

**Non-official translation -  
the German version is decisive**

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**Information on bi- or multilateral mutual agreement procedures under double taxation agreements for reaching Advance Pricing Agreements (“APA”) aimed at granting binding advance approval of transfer prices agreed between international associated enterprises**

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With reference to the outcome of the discussions held with the supreme tax authorities of the *Länder*, the following applies to mutual agreement procedures under double taxation agreements for reaching Advance Pricing Agreements (“APA”), aimed at granting binding advance approval of transfer prices agreed between international associated enterprises (“APA procedures”):

List of Contents:

- 1 General
- 1.1 Purpose of the regulation
- 1.2 The term “APA”, definition, legal basis
- 1.3 Principles
  
- 2 Initiation of the Procedure
- 2.1 Responsibilities
- 2.2 Pre-filing
- 2.3 Application requirements

- 3 Content of an APA, Documents to be Provided, Rejection of an APA Request
- 3.1 General
- 3.2 Definition of scope of application
- 3.3 Transfer pricing method, additional criteria for the determination of transfer prices
- 3.4 Justification of the applied method and of the determination of transfer prices
- 3.5 Documents to be provided
- 3.6 Special requirements for cost sharing agreements
- 3.7 Critical assumptions
- 3.8 Term
- 3.9 Rejection of an APA request, reasons for refusal
  
- 4. Conducting the APA Procedure, Procedural Principles
- 4.1 General
- 4.2 Applicant's participation in the APA procedure
- 4.3 Cooperation between federal and regional authorities [*Bund und Länder*]
- 4.4 Cooperation with the other country / countries
- 4.5 Conclusion of the APA procedure with the other country
- 4.6 Applicant's consent, waiver of right of appeal (Sect. 354 [1a] General Tax Code [AO])
  
- 5. Implementation
- 5.1 Implementation in Germany by the competent regional tax administration
- 5.2 Implementation in the other country
  
- 6. Measures During the Term, Binding Effect
- 6.1 Taxpayer's reporting and documentation obligations (annual report)
- 6.2 Reviewing critical assumptions
- 6.3 Binding effect on the tax authorities
- 6.4 Binding effect on the applicant / taxpayer
- 6.5 Cancellation or limitation of the effect of an APA
- 6.5.1 Failure to implement the underlying facts
- 6.5.2 Failure to satisfy the critical assumptions
  
- 7. Additional Procedural Rules
- 7.1 Change requests
- 7.2 Withdrawal of an APA request
- 7.3 APA roll back
- 7.4 APA renewal
- 7.5 Initial adjustments by a third country after conclusion of an APA
  
- 8. Simplified Procedure for Small and Medium-Sized Enterprises
  
- 9. Publication

## 1. General

### 1.1 Purpose of the regulation

This document concerns itself with the procedure involved when requests are filed for advance pricing agreements (“APA”) under double taxation agreements (“DTA”), aimed at granting binding advance approval of transfer prices agreed between international associated enterprises. It also deals with reviewing and implementing such requests, how to conduct the procedure, and to set out the effects of such procedure. Its purpose is to make it easier for enterprises to reach APAs and to clarify their rights, obligations and duties during mutual agreement procedures, aiming to reach the conclusion of an APA, and to regulate the handling of APA requests by the Federal Central Tax Office and by the tax authorities of the *Länder* (jointly referred to as “tax authorities”).

The German tax authorities conduct APA procedures, the intention being to reach mutual agreements if possible, in order to resolve in advance potential disputes on transfer prices arising between enterprises and the various countries’ tax authorities, and to avoid the two-fold financial burden or double taxation (respectively) they threaten to cause. APAs aim to achieve greater legal certainty for businesses and greater efficiency in transfer pricing audits. In using this procedure, the German tax authorities follow the usual practice of the majority of industrial nations, as is also recommended by the OECD (Item 4.161 ff., OECD Guidelines, 1995<sup>1</sup>).

This document applies (accordingly to) APA procedures aimed at establishing whether the distribution of profits between a domestic enterprise and a foreign permanent establishment conforms with the arm’s length principle, and at calculating the profits of foreign enterprises’ permanent establishments located in Germany.

Wherever this document does not contain any specific rules, it is supplemented by the Memorandum on international mutual agreement and arbitration procedures in the field of taxes on income and capital<sup>2</sup>.

### 1.2 The term “APA”, definition, legal basis

As widely understood internationally, an APA is an agreement between one or more taxpayers and one or more tax administrations. It lays down – before controlled transactions between associated enterprises in different countries are carried out – a transfer pricing method in accordance with the arm’s length principle, for fixing transfer prices for given business transactions over a given period (Item 2.2 and Item 2.4 of the Administrative Principles 1983; Item 3.4.10 of the Administrative Principles Procedure; Item 4.124 of the OECD Guidelines 1995<sup>1</sup>; Item 3 of the OECD “MAP APA”<sup>3</sup>). In addition, further criteria for determining transfer prices can be agreed, e.g. identification of comparables, arrangements for updating them throughout the period covered by the APA, calculations for suitably effecting adjustments, critical assumptions with regard to future incidents (cf. Sect. 3.7).

Under German tax law, tax agreements between a taxpayer and the German tax authorities are not allowed. Instead of this – provided a DTA applies, containing a clause on mutual agreement procedure in accordance with Art. 25 (1) and (3) OECD Model Convention – an APA may be reached with the other country at the request of the taxpayer (“APA Request”) on the basis of the DTA (Item 4.10 and Item 4.42 of the OECD Guidelines 1995<sup>1</sup>). Germany is bound by any agreement of this sort, i.e. the agreed content has to be implemented (Art.

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<sup>1</sup> OECD Transfer Pricing Guidelines for Multinational Enterprises & Tax Administrations, Paris 1995.

<sup>2</sup> Federal Tax Gazette 2006 I, p. 461.

<sup>3</sup> OECD Transfer Pricing Guidelines, Annex: Guidelines for Conducting Advance Pricing Arrangements Under the Mutual Agreement Procedure, p. AN-19 et sqq.

25 [2] Clause 2 OECD Model Convention). This is done by granting the taxpayer advance approval and by issuing relevant tax assessment notes.

The parties involved in the application procedure pursuant to Art. 25 OECD Model Convention are the taxpayer (applicant) and the Federal Central Tax Office as the “competent authority”. The parties involved in the actual APA procedure are the “competent authorities” of the contracting states, not the taxpayer or its associated enterprise (Memorandum on international mutual agreement and arbitration procedures in the field of taxes on income and capital<sup>2</sup>; Item 4 of the OECD Guidelines “MAP APA”<sup>3</sup>). The parties involved in the advance approval procedure are the taxpayer (applicant) and the competent local tax authority of the respective *Land* (tax office - *Finanzamt*).

As understood by Germany, the advance pricing arrangement and the advance approval together form the APA (Item 4 of the OECD Guidelines “MAP APA”<sup>3</sup>).

In cases where a DTA containing a clause on mutual agreement procedures exists with the country of a foreign enterprise, the latter’s German associated enterprises should only be granted approval of transfer prices for controlled transactions if an agreement has been reached beforehand with the other country; to this extent, successfully concluding an APA procedure is a necessary prerequisite for issuing any advance approval (cf. Sect. 5.1).

In other cases (e.g. where no DTA exists), the competent regional tax authority may – by arrangement with the Federal Central Tax Office, which is responsible for APA procedure – issue the taxpayer on request with a unilateral decision on transfer pricing with future effect, provided the specific case is appropriate and provided legitimate interest exists. The fact that unilateral measures do not reliably eliminate double taxation or might even create taxation gaps advocates rejecting such requests.

If the taxpayer reaches a unilateral APA with another country in accordance with the latter’s laws without the involvement of the German tax authorities, then the German tax authorities shall not be bound by it. If the taxpayer files a request for the competent regional tax authority to be unilaterally bound by this APA, then this request will only be granted in consultation with the Federal Central Tax Office provided it can easily be ascertained that the APA with the other country does not impair German tax interests. If the request is rejected, then the outcome of the tax audit which is regularly conducted subsequently in such cases has to be awaited.

As APAs are legally based on DTAs, they have to be distinguished from other binding approvals (Sect. 204 et sqq. General Tax Code [AO] – granted on the basis of a tax audit), and from binding rulings issued on the basis of good faith (circular of the Federal Ministry of Finance dated 29 December 2003: IV A 4 – S 0430 – 7/03, Federal Tax Gazette I, p. 742 – legal information).

In all cases where German tax authorities are legally bound vis-à-vis a taxpayer in transfer pricing matters, there is an obligation to furnish information to EU member states that are affected but not involved<sup>4</sup>.

### 1.3 Principles

Like mutual agreement procedures, the APA procedure has to be applied for (Item 2.1.1, Memorandum on international mutual agreement and arbitration procedures in the field of taxes on income and capital<sup>2</sup>); it is not regarded as a tax audit procedure within the meaning

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<sup>4</sup> ECOFIN resolution dated 4 June 2002 on the report from the Code of Conduct Group (Business Taxation) to the Council (Business & Finance).

of Sect. 193 et sqq. General Tax Code [AO]. The applicant must submit to the tax authorities all the known relevant facts for an objective review of transfer prices and give them unlimited assistance in their efforts to clarify the matter. The applicant should be involved more than in a normal mutual agreement procedure (cf. Sect. 4.2), in particular the transfer pricing method proposed by the applicant (cf. Sect. 3.3 and 3.4) has to be thoroughly discussed with it.

In view of the Principle of Investigation (Sect. 88 [2] General Tax Code [AO]), the tax authorities have to consider all the circumstances to the taxpayer's advantage and disadvantage that emerge during the APA procedure, even if the APA ultimately fails. By means of international administrative assistance the tax authorities may exchange information obtained with other countries involved under the regulations laid down in the General Tax Code, in EU laws on mutual assistance, and in DTAs. The rules on tax secrecy (Sect. 30 General Tax Code [AO]) remain unaffected.

A request for APA procedure aimed at granting advance approval to transfer pricing cases (an APA request), has no direct impact on other proceedings in or out of court (e.g. suspension of execution, appeals); measures to coordinate the APA procedure may be needed, e.g. administrative appeals that have been filed may have to be suspended. Furthermore, an APA request does not prevent a tax audit being conducted or continued, particularly since a tax audit generally involves other assessment periods; in some cases, it may be wise to arrange to prolong the audit until an agreement is reached in the APA procedure ("roll back", cf. Sect. 7.3).

## **2. Initiation of the Procedure**

### **2.1 Responsibilities**

The Federal Central Tax Office as the "competent authority" within the meaning of the DTA is responsible for conducting the APA procedure. The Federal Central Tax Office coordinates the content of an APA on transfer prices with the competent regional tax authorities.

The local tax authorities of the *Länder* are responsible for granting advance approval of transfer prices and for issuing relevant tax assessment notes. Advance approval is granted by way of implementing the APA procedure (in accordance with Art. 25 Para. 2 Clause 2 of the OECD Model Convention); for special cases, reference is made to Sect. 1.2 above, third-last paragraph).

As regards to cooperation between federal and regional tax authorities (*Bund und Länder*), reference is made to Sect. 4.3 below.

### **2.2 Pre-filing**

In an initial step, the taxpayer should request the Federal Central Tax Office to conduct preliminary talks ("pre-filing") to discuss the procedure and to agree e.g. on the right subject-matter and content of the APA request (cf. Sect. 3), and on what documents are required in the specific case (cf. Sect. 3.5 and 3.6). The *Land* concerned has to be involved (cf. Sect. 4.3). The parties may also discuss the Federal Central Tax Office's estimation of the prospects of an agreement with the other competent authority being reached in the APA procedure. It has to be pointed out to the taxpayer that the German tax authorities will only conclude an APA provided the taxpayer waives its right to appeal against tax notices implementing the outcome of the agreement during the period covered by it in accordance with Sect. 354 General Tax Code (1a) (AO) (cf. Sect. 4.6). Apart from this, a joint non-binding estimate should be made of how long it will take to conclude the APA. This estimate should

be made as early as possible, discussed with all the parties involved in the procedure, and if necessary jointly reviewed in further proceedings in the event of any changes occurring.

Pre-filing on an anonymous basis (without naming the taxpayer concerned) is also permitted. However, in any such cases all the statements made by the tax authorities that go beyond information on procedural issues are non-binding; in particular, the tax authorities will not do any preparatory work.

### 2.3 Application requirements

Only persons covered (in accordance with Art. 1 of the OECD Model Tax Convention) are entitled to file an APA request with the competent authority (Federal Central Tax Office) (in accordance with Art. 25 (1) of the OECD Model Tax Convention). Notwithstanding this, the applicant does not actually participate in the APA procedure (cf. Sect. 1.2). The applicant must expound its legitimate interest in having the APA procedure conducted and brought to a conclusion. The request has to be filed in writing and signed personally by the applicant. In addition, a request for binding advance approval to be granted may be filed with the local tax office responsible, but this request will not be met before the APA procedure is concluded; attention is drawn to Sect. 5.1 below.

An APA request has to be filed with the Federal Central Tax Office – which is responsible for the APA procedure – enclosing four copies of all the application documents required (cf. Sect. 3.5). The Federal Central Tax Office immediately forwards one copy each to the supreme tax authority of the *Land* concerned (competent supreme tax authority of the *Land*), or to the regional inland revenue office to which it has assigned the task (requested authority), and to the local tax authority responsible (local tax office).

If an APA request or an application for the granting of advance approval which requires an APA is filed with the taxpayer's local tax office, then the latter shall draw the applicant's attention to the fact that it has to file the APA request with the Federal Central Tax Office which is responsible for such matters. The date on which the request is received by the Federal Central Tax Office determines the earliest date on which the term of the APA may commence (cf. Sect. 3.8). Independently of this, the competent regional tax authority also ensures that the Federal Central Tax Office is informed of the request and receives a copy.

As a rule, the fact that a taxpayer's international transfer prices may be the subject of a tax audit does not conflict with its request. Reference is made to Sect. 1.3 above regarding the effects which the request may potentially have on other proceedings (e.g. tax audit procedure).

## 3. Content of an APA, Documents to be Provided, Rejection of an APA Request

### 3.1 General

The applicant determines the content of the APA in its request. The scope of application in terms of both content (cf. Sect. 3.2) and period (cf. Sect. 3.8) has to be defined in the request. The other country with which an advance agreement is to be reached has to be named. Whenever multilateral APA procedure is requested, in legal terms it is deemed that several requests for bilateral procedure have been submitted.

The applicant must explain the request in detail and provide all the necessary records (cf. Sect. 3.5 and 3.6). The tax authorities may make additional queries at any time and demand further information and documents relating to the request. In order to avoid any unnecessary

delays, the applicant must immediately meet such demands. If any changes occur to the underlying facts or are made to the applicant's respective plans after the request has been filed, then the Federal Central Tax Office has to be informed without delay.

The date on which the request is received by the Federal Central Tax Office determines the earliest date on which the term of the APA may commence (cf. Sect. 3.8).

At any stage of the procedure, if the tax authorities so request, the applicant must translate all or any of the documents it has submitted at its own expense (Sect. 87 [2] Clause 2 and 3 General Tax Code [AO]).

### 3.2 Definition of scope of application

The applicant may restrict its APA request e.g. to certain exactly specified types of transactions (e.g. product lines, firms, corporate divisions), or to transactions with certain exactly specified associated enterprises, or to transactions with associated enterprises in given countries. If there is any possibility of third-party countries that are not involved querying the outcome of the APA at a later date (cf. Sect. 7.5), then the applicant must point this out. Any restrictions must be appropriate and have good reasons. Attention is drawn to the possibility of the request being rejected due to arbitrary restrictions (cf. Sect. 3.9).

### 3.3 Transfer pricing method, additional criteria for the determination of transfer prices

In general, the Federal Central Tax Office reaches APAs on transfer prices regularly only accepting one or more transfer pricing methods for specific transactions or for specific types of transactions that lay down specific critical assumptions. Any arrangement that goes beyond agreeing on a method is only possible if conditions that relate to the method and that are secured by critical assumptions can be specified in the individual case (cf. Sect. 3.7). For instance, if there is any doubt about remuneration payable for contract manufacturing, then beyond the cost-plus method that is applicable, a specific range of mark-ups may only be agreed provided proof of reliable reference data, with at least limited comparability, can actually be furnished for the period covered by the APA. If this is not possible (e.g. because at a later date comparable businesses are no longer listed in databases), then one of the foundations for the APA – the “critical assumptions” – has ceased to exist (lapsed). For the consequences of this, reference is made to Sect. 6.4 below.

In order to avoid putting the APA at risk due to the critical assumptions not being satisfied (cf. Item 3.7), any apparent possibility of fluctuations in the decisive circumstances should be taken into account by agreeing mechanisms for making adjustments.

If the method proposed is not suitable (for deciding on whether transfer pricing methods are suitable, see Item 2.4.1 of the Administrative Principles 1983<sup>5</sup> and Item 3.4.10 of the Administrative Principles Procedure 2005<sup>6</sup>), then the Federal Central Tax Office will work (presses) for an application of a suitable method; attention is drawn to the fact that the APA request may be rejected (cf. Sect. 3.9).

### 3.4 Justification of the applied method and of the determination of transfer prices

The reasons given by the applicant must show that applying the proposed transfer pricing method complies with the arm's length principle as regards the transactions to be covered by

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<sup>5</sup> Federal Tax Gazette 1983 I, p. 218.

<sup>6</sup> Federal Tax Gazette 2005 I, p. 570.

the APA. The method has to be described in detail; all the necessary documents and all the computations for applying the method have to be provided; this regularly includes a detailed calculation scheme. Apart from this, third-party data recently collected for comparative purposes, with at least limited comparability (Item 3.4.12.7 c) of the Administrative Principles Procedure 2005<sup>6</sup>) (e.g. prices, gross margins, mark-ups on costs) must be given, and calculations for adjustments which may become necessary at a future date have to be explained.

### 3.5 Documents to be provided

A generalised list of the documents or records having to be provided cannot be made, because they depend on the circumstances in each individual case and on the (objective) possibilities for obtaining information (with regard to future transactions). Clarifying this for the case in hand is one of the tasks to be done during pre-filing (cf. Sect. 2.2).

If an APA request has been filed and if a tax year affected (cf. Sect. 3.8) ends whilst the APA negotiations are still underway, then the applicant must immediately submit records showing the results on the actual figures for said tax year, which have been brought about by applying the planned transfer pricing method. Relevant documentation has to be submitted on request, at the latest before the submission deadline laid down in Sect. 90 (3) Clauses 8 and 9 General Tax Code (AO); reference is made to Sect. 3.9 below.

The following list – which is not conclusive – names the documents and records which in many cases will be required for conducting APA procedure:

- a) description of shareholding ratios;
- b) description of the organisational and operative structure of the group;
- c) description of the operative areas, insofar as is required for the APA (cf. Sect. 3.2);
- d) description of the business relations with associated enterprises (planned contractual arrangements);
- e) description and explanation of the functions and risks assumed;
- f) list and brief description of the main assets (in particular intangibles) of significance to the business relations at issue;
- g) description of the market situation, competition, and the business strategy/strategies chosen;
- h) description and assessment of the planned value-added chains, and contributions from the companies involved;
- i) list of all outstanding tax issues (also in relation to other tax administrations) connected with the transactions to be covered by the APA.

These documents have to be provided insofar as they relate to the APA term and are relevant to the specific APA. It has to be stated whether any changes are anticipated during the period covered by the APA, and how they may affect application of the proposed transfer pricing method.

Further information is contained in the Federal Central Tax Office's "Questionnaire" for filing requests, obtainable at: [www.bzst.de](http://www.bzst.de).

### 3.6 Special requirements for cost sharing agreements



If the subject-matter of the APA is a “cost sharing agreement” or a “cost contribution agreement”, then at a minimum the following documents and records have to be provided:

- a) the planned (or amended) cost sharing agreement along with all its appendices, annexes and supplements;
- b) documents on the anticipated benefit for all parties, including a presentation of the method used and calculations of the forecast figures;
- c) documents on the proposed use of the cost sharing formula;
- d) if not included in the cost sharing agreement, documents on the planned arrangements for invoice controlling, on mechanisms for making adjustments (if circumstances alter), on authorising access to the relevant documents on cost sharing, and on allocating rights of use.

In all other respects, the documentation relating to cost sharing agreements that has to be submitted along with an APA request is listed in the circular of the Federal Ministry of Finance regarding documentation requirements for cost sharing agreements dated 30 December 1999 (IV B 4 – S 1341 – 14/99)<sup>7</sup>.

### 3.7 Critical assumptions

As regards future transactions, certain “critical assumptions” have to be made which have a decisive influence on the business relationship. In the relationship between the parties to the advance mutual agreement (i.e. between the DTA countries involved), these critical assumptions constitute an expressly agreed basis for the contract being concluded. Depending on the matter to be arranged under its APA request, the applicant should suggest which critical assumptions in its view should apply with regard to the effectiveness of the mutual agreement, e.g. with reference to the circumstances prevailing at the business or its business partner, or with reference to conditions prevailing generally in business, trade and industry. The applicant should also explain the extent to which the method it is proposing allows changes in the critical assumptions to be taken into account. The critical assumptions and the matter being arranged under the APA must be so interdependent that changes in the agreed critical assumptions are likely to affect or cast doubt on the material agreements reached in the APA.

Critical assumptions may include:

- a) consistent shareholding ratios;
- b) consistent market conditions, market shares, business volumes, sales prices (e.g. no drastic changes due to new technology); giving a framework in each case;
- c) consistent conditions, e.g. relating to supervisory rights, customs duties, import and export restrictions, international payment transactions;
- d) consistent allocation of functions and risks, consistent capital structure, consistent business model;
- e) consistent exchange rates and interest rates;
- f) tax levied in accordance with the APA in the other country;
- g) no substantial changes to the tax circumstances prevailing in the other country;
- h) corrections to transfer prices by a third-party country not involved in the APA, which have an effect on the APA.

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<sup>7</sup> Federal Tax Gazette 1999 I, p. 1122.

Possible consequences occurring when critical assumptions are not (cannot be) satisfied are discussed in Sect. 6.4 below.

### 3.8. Term

Since APAs relate to the future, their term generally commences at the beginning of the fiscal year in which the formal request is filed. An earlier commencement date may be allowed if, on the date when the APA request is filed with the Federal Central Tax Office (cf. Sect. 2.3), a tax return has not yet been submitted for an earlier fiscal year and the statutory deadline for submitting said tax return (Sect. 149 General Tax Code [AO]) has not yet expired.

Some other commencement date may be agreed in order to take into account normal practice in other countries, provided this does not impair the interests of the German tax authorities. Attention is drawn to the possibility of also extending the effects of an APA to preceding years on certain conditions ("roll back", cf. Sect.7.3).

In order to fix a reasonable term, the following aspects have to be taken into account amongst others:

- the permanence and stability of the business relations covered;
- the taxpayer's interest in being bound in the long-term, and any reservations the tax authorities may have to this;
- normal practice in the other country involved.

Care should be taken to avoid the expiry of all or most of the term before the APA is concluded; if necessary, the applicant should alter its request accordingly.

In individual cases, the disadvantage of just a short term can be compensated by way of (simplified) opportunities for renewal (cf. Sect. 7.4). The term should be not less than three and not more than five years.

### 3.9 Rejection of an APA request, reasons for refusal

A decision not to initiate the APA procedure is a decision on the APA request, and is thus an administrative act within the meaning of Sect. 118 General Tax Code (AO); the decision is at the due discretion of the Federal Central Tax Office, which is responsible for mutual agreement procedure, and is taken in consultation with the competent supreme tax authority of the *Land* involved (cf. Sect. 4.3).

When a decision is made on whether to initiate the procedure, discretionary consideration must be paid to the taxpayer's interest in reliably avoiding the possibility of double taxation, and to the authorities' interest in settling the question of transfer pricing by mutual agreement, which might otherwise become the (possibly complex) subject-matter of a tax audit or of ordinary mutual agreement procedure.

When weighing up interests, individual issues considered may include e.g.

- the compliance of the content of the request with the German transfer pricing principles, possibility of international implementation, APA practice in the other country;
- Foreseeable difficulties or doubts with respect to the interpretation of the applicable DTA, which it is better to resolve before carrying out the controlled transactions concerned (authorities' interest in granting approval);

- the seriousness of the business to be assessed, hypothetical transactions, any evidence that the tax authorities' position is being put to the test, tax avoidance as an evident motive for the request;
- a dispute in an on-going tax audit which, since it involves the same facts, might indirectly be solved by reaching an APA.

Factors speaking against initiating the APA procedure include e.g. if the applicant restricts its request without giving objective reasons; if the applicant has no legitimate interest or is only interested in avoiding tax; if substantial delays occur for which the applicant is responsible; if the applicant refuses to give the tax authorities sufficient information; or if the applicant insists on using a method which the tax authorities consider unsuitable.

If the applicant fails to meet the necessary requirements for initiating the procedure, then after making a prior announcement it is at the Federal Central Tax Office's discretion to refuse the APA request on consultation with the competent supreme authority of the *Land* or with the requested authority. Sect. 1.3 above must be observed as regards taking into account any insights gained as a result of the request. Before the notice of refusal is issued, the applicant is given an opportunity to eliminate the reason for its request being rejected.

## **4. Conducting the APA Procedure, Procedural Principles**

### **4.1 General**

Apart from an uninterrupted flow of information amongst the tax authorities involved and in relation to the taxpayer, it is mainly the time-wise coordination and rapid conduction of the procedure that are decisive for a successful conclusion of the APA procedure; this applies to all its stages (pre-filing, filing the request, negotiating with the applicant, informing the tax authority in the other country, negotiating with the other country, concluding a mutual agreement, the applicant's consent, granting binding advance approval). If a rapid conclusion is to be reached, this above all requires – in addition to close cooperation amongst all concerned – arranging a realistic time schedule for the entire APA procedure and for each procedural step, even if this schedule is not binding. If any of those involved encounters difficulties with respect to timing, then it must inform all the others without delay.

A decision on cancelling the APA procedure after it has been initiated has to be taken paying attention to the aspects mentioned in Sect. 3.9 above.

### **4.2 Applicant's participation in the APA procedure**

The applicant does not attend the actual APA procedure (cf. Sect. 1.2). This does not affect the possibility of terminating the APA procedure at any time by withdrawing the APA request ("voluntary withdrawal") (reference is made to Sect. 7.2 regarding the possibility of changing over to consultation procedure, which is not contingent upon a request). The Federal Central Tax Office keeps the applicant informed at regular intervals about the stage the procedure has reached. As the "competent authority", it decides together with the other country on whether the applicant or the applicant's representative may attend some of the negotiations in person, and on giving the applicant the possibility of presenting its position to both countries at these negotiations and discussing it with them; this may be expedient to accelerating procedure.

In all other respects, the applicant is a participant in its own request procedure and in the procedure for advance approval; as such, it is under obligation to cooperate, to obtain and provide information, and to submit documents and records; this may also entail allowing investigations on its own business premises.

Reference is made to Sect. 1.3 above regarding the utilisation of insights from information provided by the applicant in APA procedure.

#### 4.3 Cooperation between federal and regional authorities [*Bund und Länder*]

The Federal Central Tax Office immediately informs the supreme tax authority of the respective *Land* when pre-filing is conducted, requesting it to attend if possible. The supreme tax authority may name a representative for this.

After an APA request has been received, the Federal Central Tax Office forms an “APA team”, calling in the supreme tax authority of the *Land* or the requested authority. This team is composed of one representative of the competent department at the Federal Central Tax Office, and at least one representative of the *Land* concerned. The representatives of the *Land* should include a tax auditor, namely the inspector responsible for the company, for the branch concerned, or for APAs in general, depending on how the *Land* is organised. More than one tax auditor may be appointed. The *Land* concerned gives the Federal Central Tax Office the name of a contact person, who joins the APA team and is responsible for continuously informing the regional tax authorities authorised to take decisions (supreme tax authority of the *Land*, chief tax administration, local tax office).

The competent division at the Federal Central Tax Office decides on whether to involve a tax auditor from the Federal Tax Audit Department in the APA team; doing so is expedient in particular if the Federal Tax Audit Department cooperates in the tax audit of the company, or has special know-how relating to the branch or to transfer pricing.

The Federal Central Tax Office (“competent authority”) assumes the task of “team coordinator”, i.e. it conducts the APA procedure with the other country and coordinates job assignments with the tax auditors involved (e.g. keeping to agreed time schedules). Via the contact person who has been named by the *Land*, it also has the task at all stages of the procedure of bringing about agreement with the regional tax authorities authorised to take decisions.

#### 4.4 Cooperation with the other country / countries

The applicant should simultaneously file its APA request with the Federal Central Tax Office and with the foreign tax authority, enclosing the same documents.

On commencement of the APA procedure, the Federal Central Tax Office endeavours to consult the foreign “competent authority” about the procedure, above all time-wise (cf. Sect. 4.1). The aim of this collaboration is to achieve a complete exchange of data and ensure that both countries have the same information available.

#### 4.5 Conclusion of the APA procedure with the other country

In agreement with the *Land* concerned, the Federal Central Tax Office as “competent authority” concludes the APA with the “competent authority” of the other country in writing. The declaration of intent from the Federal Central Tax Office, which is required to this end, is issued subject to the applicant consenting to the agreement and at the same time waiving its right to appeal in accordance with Sect. 354 (1a) General Tax Code (AO) (cf. Sect. 4.6). On receipt of the relevant statements from the applicant, the other country has to be notified about the date when the APA finally takes effect, i.e. when the above reservation has ceased to exist.

The agreement has to be concluded in German and if necessary in the language of the other country as well. Several bilateral APA procedures based on a single request may be concluded in a single contract document. For simplicity's sake, just a single language version (usually English) may in such cases be declared binding by mutual agreement; the applicant has to provide a German translation on consultation with the Federal Central Tax Office, which forms the basis for the binding approval (cf. Sect. 5.1).

The possible wording of an agreement is given in the specimen attached by way of an annex (Annex).

#### 4.6 Applicant's consent, waiver of right of appeal (Sect. 354 [1a] General Tax Code [AO])

After the APA has been signed, the Federal Central Tax Office notifies the applicant in writing about the outcome. The applicant has to immediately issue and sign a written statement consenting to the APA (cf. Sect. 4.2 of the Memorandum on international mutual agreement and arbitration procedures in the field of taxes on income and capital<sup>2</sup>). In view of the reservation (cf. Sect. 4.5), the agreement only takes effect when the applicant waives vis-à-vis the competent local tax authority ( Sect. 354 [1a] General Tax Code [AO]) its right to appeal against tax notices correctly implementing the outcome of the advance mutual agreement during the period covered by it. The applicant also has to state that it is aware that the German tax authorities are only obliged to abide by the agreement provided the circumstances on which the APA is based are actually brought about (cf. Sect. 6.5.1), provided the critical assumptions are satisfied (cf. Sect. 6.5.2), and provided the annual reports required (cf. Sect. 6.1) are provided to the tax authorities.

## 5. Implementation

### 5.1 Implementation in Germany by the competent regional tax administration

Under Art. 25 (2) of the OECD Model Convention, the competent regional tax administration (tax office) is obliged on conclusion of the APA procedure to issue binding advance approval to the same effect (cf. Sect. 4.5) on request (cf. Sect. 2.3). With a view to Sect. 6.4 and Sect. 6.5.2 below, the advance approval must include a right of revocation.

When the further requirements have been met, tax notices in accordance with the APA have to be issued for the period covered by the APA (cf. Sect. 6.3).

### 5.2 Implementation in the other country

Implementation in the other country is of no importance to implementation in Germany or to domestic procedure. If the taxpayer finds that implementation in the other country leads to difficulties, or if any deviations from the APA occur, then it must inform the Federal Central Tax Office, which can then contact the other country and in agreement with the competent supreme tax authority of the *Land* decide whether to aim for renewed negotiations.

## 6. Measures During the Term, Binding Effect

### 6.1 Taxpayer's reporting and documentation obligations (annual report)

An integral part of the agreement with the other country is an undertaking by the taxpayer to draw up and submit an annual report "compliance report", showing that the matter underlying the agreement has been realised in the fiscal year concerned, and in particular that the critical assumptions (cf. Sect. 3.7) have been satisfied. In this report, the taxpayer must expressly draw attention to every single deviation, and state whether it has made any adjustments, and if so which. If the taxpayer breaches this obligation, this may have negative consequences (cf. Sect. 4.6).

If according to the report critical assumptions have not been satisfied, then the taxpayer should submit proposals for making relevant adjustments to the mutual agreement. Any supplementary queries made by the tax authorities in this context have to be answered by the taxpayer without delay.

The report should be delivered to the Federal Central Tax Office, and at the same time to the local tax office responsible, by the end of the statutory period for tax returns for the year concerned, either in German or in the respective foreign language with a German translation. At the latest, it must be delivered by the earlier of the following dates:

- at the same time as it is submitted in the other country,
- along with the tax return for the assessment period concerned.

## 6.2 Reviewing critical assumptions

The Federal Central Tax Office takes charge of reviewing whether according to the annual report the critical assumptions have been satisfied. Any doubts arising have to be jointly clarified with the competent local tax authority. If applicable, the latter points out to the Federal Central Tax Office any inconsistencies between the annual report and the tax return that has been filed. In agreement with the competent supreme tax authority of the *Land*, the Federal Central Tax Office decides whether it is necessary to take any measures regarding the APA, e.g. to terminate the APA, or to take up negotiations with the other country (cf. Sect. 6.5).

In a later tax audit, it has to be established whether the taxpayer has complied with the APA in the years audited, and in particular whether the decisive circumstances have actually been brought about (cf. Sect. 6.5 1) and the critical assumptions have been satisfied (cf. Sect. 6.5.2).

## 6.3 Binding effect on the tax authorities

The tax authorities are bound by the APA, provided the underlying facts of the APA have been implemented and the critical assumptions have been satisfied. They are not entitled to deviate in audits or assessments from results that are based on correct application of the APA. For example, they may not make any changes based on another transfer pricing method.

During any tax audit performed at a later date, the tax authorities are entitled to establish whether the decisive underlying facts have actually been implemented and whether the agreed critical assumptions (including the information in the annual reports to be submitted by the taxpayer, cf. Sect. 6.1) have been satisfied in the period covered by the APA. If the critical assumptions are not satisfied, then in principle the binding effect on the tax authority ceases to exist; which empowers them to effect consequences accordingly (cf. Sect. 6.5.2).

## 6.4 Binding effect on the applicant / taxpayer

The applicant / taxpayer is under no obligation by reason of the APA to implement the underlying facts used as a basis for the APA. If it fails to do so, then Sect. 6.5.1 below applies.

If the taxpayer implements the facts on which the APA has been based, then it is also bound by the agreements reached in the APA which it has arranged and to which it has expressly consented (cf. Sect. 4.5). If it charges prices other than those agreed in the APA, then the tax authorities may base taxation on the provisions of the APA, notwithstanding any divergent amounts charged. The Federal Central Tax Office informs the other country without delay about any facts in this respect. In individual cases, the tax authorities may, in consultation with the other country, treat the APA as if it had never been reached and revoke the advance approval (cf. Sect. 5.1).

If the taxpayer appeals against a tax notice correctly implementing the APA, then this appeal is inadmissible if the taxpayer has waived filing legal remedies in accordance with Sect. 4.6 ( Sect. 354 [1a] General Tax Code [AO]).

## 6.5 Cancellation or limitation of the effect of an APA

Whenever the effect of an APA is cancelled or restricted, it must be remembered that for taxation purposes, the tax authorities are obliged under Sect. 88 General Tax Code (AO) (Principle of Investigation) to take into account all and any insights gained during the procedure, both to the benefit and to the disadvantage of the taxpayer (cf. Sect. 1.3).

### 6.5.1 Failure to implement the underlying facts

Both the APA and the advance approval become obsolete and lose all legal effect if the taxpayer fails to implement the facts on which the APA has been based.

### 6.5.2 Failure to satisfy the critical assumptions

If critical assumptions fail to be satisfied in substantial respects, then the basis for the APA ceases to exist; the advance approval may be revoked (cf. Sect. 5.1) with effect as from the date when the critical assumptions are not (or are no longer) satisfied. The Federal Central Tax Office informs the other country immediately about any such circumstance.

In the case of immaterial deviations, the Federal Central Tax Office may allow the APA to continue in agreement with the supreme tax authority of the *Land*, or it may adjust it accordingly by agreement with the taxpayer after holding (written) consultations with the other country. The Federal Central Tax Office informs the other country without delay on establishing any deviation from the position taken by the German tax authorities.

In all other cases, the Federal Central Tax Office may take up negotiations with the other country by agreement with the supreme tax authority of the *Land* in order to adjust the APA to the altered circumstances. For this, a request from the taxpayer is required enclosing all the necessary documents (change request). If the request is not filed or if an adjustment by mutual agreement with the other country is not possible, then the APA loses effect as from the date when the critical assumptions are not (are no longer) satisfied; the advance approval may be revoked accordingly (cf. Sect. 5.1). Reference is made to Sect. 1.3 above.

## 7. Additional Procedural Rules

## 7.1 Change requests

Until the APA has been concluded with legal effect (cf. Sect. 4.5 and 4.6), the applicant may alter its APA request at any time. A substantial alteration to a request is regarded as a new request (in which case the later date of receipt applies, affecting the term accordingly, cf. Sect. 3.8). The tax authorities may reject any such new request if there is reason to assume that the applicant has not thoroughly prepared the procedure, or is not conducting it seriously, or if objectives beyond the actual procedure are being pursued (e.g. putting the tax authorities to the test, cf. Sect. 3.9).

## 7.2 Withdrawal of an APA request

Since APA procedure – like mutual agreement procedure – is based on a request, the withdrawal of the request means that there is no longer any basis for conducting the procedure; the procedure is terminated. Notwithstanding this, the contracting states may in suitable cases hold consultations (pursuant to Art. 25 (3) of the OECD Model Convention), which are not contingent upon a request and have to be distinguished from APA procedure, if during the negotiations any difficulties or doubts regarding the DTA have arisen (even if only in one specific case) which should be resolved by mutual agreement.

Any facts emerging during the procedure have to be taken into account in Germany in accordance with the Principle of Investigation (cf. Sect. 1.3).

## 7.3 APA roll back

If the taxpayer requests that a transfer pricing method agreed in an APA be applied retroactively to assessment periods preceding the agreed term of the APA (so-called “roll back”), then this is possible under certain circumstances, in particular if the other country consents. A roll back requires proof from the taxpayer that the circumstances brought about in the respective preceding years match the circumstances during the years covered by the APA. Apart from this, documentation must be provided for assessing the preceding years, which matches the documentation for the period covered by the APA.

In formal terms, the preceding years cannot be covered by the APA (cf. Sect. 3.8). Roll back in terms of content is possible e.g. under mutual agreement procedure pursuant to Art. 25 (1) of the OECD Model Convention, which has to be initiated separately but may be conducted alongside the APA; the conclusion of such procedure is legally independent.

As regards preceding years, the tax authorities are free to check whether – insofar as the same circumstances prevail – the results would have had to be determined in accordance with the method agreed in the APA procedure. In this respect it has to be taken into account that establishing whether transfer prices comply with the arm’s length principle – even if circumstances are the same – may frequently be done in different ways and with different (acceptable) results (Administrative Principles Procedure, Sect. 2.1, 2005<sup>6</sup>). Thus the tax authorities only make a correction for preceding years if said preceding years were treated wrongly or incorrectly. In any such cases, Sect. 153 (1) General Tax Code (AO) has to be heeded.

## 7.4 APA renewal

An APA may – with the other country’s permission – be extended beyond the period of application, if a request to this effect is duly filed and if it is credibly proved that the



underlying facts in future will match the underlying facts on which the APA has been based. In such cases, an extension (with certain adjustments) can probably be agreed in a simple, prompt procedure, as this procedure should not require submission of all the documents needed for the initial request (cf. Sect. 3.5). The term of the renewal agreement depends on the circumstances of the specific case, and generally will be geared to the periods to be agreed for APAs.

#### 7.5 Initial adjustments by a third country after conclusion of an APA

If, after conclusion of an APA, a taxpayer liable to resident taxation is subjected to double taxation involving a third country not party to the APA, because said third country does not recognise the outcome of the APA and carries out initial adjustments (cf. Sect. 3.2), then the Federal Central Tax Office either institutes or takes part in a mutual agreement procedure with this country, aiming to get it to eliminate the double taxation by amending the relevant foreign tax assessment notes. The country with which the APA was originally concluded has to be informed without delay, and if necessary included in the mutual agreement procedure with the third country. If the double taxation cannot be eliminated by way of such mutual agreement procedure, then various possibilities can be considered depending on the circumstances of the specific case, aiming on the one hand to uphold the APA and on the other to eliminate double taxation. In agreement with the supreme tax authority of the *Land*, the Federal Central Tax Office decides on procedure by the German tax authorities in each specific case. The taxpayer is given an opportunity to present its interests, which have to be fairly taken into account in the decision.

### 8. Simplified Procedure for Small and Medium-Sized enterprises

For applicants whose controlled transactions covered by the APA will probably not exceed the amounts given in Sect. 6 (2) of the Documentation Ordinance [GAufzV], the Federal Central Tax Office may on request grant simplifications regarding the requirements laid down in Sect. 3.4 and 3.5, provided this poses no threat to the objective of the APA – namely to create legal certainty for the applicant that is based on clear facts, and to reach an agreement with the other country.

### 9. Publication

This circular is being published in the Federal Tax Gazette, Part I. For an interim period it can be accessed and downloaded from the website [www.bundesfinanzministerium.de](http://www.bundesfinanzministerium.de), and it may be accessed permanently at [www.bzst.de](http://www.bzst.de).

By Order  
Müller-Gatermann