

# **Transfer Pricing in Russia, analyzing an international company during internship – Case Liebherr**

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<p><b>Abstract</b></p> <p>Transfer pricing mechanisms have been actively used by foreign companies for more than a half of century. The necessity to optimize financial flows between related parties by establishing transfer prices on the one hand, and the existence of proper economic assessment of pricing data in order to minimize negative financial flows related to possible fines and additional charging by tax authorities on the other hand, have both made transfer pricing issues relevant to foreign organizations.</p> <p>Since the beginning of the Russian transition to the market economy, Russian companies faced this problem. Underdevelopment of a given market and market institutions in Russian regions, a high degree of monopolization of individual economic sectors, the lack of consolidated information about market transactions and market prices, as well as taxation differences in each of the Russian region, all these aspects exacerbated the problem of transfer pricing between Russian enterprises. Despite the fact that efficiency of transfer pricing in companies is highly influencing the economic situation in the country, extremely insufficient attention has been given for learning the topic of transfer pricing.</p> <p>Since 1 January 2012, the situation has changed significantly, transfer pricing legislation entered into force, which aims to address the previous shortcomings, to bring into line with international practice.</p> <p>The main goal of this thesis is to learn deeper the topic of transfer pricing in Russia. The aim of the research is to get to know how companies use transfer pricing for minimizing tax risks and how they select an appropriate transfer pricing method. Fortunately, the author has an opportunity to have professional internship during thesis writing. It helps to understand the topic from the company point of view.</p>			
Keywords Transfer pricing, transfer pricing methods, taxes			

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## 1 INTRODUCTION

Transfer pricing mechanisms are actively used by foreign companies during more than a half of century. The necessity to optimize financial flows between related parties by establishing transfer prices on the one hand, and the existence of proper economic assessment of pricing data in order to minimize a negative financial flows related to possible fines and additional charging by tax authorities on the other hand made a transfer pricing issues relevant to foreign organizations.

Since the beginning of Russian transition to the market economy, Russian companies faced this problem. Underdevelopment of market and market institutions in Russian regions, a high degree of monopolization of individual economic sectors, the lack of consolidated information about market transactions and market prices, as well as taxation differences in each of Russian region, all aspects exacerbated the problem of transfer pricing between Russian enterprises. Despite the fact that efficiency of transfer pricing in companies is highly influencing on economic situation in country, it was extremely insufficient attention given for learning the topic of transfer pricing.

Since 1 January 2012, the situation has changed significantly, transfer pricing legislation entered into force, which aims to address the previous shortcomings, to bring into line with international practice.

The main objective of theoretical part of this thesis is to understand and learn deeper the topic of transfer pricing in Russia.

The aim of research is to get to know how companies use transfer pricing for minimizing tax risks and how they select appropriate transfer pricing method. Fortunately, the author has an opportunity to have professional internship during thesis writing. It helps to understand the topic from company point of view.

## 2 MEANING AND EXPLANATION OF TRANSFER PRICING

In the domestic economy, the establishment and development of competitive business based on such a large integrated formations as corporations. Market environment obliges an effective managing in those business entities, which is impossible without timely and reliable information for making optimal management decisions. The necessity of obtaining this information creates qualitatively new situation with special requirements for intra-pricing systems. Economic independence of organizations involves using new approaches for formation of intra (transfer) prices, based on the income balance. In these circumstances there is a need of management accounting tools in corporations, allows to provide execution of strategic goals, setting by central authority. (Valeeva Alexandra, 2012.)

Transfer pricing is a tool that gives an ability to transform a corporation with a complex hierarchy of management into controlled and decentralization structure in which managers' aims are coordinated and contribute to achieving corporation objectives. It should provide information for assessment of quality and timeliness of decision-making, taken by organization managers. (Valeeva Alexandra, 2012.)

Transfer pricing is widely used today in Russian and foreign companies. From economic point of view, Transfer price – is a price, which used by big companies, corporations, especially transnational, in deals, between branches, departments or subsidiaries. The transfer price can be several times lower than the price used for similar transactions.

Transfer pricing is the most common way to reduce level of taxes, therefore transfer pricing allows vertically-integrated companies to minimize taxation. It is used by as large industrial and trading companies, as small businesses. At the same time transfer prices are applied not only in order to optimize the tax, but also as a tool for managing financial resources of corporations. (Zaikin Alexey, 2012.)

The main industries of using transfer pricing are automotive industry, biotechnology, consumer products, telecommunications, financial services, oil and gas, pharmaceutical industry. (OECD Transfer Pricing Guidelines, 2015.)

### 2.1 Tax controlling

Activities of tax authorities are focused on the creation of modern taxation system and strive for achieving an appropriate tax level, which prevents and minimizes violations of

tax legislation. Thus, the tax control should be aimed on preventing tax avoidance and also on identifying arrears of tax and duties system. The primary purpose is to improve tax legislation in the field of tax control system and to provide an effective response to tax evasion. (Valeeva Alexandra, 2012.)

The priority direction of tax policy is an effective tax audit process, which helps to observe the accuracy of transfer pricing between related parties. The intensification of international companies in Russia and Russian companies abroad leads to the fact that for tax authorities with each passing day more and more difficult to implement tax control by taxpayers. Activity expansion of the most companies allows them to use different tools to minimize taxation, including transfer pricing. By establishing special prices for goods, work and services taxpayer has an opportunity to influence on the amount of tax obligations, therefore tax authorities are concerned by the practice of transfer pricing by companies in order to minimize tax burden. (Valeeva Alexandra, 2012.)

Special arrangements of tax controlling for the level of prices between related parties have been developed in several countries, the main principle of arrangements is a rule according to which transfer price should be set on the same level as if there are no financial and legal connections between parties. (Valeeva Alexandra, 2012.)

## 2.2 Documentation and preparation for tax authorities in Russia

Nowadays, for providing evidence of transactions on market terms, in most developed countries, taxpayers have to prepare documents justifying the use of transfer pricing. Since 2014, all cross-border transactions between related parties, regardless of their size must to follow to transfer pricing rules. It means that in 2014 these rules are related to all international companies which are making deals with Russian subsidiaries and other affiliated companies.

The rules of transfer pricing have increased administrative burden of Russian companies which are having deals with foreign related companies. So, according to these rules, taxpayers which are making deals with related parties, have to produce the necessary information and submit a report to tax authorities (Notification of the controlled transaction). The deadline for notification of completed controlled transactions in 2015 - not later than 20 May 2016. Transfer pricing documentation has to be provided to the tax authorities in one month from the date of receiving the appropriate request.

Figure 1 presents tax risks in Russia, as a result of transactions between related parties.

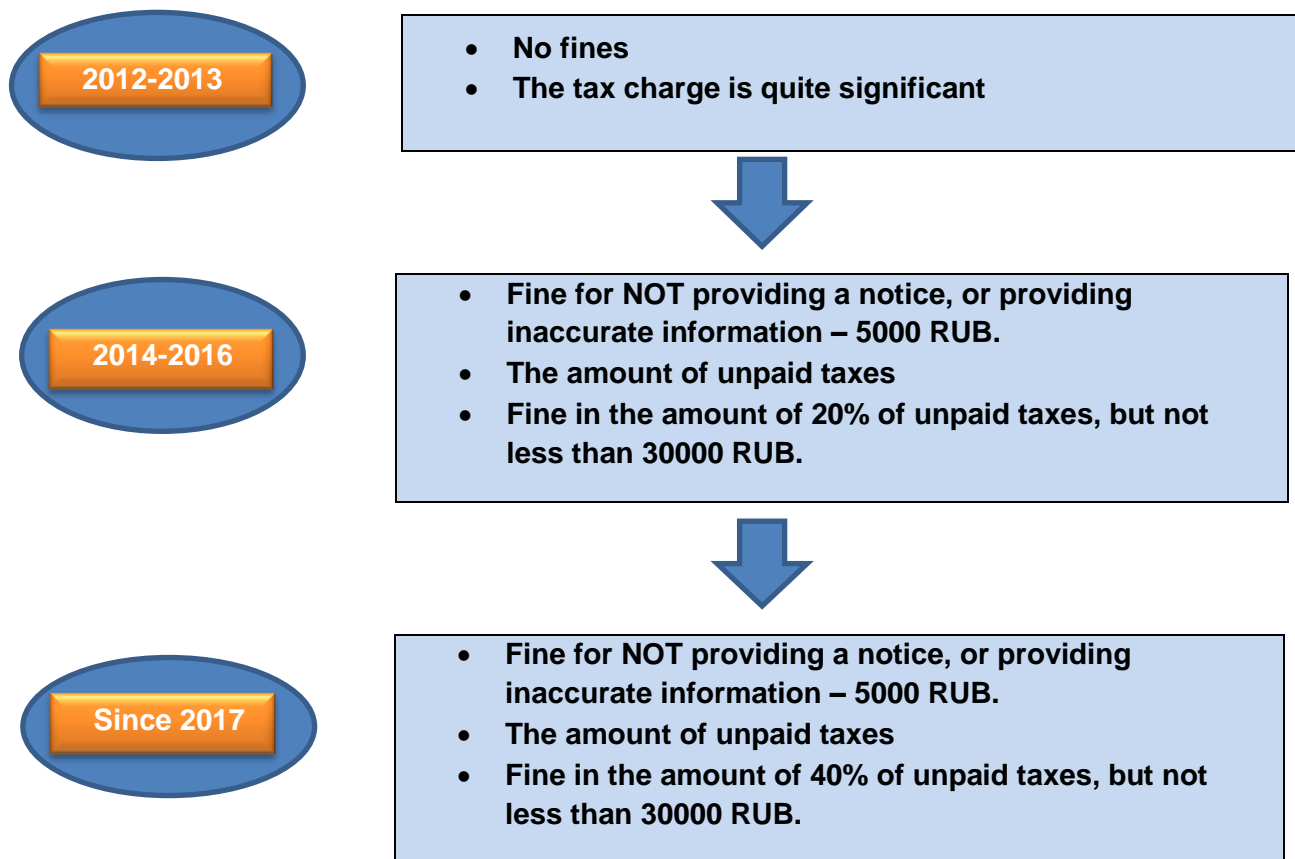


FIGURE 1. Tax risks in Russia, as a result of transactions between related parties (Liebherr Report)

### 2.3 Automated service for simplifying preparation process of documentation

As mentioned in previous chapter about strengthening documentation rules for tax authorities, many companies using special automated services for collecting documentation of transactions. Group “Interfax” has launched a new service that allows Russian companies that are required to prove market-based measures of transactions help in preparing notification and documentation for Federal Tax Service.

Short description of transfer pricing automated service “ASTRA” (Automated System of Transfer Analysis):



ASTRA service developed in accordance with Russian legislation, regulating transfer pricing, as well as taking into account relevant international and Russian practice, provide the ability to automate and document the entire procedure of transfer pricing:

- To describe controlled transactions according to the Russian legislation
- To perform a functional analysis, to identify a weak side of transaction
- Automatically or manually select the justification method of transaction price
- To do economic analysis, using wide range of indicators for selecting comparable companies with an ability of editing final results.
- To prepare documentation for tax authorities
- To fill in a notification of controlled transactions

This service allows companies to justify the cost of controlled transactions not only at the time of the conclusion (in this case, there is a risk of additional taxation), but to calculate price before the moment of transaction, and thereby reduce the tax risks to a minimum.

Service “ASTRA” is available in two versions – Standard and PRO. PRO version is designed for multiple users, who can work together under one report and differs from the standard version that has some more additional options such as:

- The possibility of teamwork administration (managing tasks and controlling of implementation);
- The adjustment of additional samples, focused on certain company (text replacement in tips and examples);
- The ability to create new user points and group them.

Thus, “ASTRA” helps companies:

- To define whether the price is intragroup or market;
- To reduce costs on compliance with legal requirements;
- To minimize tax risks;
- To prepare documentation for tax authorities with minimal expenses.

“ASTRA” guarantees confidentiality of the data with securing by software methods.

The necessary steps for getting a final result in “ASTRA”:

Step 1: Searching controlled transactions

Step 2: Description of product, parties to the transaction and markets

Step 3: Functional Analysis

Step 4: Economical Analysis

## Step 5: Download a final package of documents

### 2.4 Related/Unrelated parties; Controlled/Uncontrolled transactions

Controlled transactions are transactions between related parties, as well as transactions between persons who are not related, but equal to controlled transactions. The new rules which applied from 2012 cover the following type of rules:

Domestic transactions between related parties if they meet one of the following criteria:

- The amount of transactions exceeds 1 billion Russian rubles (RUB) (approx. 35 million United States dollars [USD]) per calendar year. According to transitional provisions of the new law, in 2012 this threshold will be RUB 3 billion (approx. USD 105 million); in 2013 – RUB 2 billion (approx. USD 70 million).
- Transactions concluded between Russian companies registered in the same administrative region that do not have any subdivisions in other administrative regions within Russia or abroad are exempt from transfer pricing control (provided none of these companies has tax losses). In addition, transactions concluded between members of the same consolidated group of taxpayers will also be exempt from transfer pricing control. (*International Transfer Pricing 2013/14 Russian Federation*)

Certain types of transactions which meet at least one of the following conditions and whose aggregate income exceeds RUB 60 million per calendar year (approx. USD 2 million):

- If one party to a transaction is subject to mineral extraction tax and the goods are subject to the above tax at a percentage rate based on sales price.
- One party to a transaction is exempt from profits tax or applies 0% tax rate, while the other party is a profits taxpayer in Russia and does not apply 0% tax rate.
- One party to a transaction is resident in a special economic zone, while the other is not resident in that special economic zone; these provisions are effective from 1 January 2014. (*International Transfer Pricing 2013/14 Russian Federation*)

Transactions where one party applies the unified agricultural tax or a unified imputed income tax (regarding certain types of activities), while the other party pays profits tax under the general rules. Such transactions are subject to control starting from 1 January

2014 if the aggregate income (prices) exceeds RUB 100 million per calendar year (approx. USD 3.5 million). (*International Transfer Pricing 2013/14 Russian Federation*)

Cross-border transactions between related parties; under a general rule, no threshold is established for such transactions. (*International Transfer Pricing 2013/14 Russian Federation*)

Cross-border transactions with certain types of commodities: (1) oil and oil products, (2) ferrous and nonferrous metals, (3) fertilizers and (4) precious metals and stones. The list of commodities is to be established by the Russian Ministry of Industry and Trade. A financial threshold of RUB 60 million per calendar year is established for such transactions. (*International Transfer Pricing 2013/14 Russian Federation*)

Transactions with parties incorporated (domiciled, tax-resident) in a state or territory included in the Finance Ministry's list of offshore zones that grant beneficial tax regimes and do not share information during financial audits (a financial threshold of RUB 60 million per calendar year applies). The list of such territories is already approved by the Russian Ministry of Finance for the purposes of applying a participation exemption on dividends. The list includes such jurisdictions as the British Virgin Islands, Cyprus (to be excluded from the list from 2013), Hong Kong, Gibraltar, Liechtenstein and certain other territories. (*International Transfer Pricing 2013/14 Russian Federation*)

Under transitional provisions of the new law, in 2012 cross-border controlled transactions will be subject to transfer pricing audit by the Federal Tax Service provided the amount of controlled transactions exceeds RUB 100 million; in 2013 – and RUB 80 million. Please note that the Russian tax authorities confirmed that for the purposes of financial threshold calculation, taxpayers should add up the value of all transactions with a particular counterparty during one calendar year. (*International Transfer Pricing 2013/14 Russian Federation*)

According to the new law, if prices are regulated by the Russian authorities or established in accordance with Russian anti-monopoly law, the Russian tax authorities will accept such prices for tax purposes. (*International Transfer Pricing 2013/14 Russian Federation*)

To conclude, the new Russian transfer pricing rules are, to a certain extent, aligned with those of the OECD, whose pricing controls focus solely on transactions between related parties. Nevertheless, by including cross-border transactions involving certain types of

commodities and transactions with residents of low-tax jurisdictions in the list of controlled transactions, the tax authorities have in effect incorporated certain elements of anti-avoidance rules in the new Russian transfer pricing rules. (*International Transfer Pricing 2013/14 Russian Federation*)

### 3 TRANSFER PRICING METHODS IN RUSSIAN FEDERATION

There are five methods of transfer pricing in Russia, which included:

- The comparable market price method (same as CUP, comparable uncontrolled price method)
- The resale price method
- The cost plus method
- The comparable profits method (same as TNMM, the transactional net margin method)
- The profit split method

It is possible to use a combination of two or more methods. Most companies prefer to use the comparable market price method. Other methods can be applied only if this method is impossible to use or if it does not produce reliable results. (Transfer pricing methods in Russian Federation, 2015.)

#### 3.1 The comparable market price method

The method of comparable market prices (Article 105.9 of the Tax Code) is applied to determine compliance with price used in controlled transaction, if the relevant market of goods has at least one comparable transaction with identical goods (works, services) and one important criteria if the information of this transaction is enough for this method. Using the comparable market price method, the taxpayer may consider his own transactions with unrelated parties as comparable transaction. (Transfer pricing methods in Russian Federation, 2015.)

#### 3.2 The resale price method

This resale price method can be used when the product is purchased from related party and after that resell to unrelated party without processing. In this method, the object of analysis is a distributor. The resale price method also can be used in following situations:

- 1) Product preparation for resale and transportation (separation of goods into the parties, sorting, repacking);

- 2) Mixing of goods, if characteristics of the final product are not significantly different from the mixed goods.

The logic of this and first methods is very similar: it is necessary to compare the gross margin (in case of the method of the resale price) or gross margin costs (in case of the cost plus method), that the company has received in the transaction with related party, with a market profitability interval, which unrelated party received in comparable transactions. Transactions must be implemented in a comparable commercial and financial terms. The choice of one of these two methods will depend on which part of the production chain is the tested group (that company, by whom a controlled transaction is considered) and independent side. (Transfer pricing methods in Russian Federation, 2015)

### 3.3 The cost plus method

The cost plus method is mainly supposed to be used for transactions with providing services, except for transactions involving intangible assets that have a significant impact on profitability. The method is based on direct and indirect costs of the supplier. The main difficulty of this method is that information about costs is a commercial secret and foreign companies, as a rule, do not disclose information about it. (Transfer pricing methods in Russian Federation, 2015.)

### 3.4 The comparable profits method

The comparable profitability method (Article 105.12 of the Tax Code) involves the use of cost-effectiveness in the commission of a controlled transaction. This method can be used, if the method of comparable market prices, the resale price method and the cost plus method cannot be used due to the lack or insufficiency of information under which we can make a conclusion about the comparability of the commercial and (or) financial conditions in transactions.

For using this method, the following operating margins can be used:

- Sales profitability (where goods were purchased from related parties and sold to unrelated parties, or purchased from unrelated parties and sold to related parties)
- Cost margin (the provision of services and production of goods)
- Profitability of commercial and management costs

(Transfer pricing methods in Russian Federation, 2015.)

### 3.5 The profit split method

This method requires allocation of total profit, earned by all parties during transaction. The profit split method should be applied only in case of impossibility of using other methods. If the considering organizations prepare their financial statements according to different accounting rules, then it should be done with a single common accounting rule for the purpose of applying this method. Profit split method may be applied only in extreme cases and under the following conditions: If the previous methods of transfer pricing are not appropriate, or parties have rights on intellectual property that have a significant impact on their profitability. (Transfer pricing methods in Russian Federation, 2015.)

## 4 ABOUT CASE COMPANY – LIEBHERR

### 4.1 Company description

Liebherr was established in 1949 by Hans Liebherr as a family business in construction machinery production. For the past years the company has grown into International Corporation with annual turnover of 6 billion, combining more than 140 companies of Liebherr all over the world with more than 40 000 employees, despite that fact, Liebherr is still a family business and belonging to the family members of Liebherr. Today the second generation runs the concern – Willi and Isolde Liebherr, the son and daughter of the company founder. (About Liebherr, 2016.)

For more than 60 years, Liebherr has been associating with various and constantly growing pallet of innovative solutions for variety of industries. High practical value of decisions, time-tested technology and high quality standards are designed to provide maximum benefit for consumers of any kind of Liebherr products. (About Liebherr, 2016.)

### 4.2 Key figures

In this chapter author demonstrated key figures of Liebherr. These key figures of Liebherr in 2014 are shown below.

TABLE 1. Key Figures (Liebherr-Report 2014)

Year company was founded	1949
Group turnover in 2014	8,823 million €
Group investments in 2014	816.0 million €
Workforce by end of 2014	40,839

In the field of construction machinery and mining equipment, the global turnover of Liebherr Group in 2014 was approx. 5294 Mill. EUR, this is 6% lower than last year's results. However, a significant growth was achieved in fields of maritime cranes and port equipment, aerospace and transportation technologies, machines and automation systems, refrigeration and freezing equipment as well as components and hotels. In these sections a combined global turnover has increased by 195 Mill. EUR or 5,8%.

(About Liebherr, 2016.)



Figure 2 and 3 show turnover by product groups in 2014, its change over the previous year and turnover by sales regions.

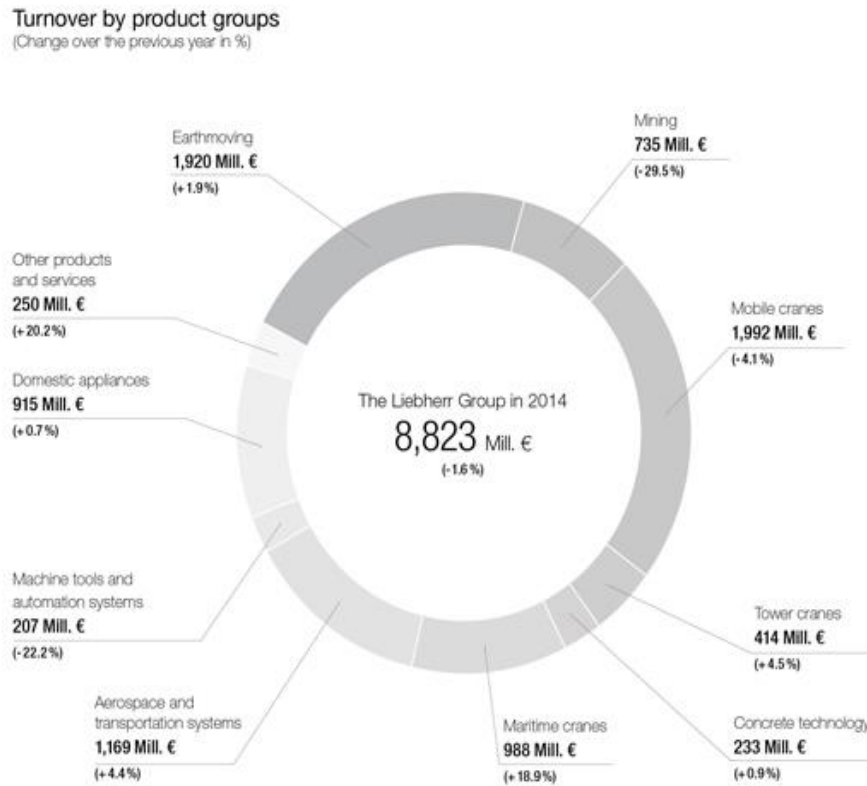


FIGURE 2. Turnover by product groups in 2014 (Change over the previous year in %). (Liebherr Annual Report 2014.)



FIGURE 3. Turnover by sales regions (Mill. €) (Liebherr Annual Report 2014.)

### 4.3 Core values

Liebherr-Group is an independent family enterprise. This fact has always been an essential part of corporate culture and it will remain as a key of success in the future.

#### **Independence**

For Liebherr-Group independence is possibility to make decisions quickly and independently. As a family corporation, they strive for keeping maximum of freedom and independence in decision-making. The basis for this is a financial independence, which they achieve through consistent planning and saving company operating profit. Big diversification of company's activities guarantees a high resistance to fluctuations of regional market and different industries. (About Liebherr, 2016.)

#### **Reliable partner**

With their customers and partners, they support close cooperation based on mutual trust and respect. At the same time they do not attach significance to short-time success, because a long-term perspective is the most important value. Liebherr offers their customers complete and effective solutions based on their individual needs and wishes. "Only when customers and partners are satisfied, then we can be happy too" - by adhering to this approach they constantly have been growing and developing since the company's founding in 1949. (About Liebherr, 2016.)

**Innovations**

Liebherr – is a huge innovative potential and effective implementation of new ideas. Based on previous successes, they consistently improve and develop all areas of activity. They encourage business initiative of employees and willingly undertake for solving the most complicated tasks. Liebherr is focused on technological progress, which realized in interests of their customers. Annually, the company sends a big quantity of investments in research and development projects. It helps in finding the most effective solutions and setting new vectors of development. (About Liebherr, 2016.)

**Employees**

Liebherr relies on well-motivated qualified employees, who keep loyalty to the company for many years and doing their job with interest and commitment. For this point, they create a suitable working environment, providing high reliability of work places and favorable work atmosphere. Horizontal hierarchical organization of Liebherr Group provides set of different kind of responsible tasks by stuff in a high degree of discretion. Liebherr encourages initiative and supports professional growth of employees through educational programs and advanced training courses. Diversity is highly valued in Liebherr particularly cultural. Also team work effort by stuff from different countries enriches corporate culture of Liebherr. The work in Liebherr is based on mutual respect, fair treatment, courtesy and trust. (About Liebherr, 2016.)

**High quality of products**

Products and services are always in conformity with the standards which are traditionally associated with the name of Liebherr. They guarantee the highest quality and promote customers' satisfaction. For maintaining the high quality products Liebherr continuously investing in modernization of their production plants. (About Liebherr, 2016.)

**4.4 Products & services of Liebherr**

For the majority of ordinary consumers this German engineering company associated with fridges and freezers exclusively. In fact, household appliances are only a small percentage of Liebherr-Group revenue. But the main source of income - machinery, port machinery, construction machinery, special machinery, mining and excavating machinery, dump trucks, etc. Liebherr products are used in the aerospace and transportation. A lot of innovations are unique, with no analogues of competitors' production on the market. (About Liebherr, 2016.)

For more than 60 years, Liebherr associated with constantly growing diversity of advanced solutions for many of industries. High practical value of making decisions, time-tested technologies and high quality standards are designed to provide the maximum benefit for any kind of Liebherr consumers. (History of Liebherr, 2014.)

Several years ago, Liebherr has opened manufacturing area in the Odintsovo district of the Moscow region. Nowadays, there is a huge area of several departments and a testing ground for the machinery. One of the workshops for the repair and maintenance of lifting equipment, which operates in Russia, and according to recent statistics, there are quite a lot of such machines - about 5,000 units. This is more than in Germany, which is the establishment country of Liebherr. Nowadays, Liebherr production in Moscow has become more available for rent. (History of Liebherr, 2014.)

Figure 4 and 5 below show example of production such as material handling equipment and mobile crane.



FIGURE 4. Material handling equipment (Liebherr report)



FIGURE 5. Mobile crane (Liebherr report)

## 5 PREPARATION OF DOCUMENTS FOR TRANSFER PRICING (LIEBHERR-RUSSLAND REPORT)

The new chapter of this thesis starts with important part of transfer pricing process such as documentation. The information below included steps of process of preparation of documents for transfer pricing.

- Identification of controlled transactions
- Filling & submitting the notice of controlled transactions
- Selection of method for justifying the level of market prices
- Stage of doing the market analysis
- Building market intervals of profitability
- Calculation of "Liebherr-Russland" profitability in accordance with the selected method
- Calculation of tax charge if the profitability of company lower than the market level
- Preparation of documentation for the purpose of tax control (in accordance with the terms of Art. 105.15, of the Russian Tax Code)

Table 2 outlines a process of preparation of documentation for the purpose of tax control in Liebherr-Russland.

TABLE 2. Preparation of documentation for the purpose of tax control in Liebherr-Russland

<b>Preparation of documentation for the purpose of tax control</b>				
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
<b>Description of goods which are the subject of controlled transactions</b>	<b>Description of company' groups</b>	<b>Information about the group of controlled transactions and functional analysis</b>	<b>Selecting the transfer pricing method for tax purposes and sources of information</b>	<b>Determination of market profitability interval</b>

Figure 6 illustrates the information which included in the notice of controlled transactions.

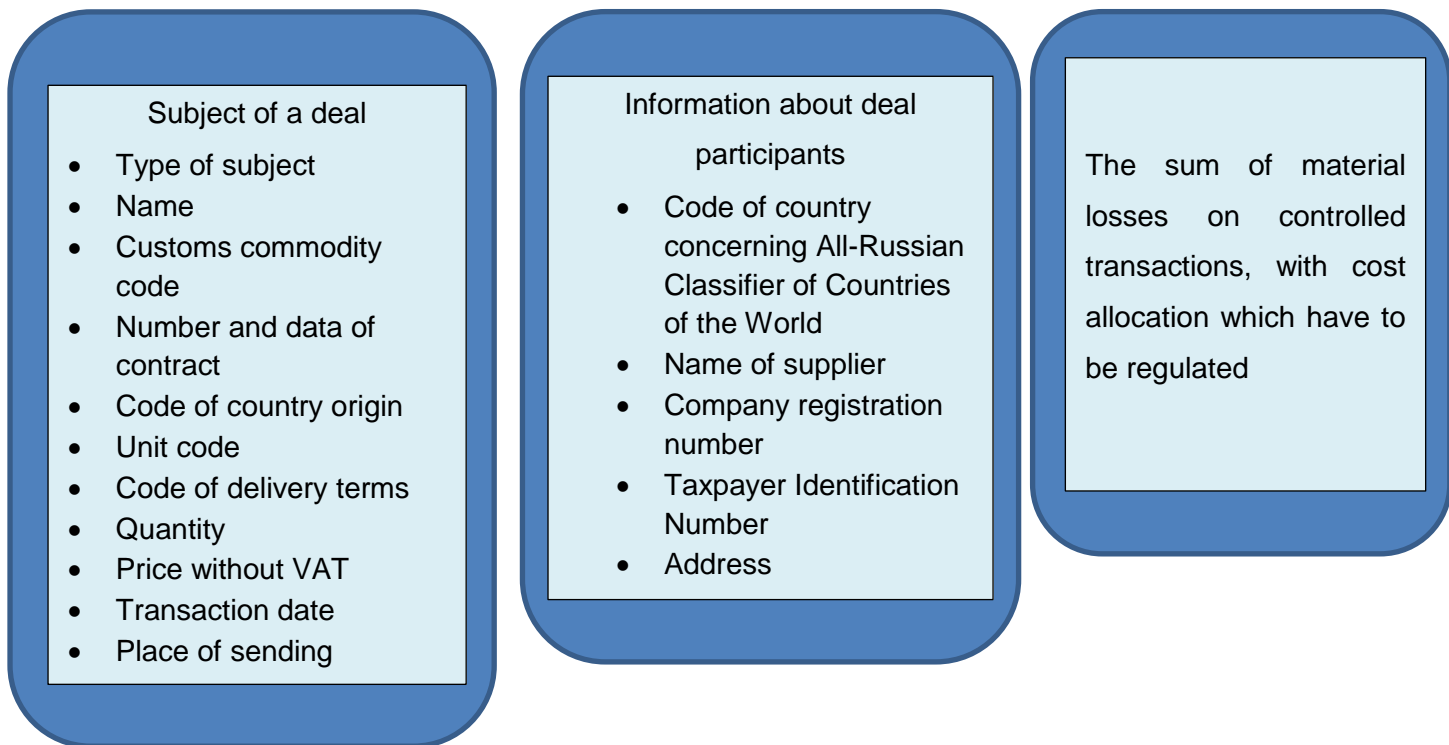


FIGURE 6. The information which included in the notice of controlled transactions (Transfer Pricing Liebherr Report)

### 5.1 Identification of controlled transactions

Since 2014, the information about all controlled transactions must be provided to Federal Tax Service.

The following table below shows Liebherr departments, in which analyses had already been conducted.

Table 3 represents list of plants which information with controlled transactions is providing to FTS and its dynamics of growth since 2012.

TABLE 3. List of plants which information with controlled transactions is providing to FTS; Dynamics of growth.

Department	Year		
	2012	2013	2014
EMT	LBH, LFR, LHB, LMD, LWT	LBH, LFR, LHB, LLG, LWT	LBH, LFR, LHB, LMD, LLG, LWT, LGB, LIS
HAU	LHG, LHM, LWL	LHG, LHM, LWL	LHG, LHM, LWL, LAK, HAU
MT	LMT	LMT	LMT, LBP
LWE	LWE	LWE	LWE
HS, HM	LWN	LWN	LWN, LCC
MIN	LEC	LEC	LEC
TDK	LBC, LIM	LBC, LIM	LBC, LIM, LNN
AER			LLI, LTS
COT			COS, COB
LVT			LVT
Others			IHT, LMB, LEX, LIN, LPS
Sum	14	14	32



## 6 RESEARCHING AND SELECTING AN APPROPRIATE METHOD FOR LIEBHERR-RUSSLAND

The first step is to analyze information sources. After internal and external information sources were analyzed, it revealed that prices of controlled transactions can be justified by using 2 methods:

- The comparable market price method (same as CUP, comparable uncontrolled price method)
- The comparable profits method (same as TNMM, the transactional net margin method)

There are three methods more, by which legally possible to justify price for a controlled transactions:

- The resale price method
- The cost plus method
- The profit split method

These methods are not applicable for justifying prices of controlled transactions, committed by Liebherr-Russland, for the following reasons:

- Lack of information in the public domain;
- Possibility of using the priority method of CMP.

By using automation system "ASTRA" and after internal and external analyses have been made the decision was to select **the comparable profits method**. Using the comparable market price method is inappropriate, because there are no information which particular external costs are related to prime cost and which are related to selling and administrative expenses, also there was no internal comparable transactions.

The comparable profits method steps:

- Functional analyses (by using special automation system)
- Choosing a testing company in a transaction
- Choosing a financial indicators
- Choosing a source of information
- Selection of comparable companies
- Calculation of market profitability interval

- Comparison of profitability obtained by the testing company with a market profitability interval

All the results from ASTRA were unloaded and calculated in MS Excel. The results are shown below. The information about type of product, CC Code, delivery terms, address, sales proceeds, prime cost, S&A expenses was already known. Calculation of the minimum and maximum value was done by special automation system. Gross profit, operating profit/loss, ROS were calculated manually.

Table 4 shows the calculation of actual return on sales and its accordance to market level

TABLE 4. The calculation of actual return on sales and its accordance to market level

Type of product	Customs commodity code	Delivery terms	Delivery address	Sales proceeds, RUB	Prime cost, RUB	Gross profit, RUB	S&A Expenses	Operating profit/loss	ROS, %	The min. value of profitability interval	The max. value of profitability interval
Spare parts	4911990000	CPT	MOSCOW	8 882,97	8 623,38	259,59	1 249,13	-989,54	-11,14%	0,80%	6,21%
Spare parts	7326909309	CPT	MOSCOW	487 716,63	402 489,44	85 227,19	68 583,06	16 644,13	3,41%	0,80%	6,21%
Spare parts	8431410000	CPT	MOSCOW	973 381,77	894 312,85	79 068,92	136 877,63	-57 808,71	-5,94%	0,80%	6,21%
Spare parts	8431498009	CPT	MOSCOW	105 560,65	126 826,81	-21 266,16	14 844,01	-36 110,17	-34,21%	0,80%	6,21%
Wheel loaders	8429519900	DAP	MOSCOW	2 442 563,51	2 062 962,48	379 601,03	343 475,00	36 126,03	1,48%	0,80%	6,21%
Wheel loaders	8429519900	DAP	SAINT PETERSBURG	40 510 349,22	34 771 567,41	5 738 781,81	5 696 593,89	42 187,92	0,10%	0,80%	6,21%
Wheel loaders	8429519900	FCA	BISCHOFSHOFEN	9 944 451,76	9 268 410,45	676 041,31	1 398 395,82	-722 354,51	-7,26%	0,80%	6,21%
Wheel loaders	8427201902	FCA	BISCHOFSHOFEN	27 312 389,92	24 749 282,27	2 563 107,65	3 840 687,54	-1 277 579,89	-4,68%	0,80%	6,21%

Higher than profitability interval

Inside of profitability interval

Lower than profitability interval

Table 5 illustrates only companies which are out of profitability interval and were the subject to further analysis.

TABLE 5. The calculation of actual return on sales and its accordance to market level (Only companies, which are out of profitability interval)

Type of product	TP method	Delivery terms	Delivery address	Sales proceeds, RUB	Prime cost, RUB	Gross profit, RUB	S&A Expenses	Operating profit/loss	ROS, %
Spare parts	CP	49119 90000	MOSCOW	8 882,97	8 623,38	259,59	1 249,13	-989,54	-11,14%
Spare parts	CP	84314 10000	MOSCOW	973 381,77	894 312,85	79 068,92	136 877,63	-57 808,71	-5,94%
Spare parts	CP	84314 98009	MOSCOW	105 560,65	126 826,81	-21 266,16	14 844,01	-36 110,17	-34,21%
Wheel loaders	CP	84295 19900	SAINT PETERSBUR G	40 510 349,22	34 771 567,41	5 738 781,81	5 696 593,89	42 187,92	0,10%
Wheel loaders	CP	84295 19900	BISCHOFSHO FEN	9 944 451,76	9 268 410,45	676 041,31	1 398 395,82	-722 354,51	-7,26%
Wheel loaders	CP	84272 01902	BISCHOFSHO FEN	27 312 389,92	24 749 282,27	2 563 107,65	3 840 687,54	-1 277 579,89	-4,68%

The results of adjustments which made by automation system equity to the minimum value of profitability interval are shown below.

TABLE 6. The results of adjustments and equity to the min. value of profitability interval

Type of product	TP method	Cust oms commodity code	Delivery terms	Sales proceeds, RUB (Adjusted)	Prime cost, RUB	Gross profit, RUB	Gross profit margin ratio, %	S&A Expenses	Gross profit, RUB (Adjusted)	ROS, %	The min. value of profitability interval	The max. value of profitability interval
Spare parts	CP	4911 9900 00	MOSCOW	9 952,13	8 623,38	1 328,75	13,35%	1 249,13	79,62	0,80%	0,80%	6,21%
Spare parts	CP	8431 4100 00	MOSCOW	1 039 506,53	894 312,85	145 193,68	13,97%	136 877,63	8 316,05	0,80%	0,80%	6,21%
Spare parts	CP	8431 4980 09	MOSCOW	142 813,33	126 826,81	15 986,52	11,19%	14 844,01	1 142,51	0,80%	0,80%	6,21%
Wheel loaders	CP	8429 5199 00	SAINT PETERSBUR G	40 794 517,44	34 771 567,41	6 022 950,03	14,76%	5 696 593,89	326 356,14	0,80%	0,80%	6,21%
Wheel loaders	CP	8429 5199 00	BISCHOFHOFEN	10 752 828,90	9 268 410,45	1 484 418,45	13,80%	1 398 395,82	86 022,63	0,80%	0,80%	6,21%
Wheel loaders	CP	8427 2019 02	BISCHOFHOFEN	28 820 534,08	24 749 282,27	4 071 251,81	14,13%	3 840 687,54	230 564,27	0,80%	0,80%	6,21%

Table 7 shows the sum of calculated additional tax which have to be paid to FTS.

TABLE 7. Calculation of accrued income tax

Type of product	TP method	Delivery terms	Delivery address	Sales proceed, RUB (Adjusted)	Gross profit, RUB (Adjusted)	The difference between the actual and adjusted revenue	The difference between the actual and adjusted revenue	Accrued income tax
Spare parts	CP	4911990000	MOSCOW	9 952,13	79,62	1 069,16	1 069,16	213,83
Spare parts	CP	8431410000	MOSCOW	1 039 506,53	8 316,05	66 124,76	66 124,76	13 224,95
Spare parts	CP	8431498009	MOSCOW	142 813,33	1 142,51	37 252,68	37 252,68	7 450,54
Wheel loaders	CP	8429519900	SAINT PETERSBURG	40 794 517,44	326 356,14	284 168,22	284 168,22	56 833,64
Wheel loaders	CP	8429519900	BISCHOFSHOFEN	10 752 828,90	86 022,63	808 377,14	808 377,14	161 675,43
Wheel loaders	CP	8427201902	BISCHOFSHOFEN	28 820 534,08	230 564,27	1 508 144,16	1 508 144,16	301 628,83
						2 705 136,13	2 705 136,13	541 027,23

#### Formulas which are used in calculations:

Gross profit = Sales proceeds - Prime cost

Operating profit/loss = Gross profit - S&A Expenses

ROS, % = Sales proceeds / Operating profit/loss

Gross profit margin ratio = Gross profit / Sales proceeds

Accrued income tax = The difference between the actual and adjusted revenue \* 0,2

The minimum value of profitability interval and the maximum value of profitability interval were calculated by automation system

## 7 SUMMARY AND CONCLUSIONS

The aim of research was to learn a topic of transfer pricing and understand how companies use transfer pricing for minimizing tax risks and how they select appropriate transfer pricing method. In the author's opinion all the objectives were achieved.

The author faced some difficulties in researching, because transfer pricing in Russia appeared not so long time ago. It was almost impossible to find books concerning transfer pricing in Russia. Despite all of the challenges, the author tried to use a variety of sources to combine information for every important part of this topic.

First, the author explained the necessity of transfer pricing and why Russia faced this problem some years ago, also the definition and meaning of transfer pricing, what type of companies use it and listed the main industries of using transfer pricing. Then the author mentioned the impact of tax controlling topic, on what it focuses, what the purposes are. Also writer payed attention to documentation and preparation for tax authorities in Russia, special automated service for simplifying preparation process of documentation and analyzed the information about related and unrelated parties; controlled and uncontrolled transactions. Next chapter was a transfer pricing in Russia, the writer listed five methods and detailed their features. After that the author has given a description to case company – Liebherr, he described core values, key factors of a company, etc. Next chapter is documentation in transfer pricing, which is a very important part of the whole process.

Then, it starts with a practical part, which included researching and selecting an appropriate method for Liebherr-Russland. The writer illustrated tables with all calculations which were made for achieving a final result. The author was involved in a process of choosing transfer pricing method and demonstrated himself as a good and motivated person. The author is totally confident that all objectives of research were successfully reached.

Based on the results, it can be concluded that the research into selecting of transfer pricing method has been very successful. The writer gained a lot of skills such as financial, teamwork and individual, and of course, knowledge in different kind of areas. The researcher believes that he will use gained skills in a future and information that he learnt from thesis writing.

Summing up the results it can be concluded that the opportunity to have internship in a company during thesis process has played a significant role of topic understanding. In author's point of view, the process of thesis topic learning was a crucial experience and brings much knowledge in a financial field.

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## ABBREVIATIONS:

GPM – Gross Profit Margin

ROS – Return on Sales

S&A Expenses – Selling and Administrative Expenses

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