

HAMBURG JOINT SEMINAR
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BEPS AND INTANGIBLES: CRITICAL
ISSUES
(ACTION NO. 8 BEPS ACTION PLAN)

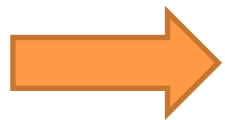


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ACTION NO. 8 BEPS ACTION PLAN

- The Action Plan on BEPS faces the trend of remunerations coming from intangible rights and obligations in low tax jurisdiction allocation



decoupling value creation from taxation

- Action no. 8 involves:
 - A clear definition of intangible
 - The accordance between profits allocation and value creation
 - Speciale measures for transfers of hard – to – value intangibles
 - Issues deriving from cost contribution arrangements

ACTION NO. 8 IN THE ACTION PLAN

- The BEPS work on intangibles is closely related to other BEPS actions contained in the action plan

➤ Critical issues involve the determination of the arm's length conditions for the use or transfer of intangibles

Intangibles as typical hard – to value assets and their ownership is geographically mobile

Intangible peculiarities represent the hard core of transfer pricing policies

ABOUT THE DEFINITION

- What is intended with the word “intangible” for transfer pricing purposes?
 - **Negative condition:** “not a physical asset or a financial asset”
 - **Positive condition:** “something which is capable of being owned or controlled for use in commercial activities” e.g. group synergies /market characteristics are not intangibles
 - **The “main” condition :** “something whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances”

TRANSFER PRICING PURPOSES

- Tp purposes is different from accounting purposes
- Tp purposes is different from an extent of legal, contractual or other forms of protections → separate transferability is not a necessary condition → goodwill is treated as intangible
- Tp purposes independent from the question of whether a particular payment constitutes a royalty in the sense of Art. 12 OECD Model Tax Convention → relevance only at Art. 9 OECD Model purposes

LIMITED RIGHTS IN INTANGIBLES

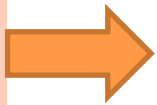
- Intangibles, for tp purposes, are not only “assets” but also “rights” → limited rights in intangibles are themselves intangibles (e.g. an intangible and a license relating to that intangible are considered to be different intangibles for tp purposes)
- Any value transfer is relevant without any distinction between limited and unlimited rights (property)

... Limited right in physical or financial assets are intangibles? (e.g. usufruct on shares)

“NEW” INTANGIBLES?

- Against this backdrop, what about the new properties?

- **Green certificates**
- **Gray certificates**
- **Milk quotas**
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- **Any right, limited or unlimited, capable of revealing ability to pay**

THE RETURN ATTRIBUTABLE TO AN INTANGIBLE ALLOCATION

- The return attributable to an intangible allocation requires the following steps:
 - Identifying the legal owner
 - Identifying the parties performing functions
 - Confirming the consistency between the conduct of the parties and the terms of the relevant legal arrangements
 - Identifying the controlled transactions related to the development, enhancement, maintenance, protection and exploitation of intangibles

THE LEGAL OWNER

- The legal owner is generally be considered the sole owner of the intangible, BUT
 - An intangible and a limited right on that intangible are considered to be different, each having a different legal owner;
 - The legal owner is not necessarily entitled to retain the return attributable to the intangible → relevance of the functions performed by the members of the group → the performance/control of development, enhancement, maintenance and protection of intangibles should be appropriately rewarded
 - If other members of the group bear the risks related to the intangible, the legal owner must compensate such members (risks related to development, risk of product obsolescence, infringement risk, product liability)
- The legal owner is free to outsource certain intangible asset related functions but he will need to control the functions outsourced end compensate those on arm's length basis

... SOME CRITICAL ISSUES

- The strict criteria of legal ownership has to be adjusted through the careful survey of the global economic effect of the transaction → the intangibles interact with other functions, assets and risk
 - Economic effects approach VS juridical form approach
 - Relevance only for States' tax power allocation purposes
 - Risks and functions sharing in intangibles transactions .. How to allocate the related return entitlement?
 - What about information/knowledge capable of being transferred instantaneously (e.g. know how)?

THE ARM'S LENGTH CONDITIONS

- One – side comparability analysis VS multiple analysis (considering the perspective of each of the parties of the transaction)
 - The “realistically available options” criteria
 - The relevant factors: exclusivity, legal protection, geographic scope, useful life, stage of development, rights to enhancements, revisions und updates, expectation of future benefit
- ➔ One side methods (resale price method and TNMM) should usually be avoided for directly valuing intangibles

THE METHODS SUGGESTED

- The OECD revised discussion draft suggests
 - ✓ the CUP method (when potential comparable uncontrolled transactions can be identified)
and especially
 - ✓ the transactional profit split method (when it is not possible to identify reliable comparable uncontrolled transactions)
- Possible, but with particular caution, the use of valuation techniques