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# Transfer Pricing: Intangible Property, Tangible Profits

Written by



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## PREFACE

**Transfer Pricing: Intangible Property, Tangible Profits** is a white paper published by ALM Legal Intelligence. ALM gathered data, conducted interviews and administered the online survey. Erik Sherman wrote the report. Matthew J. Smith was the report editor. We would like to thank all those who participated in the survey and agreed to be interviewed for this report.

- September 2014

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## TABLE OF CONTENTS

Foreword .....	5
Executive Summary .....	6
About the Survey.....	8
Intangibles and the Business of Transfer Pricing.....	9
Tax Planning for Success .....	11
Case Study: A .....	14
Making Transfer Pricing Work.....	15
Navigating Regulatory Developments .....	19
Case Study: B .....	21
Conclusion .....	23
Appendix: Survey Results .....	24
Edgeworth Transfer Pricing Invite .....	30
Edgeworth Taxation (Transfer Pricing) Firm Side Survey.....	31
Edgeworth Taxation (Transfer Pricing) Company Side Survey.....	38

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## FOREWORD

**W**ITH THE ISSUANCE OF THE ORGANISATION FOR ECONOMIC CO-OPERATION and Development's (OECD's) *Action Plan on Base Erosion and Profit Shifting* (BEPS) in July 2013 and the *Revised Discussion Draft on Transfer Pricing Aspects of Intangibles* 11 days later, it was clear that tax authorities were going to be taking a hard look at transfer pricing for intangibles. Practitioners took this to heart, with public comment on the latter document exceeding 1,000 pages and many comments noting with some urgency that they viewed some of the guidance as inconsistent with the arm's length principles that the OECD espoused. For example, there was substantial controversy over the OECD's view that an entity that owned and financed the development of an intangible was not necessarily entitled to any material portion of the associated return. Rather, the OECD's draft guidance suggested that an entity that owns and finances that development may only claim a material return if it also performs (or directly supervises) the development activities.

These developments were the motivation for this survey, which sought to gauge the state of practitioners' current transfer pricing practices for intangibles and their practical responses to the draft guidance. In particular, what intangibles are important to companies and how are they identified? What are current tax planning practices, and what are the drivers of the chosen transactional structures? What transfer pricing methods are used, and how aggressive are the tax positions taken? And, finally, how have recent regulatory developments affected planning and execution of transfer pricing for intangibles? Given the prominence of the issue, we also polled practitioners on their practical experience with how independent parties allocate ownership, financing, and development activities in arm's length licensing transactions.

On September 16, 2014, the OECD issued revisions to Chapter VI of the transfer pricing guidelines, "Special Considerations for Intangibles." Some of the guidance issued is final, but other important areas remain a work in progress. In particular, there will be additional guidance expected in September 2015 on risk, recharacterization of transactions, and hard to value intangibles. Thus, significant uncertainty remains, and the answers to the questions in this survey are likely to be relevant far into next year and beyond. We hope that these survey results illuminate key issues in transfer pricing for intangibles, and provide practical guidance on how peers are executing their transfer pricing strategies and responding to uncertainty.



## EXECUTIVE SUMMARY

**I**NTANGIBLE ASSETS ARE A SOURCE OF COMPETITIVE ADVANTAGES FOR MANY companies, whether it be through a patent for a new active compound in a pharmaceutical product or a novel business process for executing transactions. As these assets have become more important, tax authorities have become increasingly strident in their efforts to capture taxes on an appropriate share of the associated profits. In turn, multinational companies and their advisors have worked to structure transactions to keep more of these profits for shareholders.

This tension is one reason for the Organization for Economic Cooperation and Development's *Action Plan on Base Erosion and Profit Shifting* and subsequent associated releases. This and similar activities by tax authorities, legislative bodies, and other organizations have created increased uncertainty around transactional structures and pricing for transfers of intangibles. As a result, in-house and law firm tax groups must carefully monitor and assess new developments while at the same time must executing rigorous policies under existing requirements.

The main findings of the survey include the following:

**1 LAW FIRMS WORK WITH CLIENTS THAT OWN A VARIETY OF INTANGIBLES**, including patents, trademarks, business methods, and production processes, and nearly two-thirds of those clients are also active in licensing technologies.

**2 SIXTY-SIX PERCENT OF LAW FIRMS WORK** with at least some of their tax clients to identify and document all relevant intangible assets for transfer pricing.

**3 ACCORDING TO LAW FIRMS, 23 PERCENT HAD CLIENTS** with effective tax rates between 31 percent and 35 percent, and half had clients with tax rates between 21 percent and 30 percent.

**4 ALMOST THREE-FOURTHS (73 PERCENT) OF LAW FIRMS** recommend that their clients align intangible transactional arrangements around business operations, with 75 percent also suggesting the client locate managerial functions with the owner of the intangibles.

**5 WHILE 52 PERCENT OF FIRMS SUGGEST THAT CLIENTS WAIT FOR FURTHER DEVELOPMENTS** before shifting substantive operations around intangibles in response to recent OECD recommendations, 76 percent of companies reported themselves as already doing so. Nevertheless, only 3 percent of law firm respondents say they see managerial functions and ownership together “most of the time” in agreements between independent parties.

**6 NO LAW FIRMS OR COMPANIES CHARACTERIZED THEIR TAX POSITIONS AS “VERY AGGRESSIVE.”** Still, 40 percent of law firms expect anywhere from 26 percent to 75 percent of their tax clients to see a significant tax adjustment on intangible asset transfer pricing over the next three to five years. But 59 percent of law firms expect less than a quarter of their clients to see a significant tax adjustment in that time frame. Among companies, 67 percent were somewhat or very concerned about tax adjustments.

**7 ACCORDING TO LAW FIRMS, THREE-QUARTERS OF CLIENTS** used the Comparable Uncontrolled Transactions (“CUT”) method with discounted cash flow analysis as the method for pricing transfers of intangibles.

### About the Survey

Two surveys were created and administered by ALM Legal Intelligence and commissioned by Edgeworth Economics. One survey was sent to companies, the other survey was sent directly to law firms. The purpose of the surveys was to understand trends for how Transfer Pricing Groups, International Tax Groups, Tax Directors and CFOs are managing and valuing intangible assets for transfer pricing purposes. An invitation to participate in an online questionnaire hosted by ALM Legal Intelligence (the research arm of ALM Media) was sent on May 9th and May 16th, 2014, respectively. A cover letter explained the objectives of the survey and encouraged member participation (see the Appendix for copies of the questionnaires and the invitations). E-mail reminders were sent by ALM Legal Intelligence to all non-respondents in May, June, and July of 2014.

#### A WORD OF CAUTION:

- The survey results are based on a small sample of those involved with Transfer Pricing, and may be different from the results that would have been obtained if all those involved with Transfer Pricing had responded.
- Results based on a small number of respondents (count) may not be strongly representative of a particular area, and judgments based on small samples should be made with caution.

## INTANGIBLES AND THE BUSINESS OF TRANSFER PRICING

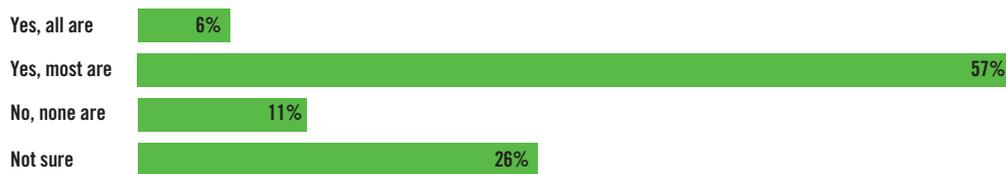
**INTANGIBLE ASSETS PLAY A KEY ROLE IN BUSINESS ACTIVITIES AND PROVIDE** substantial value for many firms. In the ALM Legal Intelligence survey of law firms and companies, law firm respondents identified multiple types of intangibles utilized by clients, each of which could have specific value.

**What types of intangible assets do your clients most frequently own and use? Please check all that apply.**



Not only do these clients own and use these intangibles, but most are also actively engaged in the marketplace for technologies. Specifically, 63 percent of law firm respondents report that most or all of their clients are engaged in licensing in or licensing out technologies.

**Are your clients with intangible assets active in licensing in or licensing out technologies?**



To the extent there are intercompany transactions involving owned intangibles, tax authorities require that multinational companies determine, document, and report appropriate transfer prices. Law firms play an important role in this process, as 66 percent work with at least some of their clients to identify and document relevant intangibles for transfer pricing.

**Does your law firm work with clients to identify and document all relevant intangible assets for transfer pricing?**

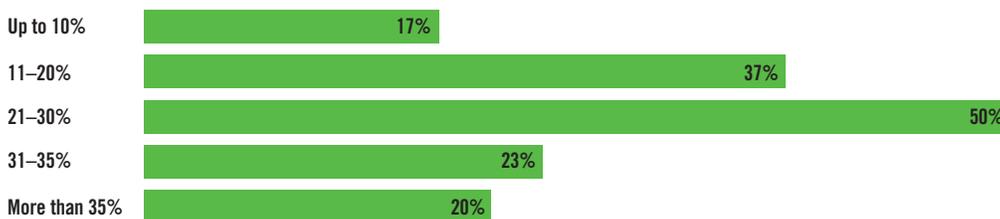


Identifying relevant intangibles is only the beginning. Given the mobility of some intangibles, companies may then decide the best location for them from both a business and a tax standpoint. “Companies are seeing the benefits of having the value of their intangibles grow in jurisdictions where intangibles are treated favorably,” said Martin Hamilton, a partner in the tax department at Proskauer Rose. “The complex structuring related to that belies a fairly simple goal, which is ensuring that the IP is not taxed at high rates unnecessarily.” Achieving these benefits in the context of practical business considerations requires careful tax planning.

## TAX PLANNING FOR SUCCESS

**C**ORPORATE TAX PLANNING STRATEGIES HAVE BEEN A PERIODIC FAVORITE target of the media. One reason is the growing number of companies that shift the location of intangible assets to low tax rate jurisdictions. However, effective tax rates vary substantially, indicating that the issue is more complex than a shifting of intangibles to tax haven, as is sometimes supposed. Specifically, the results of the ALM Legal Intelligence survey indicate that effective tax rates of law firms’ clients most commonly range from 11 percent to 30 percent, with half between 21 percent and 30 percent (the statutory rate in the U.S. is 35 percent).

**In what ranges do your clients’ overall effective tax rate tend to fall? Please select all that apply.**



There appear to be a number of reasons for these varying effective tax rates. First, while it is true that many firms are realizing tax savings through careful planning, others have eschewed these arrangements. “There are a lot of older mature U.S. companies that haven’t done anything, haven’t jumped on the bandwagon of moving the IP offshore,” said Sheila Geraghty, counsel at Reed Smith. And if they have already found mechanisms to control their tax obligations — Geraghty said that none of her clients paid more than 13 percent to 15 percent effective rates — the incentives may not be so strong.

Second, the transfer of intangible assets offshore can offer some advantages, but companies typically consider it in a larger context. “Transfer pricing or tax shouldn’t drive a business,” Geraghty said. “There are certain companies that have the facts that support the transfer of IP to another jurisdiction. “[But many] companies won’t change its business structure for transfer pricing for IP because it doesn’t make sense for the business model.”

This view is supported by the survey results. The vast majority (73 percent) of law firms recommend that their clients align transactional arrangements for intangibles around business operations versus structuring a business operation to meet tax needs. For such companies, tax planning is not driving the structure of the intercompany transaction—company-specific business realities dictate the structure.

**Which of the following statements best characterizes your preferred approach to transfer pricing for intangible assets?**



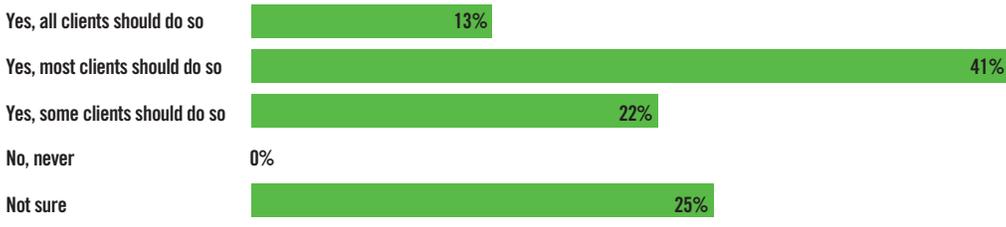
However, that's not to say all companies are unwilling to structure their businesses to better take advantage of tax strategies. Although the sample was small, 60 percent of the responding companies said they aligned business operations with transactional arrangements

**Which of the following statements best applies to your company:**



In either case, companies tend to do more than create empty holding companies for intangibles. For example, 76 percent of companies polled located functions associated with managerial control of the development, use, and protection of intangibles with the entity that legally owns them. Law firms agree.

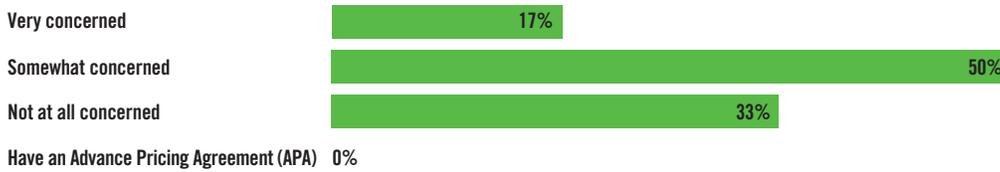
**Do you currently recommend that your clients locate functions associated with managerial control of the development/use/protection of intangibles with the entity that legally owns and funds the development/use/protection?**



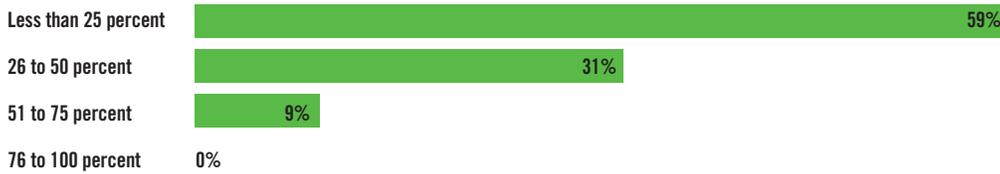
As you can also see, three-quarters of firms suggested that at least some of their clients locate managerial control with the entity that legally owns the assets. “The more substance you can give to a tax planning transaction, the better,” Robert Cudd, senior partner at Polsinelli said. The concern is that tax structures that lack substance will be subject to substantial adjustments. Sixty-seven percent of companies were still at least somewhat concerned about the possibility of a tax adjustment, while law firm advisors appear to be somewhat less concerned about substantial adjustments.

**How concerned is your department about the possibility of a tax adjustment on transfer pricing for intangible assets over the next 3–5 years?**

Note: An APA is an agreement with the IRS on the transfer price for a transaction(s).



**What percentage of your clients do you expect to realize a significant tax adjustment on transfer pricing for intangible assets over the next 3–5 years?**



#### CASE STUDY A:

### Why Companies Move Intangibles

Trying to equate an interest in transfer pricing on intangible assets to a specific range of financial benefits is a mistake. Companies have many different reasons and expected benefits.

“I have seen these strategies produce effective tax rate improvements in the double digits,” said Proskauer Rose Partner Martin Hamilton. “If a company has an effective tax rate of 35 percent, I have seen people do the more aggressive version of this where they lower their tax rate into the low 20s or even high teens. But I have even seen people willing to do this for as little as a 3 percent shift, from 34 to 31 percent. It’s a big range of results that companies that do this are looking for. I think it underlies the fact that there are a number of reasons why people choose particular times to do it.”

“The big percentage moves arise for companies that have discovered that all of their revenue growth is outside of their historic high tax main jurisdictions,” Hamilton said. “That’s just not where their growth is. A transfer pricing strategy to move IP off shore where you still have all of your other income subject to tax in an old jurisdiction is not going to produce much bang for the buck.”

“The attention particularly in the last couple of years has been extremely broad based,” he said. “It’s moved beyond the traditional areas of patents and specific technologies into business processes, sales methods, specific sales materials. Companies have come to realize how broad the opportunities are.

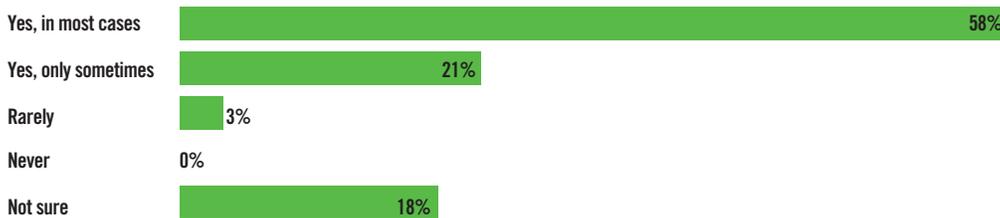
“A lot of attention given to companies shifting IP around, but a more important story from a global competitiveness perspective is new intellectual property will arise in places that not only ensure short-term tax benefits, but long-term tax benefits,” Hamilton said. “Increased globalization has made it much more palatable for companies to move large substantive portions of their operations to other countries in a way in which people might have referred to them as ‘paper strategies.’ We’re past that. The current policy environment and the ability to move materials around, people are doing big pieces of their R&D in other jurisdictions. I would say transfer pricing is inextricably linked to national competition for direct investment in R&D.”

## MAKING TRANSFER PRICING WORK

**T**AX PLANNING IS IMPORTANT, BUT SO IS EXECUTION, AND COMPANIES must execute plans in a way that works for their business. What makes sense in transfer pricing also goes well beyond media stereotypes of individual tactics like inversions (when a U.S.-based company merges with a non-U.S. entity with the intention of shifting its headquarters to the foreign location that has a lower corporate tax rate). “Generally, inversions have nothing to do with U.S. profits,” said Cudd. “We’re talking about taxation on foreign profits. A U.S. corporation does not want to pay 35 or 40 percent of tax on profits derived in China when every other country in the world charges 25 percent.” There are some ways to use inversions to lower US taxes by making a loan to the US entity and they can deduct interest payments, but this is not the driving force, Cudd said.

Because the effects of taxes and tax planning stretch across geographic boundaries and operational functions, such planning is often conducted in conjunction with multiple departments.

### Do you suggest that your clients engage with other departments when formulating transfer pricing arrangements or documentation?



Fifty-eight percent of firms said that they advise clients “in most cases” to engage with other departments. All of the responding companies said that their in-house tax groups coordinate with other departments when formulating plans.

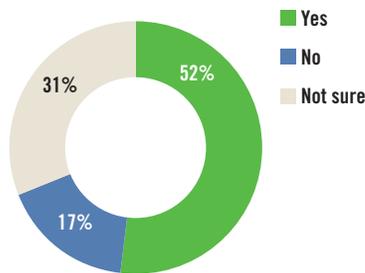
Clearly, tax and corporate strategy and planning are thought to benefit from collaboration. A corporate vice-president of tax at a chemical company who wanted to remain anonymous gave an example of an agricultural firm he worked at in the past. “We set up a company in a perceived tax haven and sent a group of engineers there in the late 1980s,” he said. “The company essentially began to develop different technologies/processes. We sold them the rights to certain products that might be long in the tooth. We told to them hire people and see if there’s a better way to make this mousetrap and license it back to us.”

As the executive explained, the movement of IP ownership overseas should be a gradual process. “We started with licensing one or two products,” he said. “Pretty soon you have all the technology owned by the overseas company. By 2001, that company probably made more than half of its income offshore, but had more than 70 percent of its sales in North America.”

Countries such as Ireland, Singapore, and other parts of Asia have become popular destinations for intangibles, but low tax rates are not enough. As a number of participants mentioned, some requirements are a highly educated populace and strong English skills. “The CEO and CFO need to be able to speak with the head of research and talk to people on the ground and be confident that the university education is comparable,” said a law firm attorney who asked not to be identified.

Financial disclosure requirements also play a role in companies’ decisions about how to structure transactions—and how aggressively they will pursue a lower effective tax rate.

**Do you or your clients typically take this FASB requirement into account when formulating your tax planning and/or tax positions?**



Just over half — 52 percent — of law firms reported that their clients typically took FIN 48, a rule of the Financial Accounting Standards Board that requires companies to disclose uncertain tax positions, into account when formulating tax plans. None of the firms considered their tax positions for intangibles to be very aggressive, perhaps because of the FIN 48 requirements.

“Most of the people we represent know they have to build in a profit motive and has to be some semblance of comparable pricing,” Cudd said. But that assumes that good comparable cases are available. In niche areas, finding similar transactions could be difficult. That is why working

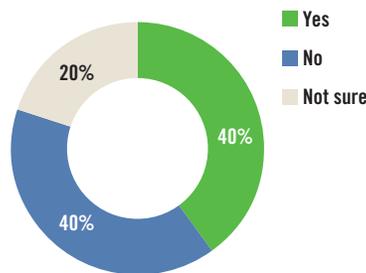
with a consulting firm as well as a law firm can be critical, because some have access to databases of transactions.

**How aggressive do you typically consider your recommendations regarding tax positions for intangibles?**



Forty percent of companies responding said that they took FIN 48 into account routinely, while none would take very aggressive tax positions.

### Does this FASB requirement affect your tax planning and/or tax positions?



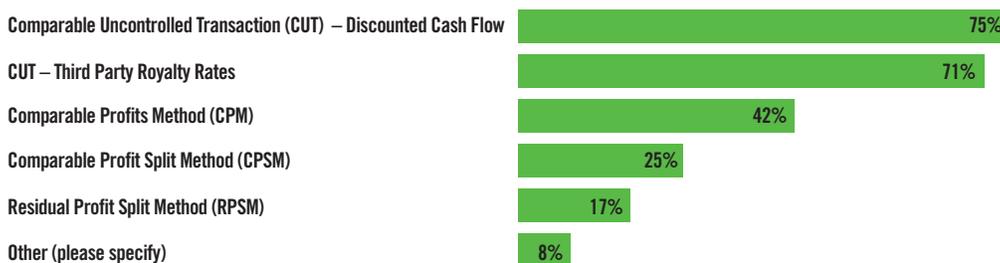
### How aggressive do you consider your tax positions for intangibles?



Companies also benefit from working with law firms and consultants to ensure defensible application of the arm’s length standard. In transfer pricing, you are trying to use economic principles to apply the arm’s length standard. “But there’s a fair amount of qualitative analysis,” said the anonymous vice-president. Each government has a different prism and sees things transfer pricing and what drives it differently. That’s where a lot of the friction is.”

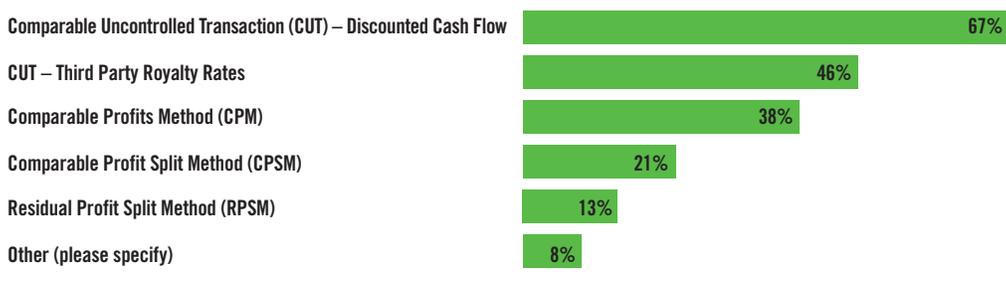
For example, the choice of methods to use in valuing intangible assets depends on an assessment of the type, amount, and quality of the data available. Survey respondents report using a variety of methods to value transfers of intangibles.

### What techniques do your clients most often use to value intangible assets for tax purposes?



The Comparable Uncontrolled Transaction (“CUT”) method emerges as the preferred method. In particular, the CUT method using discounted cash flow analysis on comparable uncontrolled transactions is used at 75 percent of clients, according to firms, with the CUT method based on third-party royalty rates close behind at 71 percent. Indeed, the CUT method using discounted cash flow is by far the most often recommended by law firms.

**What techniques do you most often recommend to value intangible assets for tax purposes?**



Interestingly, the Comparable Profits Method, which is often applied by tax authorities, is recommended and used much less often.

## NAVIGATING REGULATORY DEVELOPMENTS

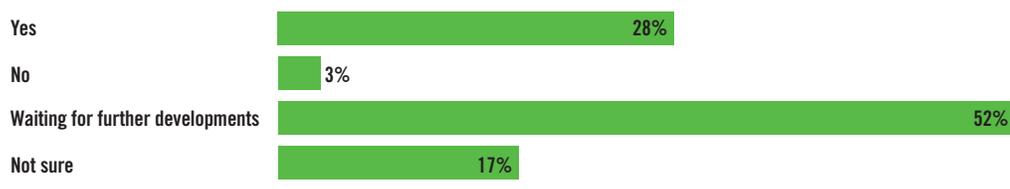
**R**ECENT DEVELOPMENTS FROM THE OECD AND OTHER FRONTS HAVE PUT significant pressure on companies to carefully consider their transfer pricing arrangements. The motivation for these actions is a concern about the potential loss of tax receipts if activities in a given jurisdiction are not properly compensated.

“Switzerland has always created tax structures,” Geraghty said. “The Dutch have always done it and Ireland is doing it. People see all this income shifting around the world and not seeing a lot of changes in the business operations of the companies. People are concerned because money is coming out of the tax coffers. They’re all focusing on how they can reduce the shift of income from one jurisdiction to another.”

The OECD’s recent work on *Action Plan on Base Erosion and Profit Shifting* (BEPS), including last year’s *Revised Discussion Draft on Transfer Pricing Aspects of Intangibles*, underscores how seriously countries have taken the question. At a time of constrained budgets and in the face of continuing global economic uncertainty, national governments want to ensure they collect appropriate tax revenues. However, taxes are ultimately a zero-sum game, leading to the potential for conflicts among national tax authorities.

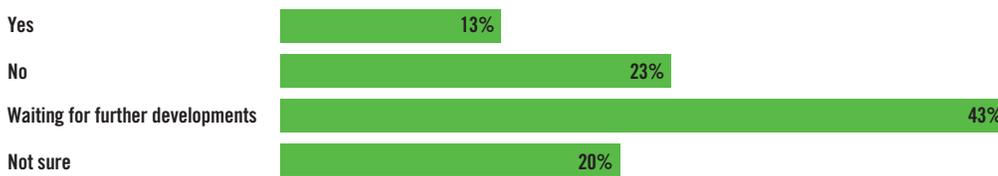
Given the OECD’s work on intangibles, how have U.S. companies reacted?

**Do you recommend your clients review or plan to review existing tax arrangements to shift “substance” (e.g., control of development, maintenance, and protection of the IP) in response to the OECD’s recent Base Erosion and Profit Shifting Action Plan and Revised Discussion Draft on Transfer Pricing Aspects of Intangibles?”**

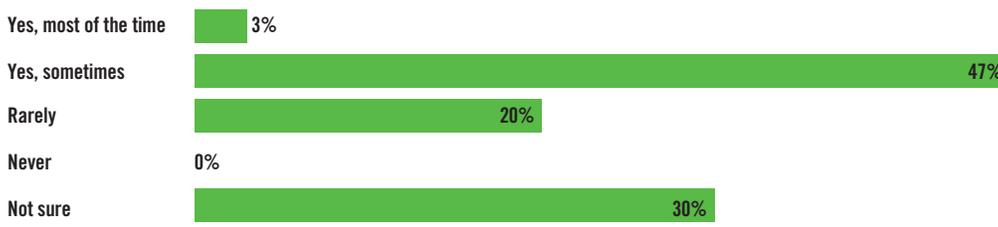


Although some law firms (28 percent) have advised their clients to review existing tax arrangements in response to BEPS, it appears that most law firms (52 percent) have advised clients to take a wait-and-see approach. The wait-and-see approach is even more pronounced with respect to the OECD’s proposed language on control of the development, use, and protection of intangibles, with 66 percent suggesting clients take no action. This may be a practical consideration, as the experience of law firms in licensing transactions between third parties is that legal ownership, oversight, and control do not always reside in the same entity, contrary to the OECD’s view.

**Has the OECD's focus on providing returns based on control of the development/use/protection of intangibles caused your law firm to make changes in your recommendations regarding clients' tax planning strategies?**



**In your experience in negotiating or reviewing licensing transactions between third parties, does legal ownership and funding always correspond to managerial oversight and control of the development/use/protection of the associated intangibles?**



Given the lack of certainty around the ultimate effects of the BEPS work, companies may look to alternatives that will help reduce that uncertainty and help avoid adjustments and penalties. “Twenty years ago, the fact that you could get penalized for transfer pricing was remote and unique,” said the chemical company vice-president. “Transfer pricing penalties have become a great source of revenue for many countries. You want to get to certainty.” Advance pricing agreements can provide a degree of certainty.

Advanced pricing agreements are an approach that can decide the ultimate outcome so a company won’t receive a penalty. “But you have to look through both sides of the prism and take off your American hat,” he said. “Now I’m the French government. How am I going to perceive the transaction and what do I want? You have two jurisdictions willing say almost anything to get you to allocate your profits to their jurisdiction.”

He mentions an example of an ongoing bilateral discussion with two governments. “I’m trying to determine going forward what the transfer price is of a product between two jurisdictions,” he said. “Both look at it differently and are convinced they are entitled to 90 percent of the profit. They’ll spend a couple of years negotiating, horse trading, and they’ll eventually come back to me with the answer.” And even after the discussion, things could remain at loggerheads. In the meantime I need to run a business and tell my shareholders the outcome of business operations. Not necessarily a process that makes either running your business or providing certainty to shareholders easy.

## CASE STUDY B:

### Addressing Complex Tax Issues

The vice-president of tax at a chemical company, who wishes to remain anonymous, said that his firm looked largely to business processes as the intangibles that drive transfer pricing. Most of the basic technology in the chemical industry has been available in the public domain for so long that it is not as valuable as the process know which optimizes processes. “Over the last fifty years, there has been very limited unique chemical technology,” he said. Processes and supply chain are what offer the biggest competitive advantage now.

“It’s a lot about process technology and logistical intangibles now,” he said. “Think about well-organized automated distribution networks, long-term agreements in place with shippers or logistics companies. These things have a lot of value. Having people who can reverse engineer a chemical process, or take steps out, reducing cost and adding significant value. These are examples of valuable know-how. Or for example, being able to take a chemical product and remove impurities from that chemical product might increase yield or make a more valuable product.”

But the opportunities to hold intangible property in a low-tax district and license it to other parts of a company (the world) could begin to see pressure from regulators. “What’s in front of us as a world in the next I’d say five to seven years, maybe even sooner, is a world that sees companies that have income that goes to nowhere (from a tax perspective). In some cases you hear about an entity in a low tax cost country that has three employees that are perceived earn their income playing tennis, not generating tens of millions of dollars of income. Eventually you’ll see governments imposing their will on other governments.” We are seeing it in the discussions of tax base erosion occurring all over the globe. Companies will be caught in the middle of the arm-twisting by the respective governments. Political pressure might overwhelm otherwise legal operating structures.

A big reason for the current pressure on transfer pricing is the need for tax revenue and a basic reality of politics. “A member of the United States Senate said to me in the mid-

1990s, ‘It’s often easier to tax people who don’t vote here.’ Taxing a foreign corporation might be easier than taxing your own local corporation. Certainly it’s easier than taxing your own local citizens.”

“This is where the tax code and government policy is twisted,” he said. “The United States provides generous incentives to do R&D in the US. There’s still a lot of technology being developed at universities. That will never change, so there’s a lot of R&D going on in the United States still,” even as more R&D moves overseas to countries like India and China where hiring scientific and engineering talent can be far cheaper.

Although his company likes to use advance pricing agreements, or APAs, the practicalities can be daunting. “They are still painful and take time,” he said. “But if you can get that process and get admitted into an APA program the outcome is generally good.” It is important to understand that Governments have limited resources to analyze and negotiate such deals. Your outcome is a function of the number of APAs the respective governments have, the horse trading they do and from time to time whether they have a bad relationship with my counterpart at the other country.”

Often shifting the ownership of intangible assets and using transfer pricing is less about tax considerations and more about other business aspects. “If you manufacture in the United States, we’ve gotten to a point in our regulatory framework that it can be cost prohibitive, whether it’s EPA rules or other regulatory rules,” he said. Companies might opt to manufacture elsewhere and transfer pricing is merely a factor in how to avoid adverse labor or environmental rules by running some aspects of the business in more business friendly countries.

His company also tries to be smart about moderation. “If you’re doing your job right, you don’t want to be a pig,” he said. “You want to get the return you need [but] pigs don’t do well in this world. If nobody ever writes anything about my tax department and I retire, and management thinks I’ve done a good job, I’m happy.”

The problem isn't only international in scope. Transfer pricing disputes over intellectual property have also become common in inter-state commerce, as Sutherland Asbill & Brennan Partner Leah Robinson explains. Companies can shop organizations and transfer pricing across state borders just as they can between countries. Except, there are additional complications. "Is the Delaware entity getting paid the correct amount by the New York entity [for example]?" Robinson said. "It's a huge issue in state tax."

"It's not just that each state has to tackle [transfer pricing] separately," Robinson said. "It's that each state has to decide whether to follow the federal approach, develop the resources to develop their own expertise, or go out to third parties. And each state has to decide whether transfer pricing is the best way to deal with each issue." If they do settle on transfer pricing, there comes the issue of what of "4 or 5 ways to deal with inappropriate pricing between affiliates" will be used.

Having one state subsidiary own the intangible property but drop the royalty payments can create an entirely different problem. "You know zero is not the right price," Robinson said. "Now states may [still] come in and make a transfer pricing adjustment." They might decide that some portion of revenue should be due to a licensing royalty. "A lot of companies have stopped paying intercompany royalty without unwinding the structure."

States also don't have the same experience and resources in dealing with transfer pricing that the IRS has. Some states have hired experts on contingency fees, which creates the potential for major conflict of interest.

But Robinson called the "overlay between state transfer pricing and New York's False Claims act" the "scariest aspect" of inter-state transfer pricing. Individuals can bring qui tam actions in New York for unpaid taxes, including allegations of improper transfer pricing between states. "Very recently a former employee of Vanguard brought a false claims act that largely focuses on the transfer pricing of inter-company services," she said. "He raises both federal and state assertions, allegedly evading more than \$1 billion in federal tax and \$20 million in New York tax. It's a perfect storm of bad tax policy."

## CONCLUSION

**A** S TAX AUTHORITIES CONTINUE THEIR EFFORTS TO APPROPRIATELY TAX transfers of intangibles, companies will need to continue to respond. These issues are complex, and companies are motivated not just by tax considerations, but primarily by corporate strategy and practical business realities. In this complex, dynamic environment, companies must work closely with legal and economic advisors to structure and price transactions appropriately. Successfully navigating these treacherous waters and thoughtfully balancing business and tax considerations can provide companies with a competitive advantage.

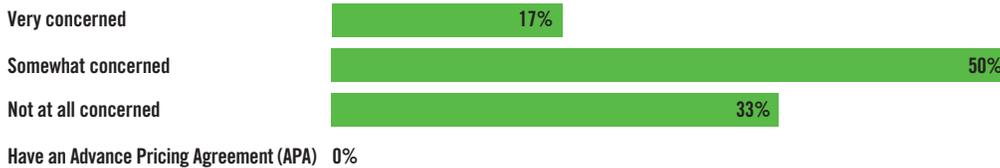
## APPENDIX: SURVEY RESULTS

### 1. Does your law firm work with clients to identify and document all relevant intangible assets for transfer pricing?

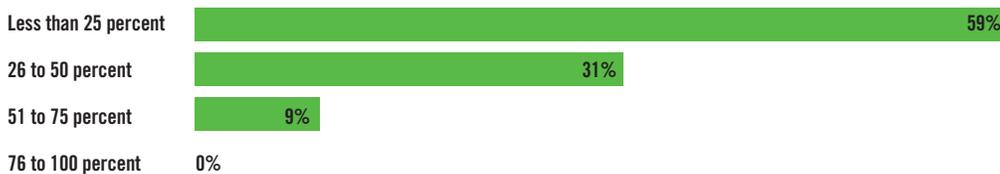


### 2. How concerned is your department about the possibility of a tax adjustment on transfer pricing for intangible assets over the next 3–5 years?

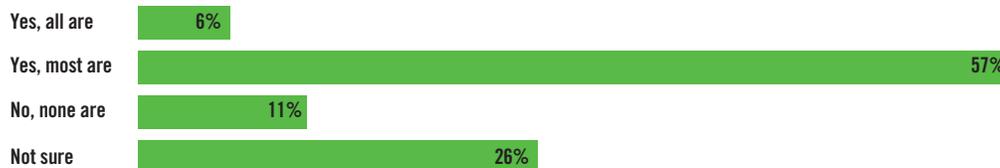
Note: An APA is an agreement with the IRS on the transfer price for a transaction(s).



### 3. What percentage of your clients do you expect to realize a significant tax adjustment on transfer pricing for intangible assets over the next 3–5 years?

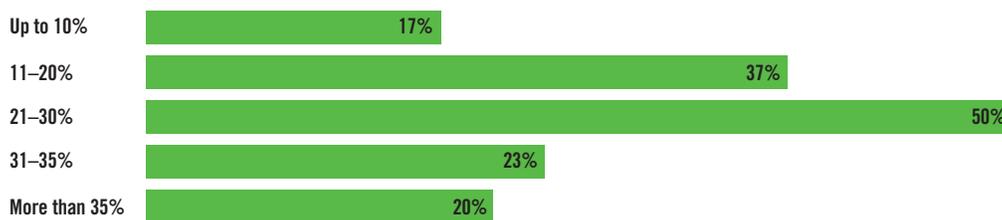


### 4. Are your clients with intangible assets active in licensing in or licensing out technologies?



## APPENDIX: SURVEY RESULTS

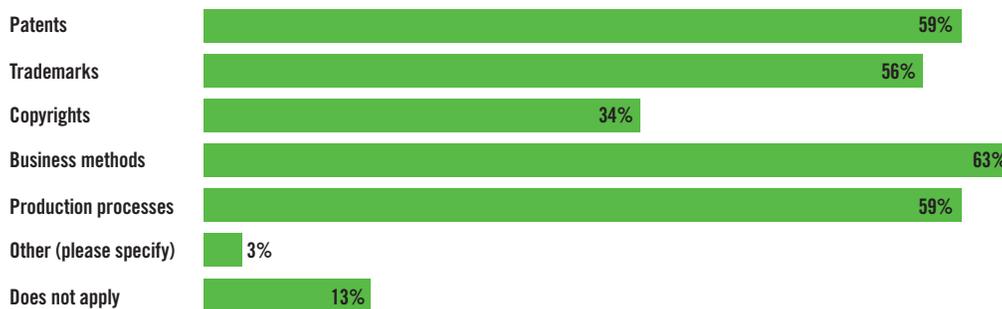
### 5. In what ranges do your clients' overall effective tax rate tend to fall? Please select all that apply.



### 6. What types of intangible assets do your clients most frequently own and use? Please check all that apply.



### 7. What types of intangible assets are at issue in most of your transfer pricing work on intangibles? Please check all that apply.



## APPENDIX: SURVEY RESULTS

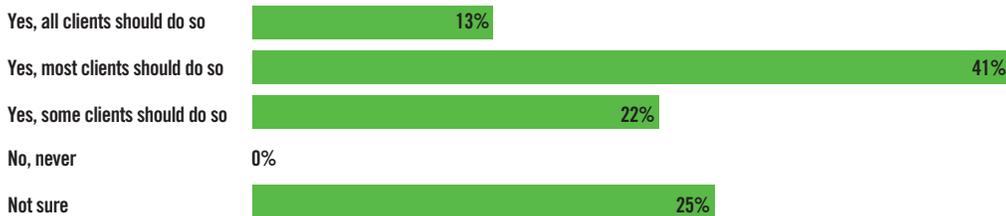
### 8. Which of the following statements best characterizes your preferred approach to transfer pricing for intangible assets?



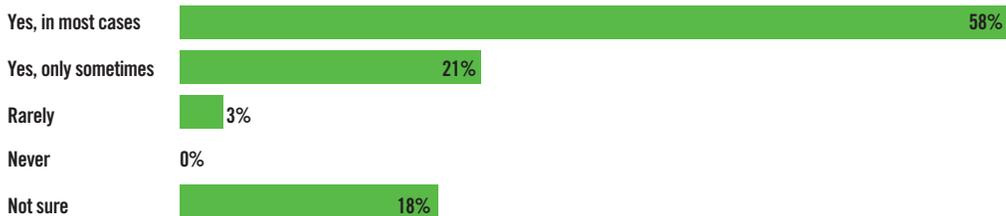
### 9. Which of the following statements best applies to your company:



### 10. Do you currently recommend that your clients locate functions associated with managerial control of the development/use/protection of intangibles with the entity that legally owns and funds the development/use/protection?

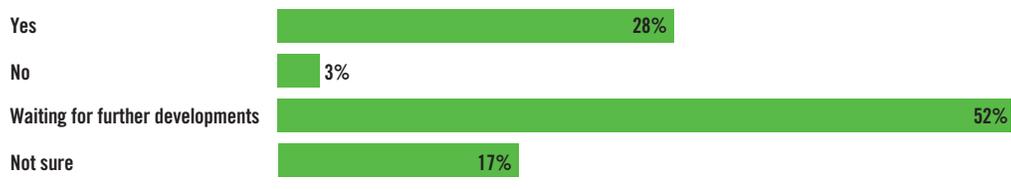


### 11. Do you suggest that your clients engage with other departments when formulating transfer pricing arrangements or documentation?

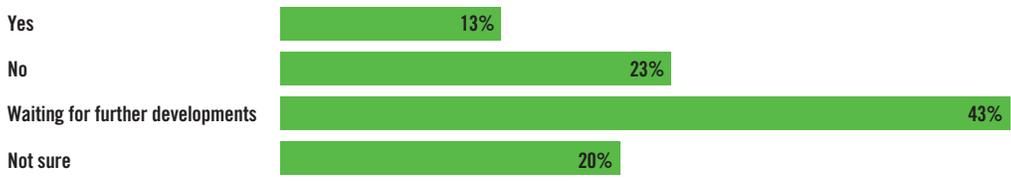


**APPENDIX: SURVEY RESULTS**

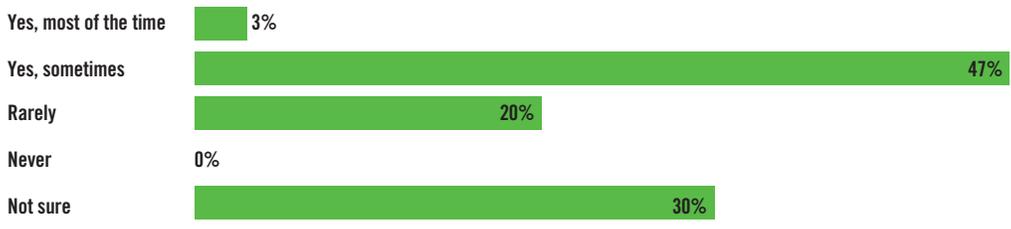
12. Do you recommend your clients review or plan to review existing tax arrangements to shift “substance” (e.g., control of development, maintenance, and protection of the IP) in response to the OECD’s recent Base Erosion and Profit Shifting Action Plan and Revised Discussion Draft on Transfer Pricing Aspects of Intangibles?”



13. Has the OECD’s focus on providing returns based on control of the development/use/protection of intangibles caused your law firm to make changes in your recommendations regarding clients’ tax planning strategies?

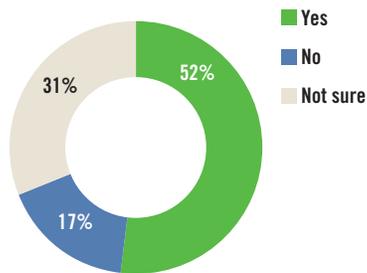


14. In your experience in negotiating or reviewing licensing transactions between third parties, does legal ownership and funding always correspond to managerial oversight and control of the development/use/protection of the associated intangibles?



**APPENDIX: SURVEY RESULTS**

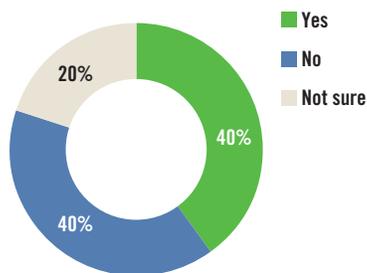
15. Do you or your clients typically take this FASB requirement into account when formulating your tax planning and/or tax positions?



16. How aggressive do you typically consider your recommendations regarding tax positions for intangibles?



17. Does this FASB requirement affect your tax planning and/or tax positions?

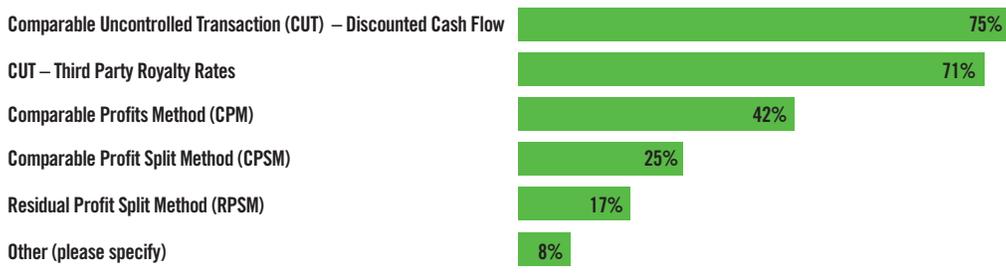


18. How aggressive do you consider your tax positions for intangibles?

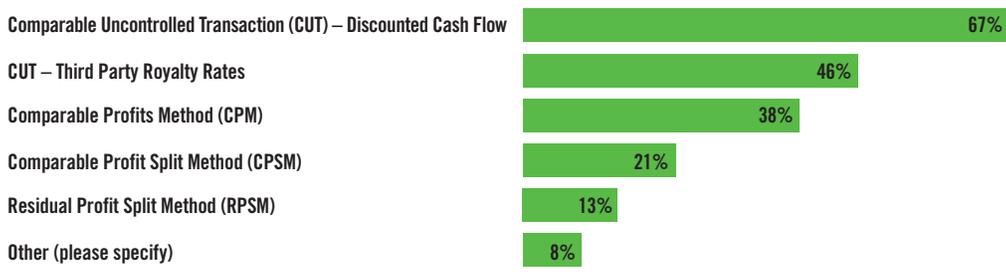


## APPENDIX: SURVEY RESULTS

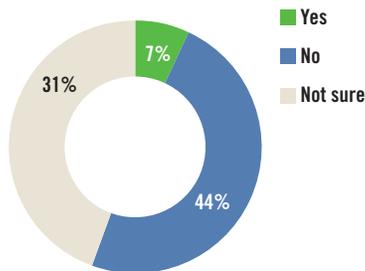
### 19. What techniques do your clients most often use to value intangible assets for tax purposes?



### 20. What techniques do you most often recommend to value intangible assets for tax purposes?



### 21. Have you changed your recommendations regarding valuation methods in response to the OECD's recent Base Erosion and Profit Shifting Action Plan and Revised Discussion Draft on Transfer Pricing Aspects of Intangibles?



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