

ALDER&SOUND

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The Finnish Transfer Pricing Firm of the Year in 2017, 2015 & 2011 | The European Tax Technology Firm of the Year in 2017 | The European Tax Innovator in 2013

Royalty Breakfast 2017: European vs Russian Approach

In cooperation with Forte Tax & Law | Wednesday October 11th, 2017 @ 9.00-12.00

Agenda | Wednesday October 11th 2017

Royalty Breakfast 2017: European vs Russian Approach

1. Opening words

Petteri Rapo | Managing Partner / A&S

2. Overview of key transfer pricing aspects related to intangibles

Henri Becker | Partner, Head of Transfer Pricing Services / A&S

3. The impact of OECD MLI on cross-border intra-group transactions

Henri Becker | Partner, Head of Transfer Pricing Services / A&S

4. Russian approach to beneficial ownership of royalties and other passive income

Anton Kabakov | Partner / Forte Tax & Law

5. Customs implications of paying royalties

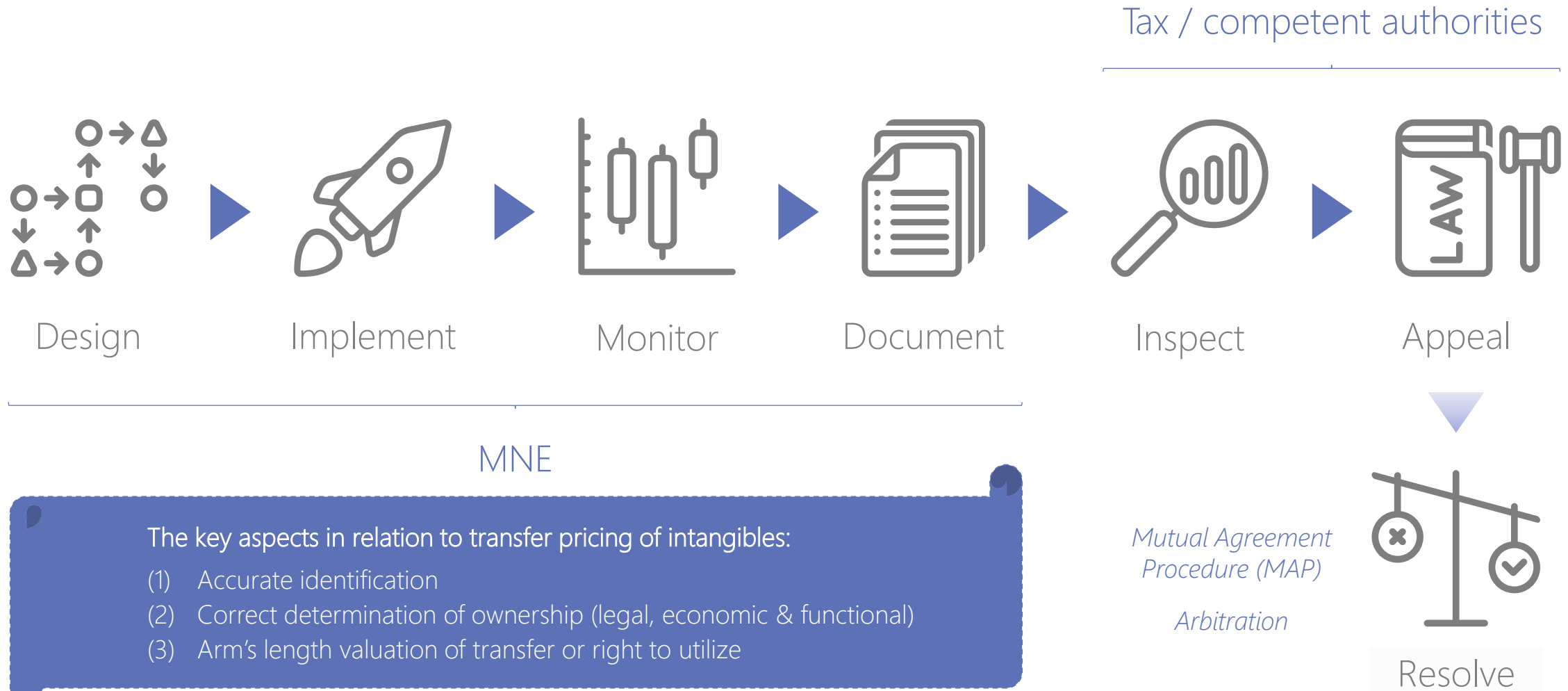
Anton Kabakov | Partner / Forte Tax & Law

Overview of key transfer pricing aspects related to intangibles

Henri Becker | Partner, Head of Transfer Pricing Services / A&S

Overview of the typical transfer pricing process

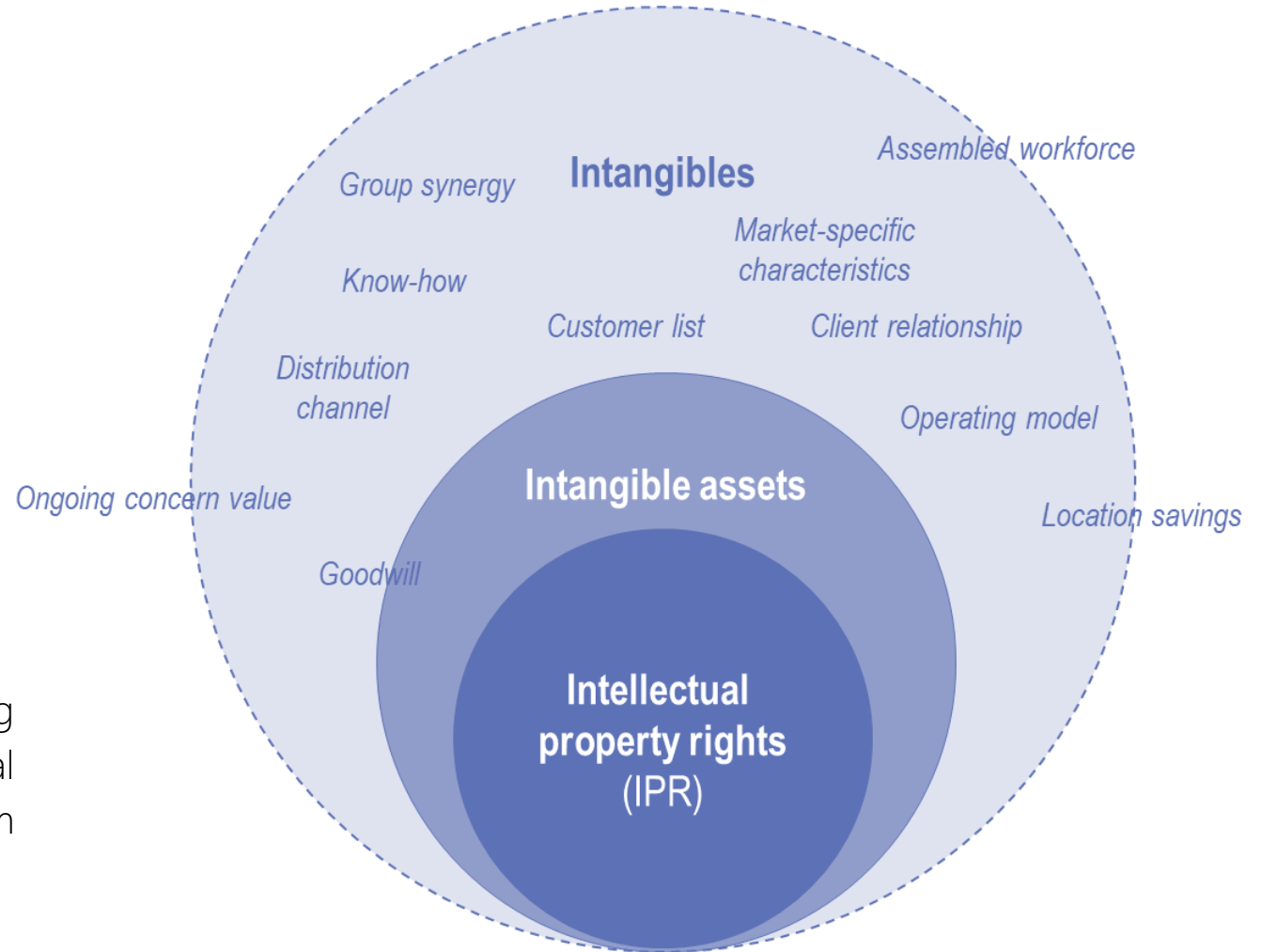
The different steps of the typical transfer pricing process aim at ensuring appropriate division of taxing power between sovereign states



Transfer pricing of intangibles - Identification

Expanding definition of intangibles in transfer pricing

- Updated definition of intangibles in Chapter VI (paragraph 6.6) of OECD Transfer Pricing Guidelines now contains a three-step test (*numbering here*):
 - [T]he word "intangible" is intended to address something which is not
 - i. a physical asset or a financial asset,
 - ii. which is capable of being owned or controlled for use in commercial activities, and
 - iii. whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.
- Under the revised text of the OECD Transfer Pricing Guidelines, an effort is made to steer away from the legal and accounting definitions of intangibles, as well as from specific categories.



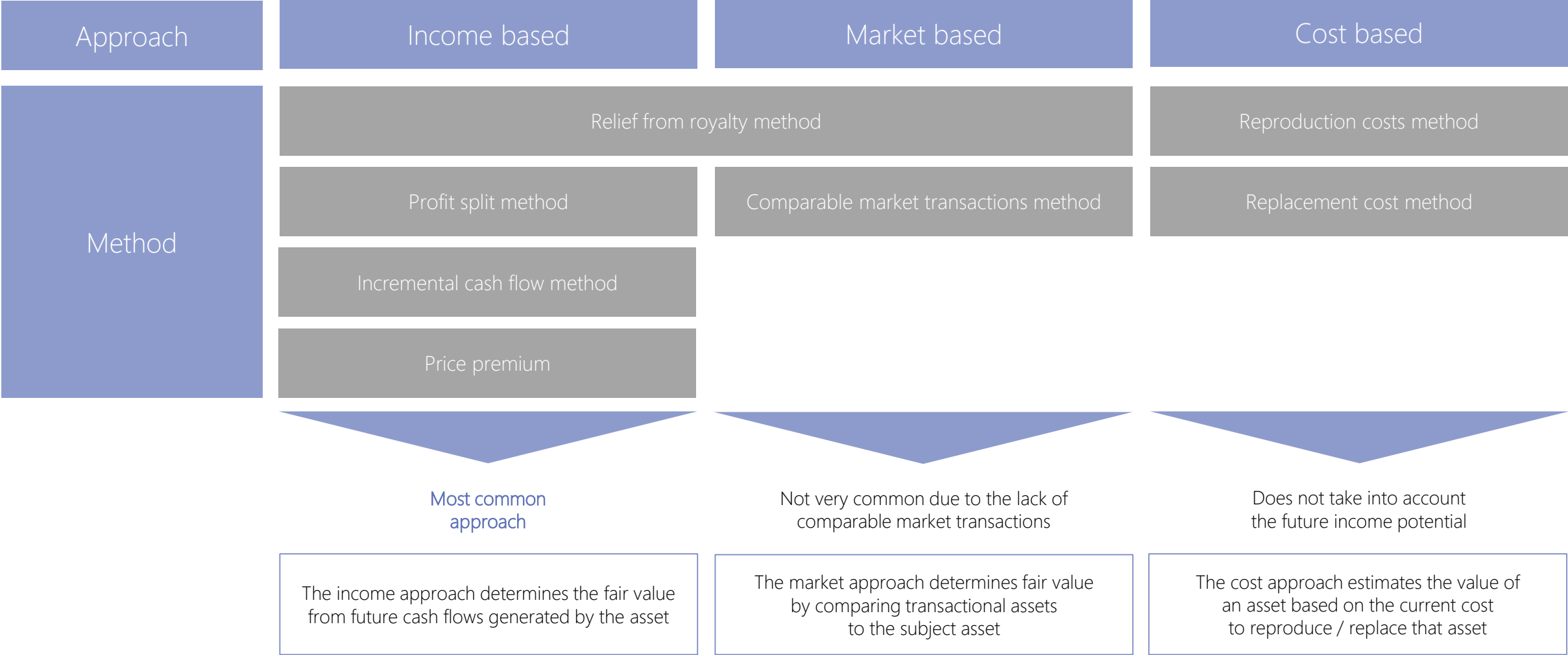
Transfer pricing of intangibles - Ownership

Section B of renewed Chapter VI provides guidance on allocation of economic profits earned through exploitation of intangibles

- Section B of renewed Chapter VI provides guidance on which of the entities in an MNE group should be entitled to retain the economic profits from intangibles.
 - The updated guidance (paragraphs 6.32 and 6.42) on ownership now states that :
 - Although the legal owner of an intangible may receive the proceeds from exploitation of the intangible, other members of the legal owner's MNE group may have performed functions, used assets, or assumed risks that are expected to contribute to the value of the intangible; and that
 - For transfer pricing purposes, legal ownership of intangibles, by itself, does not confer any right ultimately to retain returns derived by the MNE group from exploiting the intangible, even though such returns may initially accrue to the legal owner as a result of its legal or contractual right to exploit the intangible.
 - According to the guidance, the key functions with regard to intangibles are (DEMPE):
 - Development;
 - Enhancement;
 - Maintenance;
 - Protection; and
 - Exploitation of intangibles.
- **Three types of intangible ownership:** 1) Legal; 2) Economic; and 3) Functional (DEMPE)

Transfer pricing of intangibles - Valuation

Appropriate valuation analysis aims at ensuring arm's length compliance of the transaction involving intangibles (i.e. licensing / transfer)



Transfer pricing of intangibles - Service fee or license fee?

The border line between service fees and license fees is often unclear, especially with respect of IT charges

Service fee

- ▶ The basis for the fee is an identifiable activity (or series of activities) performed by the provider
- ▶ The value of benefit received is linked to the actual costs incurred by the provider in connection with performing the activities
- ▶ The legal and economic ownership of the benefit in question are usually not clearly defined or separable from each other

License fee

- ▶ The basis for the fee is a right to utilize certain know-how or other intangibles owned by the provider
- ▶ The value of benefit received is determined based on the income or profit estimated to be generated through the licensing right in question
- ▶ The legal and economic ownership of the benefit in question are usually clearly defined and separable from each other

The impact of OECD MLI on cross-border intra-group transactions

Henri Becker | Partner, Head of Transfer Pricing Services / A&S

OECD Multilateral Instrument (MLI)

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS

- ▶ On June 7 2017, over 70 Ministers and other high-level representatives participated in the signing ceremony of the OECD MLI. The MLI is still open for additional signatories.
- ▶ The MLI is intended to offer concrete solutions for governments to close the gaps in existing international tax rules by transposing results from the OECD/G20 BEPS Project into bilateral tax treaties worldwide.
- ▶ The MLI **modifies the application of thousands of bilateral tax treaties** concluded to eliminate double taxation. It also **implements agreed minimum standards** to counter treaty abuse and to improve dispute resolution mechanisms while providing flexibility to accommodate specific tax treaty policies.
- ▶ With respect to a specific bilateral tax treaty, the measures will only enter into effect after both parties to the treaty have deposited its instrument of ratification, acceptance or approval of the MLI and a specified time has passed (the specified time differs for different provisions).
 - It is expected that the changes made as a result of being a party to the MLI would be effective during 2019, though some tax treaties may be affected as early as sometime in 2018.

OECD Multilateral Instrument (MLI) – Finnish reservations & choices

At the time of signing ceremony, Finland accepted only the agreed minimum standards and certain changes to dispute resolution mechanisms

- At the time of signing ceremony in July 2017, Finland accepted only the agreed minimum standards and certain changes to dispute resolution mechanisms (with reservations) to its existing Double Tax Treaties (DTTs):
 - The **Article 6** of the MLI alters the preamble text of the DTTs by including a notion that the intention of the agreement is to eliminate double taxation *without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance*.
 - The **Article 7** of the MLI implements the Principal Purpose Test (PPT) to the DTTs. Under the PPT, *a benefit shall not be granted if it is reasonable to conclude that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the covered agreement*.
 - The **Article 16** of the MLI alters the Mutual Agreement Procedure clauses included in the existing DTTs by enabling the taxpayer to present the case to the competent authorities of either of the contracting states.
 - The **Article 17** of the MLI implements clauses on corresponding adjustments to those DTTs where such provision does not exist.
- With regard to the scope of MLI changes, Finland included all of its DTTs except the Nordic DTT and the Finland-Bulgaria DTT.

OECD Multilateral Instrument (MLI) - Application

There are five (5) key steps for application of the MLI

Applying the MULTILATERAL INSTRUMENT Step-by-Step

Key documents to assess modifications by the MLI

The MLI

Specific tax agreement

The MLI position of a Contracting Jurisdiction

The MLI position of the other Contracting Jurisdiction

Five steps for application of the MLI

Step 1

• **Entry into force of the MLI**

Step 2

• **Covered Tax Agreement**

Step 3

• **Reservations and choice of optional provisions**

Step 4

• **Notifications of existing provisions**

Step 5

• **Entry into effect of the MLI**

OECD Multilateral Instrument (MLI) – Application: Finland-Russia DTT

The OECD MLI Matching Database makes projections on how the MLI modifies a specific tax treaty covered by the MLI

MLI Matching Database
beta © OECD 2017



Select jurisdictions:	<u>Finland</u>	<u>Russia</u>
	Finland	Russia
Signature MLI	07/06/2017	07/06/2017
Ratification MLI		
Status of List	Provisional	Provisional

[Read the Disclaimer](#)

Article 2 Covered Tax Agreement		The agreement would be a 'Covered Tax Agreement'.
Article 6 Purpose of a Covered Tax Agreement		The preamble language would be replaced by the text described in Article 6(1). Article 6(3) would not apply.
Article 7 Prevention of Treaty Abuse		Article 7(1) would apply and supersede the provisions of the agreement to the extent of incompatibility. Article 7(4) would not apply. The Simplified Limitation on Benefits Provision would not apply.
MAP	Article 16 Mutual Agreement Procedure	A.24(1)1st would be replaced by the first sentence of Article 16(1). The second sentence of Article 16(1) would not apply. The first sentence of Article 16(2) would not apply. The second sentence of Article 16(2) would not apply. The first sentence of Article 16(3) would not apply. The second sentence of Article 16(3) would not apply.
Article 35 Entry into Effect MLI		For the purposes of the application by Finland, the reference to 'taxable periods beginning on or after 1 January of the next year beginning on or after the expiration of a period' would apply. Article 35(4) would not apply.



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