CASE STUDY- FACTS AND QUESTIONS

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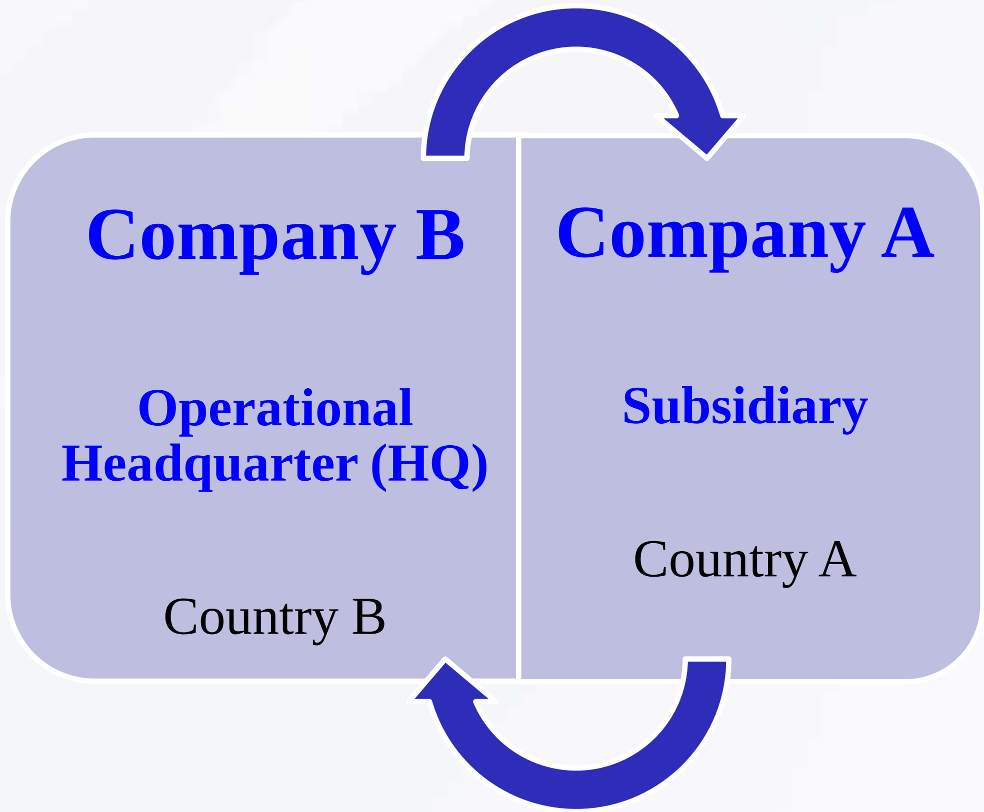
Facts and Questions



Sale of tangible fashion products

Facts and Questions

- **Company B or HQ:**
  - Is responsible for all operational and strategic business activities including the clothes designing, assortment planning, logistics, definition of the pricing policy, advertising and marketing, shop location policy, web & store selling platform management, and finance, amongst other strategic functions.
  - Develops, enhances and maintains the intellectual property used in the business activities. In addition, they are responsible for the functions regarding the overall strategic direction of the Group, and the maintenance of the Group´s brand and trademarks.

Facts and Questions

- **Company B or HQ:**
  - Carries out general support functions regarding accounts receivable or payable, human resources, and information technology (IT), nowadays referred to as business tech (BT).
  - Regarding the Online clothes selling business, HQ is responsible for the design, assortment planning, sourcing, logistics, pricing policy definition, marketing, finance, and sales strategy. Moreover, they own all operational IP related to the online business.

Facts and Questions

- **Company A:**

  – Acts as a distributor in the market, with functions that include the implementation of the store's interior design, implementation of the marketing and advertising campaigns, of the merchandising and sales policy, and pricing as well as assortment of the inventory, managing and maintaining it, and executing quality control procedures.

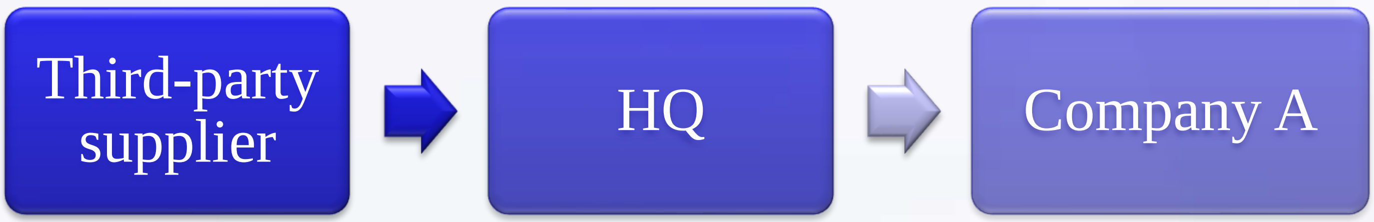
  – All of these activities are based on the support from the head quarter.

Facts and Questions

- The group proposed an APA to cover the followings transactions:
  - T1. Sale of goods and materials: tangible fashion products.
  - T2. Business platform.
  - T3. Support services to the online sales.

Facts and Questions

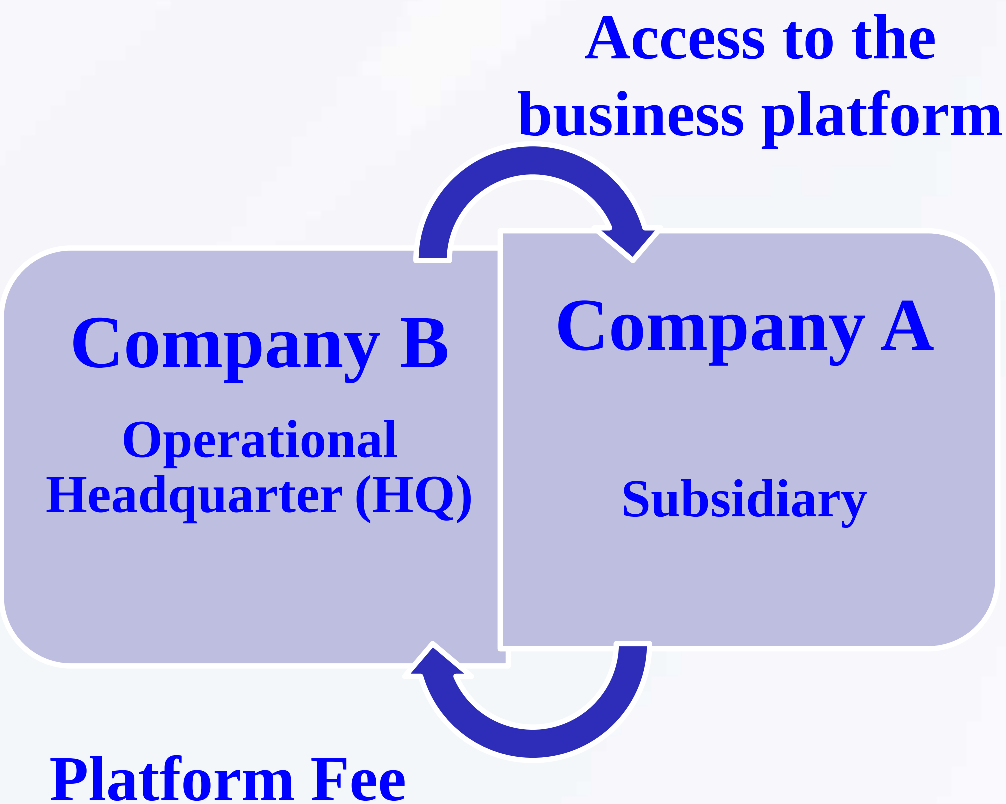
- **T1. Sale of goods and materials: tangible fashion products.**



Company A places its orders through the buying agent (HQ) at a third-party supplier. The HQ acts as an intermediary between the buyer, in our case Company A, and the supplier, and makes sure all requirements, such as quality control and documentation for shipment, are met.

Facts and Questions

- **T2. Business platform.**

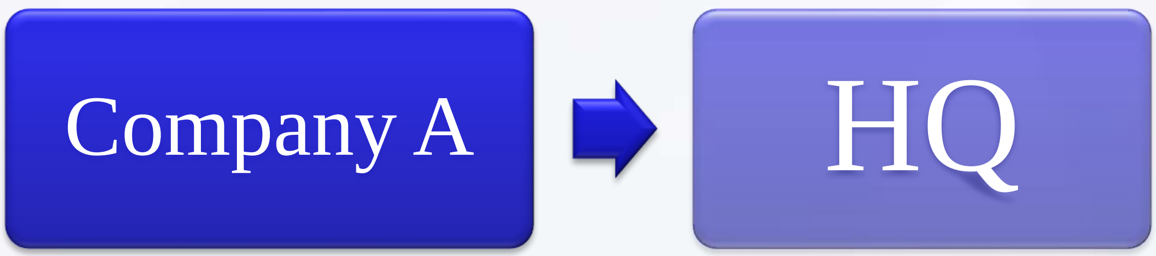


The head office owns the platform, and carries out the designing, enhancement and maintenance. These functions include amongst others the definition of the strategic framework of the Group regarding value chain, sourcing, procurement function, and sales.

By providing access to the business platform, the head office supports all the subsidiaries on all aspects of the business.

Facts and Questions

- **T3. Support services to the online sales.**



Company A provides to the HQ customer and administrative support services, communication and in-store promotional support services and, in some markets, services related to handling of deliveries and returns in-store.

Facts and Questions

- **Transfer pricing policy: T1. Sale of goods and materials: tangible fashion products.**

The pricing for the transaction under review is open market-price (third party) cost-based: the actual cost of the product, purchased from independent suppliers by HQ, is passed on to product receiver, which in our case is Company A.

The Group argues that the rationale behind the choice of method is that Product Receiver could have been purchasing the products on its own. However, for operational and cost efficiency reasons the HQ is taking on this function.

Facts and Questions

- **Transfer pricing policy: T2. Business platform.**

The Group selects the transactional net margin method (TNMM), selecting sales as a profit level indicator, to value the intercompany transaction under review. The tested party is the company A. The benchmark derived from the study is represented in table below:

Measure	Operating Profit Margin – (2016-2020)
Lower Quartile	1,67%
Median	2,89%
Upper Quartile	4,87%
Observations	14

Facts and Questions

- **Transfer pricing policy: T3. Support services to the online sales.**

The Group argues that the online selling model it's centralized and operated directly through them in the Country B, without operational presence in Country A. The uniqueness of the operational situation at hand, results in the fact that there are no reliable comparables to be found in any database, thus no comparable economic analysis has been conducted from any database.

Instead, the most appropriate arm's length remuneration has been determined based on several concluded unilateral and bilateral APA's over time. The selected method, TNMM, takes the online sales as a profit level indicator, within the next range:

Measure	Operating Profit Margin
Lower Quartile	0.25%
Median	N/A
Upper Quartile	0.4%
Formula	Operating Profit / Turnover

Questions

- Would you categorize the functions carried out by Company A related to the Online Sales in Country A, as a provision of services?

- Given that the functional characterization made by the Group is correct, do you think the remuneration for the company A is accurate?

- Do you think that the related-party transactions proposed by the company are well defined?

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