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(4) Evaluation of arm's length charge.  
 (5) Examples.  
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 (1) In general.  
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 (l) Controlled services transaction.  
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 (1) Services transactions that include other types of transactions.  
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 (4) Other types of transactions that include controlled services transactions.  
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 (6) Examples.  
 (n) Effective date.

**Par. 3.** Section 1.482-1 is amended by:

1. Revising paragraphs (a)(1), (b)(2)(i), (d)(3)(ii)(C) *Example 3*, (f)(2)(iii)(B), (g)(4)(i), the first two sentences in paragraph (g)(4)(iii) *Example 1*, and paragraph (i) introductory text.
2. Adding paragraph (d)(3)(ii)(C), *Example 4* and *Example 5*.
3. Adding a sentence at the end of paragraph (d)(3)(v).

The additions and revisions read as follows:

**§ 1.482-1 Allocation of income and deductions among taxpayers.**

(a) *In general*—(1) *Purpose and scope*. The purpose of section 482 is to ensure that taxpayers clearly reflect income attributable to controlled transactions, and to prevent the avoidance of taxes with respect to such transactions. Section 482 places a controlled taxpayer on a tax parity with an uncontrolled taxpayer by determining the true taxable income of the controlled taxpayer. This section sets forth general principles and guidelines to be followed under section 482. Section 1.482-2 provides rules for the determination of the true taxable income of controlled taxpayers in specific situations, including controlled transactions involving loans or advances or the use of tangible property. Sections 1.482-3 through 1.482-6 provide rules for the determination of the true taxable income of controlled taxpayers in cases involving the transfer of property. Section 1.482-7T sets forth the cost

sharing provisions applicable to taxable years beginning on or after October 6, 1994, and before January 1, 1996. Section 1.482-7 sets forth the cost sharing provisions applicable to taxable years beginning on or after January 1, 1996. Section 1.482-8 provides examples illustrating the application of the best method rule. Finally, § 1.482-9 provides rules for the determination of the true taxable income of controlled taxpayers in cases involving the performance of services.

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(b) \* \* \*  
 (2) *Arm's length methods*—(i) *Methods*. Sections 1.482-2 through 1.482-6 and § 1.482-9 provide specific methods to be used to evaluate whether transactions between or among members of the controlled group satisfy the arm's length standard and if they do not to determine the arm's length result. Section 1.482-7 provides the specific method to be used to evaluate whether a qualified cost sharing arrangement produces results consistent with an arm's length result.

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(d) \* \* \*  
 (3) \* \* \*  
 (ii) \* \* \*  
 (C) \* \* \*

*Example 3. Contractual terms imputed from economic substance.* (i) FP, a foreign producer of wristwatches, is the registered holder of the YY trademark in the United States and in other countries worldwide. In Year 1, FP enters the U.S. market by selling YY wristwatches to its newly organized U.S. subsidiary, USSub, for distribution in the U.S. market. USSub pays FP a fixed price per wristwatch, and USSub and FP undertake without separate compensation marketing activities to establish the YY trademark in the U.S. market. Unrelated foreign producers of trademarked wristwatches and U.S. distributors respectively undertake similar marketing activities in independent arrangements involving distribution of trademarked wristwatches in the U.S. market. In Years 1 through 6, USSub markets and sells YY wristwatches in the United States. Further, in Years 1 through 6, USSub undertakes incremental marketing activities in addition to the activities similar to those observed in the independent distribution transactions in the U.S. market. FP does not directly or indirectly compensate USSub for performing these incremental activities during Years 1 through 6. Assume that, aside from these incremental activities, and after any adjustments are made to improve the reliability of the comparison, the price paid per wristwatch by the independent distributors for wristwatches would provide the most reliable measure of the arm's length price paid per YY wristwatch by USSub.

(ii) By Year 7, the wristwatches with the YY trademark generate a premium return in the U.S. market, as compared to wristwatches marketed by the independent distributors. In