



Insights: Transfer Pricing

CRA Charles River
Associates
CELEBRATING 50 YEARS

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In this year-end edition of *Insights: Transfer Pricing*, we highlight industry recognition, the transfer pricing landscape, the work of our consultants, recent thought leadership, and speaking engagements.

Industry recognition

CRA's Transfer Pricing Practice was recognized by *Financial Monthly* as Transfer Pricing Firm of the Year–USA.

The 2015 Finance Monthly Tax Awards recognize individuals and firms who have excelled in their particular area of expertise in the past twelve months. More than 8,000 readers participated in the voting process this year.

The transfer pricing landscape

Recap of 2015

Three significant regulatory issues impacted the 2015 transfer pricing landscape for multinational companies: 1) Base Erosion and Profit Shifting (BEPS); 2) Country-by-Country (CbC) reporting; and 3) The *Altera* tax court case.

In collaboration with more than 80 developing countries and other non-OECD/non-G20 economies, the Organisation for Economic Co-operation and Development (OECD) reached a significant milestone in releasing the BEPS 2015 Final Reports. The BEPS project, which includes CbC reporting within its 15 action plans, serves as a guideline to tax authorities on how to ensure that profits are taxed appropriately according to where economic activity (and value) is generated. The OECD's BEPS Action Plan will certainly impact all multinationals, small and large. However, CbC reporting is currently impacting the largest companies.

The *Altera* case directly affects companies operating in the United States. In a decision favoring the taxpayer, the US Tax Court ruled against a 2003 cost sharing regulation, which required the sharing of stock-based compensation. As a result, the inclusion of stock options in qualified cost sharing

arrangements was ruled to be not arm's length under Section 482 regulations. Further, the *Altera* case may invalidate a portion of the US transfer pricing regulations. While the *Altera* case mostly impacts US-based multinationals with cost share structures, the case could significantly affect the way US transfer pricing regulations are written and enacted in the future.

Looking forward into 2016

In light of the BEPS 2015 Final Reports, countries around the world are creating new tax laws or amending existing laws to raise the minimum reporting standards and penalties for tax years beginning January 1, 2016. For instance, France, Mexico, and the Netherlands recently established criminal penalties (up to €100,000) for multinationals that fail to comply with new transfer pricing requirements. The BEPS project and CbC reporting create higher thresholds for documentation and compliance. As a result, we can anticipate many tax payers will struggle with the compliance process, which will involve preparing reports and data mining on a global scale.

Recently, we have seen more aggressive positions taken by tax authorities in countries that have well established transfer pricing laws. We expect this trend to continue into 2016. We will also likely see even more aggressive positions taken, as countries that did not previously have transfer pricing regulations, put in place new laws for transfer pricing. While countries are introducing new laws, changes to regulatory frameworks mostly deal with compliance and not new theory. Transfer pricing remains the same in that taxpayers have to defend the allocation of profit based on the functions, assets, and risks taken on by each entity in their organization. For the most part, new regulations require companies to disclose their global transfer pricing positions, whereas previously the focus was on the single-country under review.

One concern with tax authorities implementing stricter transfer pricing regulations is a lack of resources. It is unknown whether tax authorities have the bandwidth to support additional scrutiny of taxpayers' transfer pricing positions, and if not, how will they develop an educated audit group quickly enough without going to outside service providers for support? While new transfer pricing regulations come into effect in 2016, the real test will be in 2017, when regulatory filings will be reviewed by respective tax authorities.

Considerations for 2016

2016 is a good time for a comprehensive, open minded review of the transfer pricing policies of a multinational group. Ideally this entails a deep knowledge and understanding of the new OECD perspective and of the business and its strategic trends. Many companies are already BEPS compliant in theory, but may need to update how they document and defend their structure.

While significant tax dollars can be saved through efficient tax planning, complex transfer pricing structures can cost more money to implement and maintain than more simplistic ones. Companies should be just as concerned with the cost of any compliance work needed to prove intercompany payments are being made at arm's length. Documentation should thoroughly explain the global structure and be updated to ensure BEPS compliance with the new guidelines.

With the addition of CbC reporting, companies are being asked by tax authorities to increasingly provide greater transparency relating to their global operations. While some countries currently have annual transfer pricing reporting requirements and others do not, it is important to remember that a

company's entities are all interconnected. By periodically revisiting the entire transfer pricing structure, companies can ensure that they are consistent in their application of transfer pricing regulations across the enterprise as well as predict potential issues in an ever-changing political and economic landscape.

Our consulting work – A year in review

Our consultants help clients navigate every phase of implementing and supporting international tax structures including: IP/target planning, documentation, and audit defense. We also provide litigation support and expert testimony services in transfer pricing litigation. To follow are some highlights of projects from the past year.

Planning

Our consultants conducted over two dozen platform contribution transaction (PCT) valuations and implementations in industries including: biotechnology; medical devices; software; hardware; oilfield equipment and services; and financial services.

We worked with a developing nation in Southeast Asia to assist with the development and implementation of its tax audit process and procedures. Specifically, CRA's US transfer pricing team:

- Reviewed the then existing processes and procedures;
- Reviewed a sample of actual audits; and
- Recommended improvements and an implementation plan.

Audit defense

CRA's transfer pricing consultants have successfully defended IP valuations/migrations and international tax structures under audit by the IRS and tax authorities around the world. Some of our more notable work in this area last year includes:

- Assisting a client to navigate an IRS assessment of almost a half billion, which was more than twice the taxpayer's actual PCT valuation. CRA negotiated a final resolution that was less than a 20% increase in the PCT, and was also less than the taxpayer's reserve position.
- Assisting a client to negotiate with the IRS regarding a \$1 billion dollar acquisition. CRA's involvement spanned multiple years and concluded with an adjustment that was within the company's reserve position and represented less than 10% of the total value of the acquired company.
- Defending a Global Fortune 200 biotechnology company's international manufacturing value chain to the IRS. Currently, the IRS is proposing an adjustment of nearly \$200 million for the audit cycle.
- Successfully defending various companies throughout the world in: Italian tax court; and field audits in India, Israel, Malaysia, Mexico, Singapore, Sweden, and the US. All of the aforementioned defense work resulted in no adjustments for the clients.

Litigation consulting

CRA assisted counsel in North America and Europe to provide transfer pricing litigation consulting for the European units of a parent company involved in a bankruptcy matter. Our work included an expert report to quantify transfer pricing claims of approximately \$2 billion. We also issued a rebuttal report in the matter.

We also assisted counsel with valuation litigation consulting services in cases before US Federal District Court and US Tax Court. Specifically, our transfer pricing consultants issued an expert report quantifying the value of certain financial assets that were contributed to a trust; issued a rebuttal report critiquing the report of the expert representing the US government; and provided expert testimony.

Recent publications

Roundtable: Transfer Pricing

In the February 2016 issue of *Financier Worldwide*, [Rebel Curd](#) and other industry experts discuss some of the most significant developments in the transfer pricing arena over the past 12 months. The panelists also share their predictions for the future as transfer pricing regulations continue to evolve. To read the article, click [here](#).

Global tax reform emerging from BEPS Action Plan

According to the US Treasury Department, the Country-by-Country (CbC) Report template is expected to be very similar to what was released in the BEPS final package on October 5, 2015. It is anticipated that temporary regulations will be released to implement CbC Reports in the US for tax years beginning January 1, 2016. The announcement follows the pattern of international tax reforms (and proposals for reform) that have emerged around the world. To read more, click [here](#).

China adopts many BEPS proposals and introduces more stringent transfer pricing requirements

Since the Chinese State Administration of Taxation (SAT) released its first comprehensive TP regulation in early 2009, the SAT has aimed to protect China's revenue base by enforcing the arm's length principle for intercompany transactions. Following the September 17, 2015 release of the Organisation for Economic Co-operation and Development's base erosion and profit shifting (BEPS) Action Plan, the SAT issued a draft circular titled "The Discussion Draft on The Implementation Measures of Special Tax Adjustments." The SAT's proposals indicate that China will adopt certain guidelines from the BEPS 2015 Final Reports, with the intent to ensure companies are more transparent in information disclosure and analysis requirements. To read more, click [here](#).

BEPS: What lies within your country-by-country transfer pricing

Action 13 of the BEPS Action Plan contains the OECD's new guidance on a standardized three-tiered approach to transfer pricing documentation and introduces a requirement for large multinational enterprises (MNEs) to provide governments with information on their global allocation of income, economic activity, and taxes paid among countries according to a common template—the Country-by-Country (CbC) Report.

CRA has developed a proprietary diagnostic tool that uses CbC data to provide insight into a company's global transfer pricing position, based on BEPS concepts of value creation and risk alignment. To read more, click [here](#).

Proposal to introduce a US patent box regime

In this article published in the International Bureau of Fiscal Documentation's (IBFD) *International Transfer Pricing Journal*, [Sabera Choudhury](#) details the discussion draft of the Innovation Promotion Act of 2015 released by the US House Ways and Means Committee. This represents the first step by the United States to create a US patent box regime to encourage research and development in the US and counter the patent box regimes already in existence in other countries, such as Ireland, the Netherlands, and the United Kingdom. Only time will tell if a US patent box regime will be enacted and what its impact will be on the US and the global economy. To read more, click [here](#).

Speaking engagements

[Paul Wilmshurst](#) and [Gerben Weistra](#) spoke about "Transfer Pricing: Developing Opportunities" at an October 21, 2015 webinar hosted by BKR international EMEA and AsiaPac Regions. They discussed hot topics in transfer pricing such as base erosion and profit shifting (BEPS).

[Alberto Pluviano](#) spoke about the evolution of the transfer pricing rules for intangibles: the BEPS effect at a March 23, 2015 seminar organized by Confindustria (a leading business association in Italy), in Padova, Italy.

[Paul Wilmshurst](#) and [David Yurkerwich](#) spoke about "Valuation Across Jurisdictions and Contexts" at the 6th Global IP Exchange on March 9–11 in Munich, Germany. They discussed valuation across jurisdictions and contexts as well as differences between litigation, licensing and tax/transfer pricing; potential impacts of the EU Unitary Patent and Unified Court; global transactions and licensing by patent aggregators; and the new global taxation environment for corporates.

CRA also sponsored several industry conferences over the past year, including: the International Fiscal Association (IFA) USA 2015 Annual Conference on February 26–27 in Washington, DC; the Region VIII TEI Annual Tax Conference from June 15–18 in Santa Barbara, CA; and the 5th Annual NABE Transfer Pricing Symposium from July 21–23 in Washington, DC.

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