Chartered Institute of Taxation
Excellence in Taxation

Revised Discussion Draft on Transfer Pricing Aspects of Intangibles
Response by the Chartered Institute of Taxation

1 Introduction

1.1 The Chartered Institute of Taxation (CIOT) is pleased to comment on the Revised Discussion Draft on Transfer Pricing Aspects of Intangibles published on 30 July 2013.

1.2 We broadly welcome the new guidelines, and regard them as an improvement on the previous draft. In particular it is helpful that the guidelines do widely recognise that ownership of intangibles should be the starting point for the debate. This keeps the process linked to contractual requirements that create real and consequential arrangements for the parties involved.

1.3 We have kept our points relatively brief and focussed them on where the wording in the guidelines raises material concerns

2 The Additional Sections addressing features of the local market, assembled workforce and synergies

2.1 These are broadly helpful. It is noted that examples are included in respect of synergies, but not for local market features or for the assembled workforce. Additional examples on these areas could be helpful in illustrating the points made, especially in respect of the local market, and the allocation of location savings where there are no local comparables.

2.2 In paragraph D7.17 it should be made clear that it cannot be assumed that a secondment of an employee with valuable know-how represents the transfer of that know-how, as the employee may be undertaking a role in which that know-how is not actually used. Furthermore, there can only truly be a 'transfer' of know-how in these circumstances if the seconded employee imparts their know-how to employees in the entity to which he or she has been seconded. If, when the secondment ends, the employee takes the know-how back with them, no rights in that know-how have actually been moved.

ARTILLERY HOUSE
11-19 ARTILLERY ROW
LONDON SW1P 1RT

REGISTERED AS A CHARITY NO 1037771

Tel: +44 (0)844 251 0830
Fax: +44 (0)844 579 6701
E-mail: technical@tax.org.uk
Web: www.tax.org.uk

CFE UK REPRESENTATIVE BODY ON THE CONFEDERATION FISCALE EUROPEENNE

3 The new Chapter VI

3.1 *Paragraph 73*

3.1.1 We disagree that legal ownership of intangibles does not of itself confer the right to a return. In our view legal ownership confers the right to the full return on the intangibles less amounts that are properly due to other parties, and we take the view that there will always be some measure of the return that will accrue to the legal owner, albeit in some cases this may be very small. Ultimately the legal owner of an intangible is on risk for a total loss of value in an intangible (for example a catastrophic loss of value due to an adverse event involving a brand).

3.1.2 Legal ownership itself can confer a benefit; for example intangibles may be held separately in a special purpose vehicle (SPV) from the trading business to protect the intangibles against claims that may arise from a bankruptcy in a trading company, and this very separation has value, even if the SPV undertakes no other functions.

3.1.3 Moreover, in respect of the originator of intangibles, it surely must be the case that legal ownership does confer the right to retain a return; an author or musician, unless they sign their rights away entirely, would expect to earn a return from a book or composition for many years despite not needing to do any further work. Additionally, an intangible may be transferred for a considerable sum, and the functions required after the transfer may be relatively minimal; the return in that case would belong to the legal owner, not those carrying on the minimal ‘functions’ if they were a different party.

3.1.4 Paragraphs 74-90 should acknowledge that there will be cases where an asset owner and originator is entitled to the whole return until such time as some other person undertakes a significant function in respect to the intangible, and there may be occasions where it appears no-one is undertaking any ‘functions’ related to the asset, and, in the absence of any prior transfers of value, the whole of any return will belong to the legal owner. Such lack of activity is, of course, likely to lead to a diminution in such returns.

3.1.5 The quantum of the return due to the legal owner will have to be determined on a case-by-case basis and we believe that it should be the case of ‘working down’ to this sum recognising that substantial ‘residuals’, whilst possible, are not likely when the owner is doing little more than holding the intangible, rather than ‘working up’ from an assumed starting point of zero which paragraph 73 seems to imply.

3.2 *Section D1, Paragraphs 128-132*

3.2.1 These paragraphs deal with general principles applicable to transactions involving intangibles. We are of the view that these paragraphs could be a little more balanced, and encourage taxpayers and tax authorities to consider the context of the industry in which the transaction is taking place to a greater extent.

3.2.2 In our comments on the previous discussion draft, we noted that it would help if the guidance stated that fundamentally, a taxpayer group should have the right to sell, licence and transfer IP within its group at arm’s–length terms. We continue to take the view such a statement would be helpful.

3.2.3 We also continue to hold the view that the guidance should recognise that there are established approaches for valuing differing types of IP transactions in third party situations, undertaken by IP dependent business, and that these approaches should be highly persuasive when such businesses undertake internal transactions.

3.2.4 Finally in regard to general principles, we continue to hold the view that where the outsource of a function is an industry 'norm', outsourcing such a function to a related party should not of itself entitle the related party to an IP return.

3.3 ***Paragraph 195***

It might be useful to state that a terminal value is not a requirement, and such values can sometimes lead to implausibly high values for intangibles.

3.4 ***Paragraphs 200-206***

In third party arrangements, one side or both may be willing to accept the risk of making what will ultimately prove to be seen as deal at an undervalue. Uncertainty itself will tend to reduce a price, and increase the buyer's risk. Tax authorities, acting with the benefit of hindsight, should not ignore this.

4 Examples

4.1 ***Examples 13 & 14***

The example appears to be the successor to Example 11 in the previous draft, which we commented on in some detail; the revisions have significantly and helpfully clarified the position.

4.2 We take the view that examples 13 and 14 suggest that a pricing adjustment solution should be capable of resolving disputes in such circumstances and re-characterisation/disregard of transactions should not be necessary.

4.3 ***Example 24***

The revision of this example (previously 19) has also resulted in greater clarity.

5 The Chartered Institute of Taxation

5.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 16,800 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation

8 October 2013