

benefit shares are expected to vary significantly over the years in which benefits will be received, it may be necessary to use the present discounted value of the projected benefits to reliably determine each controlled participant's share of those benefits. If it is not anticipated that benefit shares will significantly change over time, current annual benefit shares may provide a reliable projection of anticipated benefit shares. This circumstance is most likely to occur when the cost sharing arrangement is a long-term arrangement, the arrangement covers a wide variety of intangibles, the composition of the covered intangibles is unlikely to change, the covered intangibles are unlikely to generate unusual profits, and each controlled participant's share of the market is stable.

(B) *Unreliable projections.* A significant divergence between projected benefit shares and actual benefit shares may indicate that the projections were not reliable. In such a case, the district director may use actual benefits as the most reliable measure of anticipated benefits. If benefits are projected over a period of years, and the projections for initial years of the period prove to be unreliable, this may indicate that the projections for the remaining years of the period are also unreliable and thus should be adjusted. Projections will not be considered unreliable based on a divergence between a controlled participant's projected benefit share and actual benefit share if the amount of such divergence for every controlled participant is less than or equal to 20% of the participant's projected benefit share. Further, the district director will not make an allocation based on such divergence if the difference is due to an extraordinary event, beyond the control of the participants, that could not reasonably have been anticipated at the time that costs were shared. For purposes of this paragraph, all controlled participants that are not U.S. persons will be treated as a single controlled participant. Therefore, an adjustment based on an unreliable projection will be made to the cost shares of foreign controlled participants only if there is a matching adjustment to the cost shares of controlled participants that are U.S. persons. Nothing in this paragraph (f)(3)(iv)(B) will prevent the district director from making an allocation if the taxpayer did not use the most reliable basis for measuring anticipated benefits. For example, if the taxpayer measures anticipated benefits based on units sold, and the district director determines that

another basis is more reliable for measuring anticipated benefits, then the fact that actual units sold were within 20% of the projected unit sales will not preclude an allocation under this section.

(C) *Foreign-to-foreign adjustments.* Notwithstanding the limitations on adjustments provided in paragraph (f)(3)(iv)(B) of this section, adjustments to cost shares based on an unreliable projection also may be made solely among foreign controlled participants if the variation between actual and projected benefits has the effect of substantially reducing U.S. tax.

(D) *Examples.* The following examples illustrate this paragraph (f)(3)(iv):

*Example 1.* (i) Foreign Parent (FP) and U.S. Subsidiary (USS) enter into a cost sharing arrangement to develop a new car model. The participants plan to spend four years developing the new model and four years producing and selling the new model. USS and FP project total sales of \$4 billion and \$2 billion, respectively, over the planned four years of exploitation of the new model. Cost shares are divided for each year based on projected total sales. Therefore, USS bears 66⅔% of each year's intangible development costs and FP bears 33⅓% of such costs.

(ii) USS typically begins producing and selling new car models a year after FP begins producing and selling new car models. The district director determines that in order to reflect USS' one-year lag in introducing new car models, a more reliable projection of each participant's share of benefits would be based on a projection of all four years of sales for each participant, discounted to present value.

*Example 2.* U.S. Parent (USP) and Foreign Subsidiary (FS) enter into a cost sharing arrangement to develop new and improved household cleaning products. Both participants have sold household cleaning products for many years and have stable market shares. The products under development are unlikely to produce unusual profits for either participant. The participants divide costs on the basis of each participant's current sales of household cleaning products. In this case, the participants' future benefit shares are reliably projected by current sales of cleaning products.

*Example 3.* The facts are the same as in *Example 2*, except that FS's market share is rapidly expanding because of the business failure of a competitor in its geographic area. The district director determines that the participants' future benefit shares are not reliably projected by current sales of cleaning products and that FS's benefit projections should take into account its growth in sales.

*Example 4.* Foreign Parent (FP) and U.S. Subsidiary (USS) enter into a cost sharing arrangement to develop synthetic fertilizers and insecticides. FP and USS share costs on the basis of each participant's current sales of fertilizers and insecticides. The market shares of the participants have been stable for fertilizers, but FP's market share for insecticides has been expanding. The district director determines that the participants'

projections of benefit shares are reliable with regard to fertilizers, but not reliable with regard to insecticides; a more reliable projection of benefit shares would take into account the expanding market share for insecticides.

*Example 5.* U.S. Parent (USP) and Foreign Subsidiary (FS) enter into a cost sharing arrangement to develop new food products, dividing costs on the basis of projected sales two years in the future. In year 1, USP and FS project that their sales in year 3 will be equal, and they divide costs accordingly. In year 3, the district director examines the participants' method for dividing costs. USP and FS actually accounted for 42% and 58% of total sales, respectively. The district director agrees that sales two years in the future provide a reliable basis for estimating benefit shares. Because the differences between USP's and FS's actual and projected benefit shares are less than 20% of their projected benefit shares, the projection of future benefits for year 3 is reliable.

*Example 6.* The facts are the same as in *Example 5*, except that in year 3 USP and FS actually accounted for 35% and 65% of total sales, respectively. The divergence between USP's projected and actual benefit shares is greater than 20% of USP's projected benefit share and is not due to an extraordinary event beyond the control of the participants. The district director concludes that the projection of anticipated benefit shares was unreliable, and uses actual benefits as the basis for an adjustment to the cost shares borne by USP and FS.

*Example 7.* U.S. Parent (USP), a U.S. corporation, and its foreign subsidiary (FS) enter a cost sharing arrangement in year 1. They project that they will begin to receive benefits from covered intangibles in years 4 through 6, and that USP will receive 60% of total benefits and FS 40% of total benefits. In years 4 through 6, USP and FS actually receive 50% each of the total benefits. In evaluating the reliability of the participants' projections, the district director compares these actual benefit shares to the projected benefit shares. Although USP's actual benefit share (50%) is within 20% of its projected benefit share (60%), FS's actual benefit share (50%) is not within 20% of its projected benefit share (40%). Based on this discrepancy, the district director may conclude that the participants' projections were not reliable and may use actual benefit shares as the basis for an adjustment to the cost shares borne by USP and FS.

*Example 8.* Three controlled taxpayers, USP, FS1 and FS2 enter into a cost sharing arrangement. FS1 and FS2 are foreign. USP is a United States corporation that controls all the stock of FS1 and FS2. The participants project that they will share the total benefits of the covered intangibles in the following percentages: USP 50%; FS1 30%; and FS2 20%. Actual benefit shares are as follows: USP 45%; FS1 25%; and FS2 30%. In evaluating the reliability of the participants' projections, the district director compares these actual benefit shares to the projected benefit shares. For this purpose, FS1 and FS2 are treated as a single participant. The actual benefit share received by USP (45%) is within 20% of its projected benefit share