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Prepared by KPMG LLP

Global Transfer Pricing Services

April 10, 2014

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* AT THE BEGINNING OF EACH SECTION, THERE IS A LIST OF TOPICS COVERED IN THE TECHNICAL GUIDANCE TO THAT SECTION WITH A LINK TO THE GUDANCE PAGE ON THE WIKI. EACH GUIDANCE PAGE ON THE WIKI HAS LINKS TO OTHER USEFUL RESOURCES ON THE TOPIC. **PLEASE MAKE FULL AND FREQUENT USE OF THESE RESOURCES.**
* THE DOCUMENT ALSO INCLUDES COMMENTS OR HYPERLINKS (IN BLUE) TO RELEVANT WIKI PAGES.
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|  |
| --- |
| **FAQs: [To be expanded]**   1. *How should the standard report be used if we are just doing a benchmarking study and not other economic analysis (e.g., functional analysis, selection of best method)?*   Our report should only include analyses that we have actually conducted. If we perform a benchmarking study without performing a functional analysis or selection of best method, our report should not include those sections.   1. *How does an analysis prepared for a planning study differ from one that is used in a documentation study?*   There is really no difference in the analysis prepared for a planning study versus a documentation study other than possibly not having year-end financial data. |

***[OPTIONAL]***

The following is a list of acronyms used in this report.

Table 1: List of Acronyms

|  |  |
| --- | --- |
| **Acronym** | **Description** |
| §482 regulations | Regulations under section 482 of the Internal Revenue Code |
| Amadeus | Bureau van Dijk’s Amadeus database |
| CANCO | Foreign Company Canada |
| CIF | Cost, insurance, freight |
| Compustat | Standard & Poor’s Compustat North America database |
| Compustat Global | Standard & Poor’s Compustat Global database |
| CPLM | Cost plus method |
| CPM | Comparable profits method |
| CUP | Comparable uncontrolled price |
| USCO | Company X, Inc. |
| FOB | Freight on board |
| FY10 | Taxable year ended December 31, 2010 |
| GERCO | Foreign Company Germany |
| GPPS | General purpose polystyrene |
| HIPS | Medium and high impact polystyrene |
| IRC | Internal Revenue Code |
| KPMG | KPMG LLP |
| PPE | Property, plant and equipment |
| PSM | Profit split method |
| PWAVG | Period-weighted average |
| RPM | Resale price method |
| SEC | Securities and exchange commission |
| SIC | Standard industrial classification |
| USCO Group | Company X, Inc. and its subsidiaries |

Introduction and Executive Summary

**[TECHNICAL GUIDANCE ON WIKI](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)**

[1.1 Introduction](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.2 Executive Summary](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.3 When the Tested Party is Outside the Interquartile Range – Are Transfer Prices at Arm’s Length?](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.4 When the Tested Party is Outside the Interquartile Range but Transfer Prices are Arm’s Length](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.5 Testing Vs. Setting](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.6 Cost Base](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.7 Non-U.S. Considerations](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

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[1.9 OECD Studies](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.10 Studies Involving Services](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.11 Aggregation Issues](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.12 Use of the Term “OECD Masterfile”](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[1.13 Text Alternative to Tabular Presentation of Results](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/1.%20introduction%20and%20executive%20summary%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

Introduction

Company X, Inc. (“USCO” or “Company”), a U.S. company, engaged KPMG LLP (“KPMG”) to prepare a transfer pricing analysis of certain transactions during the taxable year ended December 31, 2010 (“FY10”).[[1]](#footnote-1) USCO is incorporated in the United States, based in Portland, Oregon, and engages in diverse activities including the manufacture and distribution of chemicals and chemical processing equipment to the electronics, pharmaceutical and energy sectors.

This analysis tests the following intercompany transactions (collectively, “Intercompany Transactions”) for compliance with the arm’s-length standard.

* Transaction 1: USCO’s sale of chemicals to its wholly-owned subsidiary, Foreign Company Germany (“GERCO”); and
* Transaction 2: USCO’s purchase of chemicals from its wholly-owned subsidiary, Foreign Company Canada (“CANCO”), for subsequent sale to GERCO and unrelated U.S. customers.

KPMG performed this analysis from the U.S. perspective, in accordance with the regulations under Sections 482 (“§482 regulations”) and 6662 of the U.S. Internal Revenue Code (“IRC”).

In accordance with KPMG’s agreement with USCO, this report is limited to issues concerning compliance with IRC §482 for the specified transactions. Additional issues may exist that could affect the federal tax treatment of the transaction(s) that are the subject of this report, and the report does not consider or provide a conclusion with respect to any additional issues. With respect to any significant tax issues outside the limited scope of this report, the report is not intended or written by KPMG to be used, and cannot be used, by a client or any other person or entity, for the purpose of avoiding any penalties that may be imposed on any taxpayer. The report is also not intended to be used by a client or any other person or entity in promoting, marketing or recommending to any other party any tax related matters herein.

Table 2: List of Legal Entity Acronyms

|  |  |  |  |
| --- | --- | --- | --- |
| **Acronym** | **Legal Entity** | **Country** | **Has Transactions Covered in this Report?** |
| CANCO | Foreign Company Canada | Canada | Yes |
| GERCO | Foreign Company Germany | Germany | Yes |
| USCO | Company X, Inc. | United States | Yes |

Executive Summary

KPMG’s analyses concluded that the transfer prices for the Intercompany Transactions were within the arm’s-length range.

* **Transaction 1** – KPMG evaluated the arm’s-length nature of Transaction 1 under the Comparable Uncontrolled Price (“CUP”) method, one of the specified methods for pricing tangible property transactions discussed in the §482 regulations.
* **Transaction 2** – KPMG evaluated the arm’s-length nature of Transaction 2 under the Comparable Profits Method (“CPM”), one of the speci***f***ied methods for pricing tangible property transactions discussed in the §482 regulations.

[***This paragraph is included only because aggregation is an issue in this report. If there is no aggregation issue, there need be no reference to sequencing of the analysis.***] Further, the application of the CPM for Transaction 2 is based on a measure of financial performance that depends on the price of polystyrene sold to GERCO under Transaction 1. Thus, [KPMG tested Transaction 1 before Transaction 2 by design](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.7.5%20ordering%20and%20organization%20of%20the%20analysis%20of%20multiple%20transactions%20when%20using%20net%20margin%20methods.aspx?usersegment=F17E450CB0D9FD044379055CECED6). The arm’s-length result for Transaction 1, together with the CPM test for Transaction 2, allowed KPMG to conclude on the arm’s-length nature of Transaction 2.

An abbreviated summary of the basis for KPMG’s conclusion is set forth below in .

Table 3: Summary of Economic Analyses

| **Transaction (Transaction Volume)** | **Transfer Pricing Method** | **Economic Analysis** | **Intercompany Transaction Results** | **Conclusion** |
| --- | --- | --- | --- | --- |
| Sale of chemicals to GERCO by USCO ($50 million) | CUP | Arm’s-length price range from xx to xx | USCO’s prices fell within the arm’s-length range | USCO’s prices are consistent with arm’s-length pricing |
| Purchase of chemicals from CANCO by USCO ($270 million) | CPM with USCO’s chemical segment as the tested party[[2]](#footnote-2) | Range of arm’s-length OM[[3]](#footnote-3) over FY08-FY10 from 1.1% to 4.0% | USCO’s chemical segment OM over FY08-FY10 is 2.2% | USCO’s segmented OM is consistent with arm’s-length range |

Basis for Opinion

KPMG prepared this report to assist USCO in its preparation of certain transfer pricing documentation required for the potential avoidance of penalties under IRC §6662 and the associated regulations. Absent appropriate contemporaneous documentation, §6662 allows the IRS to assess penalties in cases in which it deems a company’s transfer pricing is not consistent with the arm’s-length standard under the §482 regulations.[[4]](#footnote-4)

KPMG has based the conclusions contained in this analysis on the facts and representations set forth in this analysis. The Company represented to KPMG that it has provided all of the facts, circumstances, and information that it knows or has reason to know are pertinent to this analysis. KPMG has not independently verified, and will not independently verify, the completeness or accuracy of any of these facts. If any of these facts or representations are not entirely complete or accurate, it is imperative that USCO inform KPMG immediately in writing, because any incompleteness or inaccuracy could cause changes to the conclusions presented herein.

Appendix B lists the materials that USCO provided to KPMG for this analysis. KPMG has not examined all of the documents necessary to execute the examined transactions, and assumes that USCO has taken all necessary steps to execute the transactions as required by applicable federal, state, or local law.

While KPMG believes that the conclusions in this report are consistent with the relevant provisions of IRC §482, as amended, the regulations thereunder, and the judicial and administrative interpretations thereof, there can be no guarantee that tax authorities will agree. These authorities are subject to change, retroactively or prospectively, and any such change could affect the validity of the conclusions presented herein. Unless specifically engaged, KPMG will not update the advice rendered in this report for subsequent changes or modifications to the law and regulations or to the judicial and administrative interpretations thereof.

Report Contents

***[THIS SECTION IS OPTIONAL]***

Subsequent to this Introduction and Executive Summary, this report contains the following sections: Section 2 presents an overview of USCO’s organizational structure, products, intangible property, customers and competition. Section 3 describes the Intercompany Transactions. Section 4 provides an industry overview. Section 5 presents an analysis of the relevant functions and risks. Section 6 discusses KPMG’s selection of transfer pricing methods. Section 7 describes the economic analysis. Section 8 presents conclusions and the Appendices provide supporting documentation.

Company Overview

**[TECHNICAL GUIDANCE ON WIKI](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.%20company%20overview%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)**

[2.1 Purpose of Company Overview Section](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.%20company%20overview%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[2.2 Company Background](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.%20company%20overview%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[2.3 Products](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.%20company%20overview%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[2.4 Financial Data](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/wiki%20pages/2.%20company%20overview%20-%20technical%20guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

Company Background and Organization

USCO, together with its subsidiaries, (“USCO Group”) manufactures and distributes chemicals and chemical processing equipment, pharmaceuticals, and synthetic food flavorings in North America, Asia and Europe. USCO is incorporated in the United States, and based in Portland, Oregon. USCO’s subsidiaries are located in several countries in North America, Asia and Europe.

Figure 1 illustrates the entities relevant to this study, as of FY11.[[5]](#footnote-5)

Figure : Partial Organization Chart

USCO

100%

CANCO

GERCO

The following sections provide a brief description of the entities relevant to this transfer pricing study and their operations.

### USCO

USCO manufactures and distributes chemicals and chemical processing equipment to the electronics, energy, food, personal care, pest control, pharmaceutical and waste management industries. USCO’s operations are organized into five business segments: (1) Chemicals; (2) Chemical Processing Equipment; (3) Laboratory Equipment; (4) Pharmaceuticals; and (5) Food Flavorings. The intercompany transactions documented in this report are undertaken by the Chemicals business segment of USCO.

### CANCO

CANCO is a wholly-owned subsidiary of USCO located in Toronto, Canada. CANCO produces chemicals, in particular, polystyrene and polyurethanes, in Canada and sells them to USCO for distribution to related and third parties.

### GERCO

GERCO is a wholly-owned subsidiary of USCO located in Munich, Germany. GERCO manufactures chemical processing equipment and laboratory equipment in Germany and sells it to third parties. The Laboratory Segment of GERCO sells petri dishes and other laboratory containers to third parties, and is the business segment that engages in Transaction 1.

Product Overview

While USCO Group sells several diverse products, the products relevant to this study belong to its Chemicals business segment and are described below.

* Polyurethane – is a type of plastic that offers the elasticity of rubber combined with the toughness and durability of metal. It is considered a specialty chemical. USCO sells polyurethane bars – both standard and custom sizes.
* Polystyrene – is a type of plastic that is manufactured from petroleum. It is considered a specialty chemical. USCO sells two types of polystyrene:
  + General purpose polystyrene (“GPPS”), which exhibits good stiffness and electrical properties but is brittle; and
  + Medium and high impact polystyrene (“HIPS”), which is characterized by its impact resistance and ease of fabrication.
* Hydrochloric acid – is a commodity chemical used as a raw material in various chemical process. It is produced by an electrochemical process using salt, water and electricity.

Table 4: USCO’s Chemical Segment Product Mix

|  |  |  |
| --- | --- | --- |
| **Product** | **FY10 Net Sales (USD millions)** | **% of Total Sales** |
| Polyurethane | $300 | 60% |
| Polystyrene | $150 | 30% |
| Hydrochloric Acid | $45 | 9% |
| Miscellaneous | $5 | 1% |
| **Total** | $500 | 100% |

Financial Performance of USCO

Selected items from USCO’s income statement are presented in Table 5.

Table : USCO’s Income Statement – Selected Items (FY10)

|  |  |
| --- | --- |
| **($ ‘000)** | **2010** |
| Sales | 1,150,000 |
| Chemicals | 500,000 |
| Chemical Processing Equipment | 200,000 |
| Laboratory Equipment | 300,000 |
| Pharmaceuticals | 100,000 |
| Food Flavourings | 50,000 |
| Cost of Sales | 690,000 |
| Gross Profit | 460,000 |
| Operating Expense | 287,500 |
| Operating Profit | 172,500 |

Intercompany Transactions

**[TECHNICAL GUIDANCE ON WIKI](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)**

[3.1 Small Out-of-Scope Transactions](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.2 Defining Intercompany Transactions](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.3 Description of Intercompany Agreements](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.3.1 Do they Exist?](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.3.2 Include the Basic Terms of the Transaction](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.3.3 Intangibles and Other Assets](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.4 Transfer Pricing Policies](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.5 Interrelationship of Related Party Transactions](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

[3.6 Financial Data on the Intercompany Transactions](http://usportal.us.kworld.kpmg.com/us/Functions/tax/evs/tp/TPWiki/Wiki%20Pages/3.%20Description%20of%20the%20Intercompany%20Transactions%20-%20Technical%20Guidance.aspx?usersegment=9D92EDE4EA54691B5BEC8CA1C42092FD)

Transaction 1 – Sale of Chemicals to GERCO

Transaction 1 is the sale of polystyrene by USCO to GERCO. GERCO uses this polystyrene in injection molding processes for producing petri dishes and other laboratory containers under its CHMETM trademark for use in biomedical research and science.

Key magnitudes of this transaction are:

* Total sales of polystyrene by USCO to GERCO in FY10 were $50 million; and
* USCO sold $500 million of chemicals, including $150 million of polystyrene, to GERCO and third parties in FY10.

### Transfer Pricing Policy[[6]](#footnote-6)

The price for the polystyrene sold by USCO to GERCO is determined quarterly in accordance with the terms of the intercompany agreement between USCO and GERCO executed in 2008. According to this contract:

* GERCO is required to send USCO an estimate of the polystyrene it will require for each calendar quarter at least 15 days before the beginning of the quarter;
* USCO is then required to provide GERCO a price for the products within seven business days;
* While the agreement does not specify actual prices for the products, it says that if USCO sells an identical product to a third party, then the price quoted to GERCO must be the same as the price quoted or charged to the third party. If USCO does not sell an identical product to a third party then it must follow the same procedures for determining price to GERCO as it would have used had a third party made the request GERCO made;
* USCO is expected to meet GERCO’s request within a certain band of volume specified in the intercompany agreement. If GERCO’s request lies outside this band and USCO does not think it will be able to produce the requested amount, USCO needs to let GERCO know within seven days how much product it can supply;
* Once GERCO receives the quote from USCO it has the option of saying no to USCO within three days and sourcing its product from elsewhere. GERCO is also always free to get price quotes from third parties;
* USCO is required to deliver the promised amount by the tenth business day from the start of the calendar quarter;
* GERCO takes title to USCO products it purchases when it takes physical possession of the product; and
* The term of the contract is for five years with automatic annual renewals unless one of the parties terminates it.

Transaction 2 – Purchase of Chemicals from CANCO

Transaction 2 is the purchase of tangible goods by USCO from CANCO. The purchase consists primarily of polystyrene and polyurethane manufactured by CANCO, and a small amount of packaging material that CANCO buys from third parties. Key magnitudes of this transaction are:

* Total purchases of USCO’s Chemicals segment in 2011 were $300 million, of which $270 million consisted of chemicals manufactured by CANCO; and
* The products purchased from CANCO were resold without being modified by USCO, and accounted for close to 90 percent of USCO’s sales of chemicals.

### Transfer Pricing Policy[[7]](#footnote-7)

Management has represented to KPMG that while there is no written intercompany agreement or transfer pricing policy that covers this transaction, transfer prices for the chemicals are set as follows:

* USCO produces a list price quarterly for each type of chemical that it sells, which forms the basis of its sale price to its third party customers. CANCO sells its products to USCO at a discount of 40 percent on USCO’s list price. USCO produces weekly list prices for its customers, which are benchmarked to certain market prices including the price of crude oil;
* CANCO does not commit to protect USCO’s gross margin if the prices received by USCO from third parties are different from the list prices;
* USCO and CANCO do not make or contemplate making year-end adjustments to bring USCO’s gross margin to a target level.

The title for product sold by CANCO to USCO passes on to USCO once it takes physical possession of the product.

Interrelationship of Transactions

Transaction 1 involves the sale of polystyrene by USCO to GERCO. Transaction 2 involves the purchase of polystyrene and polyurethane by USCO from CANCO. Some of the products purchased by USCO in Transaction 2 are, therefore, sold to GERCO in Transaction 1.[[8]](#footnote-8)

Financial Data on the Intercompany Transactions

The key data with respect to the intercompany transactions at issue are summarized in the table below. Additional detail can be found in Appendix 0.

Table 6: Summary of the Intercompany Transactions (FY11)

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Transaction** | **From** | **To/By** | **Transaction Amount** | **% of Sales/Purchases** |
| Sale of chemicals | USCO | GERCO | $50 million | 10% |
| Purchase of chemicals | CANCO | USCO | $270 million | 90% |

Intercompany Transaction Flows

The following diagram graphically represents the intercompany transactions.

Figure : Intercompany Transaction Flows

Polystyrene

Polystyrene

**GERCO**

**USCO**

**CANCO**

Other Chemicals

1. This engagement is intended to assist the Company in gathering certain information for purposes of complying with the transfer pricing documentation requirements of IRC Section 6662(e) and the associated regulations. This engagement is not intended to provide *assurance* that the Company’s transfer prices over the tested period will withstand scrutiny by the Internal Revenue Service (“IRS”) or any other tax authority. In the event of a transfer pricing adjustment by the IRS or any other tax authority, KPMG can provide no guarantee that a tax authority will not assess penalties. [↑](#footnote-ref-1)
2. The tested party is one of the controlled entities’ most narrowly definable segment that includes the intercompany transaction. It is the entity or business segment whose results are most reliably compared to the financial results of uncontrolled taxpayers. [↑](#footnote-ref-2)
3. OM or operating margin is defined as the ratio of operating profits to revenues. [↑](#footnote-ref-3)
4. This transfer pricing documentation study is not sufficient in itself for penalty protection under §6662. The Company must have all ten principal of the documents that §6662 requires, as Appendix A details, along with supporting documents for this analysis in its work papers. [↑](#footnote-ref-4)
5. KPMG understands that USCO maintains a full organization chart internally. Appendix A provides further detail. [↑](#footnote-ref-5)
6. Appendix X contains further detail related to the intercompany agreements governing this transaction. [↑](#footnote-ref-6)
7. Appendix X contains further detail related to the intercompany agreements governing this transaction. [↑](#footnote-ref-7)
8. In addition to the sales to GERCO, USCO also sold $1,498 of polystyrene to an affiliate in Asia. The Company has represented that these sales were made at market prices. KPMG does not test the arm’s-length nature of this transaction. [↑](#footnote-ref-8)