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TRANSFER PRICING IN THE MULTINATIONAL FIRM

by

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The spread of decentralized corporate operations has been accompanied by widespread utilization of the profit center concept to measure, evaluate, and motivate divisional management. As the implications of the profit center idea have been recognized, the need has arisen for rational systems to price intra-company transfers of goods at varying stages of production.

The aim, in general, has been to devise methods which would satisfy the goals of divisional managers to earn adequate profit for their divisions, while simultaneously furthering corporate profit goals. In single country operations, the system is meant to function for this purpose and to provide a foundation for a properly operating control system.

But when a company operates across national borders and exports its practice of decentralized management, with all the accompanying apparatus, new complicating dimensions are added. In international business, there are opportunities to maximize profits which may override the significance of a control system and the transfer pricing mechanism. Likewise, this environment contains threats to international firms, often unforeseen and, even when perceived, seldom factored into control systems.

This article deals with the characteristics which attach to and compound the problem of transfer pricing when a decentralized firm expands its operations into the international environment. It is based upon field interviews with

various officers responsible for control, pricing and taxation functions in the international divisions of several large United States firms.

The firms included several significant categories of products and markets. They have the common characteristic of doing the largest part of their foreign business through wholly-owned foreign subsidiaries and branches. We specifically excluded firms which manufacture in the United States for resale through company or independent sales agencies; petroleum companies were also excluded by design. The sample companies are all heavily committed to manufacturing in foreign countries as well as at home. Fiscal 1964 sales of individual firms ranged from $200 million-plus to over $3 billion. Overseas, after-tax earnings ran from $9 million to over $100 million. Net assets overseas were over $200 million for one company, and in only one case was it under $20 million. While the sample could be thought of as small in numbers, total 1964 overseas sales volume of the group was nearly $3 billion. As compared with total overseas sales of United States manufacturers of just over $37 billion, this is about 8 percent of the total.

Almost without exception, these firms have partners in one or more countries. Partnerships or jointly owned ventures are of sufficient importance in the total operation to have provided a basis for examining the effects of the transfer pricing system on these divisions. Firms varied, however, in the degree of willing acceptance of foreign partnership ventures, from complete acceptance of this form to reluctant participation only where foreign governments insist upon joint ownership (either with governments or with native individuals or corporations as partners). Finally, interviews were also conducted with United States Treasury Department officials, as well as with independent attorneys and accountants who practice in the area

of this research.

Writings on the international aspects of transfer pricing deal mainly with the impact of taxes, and the use of internal prices to minimize tax liabilities. With the United States tax rates among the highest in the world, most interest has centered about means of reducing the tax burdens which arise in this country. Little has been written about the influence exerted upon transfer pricing by the international environment, nor has the resultant effect upon internal control mechanisms occupied the attention of current writers. A survey of the most important international companies in the United States has shown the importance of those neglected elements.

As one could expect, transfer pricing practices vary widely. Each different policy is justified on a reasonable basis - on some special variable which is considered critical by the individual company. Therefore, by looking into the basic argument justifying each specific transfer pricing policy, we may study some of the variables which are critical to transfer pricing policies.

1. Taxes.

It has been observed that the pervasiveness of taxation clouds the entire background of transfer pricing in international firms, and that taxes represent the touchstone by which all transfer pricing is judged. Tax considerations lurk in the background of so many decisions in modern management that the impressions of all-importance is understandable. Although the United States Revenue Act of 1962 reduces the opportunities for tax reductions and tax postponement, managers do consider world taxes in setting transfer prices. With the United States minimum income tax rate presently 48%, corporate profit is maximized by utilizing lower tax rates of other countries. *Ceteris paribus*, greater profits will result from

shipping goods into low income tax countries at prices which are lowered in order to raise income in such countries. And if prices of goods shipped from such countries to the United States are set high, the rate differential may result in maximizing corporate profits in both countries. It is commonly considered that the bête noire of taxation is the United States. In fact, however, tax rates in some countries are close to those in the United States (in some cases higher) and the tax reducing devices available through internal pricing operate between any two countries with different rates of taxation on income. Furthermore, while we seem to think always in terms of differentials in tax rates, statutory differences in computing income subject to taxation also produce real tax differentials. For example, an identical tax rate in two countries may result in widely different real taxes if, say, the methods of allowing depreciation vary substantially, or if the degree of freedom in allocating expenses varies.

Evidence indicates that headquarters management often considers international income tax costs in setting transfer prices. But this practice evokes two kinds of problems - one external and one internal. The external problem relates to the counter-action taken by government tax authorities in both United States and foreign countries. Faced with the minimizing methods practiced by taxpayers, revenue departments throughout the world attempt to take steps which will maximize tax revenues. Despite the fact that international auditing is still relatively new, American government auditors are familiar with corporate tax-minimizing practices. It is also a fact that foreign auditors are expanding their awareness of these problems, and are increasingly taking steps to overcome the longstanding advantages of corporate tax practices. In other words, tax minimization by corporations

runs head-on into tax maximizing of government treasury departments.

Internally, pricing for tax savings causes aberrations in divisional operating results. The resulting conflicts in goals lead to dysfunctional decisions. Many control systems in international use do not make allowances for aberrations in price caused by tax minimizing schemes. When allowances are made, they are not always effective or satisfactory. The same problem holds true in other facets of the environment detailed below.

Corporate costs and profits are affected also by import duties assessed by countries of import. A change in a transfer price may cause a change in the duty, both as to amount and as to rate. Therefore, it adds to a company's profit to send goods at low prices into countries with high rates of duty. It may also be advantageous to ship goods at high prices into countries with low import tax rates.

The source of the end product may thus be affected if production processes may be performed on transferred materials equally well, and at no cost differential, in two or more countries with different rates of import taxes.

The external and internal problems which are described in connection with consideration of income taxes follow also in the case of customs costs. In other words, government treasury department officials are sensitive to the basic conflicts between corporate profit goals and their own needs for revenue maximization. At the same time, the consequence of pricing to optimize import taxes will often be to change the income statement of one or more divisions to divisional management's advantage or disadvantage.

The impact of income and import taxes upon transfer prices leads to additional problems for management, and again one of these problems occurs externally and the other internally. Externally, the goals of income tax administrators and customs officials to maximize revenues for their respective departments are in conflict, because the increased revenue of the one tends to reduce the revenue of the other. The higher the import tax assessed to the importer, the lower the profit remaining as a basis for income taxes. To add to the tax manager's headache, he finds virtually no coordination of the two revenue collecting departments in any country, and a tax-paying firm has to bear the brunt of the two taxing divisions' conflicting goals. Internally, the problems have to do with the effect of import tax pricing upon divisional operating results and upon the motivation of divisional managers. But an added twist results from the attempt of the firm to balance the added cost of duty resulting from a high import price against the lower cost of income taxation in the country of importation as well as the potentially higher income tax in the exporting division.

Notwithstanding the importance of taxation, many firms consider it only one among other factors. One company attitude is summed up in the words of the Vice President of International Operations: "We could connive on taxes, but the savings would be trivial. We prefer to give full attention to operating our company and let the tax liabilities fall where they may." This company considers anything but a straightforward application of tax laws as morally improper. Another company neglects the impact of taxes on pricing entirely, arguing that simple and consistent pricing practices tend to minimize tax investigation problems. Over the years this firm has considered the establishment of tax haven countries in its scheme of organization but each time its conservative nature has proscribed use of

this device. It has been stated by a current company official that this has been a mistake. His opinion is that during the many years that tax havens were permissible, the firm could have accumulated sizable profits, undiminished by taxes, for reinvestment overseas. Especially at present, with heavy capital requirements overseas, and new investments restricted, these funds would have largely diminished not only high-cost foreign financing but also the problems brought on by the United States balance of payments situation.

Another reason for neglecting the tax considerations is given by an electronics firm. While this company is aware of the impact of taxes on income, the importance of greater harmony among divisional managers has eliminated tax-motivated transfer price changes. In the past, moves designed to minimize taxes have caused interpersonal conflicts to such an extent as to discourage any further tax-minimizing practices. It is also observed that the narrowing gap among world tax rates makes it less possible to effect significant tax savings, and therefore the sacrifice to greater managerial harmony continually becomes less costly.

2. Currency Fluctuations.

We generally consider the problem of inflation within the context of its effect upon the purchasing power of internal consumers and its depressing effect on export trade. But inflation exerts an erosive effect on monetary assets within that country.

In most cases, the respondents of our survey use generally recognized practices to mitigate the deleterious effects of inflation in host countries. A preferable method among some firms is to withdraw funds to a safer haven. But, generally, countries which are suffering from rapid

inflation are also hard-pressed to maintain an adequate balance of foreign exchange. Therefore, in such countries, foreign exchange is often restricted by government order to necessary materials purchased, while being withheld from profit transfers.

These problems have triggered apparently opposite pricing practices in two companies operating in Brazil, where excessive inflation is a continuous threat. Because the inflationary condition has made it nearly impossible to show a profit, one firm ships goods in at low prices as a subsidy to its Brazilian division, to assist it in profitable operation. Also, the Brazilian government requirement to post a cash deposit equal to six month's projected imports is costly because the cash deposits continually lose value. Resultant side effects of the low pricing practice not only reduce this deposit, but also reduce the inflationary loss of value of the deposit over the six-month period. On the other hand, another company preferred to ship materials into Brazil at extra high prices, in order to remove as much cash as possible to the United States. In this instance, the firm was willing to show a higher profit and pay higher taxes in the United States, but at least, the Controller reported, the cash asset, even after taxes and deposit erosion, was safe from further loss of value.

Thus transfer prices can be, and actually are, used as a device to counteract inflationary erosions of assets.

3. Economic Restrictions

Under this heading we include three areas of concern to multinational corporations, the effects of which may be mitigated by adjustments to transfer prices. The first of these has to do with currency rationing. Some countries (notably Israel and several South American nations) have adopted regulations which rigidly restrict the conditions

under which profits of foreign-owned corporations may be transmitted out of the country. At the same time, governments such as these ration currencies available to corporations' imports. This system provides close supervision by the host country over the outflow of its vital foreign exchange. To some extent, it is possible to circumvent such restrictions by increasing the prices of imports from parent or related companies. High prices paid by a restricted division to related companies can result in a repatriation of profits despite the desires of a host government. Thus when one avenue is closed, alert managements seek other ways to achieve their goals.

Secondly, as a way of increasing manufacturing activity locally, some governments impose restrictions on the number and kinds of components which may be imported into their country for further processing or assembly into a larger unit. In Mexico, the systematic action of the government in forcing United States parents to ship fewer components, and causing more parts to be manufactured by local sources of supply has had impact on many firms - notably in the automotive industry.

Finally, some governments restrict allocation against local taxable income for expenses incurred and services performed in the country. Thus, for example, head office expenses such as administrative and general, R&D, marketing, and other costs may not be charged to subsidiaries in Venezuela, for example, if the services are performed (as they usually are) elsewhere. In one country, a respondent found himself forbidden to remit royalties, his method of operation in many other countries of the world. In such a case, costs may be recouped by increases in the transfer prices of the goods shipped to the foreign subsidiary. At times, the subject foreign government may suspect the compensating use of transfer prices, and local managements

are forced to devote time and effort to justify their actions to local government officials. The question of maintaining the good-will of host governments is vexing, and more is said about it below.

Apart from the economic and cost ramifications of this practice, we note the moves taken by parent corporations with respect to transfer prices on permissible imports, designed to counteract restrictive rules of the Mexican government. By attaching the mark-up connected with forbidden components to permissible imports, one United States parent attempts to maintain the status quo ante with respect to the United STates income from exported components.

4. Unstable Governments.

When a company operates in a country in which there has been a tendency for the government to be overthrown (or shaken) with recurring regularity, it is to the interest of the company to keep as little cash as possible in that country. The high feelings of nationalism which often accompany a revolutionary regime further endanger assets of foreign businesses, and expropriation is a risk in such situations.

The fact that a government has been in power for many years does not always call for confidence either. Cuba and Nigeria are two cases in point, in which comparatively stable governments (one of them of long standing) were overthrown much to the shock of managements which were not sensitive to local politics, and were not prepared to deal with the consequences of revolution. In such environments, low prices on transfers out of the country can facilitate transmittal of excess cash, since exports at low prices tend to reduce cash flowing into such countries. High prices on imports also may have the same effect. Drastic changes in transfer prices may not go unnoticed in such countries, but a planned policy can be implemented

to minimize the risks in unstable areas. Managers who use this device readily subject themselves to the increased income taxes in the country of export (usually the United States), but at least, they say, what remains after taxes is safe from expropriation and other foreign risks. One Controller stated that his company received relatively little damage from Cuban expropriation, because its foresight caused a considerable removal of monetary assets in advance of troubles. There is evidence that other firms also benefited from this foresight. (There is a significant lesson here for the inclusion of external factors in corporate information systems.)

Only in one instance has transfer pricing been used as a technique to deal with countries which are habitually governed by transient rulers, or in which the threat of revolution may be evident. Because of the general uneasiness among executives in this one company over the long-term stability of the Argentinian Government, transfer prices of materials shipped to Argentina had been inflated so as to maximize cash outflows. The constraint to excessive prices, however, is the Argentinian law providing for automatic bankruptcy against firms whose earnings habitually fall below prescribed minimums. Nevertheless, removals of profits by way of transfer pricing, even after the higher United States taxes, at least gives some assurance of stability to the after-tax profit.

5. Competitive Advantages.

Transfer prices are used to strengthen the competitive position of a company, or to control or weaken the competitive position of a company, or to control or weaken the competitive position of others in a foreign environment. In the case of integrated oil companies, for example, it seems apparent that producers enjoy substantial profit on the raw product. When competing refiners and refining divisions of the producing company enter

the market at this stage, raw material costs have already provided a large measure of profit to the producers. The small spread remaining in refining, processing and marketing tends to leave the producers in control of final market prices for finished products throughout the world. This effect seems to be confined purely to integrated firms in industries in which control over raw materials is in the hands of a relatively few companies.

In the firms of our experience this situation does not prevail to any noticeable extent. Some companies do manufacture basic products in bulk (pharmaceutical and chemical firms are cases in point), and they do sell such products to competing manufacturers which process and refine the raw or basic ingredients into competing end products. Attempts are made to maintain resale prices of bulk products at a level which will cause prices of end products to be high enough for competitive advantage. The attempts are not wholly successful. In spite of a limited number of bulk processors, competition at the bulk level keeps the access cost to competitors low enough to cause competition at the level of finished goods.

In another respect, however, transfer prices are used to mitigate the internal effects of outside competition. When competitive forces in a foreign country cause external prices to be lowered by a particular division with resultant damage to the profits, consideration is usually extended to reduce transfer prices into that division. If the local competitive squeeze is beyond the control of the damaged division, the local managers in many countries request the parent - or other divisions - to share its losses by changing transfer prices. It is recalled that in some firms, transfer prices are a function of external prices. In such cases, then, downward changes in external prices beyond local control will, in time, cause changes in transfer prices to strengthen competitive action.

6. <u>Foreign Partners</u>.

Incentive exists for companies to charge higher transfer prices to jointly-owned than to wholly-owned divisions. At the same time, in counteracting such a tendency, the jointly-owned subsidiary has incentive for a directly opposite action. In the field a higher degree of circumspection seems to surround transfer pricing practices where joint ownership exists. In other words, regardless of the locus or the method used to set transfer prices, real arm's length bargaining takes place to a greater extent. Because it also happens, not accidentally we are sure, that jointly-owned subsidiaries are usually more fully integrated, they have a measure of autonomy over outside purchasing and selling beyond the permissible limit for wholly-owned subsidiaries. This freedom is reflected in transfer prices which are acceptable by both sides.

In two countries (France and Japan) in which one firm is required by the respective host governments to accept partners, this firm also wholly owns parallel corporations. These parallel firms sell similar products, but to different classes of trade. In addition, the partnership companies are limited as to the products they may handle while the wholly-owned subsidiaries deal with the balance of the line. This practice reduces in a small measure the independence of the partnership organizations.

More common, however, is the practice of firms in which arm's length dealings with jointly-owned subsidiaries, accompanied by freedom to buy or sell outside the company, make for a happier and stronger family relationship.

In one company, for example, jointly-owned divisions are at complete liberty to buy or sell outside the company. The only preference seems to be that last refusal is uaually granted to fellow divisions before

going outside the company. The existence of an independent scheme of pricing practically eliminates income maximization resulting from other environmental influences; but it is agreed by such firms that peace in the organization is worth the price paid for it.

7. Public Relations.

Under this heading we include several effects of importance which may be attributed to or which accompany transfer pricing systems and concepts. Since external pricing exerts some influence on transfer prices, there is a secondary effect on transfer prices caused by a desire for "good citizenship." The sample companies do consider this effect in their desire to pay a fair share of taxes to host governments.

An overriding constraint to the allocation of income to foreign divisions is a desire to show some measure of good faith to host governments by submitting profits to local taxation. At most, the desire seems to be to leave in each country the minimum tax assessment which will satisfy host governments. While the willingness to pay local taxes has increased coincidentally since the passage of the 1962 Revenue Act, the officials report that a better foreign climate results from acting like "good citizens" in each country.

Along similar lines, we report here the practice of one company with a manufacturing subsidiary in Mexico. In that country the law requires a sharing of profits with employees (currently at the rate of 10% of profits with a rise in the offing). As a result this firm sets transfer prices to leave a "reasonable" profit in that country. In addition, an attempt is made to show year-to-year earnings in a gradually ascending amount. What the company considers reasonable is not always agreeable to the government or to the employees. At the same time, whenever volume of any particular item -

or group of items - varies widely from forecasts, the resulting profit is skewed. Meanwhile, the interaction of other variables renders achievement of the goal difficult. The company feels, however, that the sacrifice of 10% of its local profit must be controlled, and devotes constant attention to the outlays. Some danger exists that firms which sell like materials at varying prices to different users may be accused of price discrimination. This danger is recognized by our sample, but without exception they hold to the opinion that prices on goods transferred internally across boundaries are free of attack on this score. They recognize that a violation by a subsidiary may be imputed against the parent. Nevertheless, such considerations are not permitted to affect multinational transfer prices. Whether the danger is real or imaginary appears to be of little interest in the light of the considerable number and weight of other variables.

Finally, while possible effects on transfer prices might be brought about by the right of labor unions in Italy to audit company profits and by the right of labor representatives to sit on the boards of directors of corporations in France and Germany, the firms appear to consider the possible consequences too slight to affect their transfer prices.

8. Interpersonal Reactions.

The field survey was limited to interviews with officials at parent and international headquarters in the United States only. The findings discussed so far have been strictly from the point of view of the corporate officers who devise and administer the transfer pricing systems under review. Since interviews were not conducted with overseas managers we cannot report specific personal attitudes or perceived reactions of such individuals. However, it seemed to us that headquarters

personnel attempted to consider the perceived needs of overseas personnel. Even if it were intended to ignore managers of foreign divisions, modern management methods coupled with today's speedy communication and easy intercontinental travel make regular interpersonal contacts between management personnel an integral part of corporate life.

While this communication undoubtedly affects headquarters plans and decisions, from our point of view we see only the secondary result of the contacts. However, a closer look at overseas reactions and perceptions was available to us in a somewhat more direct manner. Since it is not uncommon in some firms to practice rotation among foreign divisional personnel, we did in fact find that several of the officials now employed at international headquarters had at one time worked as overseas line managers. And in the case of one company, the present international financial director is also the manager of an important Latin American division of the company. We would not suggest that the reactions expressed by these individuals are definitive in any real sense, but we feel that their opinions may be indicative of the kinds of interpersonal problems which are generated by the transfer pricing arrangements of the type we have witnessed.

In the case of a company whose highly directive transfer pricing system causes a disproportionate share of income to arise overseas, its international managers are sometimes tempted to boast about their "contributions" to corporate profits at periodic meetings of corporate executives. The fact that their profits are in effect allocated rather than earned does not deter their proprietary self-glorification, much to the frustration of domestic managers, not to mention dismay of headquarters executives.

In all companies whose transfer prices are a function of environmental influence some method of adjustment is used to give appropriate credit to divisions for their real contribution. The method may be credit-backs, or "dual" sets of books, or some other form of memorandum allowance, or compensation in budgets and profit plans. But regardless of the intent, "some things get lost in the wash," and dissensions result in dysfunctional upsets among all such firms at one time or another. It is a rare manager who waits patiently for a headquarters controller to adjust for profit or costs which are put out of line by headquarters directives. In one company, it was reported, the United Kingdom division was directed to lower its price to a new French subsidiary so as to improve startup operating results; but a good deal of ill-feeling was generated when headquarters seemed to forget that the resulting poor performance in the United Kingdom was not at all a reflection of local management.

When freedom to purchase and sell outside are sharply limited, divisional managers chafe for two reasons. First, they feel they are being discriminated against by having to overpay and subsidize a fellow division. Second, they complain about lack of interest for the company as a whole, because higher internal costs may at times reduce total corporate profit. If headquarters seems to be cavalier about corporate profits, local management frustrations may cause dysfunctional attitudes and action in the field. In those companies which present a uniform price to the world, the managers of more efficient plants sometimes complain of having virtually to subsidize less efficient members by reason of their own economies.

These kinds of reactions are sometimes evident in purely domestic operations, but for the most part the far-reaching influence of the multinational environment, when coupled with differences in national temperament and cultural backgrounds, causes complaints of a more serious nature to a greater extent than in a single country operation.

Conclusions

The establishment and operation of a functional control system to measure, evaluate, and motivate management in purely domestic surroundings is difficult enough by itself. In the case of multinational companies, however, the need for feasible control systems is rendered more urgent by the additional complexities of the larger environment. An executive has emphasized that the risks in international business are larger in number and different in kind than in the domestic environment. He was referring mostly to the problems enumerated here. Regardless of the risks, however, there is wide recognition among our sample that the rewards of the international environment - at least to date - have offered ample incentive to United States firms to expand in this direction. Nevertheless, any actions which affect the control mechanism are likely to be more dangerous to the firm engaged in multinational business; and when adaptations to new conditions cause alterations to an existing system, management must be careful not merely to substitute one problem for another.

Accordingly, the first criterion of a transfer pricing method in multinational business should be that it does not cause destructive changes in the existing control system, unless adequate adjustments compensate for the changes, and keep the system operational. In other words, unless a price change is called for by functional needs of managers, first attention should be directed at its effect on the control system.

For example, if transfer prices have to be recast in response to changes in cost of production inputs, the control system, such as it is, ought not to be changed. If it has been providing useful information in the first place, it will now reflect the new conditions (the causes, or inputs) as well as the resultant changes (the effects, or outputs).

But when a transfer price change is introduced in order to counteract, or take advantage of, circumstances extenral to the usual routine, then the system will reflect results which are not necessarily the result of the operations it is designed to measure. And if the measurements are false, then resultant decisions are likely to be wrong. We consider the three basic requirements of <u>measurement</u>, <u>evaluation</u>, and <u>motivation</u> to be so vital to the promotion of corporate effectiveness, that changes in the control system should not be tolerated which may react at cross purposes to these requirements.

Our recommendation is that the transfer pricing system must primarily be compatible with the operational goals of the control system, and msut reinforce its regulatory functions. But when external conditions are of such substance that they either expose the firm to grave threats or make available opportunities for material gains, then the transfer price system may be revamped to accord the greater return to the firm. The magnitude of threat or gain is of relevance to the proposal, since it is not intended to disturb control systems for every minor circumstance. Under such a practice, systems would soon cease to operate effectively. In each firm, criteria should be established for selection (or elimination) of matters for consideration.

Quantitative limits would point up the particular relevance in each case. For example, one might use as measures, a relative or absolute profit contribution, or a change in market share. Appropriate measures should be apparent in each case. Qualitative rules also have to be established, although they do not lend themselves to precise measurements. For example, one might consider interpersonal effects among managers (at all levels), reaction of public opinion, or changes in attitude of host or parent governments, to mention just a few. And again, the special conditions in each firm and its environment would dictate the criteria.

In proposing what may be thought of as a flexible approach to transfer pricing in multinational business, we are at the same time rejecting a simplistic approach to the problems. There is simply no one easy solution to the problems. We also regard a willingness to tinker incessantly with transfer prices to be equally dysfunctional, because incessant adjustment to the changing world without quantitative or qualitative tests, represents too mechanistic and narrow an approach in a complex and changing world.

We have attempted to present the subject in its multinational perspective, and not just as a problem which occurs both at home and, coincidentally, among foreign divisions. Every functional area of business has its counterpart both at home and abroad. Marketing, production, financial, behavioral, accounting, and others areas have their parallels in both theaters of operation. To some degree, and in many instances, the functions are nearly identical. For example, the financing of a new project in Kansas City, Memphis, or Milan, may require identical approaches to an optimum solution. The managers in any one of these three cities may solve the problem in an identical manner. Likewise, transfer pricing may, in many respects, not present different problems nor require different approaches

on both sides of the United States border; and it should be recognized that this is a fact in the case of transfer pricing as well as for any operational or staff function of the firm.

But it must be emphasized that, to a significant degree, many problems occurring on both sides of the United States border have similarities in name only. The trepidation with which some parochial business managers approach the international area is, in our opinion, often exaggerated out of proportion to the actual conditions. But there are adequate grounds for believing that every domestic function is at times distinctly different in its foreign environment. There are perceivable differences between the business climate in the United States and abroad, as well as differences in culture and established practices.

International business has grown by leaps and bounds, and problems have grown apace; but managers have not always been aware of them. When they have perceived the problems, they have not always responded with suitable solutions. Empirical evidence indicates that interest is high but attention is uneven.

We therefore advise extra care in approaching the concept of transfer pricing in the multinational firm. We recommend a multinational outlook, which includes consideration of regional problems. We suggest that greater effectiveness and, it should follow, greater profit will be the reward for those managements which recognize the multi-faced problems, and achieve solutions which will reconcile the differences.

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