

LB&I International Practice Service Transaction Unit

IPS Level	Number	Title	UIL Code	Number
Shelf	N/A	Business Inbound	–	–
Volume	6	Inbound Income Shifting	Level 1 UIL	9422
Part	6.9	Other Transfer Pricing Issues	Level 2 UIL	9422.09
Chapter	6.9.1	Other Transfer Pricing Issues	Level 3 UIL	N/A
Sub-Chapter	N/A	N/A	–	–

Unit Name	Taxpayer's Affirmative Use of IRC 482
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Document Control Number (DCN)	ISI/9422.09_03(2014)
Date of Last Update	03/24/16

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Issue and Transaction Overview

Taxpayer's Affirmative Use of IRC 482

IRC 482 allows the IRS to make allocations to ensure that taxpayers clearly reflect income attributable to controlled transactions and to prevent the avoidance of taxes. Generally, IRC 482 can only be used by the IRS.

However, taxpayers are allowed to invoke IRC 482 under certain situations:

- On a timely filed U.S. income tax return, the taxpayer is reporting the results of a transaction which are different than the actual prices charged, but is doing so to clearly reflect an arm's length result.
- In appropriate circumstances, the IRS may permit amended returns that increase taxable income if the results are otherwise arm's length.
- A taxpayer can request a setoff when the IRS proposes an IRC 482 allocation. The setoff transactions must be between the taxpayer and the same controlled party involved in the proposed IRC 482 adjustment, be in the same tax year and follow certain procedural requirements.

Taxpayers are not allowed to file an untimely or amended return that decreases U.S. taxable income based on allocations with respect to controlled transactions.



TREATY IMPLICATION: If taxpayer's allowed use of IRC 482 gives rise to double taxation, taxpayer may have access to double tax relief under Article 25 of the US Model Income Tax Treaty and the Mutual Agreement Process.



CONSULTATION: Consult with Counsel and the relevant Issue Practice Network (IPN) for information and resources, if necessary

Issue and Transaction Overview (cont'd)

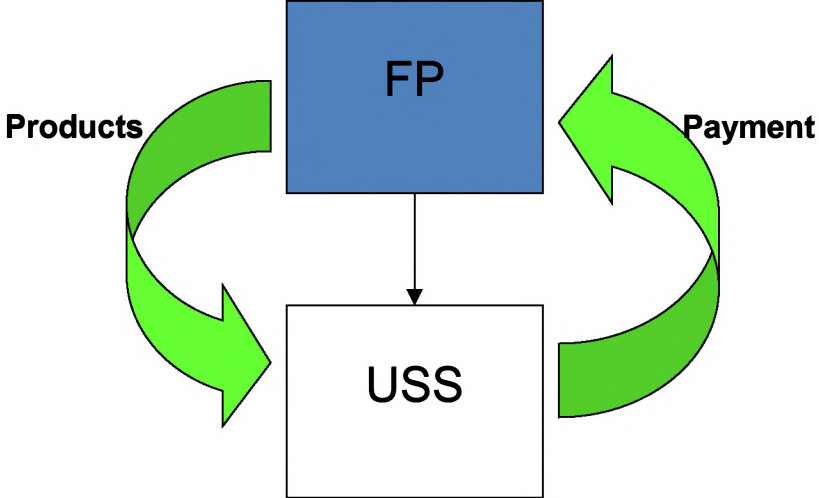
A taxpayer generally will use IRC 482 with a focus on either Treas. Reg. 1.482-1(a)(3) which discusses the taxpayer's reporting of controlled transaction based upon prices different from those actually charged or Treas. Reg. 1.482-1(g)(4) which discusses collateral adjustments and setoffs with respect to allocations under IRC 482 .

A taxpayer may claim setoffs to offset an IRC 482 adjustment made by the IRS. The setoff takes into account the effect of any other non-arm's length transaction between the same controlled taxpayers in the same taxable year in a setoff against the original IRC 482 allocation proposed by the IRS.

These types of adjustments can be applied to both inbound and outbound transactions. However, this practice unit focuses on the inbound transactions from a foreign parent (FP) to a U.S. Subsidiary (USS). Additionally, in order to fully understand the applicability of this practice unit, the reader should also review the "Three Requirements of IRC 482", "Arm's Length Standard", "Comparable Profits Method (CPM) Simple Distributor – Inbound", and "Best Method Determination for an Inbound Distributor" Practice Units.

Transaction and Fact Pattern

Taxpayer's Affirmative Use of IRC 482

Diagram of Transaction	Facts
 <p>The diagram illustrates the transaction between FP and USS. FP is represented by a blue box at the top, and USS is represented by a white box at the bottom. A black arrow points from FP to USS. Two green curved arrows form a cycle: one from FP to USS labeled 'Products', and one from USS to FP labeled 'Payment'.</p>	<ul style="list-style-type: none">▪ FP wholly owns USS.▪ FP is a multi-national manufacturing company based in a foreign country.▪ USS purchases products from FP and distributes them throughout the US.▪ USS records a purchase when these goods are transferred from FP based on a price list established at the start of the tax year. These purchases are included in the total cost of goods sold for the tax year.▪ USS tests the transfer pricing of these controlled transactions after the end of the tax year to verify that the prices charged during the tax year have produced an arm's length result. If these prices have not produced an arm's length result, USS may make its own adjustment to do so. This adjustment may increase or decrease the taxable income of USS. A corresponding adjustment would also be made on FP records.▪ USS timely files a Form 1120 that reflects an arm's length price.

Summary of Potential Issues

Taxpayer's Affirmative Use of IRC 482

<u>Issue 1</u>	Is USS permitted to report, on a timely filed return, an arm's length price that is different from the book price for goods it purchases from FP?
<u>Issue 2</u>	Is USS permitted a setoff when the IRS proposes an IRC 482 adjustment for this tax year?

All Issues, Step 1: Initial Factual Development

Taxpayer's Affirmative Use of IRC 482

USS may set the transfer price of tangible goods purchased from FP in a manner to shift income outside the United States. It is important to establish the facts by examining the supporting documentation that substantiates the transfer price of the goods sold.

Fact Element	Resources	6103 Protected Resources
<p>USS has purchased tangible goods from FP.</p> <ul style="list-style-type: none"> ▪ Is the transfer price for the tangible goods at an arm's length price? 	<ul style="list-style-type: none"> ▪ U.S. Federal Income Tax return (Form 1120) and attachments ▪ Transfer Pricing Documentation ▪ Organizational Chart ▪ Contracts ▪ Intercompany Agreements ▪ Invoices ▪ Functional Analysis ▪ Taxpayer's Financial Statements ▪ Interviews ▪ Transfer Pricing Roadmap 	
<ul style="list-style-type: none"> ▪ Was the transaction reported on USS's return? 	<ul style="list-style-type: none"> ▪ Form 5472, Part IV, Line 14 (Rev. December 2012) ▪ International Information Report (IIR) 	

Issue 1, Step 2: Review Potential Issues

Taxpayer's Affirmative Use of IRC 482

Issue 1

Is USS permitted to report, on a timely filed return, an arm's length price that is different from the book price for goods it purchases from FP?

Explanation of Issue	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ USS is required to report the transfer price of the tangible goods purchased from FP at arm's length. For tax purposes, USS may have to correct its book price (either up or down) to make sure the price paid to FP is an arm's length price. USS may report the correct arm's length price on its timely filed original Form 1120 (including extensions). ▪ If it does not timely file its original return, or if it files an amended return, USS is generally not permitted to increase the price that it paid to FP for filing purposes. (In the example, increasing the price for goods increases costs of goods sold, resulting in an impermissible decrease in taxable income.) 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.482-1(a)(3) ▪ Field Service Advice (FSA)–FSA 200031025 (April 28, 2000) ▪ <i>Intersport Fashions West v. United States</i>, 103 Fed. Cl. 396 (2012) 	



CONSULTATION: Consult with the Transfer Pricing Practice (TPP) for information and resources, if necessary

Issue 1, Step 3: Additional Factual Development

Taxpayer's Affirmative Use of IRC 482

Issue 1

Is USS permitted to report, on a timely filed return, an arm's length price that is different from the book price for goods it purchases from FP?

Fact Element	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Did USS report the arm's length price for the goods purchased from FP on its financial statements (accounting records)? 	<ul style="list-style-type: none"> ▪ Form 1120 ▪ Form 1120, Schedule M-1 or Schedule M-3 ▪ Form 5472, Part IV, Line 14 (Rev. December 2012) ▪ Financial Statements ▪ General Ledger accounts ▪ International Information Report (IIR) 	
<ul style="list-style-type: none"> ▪ What was the price/value reported for the Customs Declaration Form for the goods purchased from FP? ▪ Were the Customs Declaration Forms corrected to reflect the adjusted price? 	<ul style="list-style-type: none"> ▪ U.S. Customs Declaration (Form 7501) and Instructions 	

Issue 1, Step 3: Additional Factual Development (cont'd)

Taxpayer's Affirmative Use of IRC 482

Issue 1

Is USS permitted to report, on a timely filed return, an arm's length price that is different from the book price for goods it purchases from FP?


Fact Element	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Did USS make the adjustment to the price it paid to FP on its financial statements or as an adjustment on the tax return (Schedule M-1 or M-3)? 	<ul style="list-style-type: none"> ▪ Form 1120, Schedule M-1 or Schedule M-3 ▪ Financial Statements ▪ General Ledger system ▪ Transfer Pricing Documentation 	
<ul style="list-style-type: none"> ▪ Is the adjustment supported by documentation? 	<ul style="list-style-type: none"> ▪ Transfer Pricing Documentation ▪ Research Studies ▪ Pricing analysis & verification procedures 	

Issue 1, Step 4: Develop Arguments

Taxpayer's Affirmative Use of IRC 482

Issue 1

Is USS permitted to report, on a timely filed return, an arm's length price that is different from the book price for goods it purchases from FP?

Explanation of Adjustment	Resources	6103 Protected Resources
<p>The argument of whether the taxpayer has made a timely adjustment pursuant to IRC 482 is based on the facts and circumstances of each specific case.</p> <ul style="list-style-type: none"> ▪ Was the taxpayer's self-initiated adjustment made pursuant to Treas. Reg. 1.482-1(a)(3)? ▪ Was the self-initiated adjustment in excess of the customs value? ▪ How were the conforming adjustments treated by taxpayer? 	<ul style="list-style-type: none"> ▪ IRC 1059A ▪ Treas. Reg. 1.482-1(a)(3) ▪ Treas. Reg. 1-482-1(b) ▪ Treas. Reg. 1.482-1(c) ▪ Treas. Reg. 1.482-1(g)(3) ▪ FSA 200031025 (April 28, 2000) ▪ <i>Intersport Fashions West v. United States</i>, 103 Fed. Cl. 396 (2012) ▪ Rev. Proc. 99-32 	
<div style="display: flex; align-items: flex-start;">  <p>DECISION POINT: Determine if the taxpayer's self-initiated IRC 482 adjustment was made correctly and included on a timely filed tax return including extensions. Otherwise, the taxpayer's self-initiated adjustment should be disallowed.</p> </div>		

Issue 2, Step 2: Review Potential Issues

Taxpayer's Affirmative Use of IRC 482

Issue 2

Is USS permitted a setoff when the IRS proposes an IRC 482 adjustment for this tax year?

Explanation of Issue	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ When the IRS proposes an IRC 482 adjustment, USS may claim another IRC 482 adjustment to offset the IRS proposed adjustment. This setoff adjustment is permitted if it is an adjustment to a non-arm's length transaction in the same taxable year between the same parties to the transaction in question. ▪ USS must also satisfy the following procedural requirements: <ul style="list-style-type: none"> - Establish that the setoff transaction was not arm's length; - Establish the amount of the appropriate arm's length charge; - Document all correlative adjustments resulting from the setoff; and - Timely notify the IRS (within 30 days after the earlier of the Notice of Proposed Adjustment (NOPA) or Statutory Notice of Deficiency). 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.482-1(g)(4) - Setoffs ▪ Rev. Proc. 2005-46 	

Issue 2, Step 3: Additional Factual Development

Taxpayer's Affirmative Use of IRC 482

Issue 2

Is USS permitted a setoff when the IRS proposes an IRC 482 adjustment for this tax year?



Fact Element	Resources	6103 Protected Resources
<ul style="list-style-type: none">▪ Has USS identified any non-arm's length transactions between it and the FP for the same tax year as the IRS proposed IRC 482 allocation?	<ul style="list-style-type: none">▪ Transfer Pricing Documentation▪ Organizational Chart▪ Contracts▪ Intercompany Agreements▪ Invoices▪ Functional Analysis▪ Taxpayer's Financial Statements▪ General Ledger▪ Interviews▪ Transfer Pricing Roadmap	

Issue 2, Step 4: Develop Arguments

Taxpayer's Affirmative Use of IRC 482

Issue 2

Is USS permitted a setoff when the IRS proposes an IRC 482 adjustment for this tax year?

Explanation of Adjustment	Resources	6103 Protected Resources
<p>The argument of whether the taxpayer is entitled to a <i>setoff</i> adjustment pursuant to IRC 482 is based on the facts and circumstances of each specific case</p> <ul style="list-style-type: none"> Was the taxpayer's request for a setoff made pursuant to Treas. Reg. 1.482-1(g)(4)(ii)? 	<ul style="list-style-type: none"> Treas. Reg. 1.482-1(g)(4) – Setoffs Rev. Proc. 2005-46 	
<p> DECISION POINT: Determine that the <i>setoff</i> adjustment is allowable, has been correctly determined and the procedural requirements have been met.</p>		
<p> CONSULTATION: Consult with counsel or the relevant Issue Practice Network (IPN) and resource materials concerning setoffs, if necessary.</p>		

Training and Additional Resources

Chapter 6.9.1 Other Transfer Pricing Issues

Type of Resource	Description(s) and/or Instructions for Accessing	References
CENTRA session	▪ 2012 (TPO) SABA – Overview and Introduction to 482	
Issue Toolkits	▪ IRM 4.61.3 Development of IRC section 482 Cases	
Issue Toolkits	▪ IRM 4.61.3-4 Functional Analysis Questionnaire	
Issue Toolkits	▪ Audit Tool – Checklist and Audit Tool for Developing Transfer Pricing Issues	
Other Training Materials	▪ <i>Bittker & Lokken Fed. Tax'n Inc.</i> , Est and Gift Chapter 79: Reallocation of Income and Deductions	

Glossary of Terms and Acronyms

Acronym	Definition
FP	Foreign Parent
FSA	Field Service Advice
IBC	International Business Compliance
IPN	International Practice Network
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
LB&I	Large Business & International
OECD	The Organisation for Economic Co-operation & Development
TPO	Transfer Pricing Operations
TPP	Transfer Pricing Practice
NOPA	Notice of Proposed Adjustment
UIL	Uniform Issue List
USS	United States Subsidiary

Index of Related Issues

Issue	Associated UIL(s)	References
Purchase of Tangible Goods - Inbound	9422.07	Practice Unit, "Purchase of Tangible Goods From a Foreign Parent CUP Method", DCN: ISI/9422.07_05(2013)
Functional Analysis for Inbound Distributor	9422.07	Practice Unit, "Best Method Determination for an Inbound Distributor", DCN: ISI/9422.09_04(2013)
Comparable Profits Method (CPM) for a Simple Distributor – Inbound	9422.07	Practice Unit, "CPM Simple Distributor Inbound", DCN: ISI/9422.07_07(2013)
Three Requirements of IRC 482	9422.09	Practice Unit, "Three Requirements of IRC 482", DCN: ISI/9422.09_02(2014)
Arm's Length Standard	9422.09	Practice Unit, "Arm's Length Standard", DCN: ISI/9422.09_06(2013)
Rev. Proc. 99-32 – Inbound	9422.09	Practice Unit, "Revenue Procedure 99-32 Inbound Guidance", DCN: ISI/9422.09_08(2014)