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Transfer Pricing In Emerging Markets

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ABSTRACT

Purpose. The purpose of this article is to study the relevant areas of using transfer pricing as a corporate strategy, a model of commercial operations, and a mechanism for managing corporate finances. Methodology. The methodological basis of the study is a set of proposed tools and models for researching corporate business operations. Along with a model for analyzing the economic operations of an integrated enterprise based on improving the structural and functional approach and quantitative and analytical tools for functions assets risks analysis. The quantitative and analytical tools for the qualitative assessment of business operations of integrated operating assets of developing countries as part of holding-type parent groups have also been improved. Approach. The methodological approach takes into account the general requirements of the legislation of developing countries on the example of the CIS countries. The article describes the results of the systematization of the main characteristics of the transfer and transfer pricing. The authors examine in detail the transfer pricing methods that are most often found in the tax laws of developing countries. On the example of the CUP-method, recommendations on the use of this method in various business operations are described in detail. Findings. The article describes the experience from real practice of applying a methodological approach to the analysis of corporate operations, used by leading world-class consulting companies. The results can be applied both in scientific research of issues related to transfer pricing and in the practice of preparing tax reporting of assets from developing countries.

INTRODUCTION

Owing to global integration processes, many large industrial enterprises of developing countries in recent years have joined the large transnational integrated corporate associations (holdings and groups). The competitive advantages that these business structures have and use are based on the use of optimization schemes and tools of the corporate management system, which include the transfer pricing mechanism. The main goal of the corporate business structure is to maximize consolidated profits, and among the key strategies, the priority is occupied by the functional ones:

– price;
– commodity;
– marketing;
– innovation and investment;
– strategic development of personnel;
– IT and logistics (Adams and Drina, 2008; Forkiewicz et al., 2015).

It should be noted that the pricing strategy requires the observance of clear principles of pricing tactics. Managerial internal prices and tariffs are established for goods, services and other objects of transfer of holding structures between themselves. An effective mechanism must be created that establishes the principles for conducting business operations at special internal (transfer) prices (tariffs). Goals, methods, approaches to setting prices (tariffs) should be defined, as well as instruments of influence and implementation of holding strategies (Ugrovata, 2014; Worldwide Transfer Pricing Reference Guide, 2015). The point at issue is the transfer pricing mechanism. This mechanism is most often used by enterprises and companies that are part of a single holding business structure, when carrying out commercial operations among themselves. In this case, such prices and tariffs are used that do not necessarily correspond to the market level. Thus, a kind of redistribution of the financial resources of the holding is carried out, aimed at optimizing the consolidated profit at the highest level of the corporation. In particular, this is achieved by the following:

- reduction of production costs (due to savings on the services of related companies, ensuring the successful flow of key operational business processes at internal corporate prices/tariffs);
- tax optimization. Hence, if there are enterprises and companies (in the portfolio of the holding group) that are located outside the national economy, i.e. in places where the income tax rate (corporate tax) is lower, the company receives a large profit in this case. This is what allows owners of large corporate structures to optimize (reduce) the taxable income of a business (Dicken, 2007; Daxkobler, 2014, Fomina).

It is worth noting that at present, practically all over the world, transfer pricing is a fairly common strategy, pricing model and mechanism at the same time, which is used by corporate structures of various business sectors. This is due to the effectiveness of using this mechanism (Baker, 2014; Sadang, 2017). Besides, most often, the effect of using transfer pricing is determined by the strategy of location of cost centers (manufacturing enterprises) in developing countries and countries with weak economies. At the same time, income centers are opened in offshore and low tax jurisdictions, and head offices – in developed countries with a strong economy and a working legal base (Forkiewicz et al., 2015; Garcia-Bernardo et al., 2017).

Such a strategy is very beneficial for the holding itself, but it harms the state budgets of developing countries as a result of a shortfall in part of the fairly earned profit of the national manufacturing enterprises that are part of such holding structures. After all, redistributed capital through the use of transfer pricing is sent to offshore zones and countries where it is taxed at minimum or zero rates (Model Tax Convention on Income and on Capital, 2010; Model Double Taxation Convention between Developed and Developing Countries, 2011).

This problem stimulates both national state bodies of developing countries and international organizations (in particular, the OECD, specialized UN units, etc.) to look for ways to counter the withdrawal of capital from developing countries (economies). Such measures include BEPS, MLI, etc. (OECD, 2010; Hofmann and Riedel, 2020). However, there is a problem of revealing the facts of the use of transfer pricing by national enterprises and corporations, since the tax authorities' control systems (of such cases) in developing countries have not yet been developed. This necessitates the analysis of intra-group corporate commercial operations adapted for developing countries (economies), which, in fact, is the subject of this study (Gudehus and Kotzab, 2012; Cooper et al., 2017). Thus, the research issues addressed in this study are as follows:

- study the terminology of transfer pricing, propose an approach to the classification of corporate transfers, objects of international internal corporate operations;
- analyze the tax laws of developing countries (on the example of the CIS region);
- develop a methodological approach (adapted for developing countries) to analyze the use of transfer pricing in commercial transactions between linked assets of international corporations.

1. LITERATURE REVIEW

Most often, transfer pricing refers to the process of generating prices for goods or services that are different from the market level, for assets that are linked together within integrated structures (holdings and groups) (Klassen et al., 2017; Davies et al., 2018). The results of the analysis of existing scientific approaches to the definition of the concept and scope of transfer prices indicate the following. The transfer price is an extremely important object of corporate accounting and planning in companies that are part of the organizational structures of transnational integrated holdings and groups. The optimization effect of transfer prices in the system of corporate management accounting in the activities of integrated enterprises and companies is aimed at maximizing the efficiency of the holding (group) as a whole (Adams and Drina, 2008; Sadang, 2017).

It should be noted that in the world, especially in developing countries (including countries of the CIS region, China, India, UAE, Turkey, etc.), the number of scientific publications in the field of transfer pricing is growing every year, more and more scientists are joining to study this issue (The Law of the Republic of Kazakhstan, 2008; Federal Law of Russia, 2011; Baker, 2014; Arnold, 2016; Cabinet of Ministers Resolution of Ukraine, 2016). Many scientists offer their own approaches to the definition of the terms “transfer price”, “transfer pricing”, but everyone agrees that these are:

- parent group’s control mechanisms;
- cash flow management tools within the holding structure;
- instruments of protecting transnational corporations (TNCs) from adverse taxes, foreign exchange control, tariffs, state restrictions on operations with profit (Countries updates – Global transfer pricing insights within reach, 2017; Nagpal and Dutta, 2019).

In general, the category “transfer price” consists of two economic terms – “price” and “transfer”. The category “price” is fundamental and already well-studied in economic science and thus the authors have decided to focus on the essence of the term “transfer”. This term has a multiple spectrum of meanings, but most often it is used to denote free movement of cash or material assets between subjects of economic relations. In particular, in the budget process, it means the transfer of funds between entities of the general government sector on an irrevocable and gratuitous basis. In the preparation of the country's balance of payments – the free provision of economic values (goods, services or financial assets), in banking – the transfer of funds without changing their owner, etc. Often, authors disclose the economic nature of transfer pricing using the categories of “internal firm value” and “internal firm marginal utility” within the framework of value and marginalist price theories. Such authors also note that in organizations with a high degree of decentralization of managerial functions, structural units have significant freedom in making economic decisions (transfer prices carry out accounting, measuring, balancing, stimulating, redistributive functions, etc.- Curtis, 2008; McNair et al., 2010).

On the other hand, in the conditions of strict centralization of internal business processes, the transfer price is primarily informative, that is, to perform only an accounting and measuring function. From the point of view of researchers, in the framework of the theory of enterprise economics, the transfer price should be considered as an important component of the internal economic mechanism of the enterprise. While such a mechanism is based on decentralized management and the expansion of the responsibility of structural divisions for business results (Forkiewicz et al., 2015). Among the methods of transfer pricing, the market method is primarily used, double transfer pricing is also of interest. This system is often based on a synthesis of two approaches to setting the transfer price, namely:

- the market method for departments: an intermediate product is bought in the domestic market and, after its processing into the final one, it is sold in the foreign market;
- cost method for departments that produce an intermediate product and then sell it to other departments. Double transfer prices do not allow obtaining balanced data in management accounting, which requires the introduction of certain adjustments to units' performance. Double transfer pricing is not very common in practice, since it does not stimulate cost savings and does not give clarity to responsibility center managers on the level of decentralization (OECD, 2010; Model Double Taxation Convention between Developed and Developing Countries, 2011).

Currently, general accounting in TNCs (transnational corporations) can be divided, as a rule, into two subsystems – external financial and internal – management (production, operational). The management accounting system is associated with responsibility centers acting as accounting objects. In turn, the object of management accounting is the results, which can also be taken into account at the place of occurrence of costs and cost carriers. In the process of comparing the costs and results of various accounting objects, the effectiveness of production and economic activity is revealed. To ensure economic relations between the internal divisions of the enterprise, a transfer pricing system is being created (Porter and Schwab, 2008; The official website of OECD, 2020). The transfer price is the price used in the calculations between the internal structural divisions of the enterprise, they transfer products, works and services to each other (Urquidi, 2008; Worldwide Transfer Pricing Reference Guide, 2015). At the same time, in a number of international publications (devoted to transfer pricing), it is noted that transfer pricing is the process of establishing internal estimated prices (other than market) between units of one control center, as well as the sale of goods and services in a circle of related parties. The transfer pricing mechanism is inherent in transactions between related parties and is based on non-market factors, in business practice it is customary to refer to one of the classical optimization schemes of tax planning. In this regard, the main task and, accordingly, the starting point for building the foreign economic policy of tax legislation is to achieve a balance of interests of the jurisdiction and the taxpayer. So that the latter, for the purpose of reducing the tax burden, will not go beyond both geographical and legal borders. The authors argue that transfer prices are used in various sectors of the economy:

- by state statistics authorities when calculating price indices;
- in the banking sector, the transfer price is equal to the concept of the transfer rate that is established for the distribution of income and expenses in the structural divisions of one bank (Dicken, 2007; United Nations, 2013).

There is also another approach to the interpretation of the transfer price, according to which the transfer price is the internal estimated price at which the sale of goods (services) takes place. This proposal of scientists does not sufficiently reveal the essence of the use of transfer prices in modern business conditions. Adherents of this approach believe that transfer prices are used as a tool for:

- implementing the planning and control functions;
- regulation of corporate relations based on specialization and cooperation of production;
- implementation of planned volumes and structure of production;
- provision of raw materials and supplies within a single technological cycle;
- ensuring high quality of products (Pendse, 2012; Helminen, 2016).

In general, in the practice of corporate relations, the transfer price performs the same functions as the market price. Among these functions, the most important are measuring and stimulating. The first is manifested through the accounting of production costs for an intra-company transaction, the second – through the profit accounting, which is calculated in accordance with the structure of the transfer price. Regarding the scope of application, transfer prices apply:

- firstly, in profit centers and investment centers of large corporate structures. Sometimes they are used in cost centers. The motivation for using transfer prices is based on the regulation of cash flows between enterprises and tax optimization in the process of product sales by one structural unit of the corporate structure to another;
- secondly, transfer prices can be applied within the framework of one legal entity, but this person is a structural unit of the corporate structure and most often is the center of profit. The goal of this company is to maximize the profits of the entire corporation by increasing the profits of individual financial responsibility centers (hereinafter – FRC) participating in the production chain (OECD, 2010).

2. METHODS

2.1 Research Design

Let us consider the main aspects and highlight the legislative and regulatory framework for transfer pricing of developing countries on the example of the countries of the CIS region. Thus, in the CIS countries (such as Russia, Ukraine, Kazakhstan), there are laws establishing and regulating the transfer pricing mechanism at national enterprises that are parts of corporate integrated structures. Namely, laws on amendments to the tax codes of countries regarding transfer pricing (for example, in Russia such a law was adopted in 2011, in Ukraine – since 2013) (The Law of the Republic of Kazakhstan, 2008; Federal Law of Russia, 2011; Cabinet of Ministers Resolution of Ukraine, 2016).

Articles of tax codes related to transfer pricing, enshrined in these laws, are mostly based on "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" (2010). The key principle of using transfer pricing in corporate business transactions is the principle of an outstretched hand, the main point of which is to comply with the principle of market price that related companies must follow. The aforementioned laws usually regulate that transfer prices are applied in transactions between related parties, the volume of which exceeds the established limit for the corresponding calendar year, that is, these transactions will be treated as controlled. Besides, according to the laws, operations equated with controlled operations may fall under control. As in international practice, and in accordance with the national laws of the CIS countries, the latter include operations in the field of foreign economic activity. While the subject of foreign economic agreements-goods of world exchange trade (oil, metal, mineral fertilizers and other goods) and one of the parties is a non-resident having offshore status.

Analyzing the legislative framework on transfer pricing of a number of developing countries, it is easy to notice their close relationship and common features among themselves. In the case of the CIS countries, this is due to a common historical past, the principles of economic activity by enterprises and their associations. Many key legal acts and regulations contain similar information, distinguishing features are found in the following:

- establishment of operations equated to controlled. This criterion includes operations between persons who are not related, if they do not perform any additional functions in the agreement, except for the sale of goods (services) to a person associated with the participant in the operation. It is also interesting to consider the position of the legislator on the inclusion in this criterion of transactions with enterprises that declare losses for the last two tax periods.

– according to the norms of the tax legislation of the CIS countries, a business transaction may be deemed controlled by a court decision.

At the moment, the United States has the most developed legislative and scientific-methodological base in the field of the functioning of the transfer pricing mechanism at integrated companies. The US has accumulated rich experience in controlling transfer pricing. Transfer Pricing is governed by section 482 of the United States Tax Code (Internal Revenue Code Section 482) (Transfer pricing in the USA, 2019). It is worth noting that the theoretical and methodological basis of the United States Tax Code, like most developing countries, is the “OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations”. Despite the latter, the American analog contains specific practical recommendations based on the experience of world transnational corporations in various fields of business and economic activity. Another important fact is that the American transfer legislation, unlike the analogs of developing countries, regulates in more detail the procedure for applying a certain pricing method in relation to specific types of transactions. For some types of transactions, pricing methods are explicitly specified in the regulatory document. The use of a method not stipulated in the tax code in the United States is allowed only if the taxpayer proves that this method most reliably complies with the “arm's length principle”. Evidence must be documented. At the same time, the taxpayer takes all the same measures as in the case of justifying the stipulated pricing method (Transfer pricing in the USA, 2019).

In the recommendations on documentation when concluding a price agreement, the legislation of developing countries (for example, the CIS – Russia, Ukraine, Kazakhstan) discloses the order of evidence in a way similar to that in the USA. Namely, each of the recommended methods is consistently assessed and by exclusion the optimal pricing method is selected (The Law of the Republic of Kazakhstan, 2008; Federal Law of Russia, 2011; Cabinet of Ministers Resolution of Ukraine, 2016). When considering the Law “On Transfer Pricing” in the Republic of Kazakhstan, it should be noted that it has been adopted earlier than in Ukraine and Russia (2013 and 2011, respectively) – back in 1995. Its last revision – July 5, 2008. Among the features of the Law, there are many differences in the interpretation of the main provisions (despite the similarities in essence):

– Firstly, the detailed description in this law of the “arm's length principle”. The principle that is used to determine the market price taking into account the price range. It is based on a comparison of the terms of transactions between related parties with the terms of transactions between independent parties performing transactions at a market price, determined in the manner prescribed by this law;
– Secondly, the presence of such categories and concepts as differential, price range, price information source, etc. The very concept of transfer price (transfer pricing) in the legislation of Kazakhstan is the price that is formed between related parties and (or) differs from the objectively forming market price, taking into account the price range (controlled by this law) for transactions between independent parties.
– Thirdly, the differences between determining the composition of participants, which can be characterized as “related parties”, a broad approach to determining the procedure for monitoring cases, etc.

Essential common features are sole methods for determining the transfer price in the legislation of all three countries – Kazakhstan, Russia and Ukraine; the use of the “arm's length principle”, a system of certain fines and sanctions in relation to violation of the law, etc. It should be noted that the system of legislation in Kazakhstan in this area is distinguished by the presence of a wide database of information resources, the data of which in one form or another are recognized by the courts as the basis for applying adjustments. The number of similar features of the legislation regarding transfer pricing (adopted at the moment in more than 60 countries of the world) can be explained by the fact that the legislation of post-Soviet countries is mainly based on the provisions of the OECD guidelines. However, such legislation still has local specificity and, unfortunately, does not yet contain practical recommendations based on the experience and realities of the economic activities of national companies.

2.2 Data Analysis

In this section, the authors analyze in more detail the main factors influencing the use of transfer pricing, its methods. On a specific example, the authors consider the correct choice of the transfer pricing method. Typically, the transfer prices are determined by the internal policies of the corporate structure – the group or holding. Transfer prices are extremely important because they determine the taxable base of profit in the countries in which the group units (involved in business operations) are registered. These are the operations on the sale of finished products, purchase of raw materials, stocks, semi-finished products, financial transactions, including provision of loans in favor of related parties, etc. Hence, transfer pricing is an object of close attention on the part of:

- tax management of international groups, as this may affect the amount of profit subjected to income tax (corporate tax) in various jurisdictions in which international group's structural business units are involved in intercompany transactions with each other in order to generate the maximum amount of total corporate profit;
- tax authorities that are concerned that the use of this mechanism by groups can negatively affect the amount of income earned on income taxes (corporate tax) in their country.

Therefore, international companies and tax authorities require a certain standard to agree on what the transfer price should be. The standard in question is applied in the jurisdictions of most developed countries of the world, and is based on the "arm's length principle" proposed by the OECD. This principle determines whether the terms of transactions (that fall under the transfer pricing rules) comply with the following conditions. Namely, the conditions that would have occurred when similar transactions were carried out between entities independent of each other (OECD, 2010). In practice, it is practically impossible to find identical market operations between independent companies that could be compared with the analyzed controlled operation. Therefore, it will be optimal to find the most approximate transaction between unrelated companies that have the same subject of operation (referring to the object of transfer – goods, services, works, loans, etc.). Besides, these companies should operate in similar financial and commercial conditions, use the same business strategies in the market, have similar functions and risks. These conditions are a kind of parameters and are used in functional analysis, and also affect the choice of the pricing method by which the controlled operation will be tested in the economic analysis.

In accordance with the articles of the tax codes of developing countries (using the example of the CIS region), most often five transfer pricing methods can be applied, namely:

- comparative uncontrolled price method;
- resale price method;
- "cost plus" method;
- net profit method;
- profit distribution method (The Law of the Republic of Kazakhstan, 2008; Federal Law of Russia, 2011; Cabinet of Ministers Resolution of Ukraine, 2016).

On the other hand, the choice of the method is also significantly affected by the structure of the transaction (composition of its participating companies) and the degree of its complexity. The structure of the transaction may include the following:

- manufacturers;
- distributors;
- transport companies;
- logistics operators;
- service providers (repair services, equipment installation, etc.);
- financial facilities;
- banking structures;

- management companies of the group (for example, in purchase-sale transactions of large assets, corporate rights to enterprises, etc.);
- end consumers, etc.

The specificity of pricing mainly affects the availability and accessibility of information on the conditions for the implementation of similar transactions between independent companies. The latter is necessary for a comparative analysis in the preparation of documentation and a report on controlled transactions. Basically, this is information about:

- prices (comparative uncontrolled price method, resale price method);
- financial and accounting reporting data of companies necessary for calculating profitability indicators (Cost Plus methods, net profit method);
- calculating the market interquartile range;
- ability to conclude whether the price in the analyzed operation is included in a given price range or profitability.

The authors consider in more detail the comparable uncontrolled price method (hereinafter – CUP method), used in OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. Let us consider the conditions for using this method and give practical examples that will allow one to more clearly understand how and where exactly this method is the most optimal for use. In general, the CUP method involves comparing the price used in a controlled operation with the price set for identical or homogeneous goods. Besides, the analyzed operation is compared with independent operations between independent counterparty companies. In order to apply this method, it is necessary to use information on agreements concluded for the purchase/sale of identical (or homogeneous) goods by the taxpayer or other persons, in comparable financial and commercial conditions in the relevant goods market. In the practice of transfer pricing in the CIS countries (Russia, Ukraine, Kazakhstan), the CUP method is usually used in two cases:

- based on information about comparable business transactions of a company participating in a controlled operation. The operations of this company with other independent counterparties are analyzed whose operations are not subject to the control of transfer pricing rules in the state;
- based on information about comparable transactions in general between third unrelated counterparties and comparing them with the price in the analyzed controlled transaction.

Let us give an example of the application of CUP method. In the example, it is proposed to consider the application of the CUP method when analyzing external prices. This is a more frequent case and is explained by the fact that it is usually quite difficult to find other operations of the company in question with unrelated counterparties. Namely, the operations that occur under conditions comparable to the studied one, or the subject of which is completely similar goods or services. *Example. 5 May 2016. Company A, located and registered in accordance with US law, exported coal mined in its own mine to a related Ukrainian company B. The price of goods is X dollars per ton. Delivery is carried out under the terms of CIF for the Ukrainian logistics metal center through Odessa State Commercial Port (Odessa, Ukraine). The price does not include all shipping costs associated with the delivery of goods.*

Thus, in this example, the commodity that is the subject of the transaction – coal – is included in the approved (in accordance with the Cabinet of Ministers' Decree as of September 8, 2016 No. 616) list of goods to be quoted on world exchanges (Cabinet of Ministers Resolution of Ukraine, 2016). Namely, it belongs to the group “Coal, anthracite, pulverized or non-pulverized, but not agglomerated, other” (according to Ukrainian classification of goods of foreign economic activity UCGFEA). In order to establish compliance of the conditions of controlled operations with the “arm's length principle”, namely the search for homogeneous operations for the export of coal, it is advisable to use the information available on the following resources for this group of goods. Namely, such as European Energy Exchange (EEX), Intercontinental Exchange, Chicago Mercantile Exchange (CME) and New York Mercantile Exchange (NYMEX). It is worth noting that it is necessary to start searching for external comparable quotes in the case when one is convinced that the company in question has not carried out other uncontrolled transactions with unrelated persons. Namely, the transactions that are homogeneous in relation to the controlled company. Thus, it will be possible to use the internal price method to apply the CUT method. On the CME portal, average quotes (that is, average consumer prices) for coal on the European market were found, which, for example, are presented in the Platts agency database published for the period from May 1, 2016 to May 30, 2016. It is worth noting here that in the search process it is necessary to pay attention to:

- comparable types of coal that are listed on the exchange according to the European classification and decide whether they can be compared with the domestic type B coal.
- delivery basis according to INCOTERMS classification (in this case, it would be appropriate to look for delivery conditions CIF European ports).
- coal is supplied from the producer (as in this case), or through resellers, in which case one needs to reject such quotes.

The authors also draw attention to the fact that in this case spot prices are indicated (not long-term prices), that are formed on the market at a certain point in time (in this case, on a date close to the contract under consideration). The latter allows judging that this is exactly the price at which independent producers sell their goods to independent distributors. Let us assume that we have been able to find comparable quotes for coal for the selected period – May 2016. Next, one forms a sample, and now a task is to calculate the market price range in order to determine whether the price in the analyzed controlled operation is included in this range. That is, whether it is a market price (if included) or a transfer price (if not included in the calculated range). However, before this can be done, the necessary adjustments must be made. For this it is necessary: *firstly*, to adjust for the amount of freight (if quotes are found for contracts that differ from the CIF conditions, for example, FOB). In this case, one should pay attention to the fact that CIF includes freight, and FOB – not, therefore, if one does not make the necessary adjustments, the prices will be quite significantly different from each other; *secondly*, adjust for transportation costs. Different delivery ports and distances also affect the shipping cost included in the price of goods. It is also necessary to evaluate, whether the price in question includes the cost of transporting cargo to the enterprise after its shipment, let us say, in the port of Mariupol. In our case, the price of coal does not include the cost of delivery and thus it is possible to make an adjustment. In other cases, it is very difficult to distinguish these delivery costs from the total price of the goods, which makes it difficult to use the CUP method. In some cases, it may also be necessary to conduct an economic analysis and find out the average delivery rate per ton in the period under review. In our case, this is May 2016. For example, in the studied sample, there may be contracts under the terms of CIF Rotterdam, that is, coal is unloaded at the port of Rotterdam (Netherlands), and then, for example, it can be transported to the customer. Therefore, one needs to see what difference in the cost of delivery will be between such a contract and the analyzed operation; *thirdly*, attention should be paid to the difference in the currency of the contracts under which operations are carried out. For example, if an operation is found in euros, then one needs to convert the price of coal into US dollars in accordance with the euro/US dollar rate on the date of transaction; *fourthly*, attention should be paid to the possible use of discounts or premiums on goods. This can be a one-time operation, but usually, operations at a spot price are carried out for fixed volumes of goods delivery, that is, discounts on large tonnage are possible, or, on the contrary, allowances that can be charged for small and/or one-time consignments. In this case, the price will also need to be adjusted for the size of such allowances or discounts. The considered case, when the CUP method is used in operations with goods (that are listed on exchanges) is quite common. Besides, as already noted, it is often used in financial transactions.

3. RESULTS

A theoretical analysis of the national base of scientific economic sources also did not reveal exact definitions of “transfer mechanism”, “mechanism of transfer pricing”. In order to give an exact definition, it was decided to pay attention to existing approaches to determining the most important component of this concept – “transfer” and possible areas of its use. An analysis of the results of research and development of scientists found that modern scientific sources of information lack exact definitions of “transfer” (as an object of corporate distribution processes), “transfer mechanism”, and “transfer pricing mechanism”. Only a superficial attempt was made to develop methodological approaches to the classification of corporate transfers, transfer mechanisms operating in large industrial holdings and groups. It is proposed to consider “transfer” as an economic category that is used to determine the objects of transfer between related divisions within the same corporate structure on financial and commercial terms that are different from market ones. The main goal of such a transfer is to optimize the pricing process and to avoid double counting of these objects of movement in order to optimize corporate taxation. Theoretical approaches to the definition of “transfer” are summarized, systematized and illustrated in Figure 1.

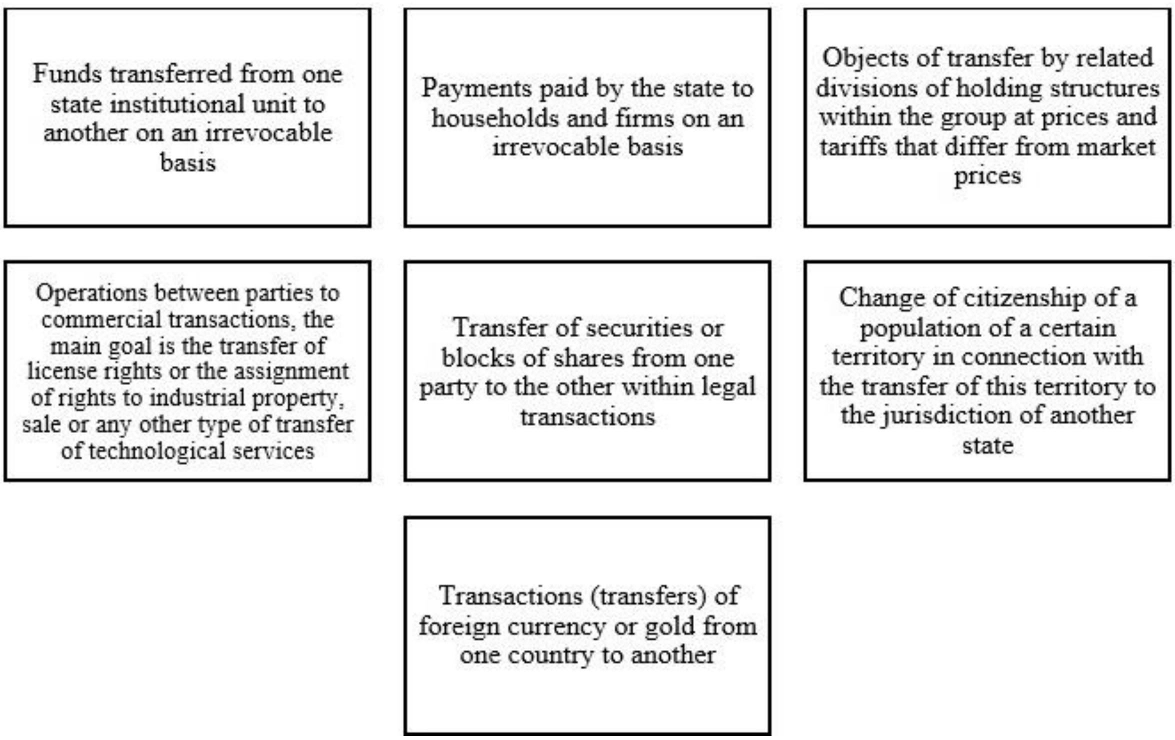

Figure 1. Theoretical approaches to the definition of "transfer"

Source: elaborated by the authors

In the current study, it was decided to clarify the concept of “transfer” specifically applicable to intragroup corporate operations at prices and tariffs other than market ones. According to this, the scope of operation is transnational corporate structures (holdings and groups). In general, it is worth noting that it is necessary to develop a theoretical and methodological framework for the functioning of transfer pricing mechanisms in an integrated enterprise. Thus, national enterprises will be able to prove that prices set for manufactured products or services are ordinary and not transfer. They will also have the opportunity not to adjust their tax base, paying the amount that the state loses as a result of applying transfer prices (which is required by national legislation in this area). Besides, the state tax authorities will be able to create a kind of mechanism that will allow controlling the amounts that the state budget loses due to the use of transfer pricing mechanism by integrated enterprises. In addition, this will allow the company to optimize its own pricing system and taxable income base. Methodological approach to effectiveness analysis of transfer pricing mechanism in an integrated enterprise (hereinafter – methodological approach) is illustrated in Figure 2.

Methodological approach to analyzing the impact of the corporate transfer pricing strategy on business operations	1. Grouping and systematization of information on the totality of company's business operations for the reporting period - use of international financial reporting databases (developing countries use: SPARK, AMADEUS, RUSLANA, TEUMPHSON ROEYTERS, Blumberg)
	2. The formation of a database of comparable operations of companies-counterparties: -comparative characteristics of markets -systematization of financial and commercial conditions for comparable operations
	3. Operations analysis: -subject analysis -functional analysis - FAR (Functions / Assets / Risks) - economic analysis

Figure 2. Methodological approach to analyzing the impact of the corporate transfer pricing strategy on business operations

Source: elaborated by the authors

It should be noted that this methodological approach was developed on the basis of the practice of commercial relations between production and marketing companies that are part of international corporations in a number of business segments (The official website of OECD, 2020; The official website of the group "Marsegaglia", 2020; The official website of the group "SCM", 2020; The official website of the Group ArselorMittal, 2020). It is necessary to develop an algorithm for detecting controlled operations of an enterprise that uses a transfer price system. The comparative analysis procedure should be structured for comparability of commercial and financial conditions of transactions of an integrated enterprise. For these purposes, it is recommended to use a model for verifying whether integrated enterprise's business operations:

- can be controlled;
- comply with regulatory provisions of national legislation on transfer pricing and practical recommendations of OECD and UN Department of Economic and Social Affairs.

Typically, such models are described in tax law. Particular attention in the proposed methodological approach is also focused on the functional analysis of operations. It was decided to improve functional analysis in the form of FAR (Functions Assets Risks) – analysis described in OECD methodologies. This analysis is a three-step analysis of the following:

- functions performed by enterprises that are parties-contractors in relation to each other under the contracts of sale of goods (works, services);
- risks that the parties assume in the production and sale of goods;
- assets that the parties attract to produce goods or provide works/services.

It is also important to analyze the commercial business strategies of the counterparties and the main sales markets for goods. The assets of the holding or group operate according to a single global strategy, respectively, the process of its implementation is controlled by the managing company. It is also necessary to take into account the nature of the financial obligations undertaken by the parties, to analyze the features of the established relations and the terms of contracts between the parties to the transaction, and analyze the economic conditions of the parties to the transaction. Functional analysis opens up an idea concerning company's interaction with its interdependent and associated enterprises and companies and their respective functional roles in controlled operations. This view allows one to understand how corporate relations between companies of one integrated holding affect the price of goods (works/services) in a transaction and the level of profit that is received as a result of a transaction. From the point of view of the OECD and the UN Department of Economic and Social Affairs, high income can be obtained as a result of transactions with the highest level of asset utilization and the highest risk. Characteristics of the level of risks, functions and assets are reflected by the corresponding symbols for the degree of growth (*, **, ***). It is proposed to improve this methodology by supplementing it with the ten-point rating scale. Accordingly, the lowest levels of risks, functions and asset utilization correspond to 1-3 points; the average level – 4-7 points, and the highest – 8-10 points. Thus, an improved quantitative and analytical toolkit for a qualitative assessment of the business operations of integrated companies within a holding/group is presented in Table 1.

Table 1. Quantitative and analytical tools for the qualitative assessment of business operations of integrated operating assets as part of holding-type parent groups in developing countries

OECD Symbol	Ten-point rating scale	Risk level	Functional Comparison	Asset utilization
-	0	Minimum	Minimum functions	Virtually no assets used
*	1-3	Least risk	Low functions set	Minimum asset utilization
**	4-7	Medium risk	Middle functions set	Average asset utilization
***	8-10	Highest risk	Maximum functions set	High asset utilization

Source: elaborated by the authors based on Ugrovata (2014), OECD (2010)

These results can be embodied as the basis for improving transfer pricing models (as part of tax planning strategies) used by developing countries in the post-BEPS world. These are typical CA, FFD, LRD models. Besides, in the structure of these models (as a direction for future research), it is recommended to add protection tools for the still rather weak tax legislation of developing economies. That is, protection against the withdrawal of profits from the states in which such profits are created to low-tax jurisdictions that are “convenient” for corporations in order to minimize general corporate taxation, which, in turn, affects the budgets of developing countries.

4. DISCUSSION

It is believed that the transfer pricing mechanism should be considered as an integral element of the internal subsystem of the system for ensuring the functioning of transfer mechanisms in integrated holdings, along with the following:

- corporate clearing mechanism (which is a transfer one);
- the internal corporate insurance and credit mechanism (the system of functioning of funds created by the holding management company structure, implemented through effective inter-

nal mutual lending);

- the movement of capital and other financial resources in both domestic and international directions (Carson et al., 2000). From the authors' point of view, these conclusions are true, but it should be noted that in this case only the financial aspects of transfer mechanism functioning in corporations are covered (Adams and Drina, 2008; Daxkobler, 2014).

Many tax specialists note that the use of the transfer pricing mechanism along with the negative consequences has a positive factor – it eliminates the problem of corporate double taxation. Double taxation in an international vertically integrated structure can be divided into:

– domestic taxation;
– external taxation (OECD, 2010; Helminen, 2016).

Internal double taxation occurs when the same tax is levied on each structural business unit of the holding in the process of moving inventory flows in cash within one country. External double taxation causes a contradiction in the definition of the object of taxation in the national laws of different countries where the holding's main and subsidiary companies are located (Porter and Schwab, 2008; Tsindeliani, 2016). However, at the same time, other scientists rightly note that in most developing countries of the world, where the cost centers of international corporations are located, transfer pricing is still used for reducing the corporate tax burden. The consequence is the lack of sufficient income to the state budget for corporate income tax (Plasschaert, 2005; Lifting the mist, 2019).

The most common methods for eliminating the problem of international double taxation in the country where holding is registered are tax credit, tax exemption and tax benefits (Plasschaert, 2005; Hofmann and Riedel, 2020). Undoubtedly, pricing is one of the important tools for managing the economy of enterprises (Gburová et al., 2013; Stevens, 2020). Currently, for large enterprises, the establishment and control of prices for settlements with relatively separate structural units are relevant. The problem is that a clear definition of domestic prices has not yet been formulated in accordance with national standards for accounting, reporting and current legislation. Therefore, for domestic enterprises, it is necessary to take into account world experience in the formation and use of domestic prices, which in holding structures are defined as transfer prices (Forkiewicz et al., 2015; Garcia-Bernardo et al., 2017).

The presented provisions and facts prove once again that the financial result of production may decrease not only due to a deterioration in the efficiency of these enterprises, but as a result of the manifestation of special cash flow management mechanisms that belong to transfer pricing mechanisms (Edmonds et al., 2016; Cooper et al., 2017). Transfer pricing mechanisms in the current global economy are of great importance in managing the economies of industrial enterprises from developing countries. The proper use of these mechanisms should reflect the economic interests of not only owners, but also society and the state as a whole.

CONCLUSION

The processes of corporatization and consolidation have affected almost all areas of business in developing countries of the world. Thus, there is a need to revise traditional approaches to determining and analyzing the performance of industrial enterprises as part of international corporate structures. New methods and tools of enterprise management should also be developed. With the advent of the latest pricing mechanisms, which include the transfer pricing mechanism, it became possible for multinational companies to use profit tax optimization schemes by: a) transfer of goods to related companies within the framework of one business structure at prices below market (transfer); b) sale of goods at market prices; and c) – payment of taxes and fees to the budget in offshore zones, or countries with a preferential tax regime.

A study of the legislative and tax base of developing countries on the example of the CIS region on transfer pricing demonstrates the need to reform and supplement it in order to eliminate the main shortcomings indicated in the article and to strengthen the integration of national business in world market conditions. Despite the damage caused to the national economy as a result of non-payment of the objective amount of income tax, it should be recognized that transfer pricing is not only a means of tax evasion, but also an effective tool for: a) managing and increasing the competitiveness of transnational integrated holding structures; and b) economic growth in subordinate enterprises.

Transnational holding structures use the transfer pricing mechanism to improve business performance. In the organizational structure of the holding, a significant role is played by the delegation of duties and responsibilities of each unit for its economic results. This gives the base for the parent company to plan and implement strategic management activities at all levels of the hierarchical structure in order to optimize the cash flows. Corporate assets are allocated to centers of responsibility: centers of costs, investments, revenues and profits.

The main result of the study is the development of a methodological approach to the analysis of the impact of corporate transfer pricing strategy on business operations. The implementation of the proposed methodological approach in practice also focuses on the following: a) comparison of markets for goods (the geographical position of markets and their size, the presence on the market of homogeneous goods (works/services), the presence of competition in the markets and the relative competitiveness of sellers and buyers in the market, supply and demand, the level of government intervention in market processes, etc.); b) analysis of market (commercial) business strategies of the parties (market expansion strategies; supporting market strategies, etc.); c) clarification of the nature of financial obligations affecting the price of the transaction (credit agreements, sureties, etc.); and d) analysis of other financial and commercial conditions that significantly affect the price of goods (services/works) in the agreement.

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