



Centre for Tax Policy and Administration

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OECD

2 rue André Pascal
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[Via e-mail TransferPricing@oecd.org](mailto:TransferPricing@oecd.org)

Dear Sirs,

On 30 July 2013, Working Party No. 6 of the Committee on Fiscal Affairs of the OECD released a **revised discussions draft on transfer pricing aspects of intangibles**, for interested parties to provide written comments.

A3F is pleased to respond to the OECD's request for comments on this discussion draft.

A3F background

A3F (French Women Tax Experts Association - Association Française des Femmes Fiscalistes) was founded in 2005. A3F is a French-based network of professional women from diverse horizons representing most players of the French and international tax system (experienced tax executives and expert tax advisors from a wide range of French and foreign companies and law firms, University professors, etc). The ever changing and rapidly evolving corporate and individual tax policies in France and around the world are a major concern for businesses. A3F provides its members with opportunities to exchange ideas and best practices, and to contribute to the shaping of tax policy through participation in public debates. A3F currently counts 100 members, all with a recognized work experience.

The president of A3F is Ms Eva Memran, Tax Director for a large French MNC. Ms Memran can be reached at +33 6 77 76 90 76 or evamemran@gmail.com.

Conclusion

A3F appreciates this opportunity to provide its views on the transfer pricing aspects of intangibles (outlined in the following pages). These comments were prepared by an ad-hoc A3F working group chaired by Ms Laurence Delorme. We will welcome an opportunity to participate in the subsequent public consultations and related discussions.

Respectfully submitted,

For Association Française des Femmes Fiscalistes

Laurence Delorme

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Revised Discussion Draft on Transfer Pricing Aspects of Intangibles

PROPOSED AMENDMENTS TO CHAPTERS I-III OF THE TRANSFER PRICING GUIDELINES .

D.6.1 Location savings

Para. 2 to 5: We are surprised and concerned to see that the developments in these paragraphs 2 to 5 of the revised DD, which discuss the treatment of location savings in determining appropriate comparability adjustments, are largely inspired by the approach developed in the UN TP Manual (released in October 2012), particularly with regard to its Chapter 5 (Comparability analysis) and Chapter 10 (Country practices for China and India).

The UN TP Manual (and observed practices of tax authorities in some developing countries) deals with the question of location savings with a strong bias that, where location savings exist, they should, as a matter of principle, be attributed to the entity located in the low cost country in total or for a large share, irrespective of the particular facts and circumstances (e.g. relocation as part of business restructuring or location of new activity), and applicable functional analysis.

This one-sided approach is currently a source of great uncertainty and unpredictability for business operating in those UN countries applying the approach described in the UN TP Manual. We feel critical that the OECD Guidelines take a less extreme and more balanced view at this question.

Para. 2 states that principles described in para. 9.148 to 9.153 of the OECD TPG (Chapter IX on Business Restructuring) "*apply generally to all situations where location savings are present, not just in the case of a business restructuring*". This statement opens the Pandora box to potentially very difficult discussions in all cases where a MNE establishes a new activity in a low cost country as part of its international development strategy, outside the scope of a business restructuring (i.e. without terminating an existing activity in a high tax country).

For example, localisation of routine functions (such as shared administrative or financial services provided to associated enterprises) in a low cost market would not trigger a market premium or added-value, and should therefore not be qualified as triggering location savings for the purpose of Chapter VI.

D.6.2 Other Local Market Features

Para. 7 & 8 The method described in view of assessing whether comparability adjustments for local market features are required, is a very theoretical approach and entails a good faith relationship between the tax payer and tax authorities in the selection of data necessary to conduct the study, as well as an access to these data which can be for their major part, rather confidential data. Sharing such information with tax authority creates a real confidentiality and competition issue which has to be addressed.

Based on recent and current experience in many emerging countries (applying principles described in the UN TP Manual), one can demonstrate that such a maturity in professional assessment is simply not existing and gives rise to unilateral approach which can only be counter-fought through uncertain long term litigation.

More generally, the economic definition of Intangibles promoted by the OECD draft, and the necessity to take into consideration a great number of new parameters in comparability process opens a wider scope of potential disagreement increasing even more the uncertain tax and legal environment for MNE groups.

This will automatically and drastically increase the tax burden and the tax costs for all range of transactions which, so far, were relatively well ring-fenced and defined through a more legal approach of the Intangible definition .

D.7 Assembled Workforce

As a reminder, we have copied below the presentation made by A3F to introduce the subject at the OECD Public Consultation held on 12-14 November 2012. This analysis reflected the views expressed by all business commentators as submitted to OCDE before the public consultation.

- **Assembled workforce**
 - *Cannot be “owned or controlled” by the employer, hence cannot be sold or licensed independently of the entire business to which the workforce relates, i.e. issue of “transfer of an assembled workforce” arises only as part of a **business transfer***
 - *As such, to be considered as business attribute that influence the value of an MNE’s assets, but **not** to be qualified as an intangible asset*
 - **Assembled workforce is NOT an intangible within the meaning of section A.1**
 - *Assembled workforce can contribute to the development of intangibles (e.g. know-how and other legally protectable intangibles), and should be taken into consideration in **transfer pricing comparability analysis***

Para. 15 rightly acknowledges that the transfer of a uniquely qualified assembled workforce may take place as part of a business restructuring. In such a case, the compensation paid for such business transfer (including the assembled workforce) should take into account time and expense savings, as well as potential future liabilities and limitations attached to this workforce.

However, **para. 17** further states that " *the transfer or secondment of employees may result in the transfer of valuable know-how*" which "*should be separately analyzed*" and for which "*an appropriate price should be paid*".

We strongly disagree with this approach, as per the analysis developed above based on business comments received for the November 2012 Public Consultation..

Also, this **para. 17** is in contradiction with **para. 157** with lists explicitly as **comparability factors** features such as "*local markets, location savings, assembled workforce, and MNE group synergies*".

We note that Chapter VI Section A4 "Illustration of categories of intangibles" (**para. 52 to 64**) does provide clear conclusions on items that should NOT be treated as intangibles, such as Group Synergies (para. 63) and Market Specific Characteristics (para. 64). However, Assembled Workforce is not listed among those items which should NOT be treated as intangibles but should instead be regarded as comparability adjustments. This is creating confusion and opens uncertainty on this matter.

We suggest to include the discussions on Assembled Workforce in Chapter VI in para. A (vi) on "Goodwill and ongoing concern value" (**para. 60 to 62**), i.e. to make it clear that Assembled Workforce is a business attribute that influences the value of a business, but is NOT an intangible which can be separately transferred for a consideration. The current presentation is very ambiguous and confusing.

D.8 MNE Group Synergies

Para. 18 to 33

A new criteria is introduced: the "*deliberate concerted group action*" which seems quite relevant in the analysis of the treatment of Group synergies. However, it may in practice create a lot of additional administrative constraints for MNE, if they need to **formally document** group decisions supporting such "*deliberate concerted group action*", which are generally taken with the view to "*reducing administrative costs and simplifying processes in order to materialise these synergies*".

When a MNE is present in one hundred countries, such documentation requirement can have a significant impact, being understood that the group policy resulting from such "deliberate concerted group action" (e.g. central purchasing function, central financial services) may not be 100% consistent in its application all over the world for maturity reasons .

Examples given in the finance field (**para. 24 to 27**) illustrate the variety of situations and the difficulty to precisely follow and document each transaction at the level of detail required by some tax administrations.

Para. 21 & 23 and Examples 3 (para. 28) & 4 (para. 29) Central Purchasing

It is unclear how these examples relate to Section F of Chapter IX (para. 9.154 tp 9.160), which also provides examples in relation to Implementation of central purchasing function in a business restructuring context.

Also, **para. 23** ends with a prescriptive conclusion that an arm's length method (in the case of a central purchasing function) requires sharing synergistic benefits "*in proportion to purchase volumes*". This statement is far too extreme and without due consideration for actual practices between third-parties. The functional analysis in relation to the contribution of the central purchasing entity to value creation will vary

depending on facts and circumstances. Particular attention should also be paid to third-party dealings in comparable circumstances and existence of CUPs which can validly be used to set an arm's length compensation for the purchasing function.

PROPOSED AMENDMENTS TO PARAGRAPH 2.9 OF CHAPTERS II OF THE TRANSFER PRICING GUIDELINES

Para. 34

We welcome the introduction in this new paragraph 2.9 of the distinction between **price setting** ("*methods to establish prices*") and **price testing** ("*methods to demonstrate that the prices charged either do or do not satisfy the arm's length principle in accordance with these Guidelines*").

This question is often a subject of debate with tax authorities upon audit, as they often tend to focus a large part of their detailed investigations on the mechanisms of "price setting", without due consideration for the actual financial results of the application of the transfer pricing methodology (which are tested against the arm's length standard when preparing the transfer pricing documentation).

This distinction is also of great relevance for Transfer Pricing documentation requirements, which should in our view focus on "price testing", i.e. documenting that the "*financial results of applying the transfer pricing methodology*" meet the arm's length standard (see para. 70 of White paper on TP documentation). We note that the White Paper on Transfer Pricing Documentation does not make such distinction, which is of importance when discussing about the purpose of such transfer pricing documentation.

NEW CHAPTER VI SPECIAL CONSIDERATIONS FOR INTANGIBLES

A. Identifying intangibles

A.1 In general

Para. 40 reads as follows: "*In these Guidelines, the word "intangible" is intended to address something which is not a physical asset or a financial asset, and which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances*".

This para. 40 still provides a definition of the word "Intangible" which is far too vague and will not provide "certainty and predictability for business", despite a clearly stated objective of the BEPS Action Plan¹. Further, this definition is not in line with BEPS Action Plan on Intangibles (Action 8²) which states as follows: "*Develop rules to prevent moving intangibles among group members. This will involve: (i) **adopting a broad and clearly delineated definition of intangibles;**...*"

¹ BEPS action plan Chapter 3 page 14: "***The actions implemented to counter BEPS cannot succeed without further transparency, nor without certainty and predictability for business***".

² BEPS action plan Chapter 3 Action 8 page 20

Reference to legal ownership, control or transfer in the definition of intangibles would be consistent with the wording in the rest of the Revised Discussion Draft which repeatedly makes reference to (i) "legal owner" (see discussions in section B.1 below), and to (ii) legal concepts and definitions in section C regarding transactions involving transfers of intangibles or rights in intangibles, and transactions involving the use of intangibles in connection with the sale of goods or the provision of services.

We suggest to replace the term "*something*" with "identifiable asset" (the word "something" is too vague), and to add the words "legally" and "transferred (separately or in combination with other business assets)" in the definition:

"...the word "intangible" is intended to address an identifiable asset which is not a physical or financial asset, and which is capable of being legally owned, controlled or transferred (separately or in combination with other business assets) for use in commercial activities..."

Para. 42 should be amended accordingly with the last sentence deleted.

A.2 Relevance of this Chapter for other tax purposes

Para. 48

This statement seems contradictory with stated objective of the BEPS project, which is to avoid double taxation for business and prevent double non-taxation.

A.3 Categories of intangibles

Para. 50 "*...generic references to marketing or trade intangibles do not relieve taxpayers or tax authorities from their obligation in a transfer pricing analysis to identify relevant intangibles with specificity, ...*

This requirement for identifying relevant intangibles with specificity seems in contradiction with the loose definition of intangibles in **para. 40**.

A.4 Illustrations

We note that **para. 52 to 64** provide clear conclusions on items that should **NOT** be treated as intangibles (but should be treated as comparability factors instead), such as Group Synergies (para. 63) and Market Specific Characteristics (para. 64). However, Assembled Workforce is neither listed among those items which should NOT be treated as intangibles, nor among those which should be treated as comparability factors. This is creating confusion and leads to ambiguous conclusions.

We suggest including the discussions on Assembled Workforce in Section A (vi) on "Goodwill and ongoing concern value" (**para. 60 to 62**), as the current presentation (no reference to Assembled Workforce in the

list of illustrations to be treated or not as Intangibles for the purpose of para. 40) is very ambiguous and confusing.

Paragraphs 60 to 62 bring some confusion and contradiction:

- on the one hand, the first statement of **paragraph 61** is that because “ Goodwill and ongoing concern” represents value in transactions (i.e. transfer of some or all of the assets of an operating business) between independent enterprises, they should be treated **AS intangibles** , and
- on the other hand, **paragraph 62** states that the accounting or business valuation measures of Goodwill “**do not, as a general rule, correspond to the arm’s length price of transferred goodwill or ongoing concern value in a transfer pricing analysis** “

We believe a reconciliation of these two paragraphs could come through some clarifications introducing the distinction between consolidated financial statements, and financial statements on a legal entity basis (for statutory and/or tax purposes), only the latter being directly relevant for the purpose of transfer pricing analysis.

We suggest at a minimum to add the words " directly" and "consolidated" in above sentence: " *As a general rule, accounting and business valuation measures of consolidated goodwill and ongoing concern value do not directly correspond to the arm's length price of transferred goodwill or ongoing concern value in a transfer pricing analysis*".

This of course is to be put in perspective with the detailed recommendation on valuation techniques (par 171 through 198) which opens a wide scope of very uncertain tax positions, in contradiction with the guidance principle to secure the Arm’s length fundamental building block.

B. Ownership of Intangibles and Transactions Involving the Development, Enhancement, Maintenance and Protection of Intangibles

B.1. Intangible ownership and contractual terms relating to intangibles

Para. 73 makes very extreme statements:

*"..for transfer pricing purposes, legal ownership of intangibles, **by itself**, does **not** confer **any** right ultimately to retain **any** return from exploiting the intangible that may initially accrue to the legal owner as a result of its legal or contractual right to exploit the intangible".*

*"For example, where the legal owner makes no contributions that are anticipated to enhance the value of the intangible, the legal owner will **not** ultimately be entitled to **any** portion of the return attributable to the intangible"*

We disagree with this extreme statement. For example, a patent may be registered solely with a view to preventing the competition for exploiting a given technology, without the patent owner exploiting it immediately. Yet, the transfer or license of such patent will entitle the patent holder to the return attributable to the intangible.

B.2. Functions, assets, and risks related to intangibles

We note that the reference to "Costs" has now been deleted, in order to concentrate on "functions, assets, risks and other factors contributing to value", and we welcome this amendment.

a) Functions performed

Para. 78: this paragraph is unclear by indicating that an arm's length compensation may comprise "*any share of the total anticipated return related to the intangibles*" to be allocated by the legal owner to other entities performing or controlling functions related to enhancement, development, maintenance or protection of intangibles. This seems to imply that attributing a routine profit (mark-up on costs) to such "outsourced" functions will never be an arm's length compensation, and seems to call for profit-split as a general rule, against evidence of third-party dealings.

Para 80 to 90 :

These paragraphs (and in particular **para. 89**) create a doubt on the "outsourcing" practice illustrated by extreme examples.

In normal business life, outsourcing is a common way to do business between independent enterprises, and terms and conditions will in practice vary depending on industry and market circumstances, with the Entrepreneur (or intangible owner) retaining control over the "Significant People Functions" or "Key Entrepreneurial Risk Taking activities" (ie strategic functions related to core business).

Para. 89 outlines the four cumulative conditions to be met in substance by the legal owner of an intangible, in order to be entitled to all returns attributable to the intangible.

However, the condition that the legal owner of an intangible should "*control other functions outsourced to independent enterprises or associated enterprises*" does not reflect third-party conduct in an outsourcing relationship. Indeed, once the outsourcing contract is concluded and the terms and conditions agreed (including price), it is frequent for the sub-contractor to operate without control by the principal over its day-to-day activities.

As long as the principal retains the full control and risk of the project, while despatching "pieces" in different locations, these pieces may have very little value taken independently and until they are finally consolidated in the whole project at the full risk of the entrepreneur.

So taking the view that any and all function are to be tailored the same way is not realistic and again gives room to disagreement and disputes .

B.4 Application of the foregoing principles in specific fact patterns

(b) Research, development and process improvement arrangements

Para 97 states "*compensation based on a reimbursement of costs plus a modest mark-up will **not** reflect the anticipated value of the arm's length price for the contributions of the research team in all cases*".

The first test should be by reference to practices between independent enterprises on the market. In some industries, it is very common to outsource part or all of the R&D activities to Contract Research Organisations (CRO's), and this should set a reference for market practices between independent parties for such contract research R&D activities. and limited cost+ reward.

C. Transactions involving the use or transfer of intangibles

Para 107 states that "*...it is essential to identify with specificity the nature of intangibles and rights in intangibles that are transferred between associated enterprises*".

While we agree with this statement, we feel it is contradictory with the loose definition of intangibles under **para. 40** (see above). Unless intangibles are precisely defined in Chapter VI, it is hard to identify with specificity the nature of such intangibles when transferred.

D. Supplemental Guidance for Determining Arm's Length Conditions in Cases Involving Intangibles

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

The complexity of analysis now recommended as a guidance to achieve comparability (**para. 133 to 198**) in order to encompass all intangibles potential features opens the systematic challenge by tax authorities of the traditional methods and clearly leads to the promotion of profit split methods.

Because of the multiplicity of factors now contemplated, and the current difference of understanding of new concepts such as LSA , Market Premium, etc... the business has a strong fear that a "Pandora box "is being open in transfer pricing methods and rules, with additional complexity and risk and no clear guidance to assess a reasonable position.

Faced with the difficulty of obtaining reliable comparable data meeting all the criteria, MNE's are faced with the risk that profit-split becomes the only arm's length methodology.

Para. 134 should include a reference to acceptability of referring to an "arm's length range" to demonstrate compliance with the arm's length standard, as given the complexity in obtaining reliable comparability data, it is not realistic to expect such data to provide a precise indication of what is the arm's length price/rate within the range.