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Exploring the Margins of Transfer Pricing: Evidence from Swiss Firms

This paper examines the determinants and margins of profit shifting through transfer pricing. We develop a theory model, where transfer pricing patterns are governed by a generalized concealment cost function (CCF). Our empirical analysis draws on micro-level data about transaction-level exports and imports, firm-level characteristics, and tax differentials between regions in Switzerland and countries abroad. We find that more productive multinational firms deviate less from the arm's length price and trade lower quantities, compared to MNEs with lower productivity. Moreover, the decision of firms to engage in transfer pricing depends negatively on a fixed cost component in the CCF, as well as on trade costs. The model allows us to estimate a theory-consistent concealment cost function, which can be used for counterfactual analysis.