally must be a corresponding conforming adjustment as specified in U.S. Treasury Regulations section 1.482-1(g)(3) as amplified by Rev. Proc. 99-32 or any successor revenue procedure. However, for this purpose, all APA Primary Adjustments for such APA Tax Year arising from the application of a Covered Method to a Repatriable Issue are first netted to yield a net APA Primary Adjustment for such APA Tax Year. Only if the net APA Primary Adjustment is nonzero is a conforming adjustment required.

Comment [A11]: As mentioned, Appendix A might be adapted for a Mutual Agreement. The phrase “for U.S. tax purposes” acknowledges that a treaty partner’s domestic tax law may differ from the U.S. domestic provisions regarding conforming adjustments.

For each APA Tax Year with a nonzero net APA Primary Adjustment, for U.S. tax purposes the conforming adjustment will be accomplished in the following steps:

- i) The conforming adjustment will be accomplished between Acme-US and Acme-Japan, which will be referred to here as U.S. Entity and Non-U.S. Entity respectively. An intercompany payable will be established between U.S. Entity and Non-U.S. Entity in the amount and direction of the net APA Primary Adjustment, as of the last day of such APA Tax Year. This payable will be denominated in CURRENCY. This payable will be treated as indebtedness for all U.S. federal tax purposes, including, but not limited to, Code section 956.
- ii) The intercompany payable will bear interest at an arm’s length rate.
 - Such arm’s length rate is not specified in this APA and will be determined under applicable legal principles.
 - Such arm’s length rate is determined as follows.
DESCRIPTION OF ARM’S LENGTH RATE (FOR EXAMPLE, FOR A U.S. DOLLAR PAYABLE, A CERTAIN APPLICABLE FEDERAL RATE UNDER U.S. TREASURY REGULATIONS SECTION 1.482-2(a)(2)(iii)(C)).

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This APA is bilateral or multilateral. As agreed between the United States and Japan, the intercompany payable will not bear interest.

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iii) The intercompany payable must be satisfied, in a manner permitted under Rev. Proc. 99-32 or any successor revenue procedure, within 90 days of the later of (1) the date for timely filing (with extensions) of the U.S. return for such APA Tax Year, and (2) the APA's U.S. Effective Date. If any amount of the intercompany payable is not otherwise so satisfied within that 90-day period, such amount, on the last day of such period, will be deemed (1) to be paid between U.S. Entity and Non-U.S. Entity in satisfaction of the payable, and (2) to be paid (directly or indirectly, as specified below) between U.S. Entity and Non-U.S. Entity in the opposite direction (that is, from the deemed recipient of the intercompany payable to the deemed payor of the intercompany payable). These two deemed payments on the same day will cancel and thus yield no net cash flow between these two entities. The second of these deemed payments will be referred to as the "reverse payment." The reverse payment will be deemed to be as follows:

a) If the net APA Primary Adjustment increases U.S. income:

The reverse payment will be deemed to be a contribution to capital from U.S. Entity to Non-U.S. Entity, either directly, or indirectly through the corporate chain, as the case may be.

The reverse payment will be deemed to be a distribution from U.S. Entity to Non-U.S. Entity, either directly, or indirectly through the corporate chain, as the case may be.

The reverse payment will be deemed to be a distribution from U.S. Entity to COMMON PARENT, either directly, or indirectly through the corporate chain, as the case may be, followed by a contribution by COMMON PARENT to non-U.S. Entity, either directly or indirectly through the corporate chain, as the case may be.

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b) If the net APA Primary Adjustment decreases U.S. income:

The reverse payment will be deemed to be a contribution to capital from non-U.S. Entity to U.S. Entity, either directly, or indirectly through the corporate chain, as the case may be.

The reverse payment will be deemed to be a distribution from non-U.S. Entity to U.S. Entity, either directly, or indirectly through the corporate chain, as the case may be.

- The reverse payment will be deemed to be a distribution from non-U.S. Entity to COMMON PARENT, either directly, or indirectly through the corporate chain, as the case may be, followed by a contribution by COMMON PARENT to U.S. Entity, either directly, or indirectly through the corporate chain, as the case may be.

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This situation is generally described in paragraph 4.66 of the OECD Guidelines, and in U.S. Treasury Regulations section 1.482-1(g) and Rev. Proc. 99-32.

In this APA, if applicable:

- * For the APA Tax Year(s) ending on or before DATE, it is agreed that the net APA Primary Adjustment(s), if any, from the application of the Covered Methods are as follows: FOR EACH SUCH APA TAX YEAR, DESCRIPTION OF WHETHER THERE IS A NET APA PRIMARY ADJUSTMENT, AND IF SO THE AMOUNT AND DIRECTION. IF THERE IS MORE THAN ONE COVERED METHOD FOR A REPATRIABLE ISSUE, ALSO PROVIDE A TABLE SHOWING THE DERIVATION, FOR EACH SUCH APA TAX YEAR, OF THE NET APA PRIMARY ADJUSTMENT FROM THE APA PRIMARY ADJUSTMENT (OR LACK OF ONE) FOR EACH SUCH COVERED METHOD. FOR ANY SUCH NET APA PRIMARY ADJUSTMENTS, DESCRIPTION OF THE MEANS BY WHICH THE CONFORMING ADJUSTMENT HAS BEEN OR WILL BE SATISFIED, WITH APPLICABLE DATES.

Comment [A12]: In some cases, APMA has agreed with the taxpayer that the covered method(s) as applied to certain years yield specific numerical results. See the corresponding provision in section 4(e) above.

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7. Effect of Certain Adjustments by Tax Authorities and Resulting Competent Authority Proceedings

The Covered Issue(s) directly concern activities in the United States and Japan (the "involved countries").

Comment [A13]: This section addresses the question of whether the application of the Covered Methods should, or should not, be modified to reflect various possible adjustments by tax authorities.

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It might be possible that the Relevant Financial Data for one or more Covered Methods would be affected by adjustments by a tax authority of one of the involved countries that concern activities only in the country of the tax authority. For example, the IRS might adjust a transaction between a U.S. Covered Entity and U.S. entity that is not a Covered Entity.

- For purposes of applying the Covered Method(s), any effect of such adjustments on such Relevant Financial Data will be ignored.

- * ALTERNATIVE PROVISION

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It might be possible that the Relevant Financial Data for one or more Covered Methods would be affected by adjustments by a tax authority of one of the involved

countries that concern activities only in the country of the tax authority and one or more other involved countries. For example, a transaction between a Covered Entity in one involved country, and an entity in another involved country that is not a Covered Entity, might be adjusted by the tax authority of either of those involved countries. Such Relevant Financial Data might also be affected by competent authority proceedings that address such adjustments.

For purposes of applying the Covered Method(s), any effect of such adjustments or such competent authority proceedings on such Relevant Financial Data will be ignored.

ALTERNATIVE PROVISION

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It might be possible that the Relevant Financial Data for one or more Covered Methods would be affected by adjustments by a tax authority that concern activities in the country of the tax authority and in a country that is not an involved country (a “third country”). For example, a transaction between a U.S. Covered Entity and an affiliate in a third country might be adjusted by either the IRS or the third country tax authority. Such Relevant Financial Data might also be affected by competent authority proceedings that address such adjustments.

Comment [A14]: For example, if a Covered Method specifies a profit split between a U.S. entity and a Japanese entity, and the Korean taxing authority adjusts a transaction involving that Japanese entity, that adjustment could affect the pool of profit to be split between the U.S. and Japanese entities.

For purposes of applying the Covered Method(s), any effect of such adjustments or such competent authority proceedings on such Relevant Financial Data will be ignored.

ALTERNATIVE PROVISION

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No inference is intended regarding the treatment, for purposes of applying the Covered Method(s), of adjustments and competent authority proceedings other than those just described.

8. Definitions

The definitions in the table below apply to this APA.

The defined terms in this table include certain measures of profitability (e.g., operating profit, operating margin). Most of these measures are ultimately defined in terms of sales revenue, operating expenses, and operating assets (defined terms), and cogs and non-interest-bearing liabilities (undefined terms). The definitions of sales revenue, operating expenses, and operating assets contain a limitation to the relevant business activity. Similarly, each use of the terms “cogs” and “non-interest-bearing liabilities” is accompanied by a limitation to the relevant business activity. Therefore, the measures of profitability based on these five terms all are defined with a limitation to the relevant business activity. (Certain other measures of profitability in this table relate to the provision of services, and are defined with reference to those services. Therefore, those measures as well contain a limitation to the relevant business activity.)

Term	Definition
Arm's Length Range	With respect to a particular Covered Method, a numerical range that defines the values for which certain financial results of the Tested Party are considered to satisfy the arm's length standard. (This term may be referenced in section 4 of this Appendix A.)
APA Primary Adjustment	(Defined in section 5 of this Appendix A.)
APA Covered Year	(Defined in section 2 of this Appendix A.)
APA Term	(Defined in section 2 of this Appendix A.)
APA Tax Year	(Defined in section 2 of this Appendix A.)
Applicable Accounting Standard	The Applicable Accounting Standard is <u>U.S. GAAP</u> for U.S. Taxpayer and <u>Japanese Generally Accepted Accounting Practices (Japan GAAP)</u> , for Non-U.S. Taxpayer.
Berry ratio Code	The ratio of gross profit to operating expenses. The U.S. Internal Revenue Code of 1986, title 26 of the United States Code, as amended.
correspond, corresponding	(With regard to APA Covered Years and APA Tax Years, defined in section 2 of this Appendix A; with regard to Covered Issues and Covered Methods, defined in section 4 of this Appendix A.)
Covered Entity(ies)	(Defined in section 1 of this Appendix A.)
Covered Issue(s)	(Defined in section 3 of this Appendix A.)
Covered Method	A method used to resolve one or more Covered Issues, as described in section 4 of this Appendix A. (In some cases, this method may be a "transfer pricing method" within the meaning of chapter II of the OECD Guidelines and U.S. Treasury Regulations section 1.482-1(b).)
Critical Assumption fails, failure of a Critical Assumption	A Critical assumption "fails" when the Critical Assumption has not been met. This situation is referred to as the "failure" of the Critical Assumption.

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Term	Definition
Early Termination	<p>A termination of this APA's effectiveness, either in its entirety or only as applied to certain Covered Issues, before the end of the APA Term. Such a termination could result from one or more of the following circumstances: (i) a Critical Assumption failure, (ii) a violation of the terms and conditions of this APA, (iii) a cancellation of the APA under Rev. Proc. 2015-41, and (iv) an amendment of the APA. If an Early Termination so terminates this APA's effectiveness as applied to a particular Covered Issue, the Early Termination is said to "apply" to or for that Covered Issue.</p> <p>Any such termination of effectiveness would occur as of the end of an APA Tax Year (see Rev. Proc. 2015-41, section 7.06). Because such end of an APA Tax Year is before the end of the APA Term, such end of an APA Tax Year is also the end of the corresponding APA Covered Year (see the definitions of APA Tax Year and APA Covered Year in section 2 of this Appendix A). Thus, an Early Termination always would occur as of the end of an APA Covered Year. That fact is assumed in the definitions in this table of Last Effective APA Covered Year and Last Effective APA Subterm Covered Year.</p>
Gross profit	Sales revenue, less cost of goods sold for the relevant business activity.
Gross profit margin	gross profit, divided by sales revenue
Gross profit markup	gross profit, divided by cost of goods sold for the relevant business activity
Gross services margin	In connection with a provision of services, the ratio of gross services profit to the price paid for the services in an uncontrolled transaction. For this purpose, gross services profit equals the amount of such price that is retained by the Tested Party.
Gross services profit markup	In connection with a provision of services, gross services profit, divided by transactional costs. For this purpose, gross services profit equals sales revenue less transactional costs. Also, for this purpose, transactional costs equal costs directly attributable to providing the services. Such costs would include, for example, all compensation attributable to employees directly involved in the performance of such services, and costs of materials and supplies consumed or made available in rendering the services.
IFRS	International Financial Reporting Standards.
Invested capital	Operating assets, less non-interest-bearing liabilities used in the relevant business activity.
IRS	The Internal Revenue Service, an agency of the U.S. government.
IFRS	International Financial Reporting Standards.

Term	Definition
Last Effective APA Covered Year	For a particular Covered Method, the last APA Covered Year for which this APA remains effective as to the Covered Issue(s) corresponding to that Covered Method. The Last Effective APA Covered Year will be the last APA Covered Year unless an Early Termination applies to such Covered Issue(s). See <i>also</i> the definition in this table of Early Termination.
Last Effective APA Subterm Covered Year	For a particular Covered Method, and with reference to a particular set of APA Covered Years that is defined as a subterm, the last APA Covered Year in the subterm for which this APA remains effective as to the Covered Issue(s) corresponding to that Covered Method. The Last Effective APA Subterm Covered Year will be the last APA Covered Year in the subterm unless an Early Termination applies to such Covered Issue(s) and renders the APA ineffective as to such Covered Issue(s) before the end of the subterm. See <i>also</i> the definition in this table of Early Termination.
Markup on total costs	The ratio of operating profit to total costs.
Median	With respect to a particular Arm's Length Range, the median of a set of observations of market data from which that Arm's Length Range was determined.
Non-U.S. Taxpayer	(Defined in section 1 of this Appendix A.)
Non-U.S. Covered Entity(ies)	(Defined in section 1 of this Appendix A.)
OECD Guidelines	Organisation for Economic Co-operation and Development, <u>OECD Transfer Pricing Guidelines for Multinational Corporations</u> (July 2010), as amended by adoption of <u>Organisation for Economic Co-operation and Development, Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports</u> (OECD/G20 Base Erosion and Profit Shifting Project, 2015).
OECD PE Report	Organisation for Economic Co-operation and Development, <u>2010 Report on Attribution of Profit to Permanent Establishments</u> , July 22, 2010.
Operating assets	The value of all assets used in the relevant business activity, including fixed assets and current assets (such as accounts receivable and inventories). The following items are excluded from operating assets: cash, cash equivalents, short-term investments, deferred tax assets, tax refunds, intangibles, investments in subsidiaries, portfolio investments.

Term	Definition
Operating expenses	All expenses (including depreciation) not included in cost of goods sold except for interest expense, domestic and foreign income taxes, amortization of intangibles, and any other expenses not related to the operation of the relevant business activity. Operating expenses normally include, for example, expenses associated with advertising, promotion, sales, marketing, warehousing, and distribution, administration, and a reasonable allowance for depreciation. For U.S. Taxpayer, foreign income taxes are defined in U.S. Treasury Regulations section 1.902-1(a)(7).
Operating margin	The ratio of operating profit to sales revenue.
Operating profit	Sales revenue, less cost of goods sold for the relevant business activity, less operating expenses.
Rev. Proc. 99-32	A revenue procedure issued by the IRS that is cited as Rev. Proc. 99-32, 1999-2 C.B. 296.
Rev. Proc. 2015-41	A revenue procedure issued by the IRS that is cited as Rev. Proc. 2015-41, 2015-35 I.R.B 263.
Repatriable Issue	(Defined in section 6 of this Appendix A.)
Relevant Financial Data	With respect to a particular Covered Method, the financial results of the Tested Party that are tested, together with any other financial data (of the Tested Party or any other party) that are considered in determining compliance with the Covered Method.
Return on invested capital	(Defined in the same way as “return on operating assets,” but with “operating assets” replaced by “invested capital” wherever it occurs in the definition.)

Comment [A15]: For example, under an implementation of the profit split (residual analysis) method under the OECD Guidelines and the residual profit split method under the U.S. Treasury Regulations, the Tested Party’s operating profit is tested, but the application of the method also takes into account the operating profit of another party and may also take into account other financial data of both parties (such as manufacturing costs, sales volumes, and historical expenditures for intangible development).

Term	Definition
Return on operating assets	<p>With respect to a particular Covered Method, the Tested Party for that Covered Method, and a testing period used in that Covered Method, the operating profit over the testing period divided by the time-weighted average operating assets over the testing period.</p> <p>For this purpose, the time-weighted average operating assets over the testing period is the sum, over all APA Covered Years in the testing period, of the following product: (i) the simple average of the operating asset levels at the start and end of the APA Tax Year corresponding to such APA Covered Year, multiplied by (ii) the ratio of the number of calendar days in the APA Covered Year, to 365.</p> <p>For example, suppose that (i) the testing period consists of two consecutive APA Covered Years, the first with 183 calendar days and the second with 366 calendar days, (ii) the total operating profit over those two years is exactly 3.4, and (iii) the operating assets levels are exactly 10 at the start of the APA tax year corresponding to the first APA Covered Year, 16 at the end of the APA Tax Year corresponding to the first APA Covered Year (which is also the start of the APA Tax Year corresponding to the second APA Covered Year), and 22 at the end of the APA Tax Year corresponding to the second APA Covered Year. Then the time-weighted average operating assets over the testing period is $[(10+16)/2]*(183/365) + [(16+22)/2]*(366/365) = 25.5699$. The return on operating assets is then $3.4/25.5699 = 13.30\%$.</p>
Rollback Period	(This term, if applicable, is defined in section 2 of this Appendix A.)
Sales revenue	Total receipts from sale of goods and provision of services, less returns and allowances, for the relevant business activity.
Tax year	A standard or irregular year that is used for tax reporting purposes. For U.S. Taxpayer, a tax year is a "taxable year," as defined in Code section 441.
Tested Party	(Defined in section 4 of this Appendix A with regard to a particular Covered Method.)
Testing period	The time period over which financial results are tested (see section 4 of Appendix A to this APA).
Total costs	Cost of goods sold for the relevant business activity, plus operating expenses.
U.S. Treasury Regulations	Tax regulations issued by the U.S. Treasury Department, found at title 26 of the Code of Federal Regulations.
U.S. Covered Entity(ies)	(Defined in section 1 of this Appendix A.)

Term	Definition
U.S. Effective Date	The date, or later date of the dates, upon which the APA is executed by the IRS and by or on behalf of each U.S. Covered Entity.
U.S. GAAP	U.S. generally accepted accounting principles.
U.S. return	Any of the "Returns with respect to income taxes under subtitle A" required by Code section 6012, and any "return" for a partnership required by Code section 6031.
U.S. Taxpayer	(Defined in section 1 of this Appendix A.)

DRAFT for Public Discussion

APPENDIX B CRITICAL ASSUMPTIONS

The Critical Assumptions are:

1. The Covered Entities' business activities, functions performed, risks assumed, assets employed, contractual terms, markets, and economic conditions faced in relation to the Covered Issue(s) will remain materially the same as described in the APA Request. For this purpose, a mere change in business results will not be a material change.
2. The Covered Entities' financial accounting methods and classifications and methods of estimation in relation to the Covered Issue(s) and Covered Method(s) will remain materially the same as described or used in the APA Request.

If indicated, the effect of a critical assumption failure may be limited as follows:

- The failure of Critical Assumptions [^]XXX listed above will affect the effectiveness of this APA only as to Covered Issues [^]YYY listed in Appendix A. Thus, as to the other Covered Issues, the APA will remain in force (except to the extent some other condition affects the APA's effectiveness as to those Covered Issues).

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The Covered Entities will not cause a critical assumption to fail for the purpose of rendering the APA ineffective, unless they have an independent business justification (unrelated to rendering the APA ineffective) for the action that causes the critical assumption to fail. If one or more Covered Entities do cause a critical assumption to fail for the purpose of rendering the APA ineffective, and without such independent business justification, then the Covered Entities will not withhold consent to an amendment to this APA to the effect that this APA will continue in force without regard to such failure. In this case, if a Covered Entity refuses to sign such an amendment, such an amendment may be executed without such signature and will then have the same force and effect as if the amendment had such signature.

**APPENDIX C
APA RECORDS AND ANNUAL REPORT**

APA RECORDS

The APA Records will consist of all documents listed below for inclusion in the Annual Report, as well as all documents, notes, work papers, records, or other writings that support the information provided in such documents.

ANNUAL REPORT

An Annual Report must be submitted for each APA Tax Year in accordance with paragraph 6(e) of the APA and section 7.02 of Rev. Proc. 2015-41.

For each APA Tax Year, the Annual Report (and each copy or version as required by paragraph 6(e) of the APA) will include:

1. Two copies of a properly completed APA Annual Report Summary in the form of Appendix D to this APA, one copy of the form bound with, and one copy provided separately from, the rest of the Annual Report. (The electronic version of the Annual Report need have only one copy of this item.)
2. A table of contents, organized according to the additional required items listed below.
3. For such APA Tax Year and the corresponding APA Covered Year, statements that fully identify, describe, analyze, and explain:
 - a. All material differences between the Covered Entities' business activities, functions performed, risks assumed, assets employed, contractual terms, markets, and economic conditions faced in relation to the Covered Issues during such APA Covered Year from those same items described in the APA Request. If there have been no such material differences, the Annual Report will include a statement to that effect.
 - b. All material differences between Covered Entities' financial accounting methods and classifications and methods of estimation in relation to the Covered Issues and Covered Methods used during such APA Covered Year, from those described or used in the APA Request. If any change was made to conform to changes in the Applicable Accounting Standard, U.S. Taxpayer will specifically identify the change. If there have been no such material differences, the Annual Report will include a statement to that effect.

- c. Regarding notices under paragraph 16 of the APA:
- i. A current statement of how the IRS should provide such notices to U.S. Taxpayer (and, if applicable, to U.S. Taxpayer's representative).
 - ii. A copy of any such notices that were submitted by U.S. Taxpayer to the IRS after the last Annual Report was submitted (or, if there was no prior Annual Report, after the APA was executed). If there were no such notices, the Annual Report will include a statement to that effect.
- d. Any failure of any Critical Assumption. If there has been no such failure, the Annual Report will include a statement to that effect.
- e. Whether or not material information submitted while the APA Request was pending is discovered to be false, incorrect, or incomplete, and if so a correction or completion of that information, as applicable.
- f. Any change to any entity classification for federal income tax purposes (including any change that causes an entity to be disregarded for federal income tax purposes) of any Worldwide Group member that is a Covered Entity or is otherwise relevant to the Covered Issue(s) or Covered Method(s).
- g. The following regarding any APA Primary Adjustments made for such APA Tax Year under Appendix A to this APA:
- i. The amounts of any APA Primary Adjustments;
 - ii. The circumstances that led to such APA Primary Adjustments being necessary;
 - iii. A calculation of the net APA Primary Adjustment as defined in Appendix A to this APA; and
 - iv. A complete description of the means by which the conforming adjustment (see section 6 of Appendix A to this APA) is accomplished, including:
 - A. a description of any accounts payable established, including the entities involved and when the payables are established;
 - B. a description of any amounts paid or deemed paid (including amounts paid or deemed paid in satisfaction of an intercompany payable established as described in section 6

of Appendix A to this APA, and including any deemed reverse payments as described in section 6 of Appendix A to this APA), that specifies the entities involved, when the amounts are paid or deemed paid, and by what means any amounts are actually paid; and

- C. the character (such as capital, ordinary, income, expense, dividend, contribution to capital) and country source of any payments and deemed payments, and the specific affected line item(s) of any affected U.S. return;
 - h. A detailed numerical explanation of how the result of the application of the Covered Methods is reflected on the U.S. return, with reference to particular line items on the U.S. return. This explanation shall include the amounts, description, reason for, and financial analysis of any book-tax differences, as reflected on Schedule M-1 or Schedule M-3 of the U.S. return for such APA Tax Year, that (i) are relevant to an APA Primary Adjustment, (ii) otherwise are relevant to the book and tax treatment of any income or expense item that is part of the Relevant Financial Data for, or is determined by, any Covered Method for such APA Tax Year, or (iii) otherwise are relevant to the APA. U.S. Taxpayer shall not simply attach a copy of the pertinent schedule. Rather, U.S. Taxpayer shall specifically identify the relevant items from that schedule, and shall describe in appropriate detail the nature of those items, how they arose, and how they are accounted for.
 - i. Whether or not U.S. Taxpayer contemplates requesting, or has requested, to renew, modify, or cancel the APA.
4. The Financial Statements and additional statements required under paragraph 6(f) of the APA, for such APA Tax Year and for any other tax year whose financial data are relevant to compliance with the APA for such APA Tax Year;
5. A financial analysis that includes U.S. Taxpayer's calculations to apply the Covered Method(s) to the Covered Issue(s) for such APA Covered Year, and supports those calculations with additional material that ties those calculations to the Financial Statements. The intent of this requirement is that the analysis submitted should provide a clear, complete, detailed, and self-contained means by which the IRS can verify compliance with the Covered Method(s). This requirement is further explained as follows:
- a. The additional material must support every numerical input to U.S. Taxpayer's calculations.

Comment [A16]: For example, if a Covered Method uses a three-year rolling average test, then financial data from prior tax years is relevant to compliance.

- b. The additional material could include, for example, consolidating financial statements, segmented financial data, and records from the general ledger.
 - c. Where segmented data are used, U.S. Taxpayer must specify in detail how it accomplished the segmentation, including how it made allocations and apportionments, including (i) the definition and calculation of any apportionment keys used, and (ii) the calculations applying such keys. The inputs used for those various calculations must be tied to the Financial Statements.
 - d. The additional material must be annotated sufficiently to let the IRS easily trace U.S. Taxpayer's entire calculations to objective, verifiable sources of data.
 - e. Where needed for clarity, terms must be defined.
6. The financial results pertinent to the Covered Method(s), for such APA Covered Year and all prior years, entered along with data concerning the Covered Method(s) in an electronic results template available by contacting APMA.
7. An organizational chart for Worldwide Group, revised annually to reflect all ownership or structural changes of the Covered Entities and any other entities that are relevant to the Covered Issue(s) or are otherwise relevant to the Covered Method(s).
- * An organizational chart for a part of Worldwide Group that includes all Covered Entities and includes any other entities relevant to the Covered Issue(s) or Covered Method(s), revised annually to reflect all ownership or structural changes of entities that are involved in the Covered Issue(s) or are otherwise relevant to the Covered Issue(s) or Covered Method(s).
8. A valid IRS Form 2848 "Power of Attorney and Declaration of Representative" for any representative to receive notices under paragraph 16 of this APA.
9. A copy of the APA and any amendment.
10. A penalty of perjury statement, executed in accordance with Rev. Proc. 2015-41, sections 7.02(8) and (9).

**APPENDIX D
APA ANNUAL REPORT SUMMARY FORM**

The APA Annual Report Summary on the next page is a required APA Record. APMA supplies some of the information requested on the form. U.S. Taxpayer is to supply the remaining information requested by the form and submit the form as part of its Annual Report.

DRAFT for Public Discussion

Internal Revenue Service	APMA Case No.	<u>2016-123456</u>
Large Business and International Division	Reviewer	<u>Julie Manager</u>
Treaty & Transfer Pricing Operations	Team Leader	<u>Peter Team Leader</u>
Advance Pricing Mutual Agreement Program	Economist	<u>Bob Economist</u>
	Int'l Examiner	<u>James Examiner</u>

APA Information

U.S. Taxpayer's Name	<u>Acme US, Inc.</u>
U.S. Taxpayer's EIN	<u>99-1111111</u>
U.S. Taxpayer's NAICS	<u>335931</u>
Unilateral/Bilateral/Multilateral	<u>Bilateral</u>
Original or Renewal	<u>Original</u>
APA Common Name, if any	<u>Acme Example APA</u>
APA Request Filing Date	<u>January 6, 2016</u>
Date APA Executed	
APA Term (date-to-date, inclusive)	<u>January 1, 2016 to December 31, 2020</u>
Foreign Countr(y)ies Involved	<u>Japan</u>
Annual Report Due Dates for years ending on or before [date]:	
Annual Report Due Dates for other years: [last month of tax year] 15 following close of year	
Covered Methods Summary Description	<u>1. CPM, OM PLI, with ALR of 1% to 3%</u>
(e.g., CPM, operating margin 2%-5%)	<u>2. CPM, MOTC PLI, with ALR of 5% to 10%</u>
Taxpayer's Principal Representative	<u>Richard Representative</u>

APA Annual Report Information:

Year(s) covered by this Annual Report	
Issues for APMA's special attention (or "None")	
Taxpayer Notice Person	Name
<i>If necessary, include a current Form 2848 for the Notice Person</i>	Title
	Address
	City/State/Zip
	Phone/Fax
	Email
Current Representative, if any	Name
<i>Include a current Form 2848 for the representative</i>	Title
	Address
	City/State/Zip
	Phone/Fax
	Email

Comment [A17]: Issues for APMA's special attention could include, for example, a failure or possible failure of a critical assumption, a purchase of the controlled group by an uncontrolled party, a startup of a new business line that might be covered under the APA, or an acquisition of a company whose business might be covered under the APA.

Date Annual Report Filed (to be filled in by APMA):