Seminar on International Taxation
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Case studies on Transfer pricing

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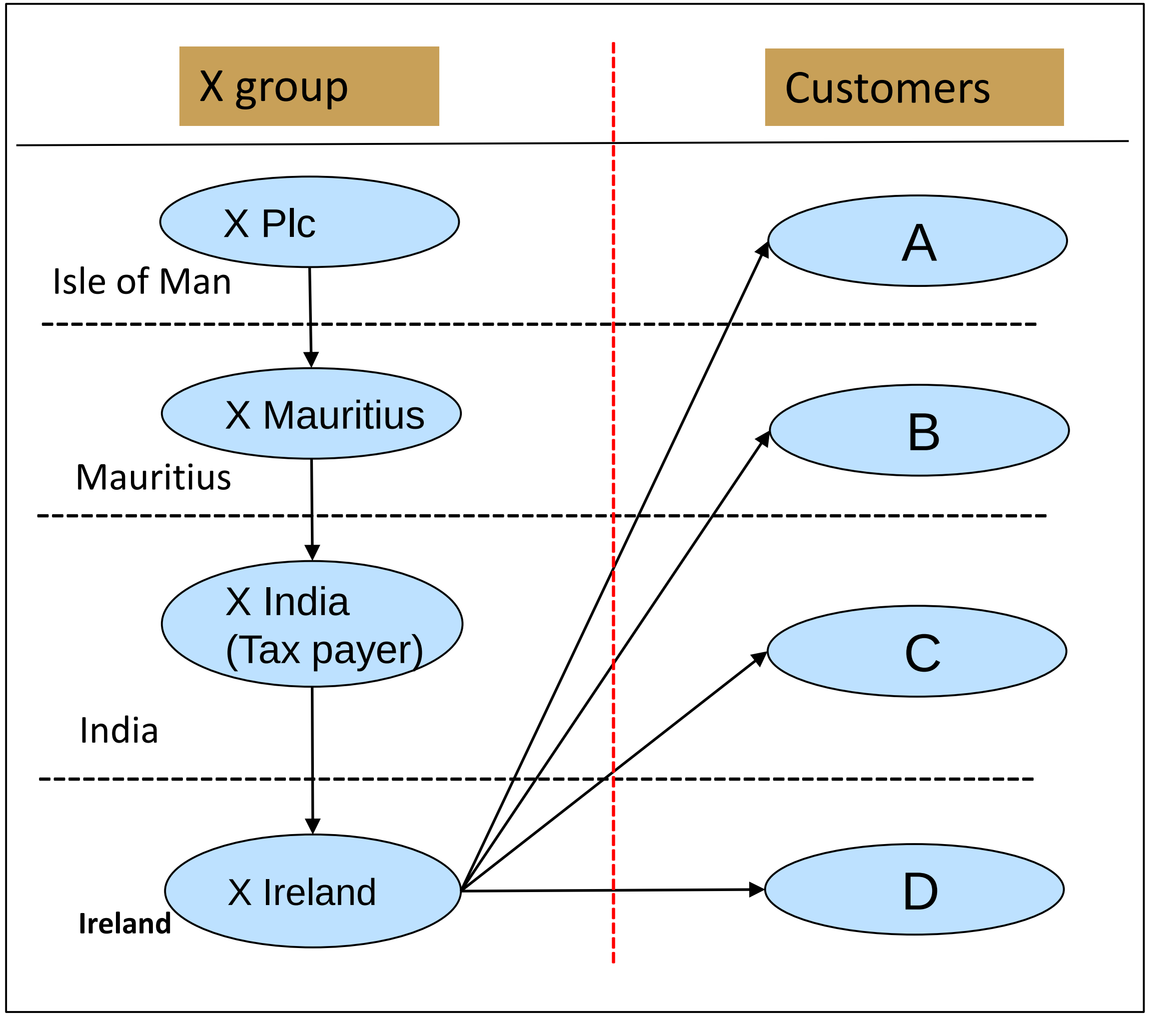
Case Study - 1



Facts of the Case:

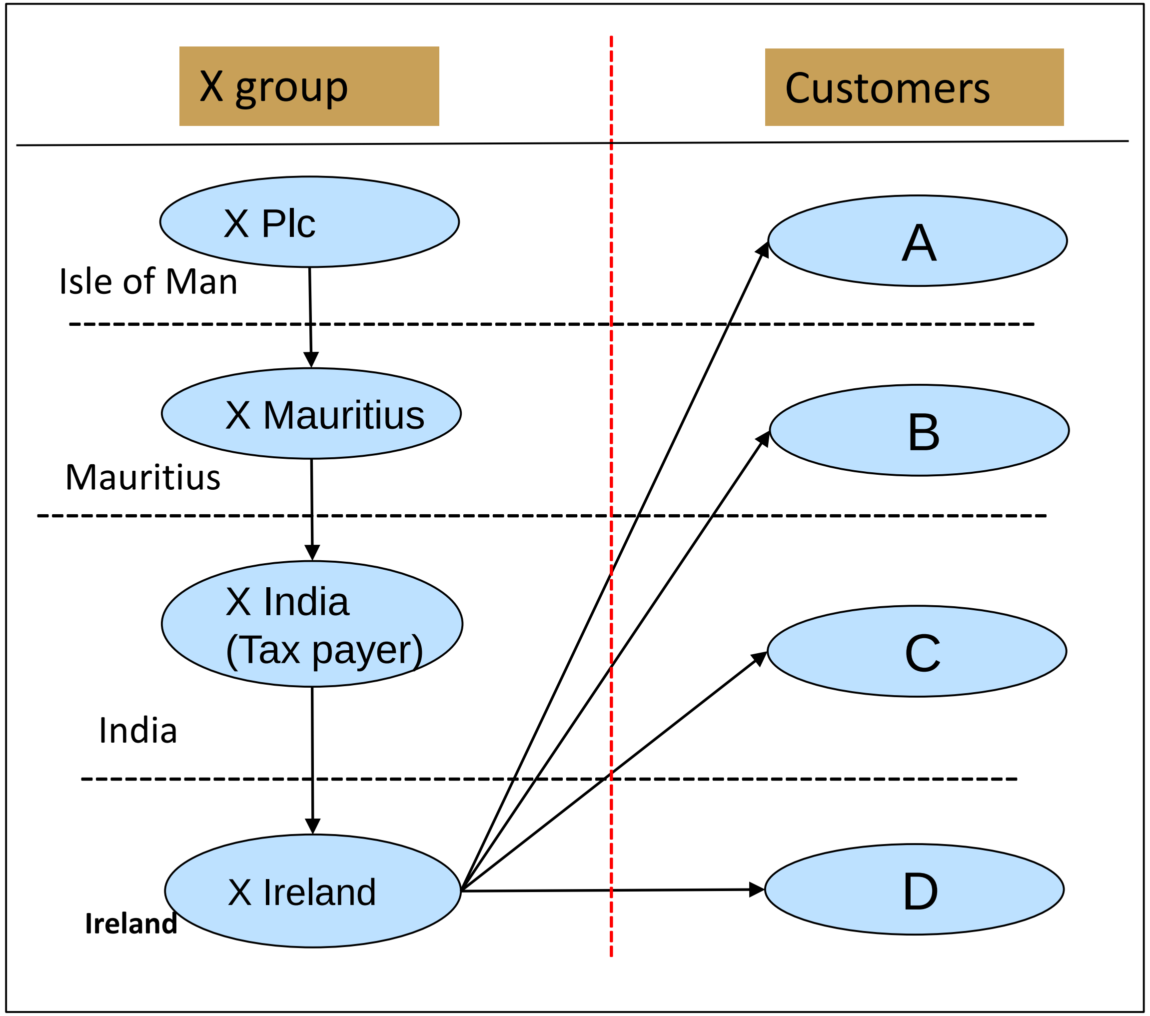
1. Taxpayer is engaged in producing animation visual effects, game art and entertainment content for Indian as well as global media and entertainment industry.

2. X India sold IP rights of intangibles generated by it to X Ireland at the developing stage based on an average of the values arrived at by two independent valuation reports.

3. TPO replaced the projections considered in DCF analysis for the purpose of valuation with actual revenues of X Ireland.

4. TPO also alleged that the taxpayer has deliberately shifted the potential revenue earning IP to Ireland being a low tax regime jurisdiction. Therefore, the TPO adopted Profit Split Method (PSM) and attributed 80 percent of the total revenue earned by X Ireland to the taxpayer.

Case Study - 1



Issues:

1. Whether actual results are relevant for valuation of intangible?

2. Whether revenue of X Ireland can be attributed to X India post sale of Intangible?

Tribunals Decision:

1. The projections cannot be replaced with actuals at a later date, as the valuation may go either way. The method adopted should be consistent and should be documented to review in the future. The review does not mean replacing projections with actuals. It is reviewing the rationale for adopting the values for decision-making.

2. Upon the sale of IP and determination of ALP, the intangible asset is the property of the AE and neither the taxpayer has any right to claim benefit nor the revenue.

DQ (International) Limited [TS-367-ITAT-2016(HYD)-TP]

DEMPE

- The determination of arm's length transfer prices for transactions involving intangibles is one of the major topics in international taxation and at the focus of multinational enterprises, tax authorities and tax advisors worldwide.

- As part of the BEPS project of the OECD and G20 countries, the OECD significantly revised its guidance on intangibles in its 2017 Transfer Pricing Guidelines, with the introduction of the so-called DEMPE approach through its Action plan 8.

- DEMPE is designed to ensure that allocation of the returns from the exploitation of intangibles, and also allocation of costs related to intangibles, is performed by compensating MNE group entities for functions performed, assets used, and risks assumed in the development, enhancement, maintenance, protection and exploitation of intangibles.

DEMPE

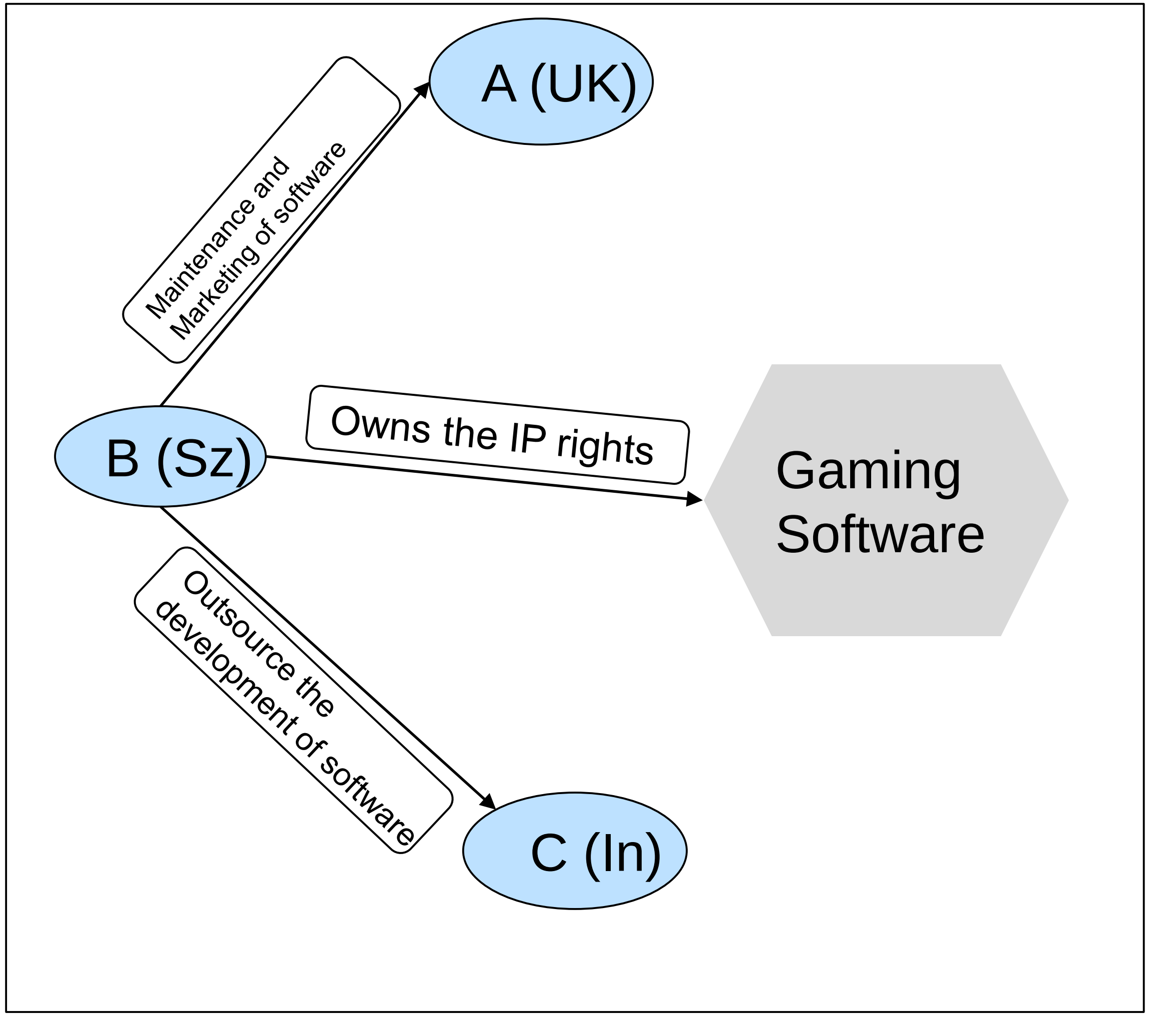
- **What is DEMPE:**
  - **Development**:
    - Everything associated with coming up with ideas for intangibles, and putting plans and strategies in place for their creation
  - Enhancement:
    - Continuing to work on aspects of intangibles to make sure they can perform well at all times and continue to be improved
  - Maintenance:
    - Actions that ensure intangibles continue to perform well and generate revenue
  - Protection:
    - Ensuring that the value of the intangible remains strong
  - Exploitation:
    - Refers to the way in which intangibles are used to generate profits

DEMPE

- **Before DEMPE:**
  - The legal owner of an intangible was entitled to essentially all the returns/income generated by that particular intangible.
    - However, if the maintenance and protection of the IP is taken care by any other group entity then that will be considered as a separate services and would charge an appropriate margin on cost.

- **After DEMPE:**
  - Any income that is generated as a result of that IP is owned by all the parties that perform the DEMPE functions.
    - Rather than the IP owner receiving the full amount of the returns/income generated by the intangible, the returns instead have to be divided among the group parties in line with each entity's contribution to the value of the IP.

Case Study - 2



Facts of the Case:

1. Company A (UK resident) holds 100% shares in Company B (Switzerland resident) and in turn Company B holds 75% shares in Company C (Indian resident).

2. Company B wants to develop a gaming software for which development work has been outsourced to Company C.

3. Marketing and Maintenance of the software is being taken care by Company A.

Issue:

1. What should be the policy for the transfer pricing.
2. Is there any relevance of DEMPE as specified in OECD TPG 2017 based on BEPS Action Plan 8.


THANK YOU