

APPENDIX 1

Questionnaire : functional analysis

Source: IRS 2006, exhibit 4.61.3-4

For guidance in performing a functional analysis of a business this questionnaire sets out a list of generic questions that might be used to gain an understanding of the various functions, risks, and intangibles. The list is not intended to be exhaustive and should be tailored to suit the needs of the specific business entity being reviewed.

ANALYSIS OF FUNCTIONS

I. Manufacturing

A. Materials purchasing

1. What materials or partly finished goods are purchased?
2. From whom are purchases made?
3. Are any purchases made from related companies?
4. Where and how are raw materials purchases?
5. Who performs the purchasing function?
6. Who plans purchasing schedules?
7. Who negotiates purchasing arrangements?
8. Who approves the vendor as being of acceptable quality?
9. Do purchasing decisions require head office approval?
10. What are the other approvals required? Who makes these approvals?
11. Are any purchases made on consignment?
12. What are your major risks?

B. Inventory

1. Where is inventory held?
2. Who controls the levels of inventory?
3. How are inventory levels controlled?
4. Is there a computer system?
5. Are any purchases made on consignment?
6. How many days of inventory are on hand?
7. Has there ever been a case, for whatever reason, where you were stuck with excess inventory?
8. Who bears the cost of obsolete inventory?
9. What are your major risks?

C. Production equipment

1. Who determines the purchasing budget?
2. Who negotiates purchasing?
3. Who maintains the plant?
4. Who has expenditure authority for capital equipment?
5. Who writes specifications for the plant?
6. From whom is production equipment purchased?
7. Are any purchases made from related companies?
8. Do you have discretion over the equipment used?
9. Can you modify the equipment?

10. What decisions require head office approval?
11. What are the approvals required?

D. Production scheduling

1. Who is responsible for production scheduling decisions?
2. What factors enter the decisions?
3. When are the decisions made?
4. Is a computer system used?
5. What decisions require head office approval?
6. What are the approvals required?
7. What are your major risks?
8. Does your distributor buy everything you manufacture?

E. Manufacturing and process engineering

1. What products are produced?
2. Who designed the products and who owns the technology?
3. What is the manufacturing process?
4. Who developed the original process?
5. Have any improvements been made locally?
6. Is it possible to compare productivity between the subsidiaries in the group?
7. Have you ever utilized a third party to produce your products?

F. Package and labeling

1. What packaging and labeling is done?
2. Where is it done?
3. Who makes the decisions in relation to packaging and labeling?
4. Have you complete autonomy to make such decisions?

G. Quality control

1. What form does quality control take?
2. Who sets finished product quality standards and procedures?
3. Who performs the quality control and who bears the cost?
4. Who provides the equipment and techniques for quality control?
5. How much product is lost because it fails quality and control checks?
6. What are your major risks?
7. What decisions require head office approval?
8. What are the approvals required?

H. Shipping of products

1. Who pays freight charges for product in and out?
2. Who arranges shipping of products?
3. Who ships your products?
4. Where are the products shipped?
5. How are they shipped?
6. Who is responsible for the selection of shippers?
7. Who is responsible for shipping deadlines?
8. What are your major risks?
9. What decisions require head office approval?
10. What are the approvals required?

II. Research and development

1. What research and development do you carry out?
2. Is any research and development carried out on your behalf by related companies?

3. Do you commission third parties to carry out research and development on your behalf?
4. Where are products designed?
5. What input do distributors have on manufacturing, product design or product modifications?
6. How important is the development of patents in the industry?
7. What patents do you own? Describe the unique products created by each patent.
8. What unpatented technical know-how have you developed that might differentiate your products from competitors, create import cost efficiencies, or give you an advantage in increasing your market share?
9. What decisions require corporate head office approval?
10. What are the approvals required?
11. Who formulates the budget?
12. Are license agreements in existence between you and related companies or third parties?
13. Is there a cost sharing agreement in force and if so what are the details?
14. Provide a copy of the cost sharing agreement and the relevant details.

III. Marketing

A. Strategic

1. Do you carry out your own marketing?
2. Are market surveys performed? Do you monitor market demand?
3. What decisions require head office approval?
4. What are the approvals required?
5. Who are your competitors?
6. Who assesses demand in foreign markets?
7. What are the risks related to demand for your products?
8. Who formulates the marketing budget?
9. Does your distributor always buy what your manufacturer produces?
10. Has your manufacturer ever refused to fill an order?
11. Do related companies carry out marketing on your behalf?
12. Are third-party distributors used?
13. Who chooses, authorizes, and controls third-party distributors?

B. Advertising, trade shows, etc.

1. What forms of marketing do you utilize?
2. What forms of advertising are used? Who pays for it?
3. Are trade shows used and if so who organizes them and who pays for them?
4. Are samples provided to distributors?
5. Who produces product brochures, specification sheets, etc.?
6. What marketing assistance do you receive?
7. What decisions require head office approval?
8. What are the approvals required?

IV. Sales and distributions

A. Sales

1. How are sales made and who is involved?
2. Who issues the invoice to the customer?
3. Who issues the invoice to you?
4. Who formulates the projections and sets targets?

5. Where are sales orders received?
6. Who is responsible for the achievement of sales targets?
7. Who negotiates sales contracts? Do they operate autonomously?
8. Does your distributor always buy what your manufacturer produces?
9. How much is sold to related companies?
10. Are only finished goods shipped from here?
11. Who are your competitors?
12. What are the risks related to demand for your products?
13. What decisions require corporate head office approval?
14. What are the approvals required?
15. Are products exported? If so, who is responsible for the export function?
16. What are the major risks in selling products in foreign countries?

B. Quality control

1. What form does quality control take?
2. Who sets finished product quality standards and procedures?
3. Who performs the quality control and who bears the cost?
4. Who provides the quality control and who bears the cost?
5. How much product is rejected by customers as below standard?
6. Who bears the loss on defective products?
7. What are your major risks?
8. What decisions require head office approval?
9. What are the approvals required?

C. Freight

1. Who pays freight charges for product in and out?
2. Who arranges shipping of products?
3. Who ships your products? To where? How?
4. Who is responsible for the selection of shippers?
5. Who is responsible for shipping deadlines?
6. What are your major risks?
7. What decisions require head office approval?
8. What are the approvals required?

D. Inventory

1. Do you actually receive the goods and hold stock?
2. Where is stock held?
3. Who controls the levels of inventory?
4. How are inventory levels controlled? Is there a computer system?
5. Are any purchases made on consignment?
6. How many days of inventory are on hand?
7. Has there ever been a case, for whatever reason, where you were stuck with excess inventory?
8. Who bears the cost of obsolete inventory?
9. What are your major risks?

E. Installation and after-sales services

1. Do you install your products?
2. Do you provide after-sales services? If so, describe the service.
3. Does any company carry out product repairs and who bears the cost?
4. Who bears the cost of installation and after-sales service?
5. Do you provide product guarantees?
6. Who bears warranty costs?

V. Administration and other services

A. General administration

1. Is there a complete administration function?
2. Do related companies perform any administration for you?
3. What decisions require corporate head office approval?
4. What are the approvals required?
5. Who is responsible for administrative codes of practice?

B. Pricing policy

1. Who determines the product pricing?
2. What is the pricing policy for the various goods and services?
3. What are your major risks?
4. What decisions require corporate head office approval?
5. What are the approvals required?

C. Accounting

1. What accounting functions are carried out? By whom?
2. Where are the financial reports prepared?
3. What decisions require head office approval?
4. What are the approvals required?
5. Is a bank account maintained? For what purpose?
6. Who has check signatory authority? What are the authority limits?
7. Do you bear the credit risk on sales to customers?
8. Who pays product liability insurance premiums?
9. Who arranges and pays for other insurance?

D. Legal

1. Who is responsible for legal matters?
2. What decisions require head office approval?
3. What are the approvals required?

E. Computer processing

1. Is computer processing and programming done here? If not, by whom and where?
2. Who developed the software and is any charge made for it?
3. Who has expenditure authority for capital equipment?
4. What decisions require head office approval?
5. What are the approvals required?

F. Finance/loans/credit

1. Are there any intercompany loans or long-term receivables and, if so, is interest charged?
2. What trade credit terms are received and given?
3. Is interest paid or charged if credit periods are exceeded?
4. Who is responsible for borrowing requirements?
5. What are your major risks?
6. What decisions require head office approval?
7. What are the approvals required?

G. Personnel

1. Are there any compensation to or from overseas affiliates?
2. What positions do they hold in the company?
3. What training do you provide your employees?
4. What is the length of the training period?

5. Is there on-the-job training?
6. Where is management training done?
7. What is the staff turnover rate?
8. Are all employees on your payroll?
9. Who is responsible for the employment of staff?
10. What decisions require head office approval?
11. What are the approvals required?

H. Use of property / leasing

1. Is property owned or leased from affiliates?
2. Do you lease property to affiliates?
3. Who is responsible for this function?

VI. Executive

1. To whom does the general manager report?
2. Does anyone report to the parent company besides the general manager?
3. Who is responsible for dealing with government agencies?
4. What are some of the regulatory requirements?
5. Has the parent ever told you to use more procedures than you have developed?
6. How does manufacturing site selection occur?
7. Where does the initial impetus in relation to corporate decisions come from?
8. What decisions require head office approval?
9. What are the approvals required?

ANALYSIS OF RISKS

I. Market risk

1. What are the market risks?
2. Do you bear the market risks? If not, who does?
3. How significant are the market risks?

II. Inventory risk

1. Does inventory become obsolete?
2. Who bears the cost of obsolete inventory?
3. Do you provide warranties in relation to finished goods?
4. Who bears the cost of returns under warranty?

III. Credit and bad debt risk

1. What credit terms are given and received?
2. Do you bear the cost of bad debts? If not, who does?
3. Is this a significant risk?

IV. Foreign exchange risk

1. Are you exposed to foreign exchange risk? If so, explain the risks.
2. How significant is the risk?
3. What steps do you take to minimize foreign exchange risk?
4. Do you have a manual that outlines your procedures/policies for dealing with foreign exchange risk? If so, provide a copy.
5. Do you engage in hedging of foreign exchange risk? If so, provide an explanation of your hedging activities.

ANALYSIS OF INTANGIBLES

I. Manufacturing

A. Research and development

1. Have you developed your own products? Are they unique?
2. Have you developed manufacturing processes?
3. How important are these processes to your business? Are they unique?

B. Manufacturing processing/technological know-how

1. Do you possess technological know-how?
2. If so, what is its nature?
3. How important to your business is the know-how?
4. Is the know-how unique?

C. Trademarks/patents, etc.

1. Do you own any trademarks/patents?
2. How significant are they to your business?

D. Product quality

1. Within your industry, and as compared to your competition, how would you rate the quality of your product?

E. Other

1. Are there any other manufacturing intangibles?
2. Request copies of all licensing agreements.

II. Marketing

A. Trademarks/trade names

1. Do you own any trademarks/trade names?
2. How significant are they to your business?

B. Corporate reputation

1. Do you consider that you have a corporate reputation?
2. What is the nature of this reputation?
3. Is corporate reputation significant in your business?

C. Developed marketing organization

1. Do you have a developed marketing organization?

D. Ability to provide service to customers

1. Within your industry, and as compared to your competitors, how would you rate the quality of the services you provide to customers?