TRANSFER PRICES: AN ECONOMIC AND FISCAL APPROACH

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Abstract:

This paper presents the transfer prices in the context of an enhanced and intensified control of the tax authorities, analyzing them both from an economic and fiscal perspective. Theoretically speaking, the economic approach is different from the fiscal one. There are arguments sustaining the disconnection between the economic and fiscal aspects of the transfer prices. We assist at a stronger regulation associated to the fiscal point of view and at an improvement of the resulted finance taxation.

Realizing a detailed and deep documentation of the existing scientific literature in this field, processing and interpreting statistical data and using a comparative data analysis, this study arrives at the conclusion that transfer prices should be considered by taking into account all the economic, taxation and custom implications. Only such a complete and integrated approach may offer safety to companies when they are confronted with custom or fiscal inspections.

Keywords: *transfer pricing, joint parties, methods, adjustments*

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1. Introduction

By approaching the issue of transfer pricing as an instrument used for moving the profits from countries with high fiscality in those with more relaxed fiscality, common problems appear both in the public environment (fiscal

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administration, customs administration, the European Union, national, regional and local governing) and in the economic sector (financial organisms and European and international audit organisms, non-guvernamental companies and counselling companies, etc.).

Within the context of fiscal reforms undegoing at European Union level, to which Romania is part of, transparency will increase through supplementary reports making reference to the activities of companies within the group, this determining a risk analysis from a fiscal point of view, especially concerning the manner of allotting revenue, profit and taxes globally.

Transfer pricing, approached from an economic perspective, has utility within the group, being considered an instrument to allot optimum resources within it, being used for touching the established objectives, as well as an instrument to evaluate the performance of joint parties within the group and its managers. The fiscal approach to transfer pricing renders an exterior utility to them, treating them as instruments through which companies stick to market values in order to preserve competivity and the tax basis in the various jurisdictions in which multinationals activate. In practice, the two approaches strongly intermingle. The causes of this strong connection between the economic and fiscal aspects in the field of transfer pricing are various: from costs implied by a separate approach up to companies trying to avoid offering the authorities information that could lead to specific adjustments in the case of transfer pricing.

Even though management and the financial leaders of the companies are aware of the importance of transfer pricing, this policy is seldom taken into consideration in making strategic decisions. The existence of an efficient policy in the field of transfer pricing contributes to a good management of operations globally, representing an instrument used for profit increase - that can be accomplished by raising the turnover and cutting down on costs, taxes and fees by respecting legal provisions.

Taking into account the above issues, the present study aims, in the second section, at shortly clarify the main concepts regarding transfer pricing, some useful aspects of the personnel involved in preparing the documents on transfer pricing and in supporting, eventually, a fiscal control.

Section 3 regards the manner in which the economic approach and/or fiscal one of transfer pricing influences a company. Therefore, the main economic methods to determine transfer pricing are presented, as well as the

types of adjustments that the audit can realize when transactions between joint parties do not respect the principle of market value.

Section 4 of the study aims at stressing the importance of transfer pricing for multinational companies and groups of Romanian companies that have transactions with joint parties and, similarly, it tries to explain the influence of transfer pricing mechanisms on a hypothetical company.

The last chapter concludes the research findings, deepening the idea that transfer pricing leaves room to interpretation, to professional judgment both from the company, as a taxpayer, and the financial audit. Another conclusion of this research is related to the difficulty of choosing the most suitable method of establishing transfer pricing. Transfer pricing policies should be designed by companies taking into account both the economic as well as tax and customs implications.

2. The Conceptual Framework of Transfer Pricing

According to a law definition in the Fiscal Code (Law no. 227/2015 regarding the Fiscal Code), **transfer pricing** is pricing at which *"tangibles or intangibles are transfered, or services are provided"* between companies that are joint parts of the same group (called affiliates).

Transfer pricing, according to the definition of the Organization for Economic Cooperation and Development (OECD) (OECD, Guide, 2017), are *"prices at which an enterprise transfers physical goods, intangible assets or provides services to an affiliated enterprise"*.

The concept of **transfer pricing** refers to a set of laws and practices by which States ensure that the profit obtained from the transferring of goods, services, intellectual property rights, assets, is recorded and taxed where obtained between the joints of the same group. This is a very important aspect, given that transfer prices can determine the profit increase paid by the group in low tax jurisdictions or, conversely, may reduce profits where taxation is high.

By law, transactions between related parties should be concluded at **market price**, namely, the price at which there would have been completed a similar transaction between independent parties in comparable economic conditions. If the transaction price between affiliates is not within the **market parameters**, it is believed that the profits obtained by parties from the transaction are not properly reflected, thereby affecting paid taxes.

The arm's length principle, laying at the foundation of the entire analysis regarding transfer pricing, is to be found in the sample Agreement to

Avoid Double Taxation issued by OECD, as well as in the national legislation. According to this principle, when the established conditions are imposed in commercial or financial relationships between two joint parties it differs from those that would have existed between independent parties; whatever profits that in lack of the respective conditions would have been accomplished by one of the parties, but they were not due to the respective conditions, they may be included in that party profit and taxed accordingly.

The notion **joint** is defined by OECD as *"*two businesses are related if one of the enterprises participates directly or indirectly in the management, control or capital of the other*"* or if *"*the same person participates directly or indirectly in the management, control or capital of both enterprises (namely, if both companies find themselves under common manager)*"*.

In terms of accounting, the International Financial Reporting Standards (IFRS) and the accounting regulations of the Romanian Ministry of Public Finance, Order No. 1802/2014 on the annual individual and consolidated financial statements (Order no. 1802/2014) are harmonized with regard to concepts specific to joint parties, namely: affiliates, associates, jointly controlled entities, related parties. The definitions of these concepts within the Tax Code are made with tax purposes and do not exactly overlap accounting. From a tax perspective, the notion of joint party is defined in the Tax Code and means that a person has at least 25% of the voting rights or as the manager of another legal person.

Market pricing parameters, according to OECD, represent *"a range of values that are acceptable in order to determine if the conditions of a transaction between joint parties respect the principle of market value and which derive either from the application of the same method of setting transfer pricing to multiple comparable data or it derives from the application of different methods concerning the establishing of transfer pricing"*.

The transfer pricing policy can be defined as "a formal document signed by the management bodies of a company which mainly regulates the means to calculate transfer pricing within each category of transactions with joint parties" (Barbosanu and Sbora, 2018). According to the Fiscal Procedure Code (Law no. 207/2015 regarding the Fiscal Procedure Code, as amended and supplemented), the tax payer who makes transactions with joint parties is required to prepare **transfer pricing documentation** and to present it to the fiscal body at request.

If the transfer pricing file aims at proving that transactions concluded with joint parties in the past respects the arm's length principle, **the transfer pricing policy** is used to determine future prices of transactions with joint parties.

Following the analysis of the main concepts related to transfer pricing, notwithstanding the complexity, knowledge and information that an understanding of this area supppose, we reach the OECD conclusion that transfer pricing is not an exact science. This feature of transfer pricing leaves room to interpretation, to professional judgment, both to the company as a taxpayer and the audit.

3. The Transfer Pricing Economic / Fiscal Approach

Analyzing the specialized literature in the field of transfer pricing, two different approaches are to be observed, yet strongly interconnected, respectively: **the economic approach** and **the fiscal approach**.

The transfer pricing economic approach disconnects from the exterior environment (social, political, etc.) in which pricing was produced or used, being considered a strategic instrument used by the managers of multinationals in order to accomplish business objectives, as well as for the monitoring and evaluation of the held parties' performances.

The latest specialized literature deals with transfer pricing as an instrument used by multinational companies in order to relocate profits within the group to the most suitable branch, the purpose being that of reducing costs with taxes and fees at the level of the entire group.

From an economic perspective, the transfer pricing policy can be defined as being "*a formal document signed by the management body of a company that regulates mainly the way of calculating transfer pricing in the field of each category of transactions with joint parties"* **(**Barbosanu, Sbora, 2018) and is used for establishing future pricing of transactions with joint parties.

A series of economic factors influence transfer pricing at multinational company level, such as:

- the innovative nature of goods, products and services exchanged, sold or used;

- market characteristics where transfer, sale or use of goods, products and services take place;

- the position occupied by joint parties in sales transactions, production or distribution, and activities undertaken by them;
- contractual conditions of transfer, namely: payment terms, commercial or financial discounts, granted guarantees, risks assumed;
- risks that arise from long-term relationships in transfer, opportunities and restrictions.

In a multinational company, the prices at which transactions between joint parties may be established:

- without taking into account the risk assumed by the related party or the role it plays in the company;
- in terms of the multinationals' consolidated profit maximization;
- in terms of minimizing due taxes and fees;
- taking into account the costs, profits or market conditions that are no longer valid.

The transfer pricing analysis from an economic perspective in particular is build on microeconomic models trying to identify the optimal method for determining transfer pricing under conditions of variable data about an organization, given the preferences of people involved in decision making processes and other factors affecting the allocation process of resources. The analyzed theoretical models of transfer pricing are useful for understanding the variety of transfer pricing practices as well as organizational approaches.

One of the most popular transfer pricing models is the standard model proposed by Hirshleifer (1956). According to this model, the problem of "*resource allocation*" between company divisions is resolved by "*correct transfer pricing*". Responsible for solving the problem of "*optimization within the group*" is **the headquarters** which has to settle "*the right price" between divisions*. The model leaves way to debate as to why companies do not train their divisions to apply for an optimal production policy in place of coordinating activities through a transfer pricing mechanism. The limits of this model owe to the fact that it does not provide a sufficient theoretical explanation for a decentralized organization. With a perfectly competitive import market, there is no incentive to integrate divisions in one company. Divisions could act independently and get the same profit as if part of an integrated business.

Among the economic models that were subsequently developed, pursuing the overcoming of conceptual deficiencies of the standard model we include:

- **Economic Models of Transfer Pricing under Assimetric Information** (Gox and Schiller, 2006), with representatives such as:

1. Kaplan and Atkinson (1998), who state that *information specialization* is one of the main reasons of decentralization but it causes informational asymmetry between headquarters and divisions. If divisions had more information on cost functionality and their income, then the standard transfer pricing model would be no longer valid because the optimum transfer pricing requires knowledge of the cost function.

2. Vaysman (1996) introduced in the standard transfer pricing model *limited communication*. In this context, decentralization dominates centralization, since decentralized structures use information better, and divisions may base their decisions on messages received from other divisions.

3. Christensen and Demski (1998) have developed a model that focuses on *moral hazard concerns* at the division level. This model formalizes the idea that the distribution of profits is inclined towards the division with the relatively smaller control problem.

4. Wagenhofer (1994) compares several transfer pricing mechanisms in the context of a binary model of adverse selection. It compares basic costs, the dual rate, and market-based transfer prices. This model emphasizes the critical role of different assumptions included in the model for understanding stimulating properties of transfer pricing methods.

5. Schiller (1999) compares a traditional transfer pricing scheme, dependent on the volume of domestic trade with an alternative incentive scheme, using information about the buyer's income. This model shows that the method of allocating costs exceeds the traditional transfer pricing method given the incertitude that income is high or whether the manager holds the control especially with a view to increase revenue.

- **Transfer Pricing Methods Based on Costs**

Transfer pricing based on costs is used by many companies. Some cost-based methods can be applied to companies centralized or decentralized. If centralized, the headquarters of the company have the opportunity to know the exact costs divisions. Lengsfeld, Pfeiffer and Schiller (2006) concluded that transfer pricing must be centralized, it should be based on actual costs, given the fact that the uncertainty is high.

Among the cost-based methods the most important are:

1. **The Method of Total Cost**

a) The method involves determining *transfer pricing including both fixed costs and variable ones*. Mathematically, the calculation formula is as follows: Transfer Pricing = Variable costs + Fixed costs without additions.

This method of measuring transfer pricing is recommended for companies centralized or decentralized but where delegation of responsibility in decision-making is low, or where there are lacks on the external market for the product transferred within the group to benefit from cost centers or between cost centers and profit centers of the company.

b) Another method of total costs accepted by the specialized literature is *the divisional contribution to the overall performance of the company as a whole* (Corlaciu, 2013). According to this method, in determining transfer pricing, it is included, in addition to total costs, also a profit margin in order to provide an incentive to the buyer subunit.

Hart (1995) focused on solving problems between unrelated parties by holding real assets or more generally, by the institutional project. When contracts are incomplete, power and control are the ones that count. Property of assets is a source of strength. Firm boundaries are chosen to optimally allocate power between parties in a transaction. Similarly, there is an analysis of the incentives offered by the alternative transfer pricing mechanism. Holmstrom and Tirole (1991) explore the relationship between divisional investment incentives and the organizational form of the company.

2. **The Method of Standard Cost**

In practice, transfer pricing is often based on the standard cost and not on the real cost. Standard costs are anticipated fixed costs, with value of norms and which are used for the comparison with real costs. Standard costs must be periodically reinforced.

3. **The Method of Variable Costs**

Transfer pricing is established by variable costs and can be efficiently applied when the "selling" division works under capacity. The relation *cost – volume – profit* is the one that governs the production decisions and the ones to subsequently establish prices.

4. **The Method of Marginal Costs**

Marginal Costs are named by some authors also *incremental costs*. Using this method, transfer pricing supposes the identification of that level of production which determines a maximum profit.

Sahay (2003) analyzed a simple policy of transfer pricing, based on the real production cost. Given these conditions, the performance of transfer pricing may be improved by using a supplementary increase, beyond the real production cost.

- **The Method Based on the Market Value**

At first sight, the activities that take place within the group do no seem to have anything in common with the outlet, transactions do not take place under the same conditions to those on the market. Yet, in order to respect the principle of market value, there must be a product or a similar service. In order to apply this method, the market price of the transaction is determined by comparing the selling price of the identic or similar products or services, sold in comparable quantities, with the selling price of goods and services submitted to evaluation. In the case in which quantities are not comparable, the selling price may be used for goods and services identical or similar, sold in various quantities. Therefore, the selling price is to be corrected with minus or plus differences that might be determined by the difference in quantity.

- **The Method Based on Negotiation**

The Edlin and Reichelstein's model of negotiated transfer pricing presents the idea according to which the division managers may make specific investments that should increase the value of trading within the company. According to the two authors, the investments must be made prior to managers obtaining information in order to determine the wanted transfer within the company. The results are efficient given the condition that divisions sign contracts at fixed prices, before the decision to invest is taken. Although these contracts will negotiate, they offer divizions a protection for specific investments. (Edlin, Reichelstein, 1995).

This method supposes a negotiation of transfer prices between the selling division and the buying division. It implies an increased degree of autonomy of responsible centres. In the process of negotiation, the following factors are implied: the market price, total costs, variable costs, opportunity costs (Accounting Details, 2019). The calculus formula of transfer pricing is the following:

For the selling division:

Transfer pricing ≥ variable cost + opportunity cost/unit of product

For the buying division:

Transfer pricing ≤ purchasing price from outer sources

Negotiated transfer pricing depends on the managers' negotiation abilities. The evaluation of division performances will be accomplished by directly implying these aspects, and this will determine a value that does not totally reflect reality.

- **Other Methods** analyzed the stimulating properties of more transfer pricing mechanisms in a given institutional framework**.**

We remember in this sense the Baldenius et al model (1999), which compares the standard transfer pricing, based on decentralized costs with negotiated transfer pricing.

Chwolka and Simons (2003) compare, in the proposed model, the profit distribution, the revenue distribution and transfer pricing in a framework with cross investments.

- **The Model of International Transfer Pricing** presented by Gox and Schiller starts from the idea that the divisions of a company are settled in different fiscal jurisdictions and they present the way in which profit taxation influences the transfer pricing policy. The authors have analyzed, firstly, the factors influencing taxation, the tension between the managerial and fiscal objectives, as well as the way in which the conflict between the two may be solved. (Gox and Schiller, 2006).
- **The Model of Strategic Transfer Pricing** offers an economic reason for **the organization of the profit centre (**Gox and Schondube, 2004**).** Transfer pricing has strategic implications, even if the strategic reason is not the main reason for the organization of the centre profit of a company. These effects must be taken into consideration with attention when a company establishes the transfer pricing internal policy and the the transfer pricing alternative methods.

Accountancy information, as a result of accounting policies adopted by a company, represents the basis of analyzing circumstances in which transactions took place with joint parties and the starting point in drawing the transfer pricing policy. Further on, the transfer pricing policy is drawn taking into consideration the accounting information and the company business strategy. The updating of the transfer pricing policy is permanently made, any time when new transactions appear or for the company's result maximization.

Even though, given the current conditions of transparency and information exchange between States, the companies generally respect the market value principle, it is possible that a method to establish transfer pricing accepted by a fiscal authority is not to be accepted by another fiscal authority. In order to avoid such risks, the existence of a transfer pricing global policy

would allow a multinational company to be consequent and implement the transfer pricing policy locally, in the fiscal jurisdiction it operates in, with more reduced costs and a greater guarantee that it is exempted by the fiscal risk characteristic to transfer pricing.

The Transfer Pricing Fiscal Approach has as main target the argument that the concluded transactions with joint parties respect the principle of market value. Fiscally, in the relation with the audit, the transfer pricing file is used as well as other instruments and in their use, multinational companies try to respect the principle of market value and do not influence the taxes and fees from the countries where a multinational company has activity through its joint parties as follows: the individual anticipated fiscal solution and the advance pricing agreement.

If the transactions between joint parties do not respect the market value principle, the audit will resort to adjustments. According to OECD, there are three types of adjustments, namely:

1. **Primary adjustment**, which according to OECD is "an adjustment to taxable profits of a company that a tax administration of a first jurisdiction brings as a result of the application of market value on transactions involving a joint party, in a second tax jurisdiction". It is the starting point for other types of adjustments.
2. **The second adjustment** is made by the same tax jurisdiction that performs the primary adjustment and represents according to OECD, the “adjustment by which additional profits resulting from the primary adjustment are treated as if they had been transferred into another form and consequently taxed”. The resulting secondary transaction is defined as "a constructive transaction about which some countries will say that it is in agreement with the national legislation having proposed a primary adjustment to make the allocation of profits to be consistent with the primary adjustment". This type of adjustment is regulated by the national legislation on transfer pricing under the form of: dividends, loans, shareholdings.

The national legislation does not provide for such an adjustment.

3. **Cross-Adjustment** is made by the other tax jurisdiction and aims to eliminate or reduce double taxation.

According to OECD cross-adjustment is “the adjusted tax liability of the joint party of a second tax jurisdiction, performed by the tax authorities of the first tax jurisdiction; it corresponds to primary adjustment performed by the

tax authorities of the first tax jurisdiction so that the allocation of profits in the two jurisdictions is uniform".

Cross-adjustment is achieved during the mutual agreement procedure and aims to reduce or eliminate double taxation in cases in which a tax administration performs a primary adjustment, increasing the tax base of a company as a result of the application of market value for transactions with an affiliated party in a second tax jurisdiction. Cross-adjustment is an adjustment of tax liability discount of a related party, carried out by the tax administration in the second jurisdiction, so that double taxation does not occur.

It is also important that fiscal independence should have priority in each OECD member country. Transfer pricing adjustments generate impact on both the income/profit tax and the VAT and customs duties (Șușnea, 2019). According to the EU Directive 2006/112 on the common system of value added tax (EU Directive 2006/112), if in agreement with transfer pricing regulations used for direct taxation the arm's length principle must be respected in all intra-group transactions, according to the VAT Directive, the principle of market value implementation is done to a much smaller extent. According to the VAT Directive, implementing the principle of market value is optional for UE Member States and can be targeted to prevent tax evasion.

In 2015, the World Customs Organization issued Guidelines for determining customs duties and transfer pricing implications. This guide attempts:

- to clarify the way in which the information in the transfer pricing documentation can be used by customs to ascertain whether the goods or services imported were or were not influenced by the relationship of affiliation;
- encouraging cooperation between customs and tax authorities, by mutual exchange of information and knowledge;
- encouraging the issuing of anticipated customs arrangements if the customs value of goods is traded between affiliates of the same group. This tool provides transparency and safety of the customs value.

Analyzing various methods for determining transfer prices, with the advantages and disadvantages of each, we conclude that there is no way to meet all types of transactions taking place between joint parties. Choosing the best method of transfer pricing depends on several factors, such as company strategy, degree of centralization, market conditions where the company operates, the organization of the company (profit centers/cost/revenue centers, investment). A correct determination of transfer prices can be achieved by

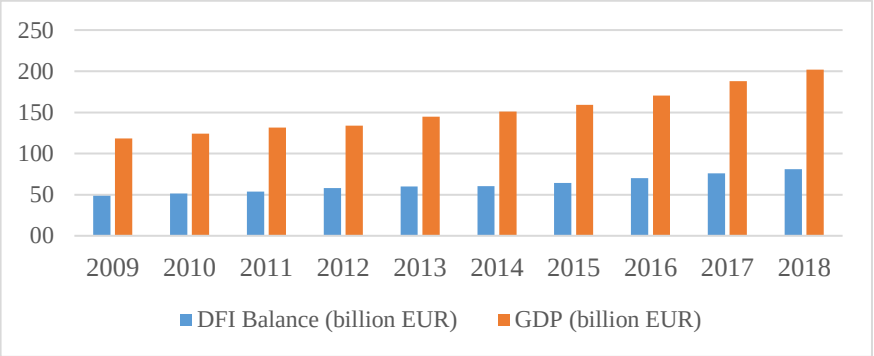
companies taking into account both the economic implications and the tax and customs.

4. The Transfer Pricing Influence over The Company

The problem of transfer pricing is a priority both for multinational companies and for the groups of Romanian companies that have transactions with joint parties.

Analyzing the chart below, regarding the evolution of the balance of direct foreign investments (DFI) in Romania, we observe the important role of multinational companies in the Romanian economy, they realizing numerous intra-group transactions, generating transfer pricing.

Figure 1: The evolution of the DFI balance in the Gross Domestic Product (GDP)

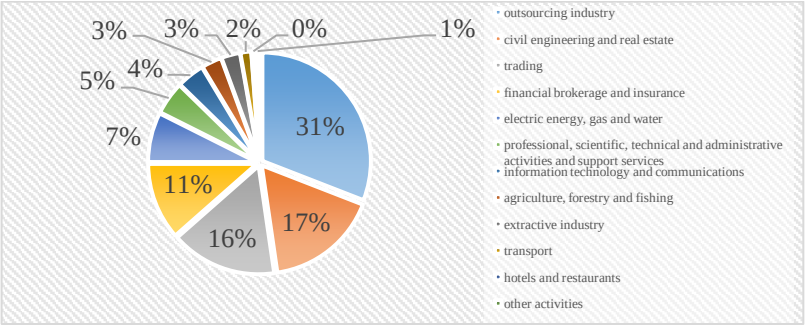


Source: personal processing of data offered by the National Bank of Romania (NBR) regarding DFI in Romania in 2018 and the National Statistics Institute of Romania regarding the GDP

The direct foreign investment represents a sustainable investment relation between a resident entity and a non-resident one. As a rule, implying the investor's exercise of a significant managerial influence in the enterprise he invested in. Direct foreign investments are considered to be the following: the paid up capital and the reserves attributed to a non-resident investor that holds at least 10 percent of the votes or from the subscribed capital of a resident enterprise, the credits from this between this investor/the group he is part of and the resident enterprise he invested in, as well as the profit reinvested by him.

The main economic activities allotting direct foreign investment in Romania in December 31, 2018 are presented below:

Figure 2: DFI balance on December 31, 2018 on the main economic activities



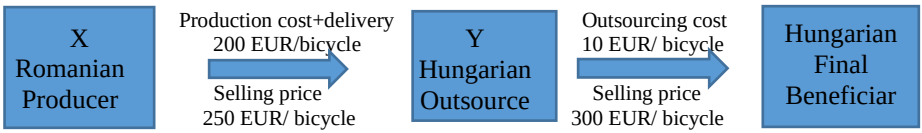
Source: NBR report on Direct foreign investments in Romania in 2018

The audit objective is to tax real profits obtained from deduced profit obtained by independent companies from transactions with their joint parties, being possible to perform due tax and fee adjustments given the situation that prices in practice within group transactions do not reflect the market value principle. These adjustments may lead to double taxation, specific to transfer pricing.

In the following example we will try to explain the influence of the transfer pricing mechanism over a hypothetic company (Feleagă, Neacșu, 2016):

- Company X from Romania is a bicycle producer and they are sold to a joint company Y from Hungary, where they will be outsourced. Company X manages expensed of 200 euros for the production and delivery of one bicycle. Company Y purchases bicycles from X at the price of 250 euros/bicycle and sells them in Hungary at the price of 300 euros/bicycle, managing expenses with a distribution of 10 euros/bicycle. We hereby schematically present the purchase chain:

Figure 3: Purchasing chain (Company Y from Company X)



Source: the author

The results of the group, given the conditions of respecting the market value principle within group transactions, is presented as follows:

Table 1: The results of the group, given the conditions of respecting the market value principle (EUR)

	Analysis in Romania	Analysis in Hungary	Total
Income from bicycles sold	250	300	550
Production + delivery cost	(200)	-	(200)
Purchasing cost	-	(250)	(250)
Outsourcing cost	-	(10)	(10)
Gross profit	50	40	90
Taxed profit	8 (50*16%)	3,6 (40*9%)	11,6
Net profit	42	36,4	78,4

Source: the author

In the analyzed case the transfer price is the selling price of 250 EUR/bicycle.

As observed, the gross profit of the group is 90 EUR/ bicycle, taxed as 50 EUR in Romania and 40 EUR in Hungary. Transfer prices are the ones that determined the profit submitted to taxation in the two countries.

In order that the transactions between company X from Romania and company Y from Hungary should **respect the principle of value market**, it is a must that prices in Hungary for selling the bicycles should level between 249 EUR/ bicycle and 301 EUR/ bicycle (pricing in practice by non-affiliated companies to company Y, which are established on the basis of the analysis of the prices practised on the market.

With a view to cutting down on the fiscal burden at group level, transfer pricing may be used in order to move the tax on profit from Romania to Hungary, due to the fact that the tax rate on profit in Hungary is inferior to that in Romania.

Therefore, company X in Romania sells bicycles at a price of 240 EUR/bicycle. The profit obtained in Romania is consequently smaller, and the tax paid is smaller as well. In Hungary, the purchasing price is smaller, which leads to a greater profit and implicitly to a higher tax on profit.

The results of the group, given the conditions of disrespecting the market value principle within group transactions, is presented as follows:

Table 2: The results of the group - given the conditions of disrespecting the market value principle (EUR)

	Analysis in Romania	Analysis in Hungary	Total
Income from bicycles sold	240	300	540
Production + delivery cost	(200)	-	(200)
Purchasing cost	-	(240)	(240)
Outsourcing cost	-	(10)	(10)
Gross profit	40	50	90
Taxed profit	6,4 (40*16%)	4,5 (50*9%)	10,9
Net profit	33,6	45,5	79,1

Source: the author

Analyzing the data in the above chart we observe the fact that the gross profit of the group did not change. What was changed, in the sense of a subtraction, is the tax paid at group level and the net profit. Transfer pricing is the one that determined the transfer of profits from Romania to Hungary, disrespecting the principle of value market (on the Hungarian market the price of bicycles is somewhere between 249 EUR/bicycle and 301 EUR/bicycle, and company Y purchased them from the affiliated company X at the price of 240 EUR/bicycle).

In conclusion, in order to respect the principle of value market, respectively the prices practised by non-affiliated companies, the audit resorts to transfer pricing adjustment. This supposes supplementary taxes, joined by accessories (interest and outdue penalties).

Transfer pricing affects companies not only fiscal indicators, but also the main performance indicators, cash flow and business strategy. These are the reasons why companies that are part of a group need to argue, in the transfer pricing file, that the practised prices within group transactions respect the principle of value market, with a purpose of avoiding the audit (Luca, Ciocănea, Pițu, 2019).

5. Conclusions

According to OECD, transfer pricing is not an exact science, it leaves room to interpretation, to professional reasoning, both from the part of the company, as a tax payer and the audit. In these conditions, the companies must find new solutions in order to manage accordingly the associated risk of transfer

pricing: regarding the internal management of the company, in the relation with the group (mother company and the joined party members of the group), as well as in the relationship with the audit authority.

Choosing the best method of establishing transfer pricing depends on a series of factors such as: the company strategy, the centralization degree, the market conditions where the company activates, the form of company organization.

Due to approaching transfer pricing from the performance perspective, the company personnel may be motivated in the activity they develop.

The transfer pricing policy must be conceived by companies taking into calculus both the economic and the fiscal and customs implications. Only such a complete approach offers security in the eventual fiscal or customs inspections.

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