

International Corporate Structures

The monthly newsletter for clients and friends of LCN Legal
and for anyone involved in creating and maintaining corporate structures.

January 2018

Get in shape for 2018



When I started out as a corporate lawyer in the early 1990s, it was all about one-off transactions and projects: helping clients to buy companies, set up joint ventures, appoint distributors, appoint agents. Most of those clients were German, Swiss or Austrian; some were well-known companies, but more often they were established 'Mittelstand' companies which were expanding internationally. After I joined KPMG's law firm in 2001, my focus shifted to internal legal structures within large corporate groups, working alongside international tax teams. It was a more holistic view, but also more tightly defined.

Now, with my colleagues at LCN Legal, the essence of our work is as much about international intercompany governance (designing, implementing and maintaining structures), as it is about corporate law. And of course clear intercompany agreements are a key tool for intercompany governance, because without those agreements,

parent and subsidiary boards have no firm reference point for considering and approving intercompany relationships.

We've chosen the theme of 1980s fitness icons to help celebrate the New Year... and to reflect the annual surge in gym membership which takes place every January. The 'body beautiful' is also an analogy for the health of a 'body corporate'. The legal, governance and accounting structure of a group may not be its beating heart or its muscles – but it can be likened to its circulation system, bones and ligaments: the conduit for interacting with the outside world, and the means of transmitting life blood around the body.

We come across a lot of 'corporate bodies' here at LCN – the good, the bad and the ugly (or maybe more fittingly: the toned, the flabby and the dysfunctional). Many of our larger clients have well-established teams and documented processes in place to align intercompany legal governance with commercial and tax objectives, and our role is to give guidance as to how those systems and documents may need to be re-aligned or improved. Other corporates may be at a less

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advanced state of compliance, or may have more modest needs – in which case more root-and-branch approach will be required.

Fitness is not a destination, it's a process. It's dynamic, not static. You can't expect consistent good results if you create appropriate habits in just one area – such as exercise – without also creating appropriate habits in related areas, such as diet, sleep and mental wellbeing. The same applies to corporate structures.

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Paul Sutton is co-founder of LCN Legal and a corporate lawyer with over 20 years' experience of international corporate structures, including as a Director of KPMG's law firm in the UK and as a corporate partner in international law firm Pinsent Masons. He has lead the legal aspects of group reorganisation projects involving assets totaling over US\$25 billion and is a contributor to the LexisNexis online Transfer Pricing resources.



Paul Sutton

Paul Sutton
Co-Founder, LCN Legal

"You've got big dreams, you want fame. Well fame costs, and right here is where you start paying: in sweat."

Lydia Grant,
'Fame'

Case study: The impact of financial records and subsidiary governance on Transfer Pricing risks



By **Paul Harrison**,
Tax Director at Trident Tax
www.tridenttax.com

Defining what is arm's length in a modern, digitalised, global economy is clearly one of the major tax questions of our time. However, a more practical question which is overlooked at great risk to the multi-national enterprise (MNE) is this: has the transfer price been accurately captured in the prime records and financial systems of the MNE, and then reported accurately in its tax returns?



This challenge is illustrated with an example, based on a very significant project I led as an advisor working alongside senior management in a US headquartered MNE with significant operations around the world.

Aspects of the MNE's transfer pricing affairs were technically complex, but the problems arose in an area of relative simplicity: allocation of costs borne in the UK to overseas legal entities benefitting from the expenditure. The MNE's transfer pricing policy, agreed with relevant tax authorities, was that these costs would be charged out in full with a fixed % mark up. The MNE discovered, almost by accident, that very significant costs had been incurred in the UK and had not been captured for inclusion in the charge, over a period of years. This resulted in a substantial understatement of UK taxable profits.

The root causes of the errors were identified at three levels:

1. Some basic financial processes had not been operated in line with existing policies and procedures. Most significantly, cost centres had been set up without correct identification so were not picked up by financial controllers, thereby understating the revenues of the UK legal entity.

2. The board of the UK legal entity had exercised inadequate governance over the affairs of that company: they had not focused sufficiently on the trading terms between the company and its sister entities and the impact of those on legal entity costs and revenues. There was no evidence of properly constructed and executed legal agreements, or that these matters had featured at all in the deliberations of the legal entity board.

3. At the whole-enterprise level (notably at HQ level in the US) there was inadequate attention paid to governance at subsidiary legal entity level; no risk assessments had been conducted and there was no clear main board ownership of the need to support subsidiary legal entity governance (which underpinned the lack of focus at local level). For example, substantial operations had been offshored without adequate risk assessment or change management (which underpinned the breakdown in some basic financial processes).

The MNE needed to reassure the UK tax authority that a remediation plan was in place and would be executed to remedy the situation. This required substantial resources and external validation. It is not difficult to link this to the Senior Accounting Officer regime in the UK, which requires certification that reasonable steps are being taken to establish and monitor accounting arrangements which are capable of producing materially accurate tax returns.

It seems clear that global tax authorities will be focusing very keenly on MNE transfer pricing issues, not least as Country-by-Country reporting starts to kick-in. It also seems highly likely that any challenge to MNE transfer pricing will include not just the 'technical' questions around what is the appropriate arm's length price, but also on establishing whether the MNE has in fact executed its asserted pricing from prime records to tax returns. MNEs failing to focus on the practical aspects of this challenge will face the real prospect of significant penalties if they cannot sustain their positions – and at least in the UK this would also put the CFO/SAO at risk of personal liabilities.

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For a real-life example of the link between governance and tax risks, see the article above kindly contributed by Paul Harrison.

We're here to help with the process of getting your corporate group fit and healthy, so that it can face 2018 in the best possible shape – and to invite you to join us in celebrating the exuberance of some of our favourite fitness icons from the 1980s. **Enjoy!**

TOP TEN 80'S FITNESS ICONS

Here's a very personal list of our favourite fitness icons from the 1980s



1.
Mr Motivator



6.
Jean-Claude van Damme



2.
The Green Goddess



7.
Richard Simmons



3.
Mad Lizzie



8.
Sylvester Stallone



4.
Jane Fonda



9.
Hulk Hogan



5.
Arnold Schwarzenegger



10.
Olivia Newton-John



Interview with BA Baracus from the 'A' Team

We are delighted to feature an interview with **Mr. B A Baracus**, who is now an extremely successful corporate lawyer with LCN Legal, following his long career with the 'A' Team.

How did you become a corporate lawyer?

Everything started as a dream. You gotta have insight, know what you want. You gotta have a plan. I met the girls and guys at LCN Legal and I said to myself "They're on the jazz. I gotta be like them." Now I am. Now I got respect.

Who has been the most influential role model for your personal life?

My parents. Because of them we didn't starve. We spent wisely. Like I tell people, "If you can buy guns and bullets, why can't you buy food?" People go out and get a fancy car and all that. The car costs more than their house. Meanwhile, your kids need shoes. That's not cool.

What's the biggest issue for multinationals in creating an effective corporate structure?

Man, it's all the jibba jabba in their intercompany agreements. I ain't got time for no jibba jabba. I pity the fool who doesn't update their intercompany agreements in time for when the tax man comes knockin'!

What's your biggest extravagance?

It's gotta be my gold chains!

In a movie of your life story, which actor would you like to play you?

Not Sylvester Stallone, that's for sure! Lawrence Tureaud is pretty cool.

What's your favourite holiday destination?

All I know is, I ain't gettin' in no airplane.

What do you do to relax?

I chop down trees. In the US Army, one of my punishments was to cut down trees until they told me to stop. The fools forgot to tell me to stop and I cut about seventy trees in twelve hours. Since then, I always get a kick from chopping down trees!

What piece of advice would you give your 18-year old self?

I'd tell him "If I fought every time somebody called me a name, I would never get out of jail. But you're disciplined. You're smarter than that. When you see who called you the name, then you understand why they're doing it. Then you don't have to stoop that low."

WORD SEARCH

N	R	U	B	E	H	T	L	E	E	F	J
K	O	S	S	C	I	B	O	R	E	A	B
Y	L	R	I	P	Y	X	S	S	Z	E	O
J	L	E	I	G	A	L	A	Z	Y	I	O
H	E	M	S	G	L	N	E	J	P	P	G
U	R	R	K	A	N	R	D	E	U	I	I
A	D	A	T	S	C	I	Z	E	Q	L	E
D	I	W	L	I	L	T	P	L	X	F	B
G	S	G	S	E	N	A	S	M	X	O	O
N	C	E	R	J	H	F	S	X	U	N	D
R	O	L	U	S	T	C	O	I	Q	P	Y
F	L	H	B	C	I	G	P	I	J	G	O

AEROBICS
BOOGIE BODY
FEEL THE BURN

JAZZERCISE
LEG WARMERS
PUMPING IRON

ROLLER DISCO
SHAPE UP
SPANDEX

Free Compliance Checklist: Processes for Managing Intercompany Agreements

A tool for Tax, Legal, Compliance and Risk professionals in multinational corporates.

Email us at info@lcnlegal.com to request your free copy of this checklist.

Sector-focussed private discussion groups on intercompany governance and intercompany agreements for Transfer Pricing compliance

We will shortly be announcing a series of private discussion groups on the practicalities of intercompany governance and intercompany agreements for Transfer Pricing compliance, each focussed on a particular sector, and each for CFOs or similar professionals within multinational groups. The relevant sectors are:

- Aviation
- Consulting
- Marketing and Advertising
- Software and technology

If you would like to be placed on our waiting list, please email us at info@lcnlegal.com and let us know.

Testimonial for LCN legal

"I really like the format! It is very clear and easy to follow.

Can you teach our lawyers to write so clearly?

I wonder sometimes if they are being paid by the word."

Brian Sturtz, Former Director of International Tax and Transfer Pricing at Walmart Stores, Inc., commenting on template Intercompany Agreements created by LCN Legal

Evolution of an Icon: Arnold Schwarzenegger

