



SEMINAR G

Tax issues relating to intangibles



Seminar G

- **Chair**
- Ricardo Escobar C. (Chile)
- **Panel**
- Antonio De Abreu e Silva (Brazil)
- Caroline Silberztein (France)
- Manfred Naumann (Germany)
- Sanjay Puri (India)
- Jesper Barenfeld (Sweden)
- Andrew Solomon (US)
- **Secretary**
- André De Souza Carvalho (Brazil)

Agenda

- Introduction: a view from a business
 - Why do MNEs transfer intangibles? What are the concerns from a business perspective - what is at stake?
- Key issues in the OECD September 16 document
- Definition of intangibles
- Goodwill
- Ownership of intangibles / residual profit
- Valuation of intangibles
- Concluding remarks

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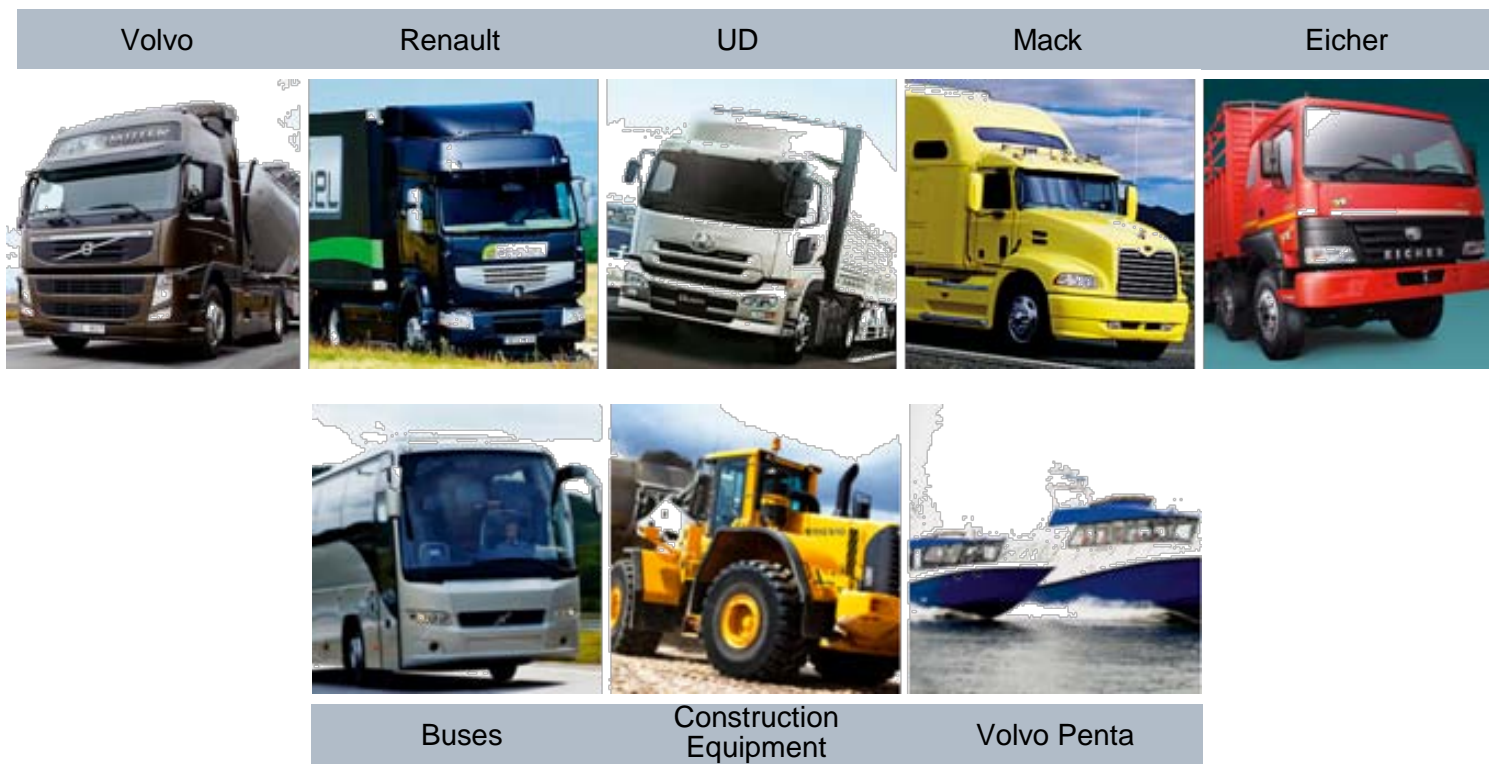


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A VIEW FROM A BUSINESS

Volvo Group

Net sales	R&D spend	Employees	Operations	Legal structure
300BSEK	15BSEK	115,000	190 countries	>300 entities





A Global Value Chain

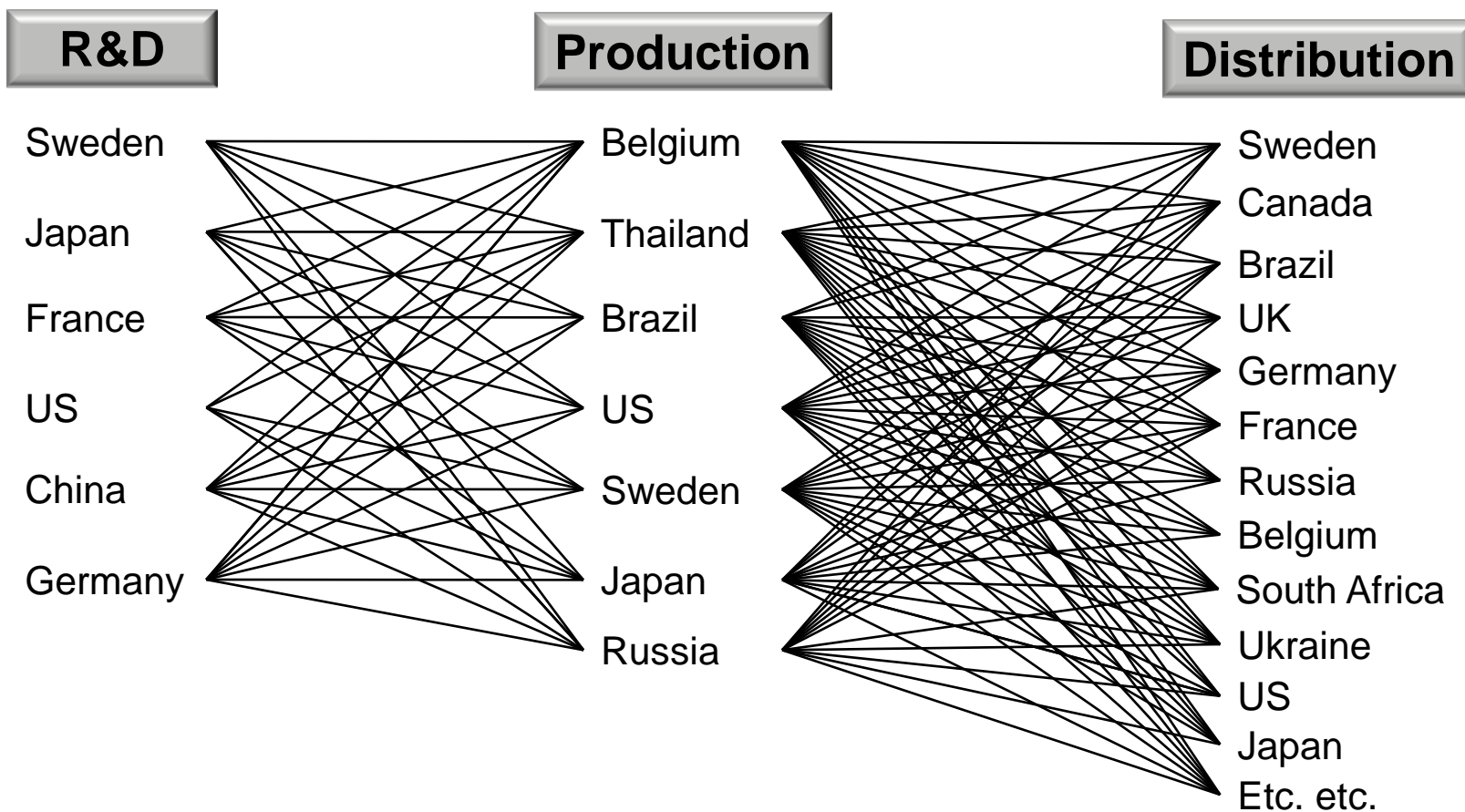


**Volvo
Group Trucks
Technology**



A Global Value Chain

“Engine Alpha project“



Principal Transfer Pricing Model

- Entrepreneurs
 - located in Sweden
 - assumes all major risks and owns all IP
- Service providers
 - receives arm's length remuneration for contract R&D, manufacturing, sales & distribution activities etc.
- Transfer of IP
 - service providers do not assume any risk associated with or retain any right in the IP
 - subsequent to an external acquisition, IP and associated risks are transferred at arm's length to the Entrepreneurs

Why transfer IP?

Comply with
the arm's length
principle

Allow global
development and
utilization of technology

Not BEPS !

Secure central
control of IPR

Secure manageable intragroup
invoicing flows

Where are we currently at?

- Principal TP-models with central ownership of IP are very common
- These models have been in place for a long time
- Often based on a residual concept
- Substance interpreted in line with principles in Ch. IX of the OECD TP-guidelines

Key concerns

From a business perspective

Immediate consequences	Going forward
<ul style="list-style-type: none"> • Reallocation of centrally assumed R&D-expenses? 	R&D activities need to be more centralized to secure central ownership
<ul style="list-style-type: none"> • How handle IP-related risks which have materialized? 	Less local R&D activities
<ul style="list-style-type: none"> • Buy back of technology? 	Less investments and acquisitions to achieve synergies
	Less efficient solution since cannot utilize groups full capacity and skills

Conclusions

- Intra group transfers of IP is key to foster efficiencies and synergies
- Centralization of IP is imperative to manage the ALP in complex value chains
- International rules must be clear and aligned to facilitate transfers and centralization of IP, in particular regarding:
 - **Identification**
 - **Ownership**
 - **Value**
- Huge transitional issues if major change of principles



OECD/G20 Base Erosion and Profit Shifting Project

Guidance on Transfer Pricing Aspects of Intangibles

ACTION 8: 2014 Deliverable



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Transfer pricing aspects of intangibles

OECD SEPTEMBER 16, 2014

RELEASE : KEY ISSUES AND POLICY CONCERNS

Contents of the September 2014 OECD document

- New Chapter VI of the OECD Transfer Pricing Guidelines (“TPG”)
- Amendments to Chapters I-II
- Unfinished business : Shaded portions of Chapter VI not yet fully agreed => 2015 work
- “Special measures” to be considered in 2015
- 33 examples (20 agreed, 13 to be reviewed in 2015)



DEFINITION : WHAT IS AN INTANGIBLE FOR TRANSFER PRICING PURPOSES ?

New OECD definition of intangibles for transfer pricing purposes

“Something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.”

Location Savings

- OECD: a comparability factor
- UN Manual: The net cost savings an MNE realizes as a result of relocation of operations from a high-cost to a low-cost jurisdiction
- The cost savings may be offset at times by “*dis-savings*”
- *Accordingly, only the net location savings (i.e. savings minus dis-savings) may give rise to an extra profit arising to an MNE*

Other amendments to Chapters I-II of the TPG

- **Synergies** may require comparability adjustments
 - “Deliberate concerted group actions” are chargeable.
 - Example on guarantees
 - “Halo effect”
 - Central purchasing function.
- **Assembled workforce** in business restructurings

Location Savings: UN Manual on TP

- India's position
 - Arm's length compensation for cost savings and location rents should be such that both parties would benefit from participating in the transaction.
 - It should not be less than zero and yet not greater than the value of cost savings and locations rents combined
- China's position
 - Illustrated by an example about quantifying TP adjustment in 'Location Savings Advantage' cases where markup on the location saving is to be added to ALP to arrive at 'adjusted' ALP

Definition of intangibles

Issues for discussion

- Why do we need a definition of intangibles for TP purposes? Is it a real issue in practice?
- OECD's definition - is it adequate?
 - Note “something of value” in Chapter IX ; how broad should the definition be ?
- What about UN's definition?
- Legal domestic definitions for different purposes



Indian Tax Laws: 'Intangible Property' for TP purposes

trademarks, trade names, brand names, logos; process patents, patent applications, technical documentation; laboratory notebooks, technical know-how; literary works and copyrights, musical compositions, copyrights, maps, engravings; proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters; industrial design, product patents, trade secrets, engineering drawings and schematics, blueprints, proprietary documentation; customer lists, customer contracts, customer relationship, open purchase orders; favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements; trained and organised work force, employment agreements, union contracts; leasehold interest, mineral exploitation rights, easements, air rights, water rights; institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value, methods, programs, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data; any other similar item that derives its value from its intellectual content rather than its physical attributes, and use of rights regarding

land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or

any other business or commercial rights of similar nature;

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GOODWILL

Policy concern – an example

- Acquisition by MNE of Target Co for 100
- Post acquisition valuation of IP: 70;
goodwill 30
- Business restructuring :
 - Transfer of IP from Target Co to Group IP Co
for 70
 - Conversion of Target Co into Cost Plus R&D

Goodwill / ongoing concern value

The OECD view

- **Not defined**, but “important and monetarily significant part of the compensation” in asset transfers.
- Purchase Price Allocation residual not necessarily appropriate measure.

Goodwill

Issues for discussion

- What is goodwill ?
- To whom does it belong?
- Is it transferable ?
- How is it measured ?



IP OWNERSHIP AND RIGHTS TO RESIDUAL PROFITS (LOSS)

Policy concern

Parent

High tax ;
original IP
development

IP co

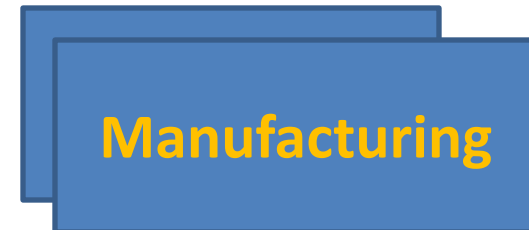
Low tax ;
intragroup
acquisition of IP



High tax / low tax;
further IP
development



High tax ; IP
exploitation



Controversial issues:

- ⇒ Valuation of IP transfer to IP co?
- ⇒ Arm's length remuneration of R&D, marketing and sales functions ?
- ⇒ Arm's length remuneration of IP ownership / funding / risk bearing ?
- ⇒ Interaction with CFC rules ?

Shaded portions of Chapter VI not yet fully agreed => 2015 work

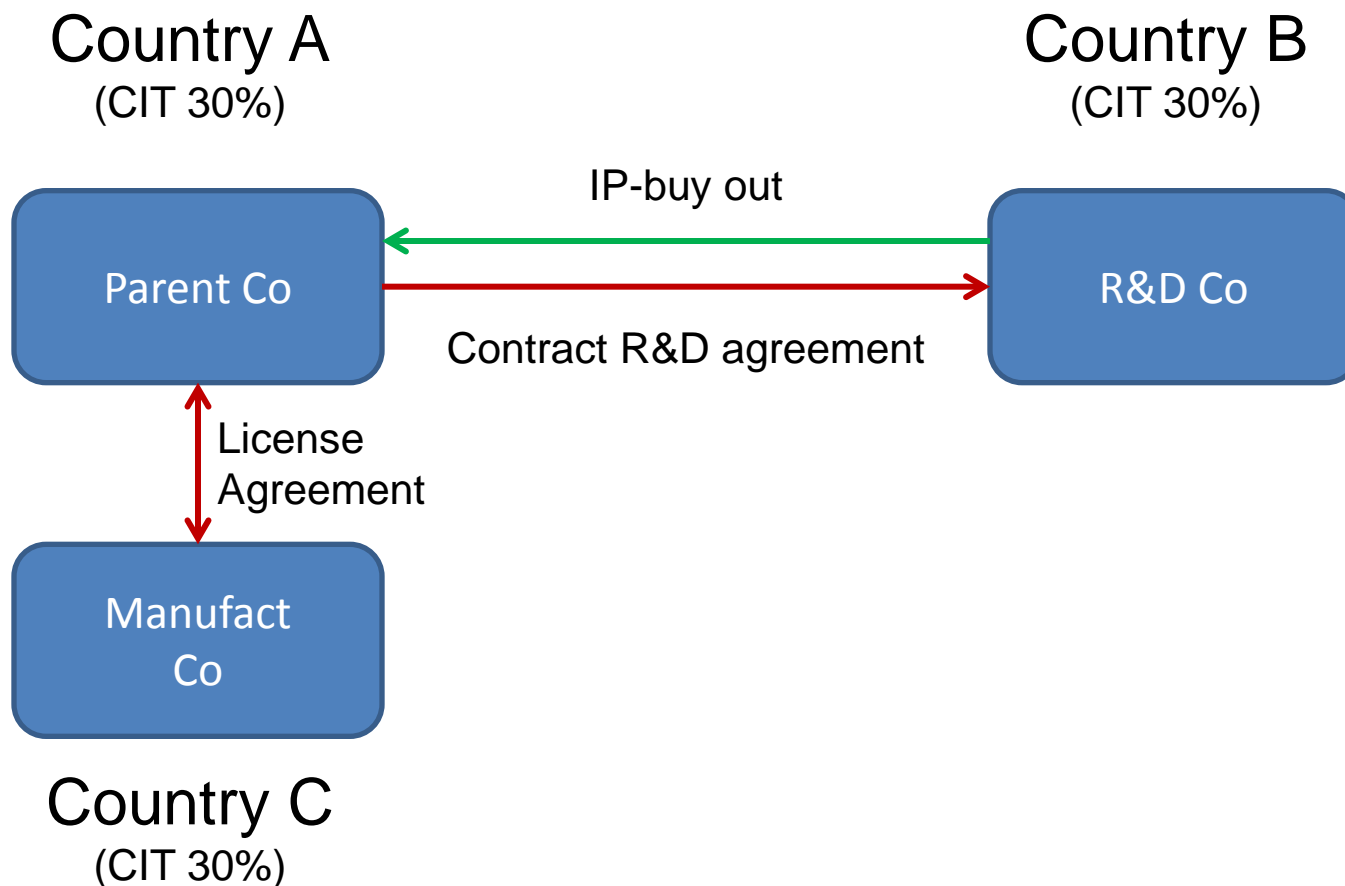
- **Ownership of intangibles** : profits of IP owner / role of contracts / funding / risk versus people functions (Sections B.1 and B.2) ;
- Interaction with work on **risk and recharacterisation** “particularly pronounced”.

Special measures to be considered in 2015 include:

- Limiting the return to entities whose activities are limited to providing funding for the development of intangibles, and potentially other activities, for example by treating such entities as **lenders rather than equity investors** under some circumstances;
- Requiring application of rules analogous to those applied under Article 7 and the Authorised OECD Approach to certain situations involving **excessive capitalisation of low function entities**.

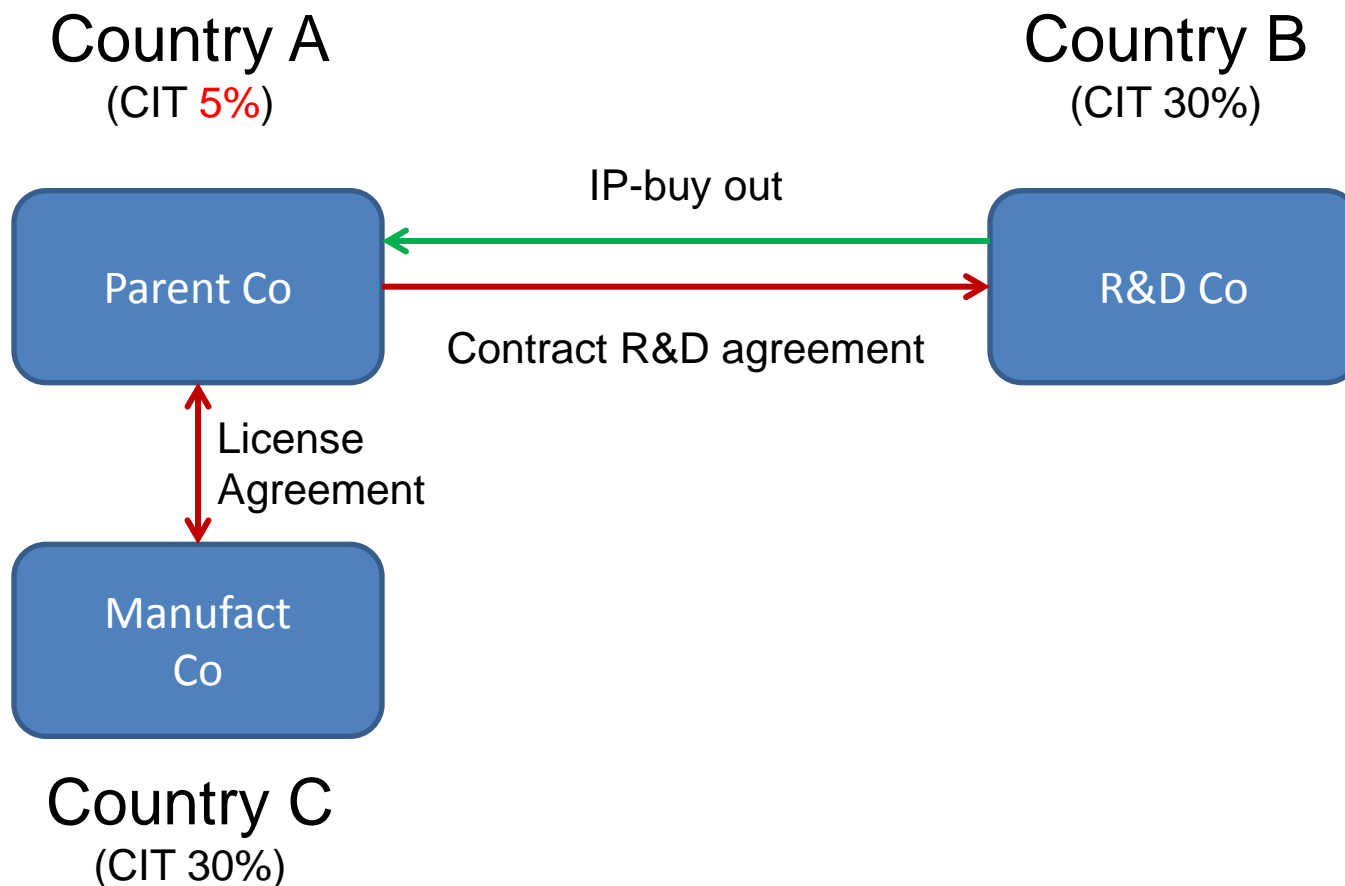
Ownership

Example 1



Ownership

Example 2



Ownership of intangibles

Issues for discussion

- What do we mean by “ownership”?
- Anti abuse or arm’s length?
- What are the criteria?
 - Contracts
 - Control
 - Activity
- Any reasons to deviate from normal ALP-standards? / Use of special measures?



VALUATION OF INTANGIBLES FOR TRANSFER PRICING PURPOSES

Valuation of intangibles

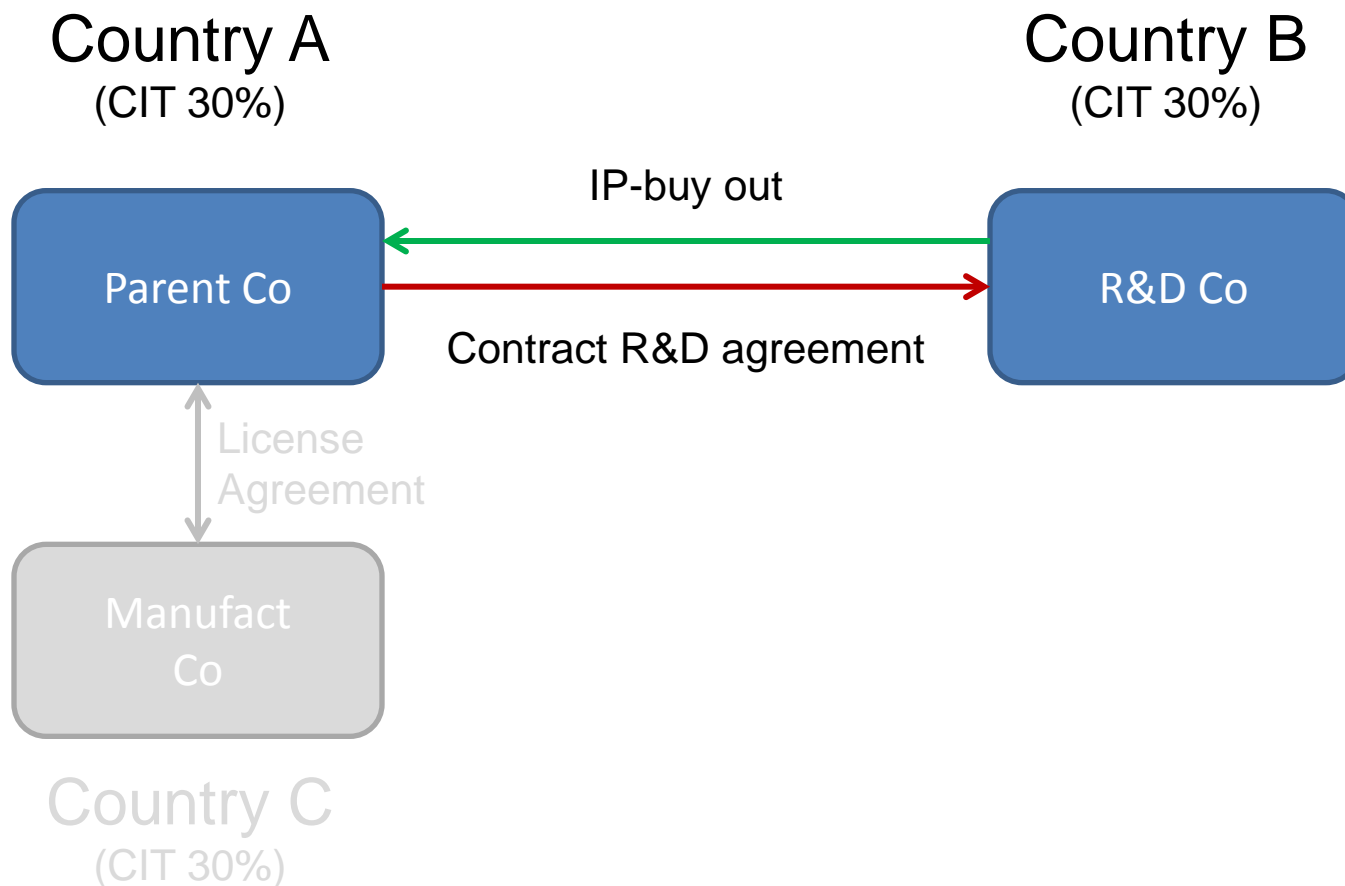
- **New Chapter VI : Valuation** techniques:
Discounted Cash Flow “yes, but...”
- Shaded portions not yet agreed, to be finalized in 2015:
 - Intangibles whose valuation is uncertain at the time of the transaction (Section D.3.);
 - Use of “**other methods**” (TPG 2.9) ;
 - Application of **profit split** methods (TPG 6.145 to 6.149) .

Special measures to be considered in 2015 include:

- Providing tax administrations with authority in appropriate instances to apply rules based on **actual results** to price transfers of hard to value intangibles and potentially other assets;
- Requiring **contingent payment terms and / or the application of profit split methods** for certain transfers of hard to value intangibles;

Valuation

Example 1 – sale of an intangible



Valuation of Intangibles

Issues for discussion

- What can be observed at arm's length?
- Do we find comparables?
- What are the concerns?
- What are the alternatives?



CONCLUDING REMARKS

THE END

- DHANYAWAD
- THANK YOU
- MUCHAS GRACIAS
- VIELEN DANK
- MERCI BEAUCOUP
- MUITO OBRIGADO
- TACK
- **OR ANY OTHER SIMILAR EXPRESSION**