



Global TP Risk Management

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I. Introduction to corporate governance and TP

Reality

- A record surge of data disclosure and accounting fraud scandals
- Economic stagnation, squeezed costs and a shrinking domestic market
- Risk management structure in place, but control mechanism is weak
- Different stakeholders, different expectations

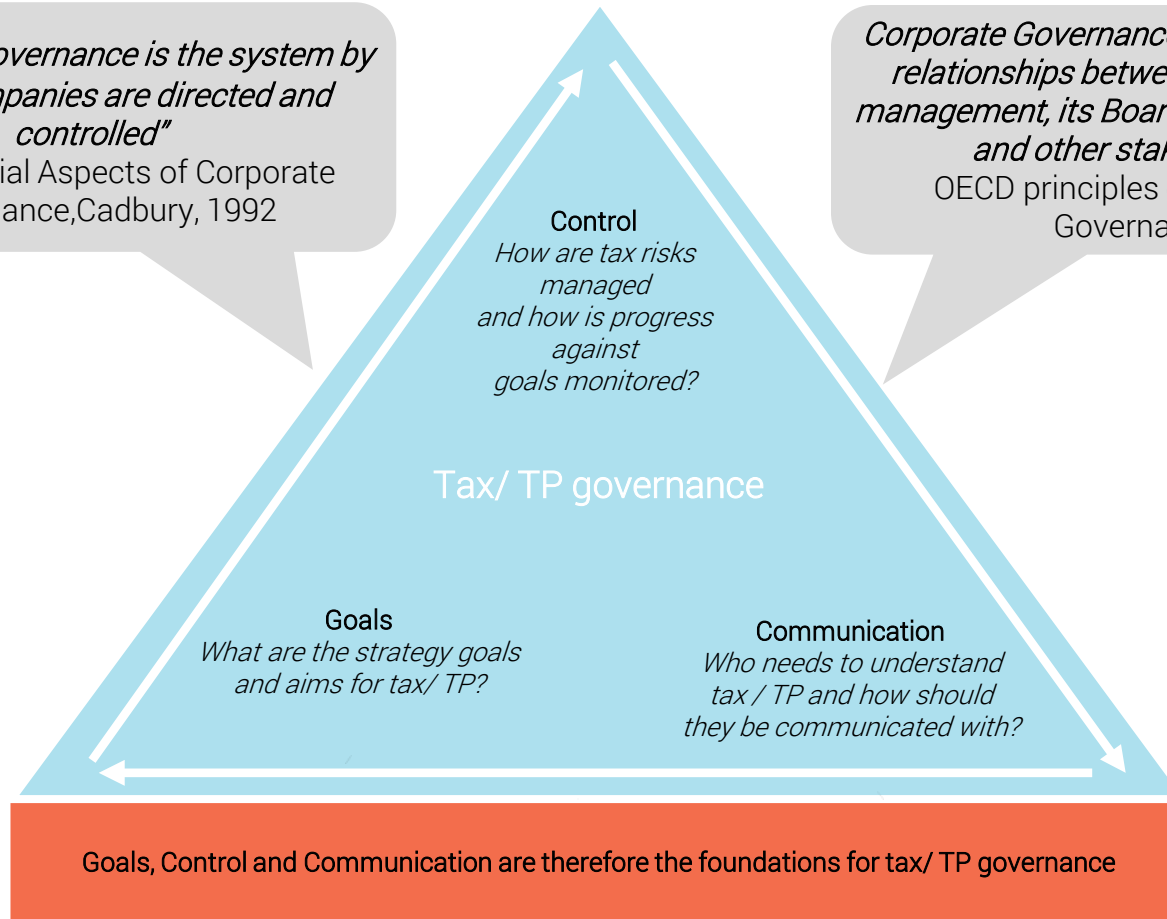
What is Tax/ TP governance?

"Corporate Governance is the system by which companies are directed and controlled"

The Financial Aspects of Corporate Governance, Cadbury, 1992

Corporate Governance involves a set of relationships between a company's management, its Board, its shareholders and other stakeholders"

OECD principles of Corporate Governance

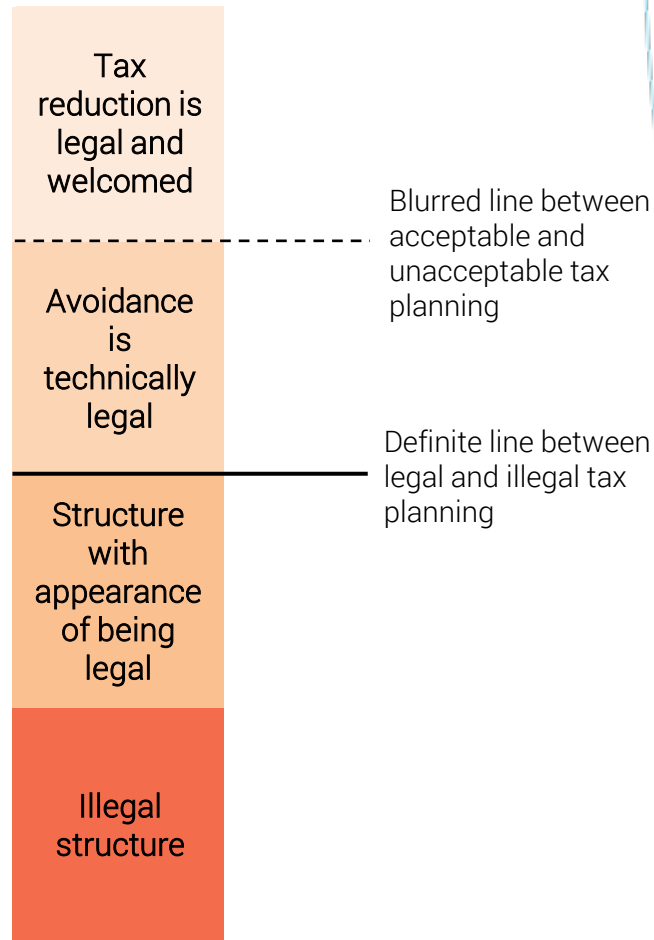


The dilemma of management board: alignment of various stakeholders' needs

Nr	Stakeholder	Expectations	Tax responsibility
1	Shareholders/investors	Net profit	Optimize tax position
2	Analysts, Banks	Transparency	ETR/Tax cash/Risk
3	Tax Authorities	Cost reduction audits Fair share	Enhanced relationship Compliance with tax laws
4	Supervisory Authorities	Solvency 2 / Basel 3 (Financial institutions)	Equity forecasting (deferred tax assets/liabilities)
5	Audit Committee	No (tax) surprises	Tax reporting/Communication
6	Supervisory and Management Board	Reputation Solid tax position	Tax strategy / Tax risk management
7	External Auditor / Internal Audit	Reasonable tax assurance (no claims)	Monitoring effectiveness Tax Governance Framework
8	Public society	Fair share	Tax Communication

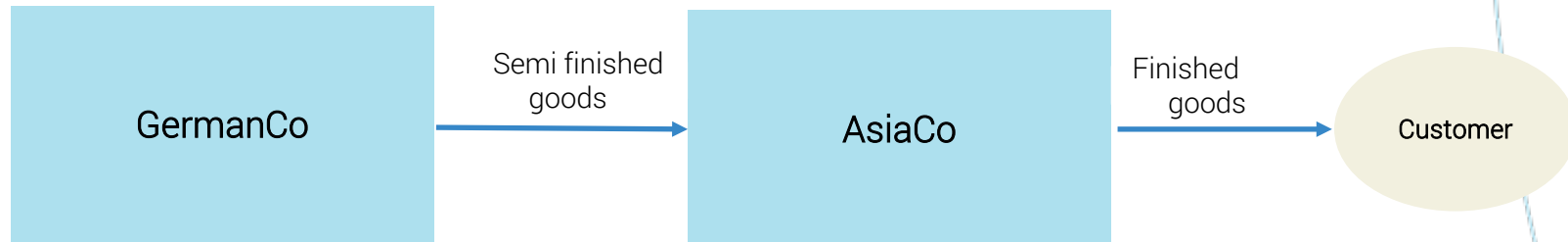
A call for corporate responsibility agenda on Tax

- Financial reporting alone no longer satisfies the needs of the various stakeholders that have an interest in it
- Tax is not simply a legal concept, ethical values can and should be considered
- Tax evasion versus tax avoidance: what is acceptable tax planning?



II. Examples

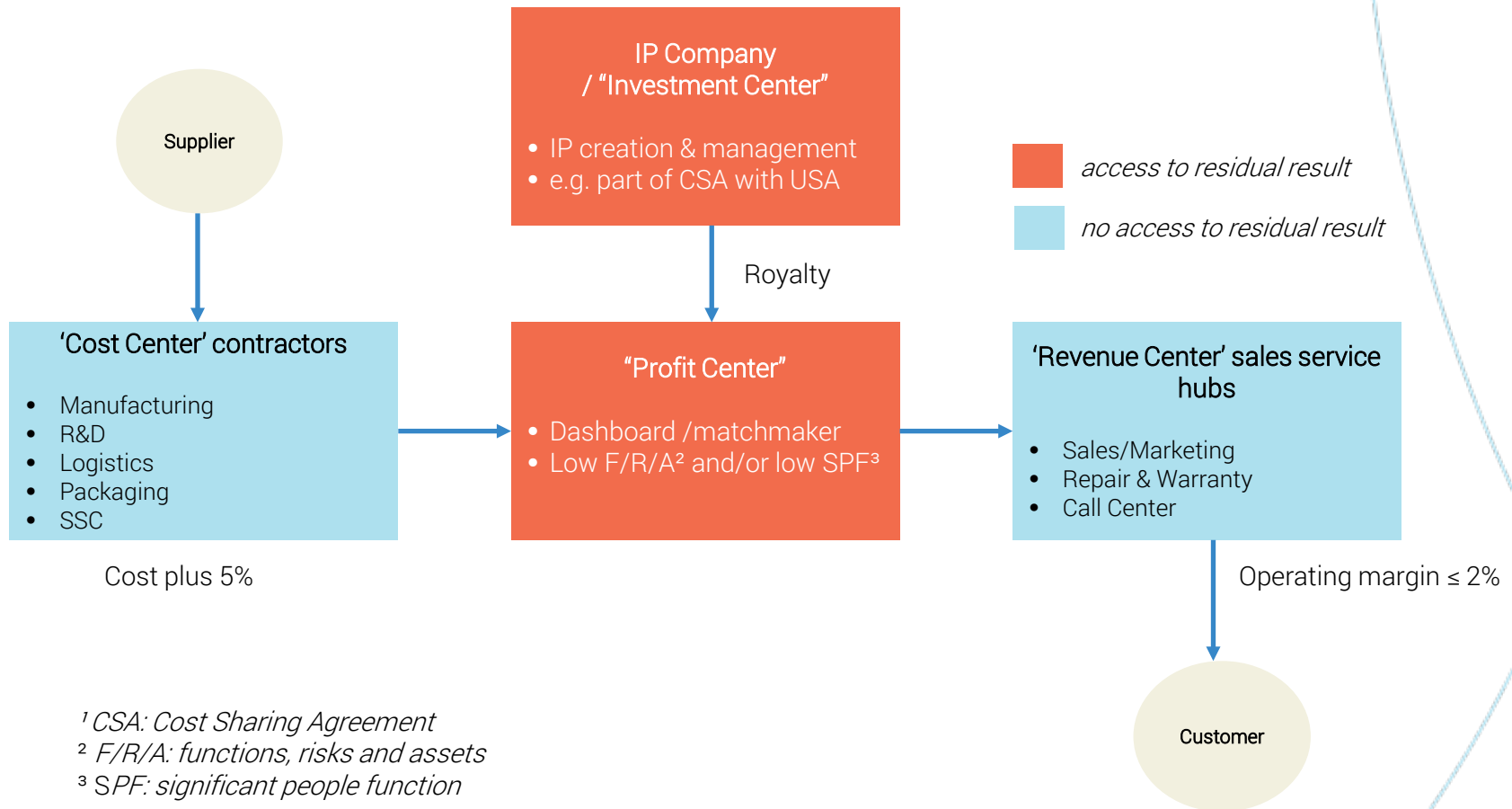
Contemporaneous documentation



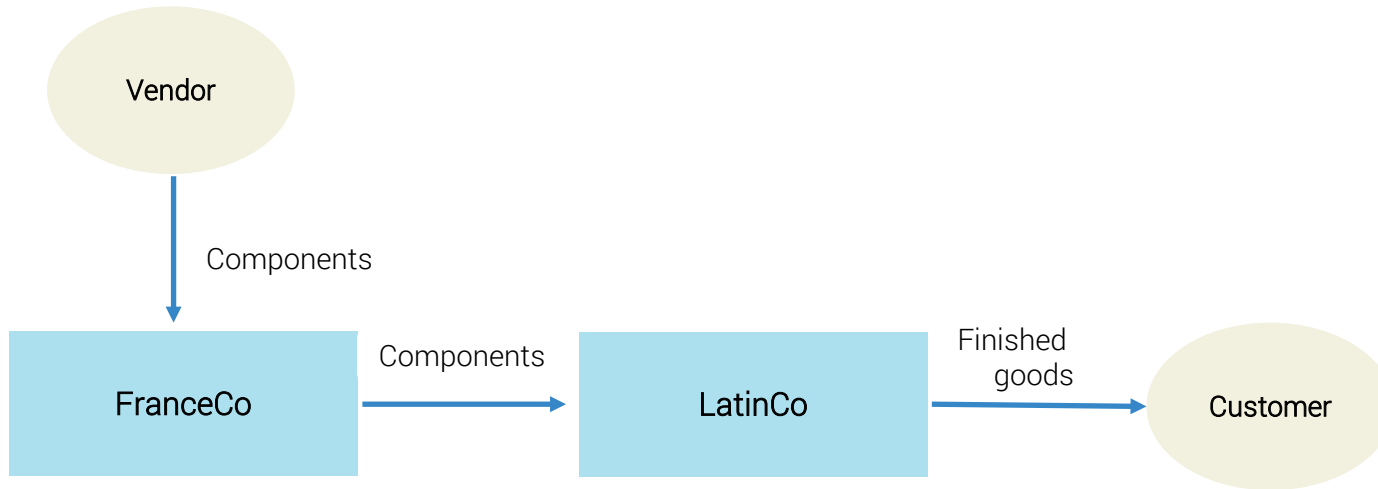
- TP documentation not prepared contemporaneously
- The MD assumed the responsibility for signing off documentation and TP forms
- Local consultant with general tax knowledge managed transfer pricing AsiaCo

Centralized business configurations are under fire - red zone

> 50% overall operating margin = "white income"



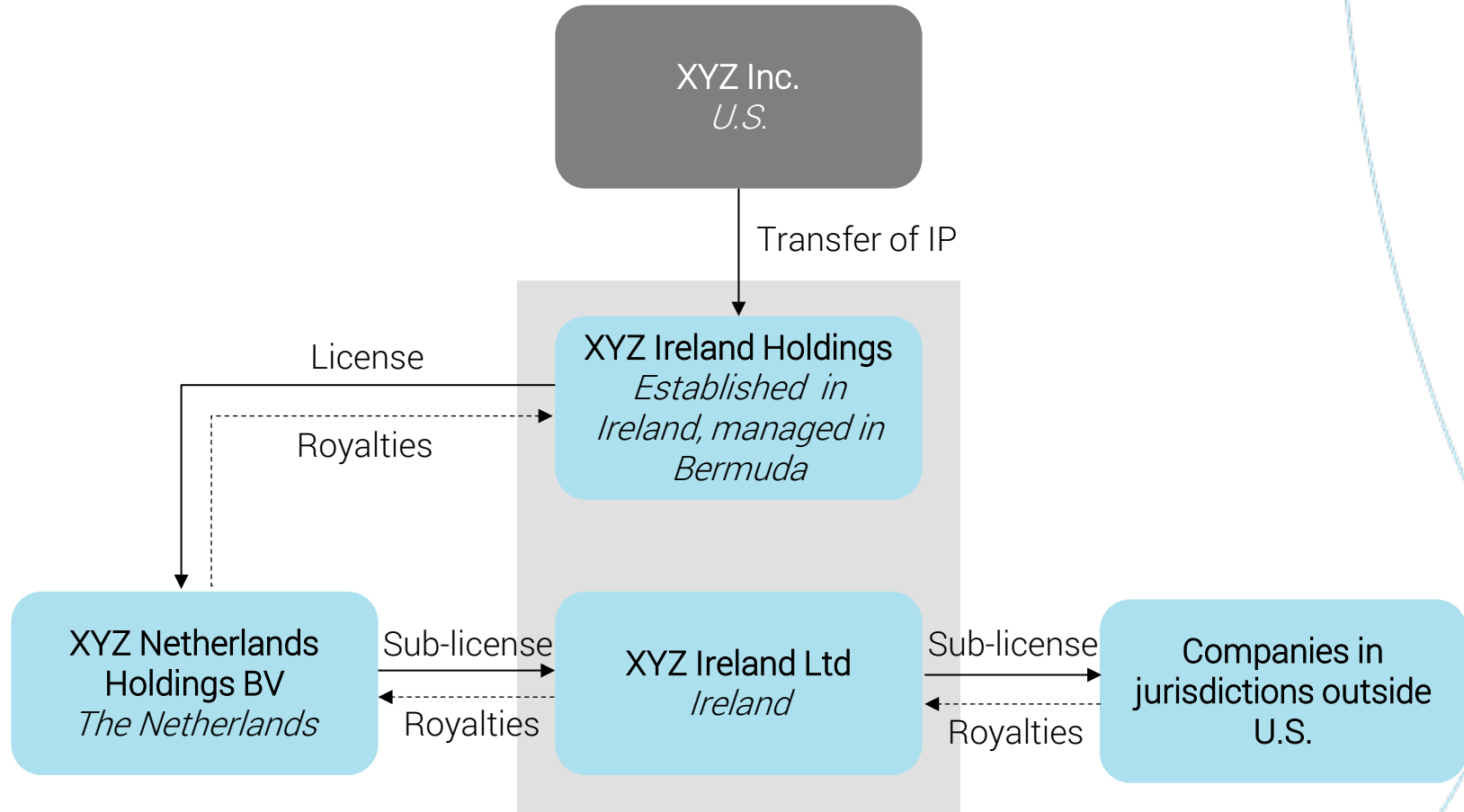
Audit trail



- LatinCo was a JV
- After the foreign partner acquiring the local partner's stake in the JV, major audit proceedings started
- CUP method applied to justify intercompany pricing
- Audit trail was not maintained at the time of preparing TP documentation

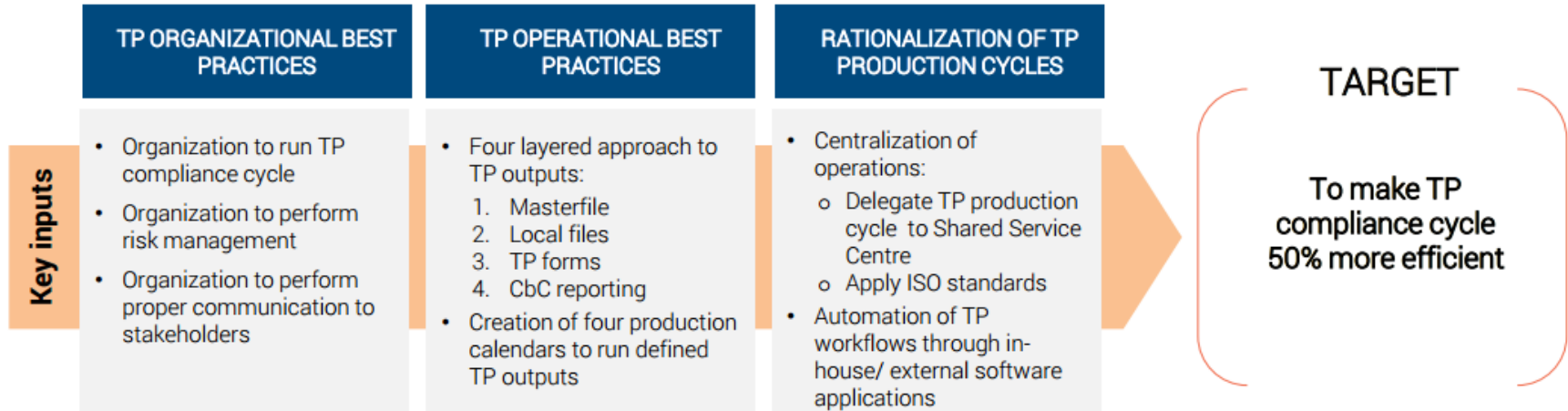
Leakage example: Non-US IP rights structured through a hybrid entity

What is all the fuss about?



III. TPA's practical approach to Tax governance

Introduction – TPA Global approach to moving Clients' TP compliance cycles towards higher efficiency



BEPS compliant organisation + automated software solutions = increased process and compliance efficiency by >50%

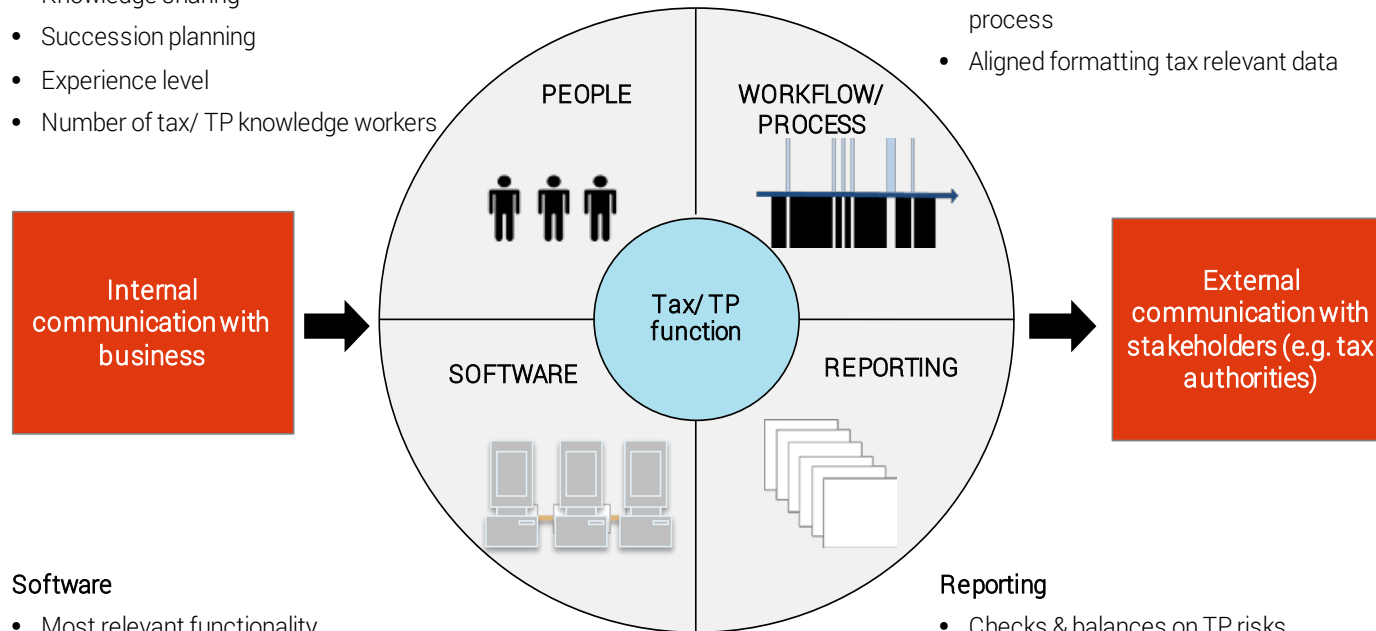
TPA's approach – general Tax/TP control framework

People

- Performance measurement
- Geographical spread of knowledge workers
- Knowledge sharing
- Succession planning
- Experience level
- Number of tax/ TP knowledge workers

Workflow

- Global benchmarking process
- Document management process
- Financial data retrieval and conversion process
- Aligned formatting tax relevant data



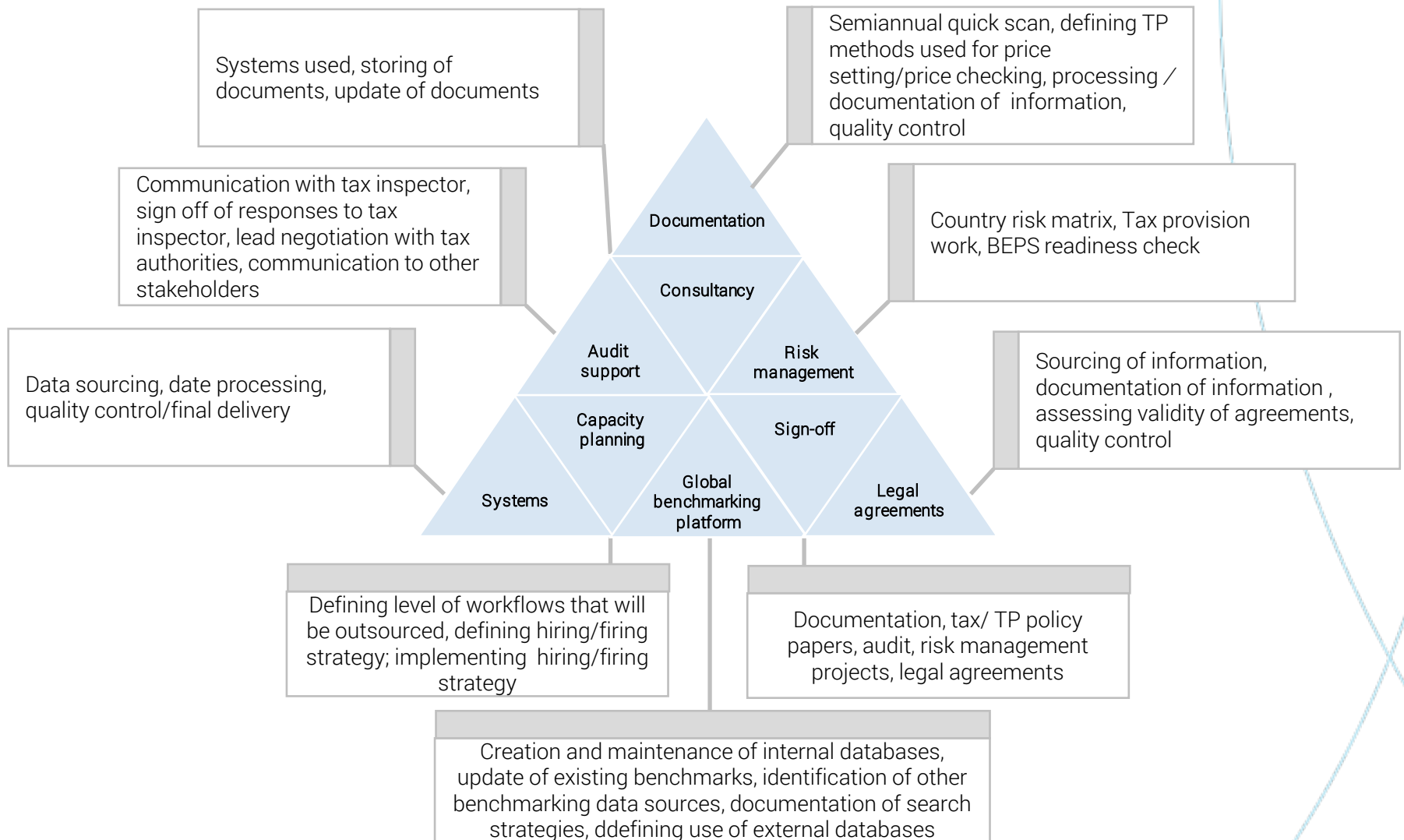
Software

- Most relevant functionality
- Tax/ TP specific storage platform
- Alternative software solutions

Reporting

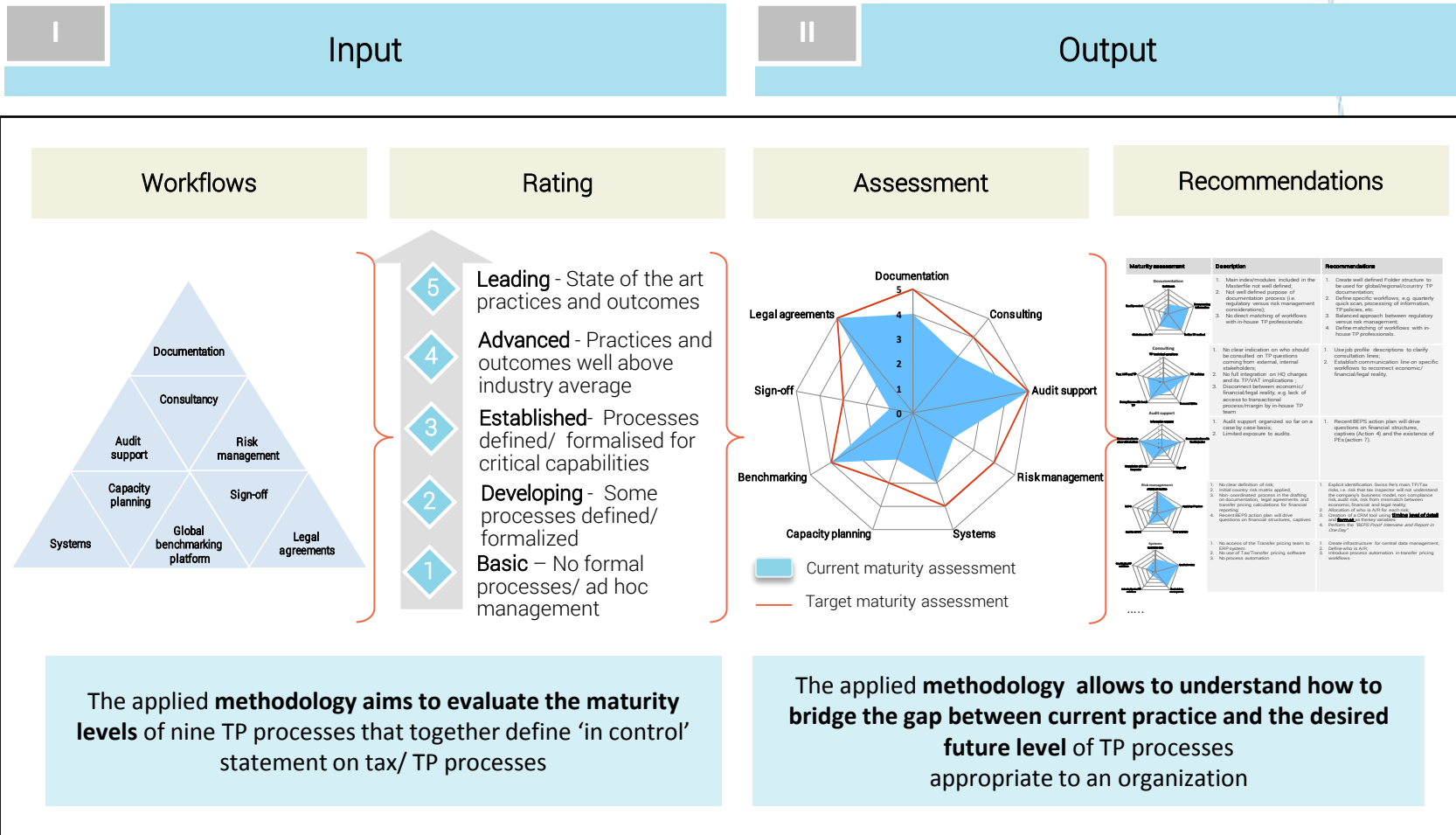
- Checks & balances on TP risks
- Interaction central tax/TP – local tax/TP team
- "Dashboard" for CFO
- Responsibility/accountability
- Tax/TP policy paper

Nine building blocks of a successful TP function



IV. TP “in control” assessment

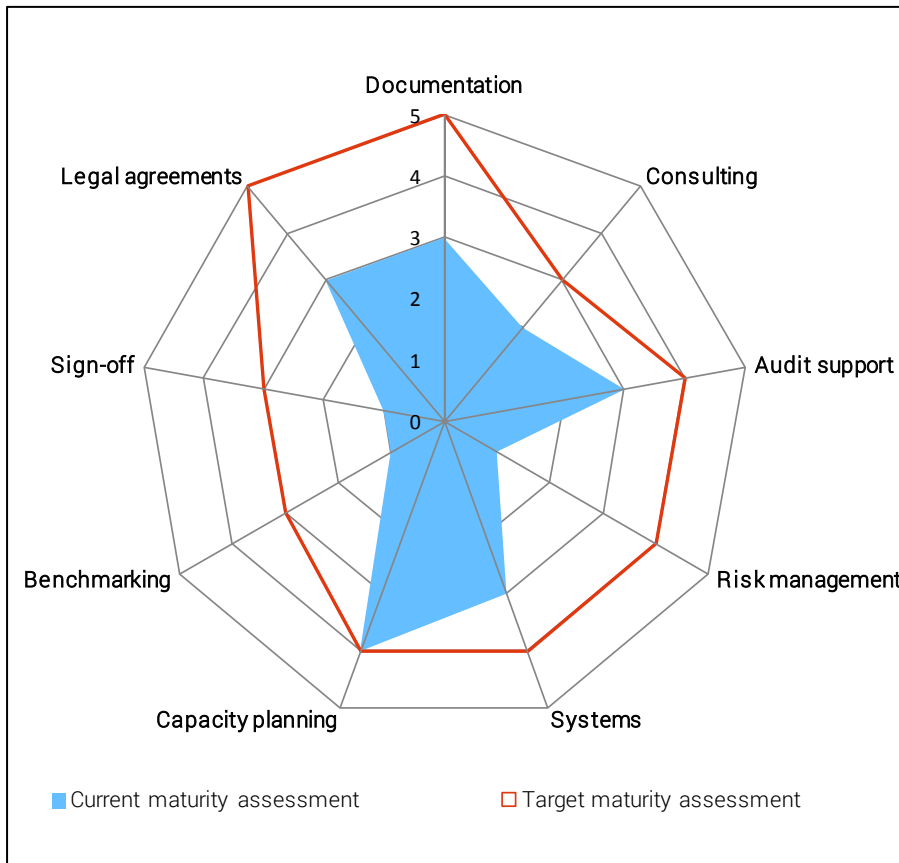
TP “in control” assessment: How it works in practice?



Eventually, the aggregated result of the assessment is transformed into meaningful and predictive insights

illustrative

MNE's TP processes maturity assessment



Key insights

Documentation: Not well defined purpose of documentation process

Consulting: Disconnect between economic, financial and legal realities

Audit support: organized on case by case basis

Risk management: No clear definition of risk, non-coordinated process in drafting documentation, legal agreements, and TP calculations for financial reporting

Systems: No use of tax/ TP software, no process automation, no access of the TP team to ERP system

Capacity planning: No clear definition on who is accountable/ responsible for hiring outside resources

Benchmarking: Fragmented approach to benchmarking (a lot of service providers), undefined level of use of external versus internal databases, unclear connection between the outcome of benchmarks and I/C transactions

Sign-off: No defined responsibility on sign-off processes

Legal agreements: delivery terms for transactions between HQ and branches are not properly defined

Example of next steps: “Close the gaps”

illustrative

Workflow	Maturity assessment	Key insights	Recommendations
Risk management	1 → 4	<ol style="list-style-type: none"> 1. No clear definition of risk; 2. Initial country risk matrix applied; 3. Non- coordinated process in the drafting on documentation, legal agreements and transfer pricing calculations for financial reporting; 4. Recent BEPS action plan will drive questions on financial structures, captives 	<ol style="list-style-type: none"> 1. Explicit identification main TP/Tax risks, i.e. risk that tax inspector will not understand the company’s business model, non compliance risk, audit risk, risk from mismatch between economic, financial and legal reality; 2. Allocation of who is A/R for each risk; 3. Creation of a CRM tool using timing, level of detail and format as the key variables 4. Perform the “<i>BEPS Proof Interview and Report in One Day</i>”
Global benchmarking platform	1 → 3	<ol style="list-style-type: none"> 1. Fragmented approach to benchmarking. A lot of service providers; 2. Undefined level of use of external vs internal databases (i.e. a number of internal databases and internal pricing models already available by business teams).; 3. Unclear connection between outcome of benchmarks and intercompany transactions for accounting 	<ol style="list-style-type: none"> 1. Central management through development and maintenance of a Global; Benchmarking platform; 2. Establish holistic view on how the different transfer prices fit the profitability of the entire group. 3. TP central team to explicitly define use of external databases
Sign-off	1 → 3	<ol style="list-style-type: none"> 1. Non defined responsibility on Sign-off process 	<ol style="list-style-type: none"> 1. Sing-off process to be managed centrally

Potential benefits of TP governance assessment

I. Process

1. Assess "as is" status of TP processes

2. Define "to be" status of TP processes

3. Identify the gaps between "as is" and "to be"

4. Develop an action plan

TP "in control" assessment evaluates internal TP function performance, identifies performance gaps and develops an action plan on how to address these gaps

II. Key benefits

Being in control:

- Enhances risk management: brings more certainty about existing and future TP position & TP processes
- Ensures better planning: calls for responsible and quantified tax/ TP planning)

Transparency:

- Steers behavior: directs behavior of the tax people to the right direction
- Improves communication: encourages facts-based communicate to your both internal and external stakeholders

Serves as a catalyst for efficiency in the (Tax/ TP) organization and continuous development

Lessons learned– Are you in Control?

Pro-active:

- Have your corporate governance model in place;
- Have your TCF/TPCF in place;
- Have your finance tax/transfer pricing/intellectual property policy fully documented;
- Proper and timely implementation of your policies should synchronize your realities: economic reality = legal reality = financial/accounting reality;
- Strive for transparency, but control your channel and intensity of communication;
- Stick to your business model; i.e. make a BEPS proof “value chain” analysis
- Have your media/press communication protocol, including media training, ready for use;
- Reassess your “economic substance”, e.g. do a BEPS readiness test

Re-active:

- Cost plus 5% could become Cost plus 15%?
- Operating margins for distributors of less than 2-4% are dangerous, unless your whole value chain makes less than 4-8%?
- What is the “right” balance between favorable tax regimes and “economic substance”

Q & A

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Appendix A – Illustration of TP “in control” assessment questions

Examples of TP “in control” assessment questions (1/3)

Development/ maintenance of TP documentation

Sub-workflow	Question	As is	To be	1 - Basic	2 - Developing	3 - Established	4 - Advanced	5 - Leading
Processing/ documenting TP information	To what extent are procedures around TP information processing and documentation structured?	3	5	No organizational capability to process/document TP information. Lack of clear definition of roles/responsibilities for processing/documenting TP information	Limited capability to process/document TP information. Poorly defined roles/responsibilities for processing/documenting TP information with possible overlap	Some standardized capability to process/document TP information. TP information processing and documentation activities are centralized and standardized by country. Roles/responsibilities for processing/documenting TP information are defined, with some degree of institutionalization. Limited overlap in roles/responsibilities	Standardized capability to process/document TP information. TP information processing and documentation activities are centralized and standardized by large regions (e.g., EMEA, Americas, Asia Pacific). Roles/responsibilities for processing/documenting TP information are clearly defined, communicated and institutionalized within the organization. No overlap of roles/responsibilities	Fully standardized capability to process/document TP information. TP information processing and documentation activities are globally standardized and coordinated in a consistent manner. Well defined roles/responsibilities for processing/documenting TP information, that are fully institutionalized in the organization. No overlap of roles/responsibilities

Consulting

Transfer pricing policies	To what extent is TP policy defined/documentated?	2	3	TP policy underlying transfer pricing decisions is not defined/documentated	Loosely defined/documentated TP policy- no formal documentation around TP objectives. TP policy is set by local finance teams to meet the needs of local business. There is no clear understanding of TP policy across the organization	Basic TP policy and procedures with formal documentation defined/documentated by tax/TP divisions, which are communicated to selected areas throughout the organization. However, TP policies are not regularly reviewed/updated	Basic TP pricing policy and procedures with formal documentation defined/documentated by tax/TP central teams, which are communicated throughout the organization. However, no consultation lines with tax/TP divisional/local teams are established. TP policies are regularly reviewed and cascaded throughout the organization. However, information on how TP policies are implemented is rarely communicated back to relevant parties	Well-defined/documentated TP policy exists. TP policy is defined by central teams in consultation with divisional/ local tax/TP teams. The process of TP policy setting is linked to organization-wide risk management process, meaning that TP policies are regularly reviewed, information to evidence the compliance with TP policies is produced and communicated back to the relevant parties on a regular basis. Also, external consultants are involved into TP policies design/implementation phases to stay up-to-date and adhere to the latest TP rules and regulations
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Audit support

Accurate, proper communication to other external stakeholders	To what extent are processes around communication of TP related matters to other external stakeholders structured?	2	4	No clear and consistent way to communicate TP related matters to other external stakeholders	TP related matters are somewhat communicated to external stakeholders but there are no criteria/filter in place to select only relevant/critical information	Basic communication strategy on TP related matters is defined but not institutionalized	Consistent way to communicate TP related matters to external stakeholders with basic capability to reputation management	Well defined way to communicate TP related matters to external stakeholders and full capability to reputation management
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Examples of TP “in control” assessment questions (2/3)

Risk management

<p>Development and update of Country Risk Matrix (CRM) and Country-by-Country (CbC) reporting matrix</p>	<p>To what extent is a CRM/CbC reporting matrix developed and updated?</p>	<p>1</p>	<p>4</p>	<p>CRM and/or CbC reporting matrix is not developed</p>	<p>Countries' risk profiles are assessed on an ad-hoc basis. Only limited/fragmented financial information is readily available per a particular country. Existing information on a local level is rarely reviewed (e.g., every 5 years)</p>	<p>Basic version of CRM and CbC reporting matrix exist. CRM/CbC reporting matrix is updated every 2-4 years</p>	<p>Basic version of CRM and CbC reporting matrix exist. CRM/CbC reporting matrix is updated every year</p>	<p>Advanced version of CRM and CbC reporting matrix (contains a higher degree of available information) exist. CRM/CbC reporting matrix is updated semiannually</p>
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Systems

<p>Central data processing and management</p>	<p>To what extent is a central approach in processing and managing TP data applied in the organization?</p>	<p>1</p>	<p>5</p>	<p>Low degree of automated TP data processing and managing with required extensive manual intervention. TP data processing/managing occurs locally</p>	<p>A certain degree of automation has been introduced at business units' level. The responsibility of TP data processing and managing mainly resides with business units</p>	<p>The end-to-end transfer pricing and reporting processes for each division has a high degree of automation with limited manual intervention required. The responsibility of TP data processing and managing mainly resides on a divisional level</p>	<p>The end-to-end transfer pricing and reporting processes for the group has a high degree of automation with limited manual intervention required. The responsibility of TP data processing and managing resides centrally</p>	<p>The end-to-end transfer pricing and reporting processes are centralized and has a high degree of automation to facilitate the information flow across tax/TP teams</p>
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Capacity planning

<p>Defining hiring/ firing strategy</p>	<p>To what extent is there a human resource strategy defined/documented?</p>	<p>2</p>	<p>4</p>	<p>Undefined strategy underlying TP human resource decisions</p>	<p>Loosely defined/documented TP human resource strategy – no formal documentation around human resource objectives</p>	<p>TP human resource strategy exists with formal documentation. However, TP human resource strategy is not regularly reviewed/updated and as a result might not entirely be in tune with the business reality</p>	<p>TP human resource strategy exists with formal documentation. Strategy is often reviewed to be in tune with the business reality. New employees are hired if a company lacks internal TP knowledge/certain TP capabilities</p>	<p>Well defined/documented TP human resource strategy exists and is periodically reviewed to be in tune with the business reality; TP capabilities assessment to identify internal TP knowledge gaps within a company is performed periodically. A company hires new employees following the outcome of such periodic assessment</p>
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Examples of TP “in control” assessment questions (3/3)

Global Benchmarking platform

Defining use of external databases	To what extent are external databases used?	1	3	No clear understanding of the nature of various external databases. External databases for intercompany prices benchmarking purposes are not defined/used	Basic understanding of the nature of various external databases. However, external databases are not used.	Basic understanding of the nature of various external databases. External databases are used on an ad-hoc basis.	Basic understanding of the nature of various external databases. External databases are used when internal databases are not able to provide sufficient/relevant information	In-depth understanding of the nature of various external databases. External databases are used on a regular basis.

Sign-off

Documentation	To what extent is there a clear definition of roles and responsibilities for signing-off TP documents?	1	4	Lack of clear definition of roles/responsibilities for signing-off TP documents	Poorly defined roles/responsibilities for signing-off TP documents with possible overlap	Roles/responsibilities for signing-off TP documents are defined with some degree of institutionalization. Limited overlap in roles/responsibilities	Roles/responsibilities for signing-off TP documents are clearly defined, communicated and institutionalized in the organization. No overlap of roles/responsibilities	Well defined roles/responsibilities for signing-off TP documents exist that are fully institutionalized in the organization. No overlap of roles/responsibilities

Legal agreements

Documentation of information (i.e., drafting of agreement)	To what extent are processes around drafting of legal agreements structured?	2	5	No organizational capability to draft intercompany/legal agreements. Lack of clear definition of roles/responsibilities for drafting intercompany agreements	Limited capability to draft intercompany legal agreements. A limited number of intercompany transactions are supported by intercompany legal agreements. Poorly defined roles/responsibilities for drafting intercompany legal agreements with possible overlap	Some standardized capability to draft intercompany/legal agreements. Basic intercompany transactions are supported by legal agreements. Roles/responsibilities for drafting intercompany/legal agreements are defined with some degree of institutionalization. Limited overlap in roles/responsibilities	Standardized capability (i.e., use pre-defined templates) to draft intercompany legal agreements. Almost all intercompany transactions are supported by legal agreements. Roles/responsibilities for drafting intercompany legal agreements are clearly defined, communicated and institutionalized within the organization. No overlap of roles/responsibilities	Fully standardized capability (i.e., use pre-defined templates which are regularly reviewed and updated) to draft intercompany legal agreements. All intercompany transactions are supported by legal agreements that contain a sufficient degree of information. Well defined roles/responsibilities for drafting legal agreements exist that are fully institutionalized within the organization. No overlap of roles/responsibilities