

Evolving International Rules and Standards for Taxing IP

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1. Domestic IP rules

Reasoning to locate IP in one country

- **Tax certainty (rulings)**
- **IP protection**
- **Tax benefits (incentives)**
 - e.g. patent boxes, innovation boxes and knowledge development boxes
 - often combined with research and development (R&D) credits, IP amortization and other benefits

Some countries attractive for the IP location

OECD-G20 countries: Switzerland, the Netherlands, Belgium, Luxembourg

Non-OECD, non-G20 countries: Colombia, Israel, Turkey, Korea, Panama and Uruguay

Problems

IP preferential tax regimes, harmful (low) tax competition, transfer (mis)pricing of intragroup taxations

2. International IP rules

- OECD work aims to prevent base erosion and profit shifting (BEPS) and to align IP taxation with the location of economic activity.
- BEPS Action 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance
- BEPS Action 5 Minimum Standard to be implemented by countries members of the BEPS Inclusive Framework (112 countries)
 - A “nexus” approach (location of R&D in the country offering its preferential tax rate)
 - BEPS Action 5 cited 16 regimes whose IP tax regimes did not align with this approach.

2. International IP rules

- Progress Report on Preferential Regimes, approved by the Inclusive Framework on BEPS in 2017 and 2018 (24 January)
- Results of the review of (harmful) preferential IP regimes
 - Some countries have abolished their IP regimes (e.g. Colombia, Luxembourg, Malta, Liechtenstein and San Marino*).
 - Other countries are in the process of amending their IP regimes (e.g. Spain, Andorra, Panama, San Marino*, Uruguay)
 - Still harmful: France, Italy (for the extension to new entrants for trademark between 1 July 2016 and 31 December 2016) and Turkey (potentially harmful)

Available at: <http://www.oecd.org/tax/beps/update-harmful-tax-practices-2017-progress-report-on-preferential-regimes.pdf>

2. International IP rules: Problems

Companies

- compelled to rethink their global IP management and value chains
- more uncertainty: possible challenge of IP structure and a possible fine for companies that deem to be artificially diverting taxable profits from their shores to take advantage of IP tax incentives abroad
- Possible application of general anti-avoidance rules

Countries

- to find the right balance between granting tax incentives and to protect their tax base. Is abolishing the IP regimes the solution? how to redesign an IP regime that is compliant with Action 5 Minimum Standard?
- how to ensure IP protection? And how to provide certainty to taxpayers?

3. European Union rules

2015: Action Plan for a Fair and Efficient Corporate Taxation in the EU

a) 5 Key Areas for Action:

Common (Consolidated) Corporate Tax base, ensuring fair taxation where profits are generated, creating a better business environment, increasing transparency, and improving EU coordination

b) IP regimes profits should be taxed where the actual activities take place

2016 Anti-Tax Avoidance Package

- Regarding IP regimes, some companies shift profits from where they are generated to Member States offering low tax rates and preferential regimes, and out to third countries with no link to the place of actual economic activity
- In the EU, some of the incentives may breach EU state aid rules and can be tackled via state aid control

4. Framework for International Standards

- Transparency (exchange of rulings and transfer pricing documentation requirements to prevent transfer (mis) pricing)
- Economic activity and substance
- Certainty
- Uniformity approach: OECD and EU: is the approach of the EU more burdensome for companies –Anti Tax Avoidance Package?

Countries should keep in mind:

- If the “nexus approach” is used, how will the substantial activity requirement be reviewed?
- The OECD BEPS Action 5 requires the taxpayer to engage in a substantial activity and to incur actual expenditures on such activities. Do the countries follow this approach?
- If not, are there any other conditions required to comply with the substantial activity requirement?

4. Framework for International Standards – developing countries

- Evaluation of IP regimes few developing countries (Colombia, Uruguay, Panama).
 - Developing countries problem is tax incentives- preferential tax regimes that may result in base erosion (e.g. free trade zones, investment allowance, tax holidays).
- How the OECD and EU developments regarding the IP regimes will benefit developing countries?
- Does the developing country have the administrative and technical capacity to implement the “nexus approach” including the review of the substantial activity requirement? Is the developing country expecting technical assistance from the OECD in this regard?

4. Framework for International Standards – developing countries

- Regarding BEPS Action 5: The problems that have been identified by developing countries during the regional consultations on Action 5 are
 - the absence of ruling practices,
 - the excessive use of incentives and
 - the lack of a coordinated approach that could result in greater tax competition between developing countries
- The Platform for Collaboration on Tax has developed “toolkits”
 - Aim is to assist developing countries in efficiently implementing the various Actions of the OECD/G20 BEPS initiative and in addressing additional specific, non-base erosion and profit shifting, tax issues
 - One example is the toolkit on tax incentives published in October 2015. Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment
 - It does not address the issue of IP preferential tax regimes

4. Framework for International Standards – developing countries

- Even though the OECD also intends to address preferential tax regimes in Action 5, the critical assessment of the tax incentives including of the IP preferential tax regimes in developing countries is lacking
- This new era following the OECD/G20 BEPS initiative, combined with the concomitant transparency, results in challenges for tax authorities with regard to their relationship with taxpayers (mutual trust and certainty)
- This goes beyond the toolkit on tax incentives developed by the Platform for Collaboration on Tax.

5. Conclusions and recommendations

- International tax standards regarding IP regimes have changed, but not yet clear how this nexus will be applicable?
- How substance will be defined by countries? Different approaches?
 - Result: More uncertainty for companies
- It is not clear how the changes to the IP regimes will benefit developing countries? And whether the EU rules will result in a extra burden for EU countries and for third (non-EU) countries.
- Further research should be carried out in the implementation of BEPS Action 5

Thank you for your attention



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