



Intangibles and Transfer Pricing

The interactive interplay

Lets break some ice!!



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What?



The What



Basic Definition

The term intangible in the Guidelines is defined as something,

- which is not a physical or financial asset,***
- which is capable of being owned or controlled for use in commercial activities, and***
- whose use or transfer would be compensated in a transaction between third parties.***

Patents

Trademarks

Group synergies

Know-how

Licenses

Market-specific
characteristics

Goodwill

Rules for identifying intangibles

Elements required to be an Intangible

- Capable of being owned or controlled
 - Does not include local market conditions such as the nice weather in a particular country
 - Does not include MNE group synergies which are not owned or controlled by a single member of an MNE group
- Capable of being used in commercial activities
- Use or transfer would be compensated in transactions between independent parties
- Not a tangible asset or a financial asset

Elements NOT required to be an Intangible

- Need not be an intangible for accounting purposes
- Need not be an intangible for general tax or treaty withholding tax purposes – Article 12 MTC
- Need not be legally protected
- Need not be separately transferable

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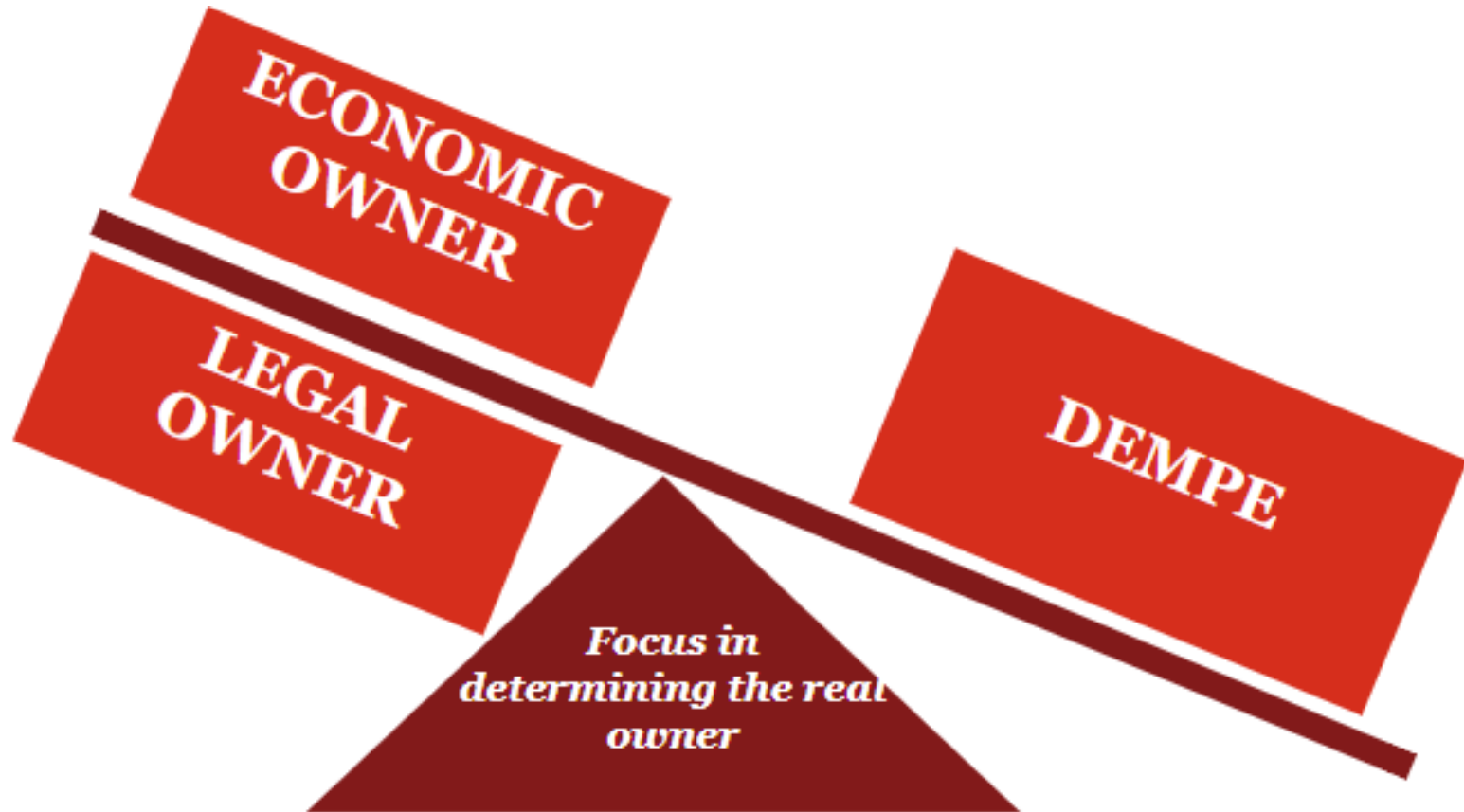
Group synergies

Market-specific characteristics

The Who



Analytical framework for identifying arm's length price for intangibles



Who's entitled to the intangibles returns?...

- Mere legal owner **NOT** entitled ultimately to the entire intangible returns – **economic ownership** is the test:
 - Development
 - Enhancement
 - Maintenance
 - Protection
 - Exploitation of the intangible
- *DEMPE functions split over different locations - need to split the returns across*

FAR for intangibles...

- Identity the entities for DEMPE
- Legal owner v economic owner
- Emphasis on the **“Control”** function
- Function and control are outsourced – need to understand the level of control / decision making
- Mere funding would entitle significantly lower returns



... FAR for intangibles

- Business reasons for engaging in the transaction
- Options realistically available to each of the transacting party
- Competitive advantages conferred by the intangibles including the expected future economic benefits



The Why

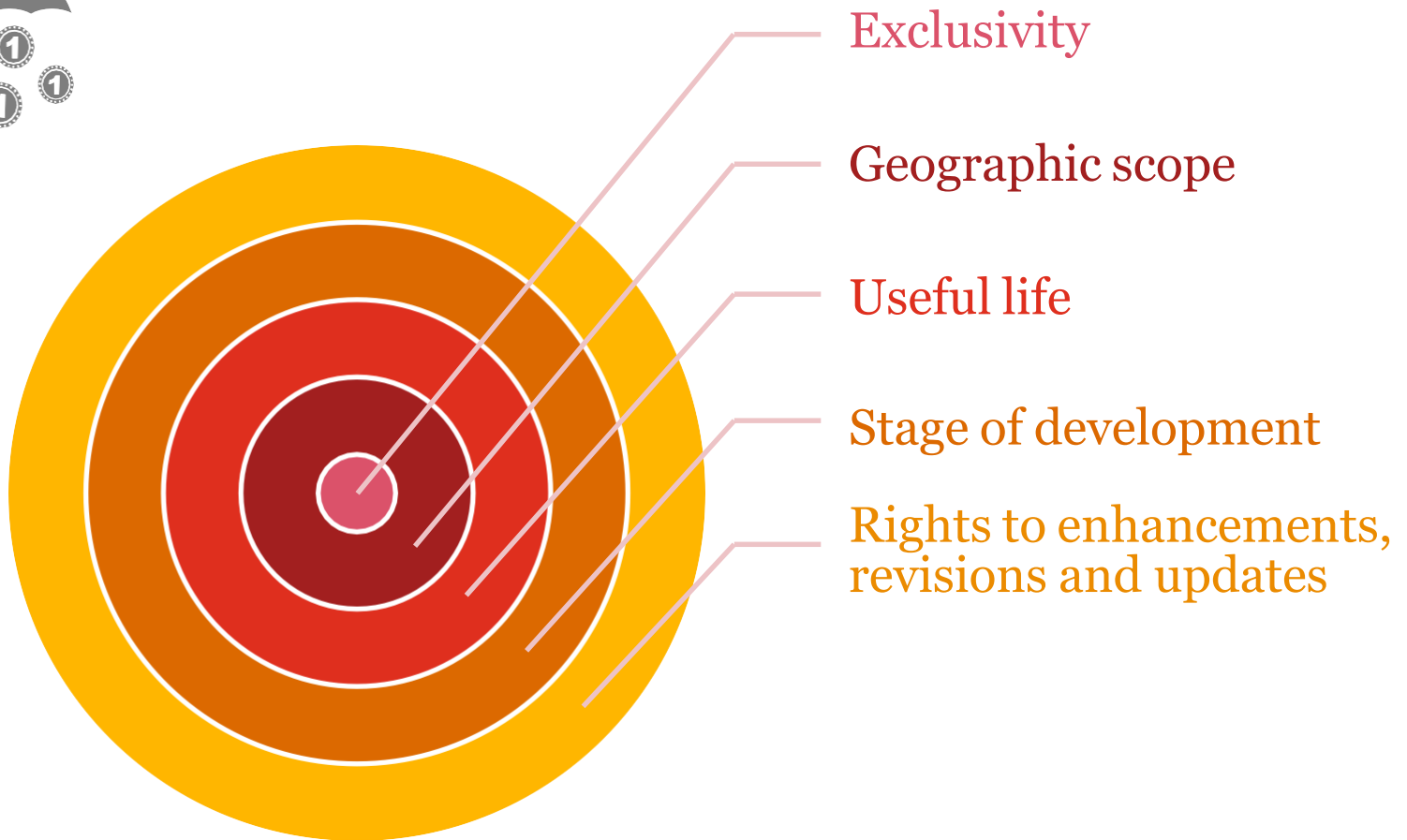


Intangible pricing – when to think

- Transactions involving intangibles
 - Sales / purchase of goods
 - Provision of services
 - Stake sale
 - IPOs
- Value / valuation required
 - Royalty
 - Franchisee Fees
 - Business valuation
 - Governance



Important factors for pricing / valuation



Some relevant TP methods

TP methods	Potential scenarios
*Comparable Uncontrolled Price (“CUP”) Method	Most common for a royalty analysis
Resale Price (“RP”) Method	Not applicable
Cost Plus (“CP”) Method	Not applicable
Profit Split Method (“PSM”)	Two or more IP owners
*Transactional Net Margin Method (“TNMM”)	Residual royalty analysis

Valuation methodologies are acceptable from TP perspective

Hard-to-value intangibles – A differentiator

- HTVI covers intangibles or rights in intangibles for which, at the time of their transfer-
 - (i) No sufficiently reliable comparable exists
 - (ii) There is a lack of reliable projections of future cash flows or income expected to be derived
 - (iii) Assumptions used in valuing the intangible are highly uncertain
- *Examples*
 - (i) Intangibles that are only partially developed at the time of the transfer
 - (ii) Intangibles that are not anticipated to be exploited commercially until several years following the transaction
 - (iii) Intangibles that are anticipated to be exploited in a manner that is novel at the time of the transfer

To sum up : A six-step framework

Identify the legal owner



Identify parties performing functions, using assets, and assuming risks related to the development, enhancement, maintenance and protection of intangibles



Confirm consistency between agreements and conduct



Identify relevant controlled transactions



Determine an arm's length price for relevant transactions identified



Re-characterize, if required, transactions as necessary to reflect arm's length conditions

Key takeaways

Identify the key IPs
/ value drivers on
the touchstone of
the guidance

Determine the real
decision makers

Align the
substance and
form

Plan the effective
exploitation of the
IP