DETERMINING IP AND OWNERSHIP HEREOF FOR TP PURPOSES

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ITR WORLD TAX
TOP TIER FIRM
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SETTING THE SCENE

- Outline
  - Selected topics.
  - Merely scracting the surface within such a vast and complex topic.
  - Terminology – intellectual property/intangible assets.
- The importance of IP in business and tax law is undeniable.
  - BEPS project – several advanced tax planning tecniques involved IP.
  - Tax incentives, including R&D super deductions and patent/IP boxes etc.
  - Tendency: Tax authorities see IP as highly valuable and quite often use a broad notion of IP.
- Typical practical issues.
  - Centralization of IP and other business restructurings.
  - Mitigating exit taxation (profit potential).
  - Securing step up in value and amortization of IP.
  - Claiming local co-development and ownership of IP.
  - Valuation.
- Overall analytical topics
  - Determining IP – including the issue of mis-characterization.
  - IP Ownership – including the concept of economic ownership and relevance of DEMPE functions.

DETERMINING IP

DETERMINING IP

- Determining IP
  - The notion:
    - Potential difference in tax, TP, accounting and IP law

      - The transfer pricing context: OECD TPG (2022)
        - Ch. VI 6.6.: "[…] *the word "intangible" is intended to address something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances."*
        - Consider: Best practices, internal procedures, human capital, non-contractual relations to customers or suppliers, network effects, and DEMPE functions?
        - Goal of TPG: Align transfer pricing outcomes with value creation – IP is vulnerable to manipulation – moving away from formality based approach.

- Key considerations
  - Typically highly valuable – drives entrepreneur status and higher remuneration (once profitable otherwise losses borne).
  - Complexity and hard to value.
  - Interaction with corporate tax law, accounting etc. – sloppyness can be costly.
  - Delineating a right to use from ownership (royalties from disposal/acquisition) of IP.
  - Mischaracterized IP (embedded IP/royalites).

MIS-CHARACTERIZED IP

- Recent developments may indicate the beginning of a global trend towards mischaracterized and embedded royalties.
  - Cases in several jurisdictions.
  - EU ATAD CFC rules.

- Tax issues in a nutshell
  - Concept (broader than TP):
    - Taking the derivative IP related component into consideration in the proper characterization of certain cross border transactions.
  - Transfer pricing context:
    - IP related transactions which should be remunerated – typically higher remuneration for IP.
  - CFC Taxation: (BEPS Action 3 - Chapter 4).
    - Active income escapes CFC legislation – IP income is considered passive/mobile income.
      - *"For instance, income from IP could be embedded in income from sales and therefore treated as active sales income under the CFC rules of some countries."*
  - Withholding tax.
    - Sale of goods/services vs. royalty payments.

MIS-CHARACTERIZED IP

- Legal basis in tax law
  - No specific provisions regarding embedded royalties in domestic law or tax treaties.
  - The starting point must be that an inherent IP component in ordinary business transactions (sale of goods or services) should not be crystalized and taxed separately.
    - NB: Mixed contracts in OECD Model article 12 commentary?
  - Decided on the basis of ordinary legislation and principles of legal classification (domestic law and treaties).
    - Certain tax authorities claim the existence of a principle of decomposition (Australia, Spain, Israel, Denmark, India).
    - Inspiration from OECD TPG? (par. A.2. (6.13. – no relevance).
  - Generally applicable anti-avoidance rules (GAAR) as legal basis to deem embedded IP/royalties?

- The Transfer pricing context (OECD TPG C.1.3. and C.2.)
  - Determine if IP transfer has taken place or other IP transaction.
  - Deeming embedded IP/royalties on the basis of "delineation of actual transaction".
  - The price of a package contract should be disaggregated to confirm each element of the transaction.

PEPSICO DECISION - AUSTRALIA

Important decision from the Australian High Court (13. August 2025)

- Facts:
  - Pepsi group US entities (PepsiCo Inc. and Stokely-Van Camp, Inc. (SVC)).
  - Entered into Exclusive Bottling Agreements (EBA) with Schweppes Australia Pty. (SAPL) which is part of the Asahi group.
  - EBA:
    - SAPL should produce, bottle, sell and distribute finished soft drinks on the Australian market under the brands Pepsi, Gatorade or Mountain Dew.
    - EBA included a royalty free license for SAPL to use trademarks and other IP rights.
    - Sale from PepsiCo of concentrates to be used in the production as part of a secret process according to a recipe made available from PepsiCo.
- The ATO position – royalty payments should be deemed and subjected to Australian WHT.
  - Subject to AUS WHT for 2018 and 2019 (AUD 3.6M)..
  - Alternatively subject to the DPT (AUD 28.9 AUD).

PEPSICO DECISION - AUSTRALIA

- The final decision of the High Court 13. August 2025.
  - The majority (4-3) (GORDON, EDELMAN, STEWARD AND GLEESON JJ).
    - Not for nothing.
      - *147. In sum, the use of a local bottler such as SAPL was mutually beneficial for both PepsiCo and the bottler. SAPL was able to leverage the PepsiCo Group's innovation and marketing capabilities, and PepsiCo received the benefit of SAPL's local investment in bottling and distribution equipment and capabilities.*
    - No royalty and not the right party.
      - *158. The payments made were for concentrate and did not include any component which was a "royalty" for the use of the PepsiCo Intellectual Property.*
      - *And, in any event, the payments were received by PBS on its own account.*
    - Diverted profits tax clause not applicable (no tax benefit).
  - However, mind the minority reasoning on DPT.
    - DPT:
      - *110. If the royalty withholding tax provisions did not apply, the DPT provisions would apply. In these appeals, accordingly, as the royalty withholding tax provisions do not apply, the DPT provisions do apply.*

DETERMINING IP OWNERSHIP

A short guided tour of a few recent challenges within the IP space

CASE LAW EXAMPLES OF IP OWNERSHIP

Recognition of economic ownership - Cancellation of royalty agreement between DK sub and foreign parent company – (SKM 2020.30 LSR).

- Facts
  - Group activity: construction of diesel engines.
  - DK sub had contributed to the design and research of the specific model and carried out services for the licensees of the specific engine.
  - Foreign parent was registered owner of the design IP.
  - 50/50 split of concrete royalty income.
  - Following centralization the agreement was cancelled - compensating payment made as lump sum payment as NPV.

- Arguments
  - Challenged by the DTA claiming that the payment was too low and the economic ownership of the IP in fact belonged to DK sub.
  - In essence the cancellation was not a cancellation of a service agreement but a transfer of IP.
  - The group argued against the co-ownership to IP stating that the payment was remuneration for service-obligations.

- Ruling of Danish Tax Tribunal
  - Valuable IP has been transferred based on the documentation available.
  - ALP requires higher remuneration than NPV of service fees.
  - Taxation of IP transfer (based on estimates of future sales).

- Comment
  - Support existence of economic ownership concept in Danish tax law (although terminology not explicitly used).
  - Broad notion of IP and questionable legal basis to tax transferred asset.

CASE LAW EXAMPLES OF IP OWNERSHIP

DEMPE functions as determinative for IP ownership (Supreme Court decision dated 9. January 2025) – The Accenture case.

- Facts
  - Complex fact pattern – Only considering the royalty issue.
  - Accenture DK paid royalties of 7% of turnover to Accenture Global Services GmbH (AGS) (CH).
  - Use of Residual profit split method – where AGS as the owner of IP received the whole residual profit while Accenture DK only earned routine profits.
  - AGS was the legal owner og the brand etc. since an alleged transfer in 2001.
    - AGS employed 9-11 staff carrying out administrative and coordinating functions and not contributing with valuable functions etc. to the development of IP.
    - Local Accenture companies possessed the local IP in the form of clients, workforce, goodwill etc.
- Arguments
  - DTA challenged the royalty
  - Stating that Accenture DK co-created the IP and that AGS merely carried out invaluable contributions to the IP and that the alleged transfer was artificial. Upheld by the Eastern High Court.
- Supreme Court decision
  - AGS owns certain IP according to the license agreement, including brand, patents, process-tools.
  - AGS had been responsible since 2001 for and made decisions regarding the development of the Accenture groups' IP, had maintained the protection of the IP and carried the costs.
  - AGS handled and financed the overall marketing within the group.
  - Carried the cost of 11 FTE as well as significant costs from hiring of labor from other group companies.
    - In fact, close to DEMPE functions – pre DEMPE concept.
  - Based on this: No reason to reject AGS as the owner of the IP covered by the 2006 license agreement.
  - Since the DTA did not provide any convincing arguments, the agreed royalty was upheld.

CASE LAW EXAMPLES OF IP OWNERSHIP

IP transfers within project SPV's?

- Among the hottest topics within TP (globally?).
  - In particular renewable energy projects.
  - DTA has taken the standpoint that valuable IP (know how) has been transferred in the context of establishing project SPV's holding the assets abroad.
  - Valuation based on future estimated cash flows even before projects have been finalized.
  - Even cases where (tax exempt) capital gains on shares are reclassified into missing management fees for the selling parent entity.
  - Pending cases with significant economic value at risk.
  - Many do not dare to engage in this area – case law is awaited.
  - Best practice to emerge……. Searching middle ground.

Guidance from Mærsk Oil & Gas Case? (Supreme court decision dated 6. September 2023)

- DTA argued that know-how had been transferred to foreign subsidiaries (Quatar and Algeria) through the initial exploration activities carried out by parent company and subsequently transferred to local subsidiary when license was granted.
- Remunerations should have been paid through a future royalty or similar.
- Final supreme court decision does not clarify this as exploration activities are viewed in combination with other contributions such as performance guarantees – not possible to conclude if Supreme Court considers exploration to constitute IP.

Thank you for the attention!

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