FIDAL

DIRECTION INTERNATIONALE

FIDAL'S COMMENTS ON THE OECD REVISED DICUSSION DRAFT ON 30 JULY 2013

FIDAL is delighted to respond to the OECD's request for comments from the business community in connection with the revised discussion draft that was issued on 30 July 2013 entitled **Revised Discussion Draft on Transfer Pricing Aspects of Intangibles.** We present our comments in the foregoing sections and would be pleased to discuss these in detail with representatives of the OECD. We set out our comments in relation to the specific paragraphs in the discussion draft.

Section A.4 Identifying Intangibles – Illustrations – paragraph 62

OECD states that *"accounting and business valuation measures of goodwill and ongoing concern value do not, as a general rule, correspond to the arm's length price of transferred goodwill or ongoing concern value in transfer pricing analysis."* We agree that goodwill book value does not necessarily correspond to market value. However, according to the International Accounting Standard 36, most companies have to conduct impairment tests to ensure that the net book values of their tangible and intangible assets are not higher than their recoverable amounts, at least once a year for goodwill and intangible assets with indefinite useful lives. The recoverable amount of an asset is defined as the greater of its market value (less the costs of its sales) and its value in use. Market value is defined as the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable, willing and unpressured parties. Thus business valuation performed for impairment accounting can be of assistance in assessing the arm's length price of transferred goodwill or intangibles assets between affiliated companies.

Section B.1 Intangible ownership and contractual terms relating to intangibles – paragraphs 73 and 74

From a financial standpoint, the legal owner of any asset (securities, tangible or intangible assets) expects a yield on its investment. The expected return will be reduced if the functions performed, assets used and risks assumed are granted or transferred to either other MNE group members or third parties. But the expected return of the legal ownership has should remunerate the capital invested in the assets and the risks involved, in particular the risks resulting from a possible decrease in the asset value.

One illustration is a business lease ("location gérance") where the owner of one business leases its operation for a certain period of time. Generally the leased assets refer to all the intangible and tangible assets required to operate the business and the personnel. Case law shows that the legal owner of the business is entitled to a business lease royalty based on two criteria : the standard yield for the leased assets and a fair profitability allocation between the lessor and lessee.

Section D.6 Location Savings

We doubt that taxpayers or tax authorities will be able to find sufficiently reliable evidence of how location savings are treated by independent parties in terms of either sharing the benefits between them or passing them on to customers. We suggest that OECD makes an acknowledgement of this, absent which tax payers may be obliged to waste a great deal of time and effort on searches for data that is unlikely to be in the public domain and may be judged as somehow showing lack of compliance by tax authorities.

OECD may like to add some illustrative examples of local market comparability adjustments to aid taxpayers. Additionally OECD may like to comment on the examples in the UN Manual on Transfer Pricing and whether it is in agreement with these and the circumstances set out there for their use.

Section D7 Assembled Workforce

14. Similarly we doubt the ability of either taxpayers or tax authorities to assess the benefit or detriments of comparable workforces to make the suggested adjustments here. The information on which such subjective judgments might be based in unlikely to be in the public domain. Again, we suggest OECD acknowledges this for the reasons mentioned above.

Section B2 Functions, assets, and risks related to intangibles

77. We note the implication of the second sentence of this paragraph seems to be that the arm's length compensation is inextricably linked to the intangible value created by outsourced service functions by related parties, and indeed this is made clear in paragraph 78 and 90. We do not agree that this is the appropriate compensation at arm's length. Related party providers of intangibles related services need to be compensated for the functions they perform, assets they use and risks they bear as is noted in the final sentence of this paragraph.

They are not necessarily or automatically entitled to any share of the intangible return. For example, in the pharmaceutical industry third party contract research organizations do not typically share in the premium profits from the creation and exploitation of drugs, they are rewarded for the research services they provide.

OECD might consider rewording this sentence and paragraph 78 and 90 to consider and emphasize which entity is bearing the risks of intangible development.

80. We note that the phrase ‘through its own employees’ is retained here. This contradicts paragraph 76 and the OECD may like to revise the wording here to make them consistent and consistent with the matters raised in the previous consultation comments. The same point arises in paragraph 89 first bullet point. The matter of legal ownership is not central to what is being discussed in this paragraph. The issue is which entity takes the decisions and bears costs in relation to intangibles development and bears the risks of its success, not which entity performs the work.

We are curious as to the precedent being set in the final sentence can be determined in practice. As acknowledged elsewhere in the OECD guidelines, related parties often undertake transactions that are not entered into by third parties. This is not a reason to disregard these in the context of intangibles, especially as to how either taxpayers or tax authorities can determine reliably and definitively what third parties would do. OECD may like to caveat the wording here for this point.

84. We suggest deletion of the words ‘not more’ at the end of the first sentence of this paragraph as they seem otiose.

94 et seq. We think the use of the word ‘distributor’ is potentially confusing here. Distributors, whilst indeed responsible for marketing products, are buy/sell entities, not agents (which do not generally take title to and sell product) as detailed in the anti-penultimate and penultimate sentences of paragraph 95. OECD might like to refine the wording here. 96. For reasons articulated above, we doubt the ability of either taxpayers or tax authorities to demonstrate the marketing costs incurred by independent distributors for comparison purposes, as such information is unlikely to be in the public domain. It is not readily reported in financial statements, for example. We can only think that if reliance is being placed on an internal CUT search, some such details might be researchable, otherwise we suggest OECD considers refining the wording here for practical application.

D.2. Supplemental guidance regarding transfers of intangibles or rights in intangibles

134. Due to the lack of prospective public data on potential comparables (other than possible for listed companies), we would welcome guidance from OECD as to how the assessment of profit potential noted in the final sentence of this paragraph and in paragraph 145 is to be carried out in practice. Perhaps OECD might be able to acknowledge that, however flawed, potential comparables should not be dismissed out of hand as they are the only publically available data to taxpayers and tax authorities.

147. OECD might like to add a sentence at the end of this paragraph to clarify what these less comparables dependent methods might be, for example, profit split, perhaps.

157 and 181 et seq. OECD may care to acknowledge that expected future benefits may be difficult to establish for internal budgetary reasons. In some organizations, in order to secure R&D funding and budgets, and indeed, to incentivize employees, it may be that these benefits and return on investment analyses are overly-optimistic. Caution should be exercised in assessing the reliability of internal data for this purpose, so as not to build up an inflated sense of the profit potential at inception. OECD may like to encourage the use of appropriate data for the exercise in hand.

171 et seq. On valuation techniques, the position of the Council of the State and administrative courts in France is to refer primarily to comparable transactions, and if not applicable, to a multi-criteria valuation approach. The evaluation of several valuation methods is a key in French jurisdictions. Additionally, because of the higher degree of uncertainty inherent to its calculation basis, the discounted cash-flow method is often results in major and lengthy discussions with the French tax administration.

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