New IRS Rules for Transfer Pricing of Services Teleconference

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The Services Cost Method ("SCM")

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Services Cost Method ("SCM")

- Updated version of the "cost safe harbor" in the 1968 regulations

- Permits intercompany services to be charged at cost, with no mark-up, for
  (1) "Specified covered services" (IRS published list)
  <u>or</u>
  (2) "Low-margin covered services" (median mark-up < 7%)

<u>IF</u> -----

  (3) Not "excluded transactions"
  <u>and</u>
  (4) Not core capabilities, etc. ("business judgment test")

- Adequate books and records must be maintained, including statement of intent to apply SCM

Services Cost Method

– Ineligible Services –

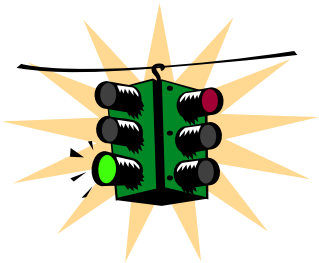
- Excluded transactions:
  - Manufacturing
  - Production
  - Extraction, exploration or processing of natural resources
  - Construction
  - Reselling, distribution or similar agency or commission arrangements
  - Research, development or experimentation
  - Engineering or scientific
  - Financial transactions
  - Insurance or reinsurance

or

- Fail business judgment test:

  Taxpayer is unable to reasonably conclude, in its business judgment, that the services do not contribute significantly to key competitive advantages, core capabilities or fundamental risks of success or failure in renderer's/recipient's business.

Services Cost Method

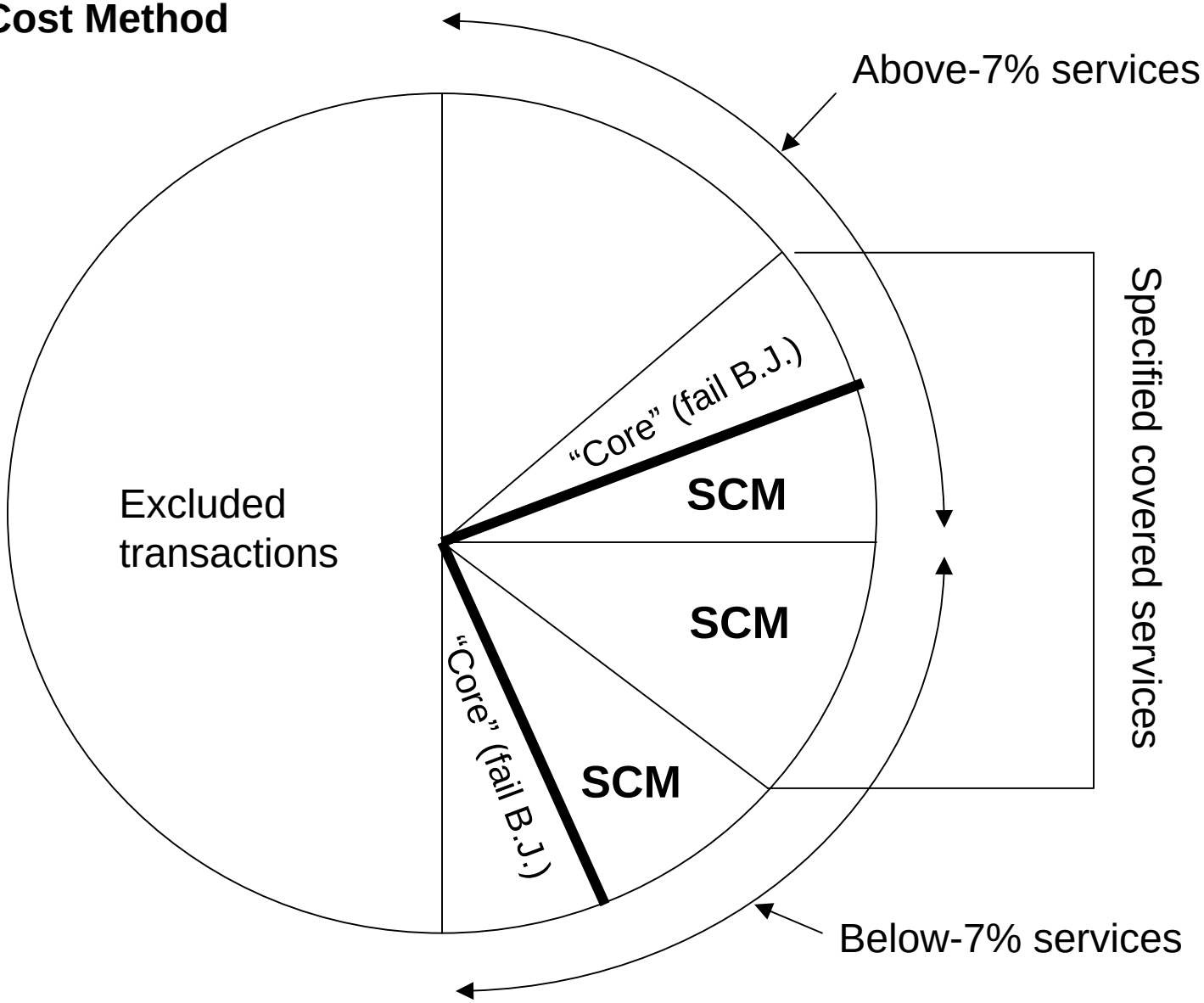


– Eligible Services –

- Specified covered services – Rev. Proc. 2007-13 "White List":

Payroll, AR and AP	Staffing, recruiting, training
Accounting, auditing, budgeting	Corporate and public relations
Treasury activities	Legal services
Tax	Insurance claims management
Employee benefits	Purchasing for support functions
IT services	Health, safety, environmental and regulatory affairs
General administrative	

or

- Low-margin covered services – Arm's length mark-up < 7% (at the median)

Services Cost Method