Internal Revenue Service
DEPARTMENT OF THE TREASURY

LB&I International Practice Service Transaction Unit

IPS Level	Number	Title	UIL Code	Number
Shelf	N/A	Business Outbound	–	–
Volume	1	Outbound Income Shifting	**Level 1 UIL**	9411
Part	1.1	Intangible Property Transfers w/ Cost Sharing	**Level 2 UIL**	9411.01
Chapter	1.1.1	Determination of Buy-In/Buy-Out Amounts	**Level 3 UIL**	9411.01-01
Sub-Chapter	N/A		–	–

Unit Name	Change in Participation in a Cost Sharing Arrangement (CSA) – Controlled Transfer of Interests and Capability Variation

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Date of Last Update	09/21/15

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Issue and Transaction Overview

Change in Participation in a Cost Sharing Arrangement

Under the U.S. cost sharing regulations, parties under common control may enter into a “cost sharing arrangement” (“CSA”) which allows the parties to share the costs of developing one or more intangibles (“cost shared intangibles”) in proportion to each party’s share of reasonably anticipated benefits (“RAB Shares”) resulting from use of the cost shared intangibles. After participants enter into a CSA, there may be a subsequent “change in participation” that affects the controlled participants’ interests under the CSA. A change in participation under a CSA occurs when there is either a controlled transfer of interests or a capability variation, and requires arm’s length consideration.

A “controlled transfer of interests” occurs when a cost sharing participant transfers all or part of its interests in cost shared intangibles under the CSA in a controlled transaction, and the transferee assumes the associated obligations under the CSA (e.g., a change in the territorial based divisional interests or field of use based divisional interests). After the controlled transfer of interests occurs, the CSA will still exist if at least two controlled participants still have interests in the cost shared intangibles. In such case, the transferee will be treated as succeeding to the transferor’s prior history under the CSA as pertains to the transferred interests, including the transferor’s cost contributions, benefits derived, and PCT Payments attributable to such rights or obligations.

A “capability variation” occurs when interests in cost shared intangibles are not divided on certain territorial or certain exclusive field of use bases but rather on other divisional bases and the controlled participants’ division of interests or their relative capabilities or capacities to benefit from the cost shared intangibles are materially altered. In such instance, the controlled participants’ RAB shares from exploiting the cost shared intangibles may change. This change in RAB shares due to a capability variation is considered a controlled transfer of interests in cost shared intangibles. The participant whose RAB share decreases is considered the transferor and the participant whose RAB share increases is considered the transferee.

Issue and Transaction Overview (cont'd)

Change in Participation in a Cost Sharing Arrangement

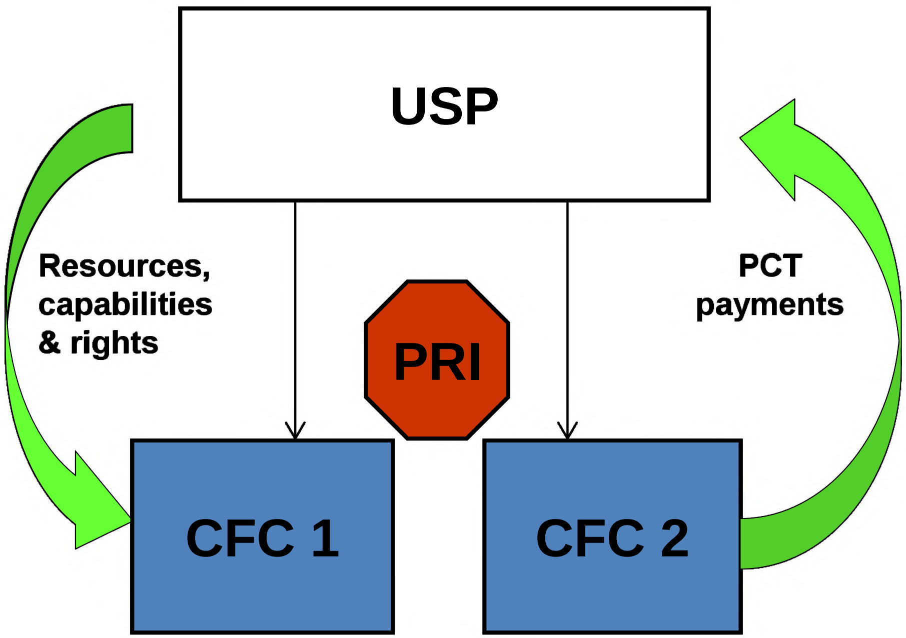
In the event of a change in participation, the arm's length amount of consideration from the transferee will be determined consistent with the reasonably anticipated incremental change in the returns to the transferee and transferor. Changes in returns themselves will depend on the reasonably anticipated incremental changes in the benefits from exploiting the cost shared intangibles, intangible development costs ("IDCs") borne, and platform contribution transaction ("PCT") payments (if any).

It is important to determine which controlled participants are affected by the change in participation to determine if there is a direct federal income tax consequence. For example, if the U.S. participant is a party to the change in participation, then the U.S. participant will be required to report the arm's length payments received as taxable income if it is a transferor of the cost shared intangibles. Likewise, if the U.S. participant is making arm's length payments as a transferee of the intangibles, it may be entitled to a deduction for federal income tax purposes.

Moreover, when considering an arm's length adjustment for a capability variation, it is important to first determine whether the exam team has made an adjustment to improve the reliability of projections used to estimate RAB shares. In such instance, the adjustment for capability variation should be reduced or eliminated to the extent that it duplicates the adjustment to improve reliability of projections for RAB shares. Similarly, if a prior adjustment has been made for a capability variation, it is important not to make an adjustment to improve the reliability of RAB shares if that adjustment would duplicate the capability variation adjustment.

Transaction and Fact Pattern

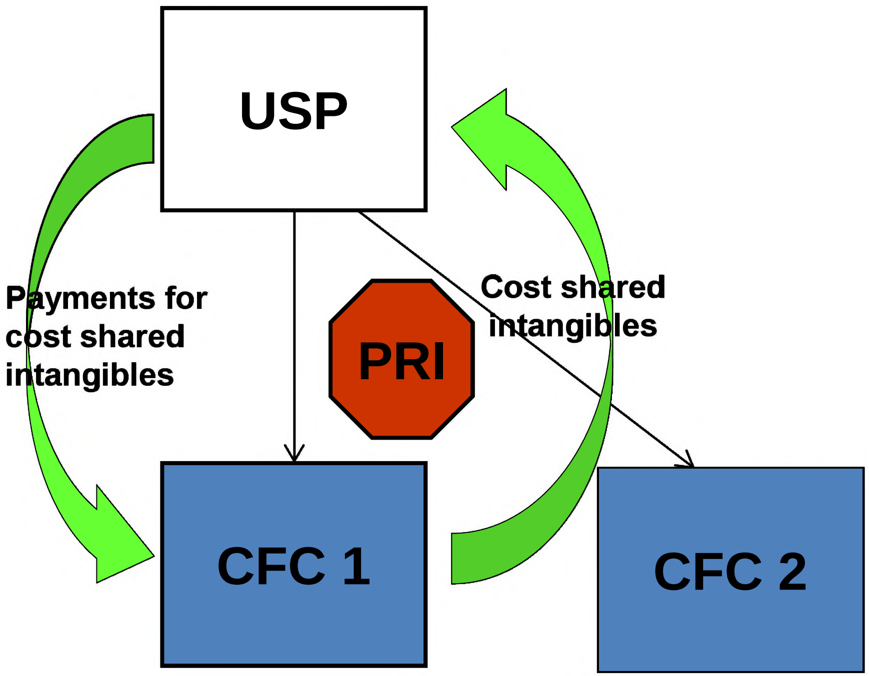
Change in Participation in a Cost Sharing Arrangement

Diagram of Transaction	Facts
 Initial entity and CSA 1 structure as of March 1, 2012 (prior to Change in Participation in CSA 1)	▪ USP is a multi-national high tech company that has successfully developed resources, rights, and capabilities, including valuable technology IP relating to data processing. ▪ On January 1, 2012, USP formed CFC 1 and CFC 2 in Country X and Country Y, respectively. ▪ On March 1, 2012, USP entered into a CSA with CFC 1 and CFC 2 to further develop all of its technology related intangibles. Each participant will utilize the cost shared technology when it provides data processing services to third party customers in their respective territories. Under the CSA, each participant gets perpetual and exclusive rights to exploit cost shared intangibles in its territory. ▪ USP's territory is the US, CFC 1's territory is Europe, and CFC 2's territory is the rest of the world ("ROW"). Development costs are shared USP 30%, CFC 1 35%, and CFC 2 35%, based on reasonably anticipated benefits ("RABs") in the parties' respective territories. The term of the CSA is 3 years but it is renewable at will based on the agreement of the parties. ▪ On the same date USP, CFC 1, and CFC 2 entered into a Technology License Agreement ("TLA") for IP which will be used in the intangible development area within the CSA ("platform rights"). The TLA also covers a license of rights to exploit existing IP in CFC 1's and CFC 2's territories ("make-sell rights").

Transaction and Fact Pattern (cont'd)

<table>
<tr><th colspan="2">Change in Participation in a Cost Sharing Arrangement</th></tr>
<tr><th>Diagram of Transaction</th><th>Facts</th></tr>
<tr><td>

<u>CSA 1</u>



Example 1 – Change in Participation in CSA 1 due to Controlled transfer of interests in cost shared intangibles from CFC 1 to USP.

</td><td>

- On January 1, 2013, CFC 1 transfers its interests in cost shared intangibles to USP relating to the Europe territory and the associated obligations under the CSA.
- At the time of transfer, the RAB from exploiting cost shared intangibles in Europe have a present value of $50 million, the reasonably anticipated intangible development costs (IDCs) to be borne relating to the European territory have a present value of $10 million and the reasonably anticipated PCT Payments to be made to USP relating to sales in the European territory are $5 million.
- On January 2, 2013, USP and CFC 2 are the remaining controlled participants where USP's territory is the U.S. and Europe and CFC 2's territory is ROW.
- Accordingly, USP's RAB share increased from 30% to 65%, CFC 2's RAB remained at 35%, and CFC 1 RAB share was reduced to zero because it exited the CSA.

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Transaction and Fact Pattern (cont'd)

Change in Participation in a Cost Sharing Arrangement

<table>
<tr><th>Diagram of Transaction</th><th>Facts</th></tr>
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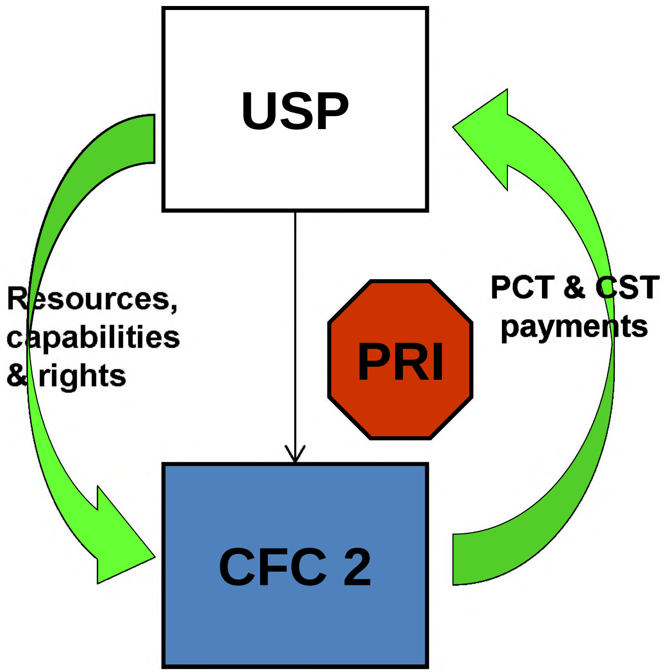
<u>CSA 2</u>



Example 2 – Change in Participation in CSA 2 due to capacity variation of CFC2
</td><td>

- On April 1, 2013, USP and CFC 2 enter into a new CSA ("CSA 2") to develop new technology related to the manufacture of computer hardware in the U.S. and Country X. USP had a platform technology that it contributed to CSA 2 and CFC 2 is obligated to pay PCT Payments to USP based on a 5% sales based royalty.
- USP and CFC 2 agree to divide their interests in cost shared intangibles based on the site of manufacturing. USP will have exclusive and perpetual rights in hardware manufactured in facilities owned by USP and CFC 2 will have such rights for hardware manufactured in facilities owned by CFC 2.
- The term of CSA 2 is 3 years and initial RAB shares are 50-50.
- At April 1, 2012, all facilities are operating near capacity and are expected to continue to operate near capacity when the computer hardware enters production, such that it would not be feasible to shift production between USP's and CFC 2's facilities.
- USP and CFC 2 do not have plans to build an additional facility to manufacture hardware.
- On October 1, 2014, CFC 2 acquired a manufacturing plant in Asia due to a change in plans that was not reasonably foreseeable when the CSA was entered into. Based on the additional manufacturing capacity, CFC 2's RAB share increases from 50% to 65% in CSA 2.
</td></tr>
</table>

Transaction and Fact Pattern (cont'd)

Change in Participation in a Cost Sharing Arrangement
Facts
Example 2 (cont'd) ▪ CFC 2's acquisition of the additional plant results in a \$35 million increase in its reasonably anticipated benefits from exploiting the cost shared intangibles. However, due to the increase in its RAB share, it expects to bear additional IDCs of \$10 million and make additional PCT Payments of \$5 million, resulting in a net present value benefit to CFC 2 of \$20 million. ▪ There were no other adjustments to improve the reliability of projections used to estimate RAB shares.

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Effective Tax Rate Overview

Change in Participation in a Cost Sharing Arrangement

ETR of Company
▪ When there is a change of participation in a CSA, then the worldwide effective tax rate of the U.S. participant(s) may change. For example, if the change in participation results in the foreign participant exploiting the cost shared intangibles to a higher degree than it did in the past, then USP's ETR may decrease if it does not receive arm's length compensation for the incremental change in its expected returns under the CSA (after subtracting the present value of anticipated IDCs and expected PCT Payments). This ETR impact may occur because the income streams from these cost shared intangibles will now remain offshore where they may indefinitely escape U.S. taxation.
ETR Impact of Adjustment
▪ An adjustment to increase the compensation to USP for the capability variation pursuant to IRC 482 will increase its taxable income and will therefore increase the ETR.

Summary of Potential Issues

Change in Participation in a Cost Sharing Arrangement

Issue 1	What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?
Issue 2	What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Change in Participation in a Cost Sharing Arrangement

When there is a change in participation in a CSA due to either a controlled transfer of interests or a capability variation, the transferee(s) must provide arm's length consideration to the transferor(s).

Fact Element	Resources	6103 Protected Resources
▪ Was there a change in participation under the CSA where either (1) a controlled participant transferred all or part of its interests and obligations under the CSA to another controlled taxpayer or (2) the participants' division of interests or relative capabilities to benefit from the cost shared intangibles were materially altered?	▪ CSA, RAB computations, and all facts ▪ Transfer pricing studies	
▪ Determine what, if any, consideration was reported by the taxpayer for the transfer of the interests in the cost shared intangibles.	▪ Valuation studies	
▪ Compare the controlled participants listed on the required CSA statement to the tax return.	▪ Required CSA Statement	

Issue 1, Step 2: Review Potential Issues

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interest in the cost shared intangibles?

Explanation of Issue	Resources
As previously discussed, a "controlled transfer of interests" occurs when a cost sharing participant transfers all or part of its interests in cost shared intangibles under the CSA in a controlled transaction, and the transferee assumes the associated obligations under the CSA. In Example 1, CFC 1 transferred its interests in cost shared intangibles relating to the European territory and the associated obligations under CSA 1 to USP. Therefore, there is a controlled transfer of interests where CFC 1 is the transferor of cost shared intangibles and USP is the transferee. In such case, USP will be treated as succeeding to the CFC 1's prior history under CSA 1 as it pertains to the transferred interests, including the transferor's cost contributions, benefits derived, and PCT Payments attributable to such rights or obligations.	▪ Treas. Reg. 1.482-1(c) – *Best method rule* ▪ Treas. Reg. 1.482-1(d) – *Comparability* ▪ Treas. Reg. 1.482-1(e) – *Arm's length range* ▪ Treas. Reg. 1.482-4(a) –*Methods to determine taxable income in connection with a transfer of intangible property* ▪ Treas. Reg. 1.482-7(a)(3)(ii) – *Transfer of interest in cost shared intangible* ▪ Treas. Reg. 1.482-7(f)(2) – *Controlled transfer of interests*

Issue 1, Step 2: Review Potential Issues (cont'd)

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interest in the cost shared intangibles?

Explanation of Issue	Resources
In this fact pattern, USP is a U.S. taxpayer and considered to be the transferee of the interests in cost shared intangibles under CSA 1 with respect to the European territory. It is important to follow the rules in Treas. Reg. 1.482-1 and -4 through -6 in determining the arm's length amount of consideration that USP must pay to CFC 1 for the interests in cost shared intangibles less the IDCs and less the PCT Payments that are related to the European territory at issue, because USP may be entitled to a deduction for federal income tax purposes.	▪ Treas. Reg. 1.482-7(f)(4) – *Arm's length consideration for a change in participation* ▪ Treas. Reg. 1.482-7(f)(5) *Example 1*

Issue 1, Step 3: Additional Factual Development

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?

Fact Element	Resources	6103 Protected Resources
▪ What is the present value of the reasonably anticipated returns from the transferred interests in the cost shared intangibles? ▪ Determine what, if any, consideration was reported by the taxpayer for the transfer of the interests in the cost shared intangibles? ▪ What are the reasonably anticipated intangible development costs to be borne relating to the transferred interests in the CSA? ▪ How are the cost shared intangibles being used by each of the controlled participants? ▪ What are the reasonably anticipated PCT payments that will be paid relating to the transferred interests in the CSA?	▪ Taxpayer projections of sales with respect to the transferred interests at issue. ▪ Taxpayer projection of IDCs that will be borne by the transferor. ▪ PCT calculations with respect to the transferred interests ▪ Transfer pricing studies ▪ Functional analysis ▪ Valuation reports	
CONSULTATION: Consult with Economist, TPP, Counsel and/or Engineers as necessary.		

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

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?

Fact Element	Resources	6103 Protected Resources
▪ How are the divisional interests defined and are they adequately documented? ▪ How are the forecasted sales derived? ▪ What is the assumed growth rate and is it reasonable and supported with valid assertions? ▪ How are the exploitation costs identified, selected and verified? ▪ How are the operational cost identified, selected and verified? ▪ What are the discount rates used in the models and are they reasonable and used consistently across the various models?	▪ Transfer Pricing Studies ▪ Taxpayer's Valuation Study ▪ Segmented Financial Statements ▪ Discounted Cash Flow Models ▪ Taxpayer's WACC computations	

Issue 1, Step 4: Develop Arguments

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm's length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?

Explanation of Adjustment	Resources	6103 Protected Resources
Develop the facts of the controlled transfer of interests transaction through a functional analysis to fully understand the nature of the interests in cost shared intangibles that were transferred as well as the present value of the expected IDCs to be borne and the PCTs that would be paid with respect to the transferred CSA interests. Here, the cost shared intangibles have a present value of $50 million, the reasonably anticipated IDCs to be borne have a present value of $10 million and the reasonably anticipated PCT Payments for the same territory is $5 million. Therefore, the net consideration that USP must pay to CFC 1 is $35 million ($50 million less $10 million IDCs less $5 million PCT). If taxpayer had not correctly determined the PCT, IDCs, and RAB, an adjustment would be required.	▪ Treas. Reg. 1.482-1(c) -*Best method rule* ▪ Treas. Reg. 1.482-1(d) -*Comparability* ▪ Treas. Reg. 1.482-1(e) -*Arm's length range* ▪ Treas. Reg. 1.482-4(a) -*Methods to determine taxable income in connection with a transfer of intangible property*	

Issue 1, Step 4: Develop Arguments (cont’d)

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm’s length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?

Explanation of Adjustment	Resources	6103 Protected Resources
When valuing the transferred interests in the cost shared intangibles, apply the best method rule to determine the most reliable method for determining an arm’s length result For additional guidance on the issue of determining the best method for transactions involving cost sharing arrangements or intangibles or for the application of the principles of the investor model and best realistic alternative, please refer to the following Practice Units: ▪ Practice Unit, “Pricing of Platform Contribution Transaction (PCT) in a Cost Sharing Arrangement (CSA) – Initial Transaction”, DCN: ISO/9411.01_01 (2013)	▪ Treas. Reg. 1.482-7(a)(3)(ii) - *Transfer of interest in cost shared intangible* ▪ Treas. Reg. 1.482-7(f)(2) - *Controlled transfer of interests* ▪ 1.482-7(f)(4) – *Arm’s length consideration* ▪ Treas. Reg. 1.482-7(f)(5) -Example 1	

Issue 1, Step 4: Develop Arguments (cont’d)

Change in Participation in a Cost Sharing Arrangement
Issue 1
What is the arm’s length compensation that USP must provide to CFC 1 for the controlled transfer of interests in the cost shared intangibles?

Explanation of Adjustment	Resources	6103 Protected Resources
▪ Practice Unit, “Pricing of Platform Contribution Transaction (PCT) in a Cost Sharing Arrangement (CSA) – Acquisition of Subsequent IP”, DCN: ISO/9411.01_02 (2013); ▪ Practice Unit, “Cost Sharing Arrangements versus Licensing Alternatives”, DCN: ISO/9411.01_03 (2013); and ▪ Practice Unit, “License of Intangible Property from U.S. Parent to a Foreign Subsidiary”, DCN: ISO/9411.02_03 (2013).		

Issue 2, Step 2: Review Potential Issues

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Explanation of Issue	Resources
When a capability variation occurs, the primary issue is determining the required arm's length payment for the incremental change in the divisional interests in the underlying cost shared intangible property among the relevant controlled participants. As previously stated, a capability variation occurs when cost shared intangibles are divided on a divisional basis (e.g., division of interests based on site of manufacturing) other than certain territorial or field of use divisional interests and the controlled participants' division of interests or their relative capabilities or capacities to benefit from the cost shared intangibles are materially altered. In the instant case, CSA 2 divides up the interests in cost shared intangibles based on the site of manufacturing and CFC 2 acquired an additional manufacturing plant that increased its RAB from 50% to 65%. A sub-issue is whether this capability variation was reasonably foreseeable at the time that CSA 2 was formed. Here, the facts indicate that it was not foreseeable. However, that determination should initially be made in an actual case, because, if the increase in capability was reasonably foreseeable, that may suggest that the initial RAB projections were unreliable instead of there being a capability variation.	▪ Treas. Reg. 1.482-1(c) - *Best method rule* ▪ Treas. Reg. 1.482-1(d) - *Comparability* ▪ Treas. Reg. 1.482-1(e) - *Arm's length range* ▪ Treas. Reg. 1.482-4(a) - *Methods to determine taxable income in connection with a transfer of intangible property* ▪ Treas. Reg. 1.482-7(a)(3)(ii) - *Transfer of interests in cost shared intangible* ▪ Treas. Reg. 1.482-7(b)(4)(iv) - *Other divisional basis*

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Issue 2, Step 2: Review Potential Issues (cont'd)

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Explanation of Issue	Resources
A capability variation is considered a controlled transfer of interests in that any participant whose RAB share decreases as a result of the capability variation is considered a transferor and any participant whose RAB increases is considered a transferee of cost shared intangibles. Thus, the same analysis of determining the present value of the transferred cost shared intangibles, present value of IDCs borne, and expected PCT Payments must performed as in Issue 1. Therefore, the issue becomes whether USP as the transferor of the cost shared intangibles due to the capability variation has received arm's length compensation from CFC 2. Therefore, it is critical to develop the facts to determine the incremental change in the RAB shares of the respective controlled participants as well as the most reliable method for determining the arm's length price of the interests in cost shared intangibles that were considered to be transferred as a result of the capability variation..	▪ Treas. Reg. 1.482-7(e) - *Reasonably anticipated benefits share* ▪ Treas. Reg. 1.482-7(f)(3) - *Capability variation* ▪ Treas. Reg. 1.482-7(f)(5) Example 2 ▪ Treas. Reg. 1.482-7(a)(3)(ii) - *Transfer of interest in cost shared intangible* ▪ Treas. Reg. 1.482-7(b)(4)(iv) - *Other divisional bases* ▪ Treas. Reg. 1.482-7(f)(3) - *Capability variation* ▪ Treas. Reg. 1.482-7(f)(4) - *Arm's length consideration* ▪ Treas. Reg. 1.482-7(f)(5) Example 2

Issue 2, Step 2: Review Potential Issues (cont'd)

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Explanation of Issue	Resources
It is also important not to duplicate a prior adjustment that has been proposed to improve the reliability of projections used to estimate RAB shares if that adjustment results from the same capability variation. Thus, any arm's length consideration that would have been required by the capability variation must be reduced as necessary by the exam team to prevent this duplication. Here, the facts indicate that no such adjustment has been proposed by the IRS so there would be no duplication of a prior adjustment if the IRS proposes an adjustment due to the capability variation.	

Issue 2, Step 3: Additional Factual Development

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Fact Element	Resources	6103 Protected Resources
▪ What is the reasonably anticipated incremental change in the present value of the benefits from exploiting the cost shared intangibles? ▪ What is the present value of anticipated IDCs and PCT Payments with respect to the transferred interest that resulted from the capability variation?	▪ Transfer Pricing Studies ▪ Annual Reports and references ▪ Interview key employees ▪ SEC Filings ▪ Press Releases – Joint Efforts w/FP ▪ Capital IQ – Research Market Studies as well as competitors ▪ Internet Searches on taxpayer ▪ CSA checklist Revised 2008 ▪ RAB projections by taxpayer ▪ Cost sharing agreement ▪ Studies or reports related to the capability variation	
CONSULTATION: Consult with Economist, TPP, Counsel and/or Engineers as necessary		

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Issue 2, Step 3: Additional Factual Development (cont'd)

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Fact Element	Resources	6103 Protected Resources
▪ How did the controlled participants divide their interests in the cost shared intangibles? ▪ Was the capability variation reasonably foreseeable at the time that the CSA was entered into? ▪ What is the most reliable method to determine the arm's length price due from CFC 2 to USP for the interests in cost shared intangibles? – comparability – quality of data – reliability of assumptions (tax rates, discount rates, projections, etc.) – sensitivity of results to possible deficiencies	▪ Transfer Pricing Study ▪ Economist Report ▪ Valuation Study ▪ Technology License Agreement ▪ Cost Sharing Agreement ▪ Financial statements and disclosures for all controlled participants ▪ RAB projections	

Issue 2, Step 4: Develop Arguments

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Explanation of Adjustment	Resources	6103 Protected Resources
Verify how the cost shared intangibles are divided among the controlled participants. If the cost shared intangibles are divided on a basis described in Treas. Reg. 1.482-7(b)(4)(iv) (for instance, site of manufacturing), then determine whether the capability variation was reasonably foreseeable at the time that the CSA was entered into, because, in such instance, an adjustment to improve the reliability of projections used to estimate RAB shares may be warranted instead of an adjustment for a capability variation. Here, the facts indicate that acquisition of the plant in Asia was unforeseeable, so there is a capability variation between USP and CFC 2 with respect to CSA 2.	▪ Treas. Reg. 1.482-1(c) - *Best method rule* ▪ Treas. Reg. 1.482-4(a) - *Methods to determine taxable income in connection with a transfer of intangible property* ▪ Treas. Reg. 1.482-7(a)(3)(ii) - *Transfer of interest in cost shared intangible* ▪ Treas. Reg. 1.482-7(b)(4)(iv) - *Other divisional basis* ▪ Treas. Reg. 1.482-7(f)(3) - *Capability variation* ▪ Treas. Reg. 1.482-7(f)(4) - *Arm's length consideration*	
CONSULTATION: Consult with Economist, TPP, Counsel and/or Engineers as necessary		

Issue 2, Step 4: Develop Arguments (cont'd)

Change in Participation in a Cost Sharing Arrangement
Issue 2
What are the tax consequences to the controlled participants resulting from the capability variation when CFC 2 acquires a new manufacturing plant in Asia?

Explanation of Adjustment	Resources	6103 Protected Resources
The arm's length price for the transfer of interests in cost shared intangibles must be determined and an economist can assist with that determination. In this fact pattern, the facts indicate that the incremental change in the present value of the benefits of the cost shared intangibles ($35 million) less the present value of expected IDCs borne ($10 million) and expected PCT Payments ($5 million) is $20 million, which is the arm's length price.	▪ Treas. Reg. 1.482-7(f)(4) - *Arm's length consideration* ▪ Treas. Reg. 1.482-7(f)(5) Example 2	
CONSULTATION: Consult with Economist, TPP, Counsel and/or Engineers as necessary		

Training and Additional Resources

Chapter 1.1.1 Determination of Buy-In/Buy-Out Amounts		
Type of Resource	**Description(s) and/or Instructions for Accessing**	**References**
CENTRA sessions	▪ 2012 CENTRA - Cost Sharing: Advanced Cost Issues and New Developments ▪ 2012 CENTRA - Income Method ▪ 2012 CENTRA - High Value Services ▪ 2013 CENTRA - Income Method - Part II	
Issue Toolkits	▪ IRM 4.61.3 -4 - Functional Analysis Questionnaire ▪ IRM 4.61.3 - Development of IRC section 482 Cases	

Glossary of Terms and Acronyms

Term/Acronym	Definition
CFC	Controlled Foreign Corporation
CPM	Comparable Profits Method
CSA	Cost Sharing Arrangement
CST	Cost Sharing Transaction
ETR	Effective tax rate
IDC	Intangible Development Cost
IP	Intangible Property
IPN	Issue Practice Network
IRC	Internal Revenue Code
PCT	Platform Contribution Transaction
RAB	Reasonably Anticipated Benefits
ROW	Rest of World
TLA	Technology License Agreement
TPP	Transfer Pricing Practice
USP	United States Parent
WACC	Weighted average cost of capital

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Index of Related Issues

Issue	Associated UIL(s)	References
Initial PCT transaction	9411.01 – Intangible Property Transfers with Cost Sharing	Practice Unit, “Pricing of Platform Contribution Transaction (PCT) in Cost Sharing Arrangements (CSA) Initial Transaction”, DCN: ISO/9411.01_01(2013)
Subsequent PCT - Acquisition	9411.01 – Intangible Property Transfers with Cost Sharing	Practice Unit, “Pricing of Platform Contribution Transaction (PCT) in Cost Sharing Arrangements (CSA) Acquisition of Subsequent IP” DCN: ISO/9411.01_02(2013)
Cost Sharing vs. Licensing	9411.01 – Intangible Property Transfers with Cost Sharing	Practice Unit, “Cost Sharing Arrangements vs Licensing Alternative”, DCN: ISO/9411.01_03 (2013)
Annual Royalty Income and IRC 367 (d)	9411.02 – Intangible Property Transfers without Cost Sharing	Practice Unit, “Deemed Annual Royalty Income Under Section 367(d)”, DCN: ISO/9411.02_01(2013)
Sale, License and Other Transfer Distinctions	9411.02 – Intangible Property Transfers without Cost Sharing	Practice Unit, “Distinguishing Between Sale License and Other Transfers of Intangibles to CFCs by US Transferors”, DCN: ISO/9411.02_02(2013)

Index of Related Issues (cont'd)

Issue	Associated UIL(s)	References
Licensing Intangibles to Foreign Affiliate	9411.02 – Intangible Property Transfers without Cost Sharing	Practice Unit, "License of Intangible Property from U.S. Parent to a Foreign Subsidiary", DCN: ISO/9411.02_03(2013)
Arm's Length Standard	9411.07 – Other Transfer Pricing Issues	Practice Unit, "Comparison of the Arms Length Standard with Other Valuation Approaches - Outbound", DCN: ISO/CU/V_1_03(2014) In Process
Functional Analysis	9411.07 – Other Transfer Pricing Issues	Practice Unit, "Comparability Analysis for Tangible Goods Transactions Outbound", DCN: ISO/PUO/V_1_01(2014)
Arm's Length Standard	9422.09 – Other Transfer Pricing Issues	Practice Unit, "Arm's Length Standard", DCN: ISI/9422.09_06(2013)