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Transfer Pricing Enforcement Continues to Evolve at the IRS

Middle-Market Businesses Need to be Prepared

By David Bussius, CPA, MST

As part of its continuing efforts to curb perceived abuses by U.S. multinationals that shift profits offshore, the IRS has reorganized, realigned and reinforced its transfer pricing compliance practice. While the impetus for these changes may have been to increase compliance efforts against the multinationals, the IRS also is able to focus increased attention on middle-market companies with transfer pricing issues. As a result, middle-market companies should take the necessary precautions to ensure that their transfer pricing is reasonable and properly documented.

History

Since the Large and Mid-Sized Business (LMSB) division of the IRS realigned into the Large Business & International (LB&I) division in 2010, the IRS has created a Transfer Pricing Practice (TPP) and also combined the Advance Pricing Agreement (APA) program and Mutual Agreement Procedure (MAP) program into the Advance Pricing and Mutual Agreement Program (APMA). The organizational realignments have included the addition of dozens of specialized transfer pricing professionals into the LB&I TPP and the consolidation of specializations of both the APA and MAP personnel. The realignment of structures and specialists provides the IRS with improved field coordination and issue risk assessment to provide a more centralized and enhanced focus on transfer pricing enforcement and compliance.

With the 2011 addition of Samuel Maruca, Director of Transfer Pricing Operations, as well as revisions of tax treaties and tax information exchange agreements, the IRS and the Department of Treasury introduced new transparency requirements for large companies, seeking to ensure that U.S. multinationals are abiding by U.S. tax laws and paying their fair share of tax. Traditionally, IRS international tax and transfer pricing resources have been focused on large companies' use of transfer pricing and its perceived abuses. With these additional specialized staff, new reporting requirements, and a better grasp on the large-market, the depth of the IRS has grown enough to enable it to redirect some of its attention on middle-market businesses with assets between \$10 million and \$250 million.

Current Environment

Currently the combined APMA program has a total of 60 staff members, and the hope is to have close to 100 professionals in the program. This program, designed to form agreements between the IRS and taxpayers prior to filing a tax return, will also help the IRS reallocate resources. This move is just one of many that the U.S. is contemplating in order to reduce the number of routine transfer pricing cases. In



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February, Maruca introduced the concept of bilateral and multilateral safe harbors memoranda of understanding. As Maruca has said recently, however, interest has been limited and he "doesn't want to get people too excited about timing."

The U.S. initially expects to start with those countries in which they already do a fair amount of business, such as Canada. Safe harbors signify that the IRS is taking additional steps to manage transfer pricing cases more efficiently in order to open up more resources to a broader span of companies like those in the middle-market.

Preparing for an Inspection

As the IRS continues to increase the resources allocated to transfer pricing enforcement, transfer pricing audits will continue to increase in frequency and sophistication. In order for taxpayers to comply with transfer pricing regulations and to be prepared for domestic and foreign inquiries, proper transfer pricing documentation is required. Preparing transfer pricing documentation includes a thorough factual development of the taxpayer's operations, controlled transactions and transfer pricing policies evaluated against the arm's length standard. While documentation specifics vary by country, the approach to documenting a taxpayer's transfer pricing is consistently based on robust factual development and analysis supporting operation in accordance with the arm's length standard.

To learn more about preparing adequate transfer pricing documentation, please contact your CBIZ Tofias tax advisor, or you may reach us at TheBottomLine@cbiztofias.com and 617.761.0600.

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