Lund University

School of Economics and Management
Department of Business Law

The incompatible Definitions of Intangibles between the OECD Guidelines and the U.S. Tax Cuts and Jobs Act from a Transfer Pricing Perspective.

by

Julia Hochreiter

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Supervisor: Jérôme Monsenego
Examiner: Cécile Brokelind

Author's contact information:
julia.hochreiter@outlook.com

Abstract

"What discrepancies arise from the incompatible definitions of intangibles for transfer pricing purposes according to the OECD Transfer Pricing Guidelines 2017 and the U.S. Tax Cuts and Jobs Act, and what are the risks?"

The thesis analyses the discrepancies of the different definitions of intangibles in a transfer pricing context, between the OECD Transfer Pricing Guidelines 2017 and the U.S. tax reform of 2017, namely the U.S. Tax Cuts and Jobs Act. The different treatment of goodwill and ongoing concern value within the OECD Guidelines and the U.S. Tax Cuts and Jobs Act is the main focus of the thesis.

While the core analysis highlights and discusses the discrepancies of the different definitions and the legal risks that arise through that, another focus is to provide the reader with an outline on the importance of a plain and proper definition of intangibles for transfer pricing purposes.

Keywords: Transfer pricing, definition of intangibles, goodwill, ongoing concern value, double taxation, double non-taxation, the OECD Transfer Pricing Guidelines, the U.S. Tax Cuts and Jobs Act.

"When you are winning even when you lose, there is no point in trying too hard."[1]

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[1] Kyriazis, D. A., Head of the Law Faculty at New College of the Humanities, London, UK.

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List of Abbreviation

ALP	Arm's Length Principle
BEAT	Base Erosion and Anti-Abuse Tax
BEPS Project	Base Erosion and Profit Shifting Project
CSA	Cost-Sharing Agreement
CUP method	Comparable Uncontrolled Price Method
DTC	Double Taxation Convention
EU	European Union
GILTI	Global Intangibles Low Taxable Income
IRC	Internal Revenues Code
IRS	Internal Revenue Services
MNE	Multinational Enterprises
MS	Member State
OECD MC	OECD Model Convention
PSM	Transactional Profit Split Method
TCJA	The U.S. Tax Cuts and Jobs Act 2017
TP	Transfer Prices / Transfer Pricing
TPG 2017	OECD Transfer Pricing Guidelines 2017
The U.S.	The United States

1 Introduction

1.1 Background

Different tax regimes in different jurisdictions can be used by associated multinational enterprises (MNE) to lower their tax burden, by shifting profits through transfer pricing (TP) from a high tax jurisdiction to a low tax jurisdiction.[2] The value of a transaction between associated MNEs is supposed to be determined by TP and since they must be taxed properly, the arm's length principle (ALP) is used as an aid.[3] Without the ALP, or a similar approach, companies could price their transactions between related parties at a value of zero, therefore it would be possible to transfer their items from a high tax jurisdiction to a low tax jurisdiction without paying any taxes.[4]

Because of the non-physical nature of intangibles, as well as their difficult value determination, they are particular suitable for this kind of transfer.[5] Even though guidelines on TP are continuously enlarged, in order to prevent such profit shifting and tax evasion, MNEs are still able to reduce their tax liabilities by involving intangibles in their transactions.[6] Additionally, a split in the value chain of intangibles in MNEs leads to an intensive loss of tax bases for many states.[7] Another problem occurs within the present methods

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[2] Gravelle, J. G., Tax Havens: International Tax Avoidance and Evasion, Congressional Research Service, 2015, p. 10.

[3] OECD, Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, OECD Publishing, Paris, 2017, para. 1.2, (hereinafter: OECD Transfer Pricing Guidelines 2017).

[4] Avi-Yonah, R. S., Benshalom, I., Formulary Apportionment - Myths and Prospects - Promoting Better International Tax Policy by Utilizing the Misunderstood and Undertheorized Formulary Alternative, 2 World Tax Journal 371, 2011, p. 373. (hereinafter: Avi-Yonah, R. S., Benshalom, I., Formulary Apportionment, 2011).

[5] Gravelle, J. G., Tax Havens: International Tax Avoidance and Evasion, Congressional Research Service, 2015, p. 10.

[6] Avi-Yonah, R. S., Benshalom, I., Formulary Apportionment, 2011, p. 373.

[7] Haumer, S., Brennpunkt immaterielle Wirtschaftsgüter – die eigentliche „Substanz" jedes Unternehmens, in Macho, Steiner, Spensberger, Verrechnungspreise kompakt, Linde, 2017, Ch. 16.1.

of valuation. These methods value intangibles at an early stage of their development, i.e. they measure the future value of intangibles, without plentiful information about its actual value in the future. Therefore, each MNE who has all the information of the intangible, can influence the result of the valuation and estimate the value according to their needs. In agreement with Fedan, a linkage between the present and the future value of intangibles is necessary, to coordinate the present valuation with the future valuation, in order to get that problem solved.[8] Hence, there is still the need to develop a method which can assess the value in a proper way.[9]

Since there are many concerns within intangibles in a TP context, such as briefly introduced above, the proper application of the ALP because of its difficult valuation, the determination of the most suitable TP method or the concern of profit shifting and tax evasion, the starting point relates to define what constitutes an intangible.

Tax treatments should not only get enlarged and more complex, as already mentioned above, but also get continuously revised, which includes TP issues connected to intangibles. MNEs strive for the most tax efficient treatment, while tax authorities are worried about aggressive tax planning.[10] As a result of that, the OECD published in 2017 its new Transfer Pricing Guidelines (TPG 2017), and the U.S. introduced in the same year its new tax reform, namely the U.S. Tax Cuts and Jobs Act (TCJA)[11], both with a focus on the treatment of intangibles[12], and most relevant for that thesis, their definition.

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[8] Fedan, A., Transfer Pricing and Intellectual Property: Identifying issues and reviewing the existing and alternative solutions, 2014, p. 4.

[9] Avi-Yonah, R. S., Benshalom, I., Formulary Apportionment, 2011, p. 8.

[10] Dziwiński, K., Peng, C., Introduction to the post-BEPS transfer-pricing aspects of intangibles in Lang, M., Storck, A., Petruzzi, R., Risse, R., Transfer Pricing and Intangibles, Linde 2019, Ch. 1 (hereinafter: Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019).

[11] The U.S. Tax Cuts and Jobs Act, Pub. L. 115-97, 2017: https://www.congress.gov/115/plaws/publ97/PLAW-115publ97.pdf, (hereinafter: the TCJA).

[12] See for the OECD TPG: Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1., see for the TCJA: EY Tax Insights, US tax reform may complicate supply chain

Before the publication of the TPG 2017, there were discussions about relying on other sources related to the definition of intangibles, such as from accounting or law. However, the OECD introduced an autonomous definition for intangibles in a TP context[13], which also differs from the definition according to the TCJA[14] in an extent that would turn over various tax court cases, as introduced in section four of this thesis. OECD Member States (MS) are suspicious that the definition under the TPG 2017 does not capture all intangibles which are exchanged between independent parties, but should be considered for TP purposes.[15] Because of its broad definition, as well as the differences compared to the TCJA, the guidelines do not protect a legal basis[16] and do not provide certainty for tax administrations and taxpayers[17].

1.2 Research Purpose

The research purpose of this thesis is the lack of clarification within the definition of intangibles in a transfer pricing context under the OECD Transfer Pricing Guidelines, and its discrepancies to the revised and extended transfer pricing rules under the U.S. Tax Cuts and Jobs Act.

While the main question to be answered is: "What discrepancies arise from the incompatible definitions of intangibles for transfer pricing purposes according to the OECD Transfer Pricing Guidelines 2017 and the U.S. Tax

issues, https://taxinsights.ey.com/archive/archive-articles/us-tax-reform-may-complicate-supply-chain-issues.aspx.

[13] OECD Transfer Pricing Guidelines 2017, para. 6.6; Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, in Lang, M., Storck, A., Petruzzi, R., Risse, R., Transfer Pricing and Intangibles, Linde 2019, Ch. 2, (hereinafter: Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, 2019).

[14] TCJA 131 Stat. 2218 (a)(2)(vi).

[15] Silberztein, C., Transfer Pricing aspects of Intangibles: the OECD Project, Transfer Pricing International Journal 08/11.

[16] Verlinden, I., Bakker, A., Mastering the IP Life Cycle from a Legal, Tax and Accounting Perspective: Grasping the Intangible, IBFD 2018, Ch. 1.3.1.2.

[17] Schwarz, J., Tax Certainty: Cure the disease, not the symptom, 2018, http://kluwertaxblog.com/2018/08/28/tax-certainty-cure-disease-not-symptom/; Markham, M., A Rose by Any Other Name? The OECDs Proposed Revised Definition of Intangibles, Intertax Vol. 43, 2015, p. 673-687.

Cuts and Jobs Act, and what are the risks?", the thesis also aims to provide a clear outline of the importance of a plain and proper definition of intangibles in a TP context. The vague definition in the TPG 2017 is getting analysed, followed by a discussion of the discrepancies between the different definitions according to the TPG 2017 and the TCJA, and an assessment of its legal risks.

1.3 Method

The thesis relies on the legal-dogmatic research method[18], taking an internal perspective and assessing the law as it stands today. Current primary and secondary legal sources are analysed from a critical point of view, with also mentioning some historical developments.

The basis of the analysis are the OECD Transfer Pricing Guidelines 2017 and the U.S. Tax Cuts and Jobs Act, written from an EU perspective, and therefore focusing on the TPG 2017. The legal sources are analysed and confronted with each other, also with the application of available case law. In order to provide a far-reaching answer to the raised question, other legal doctrines, academic journal articles and papers, books, commissions' publications and other internet sources are analysed.

1.4 Delimitation

This thesis exclusively deals with intangibles in a transfer pricing context and focuses on its different definitions. It is assumed that the reader provides good knowledge in tax law and especially within the concept of transfer pricing, since the thesis does not introduce transfer pricing itself.

The focus is on the vague definition of intangibles for transfer pricing purposes within the OECD Transfer Pricing Guidelines 2017, as well as on the discrepancies of the definitions of intangibles under the TPG 2017 and the U.S. Tax Cuts and Jobs Act. Occurring legal risks such as uncertainty for tax administrations and taxpayers, as well as the risk of double taxation and double non-taxation are getting analysed. However, how to prevent double taxation and double non-taxation is out of the scope of the thesis and is only mentioned briefly.

The importance of a clear and precise definition of intangibles for associated MNEs, exclusively for transfer pricing purposes, is getting highlighted. The different definitions of intangibles for a legal or accounting purpose,

[18] Douma, S., Legal Research in International and EU Tax Law, 2014, p. 17-20.

compared to the one for transfer pricing, is mentioned, but is not discussed further.

1.5 Outline

The first section of this thesis already provided an overview of the purpose and background of the research.

The second section deals with the legal sources. In its first subsection the OECD Guidelines are getting introduced, while the second subsection discusses intangibles within the OECD and its relevance. That subsection will also give an overview about other issues and legal changes related to intangibles in a TP context, such as the determination of ownership or the valuation of intangibles. The third subsection provides an overview of the U.S. Tax Reform of 2017, namely the U.S. Tax Cuts and Jobs Act.

Section three exclusively deals with the definition of intangibles. While the first subsection focuses on the definition according to the TPG 2017, the second subsection defines intangibles in the TCJA and the changes to its previous tax law. This subsection provides a basic knowledge of the TCJA and its definition of intangibles, in order to understand its related case law, as introduced in the first subsection of section four.

Section four provides an in depth discussion of the discrepancies between the definitions of intangibles with the application of available case law. It starts with the U.S. Amazon case from 2019, followed by the older U.S. case Veritas, and a Danish National Court case, which exclusively deals with the amortization of goodwill. The second subsection concludes the discussion by analysing the different legal sources and the arguments provided.

The fifth section presents the risks occurring through the discrepancies discussed in the sections above. The first subsection deals with uncertainty, mainly from a perspective of the vague definition of the TPG 2017. This subsection deals with the importance of clear and precise regulations. The second subsection introduces the risk of double taxation and double non-taxation for associated MNEs, with one jurisdiction applying the TPG 2017 and the other one applying the TCJA. This subsection concludes with a brief analysis of existing legal regulations on how to prevent such risks.

Section six concludes and summarizes the thesis, and provides an impetus for further questions.

2 Legal Sources

2.1 The OECD TPGs

The TPG 2017 are a revision of the OECD Transfer Pricing Guidelines 2010[19], and a result of the Base Erosion and Profit Shifting Project 2015 (BEPS Project)[20], more specifically Action 8-10[21] of the Project. The first report the guidelines are based on, is the OECD Report on Transfer Pricing and Multinational Enterprises of 1979.[22] The guidelines are seeking to meet the interests of both, tax administrations, as well as taxpayers, in a balanced and fair way.[23] However, they do not consider domestic TP issues, but rather focus on the international aspects, because international transactions of associated MNEs are more difficult to deal with than domestic transactions, since they involve different tax jurisdictions.[24]

The importance of the TPG 2017 depends on how the guidelines are getting implemented into national legislation by each MS, hence, they are soft law.[25] However, the guidelines are still adopted by many MS of the OECD, as well as outside the OECD[26], but since they are not legally binding, regulations on TP are within the competence of each jurisdiction. Meaning, even though the U.S. is a MS of the OECD, and therefore relies on the TPG 2017,

[19] OECD, Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, OECD Publishing, Paris, 2010.

[20] OECD/G20, Action Plan on Base Erosion and Profit Shifting Project, Final Report, 2015, (hereinafter: OECD/G20, BEPS Project).

[21] OECD/G20, BEPS Project, Actions 8-10: Aligning Transfer Pricing Outcomes with Value Creation.

[22] OECD Transfer Pricing Guidelines 2017, Preface, para. 13.

[23] OECD Transfer Pricing Guidelines 2017, Preface, para. 18.

[24] OECD Transfer Pricing Guidelines 2017, Preface, para. 12.

[25] OECD Homepage, Regulatory policy, Soft Law, https://www.oecd.org/gov/regulatory-policy/irc10.htm.

[26] Strotkemper, N., Das Spannungsverhältnis zwischen Schiedsverfahren in Steuersachen und einem Internationalen Steuergerichtshof, Nomos, 2017, p. 480; Solilová, V., Transfer Pricing Rules in EU Member States, Acta univ. agric. et silvic. Mendel. Brun., LVIII, No. 3, pp. 243–250, 2010, p. 247.

discrepancies still occur because of the vague formulated guidelines, and the clearer formulated U.S. tax law, as discussed in section three and four.

2.2 Intangibles in the OECD TPGs

Developed or acquired intangibles take on a decisive role within the value creation process of many MNEs, expressed in numbers, that value is about 80 percent or more.[27] Intangibles have become one of the most relevant factors to consider when it comes to running a global business.[28] The importance of intangibles increases for economies[29], especially in states that export technology. MNEs are looking for the most tax efficient treatment related to intangibles, and tax authorities are worried that the increasing use of intangibles will result in aggressive tax planning such as base erosion and profit shifting.[30] Action 8 of the BEPS Project from 2015 deals with intangibles in TP[31]. This was taken over in the TPG 2017, and especially Chapter VI is dealing with the transfer of intangibles. Determining the conditions in comparable transactions between unrelated parties is the main focus of TP, also in the context of intangibles.[32]

One of the main goals of the TPG 2017 is the definition of intangibles, as well as the appropriate allocation of profits related to the transfer of intangibles in conformity with value creation. Another significant goal of the TPG 2017 is to clarify the situation with the transfer of hard to value intangibles (HTVI), to develop new rules or special measure.[33]

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[27] Prasanna, S., Chapter IV, Valuation of Intangibles: Valuation of intangibles – panel discussion in Lang, M., Storck, A., Petruzzi, R., Risse, R., Transfer Pricing and Intangibles, Linde 2019.

[28] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1.

[29] Bakker, A., De Baets, S., Mazio, M., Szotek, P., Increasing Importance of IP Rights, in Verlinden, I., Bakker, A., Mastering the IP Life Cycle from a Legal, Tax and Accounting Perspective: Grasping the Intangible, IBFD 2018, pp. 3–11.

[30] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1.

[31] OECD/G20, BEPS Project, Actions 8-10: Aligning Transfer Pricing Outcomes with Value Creation.

[32] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.

[33] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1.

The OECD also clarifies the importance of the ability to an ownership or to be able to control an intangible by an associated MNE. Those criterions must be fulfilled to fall within the catalogue of intangibles.[34] Before the BEPS Project, legal ownership got accepted by most states to determine returns related to intangibles. However, after the BEPS Project a change in determining the ownership happened. That change can be seen in the new TPG 2017 under the DEMPE functions[35] or para. 6.32 of the TPG 2017, delimiting the legal owner from the MNEs that perform functions, used assets or assumed risks of the future value of the intangible[36]. Hence, a move forward in analysing the actual functions performed by the group companies can be noted, as well as assets used and risks assumed in relation to intangibles.[37] Determining the legal owner of intangibles does not "necessary imply that the legal owner is entitled to any income generated by the business"[38] through the owned intangible[39]. If the legal owner does not control, nor perform or assume all the risks within the development of the intangible, the legal owner is not entitled to ongoing benefits[40].

Next to knowing what kind of intangible is involved in a TP issue, as well as identifying the owner of the intangible, it is relevant to identify the specific controlled transaction of the intangible[41]. The general types of this kind of transactions either involve transfers or rights of intangibles, or transactions that involve the use of intangibles. The second transaction is connected with selling goods or providing services.[42]

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[34] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.3, see for the catalouge of intangibles the second subsection of this section of the thesis.

[35] Ludovici, P., Transfer Pricing and Intangibles, in Fundamentals of Transfer Pricing: A Practical Guide, Lang, M., Cottani, G., Petruzzi, R., Storck, A., Kluwer Law International 2019.

[36] OECD Transfer Pricing Guidelines 2017, para. 6.32.

[37] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1.

[38] OECD Transfer Pricing Guidelines 2017, para. 6.47, first sentence.

[39] OECD Transfer Pricing Guidelines 2017, para. 6.47.

[40] OECD Transfer Pricing Guidelines 2017, para. 6.54.

[41] OECD Transfer Pricing Guidelines 2017, para. 6.86.

[42] OECD Transfer Pricing Guidelines 2017, para. 6.87.

For the valuation of intangibles, it is important to understand the role of each intangible in the value chain analysis, and to identify the activities that influence the value of it. Each valuation method should also fulfil accounting and tax purposes. However, this is not always the case, i.e. not every identified value of intangibles are necessarily relevant for TP purposes. Therefore, it is significant to choose a proper valuation method.[43] Another significant factor for the valuation of intangibles might be the protection in its legal, contractual or other different forms, which also applies to its structure. Some of them can be identified and transferred separately, while others are related to other business assets and cannot be transferred on their own.[44]

Para. 6.7 TPG 2017 identifies the dispute between the different definition of an intangible for TP purposes and for accounting purposes.[45] Hence, relevant intangibles from a TP perspective are not necessarily considered as an intangible for accounting purposes, and the other way around. For example, internally developed intangibles of a company are not mentioned in their balance sheet, but they most likely generate a profit, therefore they have to be taken into account for TP purposes. That is also applied when it comes to improving the value of an intangible during exploitation.[46]

It got discussed and requested, before the publication of the TPG 2017, to use sources such as from accounting, financial valuation, intellectual property law and other similar legal basis, to define intangibles.[47] However, accounting rules can be used as a basis for information from a TP point of view, but they do not cover all relevant factors to determine an item as an intangible or not. Similar for the characterization for general tax purposes, such as tax treaty law. Certain items might be considered as intangibles according to tax treaty

[43] Prasanna, S., Chapter IV, Valuation of Intangibles: Valuation of intangibles – panel discussion in Lang, M., Storck, A., Petruzzi, R., Risse, R., Transfer Pricing and Intangibles, Linde 2019.
[44] OECD Transfer Pricing Guidelines 2017, para. 6.8.
[45] OECD Transfer Pricing Guidelines 2017, para. 6.7.
[46] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.2.
[47] Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, 2019, Ch. 2.

law, but not for TP purposes. On those grounds the OECD established its own system in a TP context in order to define and classify intangibles.[48]

2.3 The U.S. Tax Reform (The TCJA)

The tax reform in the U.S. came into force in January 2018, namely the Tax Cuts and Jobs Act of 2017. This tax reform is particularly intended to attract investment and capital, and to make the location U.S. more attractive, yet, some regulations are limited and will expire in 2025.[49] The Internal Revenues Code (the IRC) is the U.S. Federal Tax Law, published in Title 26 of the U.S. Code (the USC). The official interpretation of the IRC is in the Treasury Regulations (the Treas. Reg.)[50] from the U.S. Department of the Treasury, introduced in Title 26 of the Code of Federal Regulations (the CFR).

The IRC provides far-reaching changes by the TCJA, related to taxation of international income, and attention was paid on strengthen the U.S. economy. A significant change of the TCJA is the reduced corporate income tax rate, and instead of a progressive tax rate, a flat rate got introduced.[51] The transfer of taxable income to low- or no-tax jurisdictions should be avoided, and is also a highlight of the tax reform, i.e. low-taxed income should be identified with the Global Intangibles Low Taxable Income (GILTI)[52]. Another incentive for economic activities in the U.S. is the Foreign-Derived Intangibles Income (FDII)[53]. And in order to prevent the U.S. tax base, the Base Erosion and Anti-Abuse Tax (BEAT)[54] got introduced, expecting a minimum tax on some tax-deductible payments from U.S. MNEs.[55]

The regulations in the Treas. Reg. Section 482[56], and some in Section 367 IRC, as well as some provisions under the TCJA, provide specific U.S. TP regulations and guidelines on the valuation of assets and intangibles between MNEs.

[48] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.2.
[49] Freiberg, J., Weitreichende Änderungen des US-Steuersystems – Keine Erleichterungen nach IFRS, PiR Nr. 2, 2018, p. 60.
[50] The U.S. Treasury Regulations, (hereinafter: Treas. Reg.).
[51] Freiberg, J., Weitreichende Änderungen des US-Steuersystems – Keine Erleichterungen nach IFRS, PiR Nr. 2, 2018.
[52] TCJA 131 Stat. 2208 (b), added in Section 951A IRC.
[53] TCJA 131 Stat. 2214 (b), added in Section 250 IRC.
[54] TCJA 131 Stat. 2226 (a), added in Section 59A IRC.
[55] Novak, K. L., Thomas, M. P., Lowell, C. H., Treatment of Intangibles under New US Tax Regime, International Transfer Pricing Journal, IBFD 2018.
[56] Treas. Reg., Section 482: https://www.irs.gov/pub/irs-apa/482_regs.pdf.

3 Definition of Intangibles

3.1 The Definition of Intangibles in the OECD TPGs

Chapter VI of the TPG 2017 specifically deals with the special considerations of intangibles.

Para. 6.13 TPG 2017 clarifies that the definition of intangibles in the TPG 2017 is only relevant for TP purposes. Meaning, this definition is just applicable for Art. 9[57] of the OECD Model Convention (OECD MC)[58].[59] That article deals with associated MNEs in different contracting states. It clarifies that in order to fall within that article, "[…] conditions are made or imposed between the two enterprises"[60] in their relations, that differ from the ones of independent enterprises.[61] Hence, the definition of intangibles is according to the OECD relevant for cross-border transactions. However, a broader or narrower definition does affect domestic transactions as well, e.g. since direct taxation is not harmonized within EU law and many MS rely on the TPG 2017, they implement the TPG 2017 into national legislation, using the definition for both, domestic and cross-border transactions.

The guidelines provide various classifications of intangibles, such as hard or soft, and routine or non-routine intangibles.[62] The OECD does not follow a specific classification, but rather provides a wide catalogue of items[63] that are generally considered as intangibles for TP purposes. Para. 6.17 categorises intangibles, that are not comparable or intangibles that are expected to provide

[57] In a certain extent, the definition is also applicable for Art. 7 OECD MC, dealing with Business Profits, clearifying the State where profits should be taxable. Para. 1: "Profits [...] shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therin.".

[58] OECD, Model Tax Convention on Income and on Capital, 2017, (hereinafter: OECD Model Convention, 2017).

[59] OECD Transfer Pricing Guidelines 2017, para. 6.1-6.2; Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, 2019, Ch. 3.

[60] OECD Model Convention, 2017, Art. 9, para. 1, first sentence.

[61] OECD Model Convention, 2017, Art. 9, para. 1.

[62] OECD Transfer Pricing Guidelines 2017, para. 6.15-6.16.

[63] OECD Transfer Pricing Guidelines 2017, para. 6.19-6.31.

a great future benefit, as "unique and valuable intangibles". This is important to know for the comparability analysis to determine the transaction for an intangible. Hence, it is not just relevant to identify if the item is an intangible or not, it is also from importance if a specific intangible is unique and valuable, or if it can be classified with other intangibles.[64] Looking at the TP methods under Chapter II of the TPG 2017, it already got highlighted in para. 2.4, that the transactional profit split method (PSM) might be the most appropriate method to apply on, when both parties represent unique intangibles to the transaction. That shows again its significance to know if a unique intangible is related to a transaction of one party. However, this paragraph also clarifies that the PSM might be also suitable in other transactions and is not bound to intangibles. Nevertheless, profit based methods can only be accepted as long as they are compatible with Art. 9 OECD MC[65].

Section A.4. of Chapter VI of the TPG 2017 provides an illustration of items that are often seen as intangibles for TP purposes, considering that this illustration should not replace a detailed analysis. According to that section, the catalogue of items includes patents[66], know-how and trade secrets[67], trademarks[68], trade names[69], brands[70], rights under contracts[71] and licenses[72], therefore, they do fall within the meaning of intangibles for TP purposes.

The nature of a goodwill and ongoing concern value is followed by a comprehensive debate of the OECD.[73] A goodwill has many different meanings and definitions, depending on the field applied on.[74] Therefore, it

[64] Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, 2019, Ch. 2.
[65] OECD Transfer Pricing Guidelines 2017, para. 2.6.
[66] OECD Transfer Pricing Guidelines 2017, para. 6.19.
[67] OECD Transfer Pricing Guidelines 2017, para. 6.20.
[68] OECD Transfer Pricing Guidelines 2017, para. 6.21.
[69] OECD Transfer Pricing Guidelines 2017, para. 6.22.
[70] OECD Transfer Pricing Guidelines 2017, para. 6.23.
[71] OECD Transfer Pricing Guidelines 2017, para. 6.25.
[72] OECD Transfer Pricing Guidelines 2017, para. 6.26.
[73] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.2.
[74] OECD Transfer Pricing Guidelines 2017, para. 6.27; Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.4.

is of great importance to have an exact definition of goodwill for TP purposes, and if a goodwill or an ongoing concern value can be treated as an intangible.[75] However, the OECD leaves the task open, of analysing and determining the question if goodwill or ongoing concern value falls within the definition of intangibles for TP purposes or not.[76]

The OECD sets out, that separate transferability does not constitute a necessary condition for an item to be defined as an intangible[77], i.e. the issue of separate transferability does not have to be seen as a crucial element in determining whether an item is an intangible from a TP perspective or not.[78] However, the guidelines still mention that separate transferability from other assets of a company is not possible for goodwill and ongoing concern value[79], while they also could not provide any specific clarifications on how to treat them within a TP context. This results in uncertainty for tax administrations and taxpayers, since goodwill and ongoing concern value would be involved within every transaction made, and it would be neither wrong, nor right to not consider goodwill and ongoing concern value at all.

3.2 The Definition of Intangibles in the TCJA

The TCJA has a focus on intangibles, as it gives limitations on income shifting with the help of the transfer of intangibles. In order to provide the Internal Revenue Services (IRS) with more authority, the tax reform introduces more specific regulations of some principles when it comes to the valuation of the transfer of intangibles. Since 2008 the IRS follows the position that intangibles must be valued within an intercompany intangible transfer, in order to offer the most reliable valuation method.[80] While the tax

[75] OECD Transfer Pricing Guidelines 2017, para. 6.29.
[76] OECD Transfer Pricing Guidelines 2017, para. 6.28.
[77] OECD Transfer Pricing Guidelines 2017, para. 6.7.
[78] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.2.
[79] OECD Transfer Pricing Guidelines 2017, para. 6.27.
[80] EY Tax Insights, US tax reform may complicate supply chain issues, https://taxinsights.ey.com/archive/archive-articles/us-tax-reform-may-complicate-supply-chain-issues.aspx.

reform of 2009 already expanded the definition of intangibles, it was yet not enough to meet the position of the IRS.[81]

Nevertheless, that position of the IRS got confirmed in the TCJA by emending the Treas. Reg. Section 482, namely the aggregation rules, by adding the sentence "For purposes of this section, the Secretary shall require the valuation of transfers of intangible property (including intangible property transferred with other property or services) on an aggregate basis or the valuation of such a transfer on the basis of the realistic alternatives to such a transfer, if the Secretary determines that such basis is the most reliable means of valuation of such transfers."[82], i.e. to get a more reliable result, the new provision requires that transactions should be analysed in aggregate.[83]

As already mentioned in the second section, the regulations in the Treas. Reg. Section 482, as well as some regulations in Section 367 IRC, and some provisions under the TCJA, provide specific U.S. TP regulations and guidelines on the valuation of assets and intangibles between associated MNEs. Treas. Reg. § 1.482-4 gives guidance on the pricing of controlled transactions with intangibles being involved, whereas Treas. Reg. § 1.367(d)-1T[84] deals with the transfer of intangibles to foreign corporations. Treas. Reg. § 1.482-4(f)(3)(i) and (ii)(A) clarifies the ownership and legal protection of intangibles. That provision states that the legal owner should also be the owner for tax purposes, unless legal ownership conflicts with the economic substance of that transaction.

However, the most significant change for this thesis is the amended definition of intangibles according to Section 936(h)(3)(B) IRC, also listed in the Treas.

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[81] Dziwiński, K., When old rules prevail over new rules – Amazon wins again in U.S. intangibles case, Linde TPI 2/2020, (hereinafter: Dziwiński, K., When old rules prevail over new rules, Linde TPI 2/2020).

[82] TCJA 131 Stat. 2219 (b)(2), Treas. Reg. § 1.482-1(f)(2)(i)(C).

[83] EY Tax Insights, US tax reform may complicate supply chain issues, https://taxinsights.ey.com/archive/archive-articles/us-tax-reform-may-complicate-supply-chain-issues.aspx.

[84] Treas. Reg. §1.367(d)-1T, https://www.govinfo.gov/content/pkg/CFR-2019-title26-vol5/pdf/CFR-2019-title26-vol5-sec1-367d-1T.pdf.

Reg. § 1-482(4)(b)(1)-(6). The old provision under that Section defined an intangible as "an asset […] that has substantial value independent of the services of any individual"[85], without including "goodwill", "ongoing concern value" or "workforce in place". In order to prevent MNEs from a tax-free transfer of intangibles, its definition got expanded by the TCJA[86], expressively defining "goodwill", "ongoing concern value" and "workforce in place" under Section 936(h)(3)(B)(vi) IRC as being an intangibles. Also, the TCJA removes the need for an intangible to be of significant value regardless of the service of an individual[87], i.e. U.S. MNEs are getting encouraged to place their valuable intangibles in the U.S.[88]

The new definition of intangibles according to the TCJA makes planning of TP more challenging. Because of the expanded definition, that an intangible includes assets such as goodwill and ongoing concern value, it results in a higher value of the intangible. Before the tax reform got into force, it was reasonable to aim a low value for cross-border transactions of intangibles, especially when the related parties were located in a low tax jurisdiction. However, the TCJA changed that view with the possibility of getting a tax benefit for higher valued intangibles, when the intangible gets transferred from a low or no-tax jurisdiction to the U.S. The tax benefit results in a possible deduction in the U.S., which is the jurisdiction of the purchasing MNE. Hence, it encourages taxpayers to have a higher value of intangibles, as long as that transaction does not trigger GILTI or BEAT, which leads to negative tax consequences.[89]

With the knowledge, that the TCJA might provide tax benefits from having a higher tax burden and getting taxed in the U.S., it is not safe to say if a MNE based in the U.S. would benefit from shifting its tax burden to a jurisdiction with a less extensive definition of intangibles. However, that discussion is out of the scope of this thesis.

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[85] Treas. Reg. § 1.482-4(b).

[86] TCJA 131 Stat. 2218 (a)(2)(vi), added in Section 936(h)(3)(B) IRC.

[87] TCJA 131 Stat. 2218 (a)(2)(vii).

[88] WTP Advisors, New Tax Legislation Consequences on US Transfer Pricing and Intangibles https://wtpadvisors.com/new-tax-legislation-consequences-on-us-transfer-pricing-and-intangibles.php.

[89] EY Tax Insights, US tax reform may complicate supply chain issues, https://taxinsights.ey.com/archive/archive-articles/us-tax-reform-may-complicate-supply-chain-issues.aspx.

4 The Discrepancies of the different Definitions

While the TPG 2017 does not provide a clear treatment of goodwill and ongoing concern value, the TCJA explicitly includes them within the definition of an intangible for TP purposes.

The following section will discuss the significant meaning of goodwill and ongoing concern value in the light of case law, and will conclude with a discussion of the discrepancies within the definition of intangibles according to the TPG 2017 and the TCJA.

4.1 Case Law

4.1.1 U.S. Amazon[90]

Amazon.com, Inc. (Amazon), located in the U.S., established a subsidiary in Luxembourg 15 years ago, namely Amazon Europe Holding Technologies SCS (Amazon Europe). While the companies entered in a cost-sharing agreement (CSA), one of the conditions of the agreement was, that Amazon Europe had to make a buy-in payment for the assets of Amazon. Those buy-in payments became part of the CSA and fell into the definition of intangibles according to U.S. law, which was in force during that time. With going into that kind of agreement, one or more enterprises outside the U.S. could use intangibles developed in the U.S. to generate profits, i.e. Amazon and Amazon Europe became owners of these intangibles. The buy-in payments of Amazon Europe result in being a taxable income for Amazon, while cost-sharing payments of Amazon Europe on the other side, could reduce the tax deductions of research costs by Amazon.

While the Amazon case in 2017 focused on the valuation of transferred intangibles, the case in 2019 is about the definition of intangibles.[91]

[90] United States Court of Appeals for the Ninth Circuit of 16 of August 2019, Amazon.Com, Inc. & Subsidiaries v. Commissioner of Internal Revenue, No 17-72922, T.C. No 31197-12, (hereinafter: Amazon.Com, Inc. & Subsidiaries v. Commissioner).
[91] Dziwiński, K., When old rules prevail over new rules, Linde TPI 2/2020.

On one side, only specific intangibles transferred under the CSA were taken into account by Amazon, namely technology, fulfilment centers, marketing intangibles, customer information and other related business activities, resulting in a value of intangibles of 217 Mio $. On the other side, the Commissioner considered the entire Amazon Europe business in its valuation, such as education and experience of its employees, ongoing concern value, goodwill and growth options, such as unique business expectations, resulting in a value of 3.6 bn $. Hence, those different approaches led to a major mismatch of valuation.[92]

The case was governed by the regulations from 1994 and 1995, therefore one of the arguments of Amazon was, that in order to be qualified as an intangible, an item must be separately transferrable, i.e. it must be independent of the business. Since residual-business assets are inseparable from the business, that requirement is not fulfilled. This position of Amazon is also supported by case law such as Arcadia[93] and Veritas[94].[95] Looking at the Veritas case of 2009, the United States Court of Appeals for the Ninth Circuit (the Court) stated that a subsidiary outside the U.S. should not include the value of workforce in place in the buy-in payment when entering into a CSA with its parent company in the U.S., because it is not separately transferable. However, the Court disagreed with that point in the Amazon case, without any further clarification[96], i.e. separate transferability should not be a requirement to be considered as an intangible according to the Amazon case.

While the amended rules of the TCJA of 2017, or the already broader definition of intangibles under the tax reform of 2009, were not applicable for the case at stake, the definition of intangibles did not include residual-business assets. However, one of the arguments that made Amazon win the case, was that the items at stake would not be compensated between non-related companies. Nevertheless, it is notable the Court did not consider

[92] Amazon.Com, Inc. & Subsidiaries v. Commissioner, pp. 11-12.
[93] Arcadia, Ohio v. Ohio Power Company, 498 U.S. 73, 78, 1990.
[94] Veritas v. Commissioner, 133 T.C. 297, U.S.T.C. 2009.
[95] Amazon.Com, Inc. & Subsidiaries v. Commissioner, p. 17.
[96] Amazon.Com, Inc. & Subsidiaries v. Commissioner, p. 13.

intangibles that are transferred after the definition of intangibles got amended, i.e. after the TCJA got into force. Which would have been interesting since the new TCJA definition of intangibles would overturn the decision in the latest Amazon case of 2019.[97]

4.1.2 Veritas[98]

Veritas Software Corporation (Veritas), is another U.S. case, dealing with the financial years of 1999, 2000 and 2001. The U.S. Software developer Veritas, set up a wholly owned foreign subsidiary in Ireland (Veritas Europe), and the companies agreed in 1999 on a CSA in order to share the costs of developing intangibles. Veritas contributed intangibles such as trademark, patents and source code, for a platform developed together. Veritas Europe received in return rights to the intangibles according to the agreement. For its valuation, Veritas used the comparable uncontrolled price method (CUP method) at 118 Mio $. The IRS did not except the CUP method and replaced it with the comparable profit method (CPM method), calculating a value of 1.7 bn $[99]. Nevertheless, the Court held that the CUP method was the most appropriate method to use in that case, to be consistent with the ALP, and rejected the evaluation of the IRS as arbitrary, capricious and unreasonable.[100]

The Court held, that for the years at issue, there was no clear authorization to include workforce in place, goodwill or ongoing concern value in the definition of intangibles. Also, these items are not transferable independently, i.e. they are an inseparable intangible of the residual-business profit of a company. Therefore, it is not permitted to include workforce in place,

[97] Dziwiński, K., When old rules prevail over new rules, Linde TPI 2/2020; Novak, K. L., Thomas, M. P., Lowell, C. H., Treatment of Intangibles under New US Tax Regime, International Transfer Pricing Journal, IBFD 2018.

[98] United States Court of Appeals for the Ninth Circuit of 10 of December 2009, Veritas Software Corp. & subs. v. Commissioner, 133 T.C. 297, T.C. No 12075-06, (hereinafter: Veritas v. Commissioner).

[99] Veritas v. Commissioner, at 313.

[100] Veritas v. Commissioner, at 312.

goodwill, or ongoing concern value in the valuation nor the buy-in payment for these pre-existing intangibles. [101]

According to the IRS' action on decision[102], the IRS does not agree with the decision of the Court.[103] The facts found by the Court differ significantly from the findings of the IRS, since the IRS clarifies that workforce in place, goodwill, and ongoing concern value do have a beneficial impact on the transactions of Veritas Europe, and that they should not be considered separately.[104]

4.1.3 Denmark vs. Pharma Distributor[105]

Denmark vs. Pharma Distributor is a Danish National Court case from 2017, published in March 2020. The case deals with the financial years from 2006 to 2010, and with the question if Pharma Distributor were authorized to not consider the amortization of goodwill within their TP comparability analysis, i.e. that the annual amortization got not treated as an operating cost. The company chose to use the transactional net margin method (TNMM), and the documentation showed that the company's net margin was below the benchmark in the years from 2006 to 2009, where the annual goodwill amortization was deducted. In the year 2010, the amortization of the goodwill was deducted from the net profit as well, however the net profit was within the arm's length interval, but within the quartile range.

[101] Veritas v. Commissioner, at 316.

[102] Department of the Treasury, Internal Revenue Service, Action on Decision of Veritas Software Corp. & subs. v. Commissioner, IRB No. 2010-49, 803, 2010, https://www.irs.gov/pub/irs-aod/aod201005.pdf, (hereinafter: IRS, AOD, Veritas v. Commissioner).

[103] IRS, AOD, Veritas v. Commissioner, p. 1.

[104] IRS, AOD, Veritas v. Commissioner, p. 2.

[105] Danish National Court on 13. Janurary 2020, Denmark vs. Pharma Distributor A A/S, B-1253-17, SKM2020.105.OLR, this Chapter relies on the last section of the case: "National court reasoning and result (Landsrettens begrundelse og resultat)"; TPguidelines.com, https://tpguidelines.com/denmark-vs-pharma-distributor-a-a-s-march-2020-national-court-case-no-skm2020-105-olr/.

Even though the National Tax Court ruled in favour of Pharma Distributor, the National Court did not. Since the goodwill must at least have an indirect connection to the company's profit, according to the National Court, it found that such goodwill should have been treated as an operating asset, hence the amortization of the goodwill should have been considered for the calculation of the net profit of the company and not been deducted.

4.2 Analysis

As already mentioned in the introduction, OECD MS are concerned whether the definition of intangibles in the TPG 2017 does capture all relevant intangibles for TP purposes or not. The broad definition and the significant differences to the TCJA does not protect a legal basis[106].

Looking at the U.S. Amazon case from a current perspective, the argument of Amazon, saying that the affected items would not be compensated between non-related companies, hence, they should not be considered as intangibles, is confirmed by the OECD in para. 6.6 TPG 2017. This statement got further supported by the catalogue of intangibles under para. 6.18 TPG 2017, since the items do not explicitly fall within that catalogue.[107] Therefore, from a current perspective, the U.S. Amazon case would show the same result if the TPG 2017 would be applicable, assuming that the MS have adopted the guidelines without further changes related to the definition, and that the court does not overrule the guidelines, e.g. making a straight forward argument on the treatment of goodwill and ongoing concern value, as one can see in Denmark vs. Pharma Distributor. On the other hand, Amazon would lose according to the TCJA.

The argument of Amazon, that an intangible, or item in general, must be separately transferable in order to be considered as a residual-business assets, is not a criterion for falling into the definition of being an intangible, and got dismissed. It is notable, that this argument got accepted in the Veritas case of 2009, while both cases are governed by the regulations from 1994 and 1995. This proves the importance of clear and precise formulated regulations and treaties. However, the argument that intangibles must be independent of the business, in order to fulfil the requirement for a residual-business asset, cannot be accepted anymore, neither within the TPG 2017, nor within the TCJA, since separate transferability does not constitute a criterion to fall

[106] Verlinden, I., Bakker, A., Mastering the IP Life Cycle from a Legal, Tax and Accounting Perspective: Grasping the Intangible, IBFD 2018, Ch. 1.3.1.2.
[107] Dziwiński, K., When old rules prevail over new rules, Linde TPI 2/2020.

under the definition of intangibles in a TP context, as also discussed in section three.

Going back to current case law, the Danish National Court made a straight forward statement in early 2020 in its Denmark vs. Pharma Distributor case. It states that a goodwill has at least an indirect connection to the company's profit and that is why it should be considered an operating asset. Hence, the amortization of the goodwill at stake should have not been deducted of the net profit of Pharma Distributor.

In accordance with the opinion of Dziwiński and Peng, goodwill and ongoing concern value do influence the determination of the arm's length price. While they cannot be transferred or owned, they do not fall within the scope of the general definition of intangibles according to the TPG 2017.[108] However, this does not constitute a criterion for being an intangible or not, and just because it does not fall within the general definition of intangibles, it still provides companies with a significant value. The beneficial impact of goodwill and ongoing concern value should be seen separate from the actual nature of a transaction, as already mentioned in the discussion of the IRS in 2010 about the Veritas case. And as mentioned in Denmark vs. Pharma Distributor, since goodwill must at least be connected indirectly to the generated profits of a company, it should be treated as an operating assets, hence, it should be considered when determining the TP of transactions.

[108] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 2.3.

5 Legal Risks of the Discrepancies

Tax treatments are under constant scrutiny, including TP issues connected to intangibles[109]. That scrutiny results in expanding treaties and regulations, in order to provide tax stability for tax administrations and taxpayers regarding international transactions. However, this increases the improper use of such treaties and regulations[110], especially talking about the treatment of goodwill and ongoing concern value for TP purposes, since the TPG 2017 got expanded, but not precise enough. Tax planning techniques in an international context might abuse different MS tax laws or the tax treaty between those MS[111], which gets easier within regulations not precisely formulated.

The following sections will first introduce the risk of uncertainty, mainly within the TPG 2017, and is followed by discussing the possible issues of double taxation and double non-taxation, resulting from the significant discrepancy of the definition of intangibles between the TPG 2017 and the TCJA.

5.1 Uncertainty within the TPG 2017

According to Wagner, ”legal uncertainty always occurs when individual actors are uncertain of the effects of the provisions of the dominant legal system on the results of their actions.”[112], meaning that taxpayers are unsure if the actions they take are following the legal provisions of their jurisdictions. Objective legal uncertainty is described as a lack of statutory regulations, or even no existence of such regulations at all, while subjective legal uncertainty

[109] Dziwiński, K., Peng, C., the post-BEPS TP aspects of intangibles, 2019, Ch. 1.

[110] García Prats, F. A., The “Abuse of Tax Law”: Prospects and Analysis, 2017, p. 70, https://www.researchgate.net/publication/255698380_The_'Abuse_of_Tax_Law'_Prospects_and_Analysis, [acessed on 16 May 2020]. (hereinafter: García Prats, F. A., The “Abuse of Tax Law”, 2017).

[111] García Prats, F. A., The “Abuse of Tax Law”, 2017, p. 71.

[112] Wagner, H., Costs of Legal Uncertainty: Is Harmonization of Law the right Answer?, Discussion Paper No. 444, University of Hagen Department of Economics, 2009, Ch. 2.1., first sentance.

differs from individual to individual.[113] This position is, among others, followed by case law of the Court of Justice of the European Union, arguing that legal elements should set clear rules, in order for taxpayers to guess the consequences of their actions.[114] Hence, rules must be "clear, precise and predictable" [115] to be considered as being proportional to the pursued goals.

The broader the formulation of the legislator in its tax law, the higher the possibility in reformulating such tax law, resulting in a situation of applying counteractive anti-abuse techniques.[116] However, not using a treaty in a correct way does not always mean that an illegal act is involved or that a formal breach of the treaty has appeared.[117]

As already discussed in section two and three, the OECD established its own definition of intangibles, only relevant for TP purposes. This definition lacks clarification, since it provides examples of items that can be seen as intangibles, and also discussing items that might or might not be seen as intangibles, but not giving a clear and proper definition. Even though the OECD Guidelines constitute soft law, many MS, as well as non-MS, adopt the guidelines, and as demonstrated in the Danish National Court case about the amortization of goodwill, the treatment of goodwill and ongoing concern value remains uncertain within MS relying on the TPG 2017.

To illustrate the issue with a simplified example, it is assumed that Company A in MS A sells licenses to its associated enterprise, Company B, based in MS B, for a price of 80. It is also assumed that both Companies apply the TPG 2017. Since the treatment of goodwill in the TPG 2017 has not been clarified, the uncertain treatment can be explained as follows: Looking at MS A, the tax administration would claim that goodwill, with an assumed amount of 20, should be part of the licences. The adjustment of the amount of 80 with the goodwill would result in a tax burden of 100 for Company A. While Company A would claim that goodwill does not fall within the definition of intangibles, and the price of 80, with not considering goodwill, is correct. On the reverse side, the tax administration of MS B would declare that goodwill is not a part of the intangible at stake, in order to lower the deducted amount from the tax base of Company B, meaning that 60 is the correct price that can be deducted from the tax burden. While Company B would claim that

[113] Wagner, H., Costs of Legal Uncertainty: Is Harmonization of Law the right Answer?, Discussion Paper No. 444, University of Hagen Department of Economics, 2009, Ch. 2.1.
[114] Judgment of 3 June 2008, Intertanko, C-308/06, EU:C:2008:312, para. 69; Judgment of 14 April 2005, Belgium v Commission, C-110/03, EU:C:2005:223, para. 30.
[115] Judgment of 3 October 2013, Itelcar, C-282/12, EU:C:2013:629, para. 44.
[116] García Prats, F. A., The "Abuse of Tax Law", 2017, p. 56.
[117] García Prats, F. A., The "Abuse of Tax Law", 2017, p. 72, second and third sentence.

goodwill should be considered within the definition of intangibles, in order to have a higher deduction, hence a lower tax burden, i.e. Company B would claim no adjustment for the price of 80.

Company A and B consider the price of 80 correct, while Company A would not include goodwill within the definition of an intangible, and Company B would assume that goodwill is a part of it. From the perspective of the tax administrations, MS A would adjust the price up to 100, declaring that goodwill is not included but should be, while MS B claims that goodwill is included but should not be, resulting in an adjusted price of 60.

According to the TPG 2017, none of the four views is neither right, nor wrong. Hence, if MS do not formulate clear rules within their domestic legislation, or within tax treaties between MS, but rather adopt the guidelines as they are, it leads to uncertain treatment of goodwill and ongoing concern value. That kind of uncertainty does not exist in the U.S. anymore, since they explicitly added goodwill and ongoing concern value as an intangible throughout their tax reform in 2017.

While the importance of a proper definition of an intangible for TP purposes did not got highlighted in Chapter VI of the TPG 2017, it is, in agreement with Van Den Brekel, still essential.[118]

5.2 Double Taxation and Double Non-Taxation

According to Wittendorff, the initial intention of an ALP is the prevention of income shifting, tax base erosion and double taxation. However, before applying the ALP, the transaction to apply on must first be defined.[119] As already discussed above, different jurisdictions apply different definitions, and as a result of occurring discrepancies through that, a situation of double taxation or double non-taxation might arise.

While a MS has the right to tax all profits made on its territory and adjust those of associated enterprises in the case of discrepancies, it is not compelled to prevent MNEs from the risk of double taxation or double non-taxation, which might result from that. Meaning, if associated MNEs do not adjust their transactions accordingly, they can face a situation of double taxation or double non-taxation.[120]

[118] Van Den Brekel, R., Chapter I, Defining Intangibles – an Introduction, 2019, Ch. 1.
[119] Wittendorff, J., The Arm's-Length Principle and Fair Value: Identical Twins or Just Close Relatives?, Tax Notes International, 2011.
[120] Buriak, S., Lazarov, I., Between State Aid And The Fundamental Freedoms: The Arm's Length Principle And Eu Law, Common Market Law Review 56 (4), 905-948, 2019.

5.2.1 The Risk of Double Taxation

To answer the question if the discrepancy leads to double taxation, a distinction between economic and juridical double taxation is necessary. According to Lang, juridical double taxation arises when the income of a taxpayer is taxed in two or more states, while economic double taxation occurs when the same income is taxed by two different taxpayers. When it comes to transactions between associated MNEs based in different jurisdictions, each state determines the taxable income for the MNE under its domestic rules. Since rules differ from one jurisdiction to another, tax administrations might end up in a different valuation of the transaction, i.e. economic double taxation arises.[121]

Based on the facts above and the description of economic double taxation, that kind of discrepancy gives rise to economic double taxation, since different definitions end up in different valuations, regardless of the method used. The value of the transaction will increase in one state and decrease in the other, hence the tax burden will rise for both MNEs.

An example for simplicity, it is assumed that Company A, based in MS A applies the OECD TPG 2017 and buys licenses for 80 from its associated MNE, Company B, based in the U.S. (MS B), hence Company B applies the TCJA. The tax administration of MS A claims that the price of 80 already includes goodwill, which is not explicitly part of an intangible and is therefore not deductible by Company A in MS A. Assuming that the goodwill is valued at 20, Company A is just allowed to deduct 60. On the other side, the tax administration of MS B claims that goodwill did not get considered within the price of 80, hence Company B sold the licenses low-priced, meaning that the intangible should have been sold for 100, which would increase its tax burden by 20. Therefore, Company B has to adjust its taxable profit by 20, meaning the tax burden will be 100. While on the other side, Company A, which bought the license for 80, is just allowed to deduct 60, hence the taxable profit will be increased by 20, while these 20 are also getting taxed in the U.S.

[121] Lang, M., Introduction to the Law of Double Taxation Conventions, IBFD 2013, Ch. 1.2.4.

One could argue that this kind of economic double taxation arises because a MS sets its tax powers on activities that may not have been performed in its area of responsibility.[122] However, this discussion remains untouched within this thesis.

5.2.2 The Risk of Double Non-Taxation

A situation of tax avoidance might occur through shifting the tax base or profits from one jurisdiction to another[123], which leads to a decrease of the tax burden in one state, and an increase in the other state. A situation of double non-taxation is often a result of tax avoidance[124], and might occur through increasing the value of a transaction in one state and decreasing the value in the other state. While in a situation of double taxation, this would lead to an increase of the tax burden for both MNEs, the reverse perspective decreases the tax burden and carries out the risk of double non-taxation.

However, one must distinct between double non-taxation resulting out of a proper use of a treaty and double non-taxation resulting out of the improper use of a treaty. In 1998, Van Weeghel described the improper use of a treaty as an intention of avoiding taxes in one or both contracting states, with the expectation to defeat the objectives of the treaty in a broad sense, shared by both states. Hence, a situation of double non-taxation resulting from the proper use of a treaty, is not an abusive act per se[125], but it still avoids paying taxes.

The provided example assumes again that Company A, based in MS A and applying the OECD TPG 2017, is selling licenses for 80 to its associated Company B, based in the U.S. (MS B) and applying the TCJA. As in the example before, the tax administration in MS A claims again that the price

[122] Buriak, S., Lazarov, I., Between State Aid And The Fundamental Freedoms: The Arm's Length Principle And Eu Law, Common Market Law Review 56 (4), 905-948, 2019.
[123] Judgment of 18 July 2007, Oy AA, C-231/05, EU:C:2007:439, para. 62.
[124] Molina, F. J., DTCs and Double Non-Taxation in Blum, D., Seiler, M., Preventing Treaty Abuse, Linde, 2016.
[125] Van Weeghel, S., The Improper Use of Tax Treaties: with particular reference to the Netherlands and the United States, Kluwer, 1998, p. 258.

already includes goodwill and must therefore be adjusted to 60. While the tax administration in MS B claims to adjust the price by 20, hence Company B should have bought the licences for 100. Meaning, the taxable profit of Company A decreases by 20, while Company B can deduct 100 instead of deducting 80. This ends up in a situation of double non-taxation, since the taxable profit of both Companies decreases by 20.

5.2.3 Prevention by Tax Treaties

The OECD actively tries to prevent double taxation and double non-taxation[126], such as section B of Action 6 of the BEPS Project, which explicitly clarifies that tax treaties should not get used for double non-taxation[127]. The Action formulates that the main purpose of the existing provision is the prevention of double taxation[128] as well as the prevention of tax avoidance.[129]

Many states enter into tax treaty agreements such as Double Taxation Conventions (DTCs), in order to eliminate double taxation or double non-taxation. While not all cross-border situations are covered by the DTCs, states provide unilateral measures.[130] However, OECD MC provides guidelines for the contracting states on what a DTC should include, having an impact on tax treaties between MS, between MS and non-MS, as well as between non-MS.[131]

According to Kofler, economic double taxation is generally not addressed by tax treaties, and leaves the choice to prevent it, with either an exemption method or a credit method, within the competence of the contracting states of

[126] Molina, F. J., DTCs and Double Non-Taxation in Blum, D., Seiler, M., Preventing Treaty Abuse, Linde, 2016.
[127] OECD/G20, BEPS Project, Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances.
[128] OECD/G20, BEPS Project, Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, para. 69.
[129] OECD/G20, BEPS Project, Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, para. 72.
[130] Lang, M., Introduction to the Law of Double Taxation Conventions, IBFD 2013, Ch. 1.3.
[131] Vogel, K., Rust, A., Double Taxation Convention, Wolters Kluwer, 2015, p.3.

the DTCs. Meaning that it if and how economic double taxation should be removed, depends on domestic policy choices.[132] Nevertheless, Chapter V of the OECD MC provides methods for the elimination of juridical double taxation, after which Art. 23A OECD MC deals with the exemption method, where foreign income gets exempt from domestic taxation[133], and Art. 23B OECD MC with the credit method, allowing a credit for foreign taxes[134].

However, the application of DTCs can produce both, double taxation and double non-taxation, in an extent that would not have happened if the DTC would have had different rules.[135] Hence, a DTC does not completely eliminate the risk of double taxation nor double non-taxation.

Analysing the situation again, the provided examples of the second subsection discusses two MS, one relying on the TPG 2017 and one on the TCJA. While the TCJA constitutes a tax reform, tax administrations do not have much scope of interpreting the treatment of goodwill and ongoing concern value, while tax administrations applying the TPG 2017 have no clear instructions. Meaning, even if the DTC relying on the OECD MC provide rules to eliminate double taxation or double non-taxation, the treatment of goodwill and ongoing concern value remains uncertain for the contracting state applying the TPG 2017. Hence, even if that problem wants to get tackled by the OECD through e.g. the BEPS Project, as soon as states come up with significant changes of the guidelines, i.e. adopting the guidelines and making them clearer such as done by the U.S., this leads to difficulties for associated MNEs applying the different legal sources.

[132] Kofler, G., Indirect Credit versus Exemption: Double Taxation Relief for Intercompany Distributors, Bulletin for International Taxation, IBFD, 2012.
[133] OECD Model Convention, 2017, Art. 23A.
[134] OECD Model Convention, 2017, Art. 23B.
[135] Molina, F. J., DTCs and Double Non-Taxation in Blum, D., Seiler, M., Preventing Treaty Abuse, Linde, 2016.

6 Conclusion

Associated enterprises, where one MNE relies on the TPG 2017 and the other one on the TCJA, runs the risk of double taxation or double non-taxation, due to the inconsistency regarding the definition of intangibles of the discussed legal sources. Since a lower value of intangibles seems reasonable for most MNEs operating according to the TPG 2017, the TCJA turned that thought in the U.S. upside down, by granting a possible tax benefit for a higher valuation of intangibles, and also giving less space when defining an intangible. Hence, a proper planning of TP got more relevant, as well as a precise documentation.[136]

The given arguments from above show that the definition of intangibles in a TP context could be rethought from the OECD in its Guidelines, by revising the definition with a precise treatment of goodwill and ongoing concern value.

The thesis provided the reader an outline of the importance of a plain and proper definition of intangibles in a TP context. It can be concluded that legal sources should have clear instructions according to intangibles, to prevent the risk of double taxation or double non-taxation, and to provide certainty for tax administrations and taxpayers.

Since the thesis exclusively discussed the definitions of intangibles within a TP context, a further research suggestion can be the analysis of the different definitions for legal, accounting, and TP purposes, since this provides uncertainty for tax administrations and taxpayers as well.

Furthermore, an indirect link to EU law can be established, and a discussion about the question if the different definitions of intangibles in a TP context within the TPG 2017 and the TCJA constitute state aid, can be analysed.

Another suggestion for further research can be to take a deeper look into the U.S. Amazon case and discussing a possible influence on the EU Amazon

[136] Valentiam Group, The impact of U.S. Tax Reform On Transfer Pricing Planning & Compiance, 2019, https://www.valentiam.com/newsandinsights/impact-of-us-tax-reform-on-transfer-pricing.

case, since they do have similarities. The EU Amazon case was first decided in 2017 by the European Commission[137] and is now in progress by The Court of Justice of the European Union (the CJEU)[138]. Looking at the action brought to the CJEU, the Commission's TP calculation, for specific intangibles of the key issue at stake, "would lead to an outcome that deviates clearly from the arm's-length principle."[139] The fifth plea of law deals with the incompatibility of the principle of legal certainty by demanding a recovery of the aid, considering Luxembourg's good faith when calculating TP "[…] and the fact that the new transfer pricing approach applied by the Commission in the contested decision could not have been foreseen."[140]

[137] Commission Decision of 4 October 2017 on State Aid SA.38944 (2014/C) (ex 2014/NN) implemented by Luxembourg to Amazon.

[138] Action brought on 14 December 2017 - Luxembourg v. Commission, T-816/17, Official Journal of the European Union, 2018/C 072/49, The date of announcement of the case is not published yet.

[139] Action brought on 14 December 2017, Luxembourg v. Commission, T-816/17, first plea in law, third part.

[140] Action brought on 14 December 2017, Luxembourg v. Commission, T-816/17, fifth plea in law.

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