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Transfer Pricing of Intangibles

A multi-case study of transfer pricing of intangibles within Swedish multinational manufacturing companies

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Abstract

This paper investigates the determinants of transfer pricing of intangible assets within Swedish multinational manufacturing companies. A special focus is put on the interdependencies between the transfer pricing system and the operations. In the literature, there is currently a lack of empirical data on companies' transfer pricing system especially with regards to intangible assets and the Swedish business environment. This paper contributes to the empirical evidence through an explorative multi-case study analysis of six Swedish multinational manufacturing companies. The theoretical foundation for this study is mainly provided by contingency and behavioral theory. We find that all analyzed companies pursue similar objectives in transfer pricing and prioritize supporting their operations and being tax compliant over achieving tax optimization in transfer pricing. Their objectives are mostly contingent on the external environment. However, differences in the design of the transfer pricing systems are observed and can be attributed to differences in the operations, strategy and history of the companies. We find that transfer pricing of intangible assets is closely linked to the overall transfer pricing system. Furthermore, most companies avoid influences of the transfer pricing system on performance measurement either by separating the books or making adjustments below the line for performance evaluation. Finally, we develop a theoretical model to illustrate the influences of contingent factors within the transfer pricing of intangible assets.

Key words: Transfer Pricing, Intangible Assets, Multinational Companies, Manufacturing Industry

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1. Introduction

In 2005, Sandvik AB, a Swedish engineering company, reorganized all its intellectual property in a newly created intellectual property company. This maneuver involved transfers of intangible assets[1] to the Netherlands, which were then sold back to Sweden. According to the company, this centralization of the company's intellectual property in one place was based on operational reasons. It resulted, however, in a tax-free profit of SEK 18 billion in the Netherlands and a corresponding charge in Sweden. This gave rise to legal struggles between the Swedish tax authorities and Sandvik over these transactions, a struggle that still has not been resolved (Aktiespararna, 2012) (Tidningarnas Telegrambyrå, 2008) (Sandvik, 2012).

Transfer pricing of intangibles is thus a controversial topic in the Swedish business community. The case is the starting point for this thesis to investigate how Swedish multinational manufacturing companies set their transfer pricing system for intangible assets and how these choices are motivated.

Sandvik is not alone in moving substantial amounts of its income to more tax friendly locations (Huizinga & Laeven, 2008). Companies with significant intangible assets have the ability to move profit more easily since intangibles are valuable and can be transferred at almost no cost (Dawson & Miller, 2009). As a response to the income shifting, the OECD[2] is constantly updating its transfer pricing guidelines, which are the basis for the legislation of its member states (OECD, 2010).

Transfer pricing exists because companies exchange finished and unfinished goods, services and corporate overhead costs between different parts of their organization (Emmanuel & Mehafdi, 1994). As a result, an internal price is determined for each transaction between those entities. The phenomenon of transfer prices dates back to the end of the 19th century (Boyns, et al., 1998) and has been subject to scientific research as early as 1908 by Schmalenbach (1908). The goals of transfer prices can be very different depending on the analyzed corporation (see e.g. Cravens, 1997). Tax effects of transfer pricing are especially relevant for multinational companies, which can minimize the tax burden and their tariffs or simply want to comply with local regulations. Taxation is therefore a topic that can be found throughout the discussion of international transfer pricing, although it might not always be in the immediate focus.

In a transfer pricing context, intangibles and tangibles are treated differently as the marginal cost of an intangible asset is zero (Borkowski, 2001). As a result, they offer the greatest potential for profit shifting (Dawson & Miller, 2009). As intangibles make up a growing part of the value of companies, there is also an increasing interest in their effective management (Johnson, 2006). Intangible assets that are most often transferred relate to intellectual

[1] The terms "intangibles" and "intangible assets" are used interchangeably, "intellectual property" (IP) is considered a subset of intangibles

[2] Organisation for Economic Co-operation and Development

property. Transferring them can be done easily and at no marginal cost. The key issues and most difficult tasks in the transfer pricing of intangibles are the identification and subsequent valuation of the intangibles (OECD, 1998). This valuation is even more complex when intangibles cannot clearly be separated from each other or from tangible assets. The manufacturing industry provides an interesting study object as manufacturing companies have both significant amounts of intangible and tangible assets.

For an analysis of transfer pricing of intangibles, several perspectives can be taken. Most covered in the literature is the tax perspective, describing how companies can minimize their tax burden (Brauner, 2008). This is not surprising in the view of recent cases of companies which engage heavily in income shifting on the basis of licensing fees for intangibles. Governments in turn want to defend their tax income. Companies have to comply with the local tax regulations. Otherwise they face the risk of costly tax audits, which might also damage their reputation. The regulations in most jurisdictions are based on the OECD (2010) guidelines but there are important exceptions which complicate the transfer pricing especially in Brazil, Russia, India and China (BRIC).

Mostly overlooked so far has been the relationship between transfer pricing of intangibles and the operations of a company. This area is covered only without taking the special characteristics of intangibles into consideration (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010). These case studies have shown that the goal of tax compliant transfer prices has an effect on the management control system and environment of a company. They analyze transfer pricing that is used with one book[3] for both tax and management control purposes. This can create tensions in the organization as the solution that is optimal for tax purposes might not create the best incentives for internal management. To mitigate those tensions other authors (Durst, 2002) suggest using separate books for the accounting of the two purposes, which also seems more common in practice (Hyde & Choe, 2005). Another important aspect in the organizational setup of the transfer pricing system is the tension between centralization versus decentralization (Emmanuel & Mehafdi, 1994). Centralization of intangible assets leads to more efficient operational structures but can also be used for tax saving purposes, while decentralization allows more local adaption.

The current research on transfer pricing of intangible assets is limited. The research in this area has largely focused on taxation considerations and not so much on the operational side of transfer pricing of intangible assets. There is a lack of in-depth empirical data through case studies. The factors and contingencies that influence the transfer pricing system of intangibles can be understood through case study research based on behavioral and contingency theory (Plesner Rossing & Rohde, 2010). A focus is on the companies' decision making regarding their transfer pricing of intangibles system. Relevant in-depth case studies of the transfer pricing system as a whole, based on those theories emphasize mainly the change in the introduction of a new tax compliant transfer pricing system (Plesner Rossing & Rohde, 2010)

[3] The expressions "one book" and "single book" as well as "two books" and "double book" are used interchangeably in this thesis

(Cools, et al., 2008). Furthermore there have been no in-depth case studies in transfer pricing, with a focus on the Swedish context. Most research has been in American companies (Borkowski, 2001). Given the case of Sandvik, a study of Swedish multinational industrial companies could be especially interesting.

The current developments in the area of transfer pricing of intangibles lead us to the following research questions for this study:

> *How do Swedish multinational companies in the manufacturing industry conduct transfer pricing of intangible assets?*

The following sub-questions should additionally be answered:

> *What goals do Swedish multinational manufacturing companies want to achieve with their transfer pricing of intangibles?*
>
> *How is performance measurement affected by transfer pricing of intangibles?*
>
> *What factors influence transfer pricing of intangibles?*

The purpose of this study is to contribute to current research through a multi-case study with empirical data. The understanding of the interdependencies between transfer pricing practices of intangibles and operations should be deepened. Through an explorative study, we intend to develop a theory to determine the factors affecting transfer pricing of intangibles. This study should therefore be based on behavioral and contingency theory.

1.1. Scope and Outline

The research question will be answered using a multi-case study of six Swedish multinational companies operating in the manufacturing industry. The transfer pricing system, especially with regards to intangible assets is described and analyzed. All selected companies have significant amounts of intangible assets and are active in numerous countries around the world. This makes them highly relevant organizations for this study.

This paper is organized in five parts. After this introduction, the current research literature in transfer pricing is reviewed. The relevant literature discusses transfer pricing systems, intangible assets and taxation. In the third part, the methodology of this study is described. The fourth section contains the analysis, which combines the presentation of the empirical findings with the comparison and analysis of the cases by employing frameworks and theories discussed in the literature. Finally, the relevant findings are summarized and a conclusion for the paper is drawn, which acknowledges the limitations of the paper and gives suggestions on further research.

2. Previous Research

2.1. Introduction to Transfer Pricing Research

This paper focuses on the transfer pricing of intangibles and how the choice in transfer pricing affects managerial decision making and the organizational structure. Transfer pricing research has focused on a variety of different aspects of transfer pricing based on different theories. The main theoretical background for this study is provided by behavioral and contingency theories, which are used for case study research in transfer pricing. Those theories are used to highlight different aspects and can be found in the studies of Cools et al. (2008) and Plesner Rossing & Rohde (2010).

This chapter is structured as follows: First, the most relevant transfer pricing theories for this paper, contingency and behavioral theory are presented as well as the debate between single or double book accounting is introduced. Then intangibles in transfer pricing are described together with the special challenges that are associated with them in the literature. Thereafter tax applications from a firm and a regulatory perspective are discussed focusing on the OECD guidelines on transfer pricing. After that the company structure is considered concerning the centralization and the principal structure of legal companies. The chapter is concluded with the gap identification in previous research and the development of the framework for the subsequent analysis.

2.2. Transfer Pricing Theories

Two major theories can be found in today's empirical transfer pricing literature: behavioral theory and contingency theory. The multitude of articles demonstrates that they have had a great influence on transfer pricing. For in-depth case studies such as this paper, a behavioral approach is appropriate to analyze the transfer pricing system. While there are many different contingency factors that have been considered by the various studies, there is a general consensus that both the external environment and internal conditions have to be taken into account. The research literature can roughly be divided into domestic transfer pricing that focuses on optimizing transactions within a country and international transfer pricing that looks at cross border transactions. In international transfer pricing, taxation is considered as a dominating factor.

2.2.1. Behavioral Theory

The behavioral theory of the firm has been pioneered by Cyert & March (1992). Behavioral theory puts a focus on the internal perspective of the firm and especially the decision making in organizations. Organizational goals, expectations and choices are key concepts in behavioral theory. It can be used as a basis for the description of individual firms and industries. The underlying ideas of behavioral theories are bounded rationality, imperfect environmental matching and unresolved conflict (Cyert & March, 1992). Behavioral theory in transfer pricing has been pioneered by Watson & Baumler (1975). It takes not only economical reasoning into account but looks at the social and organizational context as well. Watson & Baumler (1975) study the organizational design of a company, structures, systems and conflict resolution. The emphasis in their paper is on the constraints the organization puts on the design of the management accounting system.

2.2.1.1. Domestic Transfer Pricing

Behavioral approaches to transfer pricing are clearly identifiable in papers that examine transfer pricing through in-depth case studies. Eccles (1985) has conducted several extensive empirical case studies of American companies and their application of transfer pricing. He concludes that strategy and organizational issues play a significant role in the design and choice of transfer pricing methods. As a result he develops the Manager's Analytical Plane (MAP), a model with two dimensions, degree of vertical integration and degree of diversification, which can explain why the observed companies use a specific transfer pricing method. This can also be used to analyze the effect of changes in the organization on the transfer pricing system. Drawing on the empirical findings of Eccles (1985), Spicer (1988) develops a broader theory how strategic, organizational and transactional circumstances influence the transfer pricing system. The findings suggest that the transfer pricing methods are dependent on a firm's organizational structure and its management accounting and control systems.

An empirical in-depth study of the functioning of transfer pricing systems in four Dutch multinational companies was conducted by van der Meer-Kooistra (1994). Taking transaction cost theory and behavioral theory into account, she came to the conclusion that it is necessary to look at all stages and elements of a transfer pricing system as well as its context. She also found that the uniqueness of the assets as well as information asymmetry and uncertainty about the transaction provided an explanation for the firm's strategy of differentiation and integration, which relates to the transaction cost theory. Similar results were found in an empirical investigation of a theory of the sourcing and transfer pricing process from a transaction cost and behavioral perspective, which was carried out by Colbert and Spicer (1995). The authors conducted a multi-case study in four large, vertically integrated high-technology companies in the electronics industry based in the US. The paper concluded that the companies' setting of transfer prices is positively correlated with how unique and strategically important the asset transferred is.

2.2.1.2. International Transfer Pricing

Newer applications of behavioral theory do not as the studies above list a number of goals of transfer pricing system, but instead focus on tax compliance as the dominating contingency factor in transfer pricing (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010). They analyze how tax compliance as an important contingency in transfer pricing can affect the management control system of multinational companies. By studying cases, those studies are focusing on behavioral aspects of the firm but take contingency theory as a background, which is the same approach as used in this paper.

Cools et al. (2008) present an in-depth case study of the introduction of a universal tax compliant transfer pricing policy. This study focuses on the impact that the dominance of the goal of tax compliance has on a company that uses single book accounting. The impact was visible on all levels of the organization and led to a more centralized and standardized process. The performance measurement was adjusted to non-financial measures to mitigate the effect of standardization. The tax compliant policy thus led to more centralization and transparency at the expense of flexibility for exceptions. These consequences might restrict the entrepreneurial activities in companies and should be taken into account by the regulators, especially the OECD, when drafting regulations.

This is also observed in the paper by Plesner Rossing and Rohde (2010), which looks at overhead cost allocation in a multinational companies as another aspect of transfer pricing through a dynamic in-depth case study. The company studied moved towards a more centralized structure where the allocation of overhead cost is carried out at the headquarters. A rise in standardization and formalization of the overhead cost allocation process arises parallel to the more centralized process. Through increased documentation the transparency of the process is enhanced. One important variable is thus the company's strategy in the tax environment.

2.2.2. Contingency Theory in Transfer Pricing Research

Contingency theory focuses on the behavioral and organizational aspects in management accounting. The main assumption of contingency theory in accounting is that there is not one optimal system that can be applied to all organizations. The appropriateness of an accounting system depends more on the distinct situation of an organization as measured by both external factors, such as technology and the environment and internal factors, mostly the organizational design (Otley, 1980). Contingency theory in management control research has proven to produce generalizable findings and to provide a helpful framework (Chenhall, 2003). Managers adapt their management control systems to fit the circumstances of the contingencies. There are numerous studies from the contingency theory angle, which look at different contingencies and their impact on the transfer pricing system.

2.2.2.1. Domestic Transfer Pricing

Borkowski is one of the most active and renowned researchers taking a contingency theory approach for transfer pricing. She has published a range of papers dedicated to this issue. Her survey (Borkowski, 1990) of 168 companies confirms findings that both organizational and environmental aspects impact the transfer pricing methods chosen. For the current setup of the firm, the method currently employed is mostly regarded as optimal. In particular the size and the degree of centralization can indicate the selection of a certain transfer pricing method. Another study by Borkowski (1996) provides a good overview of the research up to that point in time. The findings of those studies do not lead to a comprehensive picture of transfer pricing practices, as the research was not consistent enough. The only statistical significant finding was that large companies prefer to employ market-based methods.

2.2.2.2. International Transfer Pricing

One of the first studies in this area compared the practices of Japanese and American companies in transfer pricing (Tang, et al., 1979). The study finds that although the goals of transfer pricing in those two countries are similar, the resulting systems exhibit significant differences. The conclusion is thus that the differences can mostly be attributed to environmental factors of the countries.

While her first studies focused on domestic transfer pricing, a later survey (Borkowski, 1992) compares the differences between domestic and international transfer pricing. In international transfer pricing considerations for taxes and tariffs play the most important role in her findings. Simplicity and low cost are secondary and supplement support the goals of tax compliance and optimization. Performance measurement on the other hand does not have a great influence on the transfer pricing system and the applied measures can differ for domestic and international managers. However, not all surveyed companies have different domestic and international transfer pricing systems. These findings are supported by another survey (Cravens & Shearon, 1996) that concludes that while companies have a variety of goals they want to achieve with international transfer pricing, the financial outcome of transfer pricing is mostly determined by the tax management.

An exploratory study by Elliott and Emmanuel (2000) examines companies in three different industries: financial services, manufacturing and services. Differences are found in the application of international transfer prices between those industries, whereas the transfer pricing methods within the industries is comparatively consistent. This is the case despite of differences between the underlying structures for these transfer pricing systems within the industries regarding strategic issues, internal structure, managerial reward and fiscal policies.

In another study Cravens (1997) focuses on the strategic objectives of transfer pricing. The study consists of a survey of international transfer pricing objectives and strategies in multinational companies. In order to understand the appropriate method selected by a company, it is important to understand the goals of the transfer pricing. Transfer pricing can be used as a strategic tool and her findings show that it does influence the performance of a company and contributes to its strategic objectives. She has identified three groups of objectives for international transfer pricing: tax related, internal management-oriented and international or operational goals.

Additionally to the articles mentioned before, numerous other studies can be found that are based on contingency theory. These focus on various aspects, like the historical development of a transfer pricing system over time (Boyns, et al., 1998), (van Helden, et al., 2001) or develop their own model and prescription on how to implement a transfer pricing system (Chen, 2005), (Wolff, et al., 2008).

2.3. Single or Double Book Accounting

There is an ongoing debate in transfer pricing if companies are best served by using a single book for accounting for both tax and managerial purposes or if it is better to separate book. In the above mentioned studies, single book accounting is used for the overhead cost allocation system (Plesner Rossing & Rohde, 2010) and the transfer pricing system (Cools, et al., 2008). While it is simpler, the introduction of a single book has a noticeable impact on the whole management control system. This can create tensions in the organization as the optimal for taxes purposes solution might not create the best incentives for internal management.

Durst (2002) discusses the reasons behind the conflict between accounting suitable for managerial purposes and tax purposes. He argues that multinational companies should use separate accounting for tax and managerial purposes. The main reason behind his standpoint is that tax compliant transfer pricing generally requires companies to incorporate a profit component in each transaction. That might lead to the double marginalization problem and can prevent optimal outcomes for the group. Furthermore, other studies conclude that two transfer prices enhance the flexibility of a company (Hyde & Choe, 2005). Economic studies support the reasoning that a separation of internal and taxation transfer prices of intangibles lead to more economically efficient outcome (Johnson, 2006). Dawson & Miller (2009) find that optimal results in transfer pricing negotiations can be achieved if performance evaluation is not affected by transfer prices.

The underlying question in the tension between single or double book accounting is if transfer pricing should affect performance measurement. Controversies can arise if the bonuses are affected by legal transfer prices. Separated accounting systems for different purposes are only one way of avoiding conflicts between performance measurement and transfer pricing. The usage of single or double book is thus not a discrete choice but there are different approaches companies can choose to fit their needs. In her survey, Borkowski (2001) divides the practices used by companies into five different categories to describe companies' books in transfer pricing: (1) Using two sets of books, one for tax, finance, and local purposes, the other for management and control purposes; (2) approximating in the host-country subsidiary, as closely as possible, those conditions what would be faced by an independent market entity; (3) disregarding transfer pricing aberration effects when evaluating the performance of host-country subsidiary performance; (4) taking account of any transfer pricing adjustments in the budget, so subsidiary managers are not evaluated on parent company usage of transfer prices to achieve certain goals, such as tax minimization and (5) none of the above.

2.4. Intangible Assets

Intangibles are becoming increasingly important in the global economy and make up a growing portion of the value of companies (Johnson, 2006). Surprisingly, according to Johanson et al. (2001) there is no generally accepted definition of intangibles. Croes (1998) points out that one of the reasons that the line between the tangible and intangible assets is unclear is because intangibles use a tangible storage medium while tangible goods often include intangible elements.

Cañibano et al. (2000) conduct a review of the literature related to intangibles and give a good overview over the research in the area up to that point. They also points out that even though intangible assets lack a generally accepted definition, it is quite generally accepted that intangible assets have four distinct characteristics: (1) They are sources of probable future economic profits, (2) lacking physical substance, (3) which are controlled by a firm (4) as a result of previous events or transactions.

2.4.1. Intangible Assets in Transfer Pricing Research

Despite the increasing importance of intangible assets for multinational firms, there has so far been only limited research investigating transfer pricing of intangibles. Intangibles can be moved at zero marginal cost and their valuation is challenging. Consequently research has shown that intangibles offer the greatest potential for transfer pricing abuse compared to tangible assets (Dawson & Miller, 2009). They are therefore increasingly in the focus of tax authorities. To comply with taxation regulation multinational companies thus have to build up an effective transfer pricing system.

2.4.1.1. Description of Transfer Pricing of Intangibles Systems

Transfer pricing for intangibles is treated differently from transfer pricing for tangible assets and should thus be considered separately. This is demonstrated by Borkowski (2001) who shows that intangible property valuation is similar across countries, while differing significantly in tangible assets. Furthermore she finds that the choice of a transfer pricing method is related to the industry and thus on the type of intangible. Her study is based on a survey on companies based in five different countries (US, Germany, UK, Japan and Canada). Due to the requirements of the companies based outside the US to have at least one subsidiary in the US, while no such corresponding requirements is made for the US-based part of the sample, the sample used in the study is rather unbalanced toward US-based companies (113 of the total 159 companies used in the study are US-based). Therefore the non-US result has to be taken somewhat cautiously but the results can still give a good indication about the situation, which is especially important given to lack of other studies on the same subject.

As in transfer pricing for tangible assets, the OECD plays a very important role for intangibles in both the valuation and transfer pricing. The OECD guidelines (OECD, 2010) differentiate between commercial and marketing intangibles. While commercial intangibles include patents and know-how, marketing intangibles relate to trademarks and customer relationships. Ainsworth & Shact (2011) investigate how business restructurings and their effect on the firms' intangibles are covered properly by the OECD guidelines. The authors find that the OECD fails to understand that business restructurings core activity is not asset movement but instead fundamentally changing the enterprise's decision-making. The authors claim that the OECD's abstract view towards business restructurings is not in line with the business in practice and is preoccupied with tax avoidance schemes.

Abdallah & Murtuza (2006) identify three important factors that have to be considered for understanding and designing a transfer pricing system for intangibles: (1) The historical context of the company structure and how the intangibles were developed; (2) the management philosophy and (3) the tax strategy of the company. They stress that transfer pricing of intangibles should not only focus on taxation but should mostly consider operational consequences. Multinational companies today should thus base their transfer pricing more on the reality in the marketplace.

2.4.1.2. Taxation Considerations

A comprehensive overview over transfer pricing of intangibles is given by Brauner (2008). He concludes that the currently used arm's length principle is inappropriate and should be replaced by formula based transfer pricing. His critique is based on the reasoning that compliance with transfer pricing of intangibles is burdensome, valuation of intangibles is dominated by complexity and uncertainty and that the various intangibles are too different to just use the same method. The current regulation provides only limited guidance for the companies. Inaccuracy in transfer pricing of intangibles regulation creates advantages for multinational companies, which can profit from income shifting.

Those issues are similar to the ones identified by Picciotto (1992). He regards intangibles as joint cost that create profits in the organization and thus have to be allocated, but are subject to a high degree of uncertainty and risk. He concludes that this leads to problems with the valuation and their transfer at cost is not possible. Therefore tax authorities allow for a spread in royalty rates, but this still can create conflicts between home and host countries. He finds that consequently the best method in transfer pricing of intangibles is the transactional net margin method.

2.4.2. Measuring Intangibles

The differences in the handling of intangible assets are closely connected with what is seen as perhaps the biggest problem for companies in relation to intangibles, measuring them in a reliable and credible way. In 1998, the OECD issued a report regarding intangibles (OECD, 1998), which concluded that there is a lack of investment in intangible assets and that the reason behind this was their lack of visibility. The lack of visibility comes from the fact that companies have a hard time to measure and manage intangibles internally, as well as report about them to external actors in a credible and transparent way.

The problem of measuring and reporting intangibles assets in a good way does also have a significant negative effect for investors. Lev & Zarowin elaborate on the problem of measuring intangibles in relation to its influence on the usefulness of financial reporting (Lev & Zarowin, 1999). The authors come to the conclusion that the usefulness of financial information has decreased during the studied time period and that the increased importance of intangibles is one of the main reason behind this.

As intangibles make up a growing part of the value of companies, there is also an increasing interest in an effective management of them. The management control of intangibles is becoming more formalized and embedded in the performance management systems. One interesting study on the measurement of intangibles in a Swedish setting is made by Johanson et al. (2001), who investigate how eleven Swedish companies in different sectors measure intangibles and how they use the measurement for management control purposes. They conclude that even if all companies in the study have an extensive measurement of intangibles, the usage of the measured values for management control purposes varies extensively. This study is only focusing on intangibles and does not take any transfer pricing issues into consideration, but the insight into intangibles are relevant given its focus on Swedish based companies.

2.5. Taxation Theories

Taxation is a big recurring issue in the literature of international transfer pricing and is addressed in many different ways. It is mostly influenced by the OECD guidelines. The possibility to engage in income shifting through transfer pricing is used by many multinational businesses. The literature on taxation takes different viewpoints. One strain studies the role of the government and analyzes how income is shifted between countries and how countries should design their regulations in order to not lose out on taxable income. Other authors look more at the micro-perspective of a firm and how tax optimization is handled on this level.

2.5.1. Guidelines

The most important document to understand the taxation regulations of transfer pricing are the OECD transfer pricing guidelines (OECD, 2010). The guiding principle of the OECD guidelines is the arm's length principle. It states that in internal transfers, prices should be set as if the involved parties were unrelated to each other. The guidelines prescribe five different methods which fulfill the arm's length principle. Three of them are traditional methods: comparable uncontrolled price, cost plus and resale price, while two are transactional, the transactional net margin and transactional profit split method. Within all those methods comparability with market transaction should be achieved to ensure the validity of the transfer price.

They should ensure a fair taxation at the point of value creation and prevent profit shifting by multinational companies while also avoiding double taxation. Furthermore they should harmonize local regulations as well as prevent double taxation and conflicts between the member states. The member states adapt those guidelines into local regulation, which therefore differ slightly. Parallel to the OECD, the United Nations (UN) has also issued transfer pricing guidelines (United Nations, 2012). They are more tailored to the needs of developing countries. Due to the large differences in local regulations around the world, the "Big Four" accounting firms issue detailed reports on the regulations of each country (see e.g. (PwC, 2012), (KPMG, 2012), (Ernst & Young, 2010) or (Deloitte, 2012)).

The OECD guidelines also deal with intangible assets in particular in chapter VI. The OECD defines intangible property for transfer pricing purposes broader as in accounting regulations (OECD, 2010). They encompass amongst others patents, trademarks or know-how. They acknowledge the difficulty of applying the arm's length principle as each intangible is unique in itself. The normal way to charge for an intangible is royalty based, for example on sales revenues, but could also be included in the transfer price of connected products. For intangibles the comparable uncontrolled price is identified as optimal method, and in special cases the resale price can be used. More common are, however, transactional net margin and the profit split method. A transfer at cost is not prescribed.

These guidelines, which have been introduced in 1996, are nowadays deemed as inadequate for this complex issue. Therefore an initiative is currently under way to improve the guidance. A first discussion draft has been released in 2012 (OECD, 2012). The proposed draft is more detailed and more complex as the current regulations. A multitude of examples is given to illustrate the application of the guidelines.

The most recent addition from 2010 to the OECD transfer pricing guidelines has been chapter IX about business restructurings. Business restructuring under the OECD guidelines is the internal reallocation of functions, assets and risks. Three main restructurings are identified as particularly relevant for transfer pricing: First the conversion of full-fledged distributors into limited-risk distributors, secondly the conversion of full-fledged manufacturers into contract-manufacturers and lastly the centralization of intangible property rights. This is important for transfer pricing, as with the restructuring the profits and compensation of entities change. A contract manufacturer carries less risk than a full-fledged manufacturing company and is thus entitled only to a smaller but more stable compensation, which is in line with the arm's length principle. The intangible assets and risks are transferred to a principal that receives the residual profit.

2.5.2. Regulatory Perspective

Transfer pricing is used by multinational companies to minimize their tax burden, which is shown in a study by Huizinga & Laeven (2008). Their findings from studying European multinationals show that reported income is dependent on the corporate tax rate and conclude that most countries gain from profit shifting and income decreased the most in Germany. Governments are constantly trying to improve their revenues by changing regulations. Picciotto (1992) provides an overview over the development of transfer pricing regulations from the introduction of the arm's length principle in the 1930s. He concludes that the current regulations are inappropriate.

The profit shifting phenomenon is not restricted to Europe. Bartelsman & Beetsma (2003) show with an analysis of manufacturing companies in the OECD countries that income shifting is related to real economic activity and thus occurs more between OECD countries than with tax havens. They conclude that increased enforcement can lead to relocations of operations. A harmonization of standards in transfer pricing is therefore beneficial for the OECD member states. They confirm findings by Mansori & Weichenrieder (2001), who have shown with an economic analysis of the subject, that competition among governments for tax revenue results in double taxation and reduced international trade. To inhibit profit shifting, tax authorities require that companies provide them with benchmarking evidence in order to strengthen the arm's length principle.

2.5.3. Firm Perspective

Companies are aware of the fact that regulators are increasingly eager to defend their tax base. Wunder (2009) therefore analyzes tax risk management as one approach to control the tax risk. Taxation is here seen in the context of the internal control system and enterprise risk management. She shows that tax risks policies in multinational companies are increasingly sophisticated and are largely the same in US and non-US companies. The overall risk in this area is however not considered to be highly threatening to the survival of the companies.

Sikka & Willmott (2010) question different practices used by companies to avoid taxes and move capital abroad. In their eyes those practices should not be trivialized as accounting techniques but treated more as an abuse of the transfer pricing system. Multinational companies have, in the author's view, a responsibility to contribute to the societies they are operating in and not just operate for private gains. Income shifting is though not always considered undesirable.

2.6. Ethics in Transfer Pricing

Ethical considerations of transfer pricing have been a recurring topic (Sikka & Willmott, 2010). Hansen et al. (1992) study how the goal of tax minimization can be understood in the light of moral ethics. They find that the goal of avoiding taxes as much as possible might be legal, but it does not necessarily contribute to the greater good of a society. Therefore they propagate a professional code of conduct, which should be applied by multinational companies to strengthen the social contract. The impact of transfer pricing practices on other stakeholders should be taken into account.

Mehafdi (2000) looks at the moral implications of international transfer pricing and suggests that only focusing on taxation issues might be too narrow. Inefficiencies in value creation that waste resources are not morally desirable. Furthermore not only companies but also tax authorities engage in morally questionable behavior. Like Hansen et al. (1992) he also embraces the idea of an ethical code of conduct, which should apply to everybody involved in the transfer pricing process.

2.7. Company Structure

When considering the issue of transfer pricing within companies it is important to take the company structure into consideration. There have over the years been many studies which have categorized company structures into different categories (see e.g. Hedlund (1986)), but there has been a lack of studies relating the company structure to the issue of transfer pricing.

2.7.1. Principal Structure

Although there has been only limited current research in transfer pricing in relation to company structure, the practitioners are already further ahead. As has been described in the OECD guidelines the structure with one principal is dominant in the practical discourse (OECD, 2010). The functions risks and assets of a company are centralized within one operating company or principal that is entitled to the residual income. All other subsidiaries just provide services and are remunerated with a fixed and low margin as shown in figure 1. Production units are converted into contract manufacturers and sales organizations into limited risk distributors. Especially consultancy companies are advocating this model in different ways highlighting the advantages, see e.g. (Reams & Dickert, 2012) or (Fazzino, et al., 2011). Through the centralization of intellectual properties, companies can make their operations more efficient and save taxes. Taxation advantages are emphasized especially in cases, where the principal is established in a low tax jurisdiction, in particular in Switzerland, where many principals are located; see e.g. (Bellingham & Zirakzadeh, 2013).

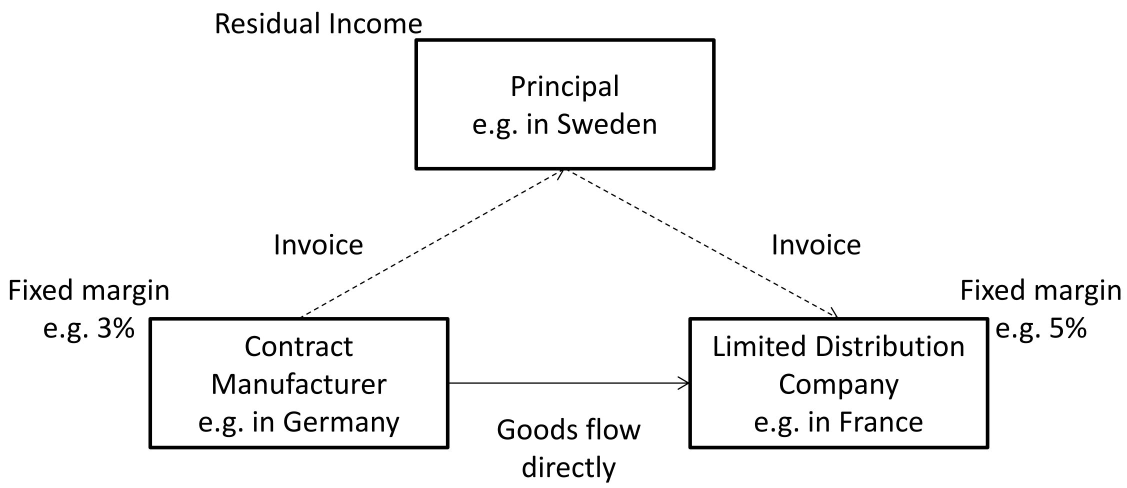

Figure 1 - Illustration of the principal structure

The problems in this area are mostly associated with the implementation and the acceptance of the restructuring by the all of the affected tax authorities; see e.g. (Silberztein & Russo, 2012). The main focus is thus to be in line with the OECD transfer pricing guidelines focusing on business restructuring (OECD, 2010). All transactions within these restructurings should be priced according to the arm's length principle, taking into account the functions carried out, assets used and the risks assumed.

2.7.2. Centralization vs. Decentralization

The degree of centralization of a company is a strategic decision. Centralization and decentralization determines on which level the decision-making lies (Martinez & Jarillo, 1989). A centralized company does have the decision-making on a higher level relatively to a decentralized company. There is a trade-off between leveraging synergies and the need for local adaptation. The first would require a degree of centralization and co-ordination, while the second would involves some level of decentralization and local autonomy (Busco, et al., 2008). Cummings (1995) suggests that the balance between centralization and decentralization changes continuously in a cyclic manner. No balance between the two will ever be achieved and an optimal position only exists in theory. Tensions between the two extremes are also observed by Busco et al (2008). An important finding in their study is that a centralized approach for global brands coupled with a decentralized approach for local brands can lead to tensions where different actors within the organization fight for different goal and goal conflicts within the organization arises.

2.8. Conclusion from Literature Review

The literature describes different areas that should be taken into account in the transfer pricing of intangible assets. The review has shown gaps in the research on transfer pricing. There are only a few published papers on international transfer pricing that conduct in-depth case studies (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010). The empirical data is thus limited and will be enhanced through this study. Furthermore there have been no special considerations for intangible assets in those case studies. Intangible assets have either been studied in surveys (Borkowski, 2001) or from theoretical perspectives (Brauner, 2008). Lastly no study has focused explicitly on the Swedish context. Most studies relate to American companies and the respective regulatory environment.

The frameworks provide an overview to systematically analyze the transfer pricing system of intangible assets. Firstly, as described by behavioral theory (Cyert & March, 1992), the objectives of transfer pricing are analyzed. The framework used in this paper has been drawn up by Cravens (1997):

1. Taxation Related
2. Internal Management Oriented
3. International and Operational

As the next point the overall structure of the transfer pricing system should be described. In absence of a holistic model for the description of an international transfer pricing system, the principal structure as described in the OECD guidelines (OECD, 2010) is used as a benchmark. The empirical data is compared against it.

An important characteristic of a transfer pricing system according to literature, see e.g. (Durst, 2002) and (Hyde & Choe, 2005), is the question if the transfer prices affect performance evaluation and bonuses. The framework by Borkowski (2001) is helpful to analyze the setup of companies:

1. Using two sets of books, one for tax, finance, and local purposes, the other for management and control purposes.
2. Approximating in the host-country subsidiary, as closely as possible, those conditions that would be faced by an independent market entity.
3. Disregarding transfer pricing aberration effects when evaluating the performance of host-country subsidiary performance.
4. Taking account of any transfer pricing adjustments in the budget, so subsidiary managers are not evaluated on parent company usage of transfer prices to achieve certain goals, such as tax minimization.
5. None of the above

After having looked at the general structure of companies, the particularities of intangibles are analyzed. By drawing upon the OECD guidelines (2010), Brauner (2008) and Abdallah & Murtuza (2006) a framework for intangibles can be derived. This framework handles intangibles through four different steps.

1. Creation of intangibles
2. Licensing of intangibles
3. Transfer of intangibles
4. Ownership of intangibles

3. Methodology

3.1. Empirical Method

The empirical method chosen for this study is a qualitative multi-case study. The reason for using this method is mainly the lack of previous research within this area, which also makes the focus of this study explorative in its nature. Another reason for the usage of a case study is that all three conditions outlined by Yin (2003) are fulfilled:

1. The form of the research question is “how” or “what”
2. The research focuses on contemporary event and
3. The researcher does not have control over behavioral events

The research question investigated in this study is a “how” question and therefore has a broad focus. Transfer pricing is subject to constantly changing regulations and therefore the systems applied are created to handle the current reality. Lastly the companies’ transfer pricing systems are not influenced in any way by researchers. In conclusion, a case approach is therefore recommended.

When focusing on how individual companies conduct their operations in depth rather than on how companies statistically operate, case studies are the preferable method to use (Cooper & Morgan, 2008). Case studies allow for more understanding of underlying reasons and connections. In our study it is more insightful to investigate real life situations for companies rather than gaining a superficial overview over many companies and their behavior in the area of transfer pricing. This all makes the case study method desirable. Case studies are also according to Scapens (1990) especially appropriate in areas where the theory is not well developed and a precursor to more quantitative research. In transfer pricing research there is a lack of empirical evidence taking recent developments into account. Consequently the theory is currently inadequate to explain companies’ transfer pricing systems. Therefore explorative research with theory development as is done in this study is necessary. Scapens (1990) also states that it is difficult to make statistical generalization from the small samples that are associated with case studies, but that it can nevertheless be helpful in generating hypothesizes that later can be tested with larger samples. This is the goal that is pursued in this study. Furthermore, Otley & Berry (1994) argue that even though case studies can be used in several different roles, their central role seems to be exploration. This makes them very useful in our study which has had little previous research done.

Case studies do not prescribe what methods should be used to gather the data. There is a range of methods that can be applied such as observations, interviews or quantitative methods (Cooper & Morgan, 2008). Due to the limited amount of previous research a qualitative focus would be more beneficial in an explorative study. Here, interviews provide the most efficient and reliable source of data.

In order to be able to make comparisons between different companies’ transfer pricing systems and with transfer pricing literature, different examples from the practice are necessary. Therefore the multi-case research strategy rather than a single-case study approach has been chosen. A multi-case study creates more robust theory since it is based on a more varied empirical evidence ground (Eisenhardt & Graebner, 2007). Due to limited amount of time and resources available for this study there is the tradeoff that multi-case studies cannot go into the same depth as single case studies. Nevertheless they provide a comprehensive insight into the studied subject. The methods applied should be suitable for the research approach selected. The qualitative research approach that has been chosen in this study prescribed that interview questions should be made relatively open-ended to a small sample of companies (Silverman, 2000).

The approach in this study is based on the concept of system combining as described by Dubois & Gadde (2002). System combining is a process where the theory, empirics and analysis evolve together and where findings within one area can lead the researcher to make improvements within another part based on these findings. This evolvement is according to the authors more useful using an abductive approach rather than an inductive approach or deductive approach. System combining is especially useful in the development of theories, which fits well with our study since it is focused on an area where the research is underdeveloped. Dubois and Gadde (2002) furthermore claim that case studies with this approach aimed at theory development should be classified as abductive. Even though the concept is developed for single case studies, its conclusions are deemed to be useful in multi-case studies as well.

The research approach in this paper is in line with the hermeneutic view of research (Llewellyn, 1993). Hermeneutics in management accounting refers to the theory of interpretation in qualitative research. It draws on the interdependence of social actions and the interpretation of texts (Llewellyn, 1993). The understanding is created through the hermeneutical circle in which the whole is referenced with the parts and vice versa. Ontology refers to the nature of reality. It ranges from a total objective view of reality to purely individual realities (Laughlin, 1995). The ontological basis for this study is located in the middle between the extremes. Therefore broad “skeletal” theories can be created from the observations (Laughlin, 1995). Epistemology is about the creation of knowledge and connected to ontology. The extremes are complete or no objective truths (Laughlin, 1995). Again a middle ground approach is selected. For transfer pricing systems, this study has to be based on the views and interpretations of individuals. Those are uncovered in qualitative approach through interviews to create a broader theoretical understanding.

3.2. Selection of the Case Companies

In order to make sure that the companies would have substantial amounts of transfer pricing within their organization, this study chose to focus on large multinational companies with extensive operations around the world. Large multinational companies are also more likely to have a separate specialized transfer pricing function. Since transfer pricing function tends to be centralized in companies’ global headquarters it was decided to focus on companies with their global headquarter in Sweden, or companies which were known to have a large headquarter function presence within Sweden. This would enable us to conduct interviews in person rather than by telephone. Face-to face interviews are deemed preferable in order to gather as much information as possible.

Transfer pricing systems across industries differ substantially (Borkowski, 2001). Comparisons within one industry can therefore lead to more fruitful comparisons and results. Comparing and contrasting improve the analytical conclusions. Thus multi-case studies and should be preferred to single cases (Yin, 2003). To limit the scope of the study, the focus is on one industry. Comparisons within one industry enable the identification of common characteristics in this explorative study. The manufacturing industry was selected as the target industry. The reasoning for this is that they have significant physical assets for their production in addition to intangible assets. Companies with significant physical assets are especially interesting to study since physical assets are more difficult to move and transfer of intangibles therefore can create more tensions within the operations in such companies. The influence of the companies' operations on transfer pricing is therefore emphasized. This is in contrast to other industries for example software companies. Furthermore, as most of the largest multinational companies in Sweden do have a manufacturing focus, the access to case companies is facilitated and the interview and information gathering process simplified. In order to make sure that the companies we approached had significant intangible assets apart from their brands, we first checked the companies' annual reports for information regarding the ownership of intangible assets. In order to get additional confirmation we thereafter checked the potential case companies in the Swedish patent office database over approved patents within Sweden, see e.g. (Patentverket, 2012).

This study is based on six cases, which provides rich data for in-depth comparisons, although the sample is not statistically significant. The sample size does however enable us to draw more general conclusions that might apply to a larger sample. The case companies were initially selected purely based on the characteristics of their operations. No previous relationship had been established between the researchers and the companies. This enhances the impartial view in the case description and the interpretation of the results. The companies have first been contacted by telephone and then an email has been sent with the outlines and goals of the study. Of the companies approached, almost all were willing to participate in this study.

At each company we focused on getting interviews with personnel directly involved in the company transfer pricing system. This function was mostly part of the tax department. If possible and deemed beneficial further interviews were conducted with other functions, mainly in the management control to fill the knowledge gap that still persisted after the initial interviews. All in all nine experts were interviewed at the companies of which seven were transfer pricing professionals and two specialists in management control. They were all responsible for the transfer pricing system within their respective company and had all extensive experience within the transfer pricing field. In all companies the transfer pricing department at the headquarters consisted of either a single person or a small team. All companies and their representatives were assured anonymity. This allowed them to speak more freely about this topic, which is sensitive, and was one of the conditions for their participation in this study. In addition knowing the identity of the companies would not add value to the results of the study. On the contrary anonymity can be beneficial as it prevents the readers to be biased by their own perception about the company.

In order to gain a holistic perspective on the subject of transfer pricing, after studying the in-depth cases, experts in the fields were approached. Six consultants from all of the “Big Four”[4] accounting firms’ representations in Stockholm were interviewed. They provided a broader view on the topic and helped to identify trends and developments in terms of both industries as well as countries. Furthermore their input was helpful to assess the data and information gathered from the companies. In addition the tax authorities play a crucial role in the area of transfer pricing. They determine the application of the regulation and are the subject of addressees of the companies’ efforts in transfer pricing. One expert at the tax authorities was interviewed in order to get the tax authorities’ perspective of companies systems and goals in transfer pricing.

3.3. Data Collection

The qualitative data for the case studies has been collected through interviews, which is described as the primary source for data in qualitative research (Rowley, 2012). The interviews were semi-structured to gain an in-depth insight into the topic, while retaining the flexibility to take up points that appear to be relevant for the research. As prescribed by Eisenhardt (1989), a well-defined focus and systematic approach for data collection is crucial for successful research. However, all pre-determined structures should be tentative to be able to adapt to the findings, which is fulfilled by a semi-structured interview approach.

The data gathering should be determined by the subject matter (Fidel, 1984). In this case the study of transfer prices is dependent on the information provided by professionals who work within this area. As the decisions in this area are more of a strategic nature and do not occur on a regular basis, interviews are the most appropriate and practical approach. This allows for the collection of rich empirical data as the studied event is infrequent, especially if several cases are studied (Eisenhardt & Graebner, 2007). Rowley (2012) identified three conditions, when interviews are especially useful: (1) the research objectives center on understanding experiences, opinions, attitudes, values, and processes. This is the case here as the study is aimed at understanding the structure, goals and overall logic of the transfer pricing system. (2) There is insufficient known about the subject to be able to draft a questionnaire. Current literature has not dealt in detail with the question of transfer pricing of intangible assets and empirical data is lacking. Explorative research is necessary as a first step. (3) The potential interviewees might be more receptive to an interview than other data gathering approaches. The interviewees’ want to retain control over the information they provide as the data regarding transfer pricing might be sensitive. The interview allows them to determine what they want to share with the researchers.

Ideally, different sources and research methods for data collection are applied to get an optimal insight from different perspectives. This triangulation enhances the quality of the study (Maxwell, 1996). Due to the sensitivity of the subject, interviews were the most important source in this study. It was not possible to gain significant access to internal pricing data, of which organizations are very protective. Observations are hardly possible and would

[4] PricewaterhouseCoopers, KPMG, Ernst & Young and Deloitte

not be very insightful. Public accessible documents, such as data from annual reports or ad-hoc publications, were used in this thesis to supplement the information gained in the interviews. The documents were used to understand the background and the strategy of the companies. Furthermore the accounting data was analyzed to determine the efficient tax rate and relate it to the statutory tax rate. This enabled a critical evaluation of the companies' tax strategies mentioned in the interviews.

3.4. Conduct & Structure of the Interviews

Semi-structured interviews are the most common interview method used in case study research (Rowley, 2012). Semi-structured interviews can be adapted to the situation of the interview and thus take into account the special characteristics of the interviewee and the organization. The interview questionnaire contained a number of areas and questions which should be covered during the interview. The order the questions were asked in depended on the flow of the interview and the questionnaire was used as a checklist to make sure that all important questions had been covered during the interview. This approach allowed for probing questions in the interview process. The probing questions help to uncover details and connections which enhance the quality and the validity of the study (McKinnon, 1988).

In total, 16 interviews were conducted. The interviews were in-depth and lasted on average between 60-90 minutes. While some lasted up to two hours, selected follow-up interviews took around 30 minutes. A pragmatic approach was used, taking into account the time the interviewees were willing to spend on the interviews (Rowley, 2012). The length of the interviews ensured a detailed overview over each of the cases.

The interviews were almost all conducted face-to-face. This approach can help to reduce potential reluctance from our interview persons with regards of talking about transfer pricing and intangibles. Both can be considered to be quite sensitive subjects for a company to talk about to an external party. We deemed that the personal interview experience would create a more open atmosphere and that the interviewees would therefore give more detailed answers. Two interviews were conducted via telephone as one interviewee was located in a different country and one shorter interview was necessary for follow-up questions.

The data collection took place from February to April 2013. First the case companies were interviewed. This was done to first gain an in-depth insight into transfer pricing in practice and be unbiased from potential normative consultancy perspectives. At a later stage input from the consultancy companies was added to assess the data gathered in the case studies. Both researchers conducted all of the interviews together to ensure that all important occurrences were noted. The insights could thus be complementary and also contradictions could be valuable. In the majority of cases, the interviews were held with an individual person from the case company. However, in some instances two persons were present in the interview. In those cases, the hierarchical higher standing person was usually more active, while the subordinate added selected insights. In some cases separate interviews were conducted with the second person to gain a holistic perspective.

During the interviews, the first step was trying to establish rapport by introducing the research, highlighting its relevance to the interviewee's experience and explaining the goals of the interview. Anonymity was ensured to all interview partners so that they were able to talk freely. The interviews were recorded whenever the interviewee agreed to this, which was not always the case. Thereafter the recordings were transcribed and sent to each interviewee for approval. For the interviews with the consultants, which provided more of a background and help for the analysis, summaries were written and the recordings provided a backup in case for the need of a more detailed analysis. Additionally, meticulous notes were taken by both researchers and afterwards compared and compiled. This was especially important for those interviews, where recordings were not desired by the interviewees.

The questionnaire used was based on recent transfer pricing theory although no questions were directly taken from other studies. The interviews started with more general questions to gain an overview over the organization and the system. In the course of the interviews, the questions became more detailed and targeted to uncover the specificities of the transfer pricing systems in each organization. During the data collection process, the questionnaire was continuously improved to take the findings into account and gain the most valuable information. Furthermore different questionnaires were used for the different groups that were interviewed. As pointed out by Maxwell (1996), it is important that the interview questions lead to the required data and not that they simply cover the research question. The questions asked in this study were as a result more open and covered different areas and aspects of transfer pricing.

Rowley (2012) argues that one should be careful not using too many scientific and professional expressions in the interviews in order to ensure the understanding of the questions by the interviewee. In the interviews conducted for this thesis all the interviewees were professionals with long experience in the field. Thus the usage of professional vocabulary was not only possible but also necessary to be able to discuss the issues.

The conditions in which the interview took place are important to consider when interpreting it (Alvesson, 2003). Important conditions are the cultural and psychological factors such as organizational position and motivations of the interviewee. In the interviews that were conducted for this study comparable conditions could be achieved in all cases.

One of the risks in the interview is that the interviewee considered was politically correct in accordance with his interests or fear that certain facts may harm himself or the organization (Alvesson, 2003). This is a problem in the case of transfer pricing which can be used for profit shifting into low tax jurisdictions. Companies in Sweden do not want to be associated with tax evasion schemes. To mitigate this effect, the tax authorities were also interviewed in this study to get a comprehensive overview in this topic. Furthermore the anonymity in the representation of the data increases the openness of the interviewees.

3.5. Analysis

The first step of the analysis is organizing the data from the different interviews and sources. Within this research, there has been some overlap in the analysis and the collection of the data. This overlap can be beneficial for the ongoing process in data collection as it enhances the flexibility and allows for adjustments in the data collection process (Miles & Huberman, 1994) (Eisenhardt, 1989). Eisenhardt (1989) describes that the comparison between different cases in the process of collection allows for an early analysis. This has been done in this paper by taking advantage of the multi-case-study approach. In this thesis the authors have continuously compared the newly gained insights from one case study to the cases and structures of previous companies. Thoughts were noted down and the researchers engaged in an ongoing dialog and reflection about the new findings and how to categorize them in the context of the previous ones. The danger in this approach is though that the earlier interviews bias the later ones, but the advantages of an early analysis outweigh the drawbacks (Maxwell, 1996).

The following step in the analysis is the within-case analysis (Miles & Huberman, 1994) (Eisenhardt, 1989), which was applied in this thesis. The different cases were outlined separately as descriptions of the current transfer pricing system in the company. This step can be regarded as data reduction as described by Miles & Huberman (1994). However, summarizing was not only done to better cope with the amounts of data but mostly to systematize the findings and also to separate the cases and to gain a comprehensive insight into each of the cases on a stand-alone basis (Eisenhardt, 1989).

After having gained an overview over the cases, they are compared to each other in detail. Coding is used in the analysis to categorize the data. This should facilitate the comparison of the data and should be grounded in the data (Maxwell, 1996). The codes are used to highlight the differences and similarities between them. Coding is the first step to prepare the analysis (Miles & Huberman, 1994). Different characteristics of the transfer pricing system were identified from the literature review and used as codes if appropriate in the context of the findings. In addition common themes that arose from the comparison of the interviews were used as bases for codes. In a spreadsheet the different characteristics of the companies were classified according to their description. Furthermore the notes were structured according to common topics. This allows for the emergence of patterns in the multi-case study and forces the researches to apply more diverse and structured viewpoints. Consequently the resulting theory is more reliable (Eisenhardt, 1989).

3.6. Quality of the Study

To determine the quality of the study, four tests are used according to Yin (2003): Internal validity, external validity, construct validity and reliability.

Internal validity: Validity is the key issue in research design (Maxwell, 1996). It refers to the correctness of the conclusion and interpretation of the study. To ensure the correct description of the problem, recordings of the interviews are conducted whenever possible (Maxwell, 1996) and the notes compared right after the interviews. Incorrect interpretation of the data is somewhat mitigated by a member check and the discussion of preliminary interpretations with experts in the field. Another issue especially with interviews is the subjectivity in answers (Miles & Huberman, 1994). This is mitigated to some extent by including different perspectives, which should contribute to a more holistic view on the subject. Additionally comparisons in a multi-case study contribute to the validity (Maxwell, 1996). Data access limitation is another significant issue for researchers, which are barred from certain documents (McKinnon, 1988). This is the case as we do not have a full insight into the companies' systems that process the transfer pricing. An observer bias cannot be avoided and is present in all researchers during interviews (McKinnon, 1988). To alleviate the observer bias, this study has been conducted by research team consisting of two people. However, this might not eliminate all risk as the different people might all have the same bias (Alvesson, 2003). Yin (2003) described furthermore analytical tactics to increase the internal validity of the study. It is imperative to make the right inferences, consider rival explanations and build up a logical model in the analysis.

External validity of a research study discusses to the generalizability of the findings. In qualitative research, the ability to generalize is not the main focus (Maxwell, 1996). It is though a general criticism of case study research (Otley & Berry, 1994). It is difficult to generalize findings of case studies for a greater population as the sample selected in this thesis is not statistically significant and thus assumptions on transfer pricing systems in other organization should be done with care. Purposive sampling can increase the possibility of being able to generalize findings (Silverman, 2000). The particular findings of one case might not be representative. However, it is possible to make an analytical generalization and build a theory from case studies by gaining insights into a case (Yin, 2003). Additionally, according to Cooper & Morgan (Cooper & Morgan, 2008) case studies only lack the generalizability potential with aspect to statistical generalization. Empirical generalization is still possible. They also state that case studies have the possibility of generalizability in terms of giving common explanations for an event or identify several events that have the same theoretical features. In multi-case studies, it is possible to increase the external validity through the replication of the case study, as has been done in this thesis. It is important though that the approach of the study stays constant so that comparisons are possible.

Construct validity refers to the correct operational measurement of the study object (Yin, 2003). Three procedures are prescribed to ensure a high construct validity of a study. Multiple sources of evidence should be used. This is fulfilled in this study by drawing on interview partners from different organizations, which are not limited to companies but also include consultancies and the tax authorities. Additionally a chain of evidence should be established. This means that the empirical findings need to be documented and combined. Through the use of transcriptions and detailed note taking a comprehensive documentation was created. In the subsequent analysis all evidence is comprehensively presented. Lastly, Yin (2003) recommends letting key informants review drafts. The case descriptions were then sent to the interview partners for review to ensure that they have been understood correctly and the description is correct. Some interviewees were contacted for clarifications.

Reliability: Reliability shows how a case study can be repeated and leads to identical results and conclusions. The goal herby is to eliminate errors and biases as far as possible (Yin, 2003). It is impossible for case studies to achieve a complete reliability as the conditions for them change constantly (Fidel, 1984). Especially semi-structured interviews will be different as human behavior changes. This does not mean that case studies can never be reliable and there are several ways to increase the reliability of the findings. The documentation of the process is crucial. Recordings and transcriptions of the interviews, as conducted in this study, improve the reliability as they provide a detailed representation of the interview (Peräkylä, 1997). When recordings were not possible, both researchers were taking detailed notes that were later compared and compiled. Furthermore the reliability in this study should be given as the major structures and systems studied, while constantly changing on a smaller scale, are relatively stable when looking at the bigger picture.

4. Analysis

The analysis is structured as follow: After the introduction of the case companies, the goals of transfer pricing are analyzed and compared, followed by the structure of the transfer pricing system. After that the choice of the companies regarding the use of one or two books is studied followed by the structure and handling of intangible assets. Lastly tax considerations are taken into account.

4.1. Case Companies

Company A

Company A has revenues of almost SEK 100 billion, more than 30 000 employees and is listed on the Stockholm Stock Exchange. A is headquartered in Sweden and active in the manufacturing and service industry. The products are solely sold in the B2B sector and the company is one of the global leaders within its industry.

With its divisions A is present in more than 100 countries around the whole world. The company has a very long history in Sweden, which spans over more than 100 years. Continuous improvement, cost efficient production and organic growth have been the company's main focus areas in order to improve profitability. As a result the company has mostly refrained from doing any major acquisitions. It is also very important for the company to be able to deliver customized solutions based on the customers' demands and the company strives to keep a long-term relationship focus with its customers. The manufacturing of A is centralized in a few locations with a significant part of the production taking place in Sweden. The distributors are located all around the world and are relatively autonomous. The group has both independent and fully owned distributors.

Company B

Company B has revenues of almost SEK 50 billion, more than 40 000 employees and is quoted on the Stockholm stock exchange. B is headquartered in Sweden and active in the manufacturing of hardware products and related services, where the services make up a substantial part of the revenues. The products are sold in the B2B sector, where the company is global market leader. Although the products are mostly standardized in each country, some have to be customized due to the customer's requirements and to local market requirements and conditions.

The company is structured into five divisions. Three of these divisions are geographical divisions related to the core products, while the other two divisions are global and focus on more sophisticated customer solutions. While the geographic divisions are still larger, the product divisions are gaining in importance. With its divisions B is present in the whole world and has subsidiaries in more than 50 countries.

B has been formed through the merger of two major companies and growth has been achieved to a large degree through frequent acquisitions. Currently there are over 200 operating companies in the group, while numerous acquisitions take place every year. The resulting organizational structure of the company is therefore rather decentralized and the subsidiaries are relatively independent in their decision making. The headquarters of the divisions are consequently located in different places around the world.

Company C

Company C is one of the largest industrial companies in Sweden. C is a truly multinational company, quoted on the stock exchange, with large operations in Sweden, but also in a variety of other countries. The company operates in the technology driven manufacturing industry, with a wide range of different products and solutions in a variety of business. The products range from smaller parts to large scale systems and are sold in the B2B sector. C is global market and technology leader in several of its businesses.

C has roots ranging back more than 100 years. The group is the result of a merger and has continuously conducted acquisitions, but also occasional divestments in recent years. The group is overall decentralized. The group is structured into several divisions and business units. The divisions and business units are strong and independent profit centers. The structure makes the company highly complex. All in all C is located in more than 100 countries. The legal entities in the countries do include multiple businesses.

While the group mainly focuses on organic growth, selected acquisitions that strengthen the businesses are also undertaken. The next growth focus should be on emerging markets and growing technologies. The decentralized structure does however reflect the companies approach to introduce market mechanism between business units.

Company D

Headquartered in Sweden, company D is one of the largest groups in the manufacturing and service industry and its history goes back over 100 years. The company has more than 100 000 employees and revenues of over SEK 200 billion. D mostly sells solutions, whereby the services make up a substantial part of the package provided to the customers. It is the leader in its B2B industry, with a limited number of large, important customers. With its solutions, D is active in over 180 countries all over the world.

The company is structured into four business areas, whereby the product and the services business areas are by far the largest parts of the company. Additionally D consists of ten geographical regions, each of which is divided into customer units. The company also compromises six product solutions. D is highly technology oriented and has over 30 000 patents in its portfolio. Overall the company aims to be a global company, making use of synergies and economies of scale. The Swedish global headquarter is the organizational parent of all the subsidiaries of which there is one per country, whenever possible. Historically, the structure has been more decentralized, but increasing global competition has led to the development of the current setup, which has been in place for over ten years.

The company follows a strategy of profitable growth and therefore conducts selected acquisitions but also divestments. The overall revenue should be more based on services and integrated solutions than on standalone products, so that the company can leverage its current customer base. Furthermore the technology leadership should be sustained, which is reflected in substantial investments in R&D activities.

Company E

Company E is a multinational company headquartered in Sweden and active within the manufacturing sector. E has around 40 000 employees and revenues of almost SEK 100 billion and is quoted on the Stockholm stock exchange. The products are solely sold in the B2B sector and the company is one of the global leaders within its industry. Its historical roots go back as far as to the late 19th century. The company is active within the B2B manufacturing and services sector, which stands for similar shares of the company's total revenue. The company is structured into four business areas divided by type of products. Each business area does in turn have many divisions under them and in total the company has over 350 subsidiaries in approximately 150 countries.

Due to its historical heritage, the company is quite decentralized and has a lot of its operations outside of Sweden. Legal entities in the different countries normally encompass several divisions. As a result E has a complex structure of operations.

Company F

Company F has revenues of more than SEK 100 billion, more than 50 000 employees and is listed on the Stockholm stock exchange. F is headquartered in Sweden and is active in the manufacturing industry. Its products are sold in the B2C sector and the company is one of the global market leaders in its industry. F sells its products in more than 150 markets around the world. The company is organized in three divisions which are based on the type of products they produce and sell. The largest division is additionally divided into geographical regions.

Historically, acquisitions have been a core part of the company's strategy for growth. Also in recent years the company has done selected acquisitions. The company's strategy is linked to becoming an even more global company and to increase sales in non-European markets. Growth mainly takes place in emerging markets. The competition in the industry is increasing. The historically more decentralized structure is moving towards more centralization in order to make use of synergies and economies of scale. This should be done by leveraging the company's brands' recognition. The company has a few main brands, which are supplemented by a large number of regional brands.

4.1.1. Summary of Sample

All companies in our study are multinational companies with major headquarter functions based in Sweden. The companies are all among the largest in Sweden. They have all a long history in Sweden dating back 100 years or more. All companies in our study are manufacturing companies and all except company F have almost exclusively other business as customers while F is mostly focused toward private customers. Even so, company F has significant business with other business as customers. The companies' structures in terms of level of centralization are differing quite significantly between the companies, but there is a general development among most of the companies of going toward a higher level of centralization.

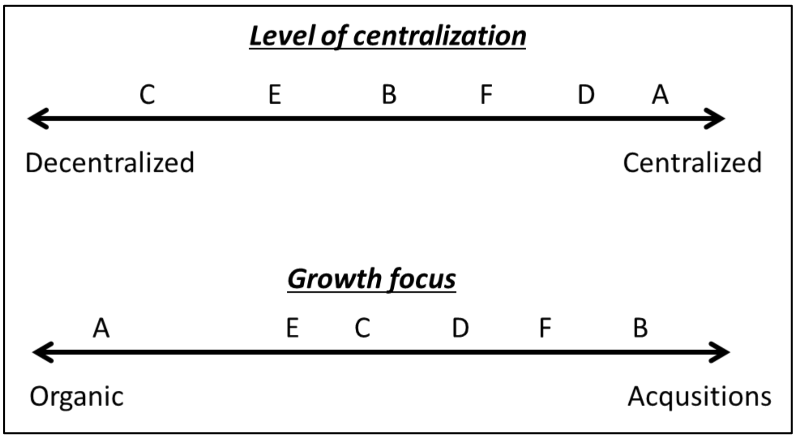

Figure 2 - Illustration of the companies' relative position in terms of centralization and growth strategy

4.2. Goals of Transfer Pricing

The goals of transfer pricing can be diverse. However, in the companies that were interviewed for this thesis, distinct patterns can be identified. The overall goals can be seen in all companies, although they are weighted in a slightly different way. It has to be noted that the goals of transfer pricing for intangibles correspond to the goals of the overall transfer pricing system and are not considered separately. The ultimate goal of all of the studied companies was to create value for the shareholders. The role for transfer pricing to achieve this is not clearly defined. The different emphases in the goals can be attributed to several factors such as the company strategy, the operations or the managers responsible for transfer pricing. Cravens (1997) has identified three different groups of primary objectives in transfer pricing:

1. Taxation related
2. Internal Management oriented
3. International and Operational

This classification is used as guidance in this analysis.

4.2.1. Taxation Related

Taxation related transfer pricing objectives are named as the most important by the majority of the companies in the study by Cravens (1997). This includes the goal to manage the tax burden, to comply with tax regulations and to manage tariffs. In the companies a strong differentiation between tax optimization and tax compliance can be seen.

4.2.1.1. Tax Optimization

We find that tax optimization is not a priority for our sample companies. All companies consider this goal to be of lesser importance compared to other objectives. They also perceive the public perception of this issue as exaggerated. The Director Transfer Pricing at company B states that: *"Transfer pricing is not as planned as the media or the tax authorities might think, tax optimization is not a major focus."* Companies do not want to be associated with heavy profit shifting. No company claims to try to optimize their taxes significantly. Those statements are confirmed by the efficient tax rate as stated in the 2012 annual reports of the companies. The average tax rate of the last three years of our sample companies stands at 27.0%[5], which is even slightly above the statutory tax rate for those years in Sweden of 26.3%. Between the companies, the average tax rate ranges from 24.2% to 33.7% showing that none of the companies is trying - or at least not successfully - to significantly minimize taxes.

In accordance with this, neither the interviewed consultants nor the Swedish tax authorities consider tax optimization the primary goal of Swedish companies in transfer pricing. The Tax Director at consultancy C especially mentioned a difference between industries: *"There are slight differences between industries. For example, it can be more difficult to move manufacturing activities compared to a software business. Manufacturing companies would normally have a larger part of fixed assets such as machinery and equipment, and even often be more labor intensive. Additionally, a manufacturing business is often located at a specific place for a longer period of time, hence making it less flexible – for example they are often located in a smaller town for many years and would have significant local presence."* On the one hand the risk for audits is considered too high and moreover the companies are not willing to change their operations to the extent required in order to pay less taxes. On the other hand, more pragmatic reasons are mentioned for the lack of tax optimization. For example the Tax Controller of company E highlighted that compliance alone is such a difficult and cumbersome task that there was simply no time or resources left to explore the possibilities for tax optimization: "*Tax optimization is not in focus as the organizational constraints are too high, there is stringent regulations in place and the tax authorities are quite aggressive. We believe that tax compliance is the best form of tax optimization."* Even though the literature mentions that tax optimization is easier with intangible assets compared to tangible assets (Dawson & Miller, 2009), the case companies in this study did not have a more aggressive approach for their intangible assets than for their tangible assets.

Nevertheless, the companies usually take the opportunities to build at least not unfavorable tax structures. Furthermore company B states that it is not totally defensive and tax disputes are not avoided at all cost, especially when the operations might be affected. Additionally in benchmarking approaches, more advantageous solutions are chosen, which are well within the borders of the legislation. All in all a reasonable approach to reduce the tax burden is sought after. Furthermore, having operations in Sweden is considered relatively beneficial by the companies as opposed to, for instance, Germany. Consultants on the other hand do not agree and name Switzerland as the most advantageous location due to its favorable tax levels for companies based in Switzerland. The Tax Partner at consultancy B described the ideal structure for intangibles as follows: ***"****An ideal transfer pricing for intangible assets would be with the principal situated in Switzerland, where you could get a ruling with a very low tax-rate. The IP department and its management have to be located there. In other countries there*

[5] This is calculated as the average of the companies' respective average tax rate over the time period 2010-2012. The tax rate for each company is calculated as tax divided by income before tax. Both numbers are taken from the respective companies consolidated income statement.

would only be toll manufacturers and sales agents. This structure could then be owned by a Swedish AB holding company."

The lack of a tax optimization focus is in stark contrast to the findings of Borkowski (1992) and Cravens (1997), which have identified tax minimization as companies' primary objective of transfer pricing. This difference can be explained with the fact that those studies are relatively old. They do not take newer regulations and especially the OECD guidelines into account, which are aimed at preventing tax planning. The regulation and its application have become more stringent in the past years, not only in Sweden but also all over the world. Companies and consultants highlight the fact that letterbox companies which have no or a very limited physical presence, are not feasible anymore.

The regulation stresses the need for substance when determining profits. Consequently the findings of this study are more in line with more recent studies (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010), which emphasize tax compliance. Furthermore some of this difference might be attributed to the fact that Borkowski's (1992) and Cravens' (1997) studies were conducted in the United States, while Cools et al. (2008) and Plesner Rossing & Rohde (2010) look into European companies. These studies did not, however, have a special focus on intangibles but mentioned assets in more general terms with no distinction between the tangible and intangible assets. No relevant studies in this area has been made since Plesner Rossing & Rhode's study in 2010, but given that the regulatory environment has been relatively stable since then, the two later studies should still be highly relevant.

4.2.1.2. Tax Compliance

On average, the second most important goal for the companies in relation to transfer pricing is the need to comply with tax regulations. In company F it was even mentioned as the most important goal. All companies stressed the importance of following the rules in all countries they operate in to avoid costly tax audits and tax adjustments by the authorities. As stated by the Tax Controller in company E: "*To be a good corporate citizen is our main goal and tax compliance is assumed as a necessary part to it. We identified compliance on transfer pricing at a very early stage and we have been actively working on this over the past few years*." Furthermore the companies do not want to be associated with questionable actions to save taxes. Even if the companies determine their transfer pricing through negotiations, like company A or in certain cases company B, the resulting prices have to be in line with the arm's length principle.

In this context it was also mentioned that this is challenging as the regulations in different jurisdictions not always agree with each other. Furthermore the companies' multinational operations result in highly complex structures. The OECD guidelines are perceived as helpful to avoid conflicts in the major countries. This was especially mentioned by the Tax Lawyer in company D: *"In general, we have less transfer pricing challenges in the OECD countries, compared to other parts of the world where the OECD transfer pricing principles are not adhered to in the same manner."* Especially the BRIC countries (Brazil, Russia, India and China) are considered as difficult and expensive to comply with as the local regulation might contradict the OECD guidelines. This is not only noted by the companies but also considered by the Swedish tax authorities. Consequently the Tax Auditor of the Swedish Tax Agency states: *"Trade with the BRIC countries is growing. The problem is that their regulation is not always in line with the OECD. There is an increased influence by the BRIC countries. These countries influence the companies and in that way they also influence us."*

Tax compliance can be considered as tax risk management (Wunder, 2009) and compromises between different countries and tax authorities have to be found. Tax audits are regarded as risks that should be avoided, which is however not always possible. The risk appetite of the companies and their employees thus determines the way they interpret the requirements of tax authorities. The observed companies can therefore be considered largely risk averse in their behavior. Compliance with the regulations takes the majority of time for the companies' transfer pricing departments. Especially documentation requirements for all countries are cumbersome and have to be updated on a regular basis. The interpretation of the requirement to keep an updated documentation varies between the companies. In company C updates its documentation on a yearly basis; this is done every two years in company D and every three years in company E. This exemplifies the trade-off that companies face between the requirement to be tax-compliant and the desire to reduce the cost of compliance.

In line with the results of Cools et al. (2008) and Plessner Rossing & Rohde (2010), the Swedish companies mention tax compliance as an important objective. The goal to reduce the risk of audits and prevent adjustments is a major driver in the transfer pricing systems of the companies. While this goal is acknowledged in other studies, it is not considered as important as found here (Borkowski, 1992) (Cravens, 1997). Cools et al. (2008) and Plessner Rossing & Rohde (2010) have shown that achieving tax compliance is a huge change in the company and affecting the whole organization. This might thus be in conflict with the goal for reducing the cost of compliance. The analyzed companies are aware of the large hurdles and almost impossible task to achieve complete tax compliance.

Tariffs have not been mentioned as a significant goal by the companies. They might only cause minor concerns, when the goods flow within one country but the invoice might be rooted through a principal, as has been explained by company D.

4.2.2. Internal Management Oriented

Internal management and motivation is found to be important by Cravens (1997) in transfer pricing. It is divided into equitable performance evaluation, motivation and promoting goal congruence. In the interviewed companies, this is not cited as a primary objective of the transfer pricing system. Internal management, which is compromised of the management control system and performance measurement, is largely separated from the legal transfer prices. Therefore the legal transfer pricing has little influence on the performance management. Other management systems and structures ensure efficient internal management. The results of this study therefore correspond more to the findings of Borkowski (1992), where performance measurement was not a primary objective in international transfer pricing. This relates to the fact that most companies make the transfer pricing adjustments for tax compliance below the line for performance measurement.

4.2.3. International and Operational

The goals under international and operational are divided into cash transfer restrictions, competitive position and reflection of actual cost and income (Cravens, 1997). In the analyzed companies however, a distinction could be made between the support of the operations and the simplification of the structure.

4.2.3.1. Support of the Operations

In most companies the support of the operations was mentioned as the most important objective of transfer pricing**.** This relates back to the competitive position goal described by Cravens (1997) since the main reason behind this focus for the companies is to strengthen the company's operations. The companies all regard themselves as operationally driven. This was the case in companies A, B, C and E that highlighted their role in supporting the operations. Also in companies D and F it was clearly one of the dominating factors. The Tax Director in company F describes it as follows: *"One thing that goes for most companies as well is that the operational managers are the strong people in the business. We cannot refer solely to the tax perspective and mandate dictate prices or price setups without their input. They pay our salaries at the end of the day."*

Notably in company D transfer pricing is supposed to have no effect on the operations and enables the business side to take the decisions that are most beneficial for them. This might be explained by the fact that D is highly technology driven, which requires fast decision-making. No decisions in transfer pricing should in any way obstruct the way of doing business or require significant changes to the operations in any of the companies. For example in company A operational efficiency is a key component of the strategy. The transfer pricing function can therefore only give recommendations while the business functions take the decisions. The rationale behind this is relatively simple: Without profitable operations, there is no room to reap any potential tax savings from transfer pricing. The whole transfer pricing system has thus to reflect the way that the company conducts its business. The companies transfer pricing system does in general not influence the operations, rather the operations are taking the decisions and the transfer pricing function has to ensure that the resulting prices are tax compliant.

Operational concerns are also considered in the literature. The survey-based study made by Cravens (1997) found that in 28% of the companies, an operational objective, especially the competitive position, is the most important goal in transfer pricing. In addition, Eccles (1985) highlights the fact that transfer pricing is influenced by the strategy and the administrative processes within a company. The transfer pricing system thus has to fit with the company's strategy and the operations. This is reflected in the case companies, where the used systems are considered as the most appropriate solutions regarding the transfer pricing system. Another explanation for the dominance of the operations can be seen in the internal hierarchy of the companies, which has been mentioned by the interviewed consultants. The operational side of the business is powerful and can take the dominating decisions. The tax functions in the companies are rather small and do not have the internal power to push through decisions against the will of the operations. They are considered a support service. As the Senior Manager Transfer Pricing at consultancy B described it: *"Many tax departments in big* *companies are seen as a support function. They are not part of the core management team. They are not able to convince the company due to the lack of internal political capital of beneficial tax solutions."*

4.2.3.2. Simplification

Another important goal of the transfer pricing is to ensure a structure that is relatively simple and manageable. This can be considered as part of the operational goals. In companies B and D this is cited as the second most important goal. This allows for a relatively lean administration and reduced cost of compliance. But also in the other companies it plays a significant role. The Tax Controller in company E highlights: *"The existing operational structure historical growth and the acquisitions still exert a significant influence in our company. This makes the structure of the operations really complex with a number of entrepreneurs and one of our goals is to work with the operations to simplify these structures where possible."* That all companies do consider this goal relevant can be seen by the fact that the transfer pricing department employs few people in the headquarters. Furthermore, simple structures are more transparent and can be more easily understood. They are accepted more readily by the tax authorities. Simpler structures imply standardization and harmonization of transfer pricing practices across several jurisdictions. As this might not always be possible, a certain complexity cannot be avoided. Not all companies seek to actively reduce complexity. Company C assumes that it is impossible to support its operations with a simplified system due to the highly complex nature of its operations and thus concludes that they have to find a way to handle the complexity in the organization. No need for simplification and standardization is identified.

Concerns regarding the simplification of transfer pricing systems and reducing the cost of compliance are also mentioned by Borkowski (1992). This goal is important, but not primary. This corresponds to the findings of this study. Simplification is desired by the companies, but other objectives are given priority in case of conflicts.

4.2.4. Conclusion from the Goals of Transfer Pricing

When comparing the companies, it can be seen that the goals the companies pursue with their transfer pricing system are quite similar. Even if the priorities are slightly differently weighted in the companies, those differences are mainly nuances.

	Company A	**Company B**	**Company C**	**Company D**	**Company E**	**Company F**
Support the Operations	High Priority	High Priority	High Priority	High Priority	High Priority	High Priority
Tax Compliance	High Priority	High Priority	High Priority	High Priority	High Priority	High Priority
Simplification	Medium Priority	Medium Priority	Low Priority	High Priority	Medium Priority	Medium Priority
Tax Optimization	Low Priority	Low Priority	Low Priority	Low Priority	Low Priority	Low Priority

Table 1 - Overview of the companies' goals for their transfer pricing system

The main objectives in the companies, when aggregated, can be ranked as follows:

1. Support the operations
2. Comply to taxation regulations
3. Simplify the structure
4. Optimize taxation

These findings are in line with the argumentation made by Abdallah & Murtuza (2006) that transfer pricing of intangibles should not only focus on taxation but consider operational consequences as well, something the companies in our study agrees with. Additionally, in our findings there are no difference between the goals for intangible assets and tangible assets. It has to be noted that the different goals are relevant for different functions. The overall transfer pricing system should support or at least not obstruct the operation. The tax department, where transfer pricing is usually located, is pursuing the goal of tax compliance more on a day-to-day basis. A simplified structure is also helpful.

The uniformity of goals might be due to the fact that the companies are quite similar. They are broadly active in the same industry of manufacturing, where the operations have a dominating stand. Shifting around productions and functions is more difficult with significant physical assets. Additionally all the companies are deeply rooted in the Swedish business environment, which has an impact on the objectives as found in the literature (Tang, et al., 1979). The companies are all affected by the same Swedish tax authorities and the Swedish application of the regulations. The authorities aim at a clear and equal treatment of all taxpayers to avoid conflicts, which is stressed by the Tax Auditor of the Swedish Tax Agency: *"We are establishing a clear and predictable application to avoid disputes between countries as well as between the Swedish Tax Agency and the tax payers."* When linking these findings to the literature, it is noticeable that all of the above mentioned goals have been discussed in previous research (Cravens, 1997) (Tang, et al., 1979) (Borkowski, 1992). The weighting and priority is, however, slightly different from those studies. Most strikingly is the fact that in all the analyzed companies, tax optimization has been given a low priority.

Contingency theory predicts that the companies structure the operations according to several contingencies. Thus also companies' transfer pricing objectives should be influenced by a number of factors. If those factors would differ, the resulting goals should be different. In our findings, the goals are quite similar. Consequently one can conclude that the decisive factors which determine the goals are the same for all companies. As the companies face a similar external environment but have different operational structure, external factors are likely to be most relevant for the goal-setting. The organizational structure and operational setup exerts only a minor influence, especially regarding the priority of simplification in the transfer pricing system.

On the first glance, this analysis seems to contradict behavioral theory, which focuses more on the internal processes. In behavioral theory, goal setting in organizations is determined through bargaining processes between different actors (Cyert & March, 1992). In contrast, this analysis is mostly taking the bigger picture into account. In the objective of supporting operations, the processes discussed in behavioral theory are included, but require a more detailed insight to be uncovered. Behavioral theory furthermore acknowledges the existence of independent constraints on this process. Tax compliance is one such constraint, as it is required by the regulatory environment.

4.3. Structure of the Transfer Pricing System

The structures of transfer pricing systems for intangibles are as diverse as the companies' structure themselves. As found in this study, for many companies it is not possible to differentiate between the transfer pricing system for intangibles and the overall transfer pricing system. A benchmark structure which is referred to in the OECD guidelines (OECD, 2010) and in the interviews with the consultants as well as the companies is the principal structure. However, it is not always possible to implement this system, as can be illustrated by the companies. A typical regulatory environment requires exceptions. The companies structure their systems to a large extent dependent on their operations. Nevertheless, elements of the principal structure can be identified in most of them. The system determines the methods used for transfer pricing within the group.

Company A

In company A there is a differentiation between the treatment of the distributors and the production units which constitute the subsidiaries. As a whole, the group is organized around an operational parent company in Sweden which performs more or less all research and development (R&D), significant production, group management and owns most of the intangible assets. Towards its distributors, the company relies on negotiation-based transfer pricing, while for the production companies a cost plus approach is used.

Distributors have significant control over their own profit which comes with full responsibility for their own operations. Company A is using a negotiation-based transfer pricing system where the involved parties are doing the negotiation on their own behalf and independently from the transfer pricing department at the global headquarter. They are negotiating mostly on the price of the transferred product in which the intangible assets are included. The transfer pricing department is not allowed to influence the negotiation directly and no direct tax considerations are therefore made in these transaction. Thus those prices are purely operationally motivated as the distributors are measured on profitability. The negotiations should replicate market structures and thus through the process comply with the arm's length principle. The Tax Specialist describes that the company is confident that their system is in line with the regulations: *"Our negotiation based system is by definition arm's-length, since it is based on the same market principles as for external companies."* The difficulty lies in defending the integrity of the negotiation process. The company aims to verify the process through regular testing of the actual outcome of the process.

For the production units, Company A has a structure that has the characteristics of a principal structure. The production units do not own the products they are using or the final product. They get compensated for services performed on a cost plus basis, meaning that they receive a small but fixed margin on the full cost incurred in the operations. In relation to production units the Swedish company thus acts as a principal. The operational parent company owns all of the risks and intangibles assets and performs the major management functions. Furthermore, the production within the company is very centralized at the headquarters. The same structure is applied to R&D development through contract R&D. This means that the R&D departments are remunerated based on their cost including a small margin, while all the results of the research are owned by the principal.

Company B

Within company B a differentiation has to be made between the structure of the geographic divisions and the product divisions. While the geographic divisions in B are more decentralized and have more independent subsidiaries, the product divisions have a centralized structure. Most of the intangibles related to the geographic divisions are owned centrally while the product divisions mostly own their own intangible assets.

The geographic division in company B is operating with largely independent subsidiaries. The subsidiaries have their own local products but they market additional products of the whole group. They are relatively free in the structuring of their operations and measured on an EBIT level. As a result, transactions between those subsidiaries, e.g. about the transfer or sales of special products are based on negotiations. They are allowed turn down any deal if they do not like or accept the terms offered by the counterparty. Thus those transfers are considered to be at arm's length. Transactions with the parent companies on the other hand are to a large extent based on intangible assets. The tool for charging for intangible assets created in the central Swedish company is a franchising fee. This is a royalty charged to all IP-owning subsidiaries with full own responsibility for the whole value chain below the operational EBIT line. All intangibles offered through the franchise are developed and designed to, through proper implementation, enhance the business of operating companies. The franchising fee is charged as a lump sum to the subsidiaries, regardless if they make use of all the parts included or not.

The product divisions on the other hand draw on the characteristics of the principal structure. The central entrepreneur takes over all the risks and controls the intellectual property. It functions as a principal in transaction with other entities. The principal earns the residual profit of the venture. The other entities are either sales organizations or contract manufacturers. The profits earned by the contract manufacturers and the sales companies are calculated by a formula based on the transactional net margin method. The resulting margin is consequently relatively low but stable. The initial transfer prices applied are fully operationally based in order for the divisional management to drive and control the business out in the sales organization. To be tax compliant if the results of the local sales companies fall outside a certain margin range, there is a transfer price adjustment, which goes below the operational EBIT line.

Company C

In company C a difference in structure can be recognized for the treatment of tangible and intangible assets. While decentralization is dominant in the company as a whole, the intangibles are either owned or maintained by a central group company or locally.

Company C has a decentralized structure where the risk and residual profit to a large extent still is decentralized at the level of the local companies. There is no overarching transfer pricing system for the whole company. The divisions have come up with different solutions that best serve their needs. This renders the whole system complex, with transaction flows that encompass all divisions on different levels. While there is a high complexity on the group level, on a local and business unit level it does not cause significant issues. Consequently the company does not use the principal structure, but employs different solutions based on the needs of the business units. When transferring goods between different entities the price might be determined through different techniques from regular price lists to negotiations between different business units. The resulting prices are always checked for their fulfillment of the arm's length principle through thorough documentation.

In the use of intangible assets, different royalty rates are applied for different technologies. There is no standard solution but the transfer pricing is based on the circumstances and the need to support the business while complying with the regulations. For the use of the trademark, which is owned centrally by the group, a royalty rate is charged as a percentage of revenue.

In transfers between different legal entities of the group, negotiations are sometimes employed. As a result, transfer prices are often negotiated as between third parties. The use of intangibles is of decisive importance for the operations and the business. Although this structure for intangibles is more centralized, it does not correspond to the principal structure. Only few characteristics of the principal structure can be identified. This is the case in the technology development which takes place largely through contract R&D.

Company D

Company D is the only company studied that has implemented the principal structure to a large degree. Company D has a very centralized structure where the Swedish parent company is the principal, owns all the intangible assets and therefore takes most of the risk and residual profit for the whole group. When the group acquires companies the group as swiftly as possible transfers all the risk and the residual profit to the parent company in Sweden.

Under the principal structure, D employs the transactional net margin method to determine the transfer prices. The Swedish main operating company is taking over all the operational risks and is the main beneficiary of the residual. In line with the R&D activities, manufacturing is taken over by contract manufacturers, who have low risk and are paid on a cost plus basis. In some cases manufacturing is even outsourced to third parties. The sales companies of D sell the goods they buy from the headquarters at a resale minus price. All transactions are therefore channeled through Sweden, whereby the subsidiaries are left with relatively low margins. The exception to this is services, which might be exchanged between countries. Those are invoiced at cost plus directly to the subsidiary. The whole transfer pricing system has no influence on the operations and is considered purely a tax issue. The legal structure is completely separated from the operational structure and followed by two separate sets of books. The operations are structured in a different way.

For the intellectual property, no separate royalties are charged to the local companies but the use of the technology and trademark is priced into the goods. Overhead costs are treated in the same way. This structure is employed throughout the whole company, whenever possible. In some countries, local regulations might demand a light adjustment of these practices. For all transactions, benchmarks are used to ensure the compliance to the arm's length principle. To arrive at the correct profit for the subsidiaries, adjustments have to be made throughout the year. The operational viewpoints are the regions and the business areas.

Company E

Company E is relatively decentralized with most of the intangible assets being owned by the subsidiaries. Risk and residual profits are still to a large extent located at the local subsidiaries. The company tries to move towards more centralization where they centralize the assets, especially intangible assets at the divisional level. But nevertheless the company is moving slowly towards a little bit more of a principal-based structure, albeit a decentralized version of it.

The company has harmonized global policies and internal regulations for the whole group. The systems developed at the headquarters are then implemented by the local business units. The exact level of transfer prices is set by the product manager to serve their operational purpose. However, guidelines and advice is given from a central level. As the Tax Controller in company E notes: *"The business units know best how they should run their business. The headquarters just gives them advice on how to handle the transfer pricing issues*." Depending on the type of transactions the guidelines can be related to a benchmarked range from comparable companies, a certain percentage profit margin, determined by the transactional net margin method or other methods. The used levels are monitored by the tax department. Adjustments to ensure tax compliance are made below the line which is used for performance measurement and have no effect on the measured internal performance for the business units. For intellectual property, license agreements are set up between product companies. Royalties are calculated as percentage of sales, usually 3-5% for intangibles, and are benchmarked for each business area. The company has instigated a standardized policy for royalties where everything has to be approved by the transfer pricing department.

Intellectual property can be found throughout the group. The company headquarters would like to centralize the ownership of all intangible assets within the group to the headquarters in Sweden. This is because the company has more expertise centrally that can handle this type of assets and it would also simplify the transfer pricing system as well as making benchmarking easier. Centralized intellectual property is based in the division's headquarters and not in the group. The centralization would make the company at the divisions' headquarters in Sweden the principal. Company E is very focused on the needs of the operations themselves and in order to make any centralization of intangibles the divisions have to agree to these changes, otherwise no changes are made. As a result E is moving towards the direction of the principal structure for its divisions but has not fully implemented it.

Company F

Company F has historically had a decentralized structure with a majority of the intangible assets owned by the local subsidiaries but has since then moved toward more centralization based around the principle structure. The structure of the company is depending on the geographical region.

F uses a principal structure in Europe and in North America with each having one principal. One designated entity from a functional and risk perspective is considered the entrepreneur and is entitled to the residual returns whereas the factories (mainly structured as contract manufacturers) and sales companies (limited risk distributors) receive a low fixed margin often determined based on the transactional net margin method. Under the principal structure, the central entrepreneur is operating as a "hub" where legal title to the goods and thus also invoices flow through the principal. This enables the companies (manufacturing and sales) operating on behalf of the principal to be remunerated fairly for the low-risk and functionally limited activities performed. In order to make sure that the end result is in line with the targeted and acceptable transfer pricing framework the company makes adjustments. They take place mostly at each quarter but in some instances only yearly. The group's transfer pricing system is not fully standardized throughout the world but may vary for strategic or historical reasons. Intangible assets are relatively centralized, which is often preferable since this enables an easier use and more straightforward and transparent pricing of intangible assets throughout the world. Conflicts derived from split IP ownership are avoided in the centralization.

The transfer prices are set with input from the head office since this is where the central expertise and designated employees mainly are located. The most commonly used method for determining transfer prices within the company is the transactional net margin method. External consultants are used for benchmarking in order to determine arm's length transfer prices. The tax department is, however, not setting the transfer prices independently but consults the divisions in the setting of transfer prices and the transaction structuring. As in most multinationals, the operational perspective plays an important role in F. The Tax Director explains this as follows: *"We try to keep the transfer pricing system as simple and practical as possible. We are not the ones actually invoicing and administering the transactions, so we have to keep it somewhat straightforward. Somebody has to implement those very elaborate methods."*

4.3.1. Comparison between the Cases

When comparing the companies it is clear that the structures of the transfer pricing systems differ substantially despite the fact that the companies are all large Swedish multinational manufacturing companies. This can be explained mostly by the differences in operations, strategies and historical developments. The influence of strategies and organizational design on the transfer pricing system has also been the conclusion of the study by Spicer (1988) Drawing on contingency theory, those factors can be seen as the major influences on the transfer pricing system. The overall setup of the company, if it follows more a decentralized or a centralized structure, impacts the transfer pricing system significantly. Nevertheless, common trends can be identified. The development towards the principal structure has increased in companies in the last years, which reflects the current debate in this field (OECD, 2010)**.** The Tax Director at consultancy C described: *"As companies grow larger they would normally strive for a principal structure, having all intangible property centralized in one group company, typically the headquarters. This model works well since it makes the business easier to manage and makes the transfer pricing model typically simpler."* This was also confirmed in in the interviews with other consultants. It is regarded as the most practical and simple solution to design a transfer pricing system that is tax-compliant. Once acceptance by the affected tax authorities is achieved, the system can be managed efficiently and at lower cost.

Contingency theory can serve well to explain the differences in the transfer pricing systems. They are mostly adapted to the operational needs of the companies. Internal factors seem to play a large role in the design of the transfer pricing system. This is in contrast to the goals of transfer pricing which have been discussed before. The differences can also be related to that transfer pricing is a very complex area where it is hard to find a single right answer for any situation. The Tax Director in company F described the problem as: *"In an area like transfer pricing there is no exact price. You can work with placing functions and risks everywhere. This is never going to be an exact science. There are always going to be discussions, one side the tax authorities and on the other the companies and they want different things."*

4.3.1.1. Principal Structure

The requirements to implement the principal structure as they have been described in chapter IX of the OECD guidelines are substantial. The centralization and new allocation of assets, functions and risks is a project that creates huge costs. In addition, in practice the guidelines are not applicable in all countries. As a result the implementation of this structure has major consequences for the operations of a company. Converting full-fledged distributors into limited-risk distributors or full-fledged manufacturers into contract-manufacturers is not only the change of a name but can affect the whole operation of this entity. Furthermore, it can trigger substantial tax payments when intangible assets are moved. It can be concluded that these obstacles prevent most companies in this study to fully implement this structure. This is in line with the results described in the literature, where the introduction of tax compliance transfer pricings systems are huge projects and trigger changes in the operations (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010). Even in company D, that mostly applies the principal structure, a complete solution is not possible and exceptions are made for special cases and countries. One of the main reasons for moving towards the principal structure, as stated by some of the companies, is that intangibles carry such a high degree of uncertainty and risk, which is in line with the study made by Picciotto (1992). This in turn makes them so complicated that they are best handled by a centralized structure. Most of the responsibility for intangibles is taken by the parent company where the competence to handle these kind of problems is the highest.

It is noticeable that the companies employ different systems within one group, for example in company B or C. This highlights the fact that differences in the operations significantly impact the structure of the transfer pricing system. As the requirements in different divisions with different products are not comparable, the need for differentiation can be observed. This can also be related to the degree of centralization within a company. Centralized companies, such as D, tend to have a more standardized transfer pricing system than for example company C, which is highly decentralized. Some companies are therefore more open to change, whereas others seem more reluctant to create a new structure. A challenge highlighted in the interviews with the consultants was that while a change towards the principal structure can have significant advantages in the long-term, a change project creates high cost in the short-term. This is also in line with Busco et al. (2008), who's case company explains that there is always problems associated with a centralization process and that the process itself always takes a considerable amount of time. This can explain the fact that the companies in our study are approaching the creation of a principal structure in smaller steps in order to mitigate potential conflicts.

The dependency of the introduction of the principal structure on centralization can also be observed. Owning the relevant intangible assets is a necessary prerequisite for a parent company to become a principal. This does not mean that all centralization of intangible assets is aimed at creating the principal structure. As can be seen in company C centralized intangible assets are advantageous from an operational perspective even for decentralized companies.

In their approach to the principal structure, the companies exhibit the characteristics as described by behavioral theory. A theoretically optimal transfer pricing system cannot be fully implemented. Constraints and limitations for the companies have a large impact on the transfer pricing system and prevent optimal solutions, even though the actors are as such rational. The transfer pricing system is constantly subject to changing requirements.

4.3.1.2. Methods

The methods used for transfer pricing in the companies are dependent on the overall system. It can be observed that the transactional net margin-method (TNMM) is common among the companies that employ the principal structure or some variation of it. With TNMM the companies earn a defined margin which corresponds to what a company with similar functions, risks and assets earns in the market. According to the Tax Director of company F this method is often used in practice: *"Some type of TNMM is what almost all companies use all the time."* This finding is in line with the study by Elliott & Emmanuel (2000), who conclude that within industries, the methods used are fairly consistent. Although they find mainly applications of cost plus and resale minus methods in the manufacturing industry, these can actually be interpreted as TNMM, as the margins should be comparable to market rates. It corresponds directly to the findings by Plesner Rossing & Rohde (2010), where the company's transfer pricing system is based on TNMM. In other cases it is remarkable that negotiations are employed. Those are not prescribed as arm's length in the OECD guidelines (OECD, 2010) and consequently are not accepted by the Swedish tax authorities. This is not considered a problem by the companies and they are convinced of the integrity of their processes. Consequently the companies employ other methods, most notably the comparable uncontrolled price method to benchmark the prices they have set. Furthermore it can be said that the selection of the method for transfer pricing of intangible assets does not create huge debates within the company.

As has been observed by Borkowski (1990), the choice of different methods is mostly determined by different organizational and environmental factors that constitute the operations. The selected methods are considered optimal in a given situation. While a lot of papers discuss the advantages and disadvantages of certain approaches, (see e.g. Halperin & Srinidhi, 1996 Eccles, 1985), in practice the OECD guidelines provide a reference and combined with the specific requirements of the company. Standard market rates are used to benchmark the results of transfer pricing. Companies furthermore do not stick to one method but employ a variety of them to arrive at a range of transfer prices. The choice between the five different methods allowed by OECD increases the flexibility in the companies' transfer pricing.

Furthermore, it is acknowledged by the companies and the tax authorities that the arm's length principle does not always lead to one correct price but rather suggests a certain range. This is especially true for intangible assets where it is difficult in the first place to define a correct value. It is though surprising that only company E prescribes that this range from a transfer pricing perspective should be used in the operations. The Tax Controller stresses: "*We can provide good evidence on our transfer pricing studies. The benchmark range is supported by focused analysis*."

4.4. Single or Double Book Accounting

The structure between the different companies with regards to the usage of single or double book accounting differs significantly in this case study. This can be linked to the variations in their transfer pricing systems and thus their operations. The decision for the use of single or double books or a variation of it is mainly a question of whether or how transfer pricing should influence performance measurement and the bonuses of managers. Most companies use a mix between one or two books; however, company A uses a pure single book accounting system and company D a pure double book system. The avoidance of arbitrary impacts on performance measurement is important for the companies. This relates to internal management goals in transfer pricing as described by Cravens (1997).

In order to analyze the usage of one or two book accounting we have classified our findings in accordance with the different categories specified by Borkowski's (2001) study of transfer pricing usage for intangibles. In one of the survey questions Borkowski divides the practices used by companies into four different categories:

1. Using two sets of books; one for tax, finance, and local purposes, the other for management and control purposes.
2. Approximating in the host-country subsidiary, as closely as possible, those conditions that would be faced by an independent market entity.
3. Disregarding transfer pricing aberration effects when evaluating the performance of host-country subsidiary performance.
4. Taking account of any transfer pricing adjustments in the budget, so subsidiary managers are not evaluated on parent company usage of transfer prices to achieve certain goals, such as tax minimization.

Borkowski also included the alternative “none of the above” as a fifth category in the question. Given that our research is more qualitative than Borkowski’s, this alternative was disregarded and excluded in the comparative analysis of Borkowski’s results. In her study Borkowski (2001) does not give any detailed definition on what the different characteristics in each different group are. In order to be able to classify our case companies in a meaningful and cohesive way, a more detailed definition of each different group based on Borkowski’s initial categorization was developed in this study. This development was made in order to create a framework that allows for a more detailed analysis of the case companies than Borkowski’s initial definitions.

4.4.1. Using Two Sets of Books

This category is defined as where companies accounting for tax purposes have no impact on the accounting used for internal management purposes. The two books are completely separated. In this case the internal management systems do not have to take the arm length’s principle into account, if it is not beneficial for internal control purposes. This setup can be observed in company D.

D’s accounting system is a strict double book system where the transfer prices for tax purposes are not used for management control and performance measurement purposes. This separation between accounting for management control purposes and accounting for tax purposes enables the company to focus its tax related accounting solely on tax compliance on the legal entity level. Performance measurement is done on a business unit level where the legal entities do not play a role. The legal entities’ results are purely interesting from a tax perspective and not from an operational perspective where the focus instead lies on the business units and geographical regions. The Tax Lawyer at the company summarizes this with: *“Managers are measured in an operational dimension so that internal prices don’t matter. From that perspective we can handle transfer pricing without too much of a debate in the operational dimension. It is almost a purely tax and equity issue.”* Therefore the design of the transfer prices has no influence on the bonuses of managers, who should as a result focus on optimizing the group result and not the result of some subsidiaries.

Earlier, the company had used an accounting system which was more oriented on the one book system, where the same accounting figures to a larger extent were used both for tax compliance and internal management control purposes such as performance measurement. The company did, however, feel that it made much more sense business-wise to separate the two different goals through two different systems. The progress in IT technology led to the development of more advanced accounting systems. This has enabled company D to implement a two book accounting based system, which had not been possible before. The Controller from the company explained: *“We realized that it is the consolidated result that is important from an operational point of view. 20 years ago we didn’t have the tools to do a correct consolidated result. Now we use SAP. We have one global system that really can talk to each other and have a much higher quality in the consolidated numbers.”*

4.4.2. Approximating Conditions Faced by Independent Market Entity

In this category, companies focus on replicating the market conditions comparable to transactions for unrelated companies within internal transactions. The companies can motivate that their system is compliant with the arm length's principle on the basis that the internal transactions is done in the same way as external transactions. Those kinds of market transactions are present in companies A and C.

The transfer pricing system that company A uses in its transactions with the fully owned distributors corresponds closely to this category. The company stresses that all distributors are treated in exactly the same way, regardless if they are owned by the company or act as independent distributors. All transfer pricing related charges are included in the performance measurement done by the company. Tax related accounting is also used for management control purposes. The transfer price setting is based on negotiations between the different parties within the company that are part of the transaction. This negotiation is made independently from the headquarters' influence and the central transfer pricing function is not allowed to affect this negotiation in any way. Therefore the results of the negotiation are not influenced by taxation considerations.

The company is reluctant to make any changes to the initial transfer prices since that would risk undermining the logic of their transfer pricing system. Instead, the company tries to convince the tax authorities that their methods are in line with what the relevant regulations prescribe. It is important to note that according to the tax authorities negotiations-based transfer pricing setting within a group is not considered a "real" negotiation. The companies therefore have to prove that the set transfer prices are at arm's-length in some other way. If absolutely necessary, tax adjustments are therefore made by company A. Consequently, company A has had its current transfer pricing system in place for a long time and has had very little problem with the tax authorities in relation to their transfer pricing system.

Company C also uses a transfer pricing system based on one book. The transfer pricing charges are included in the performance measurement system. Company C does not have the same structure for both, fully owned and independent entities that can be used to benchmark internal with external transactions. Thus, the company does not fit as clear-cut within this category as company A. Due to its decentralized structure the entities within the group are quite independent in the setting of transfer prices through negotiations. The setting is similar to that of unrelated actors since the influence from the company group is rather limited but still significantly larger than in company A, as transactions can be mandated by the group. Given that transfer pricing within C is not as market based as within A, C also has to do significantly more adjustments to the initially set transfer prices than A in order to make sure that the transfer prices are tax compliant.

The performance measurement system is structured in such a way that the units are measured on profitability. An important distinction compared to company A is that company C does not have a centralized transfer pricing system and the same transfer pricing design across the divisions. These are decided by the divisions themselves. The transfer pricing can therefore, depending on the products and divisions involved, use different methods such as list prices or negotiations. The centralization process of intangibles within company C leads to the loss of control over valuable intangibles by the local companies. Therefore the profitability of a division is influenced which can create potential conflicts. The company takes those effects on the profitability into account regarding the performance evaluation and goal setting.

4.4.3. Disregarding Transfer Pricing Effects in Performance Evaluation

This category is defined as one book accounting that excludes all transfer pricing effects in the performance evaluation from the performance evaluation. In the sense of excluding the tax compliance transfer pricing effects from performance evaluation, it is quite similar to the two book category but the company only uses one set of numbers. On the other hand it is different in the sense that it is still based on a distinct one book accounting system. This logic is used by company B and company A's production units.

Transfer pricing is handled differently between the geographic and the product divisions in company B. Company B's transfer pricing system within the geographic divisions is based on a franchise fee that is paid by all its subsidiaries. The fee relates to their usages of intangible assets owned by the Swedish company. In order to make this fee politically accepted within the organization when it was established over ten years ago, it is excluded from all performance evaluation. All adjustments are made below the line of profit measurement. On the other hand, the geographical divisions are quite decentralized and own their own local IP. They are allowed to conduct and price their internal transfers independently without interference from the headquarters. The divisions are then measured on their EBIT-level with all transfer pricing included in the performance measurement except the central franchise charges. The product divisions work similarly in this area except that all tax related transfer pricing adjustments are excluded from the performance measurement. The geographical divisions' independence mostly makes tax related transfer pricing adjustments unnecessary since the transactions are at arm's length according to the company.

The production units of company A also fit within this category since the transfer prices themselves are excluded from the performance evaluation. The production units do not legally own the products they are using or the final products. They are only providing a service for which they get compensated. The reason that the transfer prices are excluded from the performance evaluation is that the transfer prices are made on a strict cost plus basis, which are unsuitable for performance evaluation purposes. Instead, the performance evaluation is based on more operationally indicators such as cost efficiency.

4.4.4. Taking Account of any Transfer Pricing Adjustments in the Budget

The definition of this category is that companies use their tax compliant management accounting to fulfill goals that they do not want to affect the performance evaluation of the subsidiaries. Rather than excluding all transfer pricing effects from the performance evaluation as in the previous category, they exclude only selected parts. These parts are related to goals for the group itself, for example group tax compliance, which is does not make sense to evaluate the subsidiaries on. Another option is to provide the operations with a range of tax compliance prices as they can determine their optimal prices. Companies E and F fall in under this category.

Company E has a mixture of one book and two book accounting. The initial transfer prices are set by the product managers within the division in order to serve their operational purpose. The level of transfer prices set this way is also used for performance measurement purposes within the company but is set within a tax compliant range. Sometimes the transfer prices set by the product managers might turn out not to be on a tax compliant level. In order to achieve tax compliance, the transfer prices are adjusted twice a year. The tax compliance related adjustments are, however, not taken into account for performance measurement purposes and made below the line. Performance measurement is based on results in the company's divisions and the legal entities themselves are not used in any way for performance measurement purposes.

Company F has a mixture of one and two book accounting. The accounting for management control purposes and tax purposes are based on the same accounting system. Selected parts of the transfer pricing system charges that are made for tax purposes are included in the performance measurement system while others are only applied for tax accounting purposes. Some numbers are nevertheless disregarded for internal management control and performance measurement purposes. Transfer pricing of intangibles such as trademarks is mostly excluded from performance measurement and management control for internal purposes.

4.4.5. Comparison between the Cases

When comparing the different cases it is interesting to see that the companies in this study have quite different ways of handling the conflicts between the operational and taxation goals of transfer pricing. The most common way is to use some sort of hybrid between one and two book accounting. Where the numbers used for tax purposes are based on the ones used for internal management purposes. Adjustments are made below the line used for performance measurement in order to make the transfer pricing system tax compliant. There were, however, important exceptions. Company C and especially company A had more purely one book accounting system with a close connection between the tax compliant numbers and the ones used for internal management. Company D, on the other hand, had a pure two book system where the numbers for internal management purpose and for tax compliant reasons where totally disconnected from each other. The reasons for choosing those different setups appear to be determined to a large degree by the structure of the operations.

Keep two sets of books, one for tax and another for management	**Approximate conditions faced by independent market entity**	**Disregard transfer pricing effects in performance evaluation**	**Include transfer pricing adjustments in the budget**
Company D	Company A (Distributors) Company C	Company B (Geographic Divisions) Company A (Production)	Company E Company F Company B (Product Divisions)
In Borkowski's Study 42%	**In Borkowski's Study** 20%	**In Borkowski's Study** 21%	**In Borkowski's Study** 17%

Table 2 - Overview over the companies' usage of single or double book accounting

4.4.6. Comparison to Literature

In the study by Borkowski (2001) the most commonly used transfer pricing practice by far was the usage of two separate sets of books. The findings of this study differ from her findings. This can to some extent be based on the fact that she did not define the categories further than the headlines for the categories, something that might have led to unreliable result. This is a risk since her results were based on the companies' answer in a survey, while our results are based on extensive interviews with companies from which we then categorized the companies. Including transfer pricing adjustments in the budget was the least used method in Borkowski's study, while it was the most common in this paper. The result within her study varied between the different countries examined. Our findings are somewhat closer to those of Canada, Germany and Japan in her study.

The sample size Borkowski based her study on was, however, only large enough for the US to draw any reliable conclusions (113 companies of 159 total companies in the study were from the US). However, there is a clear difference between how the Swedish companies in our study handled transfer pricing and their US counterparts in Borkowski's study. If the difference is related to different industries, country differences or the time that has passed since her study is hard to tell. Based on the result from the other countries in her study, differences between countries appear to play some role, while she did not find significant differences between industries.

When analyzing the findings with the help of the relevant literature some interesting observations can be made. Cools et el. (2008) found in their study that introducing tax compliance in a single book accounting systems leads to large operational changes within an organization. This is a finding that is shared by Plesner Rossing & Rohde (2010). According to our findings, the companies, irrespectively of having a two or one book accounting system, are very careful in not letting the tax compliance issue affect their operations; either by basing the tax compliance systems on operational requirements or by separating the two books to different degrees. Both options lead to the same desired results. The companies in this study are aware of the difficulties that arise with the introduction of a tax compliance one book transfer pricing system as described by Cools et al. (2008) and Plesner Rossing & Rohde (2010). They want to mitigate those effects with their current systems.

Overall our findings in relation to the single book or double book accounting are similar to the argumentation of Durst (2002). He states that companies need to separate the accounting for tax purposes and internal management control purposes. Durst, however, focuses his critique on some points that were not emphasized by the companies in our study. The issue of double marginalization and the resulting negative effect that a single book can have on a company's business were not mentioned in the interviews but emphasized by Durst (2002). The companies in our study did not appear to be too concerned about these points.

The by far most important reason most companies mentioned was that a one book accounting approach could not work for them was as they would face resistance in the organization. The main factor behind this resistance, as named by the companies, was that single book accounting would lead to tax compliance adjustments having an effect on performance measurement and in extension on employees' bonuses. Several consultants also highlighted that it is very hard to start letting incentive schemes be affected by transfer pricing without facing heavy internal resistance. Especially the centralization of intangible assets within the organization can become a political issue. This can be supported by the fact that the only company which has a pure one book accounting system, company A, focuses on internal growth rather than growth through acquisitions. Given that this company is already very centralized and conducts very few acquisitions, the need for centralization is very limited. It therefore does not have to face this problem that seems to keep most companies in our study from one book accounting.

One reason behind the difference between our findings and the findings made by Durst (2002) is the time of ten years that has passed. Since Durst's (2002) study, a rapid development has taken place in the IT systems for companies. This was mentioned by the interview partners as an important influence in the ability for companies to tailor their accounting systems to their needs and goals. Therefore previous problems with double marginalization might perhaps not be as large as before and other problems have taken higher places on the companies' priority lists.

The sophistication of the IT system of a company is an important contingency in the decision for one or two book accounting. The overall goals of the company in avoiding adjustments influences on the performance measurement can be seen as an important restriction on the design of the use of one or two books. There are several alternative designs that comply with this objective. As contingency theory predicts, the companies adjust this process to their needs, especially with regard to their transfer pricing system and their operations. Consequently, the choices of the companies differ substantially. The observations are also in line with behavioral theory. Companies focus on creating a workable system that satisfies the goal of not influencing performance measurement with tax adjustments.

4.5. The Structure of Intangibles

When considering the structure of intangibles, first the types of intangibles of a company have to be identified. The OECD guidelines (OECD, 2010) differentiate between commercial and marketing intangibles. While commercial intangibles include patents and know-how, marketing intangibles relate to trademarks and customer relationships. In practice, they are more commonly categorized into "soft" and "hard" intangibles. Hard intangibles are those that can be readily identified and protected such as trademarks and patents, also called intellectual property, while soft intangibles are less visible within the company and relate to know-how or customer relationships. In the interviews, this distinction was clearly visible. The interviewees mainly talked about the hard intangibles whereas the soft ones were only relevant in selected transactions. They constituted the bigger challenge regarding their identification and valuation (Lev & Zarowin, 1999). Interestingly, the possibility for a categorization of intangibles is acknowledged but denied in the new OECD discussion draft on intangibles (OECD, 2012).

According to our study, there are four important situations to investigate when considering a company's intangibles: *Firstly*, when intangible assets are created or acquired; *secondly*, when they are marketed within the company; *thirdly* when they are transferred in the course of company restructurings and *lastly*, the resulting ownership structure. The structure of the intangibles cannot be separated from the overall company structure and the operations, the management philosophy and the tax strategy of the company (Abdallah & Murtuza, 2006). This is in accordance with the fact that the transfer pricing for intangibles cannot be separated from the overall transfer pricing system.

4.5.1. Creation of Intangibles

In the creation of intangibles, most companies talk about R&D activities. Few actually control for more unconventional intangible assets, as it has been described by Johanson et al. (2001). The creation of marketing or soft intangibles is not as coherently managed as R&D and patents. Thus technology and patents are mostly in the focus when it comes to the internal creation of intangibles in manufacturing companies. Another way to become the owner of intangible assets is to acquire companies that own intangible assets. Especially in companies B and F, acquisitions are part of the strategy for growth, while companies C, D and E conduct them more selectively and A rarely. Due to the strategies of many of the case companies, the question of restructuring of acquired companies has a priority.

R&D activities are located and managed in three different ways by the companies. In companies D and F ***contract R&D*** plays a dominating role. Contract R&D is also important in company C, but C also has significant R&D made on a decentralized level which makes it hard to place the company solely within one category. In contract R&D, the research company is only compensated on a cost plus basis. The risk and the management functions for the development are located at the principal. Consequently the technology and patents that are created are owned by the entrepreneur or principal that finances the R&D activities. As a result, the R&D centers can be located at different locations.

Another option is that the ***R&D activities are centralized*** at the entrepreneur's and thus the headquarters' site. This setup is applied by companies A and B. Company B is in this case slightly different, as only more sophisticated technologies are developed at the headquarter, while other developments might still take place in the subsidiaries.

Furthermore, it is also possible to have ***R&D located at different locations*** in the companies in a decentralized structure, which do not act as contract R&D companies. This approach is mostly applied by company E, where the business units take the decisions on where to place and locate those activities. C also has a similar structure for some of its R&D even though they in contrast to company E also engage significantly in contract R&D.

4.5.2. Licensing of Intangibles

The next step is the licensing and marketing of the intangible assets in the regular business process where several approaches are possible. Intangible assets can be licensed separately, together as a package or bundled with physical products.

In the ***individual intangible approach*** of charging for intangible assets, it has to be noted that the charges mostly relate to the hard intangibles of either patents or trademarks. This approach is taken by companies C and E, which do charge separately for different patents between the different divisions and business units depending on the usage. The divisions and owners of the intangibles manage those transfers. A difference between the two companies can be observed when it comes to the licensing of the trademarks. While in C the group trademark is owned at the headquarters and charged to the subsidiaries, this is not done in E and the group brand can there be used free of charge within the organization. In E a strong brands that are acquired are licensed to the subsidiaries. This difference is explained by the historical development, as the licensing of the group's main brand hasn't been associated with a fee historically. The Tax Controller in company E emphasizes: "*As this has not been charged in the past, introducing a new charge such as brand royalty is quite difficult and could lead to potential issues. A brand royalty would entail all subsidiaries to pay a royalty fee which would be tax deductible in those countries. We could end up significant issues on deductibility of these costs in all countries by the tax authorities. Also, to benchmark an arm's length price would be quite difficult as we have a very diverse industry portfolio. Additionally, brand management is not handled centrally, which makes the functional analysis complex*." A special case is company B, where intangibles that belong to the headquarters are not charged separately, but intangibles that are owned by subsidiaries are invoiced to other entities that use them. This is mostly related to technology intangibles and the remuneration is based on negotiations between the subsidiaries and thus considered arm's length. Separate and detailed charges can be compared to the introduction of a new and more detailed cost allocation system as observed by Plesner Rossing & Rohde (2010), where costs were clearly separated and allocated.

The approach used by B is to license its ***intangibles as a group***. All intangibles and headquarter charges are bundled together and invoiced to the subsidiaries as a so called franchise fee. The subsidiaries gain access to a package of centrally developed proprietary intangibles related to, among other things, operational process methodologies, brands, know how, new advanced technologies, operational tools, sourcing assets, IT strategy and infrastructure, and related services for the implementation of the intangibles, and in addition some more traditional corporate management functions. As the franchise fee is charged below the operational EBIT line, the use of the intangibles are "operationally at no cost" for the franchise companies and the subsidiaries are thus incentivized to use as many intangibles as possible instead of spending own resources to develop similar intangibles. Thus the company can realize the synergies. The company sometimes has problems with the tax authorities with the use of this setup as described by the company's Director Transfer Pricing: *"Tax authorities around the world don't really like the franchise fee as it is quite a simplification; they do not quite understand that intellectual property can be licensed out as business intangible packages and cannot reasonably be measured on an individual level and is thus not detailed enough for some of them."*

The last possibility is to ***include the intangibles in the product price***. This approach can be associated with the principal structure, where subsidiaries are entitled to a certain profit margin, but also to market driven structures. It would just add complexity to differentiate between the charges for products and intangibles. It is used by companies D and A. To some extent this is also the case for company F in the regions where the principal structure is used.

The approach applied by A is described by their Tax Specialist as follows: *"The number of transactions should be limited to the extent possible. Everything, brands, know how, technology, etc. is included in the product price."* The argument is made that it is impossible to separate the value of the products clearly from the value of the brands. The difference between company D and A is that while in company D the transfer prices and thus the intangibles do not affect the transfer prices, this is the case in the products transferred to the distribution companies in company A.

4.5.3. Transfer of Intangibles

The most challenging part of the management of intangible assets in a company is when it comes to business restructurings and therefore to the transfer of intangible assets in the company. Regulations in chapter IX of the OECD guidelines (OECD, 2010) draw up detailed requirements due to the fact that the transfer of intangible assets offers a large potential for misuse (Dawson & Miller, 2009). The most common direction of these restructurings is centralization. The VP Transfer Pricing at company C names efficiency as an important reason behind the centralization of intangibles: *"The business is getting more global, which also influences the management of intangibles. You have to act more global. Thus, it is better to have centralized IP to gain more flexibility regarding the use of technology in various locations in the world."* Centralization might not only take place at the group level but also on the divisional or business unit level. The structure of the intangible assets is heavily dependent on the policies used. The basic differences are thus a dispersed ownership of intangible assets or centralization. Further differentiation can be made between a policy that strives for immediate centralization and one that is more based on pragmatic business decisions.

While there are differences between the amount of centralization and the speed, it has to be noted that all companies consider a centralized ownership and management of intangible assets as desirable. The VP Transfer Pricing at company C described the reason for this as follows: *"Centralization of intangibles is mainly a business decision. Centralized IP has important business benefits, beside its potential tax benefits*". Various obstacles and reasons nevertheless prevent full scale centralization. The most obvious one is that centralization is cumbersome and costly as it requires acceptance by the tax authorities, who might nonetheless charge exit taxation. In the companies, the centralization is always aimed at centralizing to the (divisional) headquarters to facilitate the management and administration of the intangibles rather than centralizing to a tax haven. This is in line with the objectives of all the companies for tax compliance. While avoiding centralization or even tendencies for decentralization might also be present in some companies, it has not been observed in this study and is thus not considered.

In companies A and D the ***centralization is immediate*** or as fast as possible. R&D that is developed and intangibles that are acquired (although this is rarely the case in A) are transferred immediately to the headquarters. The resulting structure is thus an almost complete ownership of intangible assets at the headquarters in Sweden. The advantages for this are operational because it allows for an easier management and a simpler structure for tax management. Furthermore, it enables the continuous concentration of functions, assets and risks at the headquarters, which is a requirement of the principal structure.

Another configuration can be identified in companies, where the ***overall policy is a gradual centralization***, which is not as stringent. This is the case in companies F and B, while in B only with regard to the product divisions. The process in B is described by their Director Transfer Pricing: *"Centralization is done in cycles. Through the acquisitions we gain more IP which may require another round of centralization."* Centralization occurs when it is considered beneficial for the business, which is not always the case, for example right after acquisitions. Centralization might turn out to be too costly or difficult in the short run, due to operational constraints or requirements by tax authorities. The resulting structure of the intangibles assets is thus that the headquarters own the majority, but on the other hand technology or brands can also be found in local markets and subsidiaries. In company F a full standardization is not achieved due to strategic and historical reasons but F is constantly monitoring efficient ways to structure its intangibles ownership.

The last possibility is the fact that ***centralization of intangibles happens occasionally*** or just on a limited number of intangible assets. This is the case in companies C and E, while in company B this is true for the geographic divisions. Here, newly developed and crucial intangibles are centralized. Those are the ones that have an added value for most of the subsidiaries of the group. Local subsidiaries can retain intangibles that are mostly relevant for them such as local brands or specialized technologies. When acquiring companies in the geographic divisions, there is generally no transfer of intangibles, although the group intangibles are made available to the acquired company through a franchise agreement. Company E follows a very business driven approach. This is stressed by the Tax Controller in company E: "*Business reasons are dominant when moving assets. The decision making is operationally driven."* In E centralization translates into centralization at the division level and not on the group level. The decision for centralization is taken by the divisions as there are significant operational changes which influence this decision. This relates mostly to technology. E also owns numerous brands that are only relevant in local markets and are therefore left in the local subsidiaries. Company C has a more flexible centralization process where centralization is not only conducted towards the divisional level but also toward the group level.

4.5.4. Ownership of Intangibles

Closely related to the creation, licensing and especially the transfer of intangibles is the ownership structure of the intangibles. An important goal for the other three parts is to facilitate the ownership structure of intangibles that have been chosen by the company. The ownership structure could in turn serve many goals of the organization such as operational goals or tax related goals as described by Cravens (1997). The companies in our study based their ownership of intangibles mostly on directly operational goals rather than tax related goals. Three different ownership structures of intangibles have been identified in this study: completely centralized, centralized at divisional level and partly centralized.

Completely centralized is defined as having all intangibles within the group centralized at the parent company. This structure is applied by companies A and D and is very closely connected to the overall centralized company structure these companies have.

Centralized at divisional level is similar to the completely centralized approach but the centralization takes place on the divisional level rather than for the overall company. This structure is used by company B for their product divisions as well as by company F and corresponds with their less centralized company structure compared to company A and D.

Lastly company C, E as well as company B's geographic divisions use a **partly centralized** ownership structure, where only some intangibles are centralized within the group and many are owned on a local level. This corresponds to the fact that these companies are the most decentralized companies within our study. The Director Transfer Pricing in company B described their reasoning behind not having a complete centralized structure for intangibles: *"We have over 470, out of which more than 200 operational, subsidiaries; therefore a complete centralization of intellectual property would be too cumbersome"*.

4.5.5. Comparison between the Companies

Creation	<u>*Contract R&D*</u> Company C Company D Company F	<u>*Centralized R&D*</u> Company A Company B (geographic divisions)	<u>*Decentralized R&D*</u> Company E Company B (product divisions) Company C
Licensing	<u>*Individual intangibles*</u> Company C Company E Company B (subsidiary IP)	<u>*Group of intangibles*</u> Company B (Headquarter IP)	<u>*Included in the product price*</u> Company A Company D Company F
Transfer	<u>*Immediate centralization*</u> Company A Company D	<u>*Gradual centralization*</u> Company B (product divisions) Company C Company F	<u>*Occasional centralization*</u> Company B (geographic divisions) Company E Company C
Ownership	<u>*Completely centralized*</u> Company A Company D	<u>*Centralized at divisional level*</u> Company B (product divisions) Company F	<u>*Partly centralized*</u> Company B (geographic divisions) Company C Company E

Table 3 - Overview over the companies' strategy for intangibles

The comparison of the analyzed companies shows that while the overall objective of centralization can be found in all of them, there are different specifications for all of them. None of the companies' intangible structures are identical. The specific systems are highly dependent on the operations. There is no generalizable best practice approach, but all companies adapt the type structure and management of intangibles that best fits their needs and requirements. This is exactly what contingency theory would predict. The needs are always operational and not related to any considerations for the optimization of tax structures. Furthermore, the process of centralization is difficult not only due to increased attention by the tax authorities but also due to internal management and operational concerns. Furthermore the interests of many different actors within the organization have to be taken into account in line with behavioral theory. When comparing with tangible assets it has to be highlighted that the movement of intangibles is easier.

4.6. Tax Compliance Approach

The companies named tax compliance as the second most important goal behind supporting the operations. Therefore it is interesting to get into more detail on what different approaches the companies take in order to handle this issue. Two distinct tactics could be identified from analyzing the companies: a proactive focus and a reactive focus. The proactive focus can be found in companies that put their focus on proactively defending the methods on which they base their transfer pricing. They make sure that their pricing system is tax compliant from the methodological perspective. This focus can be defined through company A's Tax Specialist's explanation of their approach: *"The group aims to verify, explain and justify the actual outcome rather than to correct it as we are confident in our methodology and our processes."* Changes in the regulation do not affect the transfer prices in any significant way with this focus. The reactive focus is more based on making changes to the initially set transfer prices based on what level of transfer prices that are accepted by the regulation. Changes in regulation can with this approach have big effects in the level of the transfer prices that are set. Plesner Rossing & Rohde (2010) as well as Cools et al. (2008) have studied tax compliance where it has been taken as a background in the study, but different approaches to achieve tax compliance have not been previously research. Therefore no direct comparisons can be made with previous studies in this area, tax compliance can however be seen as part of tax risk management and a way to control tax risk as described in the article by Wunder (2009). This is especially true in the reactive approach since that approach is based on adjustments.

4.6.1. Proactive Approach

Company A's system with negotiation-based transfer prices between the involved parties is essential for the company as it is linked to incentives and performance measurement. The system is based on the reasoning that the transfer prices negotiations are at arm's length. This would not be the case anymore of the company started to do adjustments on a regular basis. Since all charges are included in the internal performance measurement, this could also lead to internal political problems. Employees would start to get evaluated on values not set by themselves in negotiations. Instead the prices would be defined by tax authorities on whom they have no influence. It is important to note that according to the tax authority, negotiation-based transfer prices within a group is not considered a real negotiation. The companies therefore have to prove that the set transfer prices are at arm's length in some other way.

A similar reasoning can be found in company B. The franchise fee in company B is an almost equally important component in its transfer pricing system. It is used to charge out central cost, services and intangibles to its subsidiaries. If the company would have to do regular adjustments to its charges, they would have to redo their whole system since it is very standardized. Changes for some subsidiaries could induce other tax authorities to demand changes on their end as well. Since these charges are decided centrally and are not part of the internal performance measurement, the system is somewhat less sensitive to changes than the one implemented in company A. Furthermore, transactions between independent subsidiaries are based on negotiations and considered to be at arm's length due to the market-replicating process. Adjustments are not desired as they would distort the subsidiaries profits and curb their independence. Thus, company B's focus is mostly on defending the methods used.

4.6.2. Reactive Approach

In the other companies, a more reactive approach can be observed. Company C's entities are relatively free to decide on the transfer price that is optimal for them. At the same time it is highly important to comply with all tax regulations. One thing that stands out in C compared to the other companies is that they do not have any overarching transfer pricing system for the whole company. The divisions are free to come up with different solutions that best serve their needs given that the solutions they uses are compliant with all relevant regulation. Therefore the price might be determined through many different techniques such as a regular price lists or negotiations. The negotiations within the group is not as free from influence from the headquarters as in the case of company A and the resulting prices are always checked for their fulfillment of the arm's length principle through documentation. The company tries to change incompliant transfer prices continuously throughout the year in order to be as tax compliant as possible. The company in general is quite open to do changes to its transfer prices if required by the tax authorities.

Company D stands out in our study in that they have a very centralized transfer pricing setting where all transfer prices for tax purposes are set at the parent company. This is enabled by the usage of two separate books within the company. The transfer prices are therefore considered purely a tax issue. The transfer prices should be compliant to the regulations of the countries D is active in and reduce the risk of tax audits. In order to achieve tax compliance, transfer pricing adjustments have to be made throughout the year. Documentation for transfer pricing is updated every second year by the company to fulfill the requirements of the tax authorities. The whole structure of the transfer pricing system is more important than compliance at all cost. Consequently D will try to defend itself from unreasonable demands of the authorities. As long as the requirements to change transfer prices from the tax authorities are reasonable, the company will change them in accordance with the requirements, which can be described as a reactive approach.

Company E has harmonized its global transfer pricing policies and internal regulations for the whole group. The central transfer pricing function at the global headquarter gives guidelines and ranges of acceptable transfer prices, which the divisions have to follow. The exact level of transfer prices is set by the product managers within the company's divisions to serve their operational needs. The used levels are monitored by the tax department. The transfer prices set by the business units are adjusted twice a year in order to uphold tax-compliant transfer prices. These adjustments are made below the line which is used for performance measurement. The adjustments have therefore no effect on the measured internal performance for the business units. The company adjusts its transfer prices if required by the regulators even though fewer adjustments are desired.

In company F the transfer prices are set by the tax department at the global headquarter. Since Company F, in contrast to Company D, is not using separate books for management and tax purposes the level of transfer prices are of importance for the operations themselves. The tax Department in F therefore consults the company’s divisions and takes their opinions into account and not only focuses on tax considerations as in company D. The group’s transfer pricing system is mostly but not fully standardized throughout the world and may vary for strategic or historical reasons. Tax compliance is of great importance for the company and in order to make sure that the end result is in line with the targeted and acceptable transfer pricing framework the company makes adjustments. They take place mostly at each quarter but in some instances only yearly.

4.6.3. Comparison between the Approaches

In general not much previous research has been done about how companies handle tax compliance. Instead the focus has in general been more on different aspect of the goals of transfer pricing or what methods of transfer pricing the companies are using. The study by Brauner (2008) concludes from a theoretical perspective that tax compliance to the transfer pricing rules of intangibles is burdensome. Our findings in this area cannot be related and compared to any previous studies to any major extent. However, several interesting findings within this area of our study can be discussed even though the connection to previous research for the reason stated above is lacking. Therefore the framework of the proactive and reactive approach for tax compliance was developed.

Company A and B have both linked their operations to their transfer pricing system. They perceive this as essential and are very reluctant to make adjustments to the outcome of the system. Operational considerations are given priority over the objective of tax compliance. Therefore they apply a proactive focus where they focus on trying to explain the system and its logic to the tax authorities. It has to be highlighted that the proactive approach is not used to defend structures that are aimed at optimizing tax charges but to support the operations.

Company C, D, E and F are not so concerned about having to adjust the transfer prices they initially set, even though they try to limit them. None of them has operations for which are dependent on how the transfer prices are set. They are instead more focused on the transfer pricing causing as little problems for the operations as possible. Therefore they are prepared to do the changes required in order to make the transfer prices tax-compliant. The companies used in the studies by Cools et al. (2008) and Plessner & Rossing (2010) could be classified as having reactive approaches. Based on literature and our study it seems that the reactive approach is more commonly used by companies than the proactive approach. The small sample sizes in these studies do make a generalization difficult, but the results can be taken as an indication. It is important to note that all companies in the study from time to time do tax compliance adjustments, since even companies with a proactive focus can be forced by the tax authorities to correct errors in the setting of transfer prices.

Companies seem to generally take a reactive approach if the implication of using that method does not lead to any negative effects for the operations itself. This is the major contingency within this area. Companies C, D, E and F do not have a business model that is dependent on that the transfer pricing is set in a specific way as opposed to A and B. Therefore if the company is structured in such a way that the transfer pricing setting is an integrated part in the company's business model, they will most likely use a proactive approach. Changes in the transfer prices in such cases can have implications for the whole business. It is easier and most likely less costly to achieve tax compliance by closely following the tax authorizes guidelines than arguing with the tax authority about the methods used. This can explain the preference of the reactive approach over the proactive approach, if it does not impair the operations. Operations are always most important for the companies and if they require a proactive approach then the companies will opt for this method. That companies prioritize the business needs of the operations is also in line with our findings throughout this study. Companies that employ the reactive approach are aware that in line with behavioral theory, it is difficult to integrate all interests of the relevant actors within the organization. They retain more flexibility by allowing for ex post adjustments.

4.7. Tax Optimization

4.7.1. Taxation Literature

As has been stated, tax optimization is not a priority for the companies in this study. In the interviews the company representatives highlighted the fact that they are not tax aggressive, which is confirmed by looking at the effective tax rates. This is in contrast to findings in the literature of transfer pricing and profit shifting. The findings of Huizinga & Laeven (2008) clearly show that profit shifting is prevalent in Europe among multinational companies. Nevertheless, profit shifting is usually linked with operational activities as shown by Bartelsman & Beetsma (2003). Although tax optimization might not be the primary goal of the companies when taking operational decision, it is certainly taken into account. If it does not obstruct the operational goal, the companies opt for more tax efficient setups. One should therefore not confuse the lower priority assigned to tax optimization with ignorance of the importance and effects of taxation. Even though the company representatives argued that their tax strategy is relatively unaggressive, some of them agreed with the consultants that intangible assets offer hypothetically more possibility for successful aggressive tax optimization compared to tangible assets. This is in line with the findings made by Dawson & Miller (2009).

4.7.2. Tax Authorities

On the other hand, it is observed by the companies that the tax authorities are becoming more aggressive. The tax base is defended more forcefully, which is linked to the financial crisis and the need for states to increase their revenues. Focusing on transfer pricing is seen as an effective way to increase the tax base without increasing tax rates. At the same time, the continuous improvement of guidelines and regulations, which has been going on for decades (Picciotto, 1992), contributes to the increased focus of the tax authorities. This development is seen worldwide and in Sweden the tax authorities have significantly increased their personnel in this area. This is highlighted by the Tax Auditor of the Swedish Tax Agency: *"Before 2008* *transfer pricing was not a focus area. Before, there were only a limited number of transfer pricing audits done. During the period 2008-2010, the Swedish Tax Agency has run a national project, learning and developing the control procedures for transfer pricing audits etc. These activities have continued thereafter. As a result we do have an increased focus on transfer pricing also in Sweden. However, our objective is the proper tax in the proper country and we do not just aim to increase the revenues."*

The tax authority also acknowledge that competition among tax authorities can lead to double taxation of companies, something that is harmful for the companies affected, which is in line with the findings of Mansori & Weichenreider (2001). This risk is something that the Swedish Tax Agency actively tries to combat, as described by their Tax Auditor: *"The goal of the Swedish Tax Agency is a proper tax base allocation between different countries. The right tax should be paid in the right country. Not only double taxation should be avoided but also double non-taxation prevented. The companies should pay the proper tax"*. The correct application of the transfer pricing guidelines and regulations is the central goal. Adjustments by the tax authorities have to be fully accepted by either the companies or through a court ruling so that negotiations and compromises are not possible. As a result the Swedish tax authorities are seen as less aggressive and more pragmatic by the companies and consultants. Thus, it seems like a more conservative and pragmatic approach is favored by both tax authorities and companies. The danger is that with an increased focus, transfer pricing disputes are becoming more numerous and lead to increasing compliance cost on both sides without significantly changing the taxes paid.

4.7.3. Ethics

Ethical considerations are named in the literature as increasingly relevant with regards to transfer pricing (Sikka & Willmott, 2010). Some articles argue that companies do not only have a legal obligation to pay taxes but also a moral one to support the societies they are operating in. Excessive tax optimization and profit shifting is thus considered unethical. Not surprisingly, none of the studied companies considers itself as behaving in any way irresponsibly for the society and many also indicated that the public opinion is important for them. One example of that was the Director Transfer Pricing in company B who stated that: *"The public opinion also plays a role in transfer pricing. We don't want to be the bad guys."* In fact, since the companies are considering themselves to not be especially tax aggressive, they feel that they are responsible actors, which give significant benefits to the society as a whole. The effective tax rate of all the companies shows that the taxes paid are approximate equal to the statutory Swedish tax rate. Thus the allegation of profit shifting might not be justified for these companies. In contrast, the case of Sandvik AB, which has been described in the introduction, shows that some Swedish companies are eager to optimize their taxes. Operational concerns might serve as justification for these actions.

Even though the companies are not seeing themselves as especially tax aggressive, most of them generally do not see anything ethically wrong with tax optimization if it is based on operational reasons and within the boundaries of the regulation. It was noticeable that the enthusiasm for more elaborate tax saving schemes was greater in the consultancy companies. The most pressing ethical concern of the companies was not to damage their public image through bad press. Another important factor is that regulations are becoming more stringent. As a result unethical behavior is becoming illegal and moral questions are replaced by legal considerations. Thus a tax compliant company is generally also behaving more ethically, although profit shifting to low tax jurisdictions is still possible. Overall the companies exhibit more of a shareholder value perspective when it comes to transfer pricing, aiming at maximizing the profit through efficient operations. Society as a whole is not in the focus of the considerations.

The companies in our study shared the experience described by Mehafdi (2000) who observes that not only companies engage in morally questionable behavior but also some tax authorities. The companies in our study, as well as Swedish companies in general, according to the consultants as well as the tax authority, do not engage in especially tax aggressive behavior. However, there have been complaints about the authorities in other countries.

4.8. Discussion

4.8.1. Goals and Transfer Pricing Structure

A remarkable observation when comparing the different parts of the analysis is that while the goals are similar between the different companies, the transfer pricing systems are not. The operations are the key factor in all companies and have a tremendous influence on the whole transfer pricing structure. The goals are important and are reached in the companies, but the ways employed to achieve the second most important goal of tax compliance are diverse. No organizational structure is preferred by the tax authorities, as long as the arm's length principle is satisfied. The companies in this study exhibit different ways of achieving tax compliance. It is not possible to make a normative statement about the choice of a transfer pricing system and the methods employed. As a result, simply looking at the goals is not sufficient to determine the optimal transfer pricing policy of a company. One has to take a look at the operations as a major contingency to find the most suitable structure for the company.

4.8.2. The Principal Structure determines the Transfer Pricing System

The principal structure is seen as a benchmark structure by many consultants and companies. When implemented in a company, in this study company D, it determines the structure of intangible assets to a large extent. The creation of R&D should take place through contract R&D. When acquisitions are made, the centralization of intangible assets should take place immediately to preserve the logic of the principal structure. Newly acquired companies are integrated into the company. Furthermore the principal structure and the usage of double book accounting are correlated. Due to the fact that the subsidiaries are remunerated with a defined margin, other ways for performance measurement have to be used. As done in company D, a complete separation between the two books is desirable.

4.8.3. Restructurings and Performance Measurement

Based on our findings, there seems to be a connection between the companies' choice of accounting and the speed with which the companies can do a major restructuring of their operations. Restructurings such as centralization of intangibles are harder for companies with a single book accounting system than for companies with double book accounting. The centralization has an effect on performance measurement in the case of one book accounting, but no effect with two books.

Changing a transfer pricing structure that affects performance was mentioned to be problematic also by the Tax Director in company F: *"It is not always easy to change a transfer pricing system, as it might have effects on management incentives or bonus schemes. It is not done by just signing a paper."* Theoretically, there might be a possibility to make sure that the performance measurement is not affected by the restructuring within the company by changing the levels within the performance measurement. Given that it would be almost impossible in practice to determine new profit levels that correspond perfectly to the old ones, it is not really an option for the companies. Therefore, if the company uses more of a one book accounting system, more considerations have to be taken in order to make sure that the operations are not affected in a negative way by the restructurings. Due to these obstacles, restructurings for companies with a single book based system take much more time than for companies with double book based systems. The higher the company's need for fast restructuring capabilities, the more the company should base its accounting system on a two book system, all else being equal. Restructurings that affect the performance measurement would include changes in the decision making process to have a lasting impact as described by Ainsworth & Shact (2011).

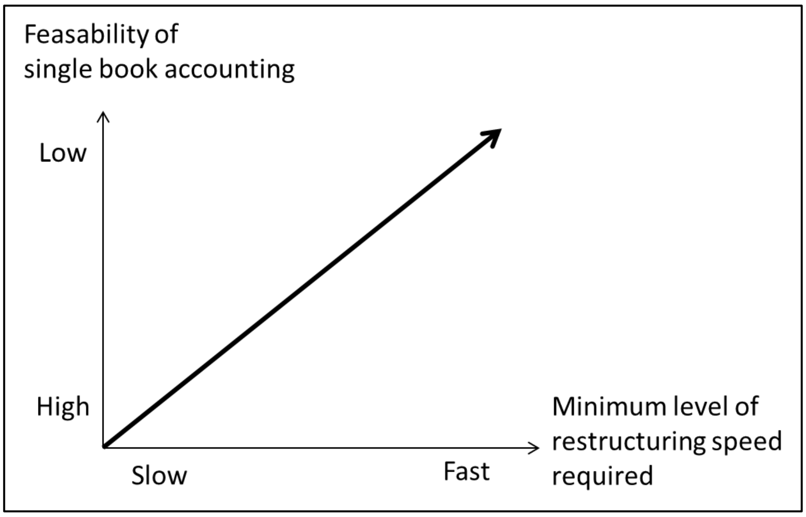

Figure 3 - Illustration of the relationship between restructuring speed and feasibility of single book accounting

4.8.4. Centralization of Intangible Assets

Cools et al. (2008) also observed that an adoption of a single tax compliant transfer pricing system led to an increase in centralization. Increased centralization, especially of intangible assets, was also something we found as a general long-term development in all the companies. The companies in general stated that the most important reason behind the centralization was operationally driven. The increased centralization enabled the companies to ensure that their resources were used to the best extent throughout the world. The most important tax related reason stated was that the increased regulatory requirements require the company to centralize its operations to make use of its regulatory expertise at the global headquarters. Cools et al.'s

(2008) reasoned that tax compliant single book accounting led to more detailed and stringent internal policies. These forced the company to centralize more in order to cope with this increase in requirements. The same development was observed by Plesner Rossing & Rohde (2010). Thus one can hypothesize that an increase in regulatory requirements leads to more centralization, which is in line with the findings in this study.

4.8.5. Proposed Theoretical Model

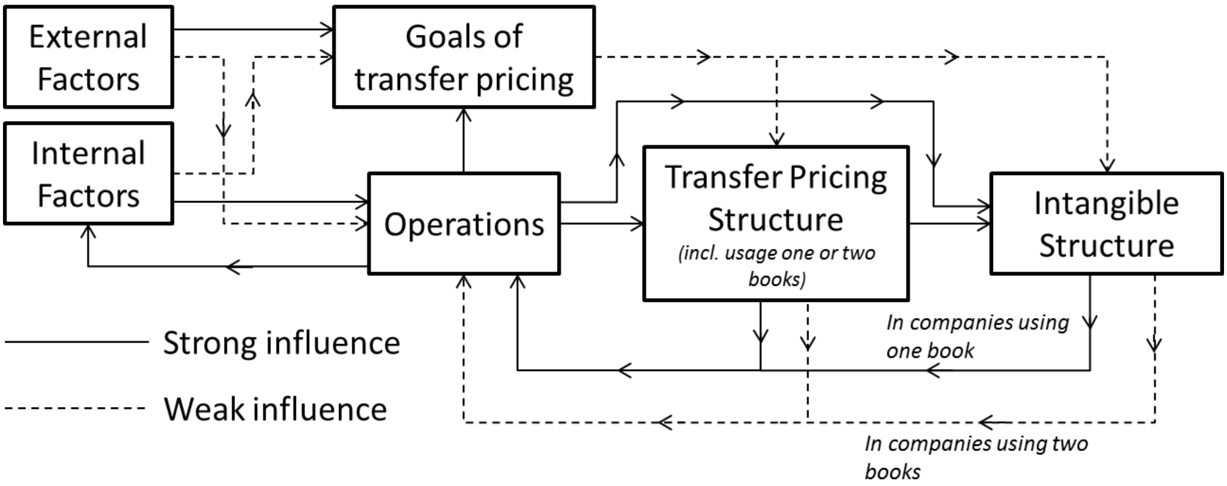

Figure 4 - Illustration of the influences on transfer pricing system of intangibles

Based on the analysis of the findings, the following model has been developed to illustrate the relationship between different aspects of transfer pricing of intangible assets. In the first step one has to take the overall situation into account. This consists of external factors and internal factors. In this study most of the external factors the companies faced were relatively similar. External factors are assumed to be largely given and independent of other influences. All of the companies operate in the manufacturing industry, albeit in different markets. They were all based in Sweden, while being active worldwide in the same major markets, such as America, Europe and the BRIC countries among others. Consequently, the tax environment, the regulations and the cultural background were similar. Internal factors on the other hand are quite diverse in the companies. The strategies employed differed as well as the historical context and internal structures. Internal factors are closely linked to the operations and are mutually dependent. The operations vary significantly across the different companies.

The goals of the transfer pricing are very similar in all the companies. Therefore it is likely that the external factors, which are shared among the companies, influence the goals. The dominance of operational objectives over tax considerations can be linked to the manufacturing industry. The dominance of tax compliance over tax optimization is influenced by the tax environment and the Swedish business environment. The operations themselves influence the goals as they are themselves the dominant objectives for transfer pricing. The differences in the internal environment have a slight influence on the importance of simplification and the hierarchy of the goals.

When looking at the overall transfer pricing structure, substantial differences between the companies can be observed. Thus, the goals, which are shared, do not offer a sufficient explanation. The structure is more heavily influenced by the operations. The transfer pricing setup cannot be removed from the overall logic of the operation. The goal for tax compliance, as important as it is, can be achieved through a variety of structures and transfer pricing methods. The companies use this freedom to design the most operationally beneficial transfer pricing system. It has to be acknowledged that the transfer pricing system itself does also influence the operations.

The structure and transfer pricing of intangible assets is diverse for different companies. Thus, the overall transfer pricing structure and the operations are the dominant considerations in the transfer pricing of intangibles. It has to be noted that although the overall transfer pricing system is a major factor in the transfer pricing for intangible assets, they are not always connected. In order to understand the transfer pricing of intangible assets for a company, one has to take the overall transfer pricing system into account. Transfer pricing for intangible assets can be designed separately from the overall transfer pricing system, if this benefits the operations and is in line with the goals of the transfer pricing system.

That transfer pricing has an influence on the operations is acknowledged in literature and in practice. The companies do have a choice between the usages of one or two books for transfer pricing in order to mitigate some of this influence. When drawing on the same books for internal management and tax considerations, the influence on the operations is more significant than when a separation between the two is used. Mixed setups that exclude performance measurement from legal accounting in other ways can be considered as two book accounting in this model.

The implications of the model are that when the requirements and the goals for transfer pricing are changing as has also been concluded in previous literature (van der Meer-Kooistra, 1994), the transfer pricing of intangibles system cannot be altered easily. The operational concerns play an important role making the structure relatively stable and changes cumbersome. A fit between the different parts is indispensable. They influence each other. Transfer pricing is thus not always as pure and rational as one would like to have it. To control and optimize the system is difficult given the variety of influencing factors and interdependencies. The model therefore just provides a simplified overview over the most important aspects to be considered.

5. Conclusion

The purpose of this study was to investigate the determinants of the transfer pricing of intangibles. Through an explorative study of six companies, we tried to answer how Swedish multinational manufacturing companies conduct transfer pricing of intangible assets, as well as to provide new empirical data on the subject. Sub-questions related to the overall research question addressed the goals of transfer pricing for intangibles, the performance measurement through one or two books and the main factors that influence transfer pricing of intangible assets. This paper adds to current research by developing a basic model to illustrate the major influences on this topic. Furthermore, it shows that contingency and behavioral theories may help explain the major influences within the topic of transfer pricing of intangible assets.

By exploring the goals of the companies in the transfer pricing system for intangible assets, this study shows that they are very similar for all the companies studied. The operations are the main concern followed by tax compliance. Simplification has a medium importance for the companies. Tax optimization on the other hand has a low priority. This was not only stated by the companies themselves but also confirmed in a larger Swedish setting by both the consultants and the Swedish Tax Agency. Those results are contradictory to older transfer pricing literature (Cravens, 1997), where tax optimization is the main focus, but in line with studies that assume a tax compliant transfer pricing system (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010). The classification model for the goals of transfer pricing as used by Cravens (1997) is expanded to accommodate the findings.

The structure of the transfer pricing systems differs substantially across companies, which can mostly be attributed to the operations. Transfer pricing structures can also differ between divisions within a company. While the principal structure is a benchmark, which has a number of advantages, it cannot be implemented easily by the organizations, due to regulatory restrictions. As a result, most companies use some elements of it, but a complete implementation is not possible. Connected to the principal structure is the fact that most companies use the transactional net margin method to determine the transfer prices for transactions of both intangible and tangible assets.

The question of the effects of transfer pricing of intangible assets on performance measurement is related to the usage of single or double books by the companies. In the companies, tax adjustment effects on the transfer prices are largely avoided. There are, however, different variations of the usage of one or two books, depending on the operation of the company. The model of Borkowski (2001) is used for the analysis and extended to better reflect the findings. The specific selection of the setup between one and two books is contingent on the operations and the structure of the transfer pricing system.

The treatment of intangible assets in companies can be analyzed in four situations, firstly their creation, secondly their licensing, thirdly their transfer and lastly their ownership. Within those situations various setups are possible. The companies all have different specifications in their intangibles system, which are heavily influenced by the operations and the strategy of the company regarding centralization and decentralization.

Taxation considerations are constantly in the background of the discussion on transfer pricing for intangible assets. Taxation optimization is a low priority in the analyzed Swedish companies as opposed to some findings in the literature (Cravens, 1997) (Borkowski, 1992). Accordingly, ethics is not considered a major topic in transfer pricing for intangible assets. Tax compliance is of growing importance, to a large extent due to increasing pressure by Swedish and international tax authorities. Tax compliance is achieved in various ways. Two distinctive approaches were identified, the proactive and the reactive approach. In the proactive approach the companies are more actively defending their current transfer pricing system to convince the authorities of its compliance and try to avoid adjustments. In the reactive approach, taxation adjustments are common to comply with the arm's length principle.

On the basis of the analysis, a model for the main influences in transfer pricing of intangible has been developed. It illustrates the conclusion of this paper that mostly external factors determine the goals of transfer pricing in the companies. Internal factors are mostly responsible for the structure of the operations. The transfer pricing system itself is primarily determined by the operations. The influence of the transfer pricing system on the operations is in the studied cases deliberately limited by the avoidance of transfer pricing effects on performance measurement.

5.1. Limitations and Suggestions for Future Research

As with all research, this study is also suffering from certain limitations. One apparent limitation of this thesis is the relatively small sample size of the qualitative multi-case study. This study has analyzed the transfer pricing system of intangible assets in six companies. Six cases are not sufficient to draw statistically significant conclusions, which can be applied in a broader context. The generalizability of the findings is thus limited.

On the other had there is a trade-off on the amount of detail which can be provided in a multi-case study. This analysis, while being more in-depth than survey based approaches, has been focusing more on a higher level. A more detailed case study can uncover more of the detailed influences and determinants of the transfer pricing system. This can relate to internal systems and processes. For their analysis, more in-depth interviews per company are necessary. This is related to the limitation that this study only provides a snapshot of the current transfer pricing system for intangible assets. Transfer pricing systems within companies are constantly evolving due to changes in the regulatory and business environment. With a more longitudinal approach, those changes and influences in the transfer pricing system for intangibles can be studied in more detail. This has been done in several other studies regarding transfer pricing (Cools, et al., 2008) (Plesner Rossing & Rohde, 2010).

Another limitation is the fact that due to the sensitivity, there was no access to internal transfer pricing data. The companies were reluctant to show their books, as this data makes up the core of their businesses. The interviews therefore have to be the major source for this study. The companies therefore can control how they will be presented. The interviews with the consultants and tax authorities can only mitigate this bias to a certain extent. With detailed data, a quantitative study might be possible to test hypotheses which can be inferred from qualitative studies.

Lastly, this study is only taking into account companies based in Sweden in the manufacturing industry. Therefore the business environment regarding the regulations and the culture is held constant. The manufacturing industry has specific characteristics, such as large amounts of tangible assets in addition to intangible assets and the predominance of the operational considerations. Other industries are characterized by different intangible assets and a different operational setup.

Suggestions for future research can be derived from this. It could be interesting to look at transfer pricing of intangible assets in other countries than Sweden. The impact of factors such as culture or regulatory environment could be assessed in more detail. Furthermore, it might be interesting to focus on a different industry than the manufacturing industry to see if the results of this study also apply to them.

As this paper is explorative, no statistically generalizable findings are generated. In future research a more quantitative approach might be taken for example through a survey. This could help to generate and confirm hypotheses. The focus might also be expanded to cross country or industry comparisons.

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Annual Reports 2010 – 2012 Company D

Annual Reports 2010 – 2012 Company E

Annual Reports 2010 – 2012 Company F

Appendix

Appendix 1: Interviews

Company E	Tax Controller	25th February 2013
Company F	Tax Director	26th February 2013
Company B	Director Transfer Pricing	28th February 2013
Company E	Tax Controller	6th March 2013
Company B	Financial Controller Director Transfer Pricing	12th March 2013
Company C	Tax Controller	25th March 2013
Company A	Tax Expert	28th March 2013
Company D	Tax Manager	2nd April 2013
Consultancy A	Senior Manager Transfer Pricing	3rd April 2013
Consultancy B	Tax Partner Senior Manager Transfer Pricing	4th April 2013
Company D	Controller	5th April 2013
Company C	VP Transfer Pricing	5th April 2013
Consultancy B	Senior Manager Transfer Pricing	10th April 2013
Consultancy C	Tax Director	11th April 2013
Consultancy D	Transfer Pricing Director Associate Transfer Pricing	17th April 2013
Swedish Tax Agency	Tax Auditor	29th April 2013

Appendix 2: Interview Guides

The following interview guides have been used to structure the interviews

Interview Guide Companies

Introduction

- Who we are
- What our thesis is about
- Time frame
- Anonymity
- Recording

Generic Questions

1. What is your current position? How long have you been in the current position? What is your background?
2. What are your key responsibilities (want to know who he reports to)?
3. Where is your position in the Group? What is your relation to the divisions?

Transfer pricing system questions

4. Could you briefly describe the transfer pricing system?
5. How are prices set?
6. What techniques for transfer pricing of intangibles do they use?
7. Why are they using these techniques?
8. What are the goals of transfer pricing (strategy, economic optimization, group performance, tax, risk minimization…)? Are those goals achieved?
9. Which parties (and which hierarchy level within that party) decides what transfer pricing techniques to be used and who decides the levels? Do they consult other parties within the company?
10. What information is used?
11. When/How often are prices set?
12. What impact do the OECD guidelines have on the transfer pricing system?
13. What impact do tax considerations have on the choice and usage of transfer pricing techniques?
14. Transparency: How detailed are the internal regulations? Is the process standardized?
15. Are there challenges associated with the current system?
16. How are potential conflicts managed?
17. Have there been any recent changes? What/Why/How?

Transfer pricing of intangibles

18. How is the transfer pricing of intangibles structured?
19. What intangibles are transferred? Which are the most important ones?
20. Where are the intangibles located and managed? (Centralization – Decentralization)

21. Is there a difference between tangibles and intangibles? Is the difference documented and fixed procedure?
22. Are the goals different? If so, in what way? Success?
23. What, Who, Why, When are transfer prices set?
24. Who is affected? How?
25. What is the effect on the group and on the divisions?
26. How transparent is the transfer pricing process? (internally and externally)
27. Ho flexible can the process be adapted to local needs?
28. How are conflicts managed? Where do they occur primarily?
29. Have there been any recent changes?
30. Do you see any trends in this area? Within and outside the company?

Taxes and transfer pricing

31. What impact do tax considerations have on the choice of the transfer pricing system?
32. What is the relevant regulation? OECD guidelines?
33. Are you happy with the tax law/arm's length principle?
34. What is their relation with the tax authorities? Do they have Advanced Pricing Agreements?
35. Is the interpretation of the tax law strict? Lots of conflicts?
36. Do you follow the drafting of the new transfer pricing of intangibles OECD guidelines?

Transfer Pricing and Management Control

37. What impact does transfer pricing have on the management control system? Is the system integrated in the process?
38. Do the outcomes of the transfer pricing setting link to performance management? Does this cause any conflicts?
39. Is the company rather centralized or decentralized?

Ending

- Next steps
- Follow up questions by email/phone
- Other potential interview partners – Intellectual Property management / Controller (group/division) / other persons mentioned during the interview

Interview Guide Consultants

Introduction (same as companies)

Generic Questions

1. What is your current position? How long have you been in the current position? What is your background?
2. What are your key responsibilities?

3. In what projects do you do in transfer pricing?
4. What type of clients (industry/size/HQ)?

Intangibles

5. What are generally the most important types of intangibles?
6. Are they more centralized at the head office or distributed in countries?
7. Is there a trend for centralization?
8. What would you recommend to clients in this respect?
9. Do you support these kinds of transactions?

Transfer pricing of intangibles

10. How does transfer pricing of intangibles differ from tangibles?
11. Is this a “hot” topic at the moment?
12. What are trends in this area? Why?
13. What are the most common goals?
14. Differences between industries?
15. Is there something special in manufacturing industry?
16. What are the main difficulties? (benchmarking/valuation)
17. Is it common to bundle intangibles together?
18. Bundles with other products/assets?
19. New OECD guidelines – are they any good?
20. Overhead cost allocation – is that a transfer pricing issue?
21. Is there anything important we have missed?

Observations

22. Nobody is tax aggressive, do you agree?
23. Operational concerns are given priority?
24. Swedish tax authorities are less aggressive and somewhat reasonable?
25. Historical/Strategic context of the company plays a large role?
26. We observe a trend for centralization?
27. Transfer pricing of intangibles does not affect performance mgmt.?

Ending

- Next steps
- Follow up questions by email/phone

Interview Guide Tax Authorities

Introduction (same as above)

Generic Questions

1. What is your current position? How long have you been in the current position? What is your background?

2. What are your key responsibilities?
3. What projects do you do in transfer pricing?
4. What type of companies do you work with?

Transfer pricing for the tax authorities

5. What are the goals of tax authorities in transfer pricing (of intangibles)?
6. What are the main challenges?
7. Guidelines – What do they think about them? How do they apply them? How do you think about the development?
8. What are the specific challenges for intangibles? Centralization desired?
9. How much do you rely on benchmarks?
10. Current development/trends – are the authorities becoming more aggressive? Are the companies more evasive?
11. How does your collaboration with the companies look like? Are they tax aggressive?
12. What do you see are the companies' goals for transfer pricing? Are those approaches reasonable? Do you see any differences between industries (esp. in the manufacturing industry)?
13. Do you prefer single or double book accounting?
14. Do you prefer certain structures (i.e. principal structure) to others?
15. What us their assessment/relationship to other authorities? How is your approach different from other countries?
16. How has the transfer pricing department at the tax authorities developed? (More people, more expertise?) Why?
17. How do you decide on audits?
18. How much money do you make on Transfer Pricing per invested SEK?

Observations

19. Nobody is tax aggressive, do you agree?
20. Operational concerns are given priority?
21. Swedish tax authorities are less aggressive and somewhat reasonable?
22. Historical/Strategic context of the company plays a large role?
23. We observe a trend for centralization?

Ending

- Next steps
- Follow up questions by email/phone