Between the Uprights: Valuations in Tax and Transfer Pricing

DLA Piper

2019 Transfer Pricing Masterclass Series

Presenters

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Background & Experience
- Transfer Pricing Technical Lead at World Bank
- Provided transfer pricing technical assistance to African & Asian tax authorities
- OECD/World Customs Organisation TP/Customs interface
- Transfer Pricing Lecturer at IBFD, UK, Swiss, Swedish universities
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Background & Experience
- Economist
- APA Team Leader at US IRS
- Led all US/Swiss APA negotiations on intangibles issues
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Background & Experience
- 18 years in-house tax and transfer pricing experience
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- Extensive operating model planning, implementation and review
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Background & Experience
- Economist
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- Transfer Pricing Lecturer at Universite de Lausanne
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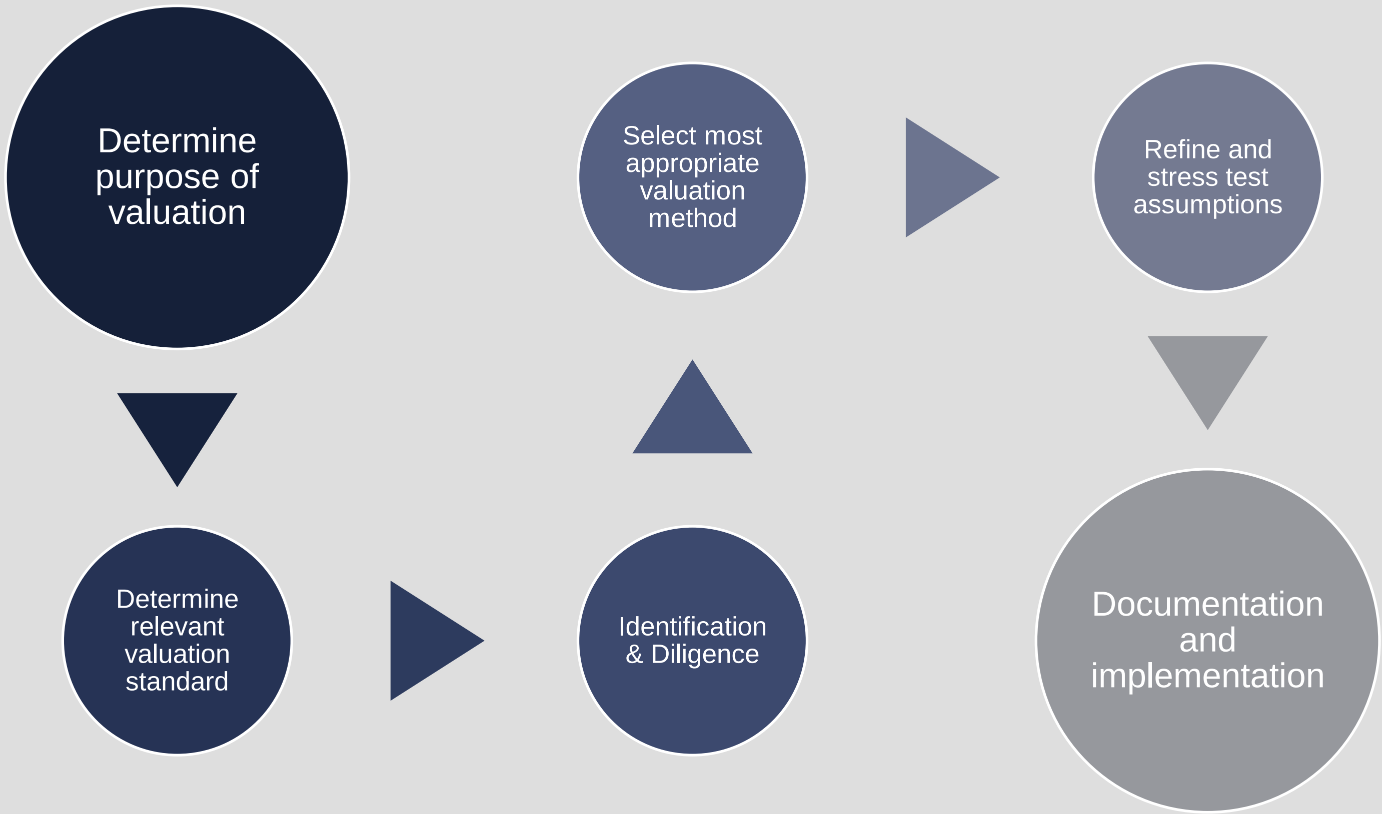
Agenda

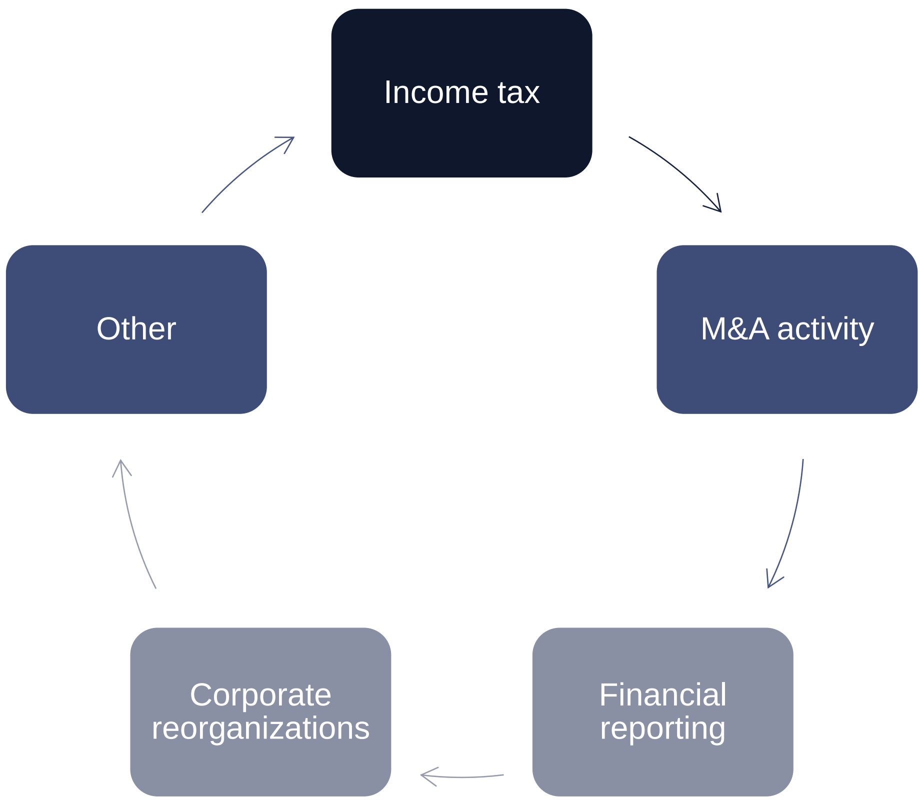
- Typical valuation process
  - Phase 1 – Determine purpose of valuation
  - Phase 2 – Determine relevant valuation standard
  - Phase 3 – Identification & diligence
  - Phase 4 – Select and apply most appropriate valuation method
  - Phase 5 – Refine and stress test assumptions
  - Phase 6 – Documentation and implementation
- Case studies and wrap up

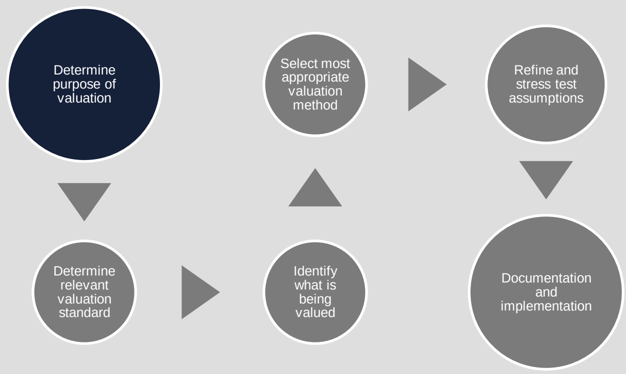
Valuation process

A structured approach



Phase 1 – Determine purpose of valuation

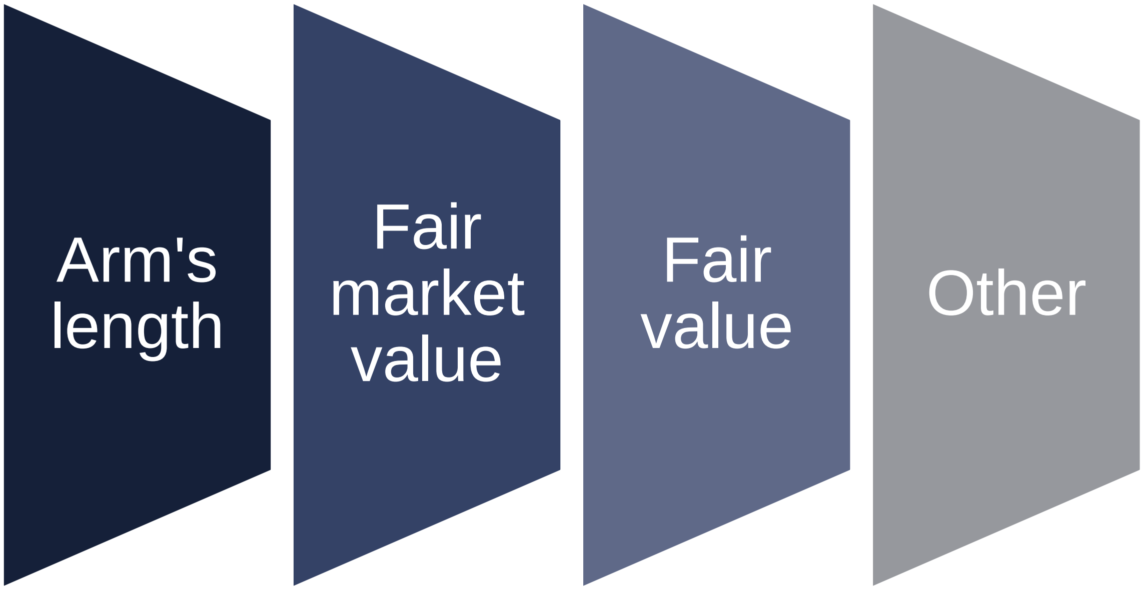


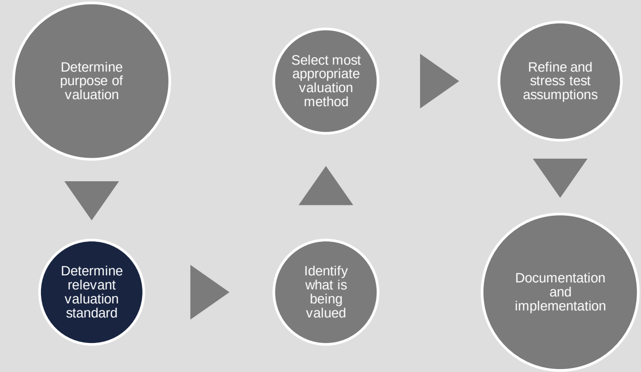


All valuations are not created equal!

There are different valuations for different purposes.

Phase 2 – Determine relevant valuation standard





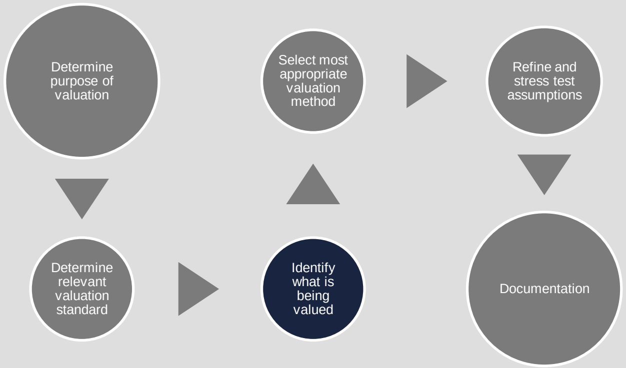
Fair market value, fair value, or other valuation approaches <u>may not</u> produce an arm's length result!

Insight: Comparison of arm's length standard with other valuation approaches

Standard	Perspective	Circumstances	Defined By	Purpose
Arm's length standard	Controlled parties to the transaction: specific buyer and seller	Actual facts of the actual controlled transaction	OECD Transfer Pricing Guidelines/Transfer pricing rules	Used to determine pre-tax prices for controlled transactions (transfer pricing)
Fair market value	Hypothetical buyer and seller	Market where item would most commonly be sold	Statute/regulations/ case law	Used in judicial, regulatory, and other tax matters
Fair value (financial reporting)	Hypothetical market participant	Hypothetical market	Accounting boards	Used in financial reporting, shareholder dissent, corporate dissolutions

Phase 3 – Identification & diligence

- Detailed functional analysis
- Assets, particularly intangibles, must be identified with specificity
- Attribution: legal versus economic ownership (intangibles)
- Historical, current and / or prospective data analysis



Basket approach to valuation can lead to unreliable results and difficult to defend in audit

Phase 4 – Select most appropriate valuation method

Cost based

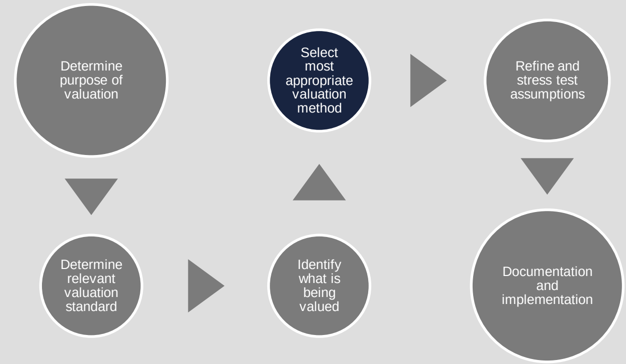
- Reference to cost to recreate or replace the property
- Used infrequently in the case of intangibles where cost is not a proxy of value
- May be useful as corroboration
- Can establish a ceiling on the buyer’s willingness to pay

Market based

- Reference to transactions or companies of the same/similar property
- Often difficult to implement due to a lack of sufficiently comparable transactions/data
- When the data does exist, a market-based analysis should be done at least as a corroboration

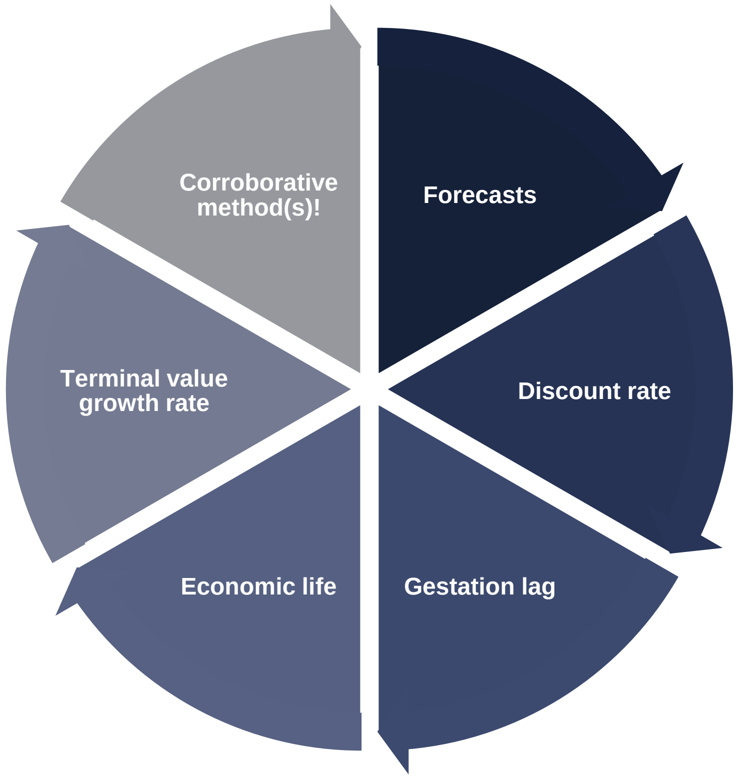
Income based

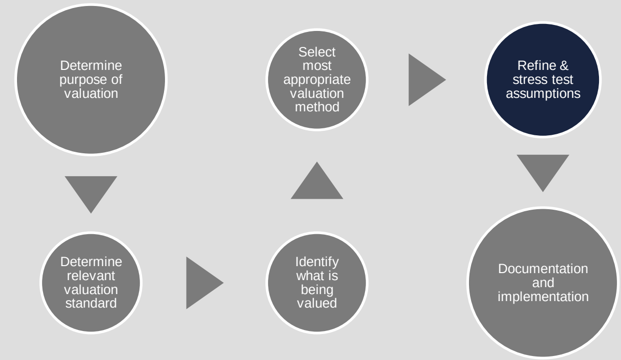
- Reference to discounted projected cash flows or profit to be generated from the property
- Most likely to have available data
- Most likely to be reliable, as the value of an asset should always be a function of the expected cash flows attributable to that asset
- Most commonly used in practice but significant assumptions required with stress test needed



Where possible, use multiple valuation methods to determine bargaining range with tax authorities

Phase 5 – Refine and stress test assumptions



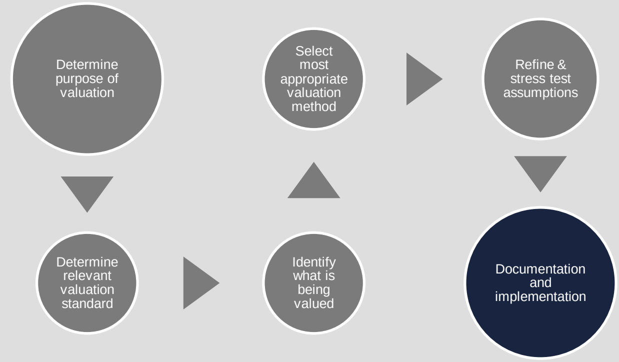


Undertake your review from different perspectives

What is tax authority A going to be focused on?

What is tax authority B going to be focused on?

Phase 6 – Documentation and implementation



1. Transfer pricing analysis supported by evidence and controversy ready
2. Carefully drafted intra-group agreements
3. Proactively address transitional issues
4. Strategic use of MAP and APAs

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