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DEVELOPMENT OF TRANSFER PRICING RISK MANAGEMENT IN COMPANIES

A. Melnyk

A significant part of world trade is conducted within intrafirm trade on the basis of transfer prices, which results in arising risks of transfer pricing. Their effective management is difficult due to the lack of their identification, classification, measures to reduce them and misunderstanding by company executives of the need to manage them. In addition, constantly growing competition level, unstable market conditions, toughening transfer pricing regulation calls for new approaches to reducing intracompany costs in the transfer pricing process.

The need to manage transfer pricing risks has been substantiated by the author, their main types have been identified and their classification has been presented based on periodicity, occurrence scope, predictability criteria. Tax, currency, reputational, legal and other risks, their sources of occurrence have been analyzed. Growing impact on reputational and tax transfer pricing risks on companies' activities has been shown. Considering the practical experience, subtypes of tax risks, based on a company's asset, has been identified; features of high-level tax-risk operations have been systematized. Measures reducing transfer pricing most frequent risks at the tactical and operational levels of management have been developed. Advantages, disadvantages and peculiarities of advance price agreements have been highlighted; two directions for transfer pricing documentation development have been presented: to be submitted to tax authorities and for internal accounting.

The mechanism of transfer pricing risk management has been formed. In its context the essence of information database development has been studied, methodical approaches to the risk significance valuation have been presented, responsibility distribution principles have been proposed. Application of this mechanism allows improving the efficiency of transfer pricing risk management, reducing its costs and increasing companies' competitiveness.

Keywords: transfer pricing, intrafirm trade, transfer pricing risk management, advance pricing agreement, transfer pricing regulation, tax risk, documentation.

**РОЗВИТОК УПРАВЛІННЯ РИЗИКАМИ
ТРАНСФЕРТНОГО ЦІНОУТВОРЕННЯ В КОМПАНІЯХ**

Мельник А. О.

Значну частину світової торгівлі ведуть у межах внутрішньофірмової торгівлі на основі трансфертних цін, у результаті чого виникають ризики, властиві трансфертному ціноутворенню. Ефективне управління ними утруднено через відсутність їхньої ідентифікації, класифікації, заходів щодо їхнього зниження й нерозуміння керівниками компаній необхідності в управлінні ними. Крім того, рівень конкуренції, що постійно зростає, нестабільні ринкові умови, посилення регулювання трансфертного ціноутворення потребують пошуку нових підходів до зниження внутрішньофірмових витрат у процесі здійснення трансфертного ціноутворення.

Автором обґрунтовано необхідність в управлінні ризиками трансфертного ціноутворення, виділено їхні основні види та наведено їхню класифікацію за критеріями періодичності, сферами виникнення та прогнозованості. Проаналізовано податковий, валютний, репутаційний, юридичний та інші ризики, вивчено джерела їхнього виникнення. Показано зростання впливу на діяльність компаній репутаційних і податкових ризиків трансфертного ціноутворення. З урахуванням практичного досвіду компаній виділено підвиди податкових ризиків, в основі яких лежить актив компанії; систематизовано ознаки операцій компаній із високим рівнем податкового ризику. Розроблено ряд заходів щодо зниження найбільш частих ризиків трансфертного ціноутворення на тактичному й оперативному рівнях управління. Виділено переваги, недоліки та особливості застосування попередніх угод про ціноутворення; наведено два напрями розроблення документації із трансфертного ціноутворення: для подання в податкові служби та внутрішнього обліку.

Сформовано механізм управління ризиками трансфертного ціноутворення, у межах якого вивчено роль і сутність формування інформаційної бази даних, наведено методичні підходи до оцінювання значущості цих ризиків, запропоновано принципи розподілу відповідальності у сфері ризик-менеджменту трансфертного ціноутворення. Застосування запропонованого механізму дозволяє підвищити ефективність управління ризиками трансфертного ціноутворення, знизити витрати на ризик-менеджмент і підвищити конкурентоспроможність компанії.

Ключові слова: трансфертне ціноутворення, внутрішньофірмова торгівля, управління ризиками трансфертного ціноутворення, попередня угода про ціноутворення, регулювання трансфертного ціноутворення, податковий ризик, документація.

**РАЗВИТИЕ УПРАВЛЕНИЯ РИСКАМИ
ТРАНСФЕРТНОГО ЦЕНООБРАЗОВАНИЯ В КОМПАНИЯХ**

Мельник А. А.

Значительная часть мировой торговли ведется в рамках внутрифирменной торговли на основе трансфертных цен, в результате чего возникают риски, присущие трансфертному ценообразованию. Эффективное управление ими затруднено из-за отсутствия их идентификации, классификации, мероприятий по их снижению и непонимания руководителями компаний необходимости управления ими. Кроме того, постоянно растущий уровень конкуренции, нестабильные рыночные условия, ужесточение регулирования трансфертного ценообразования требуют поиска новых подходов к снижению внутрифирменных расходов при осуществлении трансфертного ценообразования.

Автором обоснована необходимость управления рисками трансфертного ценообразования, выделены их основные виды и представлена их классификация по критериям периодичности, сферам возникновения и прогнозируемости. Проанализированы налоговый, валютный, репутационный, юридический и другие риски, изучены источники их возникновения. Показан рост влияния на деятельность компаний репутационных и налоговых рисков трансфертного ценообразования. С учетом практического опыта компаний выделены

подвиды налоговых рисков, в основе которых лежит актив компании; систематизированы признаки операций компаний с высоким уровнем налогового риска. Разработан ряд мероприятий по снижению наиболее частых рисков трансфертного ценообразования на тактическом и оперативном уровнях управления. Выделены преимущества, недостатки и особенности применения предварительных соглашений о ценообразовании; представлены два направления разработки документации по трансфертному ценообразованию: для подачи в налоговые службы и для внутреннего учета.

Сформирован механизм управления рисками трансфертного ценообразования, в рамках которого изучены роль и сущность формирования информационной базы данных, представлены методические подходы к оценке значимости данных рисков, предложены принципы распределения ответственности в сфере риск-менеджмента трансфертного ценообразования. Применение предложенного механизма позволяет повысить эффективность управления рисками трансфертного ценообразования, снизить затраты на риск-менеджмент и повысить конкурентоспособность компаний.

Ключевые слова: трансфертное ценообразование, внутрифирменная торговля, управление рисками трансфертного ценообразования, предварительное соглашение о ценообразовании, регулирование трансфертного ценообразования, налоговый риск, документация.

Over the past few decades, the role of transnational and multinational corporations (TNC, MNC) in the world economy has been steadily growing, which has been reflected in the increasing complexity of the current transfer pricing policy. The issues of effective implementation of transfer pricing and its further management in modern business are becoming more urgent. Such factors as the constantly growing level of competition under the influence of globalization, unstable market conditions, toughening of international and national transfer pricing regulations and others represent the need for company managers to search for new approaches to reducing intracompany costs in the process of transfer pricing system management.

One of the recent approaches to increasing the effectiveness of companies is transfer pricing risk reduction. In domestic companies, problems in this area are related to the lack of such risk identification, diagnostic, prevention and assessment systems, insufficiently elaborated measures to reduce their level, but still the main problem is the lack of understanding by company executives of the necessity and appropriateness of transfer pricing risk management to the same degree as, for example, of currency or credit risk management.

It should be noted that in the context of current struggle for financial resources, neglecting opportunities to reduce transfer pricing risks can cost a lot both for international corporations and Ukrainian companies. Thus, for many domestic companies, the development of a transfer pricing risk management policy is considered to be of live issue and should take into account situation analysis, identification and assessment of possible transfer pricing risks, decision-making on reducing their level, implementing decisions and monitoring their implementation.

The problems of transfer pricing risk management are virtually not covered in the scientific literature. Some aspects are partly mentioned in the works of J. McKinley, J. Owsley, S. Ganguli, W. J. McCarten, J. Cooper, R. Fox, J. Loeprick, R. Feinschreiber, O. Panferova etc.

A number of international documents are devoted to certain aspects of tax risks in transfer pricing: the UN Practical Manual on Transfer Pricing for Developing Countries (2013), the EU JTPF Report on Transfer Pricing Risk Management (2013), the OECD Handbook "Dealing Effectively with the Challenges of Transfer Pricing" (2012), the Code of Conduct on Transfer Pricing Documentation for Associated Enterprises in the European Union (2006) etc.

However, transfer pricing risk management has not been sufficiently studied in the scientific literature: risks have not been systematized, reducing measures have not been developed in companies, and there is no mechanism of transfer pricing risk management.

The research aims to develop the theoretical and methodological foundations of transfer pricing risk management in modern international and domestic companies.

Despite the annual increase of intrafirm trade volumes and, therefore, the practice of using transfer prices, few heads of domestic companies recognize the need for managing transfer pricing risks, which leads to serious financial consequences. According to world statistics, every fifth audit on transfer pricing leads to additional tax charges. For example, with the beginning of transfer pricing legislative regulation in Ukraine in 2013 – 2014, Ukrainian companies paid out penalties of UAH 15.4 mln for violation of transfer pricing rules. In 2015 companies self-adjusted their transfer prices additionally paying out at the time UAH 913.9 mln [1; 2]. By 2016 more than 100 court decisions on transfer pricing in Ukraine were handed down.

According to Ernst & Young company research [3], in 2016 75 % of companies considered transfer pricing risk management to be the most important issue in their transfer pricing policy (compared to 66 % in 2013 and 50 % in 2010 and 2007).

In addition, some companies are not ready for a significant increase in financial, time, labor and other costs that should be allocated to implement an effective transfer pricing policy. Usually the reasons for this are the lack of

practical experience, shortage of specialists with appropriate skills and underestimation of transfer pricing threats and opportunities.

A structured approach to transfer pricing risk management ensures the usefulness of an in-depth study of transfer pricing risks characteristics, complexity of their analysis and assessment, targeting of risk reducing measures and tools at the tactical and operational levels of management, timeliness of adjustment of previously adopted decisions, that will definitely improve management effectiveness of this process.

Transfer pricing risk management is clearly defined as a transfer pricing policy aimed at reducing the possibility of risks emerging and minimizing possible losses in order to enhance a company's competitiveness.

Basing on the conducted analysis of economic literature and companies' experience in transfer pricing, the author identified a number of basic transfer pricing risks and their main sources (Table 1).

Table 1

Types of basic transfer pricing risks and possible sources of their occurrence

Risk	Risk sources
Tax	Transfer price does not correspond to the "arm's length" principle; changes in tax legislation; dual interpretation of some terms (related parties, controlled transactions, distribution of functions, risks, assets between parties to transaction etc.); differences in selection of transfer pricing methods, information sources and characterization of the intrafirm value chain; late submission of documentation, incomplete documentation; frequent changes in transfer prices; refusal to sign advance price agreement (APA) and so forth
Currency	Exchange rate fluctuations due to state regulation and market laws
Market	Price fluctuations at international markets
Credit	Changes in interest rates levels
Loss of profits	Transfer price does not meet the optimal level for better financial results
Political	Changes in the country's trade regime, foreign economic activity regulation, instability in the political situation
Legal	Discrepancies in national and international transfer pricing regulations; protecting intellectual property in conjunction with equity participation in transaction costs, conducting trials through a company's disagreement with tax authorities etc.
Reputational	Formation of a public negative attitude to a company's use of transfer pricing as a means to minimize taxation level
Operational	Data complexity, their restructuring, deficiencies in systems and procedures of transfer pricing policy management
Behavioral	Personnel's low qualification and disloyalty, staff errors, conflict of interests

In order to facilitate identification of transfer pricing potential risks, evaluate their significance and develop effective measures for their reduction by using appropriate instruments, transfer pricing risk classification has been developed (Table 2).

It should be noted that despite numerous theoretical and empirical works on transfer pricing, there have been no attempts to classify transfer pricing risks in the scientific literature. In the proposed classification the most significant features, in the author's opinion, have been highlighted: their periodicity, occurrence area and predictability (Table 2).

Table 2

Transfer pricing risk classification

Feature	Risk type	Risk example
Periodicity	Constant	Fluctuations in exchange rates, discrepancies in national and international transfer pricing regulations
	Temporary	Loss of reputation, loss of profits, conducting litigations, change in interest rates
Occurrence area	External	Change in transfer pricing regulatory legislation, dual treatment of certain regulation provisions, changes in political situation, market prices or interest rates
	Internal	Frequent adjustment of transfer pricing policy, incomplete understanding of its essence, data corruption, commercial information leakage, underdeveloped software
Predictability	Predictable	Mismatch between the chosen methodology for calculating transfer prices and the economic nature of operations, loss of reputation, operational and behavioral risks
	Unpredictable	Changes in political situation or tax legislation; double interpretation of laws

Let us examine in detail the most common types of risks in the practice of companies which they can influence.

Legal risks resulting from differences in national legislations on transfer pricing are linked with complying with rules and regulations in different states. Divergences in national standards (for example, in rules for allocating costs and risks between transaction parties, methods of determining whether a transaction reflects the "arm's length" principle and so forth) increase compliance costs for international companies comparing to companies operating in one country. In the event of a company's disagreement with the tax authorities' decisions, the risk of resolving the dispute in court occurs.

The risk of lost profits develops when transfer price is within the benchmark of limits set by law,

but is nonoptimal for improving financial results of the group of companies.

This risk may also include incomplete capacity utilization threat, their downtime because of setting inflated transfer prices between companies, divisions. In this case, companies can choose external market, subject to its availability, for purchases in order to minimize their own costs.

Currency risks affect transfer pricing through nonsufficient income generation due to exchange rate fluctuations. Conversion currency risk is related to currency losses for particular transactions; translational – to losses in revaluation of assets, liabilities, profits of foreign affiliates, representative offices, subsidiaries in national currency during the drafting of consolidated corporate balances.

Exchange rate fluctuations also create additional taxation threat: for example, when the national currency is devalued, foreign exchange losses that are included in the operating expenses structure underestimate a company's operating profitability, which causes a discrepancy in the market price range for the taxpayer. As a result, additional taxes arise.

Particularly vulnerable to such risks are companies that are part of TNC, whose activities are aimed at importing goods from related parties and their further resale at the Ukrainian market. Often, such companies are characterized with a high level of accounts payable in foreign currency to related nonresident parties for the delivered products in transactions subject to transfer pricing control. The recalculation of such currency debt leads to certain difficulties [4].

Well-known large companies, TNC and MNC are often exposed to reputational risk. It is that a company can lose income or suffer losses as a result of damaged image. Transfer pricing litigations are loud and have a negative impact on a company's business reputation, entailing its market value decline and business let-down. It should be understood that regardless of court decisions, even if a company proves its transfer pricing legitimacy, its reputation will be at risk in any case.

The most illustrative story here is presented by Starbucks which did not recognize the tax authorities' claims to pay corporate tax in the UK (the company withdrew profits from the UK through high transfer prices to its offices in low-tax jurisdictions: to Holland through royalty, to Switzerland through the coffee beans purchases, besides, paid inflated interest rates on borrowings). As a result of public resistance expressed in the form of the company's negative criticism in social networks, press and other media, boycotting its products and public appeals to pay all taxes honestly, Starbucks announced that it would voluntarily pay \$16 mln "extra taxes" in 2012 in order to maintain their reputation.

A number of other well-known companies, among them Amazon, Google, Microsoft, Oracle, Fiat, also undergo such severe public criticism. Some companies manage to defend their position, such as Amazon, which won a \$1.5 billion lawsuit in 2017, while others have to pay addi-

tional taxes. For example, in 2017 Google should pay GBP 130 mln of corporate taxes for 2005 to 2015. Considering that the company paid about GBP 200 mln in taxes in the UK for this period with a gross income of GBP 24 bln from the activity within this territory, and its branch in Holland (where the company's bulk profit was transferred through royalties) paid only EUR 2.8 mln, the public considered these measures being too soft [5].

Reputational risk is not static, it changes in accordance with public expectations, and a key characteristic of present-day reputational risk is assessment of a company transfer pricing strategy from positions of fairness, social responsibility and corporate ethics. Shifting profits to low-tax jurisdictions by large TNC and MNC in order to avoid taxation increase tax burden on small companies and citizens, and these issues are becoming a matter of concern not only to regulators but society as a whole.

In other words, if a company, according to public opinion, does not contribute a fair share of taxes, it may face reputational risks. Thus, there is a shift in public opinion regarding transfer pricing from the tax plane to the corporate social responsibility, which in general corresponds to the latest trends of international business development.

Therefore, companies must adapt transfer pricing strategies so that they meet simultaneously the following basic principles:

- 1) follow a company's goals (maximize profits, gain market share and so forth);
- 2) stay within the law;
- 3) comply with the corporate social responsibility concept.

The main transfer pricing risks lie in the tax plane. And although taxation optimization is not the only purpose of applying transfer prices in Ukraine (other purposes are often protecting company's assets from corporate raids and unfair competition, optimizing intrafirm management accounting to improve efficiency, etc.), tax risks are inherent in any company. That is why considerable attention should be paid to their consequences and development of effective measures aiming to minimize the threats.

The purpose of tax risk management is carrying out a transfer pricing policy that will comply with the national tax legislation and will effectively optimize a company tax burden.

According to world statistics, 89 % of tax authorities consider transfer pricing as one of the five maximum tax risks of companies [6]. Relying on frequently changing legislation, tax authorities closely study transfer prices, avoiding tax evasion within the framework of intragroup trade, which leads to transfer prices adjustment, additional taxes and penalties. Despite high risks, only about 14 % of companies monitor the national transfer pricing laws update [7].

So, as a result of tax inspections on transfer pricing and error detection in financial statements in 2002, the American company WorldCom went bankrupt, paying out \$ 3.8 billion [7].

Other cases of tax risks occurrence are also well known.

GlaxoSmithKline Group was additionally taxed and fined \$ 3.1 billion for 1989 – 2005 due to a change in the method of calculating transfer prices from the resale price method to the residual profit split method. The Tax Service carried out a functional analysis and considered that marketing strategy development by the parent company in the US had a significant impact on the creation of a long-run demand for medicines (despite the fact that their production and distribution took place outside the US), so the parent company deserved higher gross profit value and, accordingly, higher tax payments.

In 2015, Chevron paid a 25 % fine of the company's outstanding tax liabilities in Australia due to its receipt of intragroup loan under nonmarket conditions and profits transfer afterwards in the dividend form in order to avoid taxation. A loan of AUD 2.5 billion was received with no guarantee or collateral, without hedging currency risks, at an inflated interest rate, while the Australian subsidiary had 47 % of debt to equity. The profit from that loan received by the financial company was transferred as a non-taxable dividend to an Australian company, and the latter in turn paid dividends to the parent company throughout the period of the loan [8].

The widespread tax risks of transfer pricing allows us to identify their subtypes based on a company's asset:

- transactions with tangible assets (goods, raw materials, etc.);
- transactions with intangible assets (license transfer, royalty payment, etc.);
- capital transactions (for example, overvalued interest rate on intrafirm loans);
- service delivery (intragroup transfer of marketing, management services, etc.).

Management approaches to these types of risks will differ. When transferring intangible assets, services, capital transactions tax risks are significantly higher than when performing transactions with tangible assets. This is primarily due to insufficiently developed international and national tax laws in the part of determining fair prices for these assets and practical difficulties in introducing the "arm's length" principle to these transactions.

Summarizing the theoretical and practical experience of companies and tax services interaction on transfer pricing issues [8 – 10], one can clearly define the features of transactions with a high level of transfer pricing tax risk:

- transactions related to business restructuring: new structures and business models creation, business restructuring (for example, corporation reorganization with transferring commercial activities to foreign jurisdictions);
- transactions related to intangible assets transfer and payments on them (special attention is paid here to the methods of transfer price calculating: as a rule, tax services negatively refer to the methods of "costs plus" and resale prices, preferring to apply transactional profit methods);

- transactions with related parties from low-tax jurisdictions and offshores;

- transactions with ambiguously interpreted financial results: financial indicators do not meet industry standards, similar indicators of comparable companies, the overall performance of the group of companies; unreasonable fluctuations in profits/losses; long-term costs without further profits (for example, a long-run low return on investment);

- capital transactions: borrowings with a company's insufficient capitalization (for example, a company's borrowings amount is higher than it had to be taken); high interest rates on loans; intragroup loans, guarantees, receivables on a noncommercial basis; operations of an inactive company which is a lender within a group of companies etc.;

- nonstandard transactions that are difficult to track or correctly report: provision of intragroup services (for example, irrevocable financial assistance, management services, insurance premiums); transfer of mobile assets, property rights; other operations on a noncommercial basis without concluding a contract or generating revenue.

This list is not exhaustive, but covers only the most significant features of the potential tax risks of transfer pricing.

The main transfer pricing risks and proposed measures of their reducing are presented in Table 3.

Special attention should be given to advance price agreements – APA, which are being activated in developed countries due to toughening the regulation rules, and in Ukrainian realities they remain an insufficiently studied mechanism for reducing transfer pricing risks.

The aim of APA conclusion is to resolve potential transfer pricing disputes between companies and tax authorities in advance by agreeing on clear rules and methodology for determining transfer prices and their adjustment.

As a result of APA conclusion some companies receive not only certainty in their interrelation with tax authorities, but also tax benefits.

In 2016, the British pharmaceutical company AstraZeneca received a tax benefit of \$453 mln as a result of a multilateral APA conclusion with Canada, Sweden and the UK. The US transport company United Parcel Service reduced its effective tax rate from 35.5 % to 34 % in 2015 thanks to the APA [11]. In general, many TNC and MNC – Sony, Nike, Apple, ASML and others – use APA agreements to minimize transfer pricing risks.

In APA, the following is agreed: transfer pricing methodology; a list of information sources that can be used to justify the price level; permissible deviations from the established transaction terms; critical assumptions by which, in the case of arising, tax authorities have the right to adjust transfer prices (for example, discounts more than a certain percentage, a loan at a percentage over the established one). In addition, there is a mandatory procedure for monitoring and ensuring compliance with APA conditions.

Table 3

Measures for reducing transfer pricing risks

Risk essence	Measures for reducing transfer pricing risks
Deterioration in the business environment and market value decline due to reputational losses	<ol style="list-style-type: none"> 1. Develop a communication plan on transfer pricing in PR activities (includes company interaction with tax services, shareholders, press and other stakeholders). 2. Develop clear and accurate transfer pricing documentation demonstrating the company's intentions. 3. Comply with the corporate social responsibility concept
Income losses due to currency fluctuations	Use contract currency clauses, parallel loans, self-insurance, netting, selection of payment instruments, forms and terms, stock exchange methods (forward, futures, options contracts), manipulate payment terms and so forth
Underestimation of a company's operating profitability resulting in additional taxes	<ol style="list-style-type: none"> 1. Use the gross profitability to exclude the impact of exchange losses. 2. Calculate the average operating profitability for several years to smooth out the impact of exchange losses. 3. Artificial increase in operating profitability due to exchange losses compensation, forgiveness of accumulated accounts payable etc. by a nonresident related party
Discrepancies in national and international transfer pricing regulations	<ol style="list-style-type: none"> 1. Develop coordinated transfer pricing documentation taking into account initiatives and requirements made by the OECD, the UN, the EU. 2. Monitor law changes and court decisions on transfer pricing. 3. Timely coordinate and regulate transfer pricing policy of a company in accordance with external changes
Profit losses, incomplete capacity utilization due to setting nonoptimal transfer price	<ol style="list-style-type: none"> 1. Control and adjust a company transfer pricing policy. 2. Comply with the corporate social responsibility concept
Additional tax charges through the dual interpretation of laws	<ol style="list-style-type: none"> 1. Increase the information transparency level, an open position of cooperation with tax authorities. 2. Develop a sound transfer pricing policy, qualitative transfer pricing documentation in the company. 3. Sign APA with tax services
Additional tax charges due to differences in the choice of transfer pricing methods, information sources and characterization of the intrafirm value chain etc.	<ol style="list-style-type: none"> 1. Justify the transfer pricing methodology: account for the economic essence and terms of operations, draw on comparable operations and other evidences. 2. Optimize a company's business model (analyze ownership structure, economic relationships, assets, functions and risks distribution within a group of companies etc.). 3. Analyze preliminary taxation particularities of company's counterparties, the nature of related relationship with them
Transfer price does not correspond to the "arm's length" principle	<ol style="list-style-type: none"> 1. Self-adjust the taxable base taking into account changes in the level of market or transfer prices, legislative regulation and other factors. 2. Sign APA with tax services
Fines due to transfer pricing documentation problems	<ol style="list-style-type: none"> 1. Timely submit complete and clear transfer pricing documentation to tax authorities. 2. Increase the information transparency level, an open position of cooperation with tax authorities
Behavioral risks through personnel's low qualification, conflict of interests	<ol style="list-style-type: none"> 1. Train staff responsible for transfer pricing policy at training sessions, seminars, conferences; study both national and international experience. 2. Develop a communication procedure between departments and branches of a company within the transfer pricing policy; implement internal arbitration aiming to eliminate conflicts of interest. 3. Develop an internal document regulating the principles of transfer pricing policy in the company
Operational risks	Purchase, develop, improve transfer pricing software, which considers business needs

APA's shortcomings include long duration and time-consuming procedure for agreeing all forthcoming operations terms, although practical experience shows that tax audits take more time and effort from companies.

But APA has a number of significant advantages:

- complete elimination of transfer pricing tax risks (subject to the agreement provisions, tax authorities have no right to adjust transfer prices);

- cost reduction of transfer pricing risk management;

- absence of payment for APA consideration and conclusion (unlike many countries, where this procedure is chargeable for companies);

- voluntary character of APA (revocation, cancellation, revision of terms are possible in case of changing business conditions in a certain period of time in the future).

APA can be considered as a powerful administrative mechanism for resolving transfer pricing disputes during the planning phase of transfer pricing risk management. APA is particularly effective in cases of high probability of transfer pricing tax and legal risks, large volumes of controlled transactions. Using APA by companies after going through costly litigations with tax authorities whereupon charging additional taxes and penalties has become the trend of recent years.

Development of clear and accurate transfer pricing documentation is an important and often underestimated instrument for reducing tax, reputational, legal and behavioral risks in this area. Two directions of documentation development can be segregated here.

1. Transfer pricing documentation in accordance with national legislation aimed to tax authorities' submission in order to justify price levels in controlled transactions, which includes:

- "master file" with basic information on MNC international operations and the principles of its transfer pricing policy;
- "local file" with information on essential transactions between related parties, the amounts of such transactions, transfer prices analysis in these transactions;
- "country-by-country" report which discloses intragroup information for companies with consolidated revenues of more than EUR 750 mln (income received from related and independent parties, profits, taxes paid, employees, declared capital gains and retained earnings, tangible assets in each jurisdiction where they conduct business etc.).

Transfer pricing policy documentation, its accurate and timely submission provides tax services with information support of audits which reduces tax and legislative risks in this area.

2. Internal transfer pricing documentation – Policy, Regulation, Code of Regulations etc., regulating the nature and principles of transfer pricing policy in company. Development and implementation of this document significantly facilitates understanding of transfer pricing as a management accounting instrument within the company, ensures coordination and helps to reduce companies' behavioral and reputational risks.

Aside from reducing measures, a risk avoidance strategy is also possible, depending on the circumstances. In Ukraine this strategy consists in avoiding transactions with related parties from the low-tax jurisdictions list approved by the Cabinet of Ministers on September 16, 2015, with a volume exceeding UAH 10 mln per year with each counterparty and with the annual company income of UAH 150 mln and more, i.e. avoiding such conditions under which operations are considered to be controlled, in accordance with Article 39 of the Tax Code of Ukraine.

World experience indicates the importance of implementing a risk analysis on an ongoing and systemic basis [12], which is possible through development of coherent rules and decision-making procedures by persons responsible for transfer pricing risk management.

Based on the developed risk identification and classification, a list of measures to reduce them, a mechanism for management decision-making was created, which will make it possible to effectively determine transfer pricing risks and minimize them (Fig. 1).

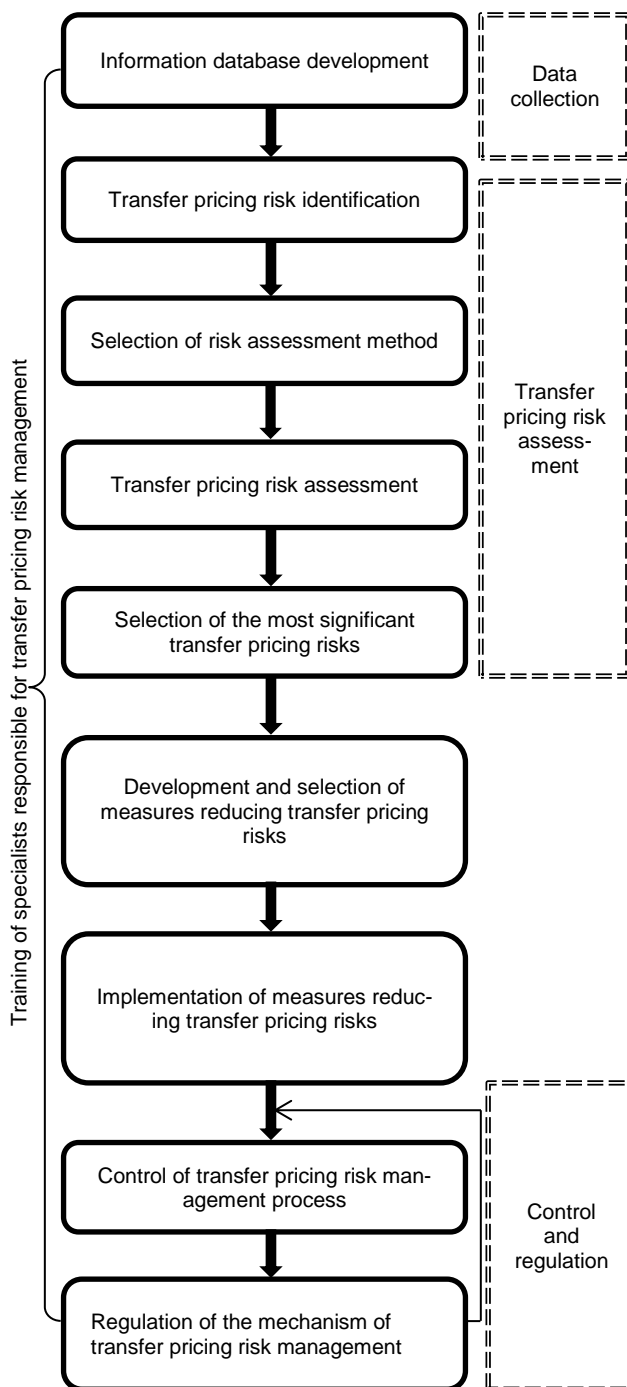


Fig. 1. The mechanism of transfer pricing risk management

Consider the most significant and often underestimated by domestic companies stages of this mechanism.

The first most important stage – information database development on transfer pricing risk management – makes it possible to minimize costs of potential risk definition and assessment, select possible mitigation measures. This stage includes: modelling financial processes, financial strategies, algorithms for conducting functional and economic analysis, factors and parameters for identifying risks, methods for minimizing them, monitoring financial information of competitors, market prices and so forth.

While searching for necessary information, Ukrainian companies should pay more attention to international information sources of world prices with a high degree of trust: Thomson Reuters, Zepol, Platts, Metal Bulletin, Argus, ICIS Pricing, Amadeus, Ruslana, Orbis Bureau Van Dijk, statistics of international exchanges and other recognized databases.

This stage also includes software development (improvement) with the aim of automating transfer pricing procedures. Typically, large corporations optimize information system movement with an additional software module that includes online database embedded in the ERP systems (Enterprise Resource Planning). Examples include One-Source module from Thomson Reuters, TP Catalyst from Bureau Van Dijk and other software solutions.

Based on the analytical processing of quantitative data, further stages of risk identification and assessment, as well as selection of the most significant risks and development of measures to reduce them, take place.

Domestic companies estimate the significance of transfer pricing risks, most often, by the criteria of the maximum possible damage and probability of risk occurrence. International experience presupposes a choice between transactional, jurisdictional and risk-oriented approaches [10].

According to the transactional approach, either simple risks with minimal costs or high income risks are chosen (for example, restructuring business processes).

The jurisdictional approach supposes that risks of transactions with related parties from low-tax jurisdictions and offshores are primarily analyzed.

A risk-oriented approach takes into account both principles of the first two approaches, as well as other factors.

Given the high level of transfer pricing risks in Ukraine, which manifests itself in frequent legislation changes, insufficient qualifications shown by tax inspectors and domestic companies' employees, it is advisable for companies to adopt a risk-oriented approach to the selection of significant transfer pricing risks, which will consider many other factors, except for the type of risk transactions or transactions with related parties from low-tax jurisdictions.

This approach is justified in a rapidly changing environment as long as Ukrainian norms, procedures, rules and judicial experience in transfer pricing topic do not stabilize and will correspond to global practice.

Feedback in the mechanism of transfer pricing risk management is provided through control and regulation. Control includes effectiveness evaluation of all phases of this mechanism, as well as monitoring occurrence of new risks. An effective form of control can be templates for transfer pricing risks that contain information on each type of risk: its features, quantitative and qualitative assessment methods, measures for reducing it and other necessary information. These templates can be created in the process of collecting information, analyzing and assessing risks and will significantly facilitate transfer pricing risk management in companies in the future.

During the regulation phase all procedures, principles, rules, methodology of transfer pricing risk management must be constantly adjusted considering the internal and external changes. Alongside all stages company's employees should be trained and upgrade their skills.

The issue of distribution of authorities and responsibilities in the transfer pricing area is settled individually in different companies. According to some estimates [6], 30 – 40 % of international corporations turn to external independent experts for effective transfer pricing policy planning and organization; about 16 % of companies outsource transfer pricing risk management services. At the same time, it is noted that the cost of outsourcing transfer pricing management services as a whole has grown by 20 % over the past two years while the effectiveness of its control and regulation has decreased. Among the reasons for this, experts mentioned increased costs for outsourcing and insufficient understanding by external consultants of the economic nature of business processes within the company, including intrafirm value chains, hidden intellectual property and other highly specialized aspects of companies' activities.

In the case of using their own workforce in large companies, the staff's number of categories involved in transfer pricing management reaches 30, including economists, accountants, lawyers, risk managers, programmers, information security specialists and tax planners, engineers, financiers, marketers, auditors and so forth [13].

Since the transfer pricing policy is characterized by a number of factors affecting it, some general principles for allocating responsibility in the transfer pricing risk management have been proposed.

1. Outsourcing of transfer pricing risk management services is more profitable at the stage of transfer pricing risk management implementation in medium-sized companies conducting standard controlled operations with small volumes and low frequency.

2. Using their own workforce, creating a transfer pricing department within the company, including managing transfer pricing risks, is more efficient for large international companies (TNC, MNC).

3. At the functioning stage of transfer pricing risk management in medium-sized companies, a combination of two approaches is possible: periodic consultations

with independent experts in controversial issues, when conducting nonstandard controlled transactions and routine operations maintenance by their own workforce.

Thus, transfer pricing risk identification and classification, the analysis and development of measures reducing them have made it possible to create a mechanism of transfer pricing risk management and study its main stages. Transfer pricing risk management based on this mechanism will help to build an effective transfer pricing policy in companies, reduce risk management costs, which eventually will increase competitive strength of the companies.

Further researches in this area include examining the peculiarities of transfer pricing risk management in operations with intangible assets, capital and service delivery, which are currently understudied but considered to be of particular relevance for Ukrainian companies.

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РЕАЛІЗАЦІЯ ПРИНЦИПУ СОЦІАЛЬНОЇ СПРАВЕДЛИВОСТІ В ОПОДАТКУВАННІ ФІЗИЧНИХ ОСІБ

**Сідельникова Л. П.
Найденко О. Є.**

Проблема реалізації принципу соціальної справедливості в оподаткуванні сьогодні постає особливо гостро, оскільки розмір середньої заробітної плати в Україні, порівняно з багатьма країнами ЄС та світу, є значно нижчим. У зв'язку із цим, виникає необхідність дослідити, яким чином в українському податковому законодавстві реалізовано принцип соціальної справедливості.

Із ухваленням Податкового кодексу України принципи побудови та призначення системи оподаткування було замінено на принципи податкового законодавства. Наявне сьогодні визначення принципу соціальної справедливості майже не відповідає своїй сутності, оскільки податки, установлені в Україні, не прив'язані до показника платоспроможності платників податків.

Переходячи у 2004 році до пропорційної системи оподаткування доходів фізичних осіб, держава намагалася забезпечити вихід із тіні значної кількості доходів платників податків. Але, як виявилось, зростання надходжень податку на доходи фізичних осіб було зумовлено підвищенням заробітної плати, а не збільшенням довіри платників податків до держави.

Проблема соціальної справедливості в оподаткуванні фізичних осіб в основному полягає у відсутності в українському податковому законодавстві неоподатковуваного мінімуму доходів громадян, що зобов'язує майже всіх фізичних осіб сплачувати податок на доходи фізичних осіб, незалежно від розміру заробітної плати (винятком є особи, у яких, завдяки застосуванню податкової соціальної пільги, базу оподаткування може бути зменшено).

Окрім того, слід зауважити неврахування в системі оподаткування фізичних осіб різного розміру заробітних плат, сплачуваних в різних регіонах України, що призводить до значного розриву між середньої заробітною платою в центральних та західних регіонах України.

Тому авторами обґрунтовано запровадження в Україні єдиної ставки податку на доходи фізичних осіб на державному рівні та регіональної надбавки з урахуванням показників соціально-економічного розвитку регіонів.

Ключові слова: соціальна справедливість, принципи оподаткування, концепції соціальної справедливості, податок на доходи фізичних осіб, мінімальна заробітна плата, середня заробітна плата.