

Transfer Pricing Guide



IRS GUIDELINES



A TRUSTED AND TAILORED APPROACH



CASE STUDY: CANADIAN PARENT'S MANAGEMENT FEE



CASE STUDY: TRANSFERRING CAPITAL OVERSEAS



Is a Transfer Pricing Study *Necessary*?

As Froehling Anderson and McGuire Sponsel continue helping clients navigate increasingly complex international tax matters, transfer pricing conversations inevitably arise. Transfer pricing conversations typically center on why a study is needed, how often to perform a study, and whether contemporaneous documentation requirements have been met.

DO YOUR CLIENT'S TAX RETURNS INCLUDE THESE FORMS?

Form 5471: Information Return of U.S. Persons With Respect to Certain Foreign Corporations. The form is titled 'Form 5471' and 'Information Return of U.S. Persons With Respect to Certain Foreign Corporations'. It includes the Department of the Treasury Internal Revenue Service logo and a table with multiple rows and columns for reporting.Form 5472: Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. The form is titled 'Form 5472' and 'Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business'. It includes the Department of the Treasury Internal Revenue Service logo and a table with multiple rows and columns for reporting.

5471

OR

5472

When reporting transactions with a related foreign party, it is essential to have a transfer pricing study in place on the date the client files the return.



IRS Guidelines

IRS transfer pricing rules set forth in IRC Section 482 and Section 6662 require that intercompany pricing between a United States company and a foreign affiliate must be based on an “arm’s length” price charged in a similar transaction with an unrelated third party.

To support the arm’s length nature of the transaction and avoid transfer pricing penalties, a company must provide contemporaneous documentation to substantiate its transfer pricing methodology.

Further, that contemporaneous documentation should be in the form of a transfer pricing opinion (or “study”) benchmarking comparable transactions.

Study *Misconceptions*

Generally, when a CPA identifies transfer pricing issues, clients shy away from completing a formal study based on preconceived notions that a study is:

- ⊗ expensive
- ⊗ time-consuming
- ⊗ only for large, multinational corporations
- ⊗ a 100-plus page deliverable

Our Approach

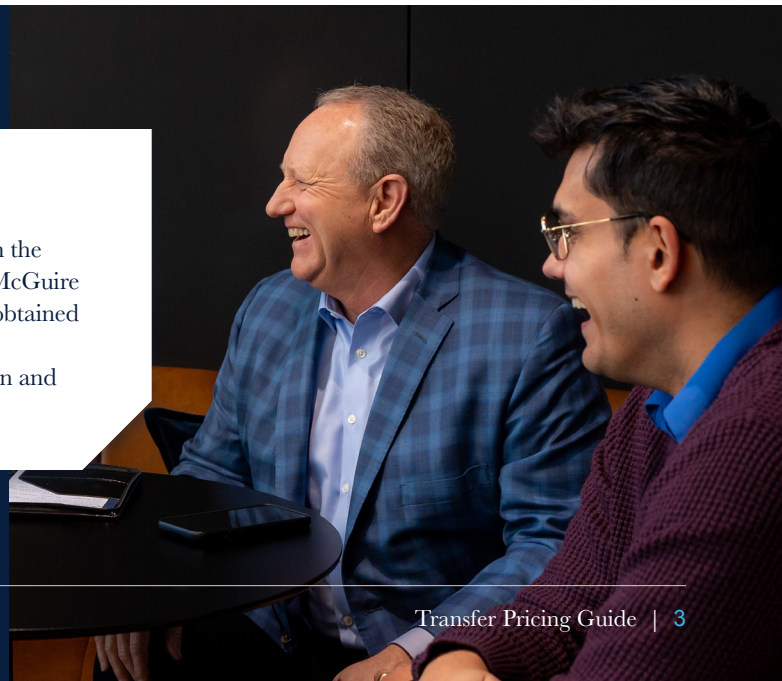
Transfer pricing studies do not need to be costly and time-consuming. In fact, the IRS gives guidance in Section 6662, providing a table of contents identifying requirements for a transfer pricing study. Our common sense approach to transfer pricing is:

- ✓ trusted and tailored to your business
- ✓ logical and efficient
- ✓ reduces exposure in the event of an audit
- ✓ generally, produced in 15-25 page deliverable
- ✓ satisfies the statutory requirements of IRC 6662



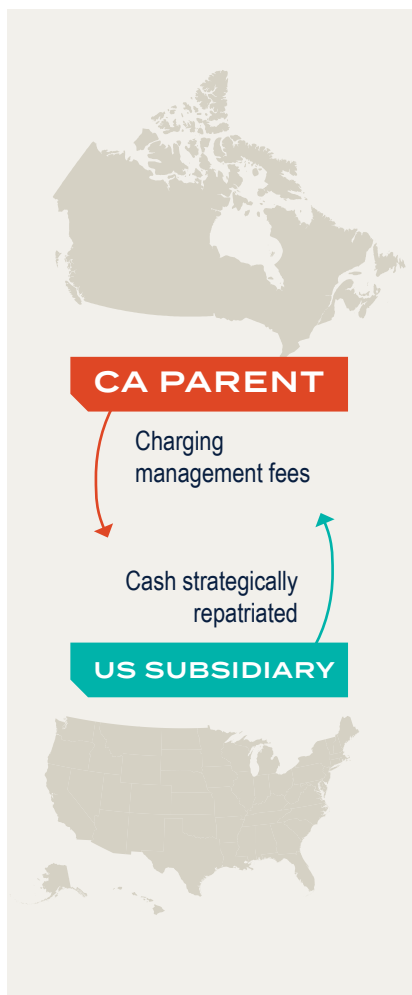
PARTNER WITH US

If a client completed a transfer pricing study in the past and it is time to update, the transition to McGuire Sponsel can be seamless. If a client has never obtained a transfer pricing study and needs guidance to understand the “whys,” the Froehling Anderson and McGuire Sponsel teams are here to assist.



CASE STUDY

Canadian Parent's Management Fee



Background

McGuire Sponsel conducted an in-depth transfer pricing study on a scenario involving a Canadian parent entity charging management fees to its U.S. subsidiary. We assessed whether the fees were aligned with the arm's length principle by evaluating the tangible value added through centralized management, strategy, and operational support provided by the Canadian parent.

Our analysis confirmed that the management services were not only critical in enhancing the U.S. subsidiary's operational efficiency and competitive position, but they also justified the cash moving strategy whereby cash is strategically repatriated from the U.S. subsidiary to the Canadian parent. This approach allowed the group to:

- ✓ optimize global tax positions
- ✓ ensure liquidity in the higher-tax U.S. jurisdiction
- ✓ capitalize on more favorable tax conditions in Canada

Using a combination of functional analysis, comparability studies, and benchmarking techniques, we verified that the management fee, determined via a cost-plus method adjusted for the value added, was consistent with what independent service providers would charge under similar circumstances.



RESULTS

Our study underscores the importance of robust documentation and economic substance in defending the intercompany arrangements, ensuring that the transfer pricing policy not only supports operational goals but also aligns with both local and international tax regulations.

Transferring Capital Overseas



Parent HQ in China



U.S. based subsidiary



Maintenance and repair (China)

SALES

MGMT FEE



Product Sales (U.S.)

RESELLING



\$4.5M
transferred

↘ TAX RATE



Background

A West Coast CPA firm sought McGuire Sponsel's counsel on cross-border intercompany transactions for a client that designs and manufactures power generators. The multinational firm's structure includes a parent headquartered in China and a U.S. based subsidiary. The parent maintained healthy liquidity in the U.S., but ultimately wanted to justify retaining more money in China.

Strategy

After reviewing the legal agreements between the related parties as well as the group's financials, we discovered maintenance and repair services of US-sold products were still performed in China and were an integral part of the business. We performed a transfer pricing study to examine comparable organizations with similar models, which yielded an ability to retain more earnings in China. This analysis supported the Chinese parent's ability to charge a fee to the subsidiary for these essential services.

RESULTS

This transfer pricing study resulted in moving \$4.5M from the US subsidiary to the Chinese parent, lowered the global effective tax rate, and met the group's goal of having more cash at the parent level.

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ON-DEMAND WEBINAR

[Understanding Transfer Pricing:
Identifying Companies in Need](#)



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