

of operating profits to total services costs is necessary. Total services costs include all costs that can be directly identified with the act of providing the services, as well as all other costs reasonably allocable to the services as determined under proposed § 1.482-9(k). The Treasury Department and the IRS intend the costs included to be comprehensive and to comprise full consideration for all resources expended, used, or made available to render the service. Generally accepted accounting principles or income tax accounting rules may provide a useful starting point for determination of total services costs, but neither will have conclusive effect. Consistent with the current regulations under the comparable profits method, proposed § 1.482-9(j) excludes certain costs from total services costs, such as interest expense and other expenses not related to the controlled services transactions.

#### 11. Allocation of Costs—§ 1.482-9(k)

Existing § 1.482-2(b)(3) through (6) provide that costs may be allocated and apportioned to a services transaction under “a method of allocation and apportionment which is reasonable and in keeping with sound accounting practices.” Proposed § 1.482-9(k) retains the flexible approach of the current rule by allowing any reasonable method of allocation and apportionment of costs where such allocation and apportionment is relevant to determining an arm’s length charge for services. In establishing the appropriate method, the proposed regulations state that consideration should be given to all bases and factors, including the general practices used by taxpayers to apportion costs for other purposes. The proposed regulations provide, however, that such general practices need not be accorded conclusive weight by the Commissioner.

Proposed § 1.482-9(k)(3) provides examples that illustrate the rules regarding the allocation and apportionment of costs.

#### 12. Controlled Services Transactions—§ 1.482-9(l)

Proposed § 1.482-9(l) provides guidance regarding the threshold question of whether an activity by one member of a controlled group constitutes a controlled services transaction, the arm’s length charge for which must be determined under proposed § 1.482-9(l). This guidance updates and substantially modifies the guidance in existing § 1.482-2(b)(3), and brings such guidance more into line with international standards in this area.

*a. General Rule—§ 1.482-9(l)(1).* Proposed § 1.482-9(l)(1) provides generally that a controlled services transaction includes any activity by one controlled taxpayer that results in a benefit to one or more other controlled taxpayers. The terms “activity” and “benefit” are further defined and described in proposed § 1.482-9(l)(2) and (3).

*b. Activity—§ 1.482-9(l)(2).* Proposed § 1.482-9(l)(2) defines an activity to include the use by the renderer, or the making available to the recipient, of any property or other resources of the renderer. The Treasury Department and the IRS intend the broad scope of the term activity to allow transactions that are not subject to the existing section 482 regulations applicable to other types of transactions (e.g., transfers of tangible or intangible property, rentals, or loans) to be analyzed under proposed § 1.482-9.

*c. Benefit—§ 1.482-9(l)(3)—i. General Rule—§ 1.482-9(l)(3)(i).* Proposed § 1.482-9(l)(3) specifies rules for determining whether an activity results in a benefit to one or more other members of the controlled group. Proposed § 1.482-9(l)(3)(i) provides that, in general, an activity is considered to provide a benefit to the recipient if the activity directly results in a reasonably identifiable increment of economic or commercial value that enhances the recipient’s commercial position, or that may be reasonably anticipated to do so. In cases where an activity may be reasonably anticipated to have a particular result or outcome, but that result or outcome in fact does not occur, the determination of whether a benefit is present is evaluated by reference to what it was reasonable to expect at the time the activity was performed.

Proposed § 1.482-9(l)(3)(i) further provides that an activity is generally considered to confer a benefit if an uncontrolled taxpayer in circumstances comparable to those of the recipient would be willing to pay an uncontrolled party to perform the same or similar activity, or if such uncontrolled taxpayer would be willing to perform for itself the same or similar activity. This proposed rule would replace the rule of existing § 1.482-2(b)(2)(i), which provides that the relevant determination is whether an uncontrolled taxpayer in circumstances similar to the renderer would charge for the service. The Treasury Department and the IRS believe that the approach of the proposed regulations is more consistent with the arm’s length standard and is more in line with international standards in this area. In addition, this

approach should be substantially easier to administer than the standard under existing § 1.482-2(b)(2)(i), which in some cases has been interpreted as requiring a difficult analysis of the subjective intent of the renderer. While the focus of this aspect of the proposed regulations is on the recipient, the determination of the arm’s length charge may require a focus on the recipient, the renderer, or both, depending on the applicable method.

The proposed regulations and the examples set forth under § 1.482-9(l)(4) do not adopt a so-called “general benefit” approach, under which certain activities in a corporate group were presumed to generate a benefit to the controlled group as a whole. This general benefit approach in some cases has been used to justify a charge to a group member for centralized activities performed by a corporate parent or service center, whether or not that particular member actually receives a benefit from those activities. The Treasury Department and the IRS believe that the general benefit concept is inconsistent with the arm’s length standard. In the controlled group context, the benefit analysis appropriately focuses on whether one or more controlled parties receive an identifiable benefit from an activity performed by another member of the group. Although the proposed regulations do not adopt the general benefit approach, in certain cases the allocation or sharing among group members of expenses or charges relating to corporate headquarters-level activities or other centralized service activities may be consistent with the rules of the proposed regulations.

Proposed § 1.482-9(l)(3)(i) clarifies that a benefit is received by the owner of an intangible when another controlled taxpayer performs an activity that contributes to the development or enhancement of the value of that intangible. This provision is consistent with proposed § 1.482-4(f)(3) and (4).

*ii. Indirect or Remote Benefits and Duplicative Activities—§ 1.482-9(l)(3)(ii) and (iii).* Proposed § 1.482-9(l)(3)(ii) and (iii) retain, with modifications, two concepts that also appear in the existing regulations. First, an activity does not result in a benefit to the extent that the activity produces only indirect or remote benefits. Second, an activity does not produce a benefit where the underlying activity is duplicative of an activity performed by the putative recipient.

Under proposed § 1.482-9(l)(3)(ii), an activity produces an indirect or remote benefit only if that activity is one for which an uncontrolled taxpayer