

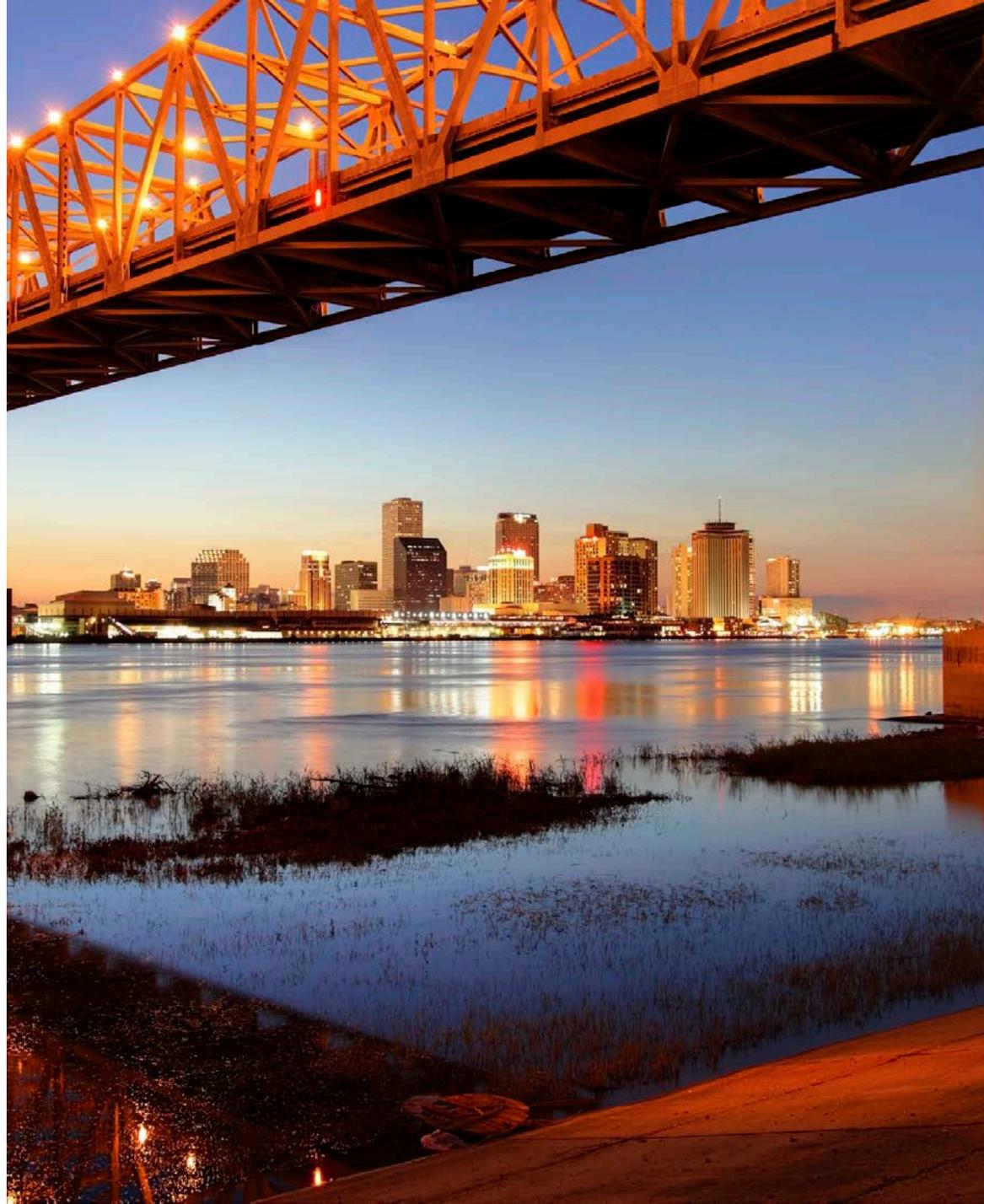
**Deloitte.**

# 2015 Engineering & Construction Conference

## Structuring International Contracts

Vivien Wang  
John Wescott  
Sajeev Sidher

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# Your Speakers

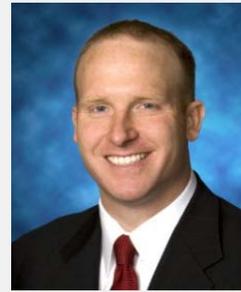
## International Tax



Vivien Wang  
Partner  
San Jose, CA

Vivien focuses on international tax planning including the and implementation of the worldwide restructurings, mergers, acquisitions, IP migrations and business optimization. Vivien is also the National Tax Leader of Deloitte's US Chinese Services Group.

## Business Model Transformation



John Wescott  
Senior Manager  
Costa Mesa, CA

John focuses on customer experience and business development strategy. John has previously served as VP of Strategy and Business Development for a national electrical and communications contractor.

## Transfer Pricing



Sajeev Sidher  
Tax Director  
San Jose, CA

Sajeev focuses on transfer pricing planning including global supply chain optimization and post-acquisition integration. Sajeev has a significant experience working with global construction and engineering companies.

# Introduction

# Important Industry Trends

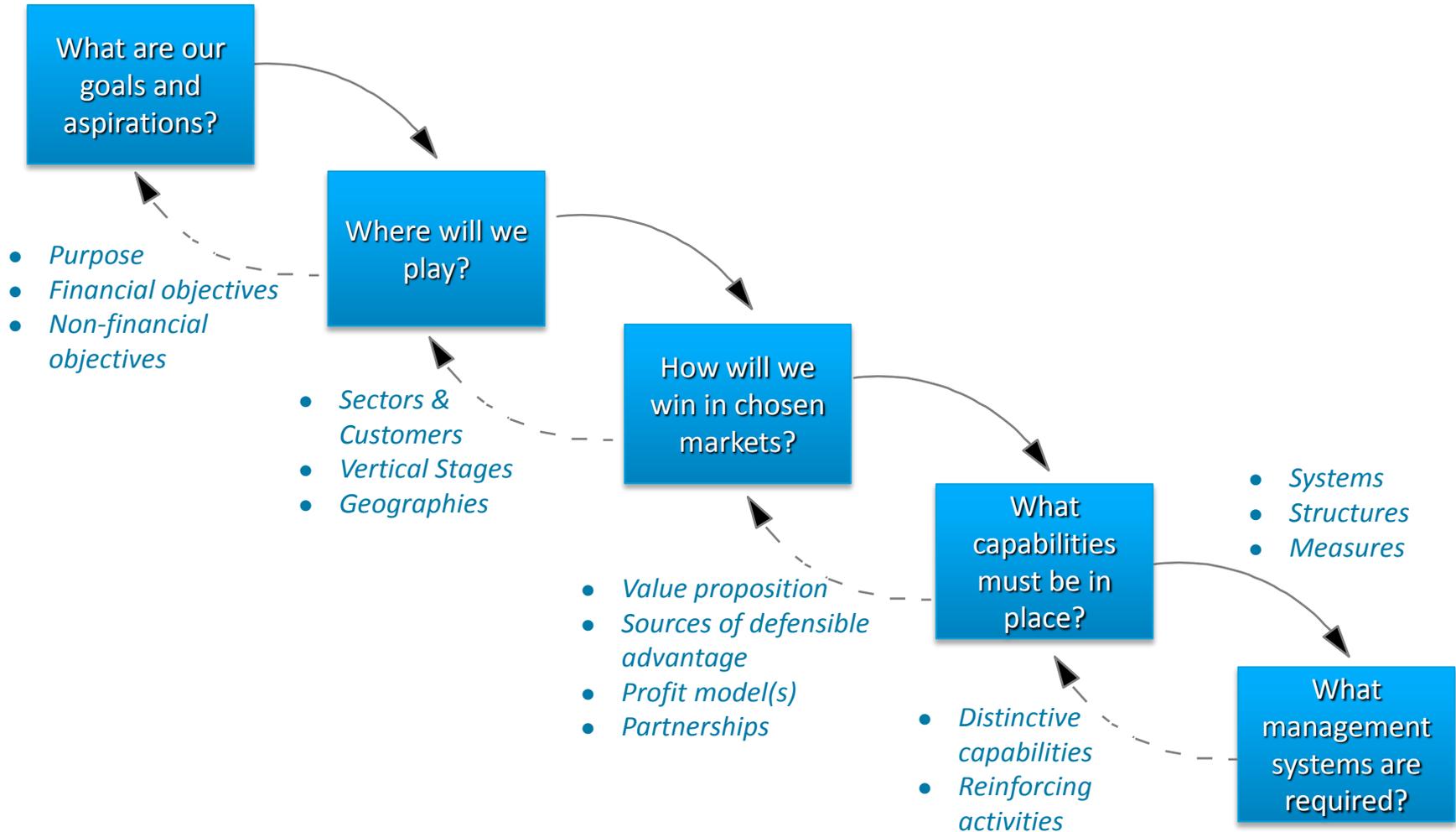
- E&C companies of all sizes are performing more business outside North America
- Growing opportunities in Asia, Latin America, the Middle East and Africa drive companies to locate more local resources to compete
- Industry consolidation accelerating as companies seek global footprints to compete. **(M&A activity in the E&C industry hit a near-record setting year in 2014).**
- In this environment, managing mobile workforce and asset deployment is critical to capturing opportunities and managing cost

These are opportunities that can introduce significant management complexity requiring companies to manage its growth efficiently and effectively.

# How to Address Industry Trends?

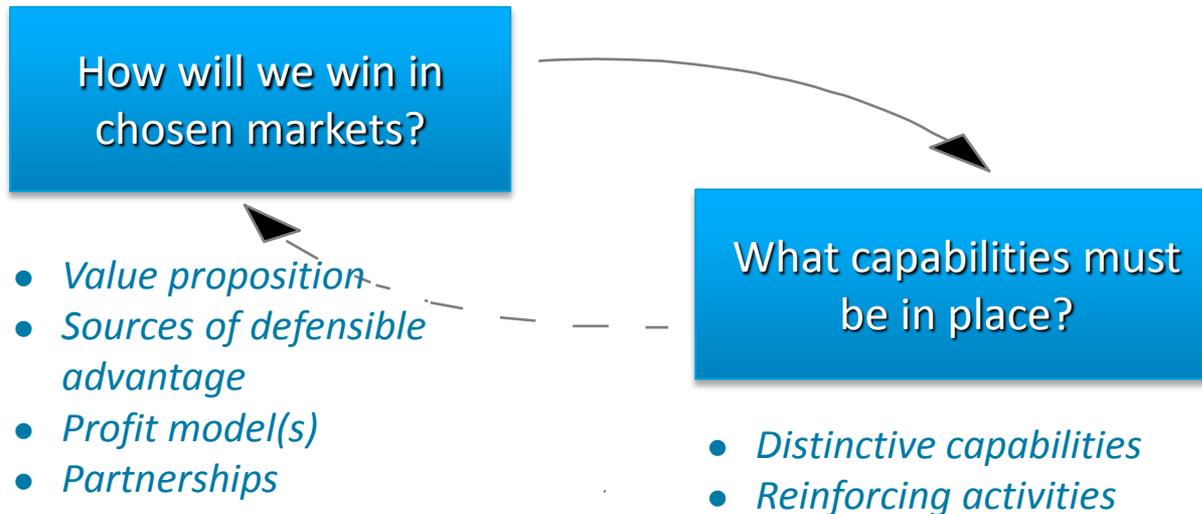
# Utilizing strategic framework developing global project delivery strategy

Identify the capabilities required for success



# Developing the Required Capabilities

Clarity on “How to Win” will drive focus on the necessary investments in capabilities



## Key Business Questions

- How significant are our capability gaps to deliver against “How to Win?”
- What is the best way to close those gaps (e.g., buy vs build vs. partner)?
- How much will we have to invest? How long will it take to break even?

# Capabilities – Top areas of focus

Identify the key capabilities required to deliver successful capital projects



# Trends in capital project delivery

## Trends and developments in delivering capital projects globally

### Increase design build

- Firms are using more of the design-build delivery system to minimize risks & reduce delivery schedules by overlapping design & construction phases

### More self perform

- War for talent will continue to challenge global expansion. With a lack of skilled labor pools to pull from, EPC are attempting to bring in house and self perform

### Outsourcing / Offshoring

- Increasing globalization enables outsourcing of services to offshore service providers, such as low-cost engineering center's

### Cloud / application program management

- Project management and field operations are making transitions to cloud based applications for real time data

### Big Data – risk analytics/PRO

- Compilation of historical data is leading to comprehensive risk management practices used in forecasting and controlling large, challenging projects

### Continued ERP/PMCS integration

- Large ERP platforms continue to fine tune and integrate their program management control systems

# The Flexible BMO Solution to Expansion

# What is Flexible Business Model Optimization (BMO) in a nutshell?

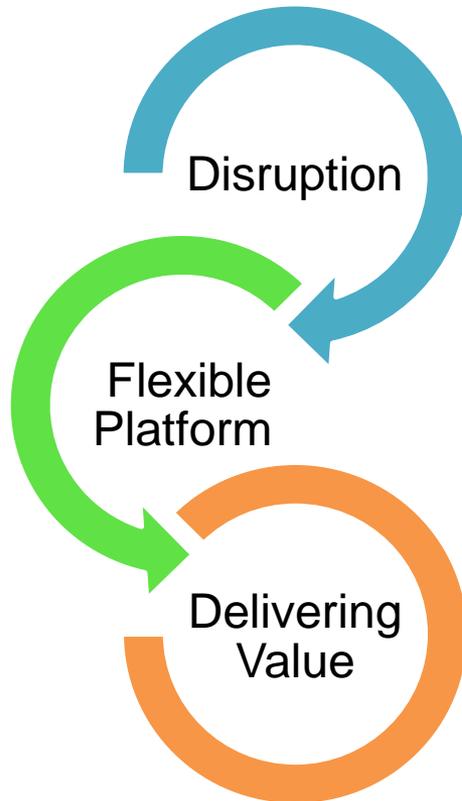
- Align transfer pricing/international tax flows with business flows (i.e. use the Company's existing hub services model to enhance tax flows) – with no disruption to business
- Leverage the Hub services model to align intercompany pricing and defend returns for operating entities (in high tax jurisdictions)
- Enhance tax flows by attributing value to: (1) Consistency of service rendering, (2) Effectiveness, and (3) Efficiencies/Synergies/Cost Savings
- Flexibility is obtained as the BMO model can be tailored to match the service offerings of the hub:
  - Pliable with regards to rendering of services
  - Easily adapts to changes and needs

# What are the Benefits?

- Combining assets and resources may lead to more operational efficiencies and efficient distribution of “know-how” and “leading practices across local entities, which ultimately leads to higher profits (i.e., key value driver of the business)
- Co-location of regional leadership may result in improved communications and quicker decision making
- Harmonized and standardized processes may result in inform and business process synergies and more efficient personnel
- Simplified functional and financial profile in local entities may | potentially lower support function needs
- Improved visibility into local performance based on standardiz performance indicators



# Why a Flexible Model?



- **Disruption** – Business model evolution requires new methods for mitigating tax risk and capturing value
- **Flexible Platform** – Sustainability tax reduction achieved through a flexible and forward thinking strategic platform
- **Delivering Value** – Creating a solution using a ‘bottom up’ fact based approach that will be BEPS compliant

**Building a flexible BMO platform will increase the value we can bring to clients**

# Transforming Disruption into Opportunity

Increasing levels of business model change driven by standardization and process improvement



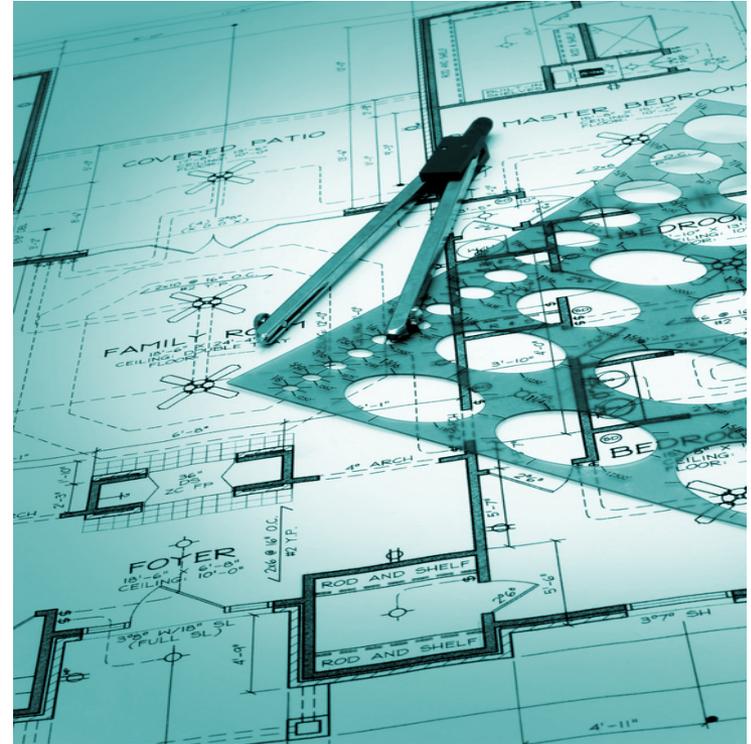
Legacy global tax structures and transfer pricing too quickly become obsolete



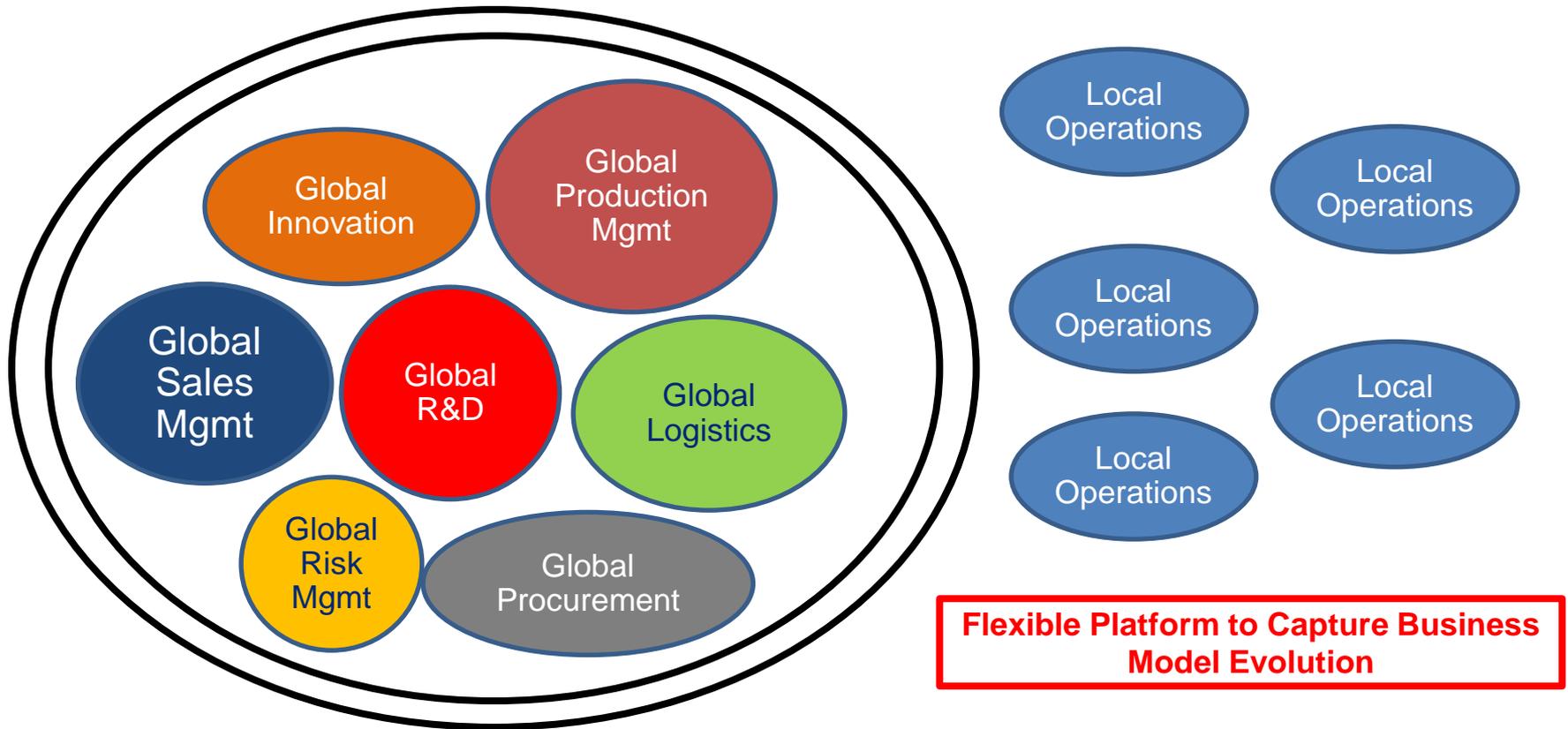
Risk is created when business model change goes unnoticed



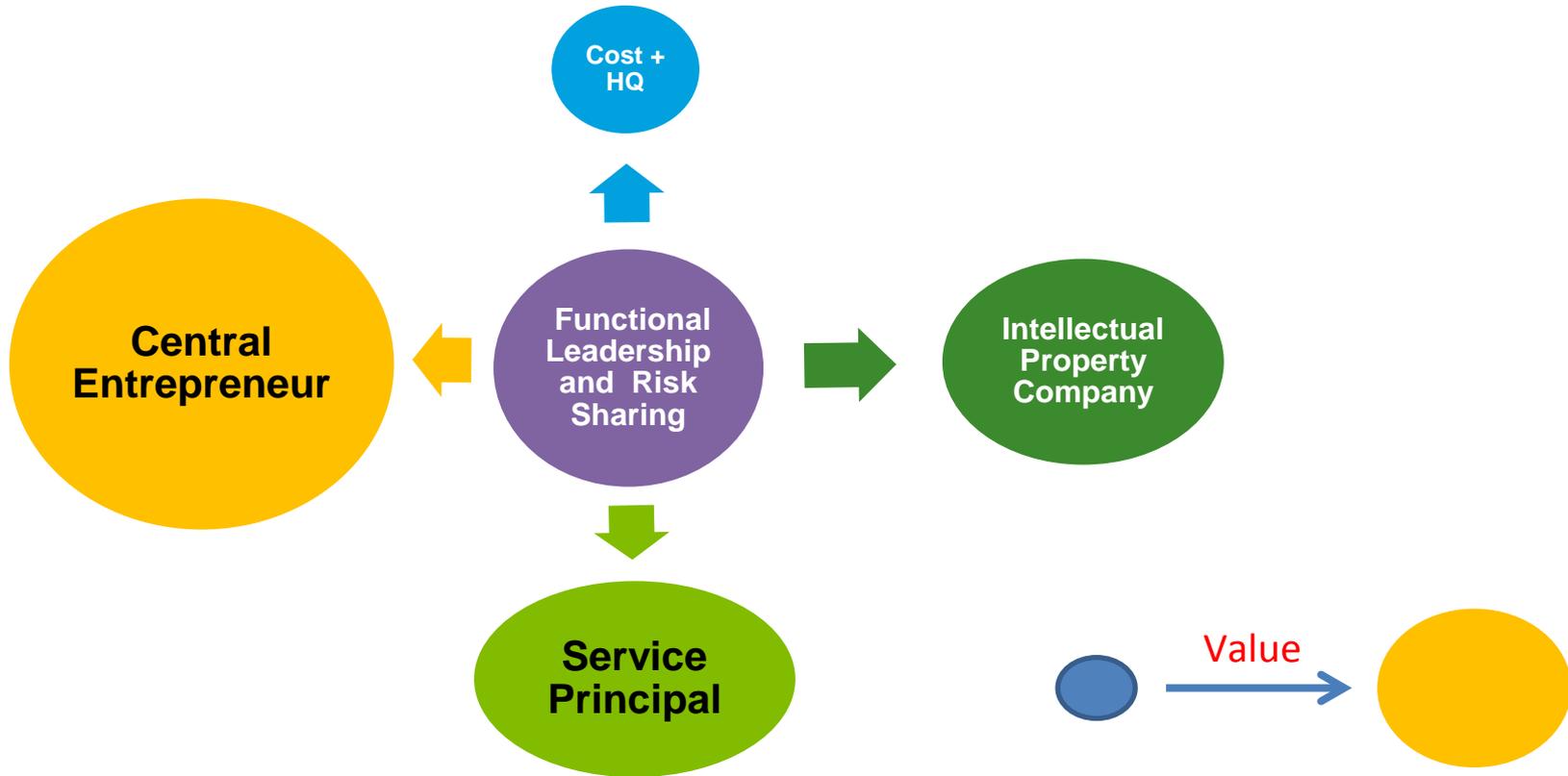
**Change will continue**  
**A Flexible Platform is required**



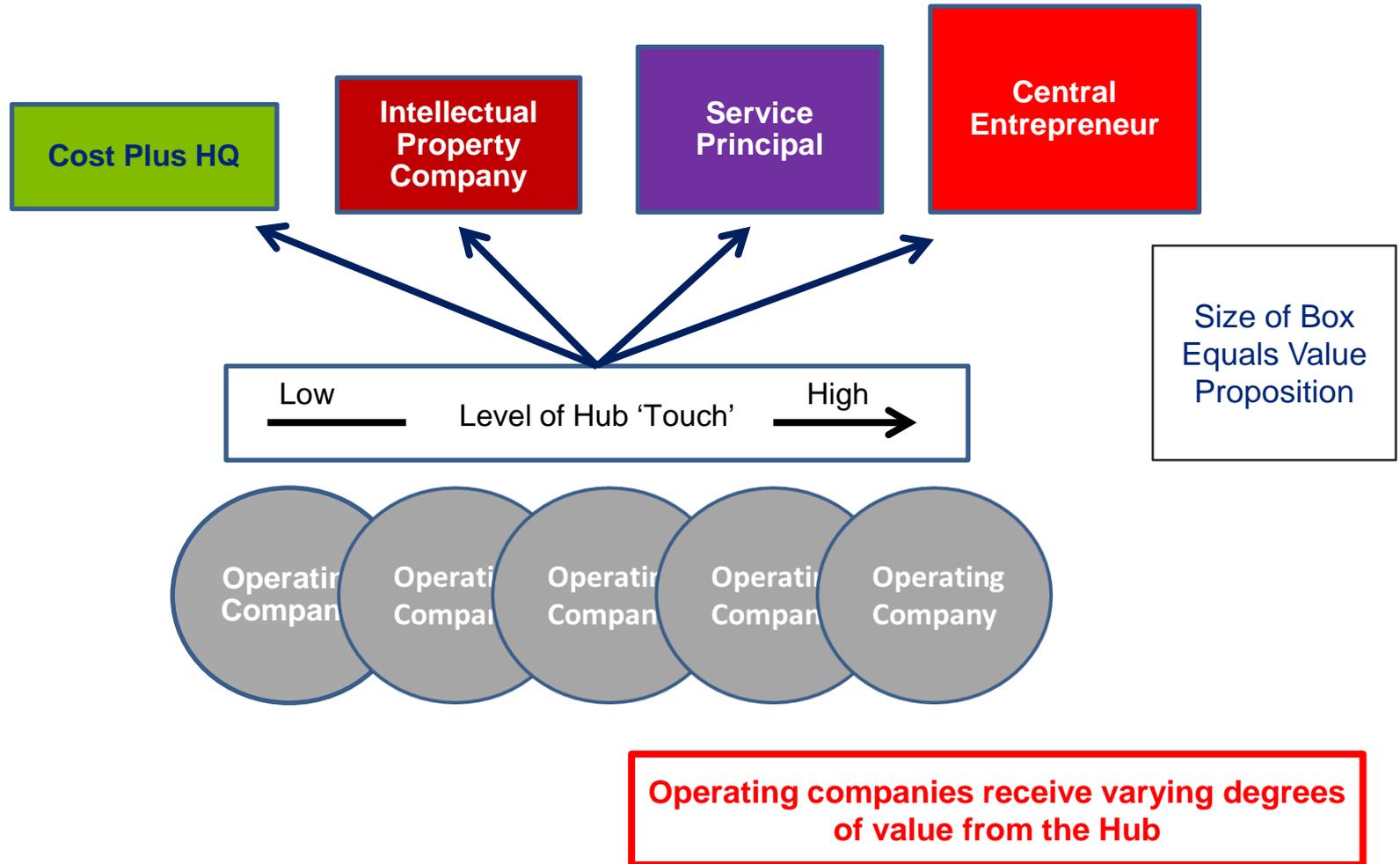
# Capturing Dispersed Value in a Hub



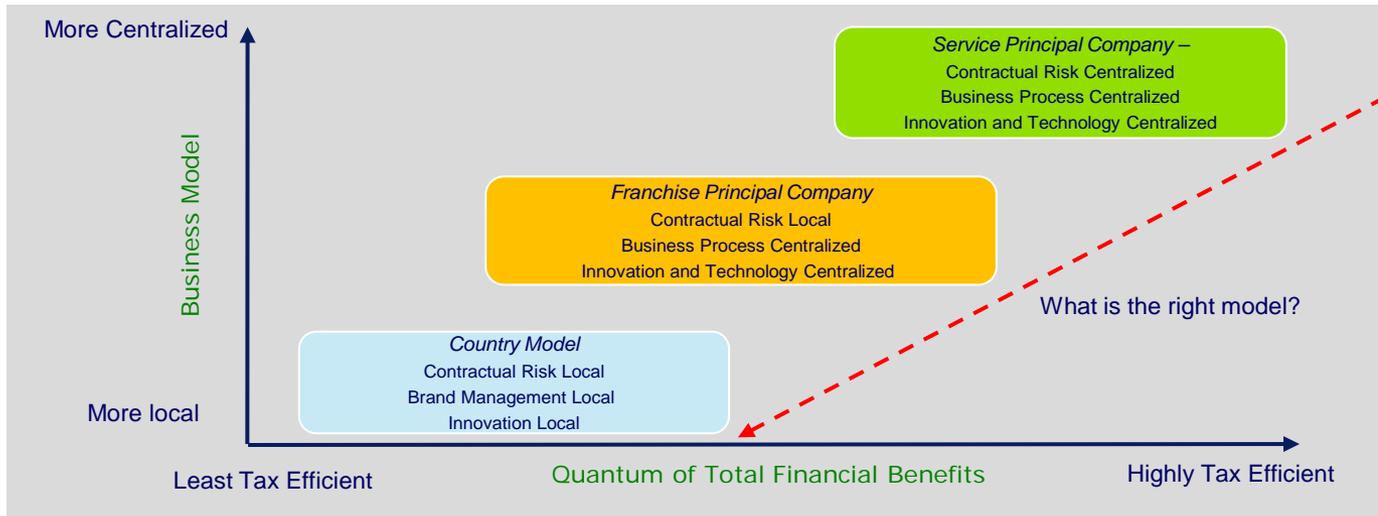
# Flexible Hubs – Functional Variability



# Flexible Hubs - Coverage Variability



# Business model evolution



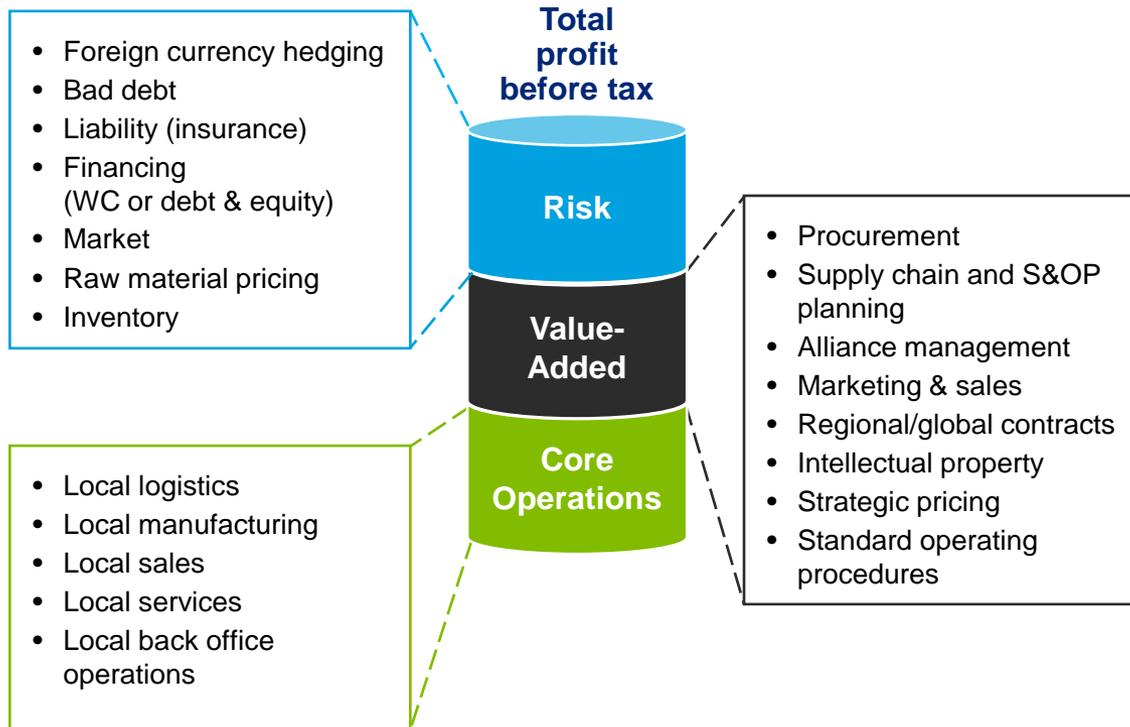
Companies have adopted a range of tax aligned operating models depending upon the degree of centralization within their business model

- Differing operating and contracting models have led to a range of options when trying to align a service business from a tax perspective.
- Critical long-term success factor is that the business must drive the tax model so the model is sustainable



# The Benefits of a Centralized Structure

Carefully planning the location of key profit drivers



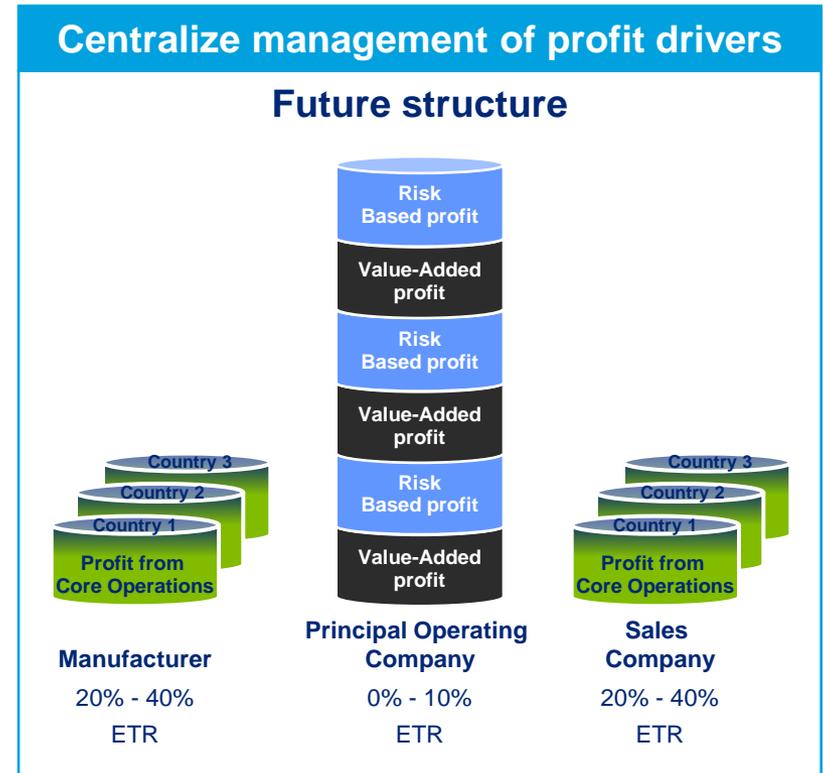
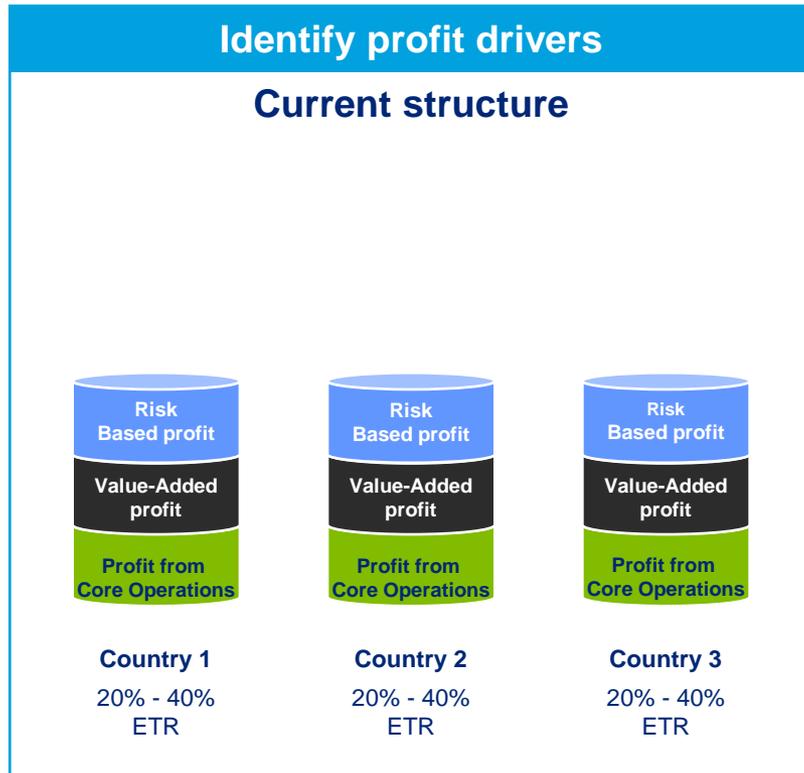
## Profit is primarily attributable to three areas:

- The successful management of risks
  - Those functions within the business which actively manage the risks the company is exposed to (e.g., financial, environmental, market, etc.)
- Exploitation of value-added functions
  - Those functions which drive the company's competitive advantage – i.e., those activities which enable it to succeed beyond its industry peers and make above industry average profits
- Excellence in core operations
  - Those functions which are necessary to operate in the market – i.e., the critical success factors of the industry in which it operates

The first task is to identify the profit drivers and their current locations in the business

# Accruing Profits to a Lower-Tax Jurisdiction

Focusing on the value added and risk proportion of the profit

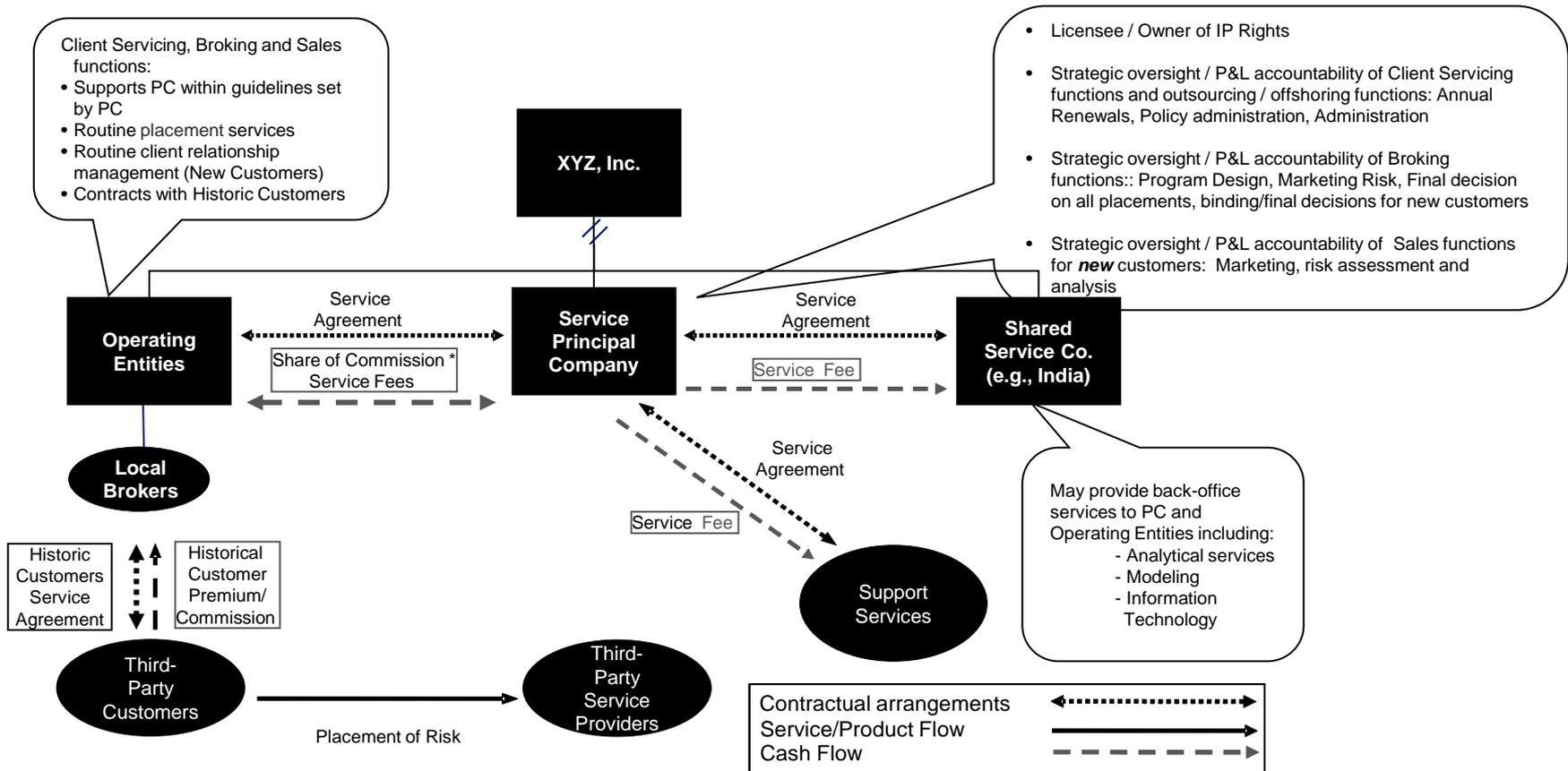


# Key Takeaways from Successful Implementation

- Most local tax jurisdictions understand and recognize the “Service Principal” concept
- Most tax authorities are also familiar with underlying comparable company analysis (i.e. third party companies or franchise comparables)
- Typically, clients have been able to negotiate Advanced Pricing Agreements with several local jurisdictions, as well as rulings for a favorable tax rate for the service principal
- Ability to factor in the next area of “value drivers” outside of typical IP planning (i.e. cost sharing or licensing)
- Service Principals may be potentially implemented across the spectrum of industries (i.e. technology, retail, manufacturing, etc.)
- Business transformation often leads to planning opportunities
- (in many cases, transfer pricing policies may need to catch up with the business. i.e. transfer pricing policy undervalues the return for “central hubs”)



# What Does an SPC Structure Look Like?



# Service Principals in the Age of BEPS

# “Substance” in an SPC business model

- Indicative Roles under an SPC model that reside in the Hub
  - Regional/Global Leadership (P&L Authority)
  - Global Business Unit Senior Management located within Region
  - Pricing Leadership located within Region
  - Innovation Leadership – Stage Gate Decision Makers located within Region
  - Center of Excellence Leadership located within Region
  - Business Development Leadership located within Region
  - Roles negotiating and concluding contracts with customers (SPC Central Contracting Model)
- Indicative Roles in an SPC model that remain Local
  - Roles negotiating and concluding contracts with customers (SPC Local Contracting Model)
  - Roles executing services for customers
  - Shared services (Finance, HR, Legal, Tax, Accounting, etc.)
  - Performance of functions under centralized leadership (e.g., innovation efforts)

# BEPS and Service Principals

- The OECD published its Action Plan on Base Erosion and Profit Shifting (“BEPS”) in June of 2013.
- In general, the intent of the OECD is to determine if contractual arrangements between related parties align with the economics of any given companies global supply chain.
- In most instances, the OECD is focusing on income earned in low tax countries with limited substance (physical location of key decision makers) and/or the use of legal entities that are taxed differently among its member States.

# BEPS and Service Principals

- Within the OECD, several participants are concerned that source countries (the location of the ultimate consumer of goods and services) are not being compensated fairly relative to low tax countries that own critical intellectual property, but lack “boots-on-the-ground” with respect to crucial leadership positions.
- Service Principal construct allows for addressing the “substance” needs of BEPS and the contractual framework/interaction
  - Contracts can be tailored to ensure that all tax jurisdictions can recognize the actual framework, and behavior of parties
  - Allows for the use of substance, processes and people systematically to tell a “BEPS compliant” story
  - Proactively addresses BEPS related concerns on using “cost plus” remuneration mechanisms for value added service providers

# Questions?



# Conference Resources

A copy of this presentation may be downloaded from the conference website.

To access this presentation – and all other presentations from this conference, please use the following url:

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