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ASSIGNMENT TITLE: INTERNATIONAL TRANFER PRICING

**SUMMARY OF INTERNATIONAL TRANSFER PRICING**

Transfer pricing refers to the determination of the prices that is used to transact between related parties which could be between the parent and the subsidiary and intercompany transactions which represents a significant portion of international trade. International transfer prices is influenced by the objective the head office wishes to achieve through the transfer pricing and the law that exist in countries governing the way the company crossing their borders may be priced.

Business enterprise are often organized by divisions, each division having division mangers who are responsible for making the decisions that concern their division thereby motivating local managers to response quickly to changing environment. The decision taken by the division mangers should be such that drives towards achieving the corporate goal of the company as a whole and not the division.

There are three transfer pricing methods commonly used. The first is the ***cost based transfer price*** where the transfer price is based on the cost to produce a good and service. The second method is the ***market based transfer price*** where the transfer price charged is based on the price that would be charged to an unrelated customer or services by other companies to unrelated parties. The third method is the ***negotiated price*** where the transfer price is the result of negotiation between the buyer and the seller and maybe unrelated to either cost or market value.

Performance evaluation and cost minimization are the two possible objectives to consider in determining the appropriate transfer price. Performance evaluation explains that to fairly evaluate the performance of both parties the transfer price should be made at a price acceptable by both parties. Cost minimization objective can be achieved by establishing an arbitrarily high price when transferring to a higher tax country and selling at a low price when transferring to a lower tax country. There is an inherent conflict between these two objectives of transfer pricing. To minimize cost, top managers must dictate a discretionary transfer price and this is not a price that has been negotiated by the both parties in the transaction, nor is it based on external market or cost of production. By doing this the performance evaluation objective has not been carried out. One way to deal with this conflict is through dual pricing.

Other cost minimization objectives includes; Avoidance of withholding Taxes, Minimization of import Duties, Circumvent profit repatriation restrictions, Protect cash flows from currency devaluation, improve competitive position of foreign operation.