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**Opinion Statement of the CFE on the OECD Discussion Draft
“Revision of the special considerations for intangibles in Chapter VI of
the OECD Transfer Pricing Guidelines and related provisions”**

Prepared by the CFE Fiscal Committee

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Transfer Pricing is undoubtedly an international tax issue of topical interest to multinational enterprises. As global trade increases, uncertainty in the tax treatment of inter-company transactions as well as double taxation may also expand. Transfer pricing relates not only to the setting of prices for goods and services supplied to related parties, but also to the structuring of transactions and financial relationships.

As stated in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereinafter, OECD Transfer Pricing Guidelines), the concept of transfer pricing should not be confused with that of tax fraud or tax avoidance, although transfer pricing transactions might in some cases be carried out for such purposes. Referring to transfer pricing as “*income-shifting*” might hinder effecting an accurate and thorough analysis of the subject matter. In addition, most of the issues that enterprises are currently facing do not involve low-tax jurisdictions but countries which have a similar level of taxes and where there is no particular tax reason to shift profits.

An examination of any transfer pricing issue should necessarily include an analysis of the arm’s length principle, as a concept generally accepted as the best possible means to set prices in intercompany transactions and avoid double taxation on international business. The arm’s length principle is outlined in Article 9 of the OECD Model Tax Convention.

The spiraling increase in cross-border flows of intangible property has become a most important international taxation issue, and arguably the main issue facing Tax Authorities, multinational enterprises and tax practitioners worldwide. The latter in particular have acknowledged that some of the most difficult transfer pricing issues have always involved the area of intangibles.

Transactions pertaining to intellectual property in the ever-expanding global economy are playing an increasingly significant role, whilst a few complexities regarding the identification, valuation and transfer of intangibles lead to a careful review of existing transfer pricing methodologies and techniques. In substance, the tax treatment of intangible assets should warrant a particular attention in the transfer pricing context.

The arm's length principle requires that multinational enterprises apply transfer prices in their controlled transactions that are in compliance with the prices that would have been applied to the same uncontrolled transaction between unrelated, independent enterprises under the same circumstances. The transfer pricing method adopted by a multinational enterprise constitutes a pivotal component in determining the arm's length consideration in a transaction involving the intercompany transfer of intangible property.

As identical transactions between unrelated enterprises are not common, transfer pricing methodologies tend to focus on comparable rather than identical transactions. However, where intangible assets are concerned, critical issues may arise even in determining a comparative analysis. In this context, a consequent shifting focus to non-traditional methodologies, especially profit-split methodologies, could occur. These latter methodologies tend to rely in whole or in part on internal data rather than on data derived from comparable uncontrolled transactions.

Different methods may be selected under different circumstances. All variables should be assessed in determining the correct methodology for a particular transaction, bearing in mind that those variables may change over time, leading to a reconsideration of the methodology to be applied.

The *Confédération Fiscale Européenne* is pleased to provide inputs on the contents of the Discussion Draft “*Revision of the Special Considerations for Intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and Related Provisions*” (hereinafter, Discussion Draft), released by the OECD on 6 June 2012, as part of the project on intangibles launched in 2010.

The *Confédération Fiscale Européenne* strongly supports the arm's length principle as well as guidance provided on the subject matter by the OECD Transfer Pricing Guidelines and deems that the project on intangibles should be conducted within a framework which:

- guarantees legal and regulatory certainty;
- complies with the internationally accepted arm's length principle;
- aims at avoiding double taxation; and
- takes into consideration all complexities relating to the identification, valuation and transfer of intangible property.

The *Confédération Fiscale Européenne's* comments on the Discussion Draft are outlined below.

In commenting on the Discussion Draft, the *Confédération Fiscale Européenne* has been influenced by the proposed timeline. As a result, our comments are not a comprehensive list of all issues and areas of uncertainty, but a focus on the most significant issues which we believe can be addressed within the said timeline. This does not preclude the discussion of other issues if it might be convenient to include these within the project.

We will be pleased to answer any questions you may have concerning the *Confédération Fiscale Européenne's* comments, outlined below.

Sincerely yours,

Confédération Fiscale Européenne

Comments to Discussion Draft “Revision of the Special Considerations for Intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and Related Provisions”

1. Introduction

On 6 June 2012, the OECD published the Discussion Draft “*Revision of the Special Considerations for Intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and Related Provisions*”, (hereinafter, the Discussion Draft) containing two principal elements:

- a proposed revision of the provisions under Chapter VI of the Transfer Pricing Guidelines;
- a proposed revision of the Annex to Chapter VI of the Transfer Pricing Guidelines, containing examples illustrating the application of the provisions of the revised text of Chapter VI.

The *Confédération Fiscale Européenne* appreciates the OECD work, which intends to provide businesses and Tax Administrations with a clear framework on the intangibles for transfer pricing purposes.

2. Definitional aspects of intangibles

The definition of intangibles, and the consequent identification, has long been a key issue in transfer pricing disputes.

The Discussion Draft provides a definition based on the concept of control, stating that an intangible is “*not a physical asset or a financial asset, and which is capable of being owned or controlled for use in commercial activities. Rather than focusing on accounting or legal definitions, the thrust of a transfer pricing analysis in a matter involving intangibles should be the determination of the conditions that would be agreed upon between independent parties for a comparable transaction*”.

By adopting the above approach, the Discussion Draft distinguishes intangibles from other items that cannot be owned, controlled or transferred by a single enterprise, such as group synergies and market characteristics, which, for this reason, cannot be considered intangibles for transfer pricing purposes.

Furthermore, the OECD focuses its definition of intangibles on what unrelated parties would have agreed rather than taking into consideration the accounting and legal definitions.

The *Confédération Fiscale Européenne* welcomes the notion of “*control*”, but at the same time believes that the definition of what an intangible is should be clearly identified to ensure legal certainty for Governments and businesses.

The definition of intangibles should comply with both accounting and legal principles.

For example, with reference to goodwill, the *Confédération Fiscale Européenne* believes that the broad definition provided by the Discussion Draft does not eliminate the uncertainty.

In the *Confédération Fiscale Européenne's* view, goodwill needs to be defined more in detail for transfer pricing purposes, taking into account the relevance of accounting and business valuation.

The *Confédération Fiscale Européenne* believes that it is necessary to have a clear framework to identify whether a particular item can be classified as intangible, in order to ascertain the nature of the transaction and to determine the *“most appropriate transfer pricing method to the circumstances of the cases”*.

3. Identification of parties entitled to intangible related returns

Determining the relevant parties who are entitled to earn income attributable to intangible assets is one of the most controversial issues for transfer pricing purposes.

The Scoping Document, published by the OECD on 25 January 2011, considers a significant issue the *“(r)ight of an enterprise to share in the return from an intangible that it does not own”*, introducing the concept of *“economic ownership”*, by contrast to its *“legal ownership”*.

Working Party No. 6 states that legal registration and contractual arrangements are the starting point for determining which members of the multinational group are entitled to intangible related returns.

However, the Discussion Draft focuses the attention on the alignment between legal form and the actual parties' conduct.

The profits attributable to intangibles must be allocated to the parties performing the functions and bearing the risks as well as the costs that relate to development, enhancement, maintenance and protection of the intangibles.

The Discussion Draft stresses the notion of control over the principle of functions and risks: when a party passively bears costs related to intangibles but does not control the risks and the fundamental functions, such party cannot be considered entitled to intangible related returns:

“Bearing costs related to the development, enhancement, maintenance and protection of intangibles does not, in and of itself, create an entitlement to intangible related returns”.

In the *Confédération Fiscale Européenne's* view, it is necessary that each associated enterprise, involved in developing, maintaining and protecting the intangibles, obtains a remuneration based on functions performed, risk and costs borne, taking into account what independent parties would have agreed to in comparable circumstances.

The *Confédération Fiscale Européenne* notes that the Discussion Draft uses often the term legal ownership: it should also address the notion of economic ownership.

The *Confédération Fiscale Européenne* recommends that a strict legal approach should prevail and that the concept of *“economic ownership”* of intangibles should be abandoned since it could create some uncertainties. The same concern applies to local marketing intangibles.

4. Transactions involving the use or transfer of intangibles

The Discussion Draft provides guidance on identifying transactions involving the use or transfer of intangibles.

The Discussion Draft identifies two broad classes of transactions:

- transactions involving the use of intangibles in connection with sales of goods and services: in this case, intangibles are used by one or both parties in connection with sales of goods and services, but there is no transfer of intangibles;
- transactions involving transfers of intangibles: in this case there will be a sale of the intangible or the transfer of limited rights related to the intangible.

The *Confédération Fiscale Européenne* emphasizes the importance of a transfer pricing analysis to:

- understand the nature of the transaction;
- identify any intangibles involved in the transaction;
- identify the nature of such intangibles and related rights transferred between associated enterprises.

5. Determination of arm's length conditions in cases involving intangibles

The Discussion Draft confirms the importance to conduct a comparability analysis considering the perspectives of both parties involved in the transaction.

During the said analysis, the Draft considers it necessary to take into account some specific features of intangibles (exclusivity, extent and duration of legal protection, geographic scope, useful life, stage of development, expectation of future benefit, rights to enhancements).

The *Confédération Fiscale Européenne* regards the comparability criteria listed above as rather stringent; generally, the comparables which can be identified in available public databases do not provide the information requested.

Furthermore, the *Confédération Fiscale Européenne* believes that some of these characteristics need to be defined more in detail. For example, the definition of useful lifetime, a key and controversial point in the evaluation of intangibles, is not sufficiently clear.

For the first time, the Discussion Draft states that evaluation techniques can be useful in a transfer pricing analysis.

However, at the same time, the OECD recommends caution in applying such techniques. In particular, it is important to consider the assumptions and other motivations supporting the application of evaluation techniques.

The Discussion Draft discourages the use of so-called “*rules of thumb*” (a formula-based apportionment of the profit attributable to an intangible between its owner and the user) and the use of cost-based methods.

The *Confédération Fiscale Européenne* deems that exclusion of a cost-based evaluation approach is too stern, since it can be a useful method at least for services with low added value.

Furthermore, it seems that the OECD is in favour of the application of the transaction profit split method in many circumstances.

It is worth noting that the Discussion Draft illustrates the reasons why some methods are not applicable in some circumstances and explains the difficulties in applying them.

The *Confédération Fiscale Européenne* believes that it is necessary to provide guidance explaining which methods are applicable under what circumstances.