INTERNATIONAL TRANSFER PRICING

Transfer pricing refers to the determination of the price at which transaction between related parties will be carried out. Transfer can be from a subsidiary to its parent, from the parents to a subsidiary, or from one subsidiary to another of the same parent. Transfer between related parties are also known as intercompany transactions, it also represents a significant portion in international trade.

Two factors influence the manner in which international transfer prices are determined. The first factor is the objective that headquarters management wishes to achieve through its transfer pricing practices, another objective relates to the minimization of one or more type of cost and these two objectives often conflict.

The second factor is the law that exist in most countries governing the manner in which intercompany transaction transactions crossing the boarders may be priced. These laws are established to make sure that multinational corporations(MNCs) are not able to avoid paying fair shares of taxes, import duties, and they operate in multiple jurisdiction.

DECENTRALIZATION AND GLOBAL CONGRUENCE

Business enterprises are often organised by divisions. A company organized by division, top managers delegate or decentralize authority and responsibility to division managers, advantages of Decentralization includes:

1. Allowing local managers to respond quickly to a changing environment.
2. Dividing large, complex problems into manageable pieces.
3. Motivating local managers who otherwise will be frustrated if asked only to implement the decisions of others.

The corporate accounting and control system should be designed in such a way that it provides incentives for local managers to make decisions which are consistent with corporate goal and this is known as goal congruence.

OBJECTIVES ON INTERNATIONAL TRANSFER PRICING

1. Performance evaluation,
2. Cost minimization

Conflicting Objectives

To minimize cost, top managers must dictate a discretionary transfer price. One of the way companies deal with this conflict is through dual pricing.

Other Cost-Minimization Objectives

They include:

1. Avoidance of Withholding Taxes
2. Minimization of Import Duties(Tariffs)
3. Circumvent Profit Repatriation Restrictions
4. Protect Cash Flows from Currency Devaluation
5. Improve Competitive Position of Foreign Operation.

TRANSFER PRICING METHODS

1. Cost-based transfer price
2. Market-based transfer price
3. Negotiated price