Transfer Pricing Associates

Transfer Pricing Handbook for the Oil & Gas Industry

August 2012

Your bridge to worldwide transfer pricing services

TPA Global

Purpose

MNE is looking to gain practical insights into transfer pricing theory and practice in an effort to create a transfer pricing function in its organization and create a sustainable transfer pricing system.

Scope

- TPA will explain the transfer pricing principles, OECD and European approaches in dealing with transfer pricing.
- TPA will share its experience in the oil & gas sector and provide generic case studies on various transactions.
- TPA will describe its approach to transfer pricing process and provide guidelines how to deal with TP processes and manage TP risks within the organization.

Transfer Pricing Associates

Regulatory Transfer Pricing Framework

Your bridge to worldwide transfer pricing services

TPA Global

- Introduction - the Organisation for Economic Co-operation and Development
- The OECD TP Guidelines
  - Technical introduction
  - TP methods
  - Global TP risk management
- Introduction – the EU Joint Transfer Pricing Forum

- The OECD was established in 1961, headquartered in Paris.

- The OECD has groups 34 member countries committed to democratic government and the market economy. It provides a forum where governments can compare and exchange policy experiences, identify good practices and promote decisions and recommendations to produce better policies for better lives.

- Decision-making power is vested in the OECD Council, which is made up of one representative per member country, plus a representative of the European Commission.

- There are about 250 committees, working groups and expert groups in total. Some 40,000 senior officials from national administrations go to OECD committee meetings each year to request, review and contribute to work undertaken by the OECD Secretariat.

- The work mandated by the Council is carried out by the OECD Secretariat. The Secretariat in Paris is made up of some 2 500 staff who support the activities of committees, and carry out the work in response to priorities decided by the OECD Council.

The OECD Transfer Pricing Guidelines provide guidance to multinational enterprises and governments to apply the arm's length principle.

Under the arm's length principle, the conditions of transactions between associated enterprises (e.g. members of a multinational enterprise) should not differ, for tax purposes, from the conditions that would have been agreed by independent parties in comparable circumstances.

- Revision of the Special Considerations for Intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and Related Provisions, Discussion Draft – June 2012
- Dealing Effectively with the Challenges of Transfer Pricing – January 2012
- Transfer pricing and intangibles: scope of the OECD project – January 2011
- OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations – July 2010
- 2010 Report on the Attribution of Profits to Permanent Establishments – July 2010
- The 2010 update to the Model Tax Convention – July 2010
- CFA response to Comments Received on the September 2009 Draft Revised Chapters I-III TPG (English)
- The 2008 update to the OECD Model Tax Convention – July 2008
- OECD Benchmark Definition of Foreign Direct Investment 2008*: Fourth Edition*
- Manual on Effective Mutual Agreement Procedures (MEMAP) - 2007
- E-commerce: Transfer Pricing and Business Profits Taxation – May 2005
- Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2001: Travel version – January 2011
- Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations - Binder+1999 Update – November 1999
- Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations - July 1995
- Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, Discussion Draft - July 1994
- Employee Stock Option Plans: Impact on Transfer Pricing - 1994
- Transfer Pricing and Multinational Enterprises: Three Taxation Issues - Oct 1984
- Transfer Pricing and Multinational Enterprises – June 1979

Associated enterprises

Two enterprises are associated enterprises with respect to each other if one of the enterprises meets the conditions of Article 9, sub-paragraphs 1a) or 1b) of the OECD Model Tax Convention with respect to the other enterprise.

Arm's length principle

The international standard that OECD member countries have agreed should be used for determining transfer prices for tax purposes. It is set forth in Article 9 of the OECD Model Tax Convention as follows: where "conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly".

Comparability analysis

A comparison of a controlled transaction with an uncontrolled transaction or transactions. Controlled and uncontrolled transactions are comparable if none of the differences between the transactions could materially affect the factor being examined in the methodology (e.g. price or margin), or if reasonably accurate adjustments can be made to eliminate the material effects of any such differences.

Business restructuring

Business restructuring is defined as the cross-border redeployment by a multinational enterprise of functions, assets and/or risks. A business restructuring may involve cross-border transfers of valuable intangibles, although this is not always the case. It may also or alternatively involve the termination or substantial renegotiation of existing arrangements.

Source: the OECD Transfer Pricing Guidelines 2010

Comparable Uncontrolled Price		
Cost Plus		**Traditional transaction methods**
Resale Price		
Transactional Net Margin Method		**Transactional profit method**
Profit Split		

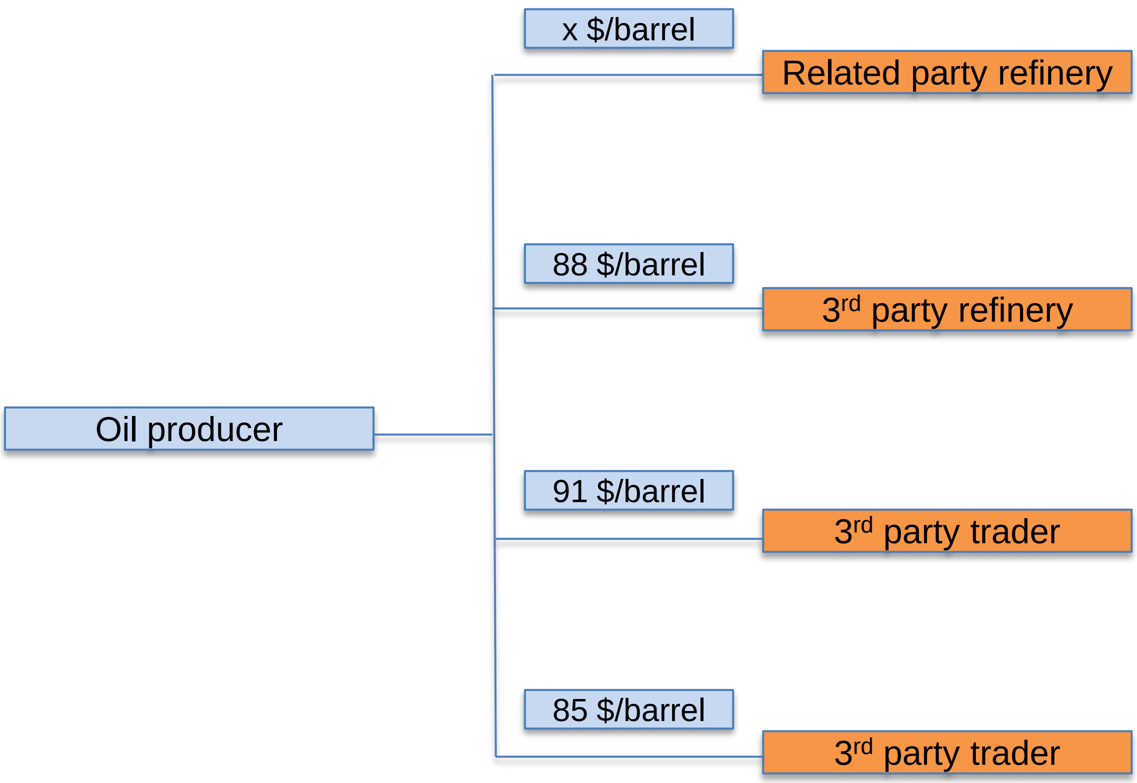
Where a traditional transaction method and a transactional profit method can be applied in an equally reliable manner, the traditional transaction method is preferable to the transactional profit method. Moreover, where the comparable uncontrolled price method (CUP) and another transfer pricing method can be applied in an equally reliable manner, the CUP method is to be preferred.

Source: the OECD Transfer Pricing Guidelines 2010

Comparable Uncontrolled Price

A transfer pricing method that compares the price for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances.

Source: the OECD Transfer Pricing Guidelines 2010



Assuming exact comparable transactions, arm's length range for x is

from 85 to 91

The OECD TP Guidelines | Transfer Pricing Methods (3)

Cost Plus

A transfer pricing method using the costs incurred by the supplier of property (or services) in a controlled transaction. An appropriate cost plus mark up is added to this cost, to make an appropriate profit in light of the functions performed (taking into account assets used and risks assumed) and the market conditions. What is arrived at after adding the cost plus mark up to the above costs may be regarded as an arm’s length price of the original controlled transaction.

Source: the OECD Transfer Pricing Guidelines 2010

Direct costs of processing plus a mark-up

Manufacturing services → Service recipient

Cost Plus mark-up will depend on the value add of the service provider. The more functions the manufacturer performs, the more risks it bears and the more assets it uses in provision of the service the higher mark-up should be allocated for the manufacturer.

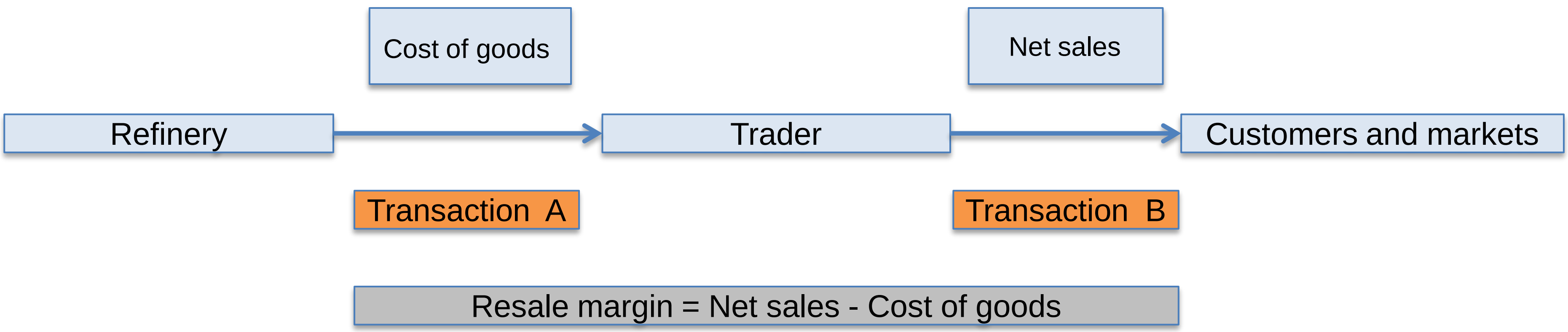
In comparison to CUP method, Cost Plus method focuses more on **functional comparability** rather than on product comparability.

The analysis has to be performed on the **gross level** of profitability.

Resale Price

A transfer pricing method based on the price at which a product that has been purchased from an associated enterprise is resold to an independent enterprise. The resale price is reduced by the resale price margin. What is left after subtracting the resale price margin can be regarded, after adjustment for other costs associated with the purchase of the product (e.g. custom duties), as an arm's length price of the original transfer of property between the associated enterprises.

Source: the OECD Transfer Pricing Guidelines 2010



Similarly to Cost Plus method **functionality** is the key determinant of the resale margin in Resale Price method.

The analysis has to be performed on the **gross level** of profitability.

Transactional Net Margin Method (TNMM)

A transactional profit method that examines the net profit margin relative to an appropriate base (e.g. costs, sales, assets) that a taxpayer realises from a controlled transaction.

Source: the OECD Transfer Pricing Guidelines 2010

TNMM is applied similarly to Cost Plus or Resale Price methods. The analysis has to be performed on the net level of profitability with a wide range of profit level indicators, e.g., net (operating) margin, net mark-up on total costs, return on assets, return on investment, etc.

TNMM is the **most widely used** method in European transfer pricing structures.

Profit Split

A transactional profit method that identifies the combined profit to be split for the associated enterprises from a controlled transaction (or controlled transactions that it is appropriate to aggregate under the principles of Chapter III) and then splits those profits between the associated enterprises based upon an economically valid basis that approximates the division of profits that would have been anticipated and reflected in an agreement made at arm's length.

Source: the OECD Transfer Pricing Guidelines 2010

The transactional profit split method is that it can offer a solution for highly integrated operations for which a one-sided or where both parties to a transaction make unique and valuable contributions (e.g. contribute unique intangibles) to the transaction.

Two approaches to apply Profit Split method – contribution analysis and residual analysis. There approaches are not necessarily exhaustive or mutually exclusive.

Contribution analysis

The combined profits, which are the total profits from the controlled transactions under examination, would be divided between the associated enterprises based upon a reasonable approximation of the division of profits that independent enterprises would have expected to realize from engaging in comparable transactions.

Residual analysis

Residual analysis divides the combined profits from the transactions in two stages.

First stage
Each party is allocated a remuneration for its non-unique contributions

Second stage
Any residual profit (or loss) remaining after the first stage division would be allocated among the parties based on an analysis of the facts and circumstances.

- The EUJTPF is an expert group, created by the European Commission in 2002 in order to reduce the high compliance costs and to avoid (or facilitate the elimination of) double taxation that easily arises in the case of cross-border inter-group transactions

- EUJTPF is not a permanent body, its mandate was renewed for the first time in 2006, for a further period of four years, by a decision of the European Commission of December 22, 2006. On January 25, 2011, the Commission again renewed the mandate, this time until March 2015.

- The renewed EUJTPF still consists of representatives of the 27 EU Member States and 16 representatives of the private sector.

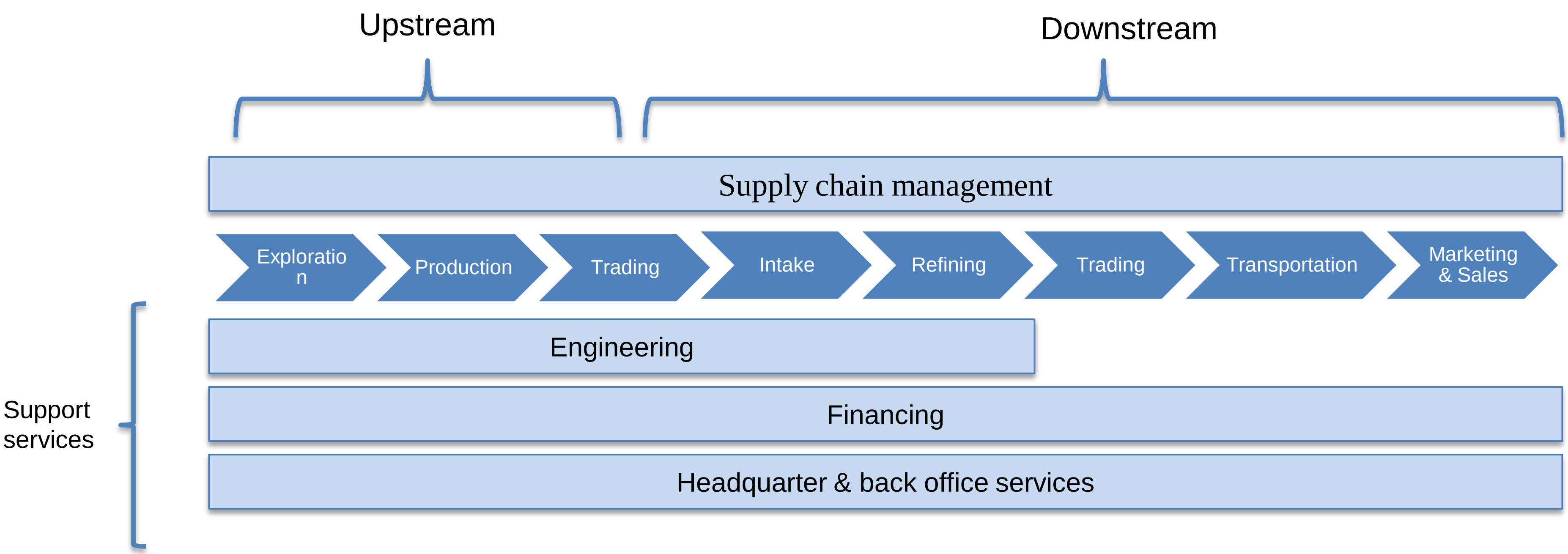
- The EUJTPF examines the practical problems related to the application of the tax rules on transfer pricing in the Internal Market and more in particular those related to the implementation of the Arbitration Convention.

- The EUJTPF works within the framework of the OECD Transfer Pricing Guidelines and operates on the basis of consensus to produce pragmatic, non-legislative solutions to practical problems posed by transfer pricing practices in the EU.

- Monitoring ongoing items.
- Completing reports on improvements to the EU Arbitration Convention and intra-group services
- Dealing with issues on small and medium enterprises and cost contribution arrangements
- Review of alternative dispute resolution and risk assessment
- Review of impact of the recent revisions to Article 7 of the OECD Model Tax Convention, compensating adjustments and secondary adjustments.
- Organizing consultation on "Double tax Conventions and the internal market: factual examples of double taxation cases"

- Report on small and medium enterprises and transfer pricing - February 2011
- Communication from the commission to the European parliament, the council and the European economic and social committee on the work of the EUJTPF in the period April 2009 to June 2010 and related proposals 1. Guidelines on low value adding intra-group services and 2. Potential approaches to non-EU triangular cases.
- Guidelines on low value adding intra-group services – February 2010
- Report prepared by the EUJTPF accompanying document to the communication from the commission to the council, the European parliament and the European economic and social committee on the work of the EUJTPF in the field of dispute avoidance and resolution procedures and on Guidelines for Advance Pricing Agreements within the EU – February 2007
- Communication from the commission to the council, the European parliament and the European economic and social committee on the work of the EU Joint Transfer Pricing Forum in the field of dispute avoidance and resolution procedures and on Guidelines for Advance Pricing Agreements within the EU – February 2007
- Code of conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises – June 2006
- Code of Conduct on transfer pricing documentation for associated enterprises in the EU – June 2006

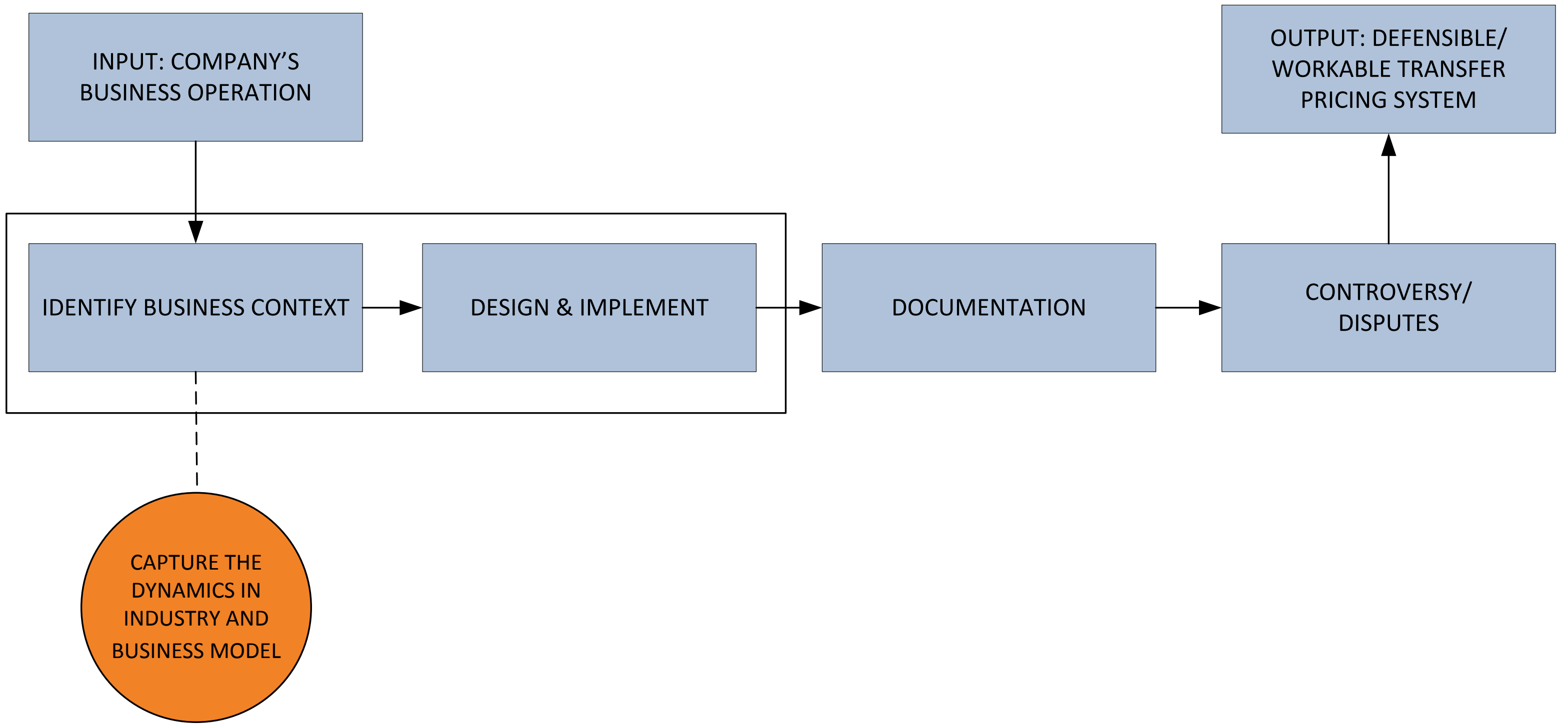
Oil & Gas Value Chain | Business Restructuring and “Crown Jewels”


Upstream
Downstream
Supply chain management
Exploratio
n
Production
Trading
Intake
Refining
Trading
Transportation
Marketing
& Sales
Support
services
Engineering
Financing
Headquarter & back office services

- **Exploration**
  - Funding the investment (and associated risk) and the rights to access any losses
  - Extraction rights / licenses: ownership and relationship with rights to profit
  - Financial and performance guarantees including obligations to “put land right”, insurance costs and indemnities
  - Access to engineering expertise and technologies. Use of centralized service centres, people, technology & expertise and equipment
  - Centralized services such as procurement and other support services
- **Production**
  - Funding issues
  - Relationship with oilfield services companies
  - Management and design of production infrastructure
  - Ownership / leasing of equipment
  - Design (R&D) and manufacture of equipment / royalties / leasing / service fees (people, technology, equipment)
  - Support services
  - Insurances and indemnities, attribution of liabilities and risk
- **Intake**
  - Design and ownership of facilities and infrastructure
  - Investment in relation to same and rights to reward
  - Ownership and management of logistics aspects and relationships
  - Characterization of activity and attributable value
  - Support services

- **Refining**
  - R&D and IP ownership in relation to refining processes and protocols etc.
  - Plant property and equipment – design, investment / funding, ownership, characterization
  - Characterization of refining activities (tolling, contract processor, risk-bearing processing)
  - Support services
- **Trading**
  - Characterization – fully fledged marketer, limited risk sales functions, commission agent, commissionaire
  - Funding
  - Support services
- **Transportation**
  - Logistics – ownership of relationships
  - Infrastructure – ownership of assets and right to remuneration: pipelines that cross borders
  - Functional profile and therefore reward structure
- **Marketing & sales**
  - Margin for retail activities of petroleum products

The Transfer Pricing Process developed by Transfer Pricing Associates is all about treating transfer pricing as a business process. The steps in this process are illustrated in the following diagram:



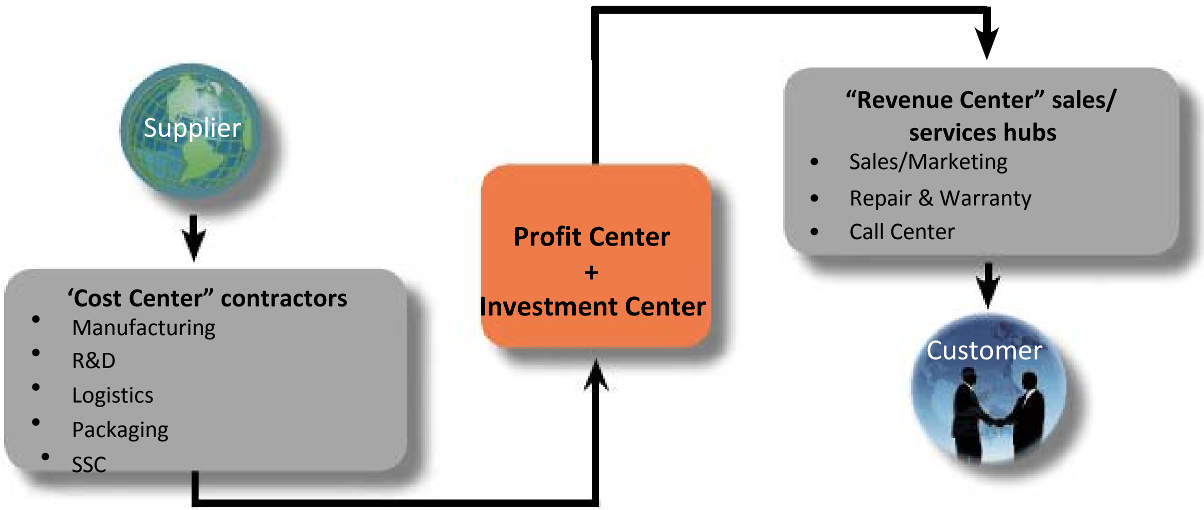
Addressing the following key issues:

1. How to identify the relevant business context
2. How to design an appropriate transfer pricing system and arrange for proper implementation
3. How to document the transfer pricing system
4. How to manage (pre-) controversy of the transfer pricing system

Matching OECD, managerial and legal labels

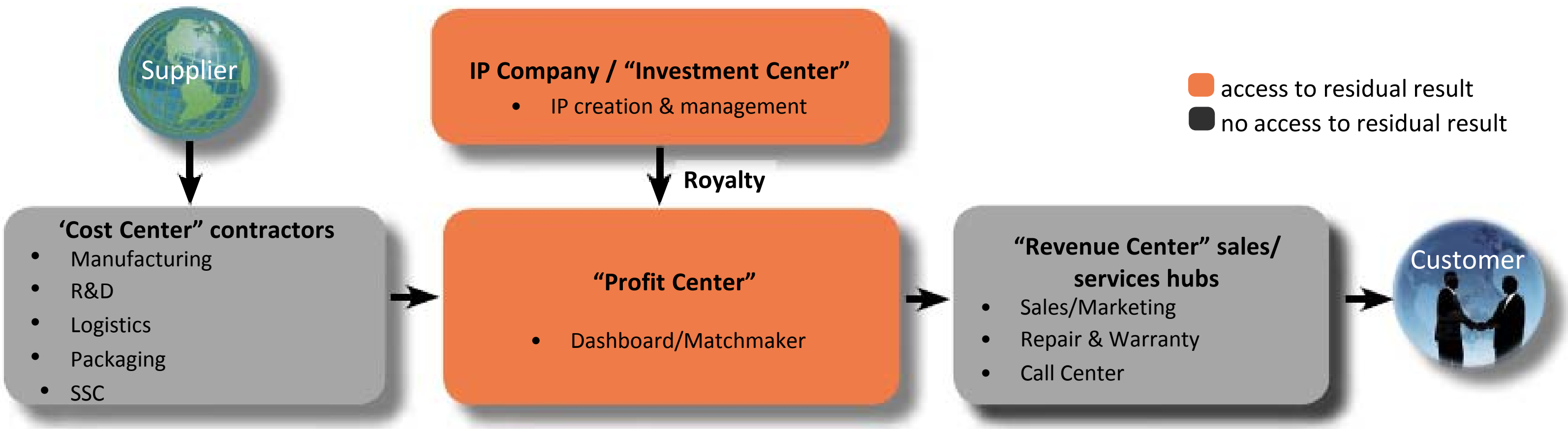
- The following table links the labels used when looking at transfer pricing from a tax, management accounting and legal perspective:

OECD labels	Managerial labels	Legal labels
CUP	Expense/cost/revenue centre	Services agreement
Resale price	Revenue/profit centre	Distribution agreement
Cost-plus	Expense/cost centre	Research and development agreement
Profit split	Profit/investment centre	Sales and marketing agreement
TNMM	Revenue/profit centre	Commission agent agreement



Addressing the following key issues:

1. What labels are used to address intangibles?
2. How do you recognize intangibles?
3. How to determine ownership of intangibles?
4. How to price/value any transfer of intangibles?



Product related intangibles	Process related intangibles	Market and Marketing intangibles	Hybrids
• Patent • Invention • Pattern • Methods • Copyright • Design / Model • Formulae/Recipes • Software • Literary, musical, or artistic composition / film • Technical data / documentation • Prescription drug files • Library • Natural resources • Database • Permit • Regulatory license e.g. from central bank • Trade secrets	• Know-how • Software • Method • Procedure • System • Supplier relationships • Procedural manuals • Technical data / documentation • Training manuals • Managerial skills and core competencies • Airport gates and slots • Financial instruments • Embedded work force • Supply chain intelligence	• Logo • Trade mark • Trade name • Brand • Campaign • Survey • Customer list • Import quota • Customer relationships • Distribution network & agreements • Retail shelf space • Subscription lists • Publications/thought leadership • Reputation • Book of business	• Franchise • Permit / right / license (air, water, land, drilling, emission, broadcasting) • Domain name • Unique location

Source: TPA's representation to OECD on intangibles project

MNE intangible assets:

- R&D pipeline
- rights to inventions, industrial prototypes and utility model
- rights to computer programs and database
- rights to trademarks and service marks
- protected results of intellectual activities and individualization means
- exploration, production and other licenses
- Staff (soft intangibles)
- Know how (soft intangibles)
- Managerial expertise (soft intangibles)
- Supply and offtake contracts (soft intangibles)
- Trading expertise (soft intangibles)
- Other...

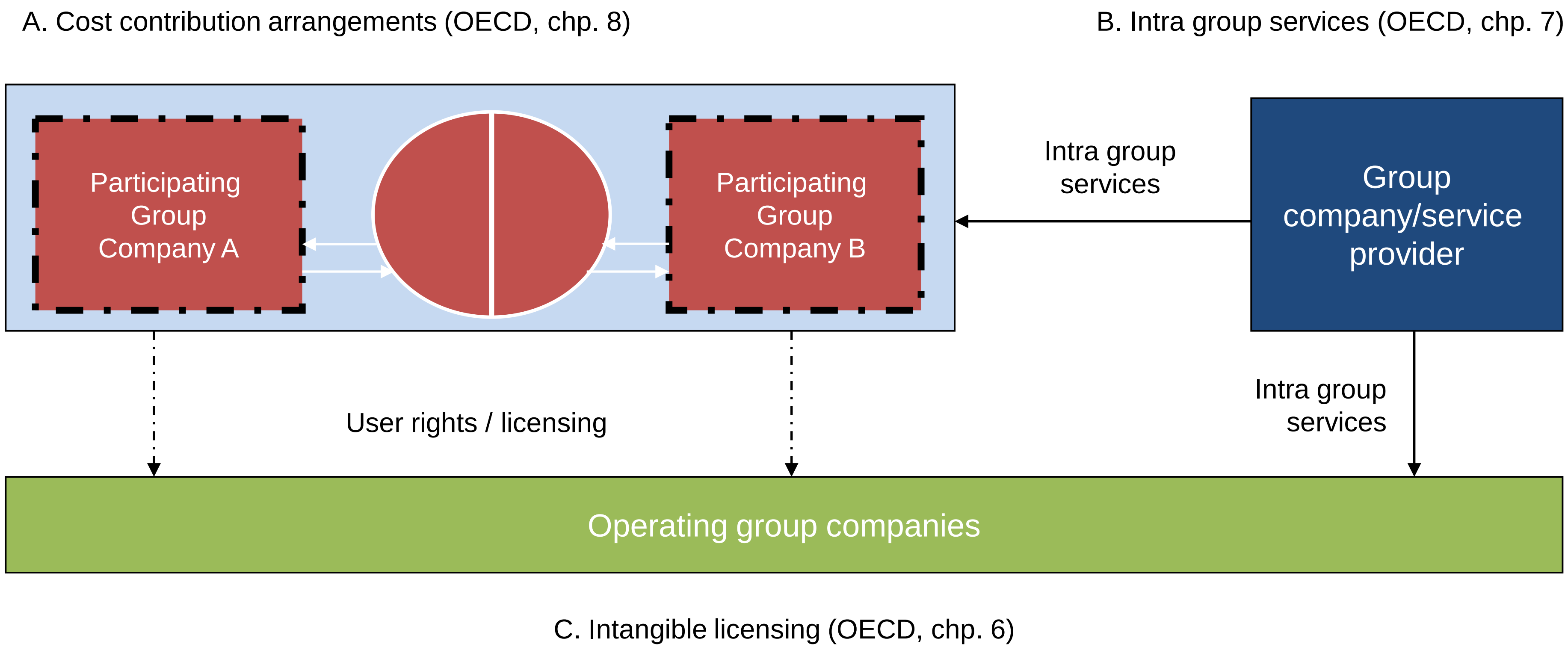
Through determining a policy for single versus shared ownership
Example: product intangibles

		R&D Cost	
		Centralized	**Decentralized**
R&D activities	**Centralized**	Sole owner	Cost contribution /cost sharing
	Decentralized	Sole owner + contract R&D	Cost Contribution /cost sharing

Addressing the following key issues:

1. How do you protect your product and process intangibles?
2. What single versus multiple ownership definition do you use?
3. What type of intercompany agreements are in place for R&D activities?
4. How do you deal with geographies transfers of R&D activities?

Relationship between cost contribution, intra group services and intangible licensing



Relationship between cost contribution, intra group services, and intangible licensing (continued)

Transfer pricing focus

A. Cost contribution	B. Intragroup services	C. Intangible licensing
• Cost definition • Allocation keys ‘cost/benefits’ • Buy-in/out valuation • Qualifying member	• Cost definition • (no) mark up • Allocation keys ‘cost’ • Benefit test	• Ownership / entitlement • Lump sum / royalty • Valuation / benchmarking

Other

• Central bank approval • Withholding taxes	• Bundling / unbundling • VAT implications • Joint ventures

Through defining do's and dont's	
Do's	Dont's
Identify key decision makers	Minimize key decision makers
Sufficient physical presence, 'Home base'	Make binding decisions abroad unless proper authorization procedure
Payroll	Split payroll if not consistent with physical presence
On site decision making	Minimize physical presence of key personnel
	Be inconsistent with own policies
Through appropriate audit trails (paper and digital)	
Decision making policy	Minutes of meetings/agenda's
Individual decision making	Negotiations
Agreements	Phone bills
Authority /responsibilities	Travel document
Pricing policy	Digital agenda
Activity	

Addressing the following key issues:

1. How to ensure a critical mass of key decision makers to geographically anchor IP ownership?
2. How can IT support or undermine your case?
3. How to deal with modern ways of communications and commuting?
4. How to manage behavioral aspects?

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Transfer Pricing Aspects of Possible Intercompany Transactions in MNE Group

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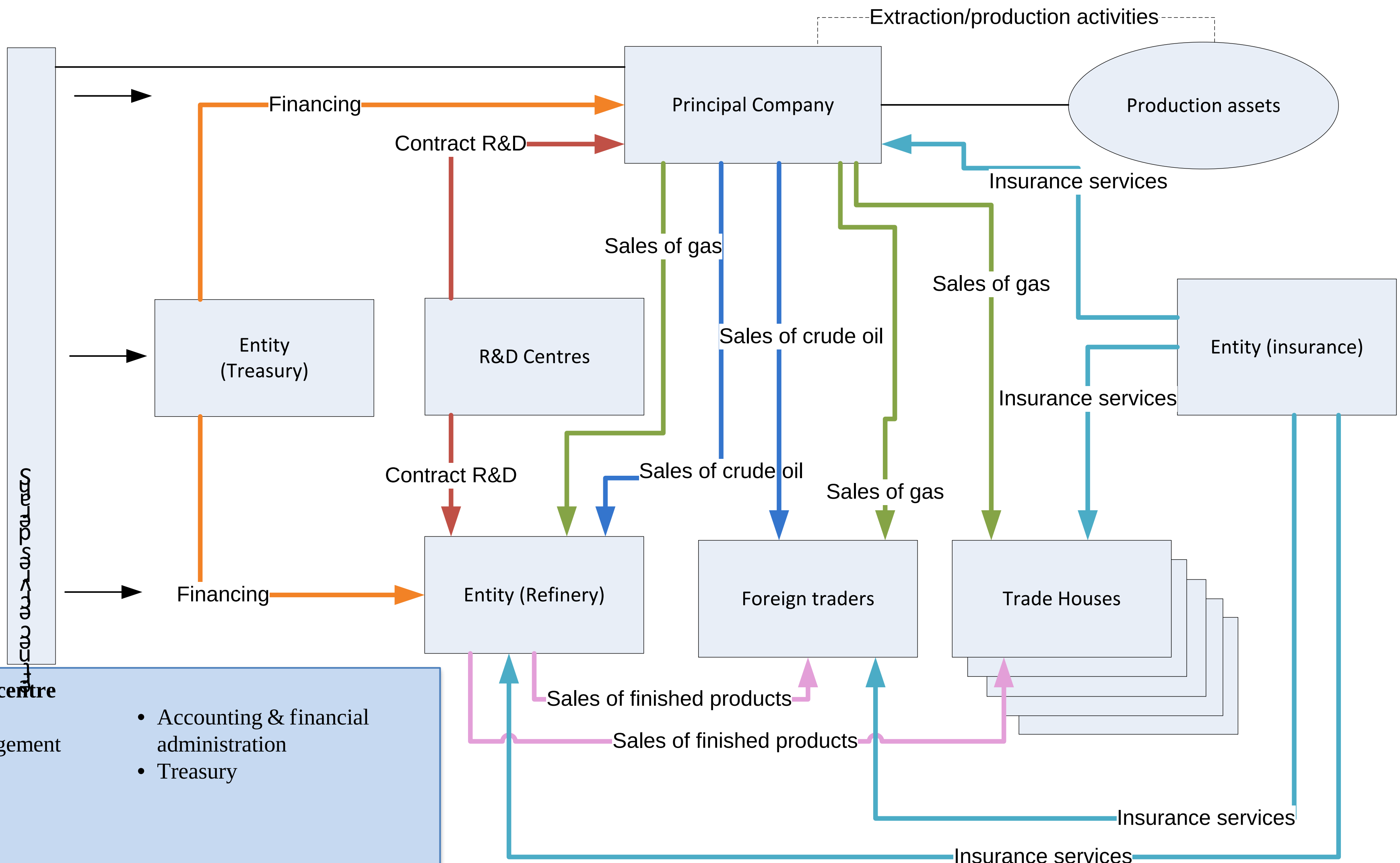
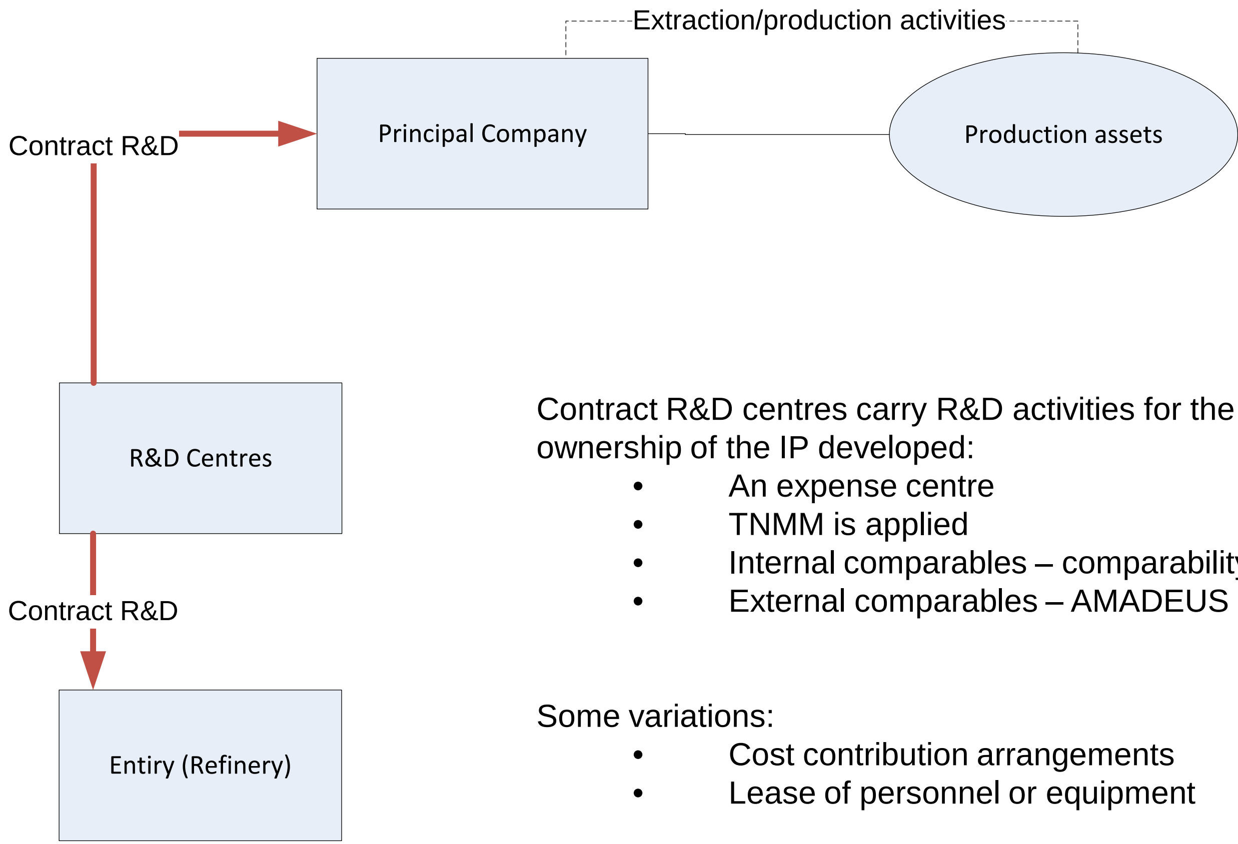
- Transfer pricing aspects of possible i/c transaction in MNE Group
- Engineering
    - Contract R&D Services
    - Rental of Professional Staff
    - Rental of Equipment
- Oil and gas extraction
- Refining
    - Transformation of refinery activities into contract refinery (conversion issues)
- Trading
- Headquarter and Support Services
    - Shared Service Centre
    - Cost Base Charges
- Captive insurance
- Financing
    - GE Capital Landmark TP case

Transfer pricing aspects of possible i/c transaction in MNE Group



Shared service centre services:

- General management
- IT
- HR
- Legal
- Marketing
- Accounting & financial administration
- Treasury

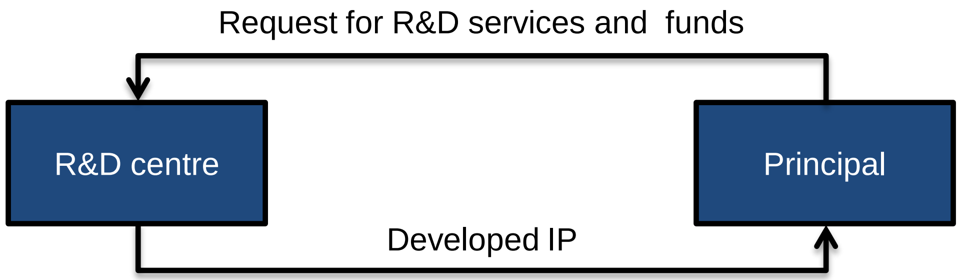


Contract R&D centres carry R&D activities for the benefit of principal who takes ownership of the IP developed:

- An expense centre
- TNMM is applied
- Internal comparables – comparability adjustments
- External comparables – AMADEUS or other database

Some variations:

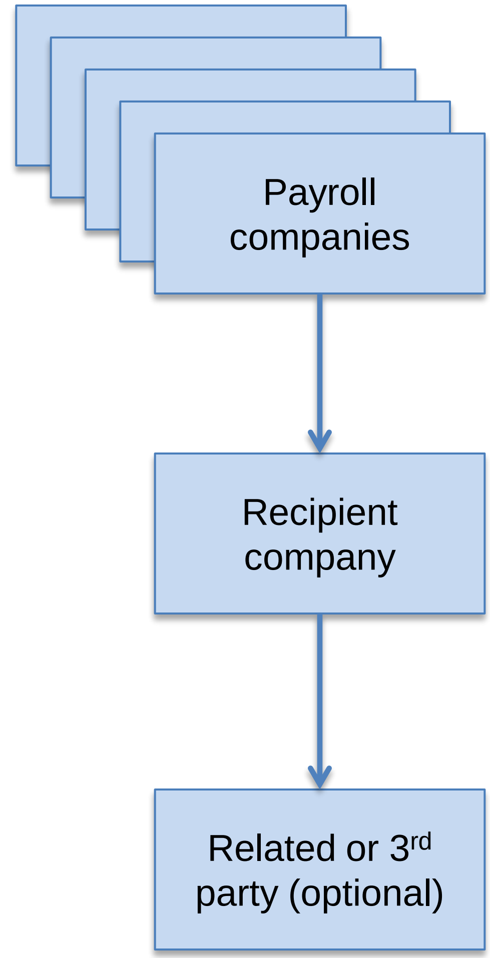
- Cost contribution arrangements
- Lease of personnel or equipment



	R&D centre (cost centre)	Principal (investment / profit centre)
Functions		
Formulation of a problem / concept		√
Planning and budgeting	√	
Providing initial information / material		√
Research and development	√	
Reporting	√	
Quality assurance	√	
Risks		
Project failure risk		√
Credit risk	√	
Cost control and poor budgeting	√	
Currency risk	√	√
Assets		
Intangible assets		√
Tangible assets	√	

In principle two different models for rental of professional staff exist:

- **Model 1 “cost plus”:** The management instructions and capacity risk shift to the “recipient company”, acting as manager. The “payroll company” obtains a cost plus for its rental of professional staff.
  - An arm’s length profit mark-up is applied on the total budgeted cost per hour by the payroll company
  - The model 1 can plant the major part of the margin at the recipient company
- **Model 2 “resellers fee”** : The management instructions and capacity risk remains at the “payroll company” (the one seconding its employees). The “recipient company” (the one borrowing the employee) is acting as the reseller / negotiator and obtains a resellers fee.
  - Recipient company fee is **set as a percentage** of net sales of professional staff fees to third party customer.
  - Payroll company gets 95% of net amount invoiced to customer. The payroll company can gain the major part of the margin.



- **The hourly professional staff rental fee:**

$$\boxed{\frac{(A + B) * 1 + D)}{C}} \quad \boxed{= (A / C + B / C) * (1 + D)}$$

A. Direct cost component:
  - Basic Salary and Overtime cost
  - Standard Employee cost (e.g. leave, 13^{th} month, etc.)
  - Country Specific Employee cost (e.g. overseas allowances)
  - Country Specific Employee benefits (e.g. super annuation)
  - General Statutory Requirement Employee benefits (e.g. Social Security, pensions)

B. Indirect cost component
  - Total indirect cost including depreciation / amortization cost
  - Overhead cost: IT related excluding branding and management fees.

C. Annual direct hours (normal and overtime)
  - Total normal hours: see definition on next sheet

    Plus
  - The average number of overtime hours

D. Arm's length profit mark up: **7.5%**

Annual direct hour definition (normal time only):

Definition Annul "Direct Hours" without overtime	
Contract Hours	Hours as stipulated at the employee's contract
less sick hours	Sick hours paid
less Holiday/leave	Holiday and leave hours paid
= Available Hours	
less Indirect Hours	All hours not chargeable to clients (certification time-training, travel time, etc)
= Direct/Chargeable Hours	

Other price considerations:

- Actual travel expenses will be charged separately to the "Recipient" company.
- Travelling hours will be charged to the "Recipient company" (starting from the time the "Payroll Company" employee leaves home, with a maximum of 8 hours per day, without any special additional charge for travelling overnight or on weekends).
- Transfer prices need to be calculated for each of the personnel categories

The equipment fee consists of the following components:

- **Time value component**
- **Cost component**
- **Occupational degree of equipment**
- **Profit uplift**

I. Time value component:

A. Historical price of the equipment

B. Estimated useful life of the equipment in years

Note: time value component equals: (A/B)

- *Per type of equipment we will decide upon the number of years*

II. Cost component:

a) Annual financial interests

b) Annual insurance cost

c) Annual maintenance cost

d) General overhead costs

Note: percentages to be calculated on the historical price of equipment

III. Occupational degree of equipment

IV. Profit uplift:

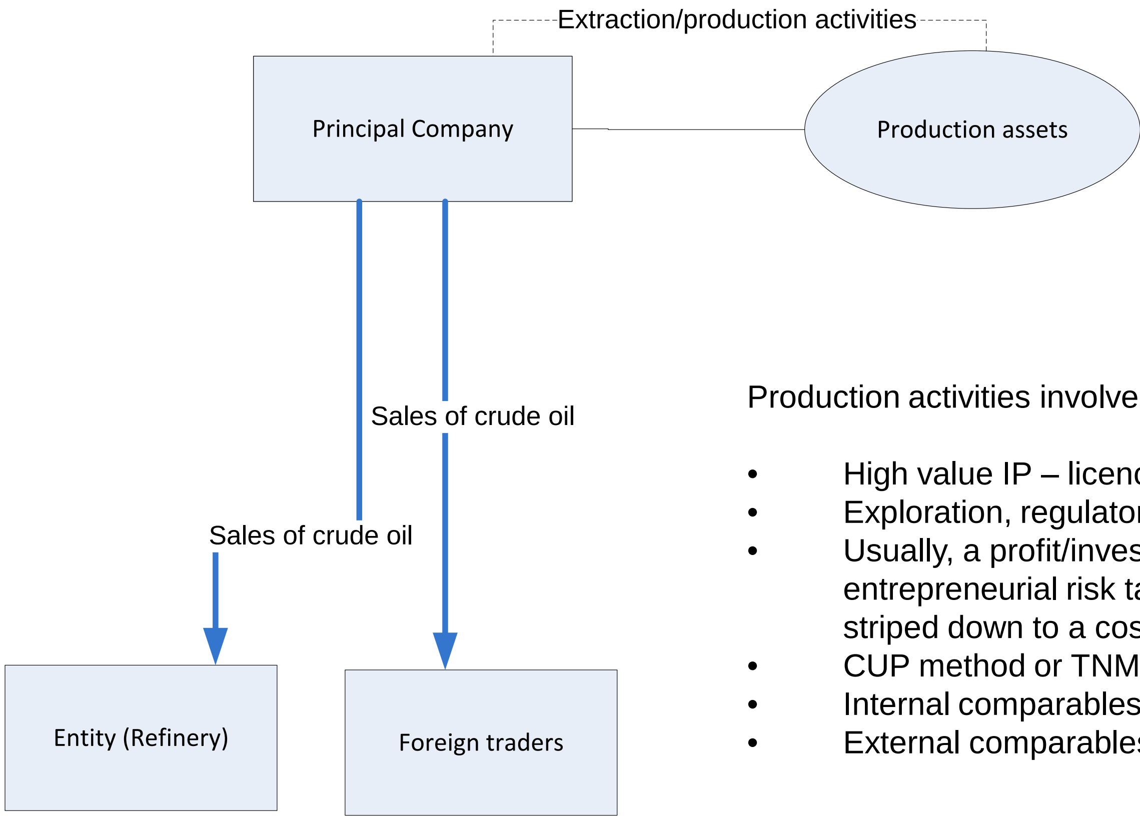
Determined on basis of benchmark

Daily equipment rental fee:

$$\frac{(\text{ Time value component I} + \text{Cost component II }) * (1 + \text{Profit Uplift IV})}{\text{Occupational degree of equipment III} * 365}$$

Other considerations:

- Mobilization and demobilization costs to be charged separately
- Rates in local currency of lending company
- Transport time charged
- For some items, minimum packaging charge
- Consumables for party using the equipment (back to back charge i.e. no margin at intermediary)
- Template available via Corporate

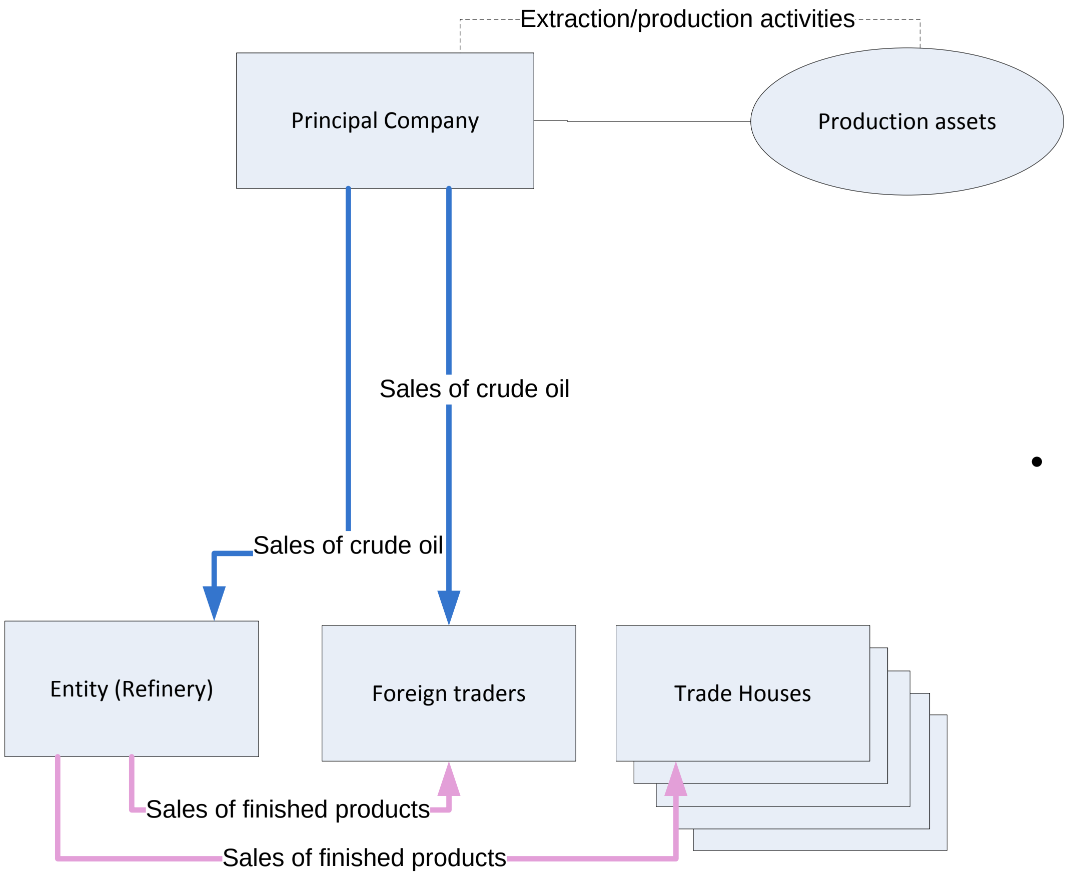


Production activities involve:

- High value IP – licences
- Exploration, regulatory & environmental risk
- Usually, a profit/investment centre, although can be disaggregated into key entrepreneurial risk taking functions and separate intangible assets to be striped down to a cost /expense centre
- CUP method or TNMM for the other transacting party.
- Internal comparables – comparability adjustments
- External comparables – Platts quotes, comparability adjustments

Index +/- differentials

- **Index:**
  - Commodity exchange
  - Platts qoutes
  - Argus
  - Etc.
- **Differentials:**
  - Logistics:
    - Incoterms
    - Spillage and waste
  - Quality:
    - Gravity / density
    - Sulfur
    - Acidity, etc
  - Bargaining / Trader's intelligence:
    - Timing, market situation
    - Relative position of buyer/seller, relative supply of similar products
    - Refining capacity utilization, etc



Refinery as a profit centre:

- Fully stand alone organisation: main decision makers and intangible assets
- CUP method is applied
- Internal comparables vs. external comparables (Platts quotes)

- Refinery as a cost centre (tolling refineries are a very usual practice in Europe):
  - TNMM method (cost plus if the refinery still bears the risks , i.e. not real tolling);
  - ROA/ROE or Mark-up on total costs remuneration

Transformation of refinery activities into contract refinery (conversion issues)

	Model 1		Model 2	
	Agent model **Where Trading hub operates as a procurement agent on behalf of Refinery**		**Principal model** **Where Trading hub takes the principal risks and pays Refinery a processing fee**	
	Trading hub	Refinery	Trading hub	Refinery
Functions	Procurement	Intake, trading, processing, sale and transport	Procurement intake, trading, sale and transport	Processing
Risks	Risks relating to procurement activities in case of gross negligence	All other significant risks	All other significant risks	Risks relating to processing activities in case of gross negligence
Assets	• Managerial expertise • Trading IT systems • Supplier relationship • Trading expertise • LP model (decision making)	• Physical refining assets • Supply and off-take contracts • Software licenses • LP model (logistics / operational fine-tuning).	• Managerial expertise • Trading IT • Supply and offtake contracts • IT systems • Trading expertise • LP model	• Physical refining assets • Software licenses

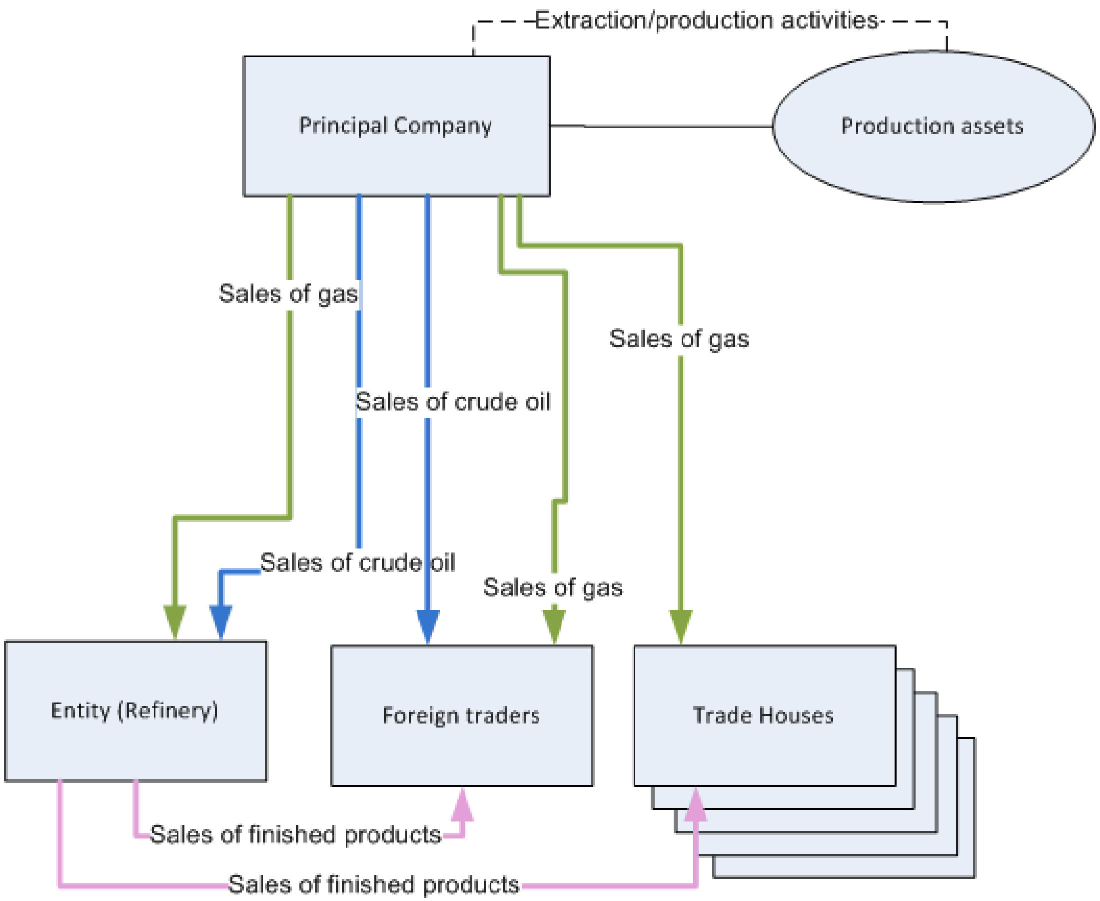
- Availability of trained/expert professionals (main functions to be shifted: Economics, Scheduling, Supply & Commercial, Trading, Finance, and IT);
- Optimizing balance sheet position to support trade positions;
- Optimizing tax efficiency (both on migration between models as well as covering ‘ future state’); and
- Assess business restructuring risks upon conversion from one business model to the other.

- Inter-company legal agreements (dynamic vs. static approach);
- Intellectual property of ‘trading software’ e.g. IT licensing and/or development cost;
- Allocation of residual risks to refinery under model 2;
- Who oversees the risk management of end-to-end margin?
- Position of local wholesale entities, e.g. broker vs.. agent/distributors; and
- Ensuring that the necessary resources (people, IT, processes) are in place before change.

- **Specific activities which <u>can</u> be executed by Refinery are any <u>refining</u> activities , i.e. being**
  - General management of the refinery;
  - Administrative activities;
  - Built up of any related refining and technical intelligence for running the refinery;
  - Performance of the actual refining process;
  - Decisions on production planning;
  - Decisions on maintenance planning;
  - Assuring the quality of the refining process;
  - Managing and assuming of all refinery related technical risks;
  - Managing and assuming of all refinery related operational risks;
  - Managing safety, health and environmental issues related to the refinery; and
  - Contractual transportation of the finished product.

- **Specific activities which <u>can not</u> be executed by refinery are any <u>commercial</u> activities, i.e. being**
  - No employees on the refinery payroll performing any commercial activities;
  - Built up of any commercial intelligence at refinery;
  - No purchasing of crude oil;
  - No intake of crude oil or any logistics thereof;
  - No trading or any support of trading activities (i.e. order processing); and
  - No sale of the finished products/debt recovery and management/exposure.

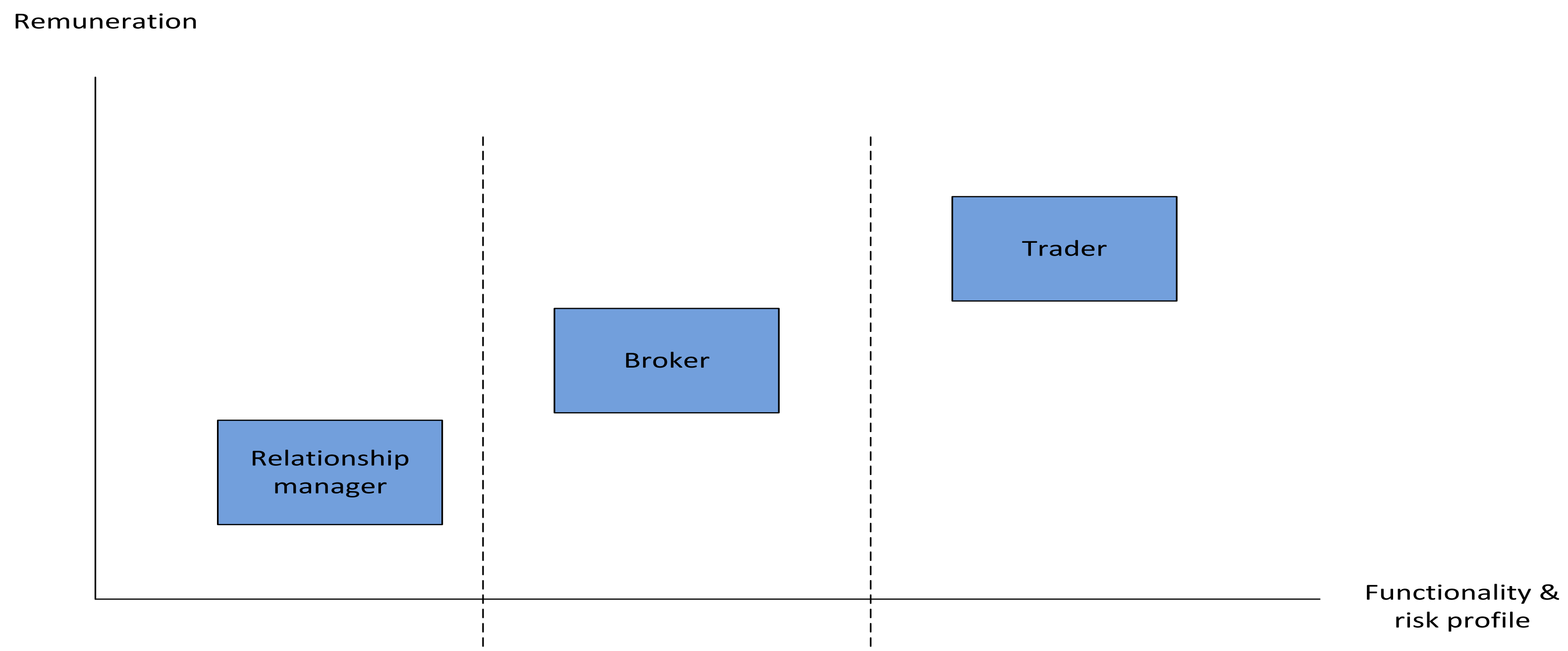
- Case to establish tolling model is compelling although exit charge for refinery needs to be minimised
- Establishing and recruiting trading hub organisation and infrastructure on critical path
- Trading hub organisation should be in place before additional refining assets are added to reduce further exit charge risk
- Organisational impact at refinery needs to be aligned with other changes
- Appropriate tolling agreement to be drafted to balance risk and reward



Distribution (sales and marketing) activities can be categorised as:

- Relationship management
- Brokerage
- Trading

Similar categorization applies to procurement and sourcing activity.



Functions	Marketing, client relations	Limited sales activities, sales administration	Full distributor activities
Risks	No major risks	Volume & budget risk	Market risk
Assets	No assets	No assets	Possible assets
Responsibility profile	Costs centre	Revenue centre	Profit centre
TP methods	TNMM	CUP, TNMM	CUP, Resale Minus
PLI	Mark-up on total costs	Commission, MOTC	Platts quotes, Resale margin

Shared service centre

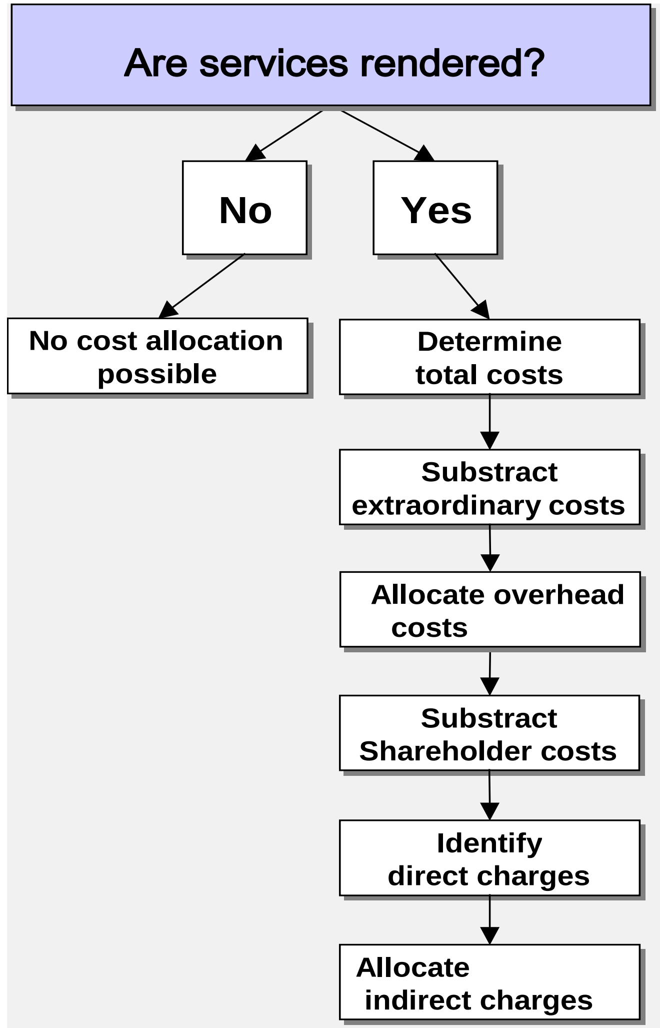
Shared service centre services:

- General management
- IT
- HR
- Legal
- Marketing
  Accounting & financial administration
- Treasury

Shared service centre activities:

- Routine, back office services
- Cost centre
- TNMM to be used by applying a mark-up on total costs
- CUP (hourly rates) is possible but difficult to obtain reliable comparables
- Determination and allocation of costs
- Benchmarking an appropriate arm's length mark-up – use of AMADEUS or other database for financial information.

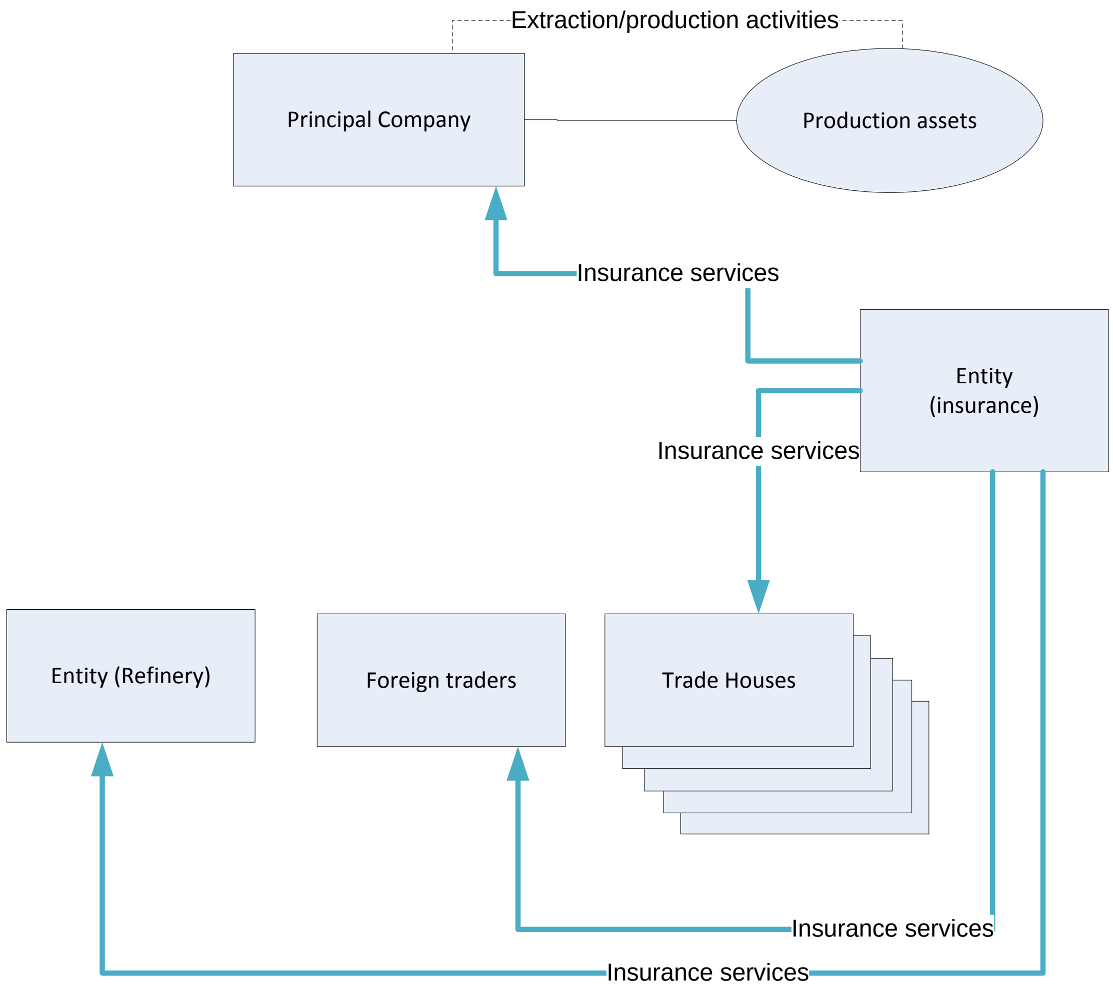
- **Benefit test**
- **Identification of potential market references and choice of transfer pricing method**
- **Allocation schedule for costs of providing intra-group services**
  - Subtract extraordinary costs
  - Allocate indirect overhead costs
  - Subtract shareholder activities costs
  - Direct charges for specific services
  - Non-specific services: indirect charges: allocation keys and mark up



- **Allocation criteria:**
  - Turnover
  - Number of employees(FTEs)
  - Invested funds
  - Number of computers
  - Etc.

- **Budgeted cost vs. actual costs**

- **Arm’s length mark-up:**
  - Bundling (weighting) of services or specific mark-up for every type of service
  - Is there a value added on the service providers side



Captive insurance activities:

- Defined by the functionality and risk profile of the insurer
- Can be cost or profit centre
- TNMM for cost centre
- Profit centre would use 'other method' – a mathematical model usually used in insurance industry

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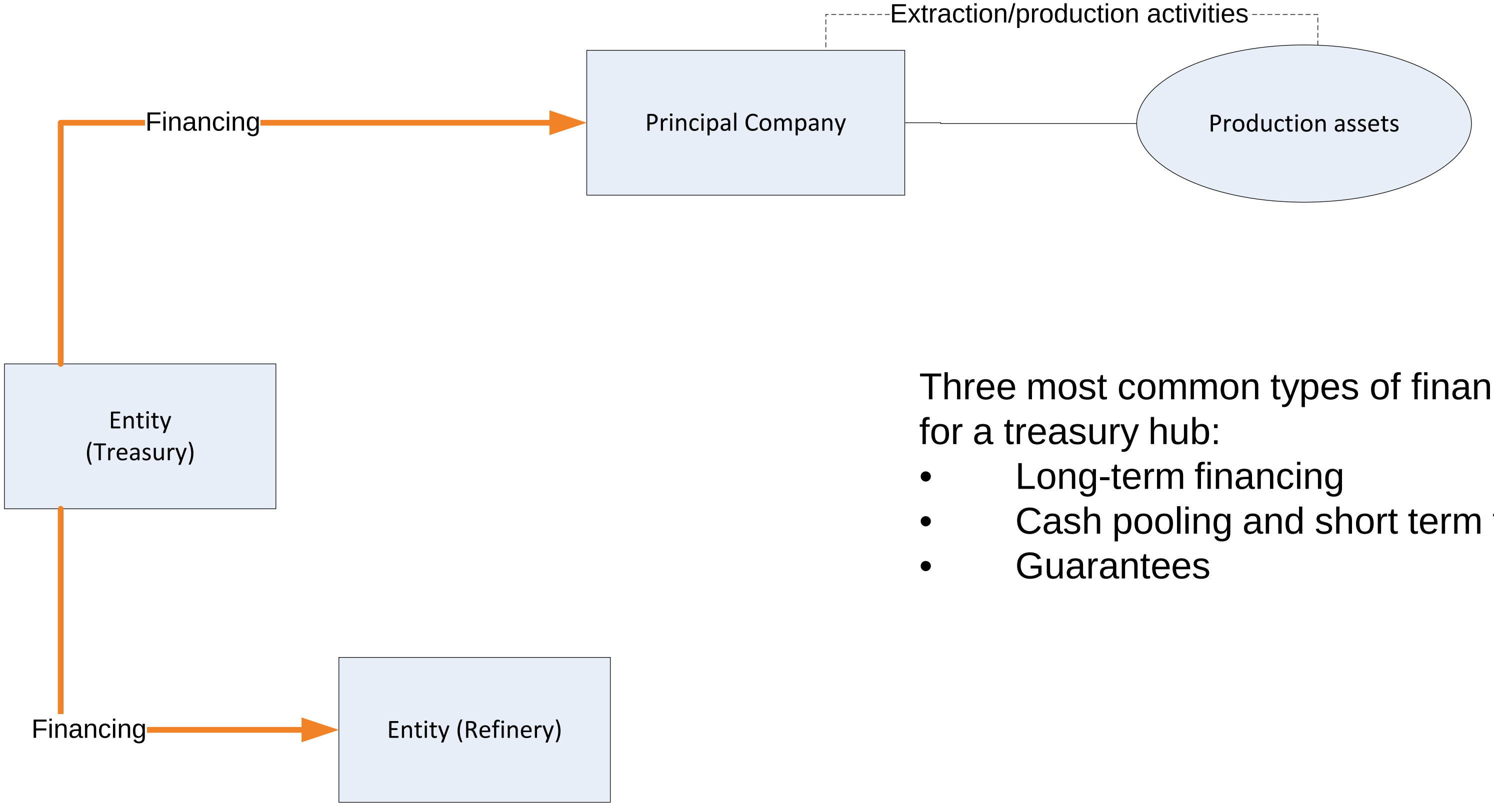
Stage of the insurance process	Key decisions	Responsible party		
		Captive Insurer	Captive's contractors	Treasury entity of the Group
Product management /product development	Market research			
	Gathering and maintaining claims statistics			
	Mathematical calculation of the premium			
	Legal stipulation of the extent of			
Sales and marketing	Client acquisition			
	Advising clients			
	Provision of quotes and proposal			
Underwriting insured risk	Setting the underwriting policy			
	Risk classification and selection			
	Pricing			
	Risk retention analysis			
	Acceptance of insured risk			
Risk management	Capital management			
	Decide on whether to use reinsurance (strategic)			
Contract and Claim management	Notification of claim			
	Adjuster appointment			
	Negotiation and acceptance of the claim			
	Decision on making payment of the claim			
Asset management	Investment management			
	Asset/Liability management			
Support Processes	Treasury functions			
	Loss control			
	Systems and development of intangibles			
	Regulatory compliance			

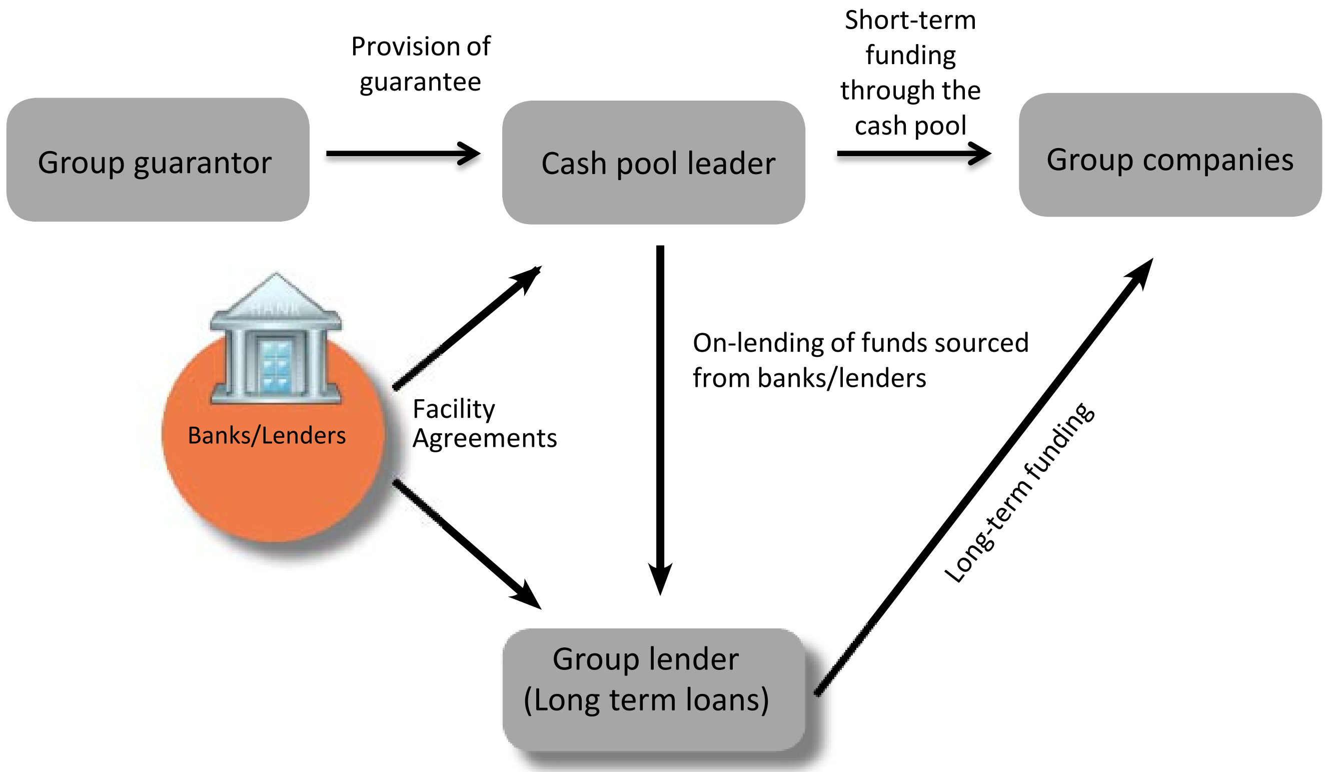
		First Model	Second Model	Third Model
Criteria	Diversification of risk	No	Yes	Yes
	Captive is making key decisions	No	No	Yes
	Captive possesses adequate capital to absorb insurance and insured risks	No	No	Yes
Outcome of the test	Responsibility of the captive	N/A	Cost centre	Profit centre
	Typical transfer pricing model	N/A	Cost plus (on Captive's operating expenses)	"CUP" or premium calculation based on: 1. Risk adjusted return on capital 2. Loss predictions 3. Compensation for the captive's operating expenses



Three most common types of financing activities for a treasury hub:

- Long-term financing
- Cash pooling and short term financing
- Guarantees

Through proper pricing of the following intercompany financial transactions



Addressing the following key issues:

1. How to deal with intermediate finance companies?
2. How to determine intercompany guarantee fees?
3. How to allocate the benefit in a group wide cash pool structure?
4. How to price long term loans?

- TPA's approach is based on the recommendations provided by the OECD Guidelines, specifically on the Report on the Attribution of Profits to Permanent Establishments (July 2010)

- Functional analysis focuses on:

  1. Loan Origination
  2. Loan Management
  3. Risks
  4. Assets

- Characterization of treasury activities:

  1. Cost Centre
  2. Revenue Centre
  3. Profit Centre
  4. Combination of the above

Process	*Functions/risks*	*Cash pool leader*	*Other group entities*
Loan Origination	Sales/Marketing	●	-
	Sales/Trading	●	-
	Trading/Treasury	●	-
	Sales/Support	●	-
Loan Management	Loan Support	●	●
	Monitoring risks	●	○
	Managing risks	●	○
	Treasury	●	-
	Sales/Trading	●	-
Risks Management	Credit risk	●	●
	Market interest rate risk	-	-
	Forex risk	●	-
	Structural market risk	○	○
	Operational risks	○	○
	Strategic risk	●	-
	Reputation risk	●	-

Legend:
● = involved regarding own capital or funds
○ = limited involvement
\- = not involved

Choice of method & Economic Analysis

	1. Direct financing via long-term cross-border loans		
Responsibility Profile	Cost / Revenue Centre	Profit Centre	Cost Centre
TP Method	CUP	CUP	Cost plus
Economic Analysis	Annual fee + Equity Risk Premium	Market Interest Rate Credit Rating	Mark-up on total costs
Database used	Loan Connector	Moody's S&P Fin. Info Co. Reuters	Amadeus

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Choice of method & Economic Analysis

2. Short term financing via an existing cash pool

Responsibility Profile	Cost / Revenue Centre	Profit Centre	Cost / Profit Centre	Cost Centre
TP Method	CUP	CUP	CUP	Cost Plus
Economic Analysis	Annual fee + Equity Risk Premium	Spread Margin	Spread Margin	Mark-up on total costs
Database used	Loan Connector	Loan Connector	Loan Connector	Amadeus

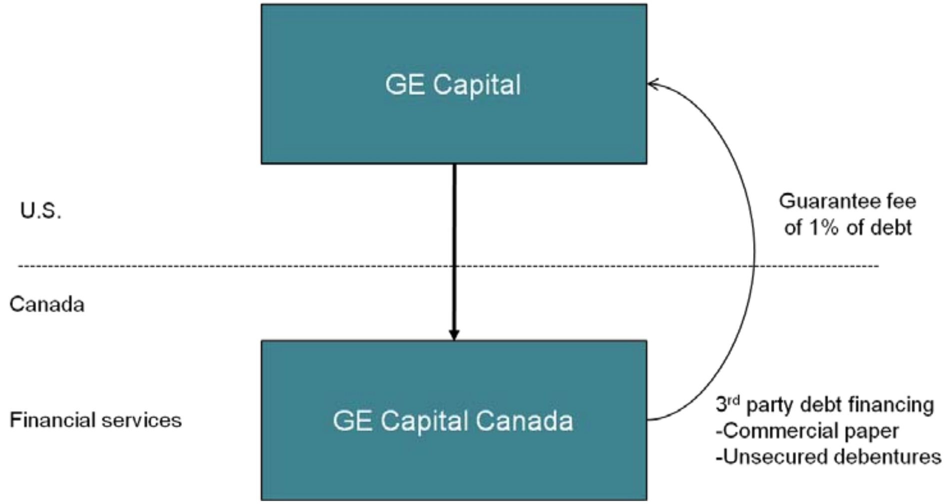
Choice of method & Economic Analysis

	3. Provision of Guarantees	
TPA's Approach	**Alternative Financing Cost**	**Compound Model**
TP Method	Guarantee Fee = Cost credit facility % (spread) – Cost alternative financing with no guarantee	Guarantee Fee = Commitment fee + (Interest Market Rate * Probability of default)
Economic Analysis Benchmark focused on identifying →	Credit rating Spread on Corporate Bonds	1. Commitment fee in syndicated loan transactions 2. Default fee 3. Borrower Credit Rating

GE Capital Landmark TP case

Case Study - GE Capital Landmark TP case (Canada)

Tax Court of Canada ("TCC")



CRA's Position:

1. Transaction was unnecessary and therefore had no value
2. Economically Relevant Circumstance
3. Transfer pricing methodologies

Taxpayer's Position

1. Arm's length transaction
2. Value of transaction
3. Methods used to establish the credit rating

Tax Court of Canada (TCC) Decision

- 1% guarantee fee was allowed as it is not more than 1.83% obtained under the yield approach
- Implicit support is a relevant economic factor in determining the arm's-length price

<u>Federal Court of Appeals ("FCA")</u>

CRA's Position

Four errors of law:

1. Tax Court Judge failed to identify the relevant transaction - analyzed and valued a transaction different from the one that took place
2. Tax Court Judge erred in preferring the evidence of the respondent's expert over other expert witnesses
3. Tax Court Judge committed a legal error in failing to conduct a "reasonableness" check
4. Tax Court Judge erred by upholding the necessity of the explicit guarantee based on the business judgment of a witness

Additional argument:

- Procedural fairness

Taxpayer's Position

The Taxpayer objected to the four errors of law raised by the CRA

1. Valuation methodology proposed by the Taxpayer specifically requires the Court to take into account the impact of the removal of the guarantee
2. Relevant factors are not mandatory
3. The Judge did not rely on the business judgment of the witness; instead, relied on the yield approach

   Even if the alleged errors were committed, the appeals nevertheless cannot succeed

Two fundamental errors in the application of the arm's length standard:

1. Reducing the arm's length price for the guarantee on account of implicit support
2. Incorrect method used for determining the arm's length price

Decision of the Federal Court of Appeals (FCA)

- **The Crown's appeal dismissed**
- **The errors of law identified by the Crown were dismissed:**
  - The error committed by the Tax Court Judge had no impact on the findings
  - Weighting of the evidence was appropriate
  - No "reasonableness" check is required
- **Procedural fairness**
  - The Tax Court Judge did not develop his own theory
- **Implicit support is a relevant factor in determining the arm's length price**

Conclusion & Implications of the Court decision

- Guarantee fees to be charged
- Recognition of concept of "implicit support"
- Boundaries of the arm's length fiction

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Oil and Gas Industry: Customs duties and excise duties in EU

Your bridge to worldwide transfer pricing services

TPA Global

		Rules/RiskFactors	BusinessModel/RiskFactors
Legacy	**CustomsValue**	Related party tests; Royalties & license fees; R&D; Debit/credits	TP; Royalties; Waivers; Invoices; Declaration process
Legacy	**Classification DutyRate**	Tariff Rules; Form vs.. Function; Changes in composition inconsistencies	New product coding; Materials; Formulation Changes
Legacy	**Origin/ Preference**	Qualification rules; Added value; Direct transport; Direct sale	Origin commitments in pricing negotiations
Legacy	**Reliefs/ Drawbacks**	Authorization; Economic Justification; Conditions; Discharge/reconciliation	Process Definition and Awareness
New	**SupplyChain Security**	Some specific (e.g. US: C-TPAT and EU: AEO), EU Proposals	Policies and standards practice; IT lead times; Reactivity

Analyze & Deliver

- Supply chain optimization through customs planning
- Customs compliance and software solutions
- Litigation (classification, custom value, origin and formalities)
- Non-tax measures

Addressing the following key issues:

1. How to identify strengths/weaknesses against customs rule base and external threats?
2. How to mitigate trade impasses, fines/penalties, seizure of goods, legal proceedings and criminal charges?
3. Do you integrate 3rd party and country considerations e.g. some countries known to act inconsistently with WCO/WTO custom rules?
4. What are your considerations on systems development which can significantly enhance compliance and security

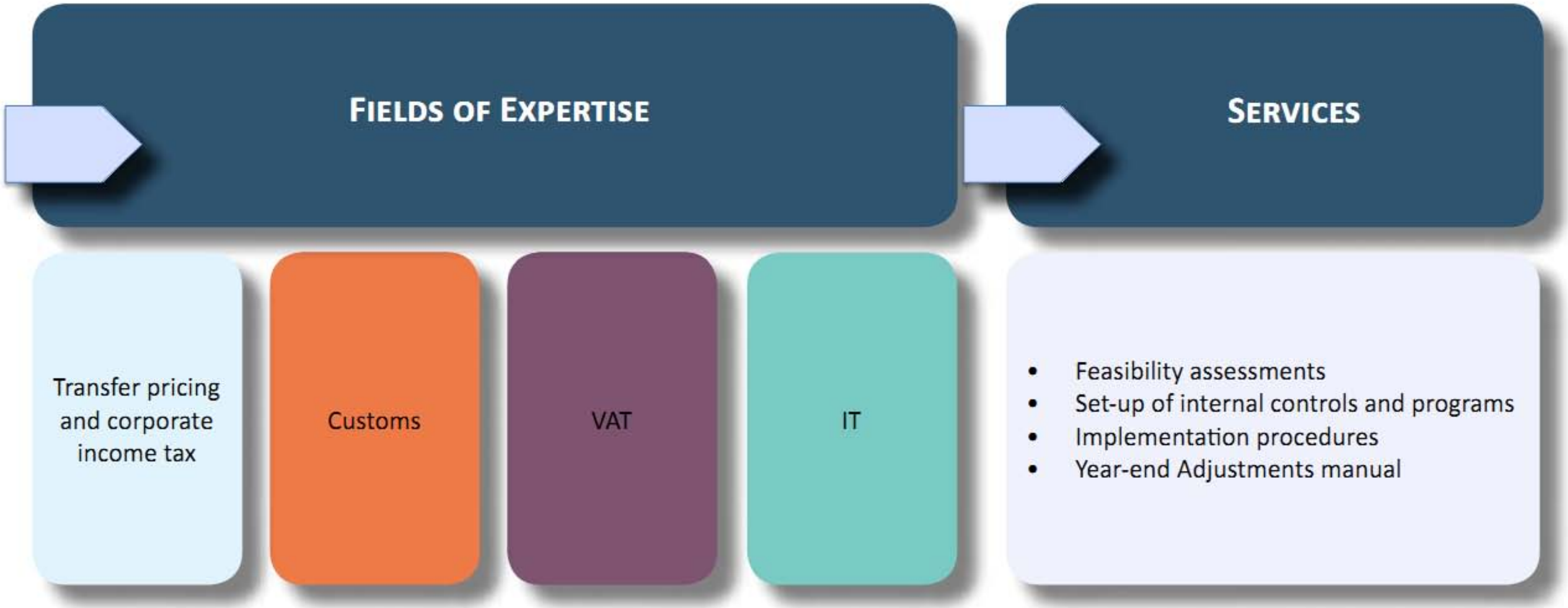
- When imported into EU27 member States:

  - The vast majority of (crude) oil and gas products are subject to 0% customs duty, or duties are however suspended, given the EU deficiency of these resources.

  - A number of refined products are subject to customs duties in the range 3.5% – 6.5% of the ‘customs value’ of the products: they are ‘ad valorem’ duties, thus there can be interplay between transfer price and customs value.

- Starting from January 2012, some oil and gas products originating in US, Turkey, Canada are subject to additional duties (antidumping measures) when imported into the EU.

WTO customs language		***OECD language***
1. Transaction Value (TV)	→	Invoice price / transfer price (*subject to amendments*)
2. - 3. Value Identical or Similar Goods	→	CUP
4. Deductive Value	→	Resale price-minus
5. Computed Value	→	Cost-plus
6. Flexible Application of methods 1-5		



Addressing the following key issues:

1. How to deal with price / profit adjustments when your financial results depart from targeted arm's length outcomes?
2. How to structure and implement internal procedures and controls to comply with arm's length standard world-wide?
3. How to build an integrated legal and financial framework to address global year-end adjustment challenges from a multiple perspective: corporate tax, transfer pricing, customs duties and VAT?
4. How to align Year-end Adjustment looking at the following 3 perspectives: transfer pricing, customs and VAT?

- Mineral oils are subject in the EU to excise duties when released for consumption into one of the EU member States.
- Excise duty is an indirect tax which is levied on the consumption of mineral oils such as leaded petrol, unleaded petrol, gas oil, heavy fuel oil, liquid petroleum gas, methane, kerosene, etc.
- Excise duty is not levied on the basis of the value declared of the products – they are 'specific' duties which apply based on the weight/ volume of the products concerned.
- The EU excise duty system is harmonized throughout its 27 member States via EU Directives, establishing the regulatory standards for production and circulation of mineral oils across member States and defining minimum tax rates valid in all member States for each product (option for each State to increase the tax rates).
- Main features of EU excise duty system:
  - Consumption is taxable
  - Consumption is national (excise duty of member State shall apply)

- Scope of EU suspension arrangements:
  - Processing of excisable goods (e.g. processing of crude oil)
  - Holding of excisable goods (e.g. movement of mineral oils from refinery to warehousing)

- Tax warehouse:

  A place where excise goods are produced, processed, held, received or dispatched under duty-suspension arrangements by an authorised warehousekeeper in the course of his business (e.g. refinery plant) – subject to provision of guarantee + appropriate records

- Moment excise duty becomes chargeable:
  - Release for consumption
    - (Irregular) departure from a suspension arrangement
    - (Irregular) manufacture outside a suspension arrangement
    - (Irregular) importation where products have not been placed under a suspension arrangement

- Payment of excise duty
  - Competent authority: country where excise duty becomes chargeable
  - Document: declaration for consumption

- **Example of excise duty pending on consumption of Leaded petrol in selected EU member States**

Leaded Petrol		
Member State	**currency**	**excise duty per 1000 litres**
EU minimum tax rate	*EUR*	421
Italy	*EUR*	704.2
Cyprus	*EUR*	421
Latvia	*EUR*	451.2
Lithuania	*EUR*	579.3
Hungary	*EUR*	422
Netherlands	*EUR*	813.5
Austria	*EUR*	554
Poland	*EUR*	587
Portugal	*EUR*	650
Sweden	*EUR*	701
UK	*EUR*	787.2

Organizational Aspects of Transfer Pricing – Transfer Pricing Control Framework

Your bridge to worldwide transfer pricing services

- **How to set up a "transfer pricing control framework":**
  - Workflow process
  - People
  - Reporting lines
  - Software solutions

By applying a multiple perspective approach

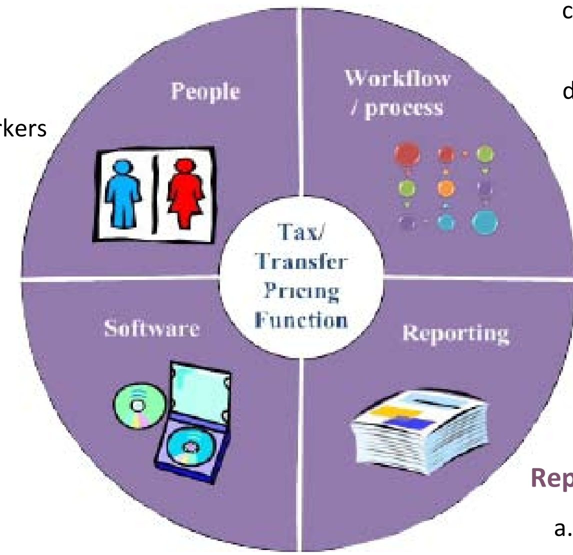
People

a. Performance measurement
b. Geographical spread of knowledge workers
c. Knowledge sharing
d. Succession planning
e. Experience level
f. Number of TP knowledge workers

Workflow

a. Global benchmarking process
b. Document management process
c. Financial data retrieval and conversion process
d. Aligned formatting TP relevant data

Internal communication with business →



→ External communication with stakeholders e.g. tax authorities

Software

a. Most relevant functionality
b. TP specific storage platform
c. Alternative software solutions

Reporting

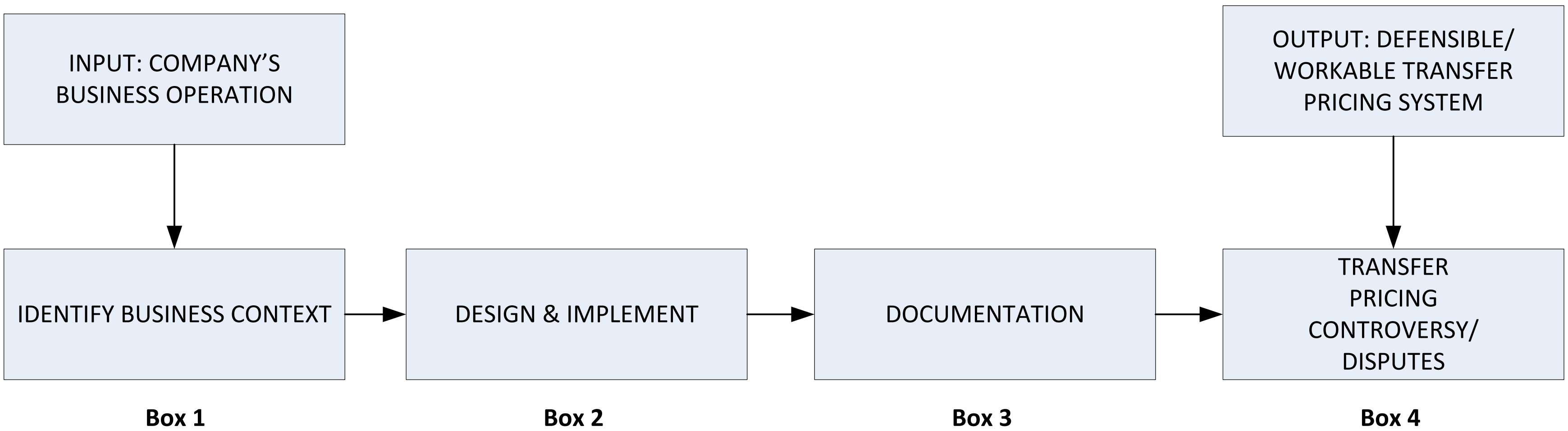
a. Checks & balances on TP risks
b. Interaction central TP – local TP team
c. TP ‘dashboard’ for CFO
e. Responsibility/accountability
d. TP policy paper

Addressing the following key issues:

1. What is your optimum in-house knowledge workers configuration?
2. How many of the TP relevant processess are in place?
3. What is your 1 to 2 years TP software strategy?
4. How is your segregation of duties & responsibilities defined for transfer pricing?

- **Separate quick scan is available at TPA’s website**

http://www.tpa-global.com/index.php?option=com_content&view=article&id=109&Itemid=279&lang=en


INPUT: COMPANY'S BUSINESS OPERATION
OUTPUT: DEFENSIBLE/ WORKABLE TRANSFER PRICING SYSTEM
IDENTIFY BUSINESS CONTEXT
DESIGN & IMPLEMENT
DOCUMENTATION
TRANSFER PRICING CONTROVERSY/ DISPUTES
Box 1
Box 2
Box 3
Box 4

To address the in-house transfer pricing knowledge workers' profile, the following variables will have to be addressed:

- Level/degree of education and number of years experience;
- Continuing education;
- Roles and responsibilities;
- Full time equivalents vs. part-timers;
- Career profiles;
- Centralized vs. localized expertise; and
- Degree of insourcing or outsourcing.

Comments TPA:
Larger multinationals tend to have up to 5 FTEs transfer pricing knowledge workers, mostly located in 1 up to 3 locations.

MNE should define a clear and transparent structure of communication on:

- Governance model relating to transfer pricing (already in existence and part of the overall governance structure);
- Global transfer pricing policy paper: a management board signed policy paper used as a communication tool and back-up/authorization by in-house tax team;
- Roll out and further implementation steps (i.e. delegate authority + define responsibilities);
- How much of the communication will be organized 'top-down‘;
- How much of the communication will be organized 'bottom-up‘; and
- Whether the current governance structure includes sufficient KPIs or other monitoring tools to keep in-house professionals accountable for upfront agreed upon 'roles and responsibilities‘.

To enhance the control framework being easy to use and access, scalable and flexible, MNE needs to define its need for the following 8 categories of functionality of software:

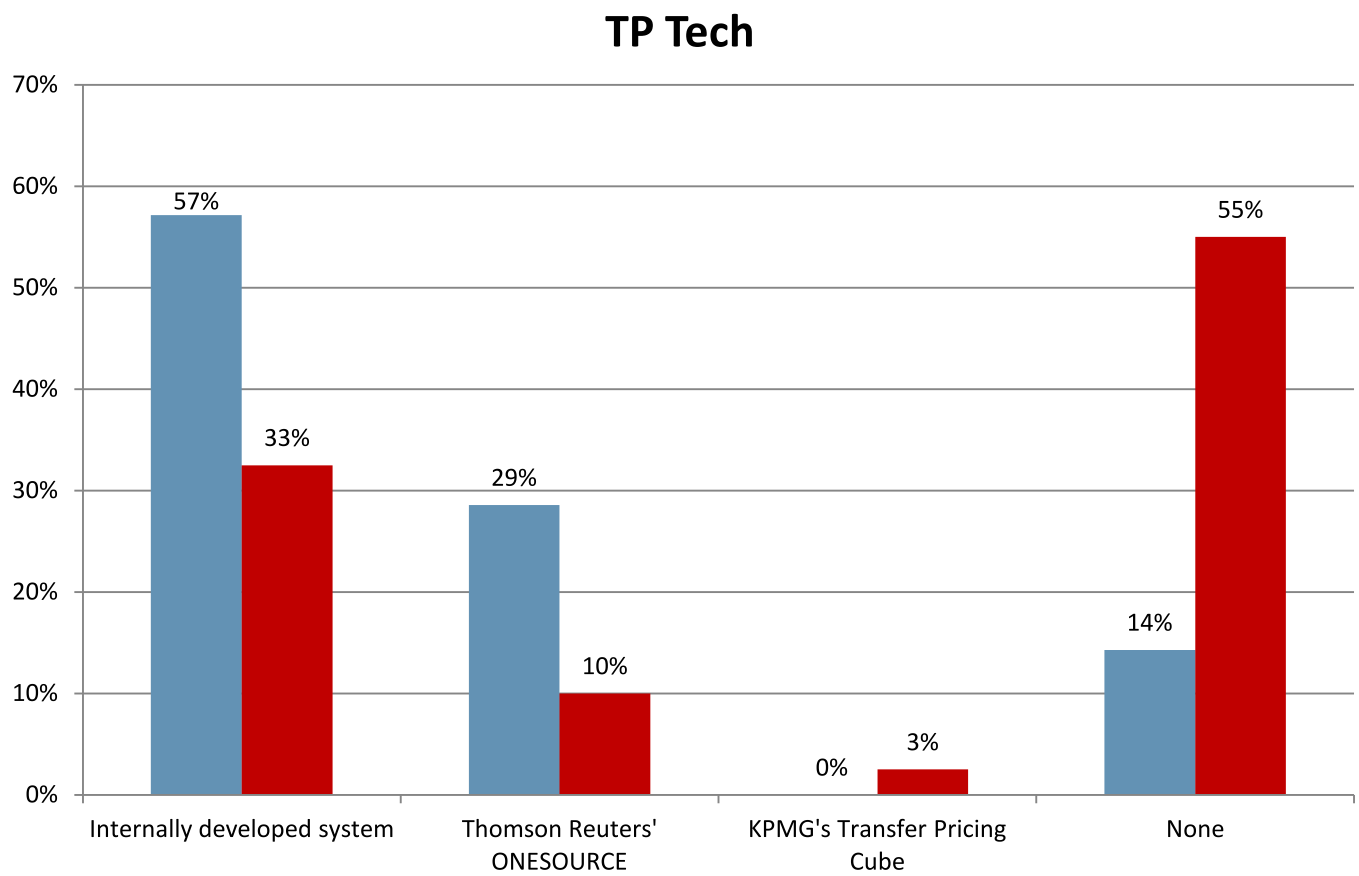
i. for design/planning
ii. for documentation
iii. for benchmarking
iv. for implementation/financials
v. controversy management
vi. MNE specific workflows embedded
vii. e-learning tools
viii. compatibility with existing (in-house tax team) software being used.

The following slides explain:

- From a 2011 survey from the US-based Tax Directors Roundtable: what software is being used by the market;
- From a 2011 survey from the US-based Tax Directors Roundtable: for what functions is the software being used;
- A 2011 comparative survey by TPA on software solutions in the marketplace; and
- What short, medium, and long term transfer pricing software ambition does MNE have?

Nearly all **Elites** have technology to support their transfer pricing, with more than half having built their own systems.

Over half of **Emerging** currently function without use of any transfer pricing-specific technology.



FINANCE AND STRATEGY PRACTICE, TAX DIRECTOR ROUNDTABLE

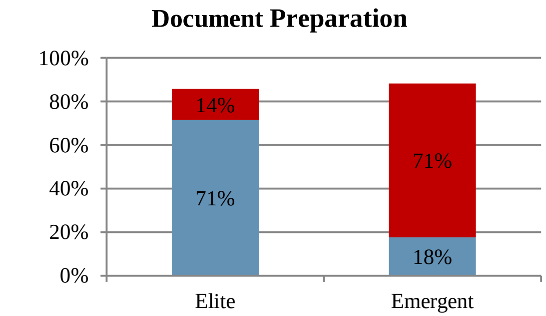
What functions is the software being used for?

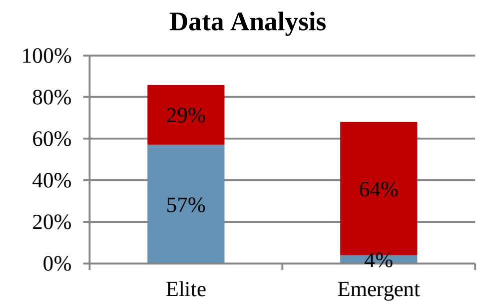
Elites' homegrown systems may explain part of the much greater strength on core functions compared to **Emerging**.

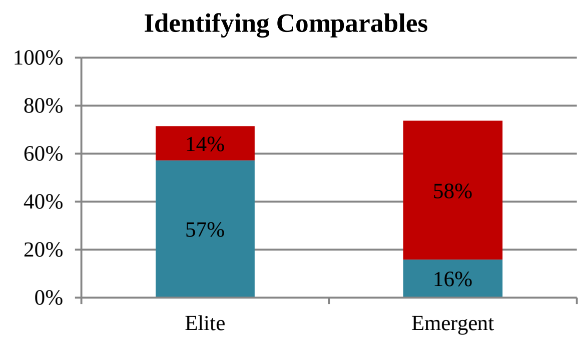
Effectiveness for both groups however drops in quality across data extraction, and tracking filings as well as documentation.

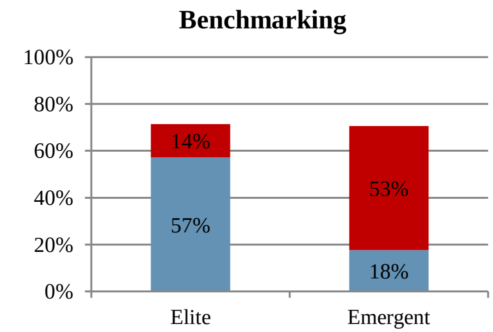
Very Good

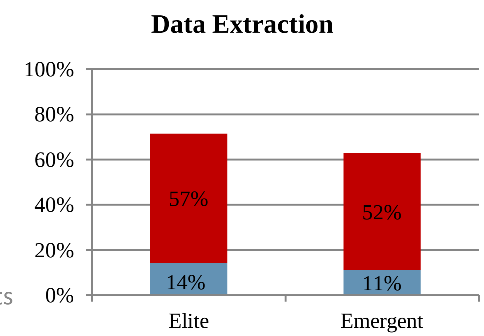
Good

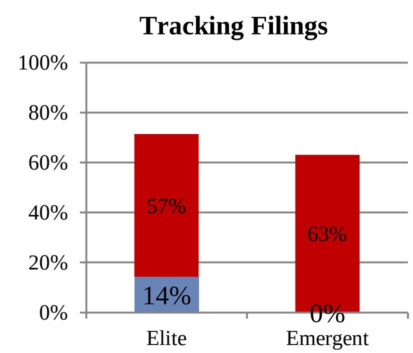


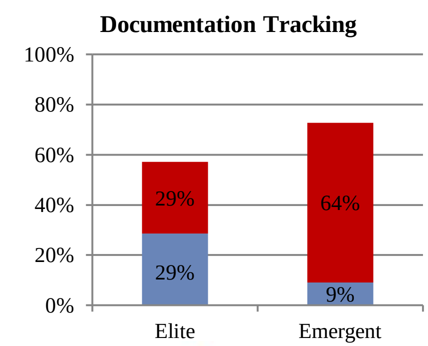












- **Needs: A centralized configuration available**

	Thomson Reuters – one source	PebbleAge	GTP	Vantage (release 2013)
TP Design / Planning	N/A	Partially (financials)	N/A	Partially
TP Documentation	Fully (standards)	Partially (financials)	Fully (flexible)	Fully (flexible)
TP Benchmarking	Fully	N/A	Partially	N/A
TP Implementation / financials	N/A	Fully	Fully	N/A
TP Controversy	N/A	Partially	N/A	Partially
Workflows embedded	N/A	Partially	N/A	Partially
Training/e-learning	N/A	N/A	N/A	Partially
Software compatibility	Partially	Fully	Partially	Partially
Type/level cost	[upon request]	[upon request]	[upon request]	[upon request]
Installed base	>300	<5	<10	N/A

Other propositions:
- KPMG's TP Cube + Interpreter
- TP Catalysts (BvD) (www.bvdinfo.com)
- Transfer Pricing Genie (www.tp-genie.com)
- Transfer Pricing Architect (www.corptax.com)
- Kamakura Corporation (www.kamakuraco.com)

What short, medium, and long term transfer pricing software ambition does MNE have?

- **What is your short term TP software ambition?**
  a. Automate global TP documentation
  b. Automate local TP documentation
  c. Automate global TP risk management
  d. Automate local TP risk management
  e. Other, please specify
- **What is your medium/long term TP software ambition?**
  a. A structured 2-5 years plan to build & implement software with all relevant functionality
  b. A global software shared service centre for tax and/or transfer pricing
  c. A software plan for TP documentation
  d. A software plan for TP design, documentation, implementation and/or defense strategy
  e. A software plan for tax and TP provisionary
  f. Other, please specify
- **Rank your top 5 most important criteria**
  a. Cost threshold
  b. # of FTE/TP knowledge workers
  c. Amount of compliance savings to be accomplished
  d. Degree of TP risk mitigation to be accomplished
  e. Adequate global project and document management
  f. Other, please specify

Transfer Pricing Associates

Organisational Aspects of Transfer Pricing – Transfer Pricing Project Workplans

- Possible overall Transfer Pricing Workplan
- Workplan for a documentation project
- Workplan for an APA project
- APA case management

The workplan is based on the following assumptions:

1. Determine key factors and ambition levels on MNE’ transfer pricing control framework in terms of (i) People, (ii) Reporting Lines, (iii) Work Flows, (iv) Software Solutions;
2. Determine the 'key value drivers' per business unit;
3. Determine whether the current transfer pricing system is aligned with the current business model (i.e. means 'economic reality' = 'legal reality' = 'statutory/tax books reality'), including drafting a global MNE transfer pricing policy paper (within existing governance model applied by MNE);
4. Organize software/intranet solution for collecting and capturing all existing documentation (determine 'as is' documentation available);
5. Define missing documentation and workplan to produce relevant documents to ensure compliance with global/regional/local documentation requirements;
6. Validation check on intercompany agreements and accounting manuals;
7. Define milestone sessions each month to monitor progress by in-house project team, including clearly defined target dates for roll-out and implementation per business unit.

Steps	Time and Scope charter												Deliverable(s)	Responsible party
Step 1		Kick off with project core team											scope and purpose of in-house project, determine MNE's ambition on global TP control framework and determine allocation of roles/responsibilities between BU tax manager and local tax managers	XXX [TBD]
Step 2	Introduction session to 'key value drivers' for each of the business units.												1-5 pages per business unit indicating the 'key value drivers' with a clear visualization of the 'value chain' AND using external publications to support the 'internal views'.	XXX [TBD]
Step 3		Obtain a written description of current transfer pricing system.											1-5 pages describing the 'as is' transfer pricing system (at level of 'price setting' AND at level of 'price or profit checking')	XXX [TBD]
Step 4		Compare 2. and 3. to determine degree of alignment between business model and 'as is' transfer pricing' system.											Description on significant and less significant differences (memo on ranking and proposed action to create alignment with business models).	XXX [TBD]
Step 5				Organise and collect at one central digital document management system all 'existing' transfer pricing documentation packages, including a full indexing.									Indexed and summarized document management system of all 'existing' transfer pricing documentation available for MNE's inter-company transactions. This step would involve a more definite decision on the use of IT enhanced software for in-house knowledge workers.	XXX [TBD]
Project management and quality control														
	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Week 8	Week 9	Week 10	Week 11	Week 12		

*** The steps above are based on TPA 'best practices', but require refinement to the MNE specific needs and priorities.**

Steps	Time and Scope charter												Deliverable(s)	Responsible party
Step 6				Organise and collect at one central digital document management system all 'existing' inter-company agreements, including a full indexing.									Indexed and summarized document management system of all 'existing' inter-company agreements available for MNE's inter-company transactions.	XXX [TBD]
Step 7							Identify missing transfer pricing documentation to remain compliant, based on practical references						Multiple sub-workplans which require project core team to (re)allocate to various in-house transfer pricing knowledge workers.	XXX [TBD]
Step 8										Creation of missing transfer pricing documents for the period up to and including FY2011.			Having a fully contemporaneously documentation package, with useful information for tax planning purposes.	XXX [TBD]
Step 9				Prepare and review tax/transfer pricing planning options for 'financial impact' analysis									Playbook of tax/transfer pricing planning options, including a ranking based on (i) financial impact (ii) type/degree of tax risks involved (iii) anticipated timing of implementation.	XXX [TBD]
Step 10							Determine 2012 maintenance plan for transfer pricing documentation and planning purposes.							XXX [TBD]
Project management and quality control														
	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Week 8	Week 9	Week 10	Week 11	Week 12		

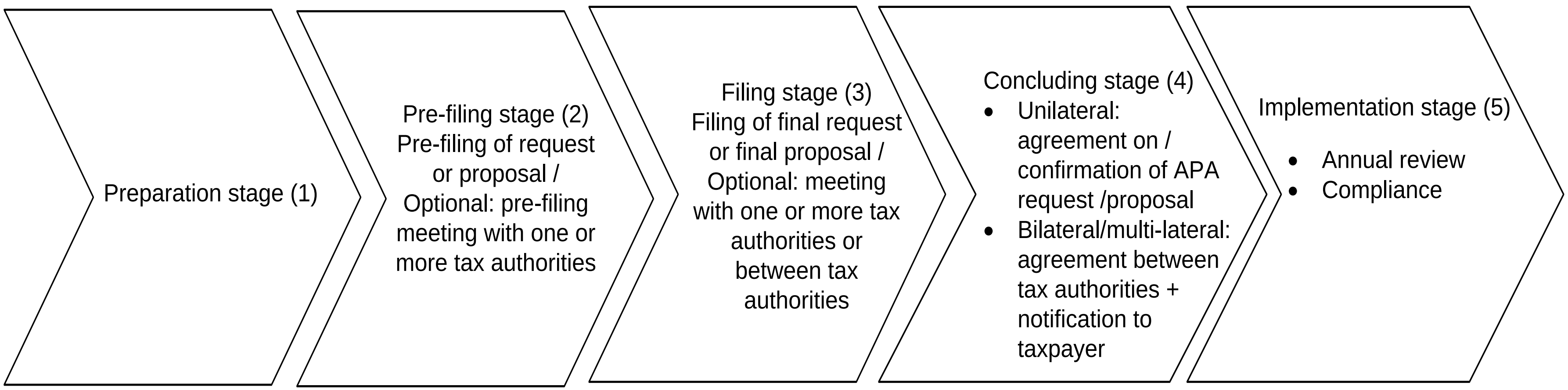
*** The steps above are based on TPA 'best practices', but require refinement to the MNE specific needs and priorities.**

Transfer Pricing Associates

Steps	Detailed description	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Deliverable(s)	Responsible party
		Time and Scope Charter								
Step 1	Kick-off meeting & information gathering	**Interview and/or conference call**							Interview minutes	TPA & XX
Step 2	Draft of company, industry and functional analysis, choice of TP method		**Write-up of company, industry and functional analysis, choice of TP method**	**Write-up of company, industry and functional analysis, choice of TP method**					Write-up of company, industry, function al analysis and choice of TP method	TPA, review by XX
Step 3	Performance of Benchmarking Studies			**Benchmarking studies**	**Benchmarking studies**	**Benchmarking studies**			Write-up of benchmarking analysis	TPA, review by XX
Step 4	Completion of the Transfer Pricing Masterfile						**Preparation of TP Masterfile report**	**Preparation of TP Masterfile report**	Draft & final TP Masterfile	TPA, review by XX
Project management and quality control										
Timing		**Week 1**	**Week 2**	**Week 3**	**Week 4**	**Week 5**	**Week 6**	**Week 7**		

Transfer Pricing Associates

Steps	Time and Scope Charter												Deliverable(s)	Responsible party
Step 1	Fact gathering												Draft APA Request	TPA & XX
Step 2		Analysis of facts												TPA, review by XX
Step 3			Determine appropriate TP policy											TPA, review by XX
Step 4				TP Documentation										TPA, review by XX
Step 5				Draft APA request										TPA, review by XX
Step 6								Prefiling meeting					Final draft APA Request	TPA
Step 7										Final APA request			Final APA Request	TPA
Step 8												Opening conference/meeting with APA team to discuss the request	Meeting/ Coordination with taxpayer and tax authority	TPA & XXX
Step 9												Questions and Answers		TPA & XXX
Step 10												Negotiations		TPA & XXX
Step 11												APA Agreement		TPA
Project management and quality control														
Timing	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Week 8	Week 9	Week 10	Week 11	Maximum two years		



Source: A Practical Guide to APAs, "Pan European APA – Request Process", Transfer Pricing Associates (2009).

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A Global Transfer Pricing Policy Paper

Your bridge to worldwide transfer pricing services

TPA Global

Transfer Pricing Policy Statement FY2011 BU X

POLICY: Transfer prices between the BU X companies shall be similar to those which would be agreed upon between independent parties. The basis used to establish prices shall be reviewed regularly and documented, and this documentation shall be retained for as many years as the relevant transactions are subject to review by fiscal or trade authorities.

PURPOSE: To ensure that transfer prices set for the transfers of goods, services and intangibles between BU X companies are consistent with Company X's long-term goals and with the tax and trade legislation of the countries involved.

RESPONSIBILITY: Each BU X company being a party to a transaction with another BU company is responsible for compliance with this policy.

BUSINESS MODEL: BU X is active in the field of [include BU industry description]

INTER-COMPANY TRANSACTIONS: The following visualizes the inter-company transactions covered by the policy: [Describe inter-company transactions]

CHOICE OF PRICING METHODS: BU X has selected the following most appropriate pricing method under the OECD Transfer Pricing Guidelines for the inter-company transactions mentioned above. The transfer pricing method that allows realization of the appropriate remuneration for the BU X entities is described below.

[Describe responsibility profile of the entities involved and the Transfer pricing method selected covered by this policy]

LEGAL FRAMEWORK: To capture the allocation of roles and responsibilities between the companies in the BU X and as part of the document of the transfer pricing system BU X companies have entered into the following agreements: [list agreements].

Appendix I: Introduction to Transfer Pricing Associates

The TPA Global group is an independent and specialist provider of expert transfer pricing, tax valuation and customs services, headquartered in Amsterdam and with our own offices and coverage in over 50 countries around the world.

Independent

- TPA is an independent firm
- No audit/attest work is carried out, only transfer pricing, customs and valuations services
- No conflicts of interest or corporate governance issues with Transfer Pricing Associates

Global

- TPA is present in 50+ countries through own offices and strategic alliances
- Global teaming/sharing model to allocate best expertise to projects/ clients - reduce delivery times
- Globally consistent top quality
- Continuity in leadership and pro- ject teams
- Running a steady, legally and operationally integrated network

Specialist

- Each TPA professional has at least 5 years of dedicated transfer pricing experience in:
  - 'Big 4'
  - Industry
  - Boutique consulting firms
- Global knowledge sharing
- Commitment to technical excellence

What are your benefits?

- Superior client service with quick turnaround
- "Senior professionals involvement" throughout projects
- A "hands on" approach to implementation issues
- Consistent global approach and performance
- Your best choice for global transfer pricing, tax valuation and customs solutions
- Coaching role: moves intelligence to corporates
- Low overheads and competitive pricing

Unique selling points

- Independent
- Global reach & staffing
- Senior staff at competitive fee
- Quick turnaround

- Tax authorities identifying “high risk transactions” and high risk industries.
- Increasing transparency due to increased disclosures and increased sophistication in revenue authority computer systems and search / data-matching capabilities; and
- Increased information sharing between revenue authorities.
- Managing your effective corporate income tax rate, i.e. for both overall profit and loss consolidated results.
- Aggressive tax authorities due to budget deficits.
- Need for control framework, i.e. talk to your business and IT professionals.
- Interplay between TP and customs / VAT / sales tax / withholding taxes.
- Special considerations for developing countries.
- Majority of transfer pricing documentation not (fully) aligned with multinational business model.
- High tax authority’s awareness on complex topics, e.g. business restructurings and intangibles.
- Special expertise requested by multinationals: year-end adjustment manuals, TP Software etc.

Appendix II: Comparability Analysis

- Characteristics of property or services
- Functional analysis
- Contractual terms
- Economic circumstances
- Business strategies

Step 1:	Determination of years to be covered.
Step 2:	Broad-based analysis of the taxpayer's circumstances.
Step 3:	Understanding the controlled transaction(s) under examination, based in particular on a functional analysis, in order to choose the tested party (where needed), the most appropriate transfer pricing method to the circumstances of the case, the financial indicator that will be tested (in the case of a transactional profit method), and to identify the significant comparability factors that should be taken into account.
Step 4:	Review of existing internal comparables, if any.
Step 5:	Determination of available sources of information on external comparables where such external comparables are needed taking into account their relative reliability.
Step 6:	Selection of the most appropriate transfer pricing method and, depending on the method, determination of the relevant financial indicator (e.g. determination of the relevant net profit indicator in case of a transactional net margin method).
Step 7:	Identification of potential comparables: determining the key characteristics to be met by any uncontrolled transaction in order to be regarded as potentially comparable, based on the relevant factors identified in Step 3 and in accordance with the comparability factors set forth at paragraphs 1.38-1.63.
Step 8:	Determination of and making comparability adjustments where appropriate.
Step 9:	Interpretation and use of data collected, determination of the arm's length remuneration.

Source: Excerpt from the OECD Transfer Pricing Guidelines Chapter III "Comparability analysis", published 22 July 2010.

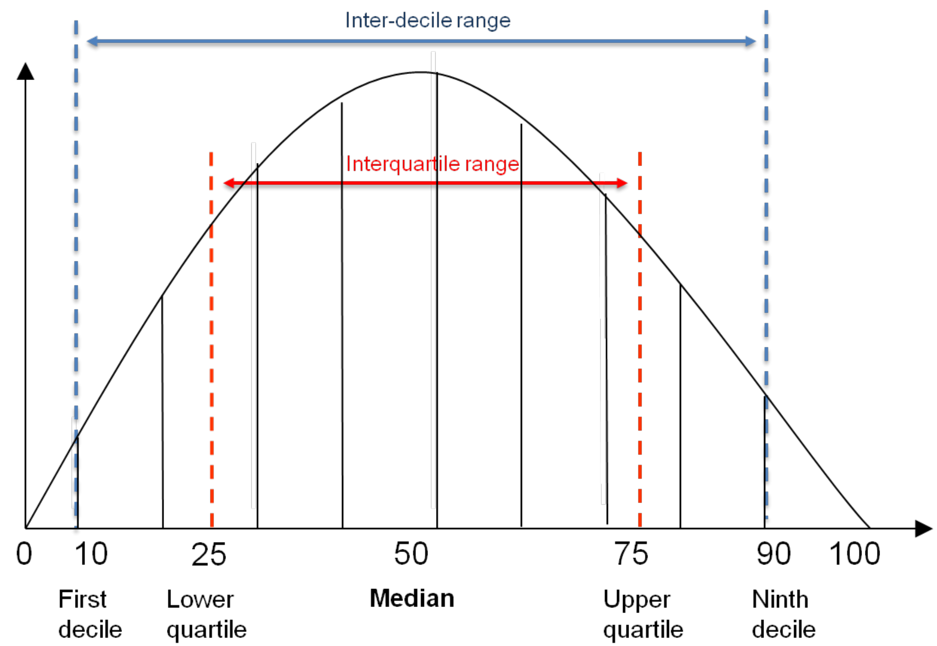
Arm's length range explanation:

- differences in the figures that comprise the range may be caused by the fact that in general the application of the arm's length principle only produces an approximation of conditions that would have been established between independent enterprises.
- different points in a range represent the fact that independent enterprises engaged in comparable transactions under comparable circumstances may not establish exactly the same price for the transaction.

Source: OECD Transfer Pricing Guidelines 2010

Statistical measures:

- Reason
- Application
- Mistakes



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- CUP method if one of two conditions is met:
  - none of the differences (if any) between the transactions being compared or between the enterprises undertaking those transactions could materially affect the price in the open market; or,
  - reasonably accurate adjustments can be made to eliminate the material effects of such differences.
- … similar type, quality, and quantity as those sold between two associated enterprises, assuming that the controlled and uncontrolled transactions occur at about the same time, at the same stage in the production/distribution chain, and under similar conditions.
- Practical considerations dictate a more flexible approach to enable the CUP method to be used and to be supplemented as necessary by other appropriate methods.

Source: OECD Transfer Pricing Guidelines 2010

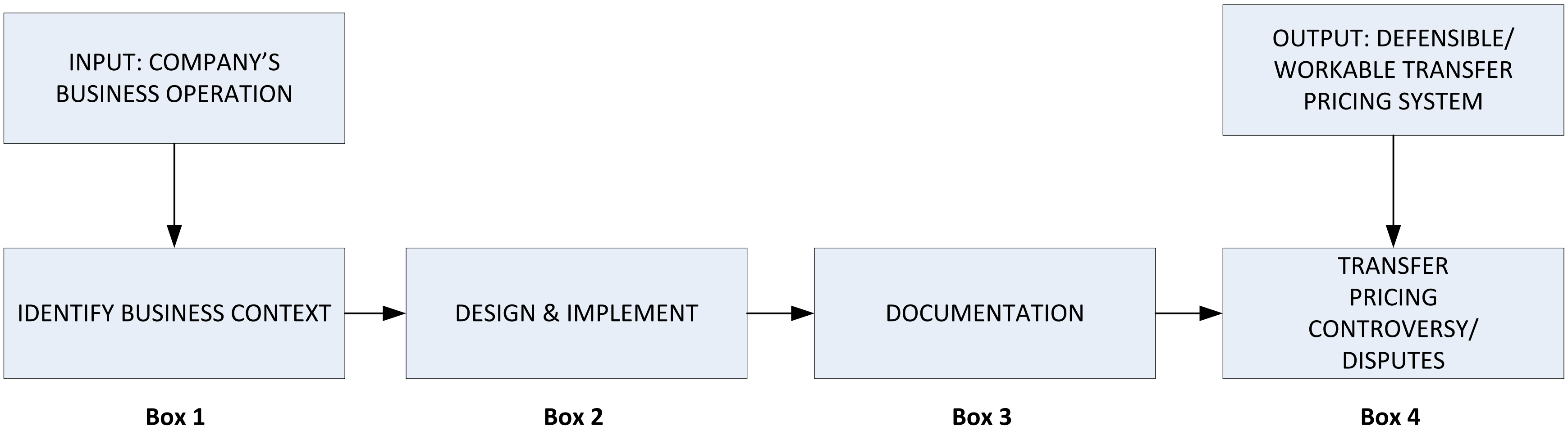
- Exact vs. inexact comparables
- CUP manual
- Price setting (real time) vs. price checking (period end)
- Tolerance range
- Application in the European TP setting

- For comparability analysis of loans the following factors have to be addressed:
  - Amount
  - Currency
  - Term
  - Secured or unsecured
  - Guarantees
  - Creditworthiness of the borrower
  - Situation in the financial markets

- Assessment of the creditworthiness can be done using methodologies/tools of the credit agencies: Moody's Investors Service, Standard & Poor's and FitchRatings
- Loan Connector and Bloomberg can be used to obtain market comparables
- Internal comparables: public corporate debt

Appendix III: Organizational Aspects of Transfer Pricing – TPA's Transfer Pricing Process

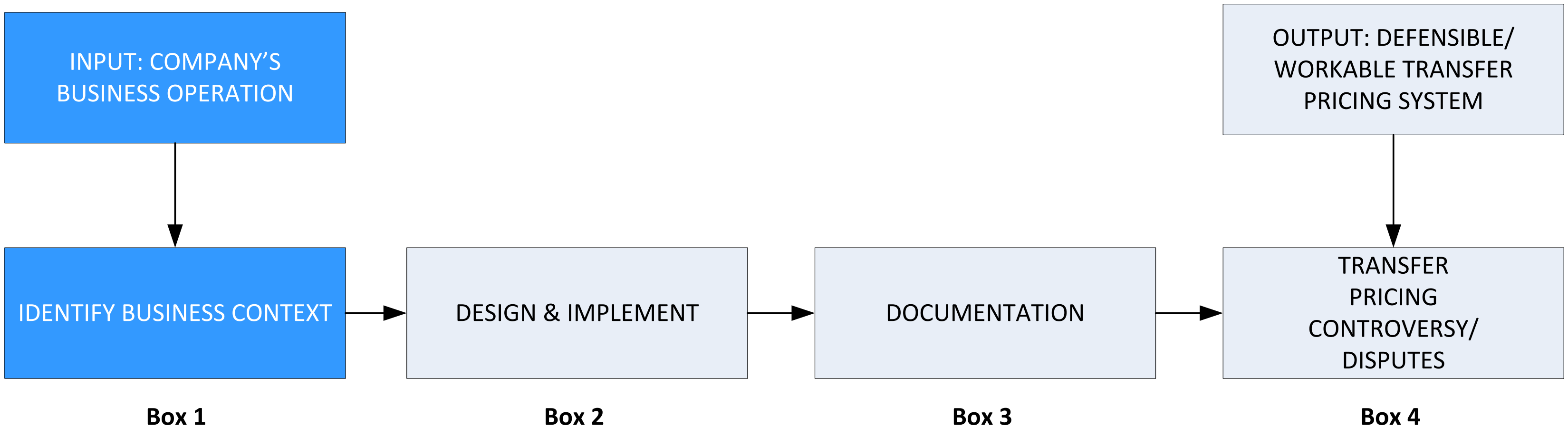
The following transfer pricing process has been developed by TPA as a structured manner to get from a 'business model' to a 'defensible and workable transfer pricing system', i.e. also referred to as the lifecycle of transfer pricing. It visualizes the necessary steps (see 4 boxes below) to obtain a systematic, scalable and user-friendly workflow approach to transfer pricing. Each of the following slides will indicate the practical steps to be taken within each of these boxes.



Addressing the following key issues:

1. How to identify the relevant business context
2. How to design an appropriate transfer pricing system and arrange for proper implementation
3. How to document the transfer pricing system
4. How to manage (pre-) controversy of the transfer pricing system

TPA’s Transfer Pricing Process | Identify Business Context



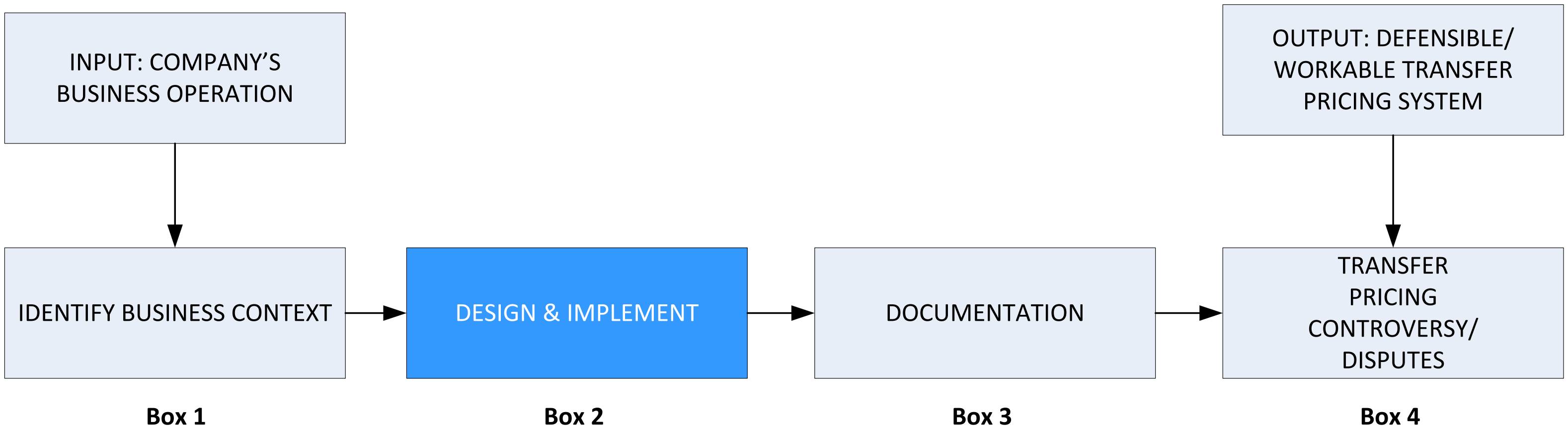
Box 1 requires MNE to define the 'value drivers' for each business unit, to understand which of the group entities should expect to be allocated the larger portions of the 'overall operating margin'. A workshop could be organized to invite the business unit tax manager to identify - using external and internal sources - the major value drivers within each of the business units.

Type of analysis:

- Industry analysis
- Functional analysis
- Commercial objectives
- Strengths and weaknesses
- Competitor analysis

Identification of the business context step includes:

- an analysis of the industry;
- identification of the MNE’s position within the industry;
- identification of competition;
- definition of the strategy applied by the MNE;
- definition of significant changes in the MNE’s business; and
- identification of the inter-company transactions, functions performed, assets used and risks assumed (functional analysis).



Box 2 requires MNE to define the relevant intercompany transactions from a business unit perspective and make an assessment of whether the current transfer pricing model is fully aligned with the current business model (and the 'value drivers' identified in Box 1).

In addition, to provide a generic 'Transfer Pricing policy' template, which is being used by many multinationals to communicate in a 1-4 page document their global transfer pricing policy.

Type of analysis:

- Responsibility centres
- Minimise overall tax rate
- Risk management
- Performance measurement
- Management
- Incentives
- Practicable system
- CUP manual

Design and implementation step comprises the following activities:

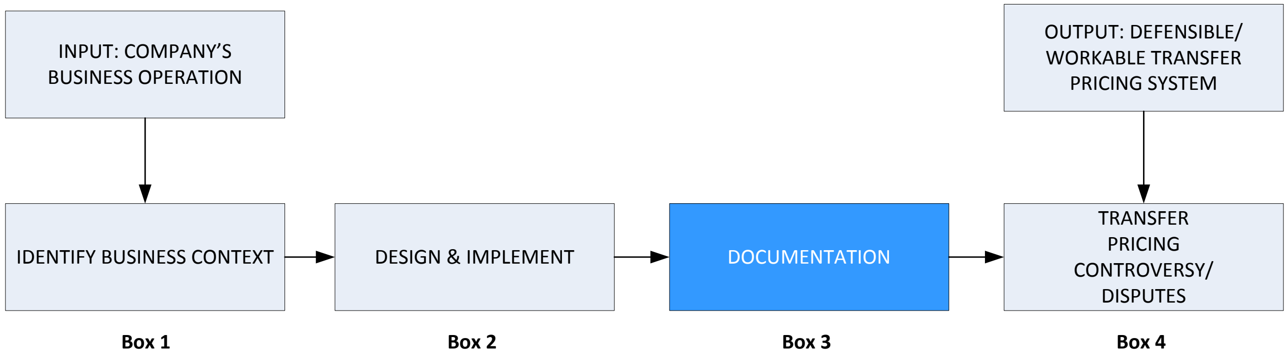
- Optimization and translation of the strategy into a practical structure allowing for: management of transfer-pricing risks, which consists of an alignment of the economic, legal and accounting reality of the MNE's business; performance of the MNE, and tax position and incentives.
- Use of the responsibility-centre concept to allocate the various roles and responsibilities performed by each group company. The number of labels attributable to a legal entity depends on the number of activities performed. A responsibility profile is determined per activity. Responsibility-centre labels enable the MNE to design an appropriate method for compensating each of the group companies.
- The drafting of inter-company agreements.
- The determination of journal entries for the MNE's budget and statutory books.

Through implementation and compliance services

Implementation	Compliance
• Draft, sign & implement an intellectual property policy	• Provide and assess country risk for all countries (country risk matrix)
• Draft, sign & implement a transfer pricing policy	• Draft, complete and sign all relevant transfer pricing compliance forms on a country-by-country basis
• Draft, sign & implement a year-end adjustment manual	• Annual check and updates of intercompany agreements
• Draft, sign & implement a (series of) intercompany agreement	• Align "legal reality" with "economic reality" i.e. business model
• Draft, assess & implement managerial aspects of transfer pricing systems (e.g. KPIs for bonus)	• Customs scan and audit program (e.g. CTPAT & AEO)

Addressing the following key issues:

1. Does your IT system support your TP system?
2. What (amendments of) legal agreement/s are needed?
3. How to monitor compliance?
4. How to keep track of relevant business developments?



Box 3 requires to define the need for (i) global documentation (e.g. captive insurance transfer pricing report AND treasury transfer pricing policy) (ii) regional documentation (e.g. sales and marketing margin for EU region captured in a so called pan-European master file) (iii) local country files (e.g. making an assessment on which type/level of local files are required to be compliant with the local legislation) (iv) transaction specific documentation (e.g. financial intermediary vehicles in most jurisdictions would require some documentation to support the arm’s length nature of the margin) (v) specific disclosure and transparency requirements towards tax authorities (e.g. various local forms as Appendix to local corporate income tax returns).

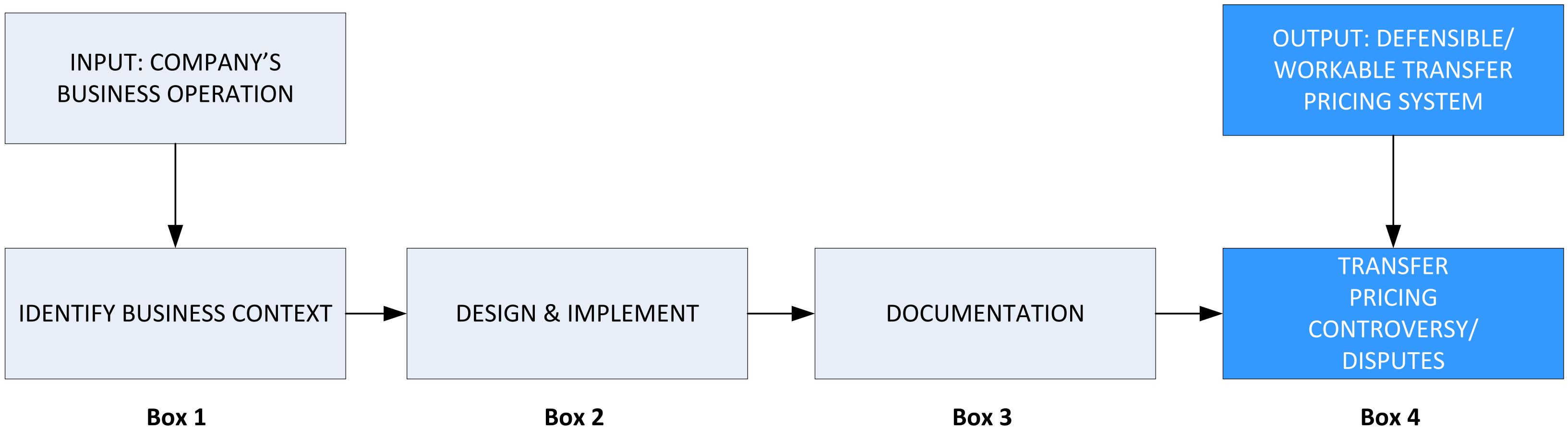
Type of analysis:

- Master file documentation
- Local documentation
- Inter-company agreements
- Third party references
- Evidence of arm’s length behavior
- Investment decisions

Documentation step consists of documenting the findings resulting from Box 1 and Box 2, reflecting the dynamics in the industry and the value chain of the multinational, including the applicable transfer-pricing policy and the economic analysis supporting the arm’s length character of the identified inter-company transactions.

- Companies required to disclose controlled transactions in annexure to tax filings.
- Threshold filters are in place in certain jurisdictions.
- Transfer Pricing method needs to be disclosed in the statutory filing in certain jurisdictions.
- Certain jurisdictions require independent verification of Transfer Pricing methodologies by a public accountant.
- Summary of income statements of overseas affiliates to be disclosed in the Transfer Pricing disclosure forms.
- Tax authorities gather information for risk assessment, also use public sources
- Risk assessment software, pre-defined issues (focus on IP transfers, business closure)
- Use of local databases and secret comparables

Conclusion: Global transfer pricing disclosure forms pose a significant compliance burden for multinationals.



To define your strategy on conflict avoidance and conflict resolution, the following considerations would have to be taken into account:

- Focus and appetite on transparency and disclosure;
- Define a policy on the use of conflict resolution instruments like APAs (rollback) and Mutual Agreement Procedures; and
- TPA has published a book APAs - a practice guide.

Type of analysis:

- Transfer pricing audit
- Competent authority
- Arbitration
- Advance Pricing agreements (APAs)

Transfer-pricing pre-controversy management step could include:

- managing the risks identified in Box 1, 2, 3 and 4, through adjustments in the business or adding more layers of support relating to an identified high-risk transaction or lack of appropriate documentation;
- use of APAs, litigation or arbitration to further minimize risk and reduce the possibility of double taxation;
- if the external auditor and/or tax authorities ask the MNE to explain its transfer pricing system, the documentation under step 3 can be wholly or partially (in so far as relevant) disclosed. The MNE is responsible for defining a clear strategy on how to approach such audits, for example, with regard to such questions as: Who is the main line of communication with the tax authorities? Should the external auditor share his working papers with the tax authorities?

BY PROPER PREPARATION AND GUIDANCE

Through conflict avoidance

Pre-audit/ provisioning

APA

Through process management

Audit

Through process management

MAP

Litigation

Addressing the following key issues:

1. What are the options available?
2. What is your 'risk appetite'?
3. What is your best controversy strategy?
4. How to best negotiate with tax authorities?

- Topics covered: intangibles, valuation, PE risks, sales commission, duplication, business restructuring, marketing spend, headquarter charges, intercompany loans and guarantee fees.
- Hotspots of aggression: Germany, Denmark, France, Italy, Canada, USA, Australia, Korea, China, India, Indonesia and Brazil.
- Countries where we have seen activity: 15 countries in Europe, Australia, Indonesia, China, Vietnam, USA, Canada.

- Adopt a global approach to tax risk and controversy management;
- Evaluate global resources, processes and systems for tax risk management;
- Address tax risk and controversy at a strategic level;
- Make strong corporate governance in tax a priority;
- Stay connected with global legislative, regulatory and tax administration changes.

- Tax authorities around the world become more aggressive and focused: see our hot spots!
- High pace of legislative change creates more risk and uncertainty: each week a new set of TP legislation and/or updates are published;
- Growing disclosure and transparency requirements: being exposed!
- Expansion in emerging markets is creating tax risk and uncertainty: how will the BRIC act?
- A new breed of tax activism emerges: the fatal impact of media on corporate image!
- Enhanced relationships opportunities are spreading: how do you communicate and interact with your tax inspector?

- Define areas of 'dispute' in transfer pricing, customs and/or valuation matters;
- Agree with client on 'case management' plan to resolve the 'dispute';
- Determine a 'critical time path' to get to a resolution;
- Choose the 'best available controversy toolbox' and 'controversy team' to handle the case; and
- Leverage from own resources and 'extended global controversy network' offered by a firm like TPA.

Appendix IV: List of I/C Agreement Templates

- Commissionaire Agreement
- Consignment Manufacturing Agreement
- Contract with a Commercial Agent
- Cost Contribution Agreement
- General Service Agreement
- Intercompany Development Agreement
- Limited Risk Distributor Agreement
- Procurement Agreement
- Production and Supply Agreement
- Production Coordination Services Agreement
- Sales and Marketing Service Agreement
- Sales and Purchase Agreement
- Trademark License and Distribution Agreement

About Transfer Pricing Associates

Transfer Pricing Associates is the leading independent provider of global transfer pricing and valuation services and part of the Transfer Pricing Associates Global group. The Transfer Pricing Associates Global group is an independent and specialist provider of expert transfer pricing, tax valuation and customs services, headquartered in Amsterdam and with our own offices and coverage in over 50 countries around the world.

Transfer Pricing Associates provides high quality transfer pricing advice and assistance to multinationals of all sizes, wherever they are located. For more details of our innovative services, please visit our website at

www.tpa-global.com