Answer-to-Question-_1_

Part 1:

As per the OECD Trnsafer pricing guideline, accurately delineating the transaction is one the imporatnt and starting point of undertaking Comparability analysis.

Following are the transactions between associated enterprises:

Company A:

1. Purchase of finished goods from Company C (possible this might not be a purchase transaction, depending on clarification of facts regarding contract manufacturing)

2.Interest free loan to Company B

3.Interest free loan to Company C

4.Interest free loan to Company D

5. Provision of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company B.

6.Provision of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company C.

7.Provision of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company D.

8.Grant Company C to contract manufature for the group.

9.Provide intellectual property to Company C.

10.Receipt of research and development services from Company C.

Company B:

1.Purchase of finished goods from Company C or Company A (this will depend upon clarification of facts regarding contract manufacturing)

2.Receipt of interest free loan from Compnay A.

3.Receipt of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company A.

Company C:

1.Sale of finished goods to Company A (This probably may not be a sales transaction depending upon facts on contract manufacturing)

2.Sale of finished goods to Company B or Company A (depending upon terms of contract manufacturing)

3.Sale of finished goods to Company D or Company A (depending upon terms of contract manufacturing)

4.Receipt of interest free loan from Company A.

5.Performing research and development activites for Company A.

6.Perform contract manufacturing for Company A.

7.Receipt of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company A.

8.Purcahse of raw material from Company A (this might be from third party but no clear facts are provided about procurement)

9.Receipt of intellectual proeperty from Company A.

Company D:

1.Purchase of finished goods from Company C or Company A (this will depend upon clarification of facts regarding contract manufacturing)

2.Receipt of interest free loan from Compnay A.

3.Receipt of management, administrative, information technology, accounting, taxation,, marketing assistance and technical assistance to Company A.

Part 2:

Transfer pricing methods are quite relevant in determination of an appropriate transfer price. OECD transfer pricing guideline 2.2, recommends that in transfer pricing analysis, parties are required to select the most appropriate method . In selecting most appropiate method parties should consider:
1. Strength and weakness of each methods
2.Appropriates of method in view of controlled transaction
3.Availability of comparable data
4.Degree of comparability between controlled and uncontrolled transaction.

OECD Tranfer pricing guideline (OECD TPG) recgnises 5 method. Below is discussion of each method and suitability of particluar method for associated transaction identified above.

Comparable uncontrolled price method (CUP method):

This method compares price charged for the property or services in a controlled transaction to the price charged in comparable uncontrolled transaction in comparable circumstances. If comparable uncontrolled transactin can be identified then CUP is usually the preferred method.It is the most direct and reliable way to apply arms length principle. Usefull for commodities and financial transaction.

A CUP method could potentially be applied in

1. Provision of routine services by Company A to COmpany B, C and D

2. Price charged by Company D for sale of Goods to Company A, B and D

3. Interest to be charged on Loan to Company B, C and D. This can be compared with interest rate generally charged by the banks for similar arrangement.

4.Grant of IP by Compnay A to Company C

Further, it is not clarified in the question if Company A will charge its subsidiaries a licensee fees for Intellecutal property, since independent enterprise may charge in a similar circumstance. So to determine licensee fee CUP method may be used.

Resale price method (RPM):

RPM begins with price charged for product that has been purchased form related party and resold to independet party. Resale price is then reduced by an appropriate gross margin on resale price representing the amount out of which reseller would seek to cover it selling expense and other opertaing expense and make an appropirate profit. What is left (after any adjustment if needed) will be considered as arm's lenght price for original transfer of property between associated entities

RPM can be used in following:

1.Purchse of finished goods by Company A from Company C, since Company will resell this good to third party

2.Purchse of finished goods by Company B from Company C, since Company will resell this good to third party

3.Purchse of finished goods by Company D from Company C, since Company will resell this good to third party

Resale margin of reseller in controlled transaction may be determined by refernce to the margin same reseller earns in uncontrolled transaction

Cost Plus method (CPM)

CPM method begins with cost incurred by the supplier in controlled trasancton and then a appropiate markup is then added to the cost, to make appropraite profit in light of functions performed and market condition. Usefule for servies , contract manufacturing and reserach and development activites.

Alternative to CUP, CPM may be used for the routine services provided by COmpany A to Company B, C and D.

CPM may be also be used research and development activites performed by Company C for COompany A, by applying a modest markup.

Similary, CPM may also be used for contract manufactring activiy provided by Company C.

Transaction Net margin method (TNMM):

TNMM examines net profit relative to an appropriate base like sale, cost,asset etc, from a controlled transaction. Advantage of TNMM is net profit indicator is less affected by difference in product characterstic and further is more tolerant to functional differeces between controlled and uncontrolled transaction.TNMM is one sided method.

Based on the facts, TNMM may be applied using Company A, B, C and D.They would be tested party and compared against appropraite comparable.

Transactional profit split method
Based on the facts of case it is unlikely that this method will be used.

In regards to routnie services rendered by Company A, consideration should also be given to Chapter VII of OECD TPG: SPecial consideration for intra-roup services. That is whether service has been rendered and is it low value adding services and whether charge is at arms length.

Part 3

Firstly it is mentioned that operaing profit margin of Company A is only 2% whereas operating marging of other companies provided in facts is between 10-20%. Tax administration of Company will likely object to lower profit margin of Company A in light of exetensive functions and risk assumed by Company A. Further Company A is the legal owner of group IP assuimg it is also the economic owner.

Futher, as per OECD TPG for rendering of low value intra group services minimum markup assumed is 5%. There may be risk that COmpany A is not appropriately compensated for group services.

Thirdly, another risk which appears is that Company A might not be compensated by assocaited entites for its intellectual property.

Lastly it is stated that Company is providing interest free loan to its subsidiaries. This arrangement may be questioned by the authority since it is unlikely that independet enterprises will provide interest free loans.

Considering the asset, employees and risk of Company A with its other associate entity it appears it is not appropriately compensated.

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Answer-to-Question-2

Part 1:
Functional analysis helps to identify economically significant acitivites and responsblites undertaken, asset used and risk assumed by the parties to the transaction.

Firstly, contractual terms of the transaction will have to be examined.

Another steps which might be taken is analysis of group organisation structure. Information available in public domain and also on companies website. Review of three tiered documentation that is master file, local file and CBCR. Conducting interview with a broad range of personnel and strategic level and at operational level. Further, if possible undertake interview of foreign associated personne. Industry knowledge of company is another important aspect. It is utmost important to understand supply chain of the group and business chain of the group.

Company A:

Functions:
1.Strategic development
2.Sales/ marketing
3.Inventory management
4.Demand planning
5.Distribution
6.Funding
7.Administrative services

Asset:
1.Inellectual property
2.Office building
3.Furniture
4.MOtoe vehicle
5.Staff
6.Warehouse

Risk:
1.Inventory risk

2.Market risk
3.Financing risk
4.credit risk
5.Manufacturing risk (depending upon contarct with Company C)
6.Warranty risk
7.Intellectual property risk
8.Capital investment risk

Company B:
Functions:
1.Sales/marketing
2.Procurement
3.Demand planning

Asset:
1.Staff
2.Motor vehicle

Risk:
1.Market risk
2.Warranty risk

Company C:
Functions:
1.Sales/marketing
2.Procurement
3.Demand planning
4.Contract manufacturing
5.Research and development
6.Logistic

Asset:
1.Staff
2.Plant and equiment

Risk:
1.Market risk
2.Warranty risk
3.Research and development risk
4.Manufactring risk (depending upon contract with COmpany A)
5.Inventory risk (depending upon contract with COmpany A)

Company D:
Functions:
1.Sales/marketing
2.Procurement
3.Demand planning

Asset:
1.Staff
2.Office (Rented)

Risk:
1.Market risk
2.Warranty risk

Part 2:
ENtity charaterisation depends upon the fucntions ,asset and risk assumed by each of the entity.

Company A: Company is legal owner of IP and other know how. It renders high value consulting service to subsidiaries.

It will be characterized as a Enterprenuer and owner of IP.
Head office functions with provision of high value services.

Company B: It only undertake sales and marketing acitvites.

It will be characterised as limited risk ditributor.

Company C: It undertakes contract manufacturing. It also provide reserach and development activites. Further it undertaked sales and marketing acitvity.

It will be characterised as Contract manufacturer. Research and development provider. And limited risk distributor.

Company D:It only undertake sales acitvites.

It will be characterised as limired risk dtributor.

Part 3:

Comparability analysis is at the heart of the Arm's lenght principle.It provided for comparaison of controlled and unctrolled transactions. COmparability analysis helps in identifying commercial or financial relation between associated entities so that transaction is accurately delineated

Further, Artcile 9 is the foundation of comparability analyses.

Similar to Transfer pricing method. Comparability analysis aims at finding most reliable comparable. General guidance can be found in section D Chapter 1 of OECD TPG that is:
1.Contractual term
2.Functional analysis
3.Charchterstic of property or services
4.Economic circumstances
5.Business strategy.

Comparability analysis does not end at the search of comparable but is linked to each and every step of transfer pricing analysis. OCED decribes steps to a comparability analysis, which is not the compulsory and may be relied upon. The process is as follows:

1.Determins number of years to be covered
2.Analyses taxpayes circumstances
3.Define the controlled transaction, select tested party
4.Review internal comparable
5.Identify and assess avaible external comparable
6.Select most appropraite transfer pricing method
7.Identify potential comparable
8.make comparabilty adjustment
9.Interpret and use data collected in determinind Transfer price.

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Answer-to-Question-3

Part 1:
HH Head co (Coutry A)

Pre-structure:

1.Full fledged manufacturer with legal and economic ownership of intellectual property (IP) and research and development funciton.

2.Functions:
Manufacturing
Inventory management
Distribution
Research and development
Procurement
Grant of technical services

2.Asset
Plant and machinery
Staff
Invetory
Intellectual property
Working capital

3.Risk: Mananges and controls all the risk

Post restrutring:
1.Act as distributor since IP is transferred and grants contract manufacturing to HH Sub 3.

2.Function
Grant contract manufacture to HH Sub 3
gant of contract manufacturing to HH Sub 3
Procurement- Assuing HH head co undertaked procurement for HH Sub 3'
Sales/marketing

Asset:
All of above except plant and machinery and IP

Risk:All risk execept for IP and research and development activity like:
Inventory risk
Market risk
Credit risk
Finance risk
Warranty risk only for sale by itslef and not of HHSub 1

HH Sub 1

Pre- restruring:

1.Limited risk distributor and after sale service provider

2.Functions:
Procurement
Marketing
After sales services and traning

3.Asset
Warehouse
Staff

4.Risk
Market risk

Post restruring
NO change execpt warranty risk will be borne by HH Sub 3

HH Sub 2.

1.Distributor

2.Functions:
Procurement
Marketing
After sales services and training

3.Asset
Warehouse
Staff

4.Risk
Market risk
Warranty risk

Post restruring

NO change

HH Sub 3.:

Pre restruring

NOt in existence

Post restructring

1.Full fledged or contract manufacturer

2.Funtions
COntract manufacturing
Research and development activity
New product development

3.Asset
Plant and equipment
staff (transferred from HH Headco)
warehouse

4. Risk
Research and development risk
Warranty risk

HH Sub 4.
Post resctruring:
1. Owner of group IP

2.Functions:
Strategic decision

3.Asset
Intellectual property

Staff (transferred from HH Headco)

4.ALl IP risk

Post restruring all the entitiey that us HH Head co, HH SUb 1, HH Sub 2 and HH Sub 3 will pay royalty to HH Sub 4.

Part 3.

This is the case of business restruring . Therefore refernce is made to OECD TPG CHapter IX- Transfer pricing aspect of business restructuring.As per the OECD TPG in case of restructuring consideration should be given to changes to function, asset and risk of the entities examing pre and post restructuring arrangment to identify arm's length nature of overall restructing and individual transaction between associated enterprises.

Two important aspect to be determined is Arm's lenght compensation for the restruring itself and remunertaion post-restrucrting.

Accordingly, most important aspect will be Arm's lenght compensation to HH Head co for tranfer of intangible.

In this connection, regards need to be given to following:
1.Has there been a legal and economic transfer of intellectual property;

2.Which entity are involved in development, maintenance, enhancement, protection and exploitation of intangible functions and has there been any change econimcally?

3.Has there been Arm's lenght compensation for tranfer of asset and risk.

4. What are the contractual terms of parties

5.Arm's length nature of royalty paid

6.Valuation issue regaring intellecual property

7.Actual conduct of parties

8.Legal form of transaction relative to the economic reality of transaction

Another, crtical aspect will be Arm's lenght price for transfer of employees from HH Headco.

Following is the summary of critical aspect will be:

1.ALP for transfer of IP, who is the legal and who is economic owner

2.ALP of royalty paid to HH SUb 4

3.ALP for transfer of Staff

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Answer-to-Question-6

Part 1:

SAfe harbour is the provision that applies to defined category of taxpayer or transaction and it relievs eleigible taxpayer from certain TP obligation.

Benefit:
1.Simplifies compliance
2.COst reduction to tax payer
3.Certainity to taxpayer that price will not be challenged by tax administration
4.Permit tax administration to redirect resources from lower risk transactiion.

Risk:
1.It may lead to reporting of non arms length price for some taxable income
2.Increase risk of double taxation
3.Open avenue for inappropriate tax planning
4.May raise concern of tax equity

Part 2: Simultaneous tax examination are defined in OECD model agreement for udertaking of Simultaneous tax examination as an arrangement between two or more parties to examine simultaneous and independently each of its own terrioty, the tax affairs of taxpayer which have common or related interest.

Simultaneous tax examination aims at information exchange between state
hence legal authorities for it are:

1.Article 26 of OECD MTC
2.Article 12 Nordic convention on Mutual assitance in tax matters
3.Article 8, Convention on Mutual Administrative Assitance in tax matters.

Part 3:

These are the intragroup services which :

1.Are supportive in nature
2.Are not part of core business of MNE group
3.do not use or create unique and valuable intagibles
4.do not involce or give rise to assumption, control or creation of significant risk.

BEPS Action plan 8-10 resulted in elective simplified tranfer pricing approach for low value adding intra-group services. Simplified approach requires that cost for low value adding intra group services should be allocated to group that receives service with an required markup of 5%.
Simplified approach reduces compliance cost of meeting benefit test and arm's lenght principle. Further, it will provide certainity to MNE group.Steps are defined to undertake simplified approach.

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Answer-to-Question-9

Part 2:

Advance pricing arrangement (APA) is a arrangement between tax authoirty and MNE , requiring tax authorities to accpet a transfer price for future transaction of associated enterprises of the MNE. APA is highly effective dispute avoidance techniques. To avoid huge cost and time on transfer pricing litigation MNE may prefer to undertake APA which will provide certainity to them, untill the facts and assuptions and transaction defined in

APA does not change, transfer price for transaction covered under APA will not be questioned by tax authorities.

There are 3 types of APA
Unilateral
Bilatreal
Multilateral

Amongst the above, most coslty is Multilateral APA, then bilateral and then unilateral.

Bilateral and multilateral APA will subsutantially reduce risk of double taxation for MNE.

Whether MNE should enter into APA will depend on a number of factors:
1.Whether tax administration have APA
2.Risk appetite of MNE
3.Materiallty and complexity of transaction
4.whether safe harbour rule apply in countries
5.whether other country has tax treaty

Part 3:

Cost contractual arrangement (CCA) is an contractual arrangement among business enterprises to share contribution and risk in joint development, production or obtaining of intangible, tangible asset or services with understanding that such intangible, tangible asset and services are expected to create benefit for each participants.

Transfer Pricing focus is the commercial or financial relations between the particpants and the contributions made by the partcipats that create opportunites to achieve this outcome.

There are two types of CCA : DEvelopment and SErivce CCA.

Arm's lenght principle focuses that part or all compensation intended by the partcipants is exepcted mutual and proportionate to benfit to be derived from CCA.