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Global Tax Alert

OECD's Forum on Tax Administration announces International Compliance Assurance Programme (ICAP) 2.0 and publishes new Pilot Handbook

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Executive summary

On 28 March 2019, the Organisation for Economic Co-operation and Development's (OECD) Forum on Tax Administration (FTA) held its 12th plenary meeting which took place in Santiago, Chile on 26-28 March 2019. At this year's plenary, the FTA focused on four priorities: (i) Delivering on base erosion and profit shifting (BEPS) and tax certainty; (ii) Improving tax cooperation; (iii) Supporting the continued digitalization of tax administrations; and (iv) Building capacity for developing countries. The high level outcomes of the plenary are discussed in a separate EY Global Tax Alert.[1]

The FTA is a subsidiary body of the OECD. It was created in July 2002 by the OECD's Committee on Fiscal Affairs, with the aim of promoting dialogue between tax administrations and identifying good tax administration practices. At the time of the Chile meeting, the FTA comprised 53 member countries.

At the plenary, FTA members welcomed the publication of seven reports which will provide direct practical assistance to tax administrations on the four priorities. Given that tax certainty is high on the agenda of the FTA, the FTA members recognized that they should focus on improving dispute prevention and dispute resolution mechanisms. To that end, alongside a new report on joint audits, FTA members also announced a second pilot of the *International Compliance Assurance Programme* (ICAP 2.0). A new handbook[2] that will guide the second pilot (the handbook) was also endorsed and published by the FTA.

Building a better working world

The handbook builds on the first ICAP pilot, and remains a working document which will continue to be revised based upon the continuing experiences of participating tax administrations and multinational enterprises (MNEs). The handbook does not provide any specific results of ICAP 1.0.

This Alert identifies and discusses the many key differences between the ICAP 1.0 and the 2.0 pilot/handbook.

Detailed discussion

About ICAP

ICAP is a voluntary risk assessment and assurance program designed to facilitate open and cooperative multilateral engagement between MNE groups willing to engage actively and transparently and tax administrations in jurisdictions where the MNEs have business activities.

The handbook notes that ICAP supports the effective use of transfer pricing documentation, including the MNE's country-by-country report, providing a faster, clearer and more efficient route to improved multilateral tax certainty. Looking forward, it is anticipated that ICAP should reduce the resource burden on both MNEs and tax administrations, and mean fewer disputes requiring resolution through Mutual Agreement Procedures (MAPs).

The handbook notes that ICAP does not provide an MNE with legal certainty as may be achieved, for example, through an advance pricing arrangement (APA). It may, however, give comfort and assurance where tax administrations participating in an MNE's risk assessment consider a covered risk to be low risk. Furthermore, the handbook notes, where an area is identified as needing further attention, work conducted in ICAP can improve the efficiency of actions taken outside the program, including via unilateral, joint or simultaneous tax audit, APAs or MAP.

The first ICAP pilot program was launched in January 2018, with the participation of eight FTA member jurisdictions (Australia, Canada, Italy, Japan, the Netherlands, Spain, the United Kingdom and the United States). In ICAP 2.0, there will be nine additional tax administrations participating: Austria, Belgium, Denmark, Finland, Germany, Ireland, Luxembourg, Norway, and Poland.

Handbook structure

The handbook is comprised of seven chapters:

- Chapter 1 – Introduction
- Chapter 2 – Overview of ICAP 2.0
- Chapter 3 – Suitability and scope
- Chapter 4 – The ICAP risk assessment and assurance process
- Chapter 5 – The role of participants in an ICAP risk assessment
- Chapter 6 – The ICAP documentation package
- Chapter 7 – ICAP governance and coordination

Significant differences between ICAP 1.0 and 2.0 pilots

Increase in the number of covered tax administrations

Under ICAP 2.0, 17 countries will participate. As well as changes to the composition of participating countries (none of the original eight have withdrawn their participation), Chapter 2 of the handbook identifies a significant number of changes to the overall program. It notes that while the number of covered tax administrations for a particular MNE's ICAP risk assessment will remain limited, the increased number of participating countries in turn heightens the likelihood that an MNE will be able to obtain comfort over a greater proportion of its operations. The handbook further notes that experiences from the ICAP 1.0 pilot suggest that a multilateral risk assessment including between four and eight covered tax administrations is likely to be most effective.

Qualification for participation in ICAP 2.0

The handbook notes that, unlike under ICAP 1.0 where MNEs were expressly invited to participate in the pilot, in ICAP 2.0, an MNE may indicate its interest in participating to the tax administration in the jurisdiction of its ultimate parent entity (UPE) – known as the UPE tax administration. Alternatively, an MNE may be proactively approached by its UPE tax administration. Either route will be followed by a discussion to identify proposed covered tax administrations, covered periods and any other covered risks (see below) the MNE would like included in its ICAP risk assessment, in addition to transfer pricing risk and permanent establishment risk.

ICAP 2.0 also introduces the concept of a surrogate lead tax administration. If the UPE tax administration is not willing to act as the leading tax administration, or if it is not included in the list of covered tax administrations on the OECD website, the MNE may approach a tax administration in another jurisdiction where the MNE has significant activities, in order to invite that tax administration to act as a surrogate lead tax administration. If that occurs, according to the handbook, the MNE should inform its UPE tax administration before approaching another tax administration.

Timing of ICAP 2.0

MNEs headquartered in a participating jurisdiction should approach their tax administration to explore the possibility of joining ICAP 2.0 absolutely no later than the end of June 2019, though earlier may be beneficial. The OECD then expects the 17 tax administrations to discuss and agree which MNEs will participate in the program by the end of the summer. The timing of actual scoping and risk assessments will then be discussed with each MNE and will depend upon a number of factors, including the time it takes for the MNE to provide documentation.

Covered risks and covered transactions

In a significant revision to ICAP 1.0, the 2.0 pilot will now include *other categories of risk as agreed by the MNE, the lead tax administration and other covered tax administrations (e.g., hybrid mismatch arrangements, withholding taxes and treaty benefits, etc.)* These types of risks were included in the initial developmental plans for ICAP 1.0, but were omitted prior to its commencement in January 2018. They now join transfer pricing risk and permanent establishment risk as the three key areas of ICAP 2.0 risk assessment focus.

A clearer, more efficient and more flexible process

Based on experience in the ICAP 1.0 pilot, the handbook notes that it is now possible to provide more detail and upfront clarity as to how an ICAP risk assessment will be conducted, providing greater certainty for MNEs and covered tax administrations alike.

In one key change, the distinction between a level 1 (high level) and level 2 (in-depth) risk assessment is removed for ICAP 2.0, and more flexibility has been incorporated into the risk assessment stage, including around the timing, format and content of multilateral engagements, including meetings and calls between the participating MNE and covered tax administrations. The handbook notes that these changes should ensure the approach adopted is appropriate to each MNE, and should further improve the efficiency and effectiveness of an ICAP risk assessment, reducing the resource burden on all participants.

A more targeted approach to documentation

The handbook also notes that the OECD hopes that a more targeted approach to documentation requirements will represent an improvement over ICAP 1.0. In particular, a new scoping stage has been added to the ICAP 2.0 risk assessment and assurance process, which takes place once it is confirmed an MNE will participate in the program, to determine whether any covered transactions will be excluded from a covered tax administration's ICAP risk assessment, if appropriate. This ensures that an MNE will only be required to provide documentation relevant to transactions that are within the scope of its risk assessment.

The handbook further notes that *In most jurisdictions, the level of documentation required for an ICAP risk assessment is less than that typically needed in order to agree an APA or in the course of a tax audit or MAP with respect to covered transactions. In addition, under ICAP an MNE is able to provide a single documentation package for use by all covered tax administrations, whereas it may be required to prepare different documents in each jurisdiction under domestic programmes*.

Specific option for issue resolution to be included in the risk assessment stage

Under ICAP 2.0, issue resolution will allow covered tax administrations to work with an MNE, within the ICAP process, to identify any changes that are needed to allow them to conclude that one or more of the covered risks is low risk. Under ICAP 1.0, such resolution approaches had to occur outside of the program, meaning that an MNE may not have been able to complete the entire ICAP program with all covered tax administrations.

Commonalities with ICAP 1.0

While there are many changes to ICAP 2.0 outlined in the handbook, a number of the original characteristics of ICAP 1.0 are retained. In particular, the following high level features merit mention:

- **Covered periods**: The periods eligible for review in an ICAP risk assessment are an MNE's tax filing periods that correspond to its fiscal years beginning on or after 1 January 2016. The specific period or periods to be included in a particular MNE's ICAP risk assessment (the covered period(s)) will be agreed between the MNE, the lead (or surrogate) tax administration and other covered tax administrations, and may therefore vary. It is anticipated that in most cases an ICAP risk assessment will focus on a single covered period.

- **Roll-forward periods**: ICAP 2.0 is forward-looking, as was ICAP 1.0. As such, covered tax administrations will typically aim to provide tax assurance to an MNE, in accordance with each tax administration's domestic framework, with respect to the covered risks for the two tax filing periods immediately following the covered period(s). These are known as the roll-forward periods, and there must be no material changes during these periods if assurance is to remain in place. The applicable roll-forward periods may be specified in the outcome letter issued by a covered tax administration.
- **Outcome letters**: The outcomes stage commences once the risk assessment stage is completed for the lead tax administration and all other covered tax administrations. During the outcomes stage, an MNE will receive a completion letter from the lead tax administration, confirming that the ICAP risk assessment and assurance process has concluded. At around the same time, it will also receive an outcome letter from each covered tax administration, setting out the results of the tax administration's risk assessment and assurance of the covered risks for the covered periods. Outcome letters will confirm the details of any roll-forward periods after the covered period(s), as well as any obligations on the MNE to provide follow-up information, either annually, or in the event of any material changes that impact the covered risks.

Implications

Although there are already other mechanisms designed to increase levels of tax certainty, ICAP is distinctive in nature as interaction between the taxpayer and the tax authorities of the countries is institutionalized in a way that the taxpayer engages with all authorities concurrently. The growth in the number of covered tax administrations indicates an ongoing shift towards a more multilateral approach to the administration of tax, supporting and expanding the important role of other processes, such as bi- and multilateral APAs, joint and simultaneous audits, and MAP. MNEs are therefore recommended to closely monitor developments with regard to all new and existing opportunities to obtain higher levels of tax certainty, including via ICAP.

While ICAP is a voluntary program, MNE groups may be approached by their national tax administration in 2019 in order to gauge overall levels of interest regarding potential participation. Conversely, MNE groups may also submit an application themselves. Interested groups should therefore ensure that they are fully aware of ICAP's inner workings, as well as the potential challenges and benefits of participation, and are recommended to review the handbook. Additionally they may also wish to discuss the potential challenges and opportunities, specifics of eligibility and application process, documentation requirements, timing, risk assessment processes, and levels of tax assurance offered with their local tax advisor.

Endnotes

1. See EY Global Tax Alert, *OECD's Forum on Tax Administration agrees on collective actions on tax certainty, cooperation and digital transformation*, dated 29 March 2019.
2. http://www.oecd.org/tax/forum-on-tax-administration/publications-and-products/international-compliance-assurance-programme-pilot-handbook-2.0.pdf.

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