Managing the transfer pricing life cycle: from planning to tax controversy

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Federico Vincenti and Carola Valente Della Rovere of Valente Associati GEB Partners/Crowe Valente illustrate the key phases and examine how multinational enterprises can manage intercompany pricing from planning through implementation, compliance, and tax controversy

Transfer pricing is no longer merely a year-end tax compliance exercise. For multinational enterprises (MNEs), it has become an ongoing management process involving multiple internal and external stakeholders and requiring close coordination between tax, finance, accounting, legal, and business functions.

A structured approach to transfer pricing can be described through the transfer pricing life cycle, which consists of four main phases:

- Planning;
- Implementation and monitoring;
- Documentation and compliance; and
- Tax audit and controversy defence.

Planning

The first phase concerns the strategic design of the group's transfer pricing policy, including the identification of the appropriate methodologies and the determination of the prices or remuneration mechanisms applicable to intercompany transactions.

This process should involve the relevant stakeholders across the organisation. Tax departments may provide technical guidance, but finance, accounting, legal, and operational teams possess information that is essential to understanding how the business actually operates. Their involvement helps align the transfer pricing strategy with the group's broader business objectives while establishing appropriate controls over tax risks.

Planning has become increasingly complex as jurisdictions have developed more extensive transfer pricing regulations and tax authorities have intensified their scrutiny of cross-border related-party transactions.

From an operational perspective, the starting point is the identification of material intercompany transactions and the entities involved. The MNE must then understand the roles and responsibilities of each entity, including the activities performed, assets used, and risks assumed.

An effective transfer pricing analysis should therefore include a value chain analysis aimed at identifying where and how value is created within the multinational group.

There is no universal value chain model. Different industries rely on different value drivers, and even companies operating in the same sector may organise their activities differently. For example, marketing functions, brands, and other intangible assets may represent particularly significant value drivers for a multinational group operating in the fashion industry, whereas manufacturing technology or R&D capabilities may be more significant in other industries.

Against this background, the functional analysis represents one of the key elements of transfer pricing planning. It identifies the functions performed, assets employed, and risks assumed by each party and provides the foundation for accurately delineating the relevant controlled transactions.

Once the substance of the transactions has been established, the group must select the most appropriate transfer pricing method and perform the relevant comparability analysis to determine whether the resulting remuneration is consistent with the arm's-length principle.

Importantly, this exercise is generally performed during the budgeting and transaction-setting process using the information reasonably available to the taxpayer at that time. This temporal perspective is particularly important when transfer pricing policies are subsequently reviewed by tax authorities, which may have the benefit of information that became available only after the relevant transactions occurred.

This also explains why the methodology used for price setting does not necessarily have to coincide with the methodology subsequently used for price testing.

For example, an MNE may initially determine an intercompany price using a traditional transaction method reflecting its commercial pricing mechanisms. At year-end, however, sufficient comparable transaction data may not be available to test the outcome reliably. The group may therefore use another method, such as a transactional profit method, to verify whether the results ultimately achieved are consistent with the arm's-length principle.

Implementation and monitoring

The second phase of the life cycle therefore translates the transfer pricing model into the group's day-to-day operations. It generally includes communicating the policy to relevant stakeholders, preparing and executing intercompany agreements, establishing pricing mechanisms, monitoring financial results, and developing internal transfer pricing manuals and procedures.

Monitoring is equally important. Transfer pricing should not be managed exclusively through year-end adjustments. Periodic monitoring throughout the financial year allows an MNE to compare actual results against the expected arm's-length outcomes and identify potential deviations at an early stage.

Actual market conditions may differ significantly from those assumed when the budget was prepared. Sales volumes may change, costs may increase unexpectedly, exchange rates may fluctuate, or extraordinary business events may affect profitability. Monitoring allows the group to assess these developments and, where appropriate, make timely adjustments to its intercompany pricing.

Documentation and compliance

The third phase concerns transfer pricing documentation and compliance.

At this stage, the MNE must demonstrate both the transfer pricing policies applied to its intercompany transactions and their consistency with the arm's-length principle under the applicable domestic rules.

Documentation should not merely describe a theoretical policy. It should provide a coherent explanation of the group's business, relevant transactions, functional profiles, economic analyses, and actual financial results. Consistency is therefore essential. Intercompany agreements, accounting records, transfer pricing documentation, tax returns, and the actual conduct of the parties should tell the same economic story.

This phase has also become increasingly important as multinational groups face multiple documentation requirements across jurisdictions. A coordinated compliance process can reduce duplication, improve consistency, and help identify potential risks before documentation is submitted to, or requested by, tax authorities.

Tax audit and controversy defence

The final phase concerns transfer pricing audits and tax controversies.

Robust documentation represents an essential element of audit defence, but effective controversy management begins much earlier. The strength of a taxpayer's position will depend on whether the underlying policy was properly designed, implemented, and monitored.

The four phases of the life cycle are therefore cumulative: weaknesses arising during planning or implementation cannot always be repaired through documentation prepared after the event.

This perspective also places transfer pricing within the broader framework of tax risk management. Groups should identify material transfer pricing risks, establish appropriate controls, assign responsibilities, and retain evidence supporting the decisions made throughout the life cycle.

Moreover, tax authority involvement does not necessarily occur only at the end of the process. In certain circumstances, what would traditionally be considered the final phase may effectively become the first. This is particularly the case where taxpayers seek greater certainty through advance pricing agreements and agree their transfer pricing methodology prospectively with the relevant tax authorities.

Key takeaways on the transfer pricing life cycle

The transfer pricing life cycle demonstrates that transfer pricing management extends well beyond the preparation of annual documentation. It is a continuous process connecting business strategy, pricing decisions, financial systems, compliance, and tax risk management.

For multinational enterprises, the principal challenge is therefore not simply to demonstrate that a particular intercompany price is arm's length. It is to build a governance framework in which transfer pricing policies are designed appropriately, implemented consistently, monitored throughout the year, documented accurately, and capable of being defended before tax authorities.

When these elements operate as an integrated life cycle, transfer pricing can move from being a reactive compliance obligation to becoming an effective component of the multinational group's broader tax governance framework.

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