

Current Status of Issue

Industry Director Directive #2, which will provide guidance to the field regarding the level of control and oversight for the cost sharing issue, issued March 21, 2008.

The position of Cost Sharing Arrangement, International Issue Specialist, has been created—announced June 2009.

Litigation

Currently there are cases in Appeals, one case tried in litigation for the Initial Buy-In issue (**Veritas Software Co.**) in July 2008, and other cases are under consideration for potential litigation.

Executing IMT Strategy for Tier I Issues

Audit Teams Should:

- Establish the Tier I Issue on IMS using the UIL code per the ID Directive.
- Research the issue on the Tier I website.
- Communicate with the IMT early to determine the strategy and any special requirements for the issue.
- Consider the issue in the audit planning and risk assessment in accordance with the IMT strategy.
- Utilize the audit tools and techniques provided by the IMT to develop the issue.
- Resolve the issue using all resolution tools in alignment with the IMT strategy.

Issue Management Team (IMT)

Issue Executive Owner—Patricia Chaback
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Office of Chief Counsel, International—Ken Christman
LB&I Industry Counsel—Michelle Korbas
Appeals Economist—Paul E. Forbes
Appeals Technical Guidance—Byron Bray
Appeals Officer, International Specialist— Bill E. Raimondi
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Tier 1



Tier I IRC 482 Cost Sharing Arrangements with Buy-In Payments

Quick Reference Guide

October, 2010

Issue Owner Executive (IOE)
Patricia Chaback, Director
**Communication, Technology, &
Media**

Tier I: IRC 482 Cost Sharing Arrangements with Buy-In

Issue Description

In general, a cost sharing arrangement (CSA) is an agreement between two or more participants to share the costs and risks of research and development as these costs and risks are incurred. Consequently, each participant receives a specific interest permitting its individual exploitation of intangibles developed under the arrangement (referred to as “covered intangibles”).

A CSA is governed by Treas. Reg. § 1.482-7. Because each participant owns specified rights to any intangibles developed under the arrangement, no royalties are paid by the participants for exploiting their respective rights to such intangibles. At the inception of the CSA, however, a participant may make available existing intangibles which it already owns to the CSA. In this situation, a “buy-in” is owed to that participant from the other participants in the CSA. In addition subsequent to the CSA’s inception, one participant may subsequently acquire intangibles outside the CSA and make those intangibles available to the CSA. This would also require a buy-in to be paid to the participant contributing such intangibles to the CSA.

During the CSA, participants share the intangible development costs (referred to as “IDCs” or “cost sharing pool”) in proportion to their shares of the benefits they reasonably anticipate from their individual exploitation of the cost-shared intangibles (referred to as “reasonably anticipated benefits”, “RABs” or “RAB shares”).

Upon termination of the CSA, a “buy-out” may be owed to the participants who relinquish their interests in the cost shared intangibles. A CSA is subject to various documentation and reporting requirements pursuant to Treas. Reg. § 1.482-7. Buy-ins and buy-outs are also subject to the rules under Treas. Regs. §§ 1.482-1, and 1.482-4 through 1.482-6. A qualified CSA produces arm’s length results if, and only if, the requirements of Treas. Reg. § 1.482-7 are satisfied. The IRC 6662(e) penalty regulations also apply to a CSA pursuant to Treas. Reg. § 1.482-7(j)(2)(ii).

Issue Specialization Teams

An Issue Specialization Team has not been created for this issue.

Administrative Codes

UIL Codes:

- * **482.11-11** - Cost Sharing Arrangements: Buy-in Payment for Pre-Existing Intangibles
- * **482.11-12** - Cost Sharing Arrangements: Buy-in Payment for Post Formation Acquisition Intangibles
- * **482.11-14**—Cost Sharing Arrangement—Buy-out Issues

Primary SAIN: **706**

Secondary SAIN: **123**

Tracking/Project Code: **0570**

Issue Tracking Attributes:

- * Transfer of Intangibles Offshore/CSA (IRC 367, 482): **C110**
- * CSA Buy-in Payment for Pre-Existing Intangibles: **C111**

Industry Director Directives (IDDs)

Industry Director Directive #1, provides the field direction on the Tier I Issue, Transfer of Intangibles Offshore/ IRC Sec. 482 Cost Sharing Buy-in Payment issue. It discusses areas in dispute with taxpayers and points out that the issue is most prevalent in the High Technology industry.

<http://www.irs.gov/businesses/article/0,,id=169313,00.html>

Industry Director Directive #2, provides guidance to the field regarding the level of control and oversight for the cost sharing buy-in issue. Issued March 21, 2008.

<http://www.irs.gov/businesses/article/0,,id=180564,00.html>

Mandatory IDRs

The mandatory Transfer Pricing IDR must be used in cases where the IRC 482 cost sharing issue is present. Refer to IRM Exhibit 4.46.3-5 for procedures. Approved language for the IDR is located at: <http://www.irs.gov/businesses/article/0,,id=169956,00.html>.

Appeals Settlement Guidelines (ASGs)

Currently there are no ASGs for this issue; however, the Coordinated Issue Paper for Cost Sharing Arrangements has been issued September 27, 2007. It has been referred to Appeals for ASG consideration.

Administrative & Technical Guidance

Cost Sharing Arrangements

Cost Sharing Arrangement Checklist

Issued August 9, 2005; revised May 27, 2008. A checklist for use in examining cost sharing arrangements can be found at the web address below. The objective of the checklist is, first, to assess the taxpayer’s treatment of the issue and second, to serve as a guide in determining whether cost sharing documentation submitted by the taxpayer complies with the contemporaneous documentation requirements of Treas. Reg. § 1.482-7(j)(2) and the IRC 6662(e) penalty regulations.

<http://www.irs.gov/businesses/article/0,,id=179794,00.html>

Coordinated Issue Paper

A Coordinated Issue Paper (CIP) was released for the Cost Sharing Issue, effective 9-27-07. It provides guidance and direction to examination teams on appropriate economic valuation methodologies for Cost Sharing Arrangements Buy-in transactions. In accordance with the Best Method Rule in the

§ 482 Regulations, the examination teams are expected to apply the CIP to all buy-in issues unless a principled factual distinction can be made to justify a different methodology. The examination team must contact the IMT Program Manager as soon as they determine the need to deviate from the CIP. The CIP can be found at the web address following:

<http://www.irs.gov/businesses/article/0,,id=174599,00.html>

Other Guidance

Access to six Field Service Advice Memorandums and one Technical Advice Memorandum, all of which address various aspects of cost sharing arrangements, is available at the web address below. At this site, sort by UIL, and look for “Cost Sharing” under “482”.

<http://www.irs.ustreas.gov/foia/lists/0,,id=97715,00.html>.

Regulations

Experience in the administration of existing §1.482-7 has demonstrated the need for additional regulatory guidance to improve compliance with, and administration of, the cost sharing rules. In particular, there is a need for additional guidance regarding the external contributions for which arm’s length consideration (the “buy-in”) must be provided as a condition to entering into a cost sharing arrangement.

Furthermore, additional guidance is needed on methods for valuing these external contributions. The regulations also address other technical and procedural issues that have arisen in the course of the administration of the cost sharing rules. 1.482-7T regs were issued January 2009.

<http://www.treas.gov/press/releases/reports/reg14461502%20final.doc>