BDO GLOBAL WEBINAR:

THE IMPACT OF COVID-19 ON YOUR TRANSFER PRICING ARRANGEMENTS

KEY TAKEAWAYS - SURVIVE, STRIVE AND THRIVE

KEY TAKEAWAY #1

SURVIVE

Survive the immediate short-term economic, financial and non-financial impacts on your business by taking urgent steps to improve cash flows.

Cash is the lifeblood of any business and cash flow management is critical to survival. Therefore, where anticipated cash flows are reduced, potential options to consider could include:

- Accessing all relevant Government incentives offered to assist companies with COVID-19-related cash flow issues by considering eligibility criteria and ensuring compliance;
- Reviewing the appropriateness of intercompany charges (e.g. services fees, royalties, interest payments) in response to the harsh economic pressures imposed by the Pandemic and any associated lockdowns;
- Reviewing the cost base in the determination of intercompany service fees in relation to 'idle' time and other costs unrelated to actual provision of services/benefits to potentially reduce recharge amounts;
- Considering the impact of idle manufacturing capacity in the determination of intercompany manufacturing service fees;
- Considering reducing returns attributable to routine entities, such as the operating margin for limited risk distributors or the mark- ups for service providers, subject to economic impacts in local jurisdictions and risk-sharing clauses in intercompany agreements;
- Considering increasing, prepaying, reducing or eliminating payments for interest on intercompany loans and otherwise working to refinance working capital facilities with both third parties and related parties; and
- Assessing whether profit split models may have to be considered as loss split models for 2020, by making the relevant calculations now and as the company goes through this period of uncertainty.

KEY TAKEAWAY #2

STRIVE

Strive to maintain as much business as possible during the COVID-19 related downturn, while adapting to temporary and longer term permanent changes to your industry and the broader markets. Consider implementing new or improved transfer pricing policies.

Potential options that may be relevant to your business as you strive to maintain business activities and revenues during the 'new normal' may include:

- Replacing existing loan arrangements with new loan arrangements to take advantage of potentially lower credit ratings to achieve higher interest rates, or looking to utilise guarantees to achieve lower interest rates;
- Where it makes commercial sense, and particularly if it was previously contemplated, implementing intercompany transfers of intellectual property where depressed values exist resulting from the impact of COVID-19;
- Reconsidering whether COVID-19 related changes in 'market risk' should lead to a broader revisiting of functional characterizations and therefore a redistribution of profits;
- Updating transfer pricing policies in response to business and commercial changes that occur in response to COVID-19, for example a significant move online can lead to potential 'digital' tax related matters for consideration;
- Adjusting any transfer pricing policies that had been changed during Survival mode, to cost bases and returns (operating margins / mark-ups) that allow the company to strive for a return to pre-Pandemic levels; and
- Performing the detailed analyses to be documented in the company's 2020 Transfer Pricing Documentation to safeguard the decisions made and the positions taken during the economic downturn.

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KEY TAKEAWAY #3

THRIVE

Position your business to ultimately thrive as the general economy recovers by considering whether any changes should be made to your supply chain.

Undertake the associated transfer pricing planning required to better align the overall supply chain to the 'new normal' while considering the overall tax impact of doing so.

Potential options that may be relevant to your business in this phase include:

- Evaluating the overall supply chain from a business perspective to determine what, if any, changes are required because of the impact of the Pandemic or that are becoming evident in the post-Pandemic economy (for example relocating and/or diversifying sources of supply to manage local country risks);
- Evaluating the tax efficiency of the supply chain, whether or not any changes are made as a result of the evaluation of the supply chain from a business perspective;
- Considering restructuring for: cost efficiency and cash efficiency; shifting or centralizing resources; centralization/ decentralization of manufacturing units; centralization/ decentralization of executive structure; or centralization/ decentralization of innovation/development teams;
- Considering where 'one off' costs should sit within the group, and whether recharges should be put in place between group entities; and
- Conducting a full transfer pricing planning exercise that would, in the absence of a full overhaul of the company's supply chain, result in improvements to the Group's transfer pricing model(s), guideline(s) and resulting tax efficiencies.

It is imperative that all factors considered for any of these decisions be fully documented, internally within the company, and in the company's transfer pricing documentation for 2020.

Further, it is important that evidence of arm's length behaviour that is supportive of the proposed changes be identified and documented. There are many examples of arm's length behaviour in the current environment that would have been unprecedented prior to the arrival of COVID-19, such as rental relief and interest payment deferrals taking place between third parties.

Therefore, it is important to keep in mind that the broader landscape has changed and particularly in transfer pricing, applying our knowledge and practices of the past, will not necessarily help us address the challenges currently faced in the 'new normal' whatever this becomes.

Transfer pricing is facts and circumstances based, so when making decisions regarding transfer pricing policies, don't forget to solicit input from operating divisions such as purchasing, marketing, logistics, R&D, etc. Transfer pricing changes may also affect indirect taxes such as VAT, GST and customs duty, so be sure to bring those teams in as needed.

NOTE: When considering these or other options, bear in mind that the tax authorities are cautioning taxpayers not to make drastic changes to their transfer pricing policies that would or could taint the characterization of the entities in the post- Pandemic periods.

We expect any changes made to transfer pricing policies will come under close scrutiny in the months and years to come.

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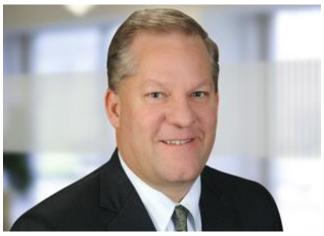

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HOW CAN BDO ASSIST?

Our transfer pricing experts can provide input on the relevant transfer pricing matters you should consider as a result of COVID-19 and guide you through the priority issues and longer term road map to support the business through the Pandemic. We are hosting regular webinars on this and other topics.

Please contact a member of BDO's Transfer Pricing team if you require assistance.