

# A closer focus on marketing intangibles

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## US BACKGROUND:

THE CONCEPT OF 'MARKETING INTANGIBLES' HAD BECOME A VIGOROUSLY DEBATED ISSUE WITHIN THE TRANSFER PRICING COMMUNITY IN THE US AND OTHER KEY COUNTRIES. WHILE ITS PRECISE MEANING IS RATHER UNCLEAR FROM A TAX AND LEGAL PERSPECTIVE, AND MAY VARY IN APPLICATION BY COMPANY AND INDUSTRY, THE BREADTH OF ITS GRASP CONTINUES TO GROW AS THE CONCEPT HAS BEEN VARIOUSLY APPLIED. GENERALLY, HOWEVER, THE TERM MARKETING INTANGIBLES CAN BE MEANT TO INCLUDE BRANDS, TRADEMARKS, THE LOCAL MARKET POSITION OF A COMPANY OR ITS PRODUCTS AND KNOW-HOW THAT SURROUNDS A TRADEMARK SUCH AS THE KNOWLEDGE OF DISTRIBUTION CHANNELS AND CUSTOMER RELATIONSHIP. THE IRS BELIEVES THE INVESTMENT IN THESE INTANGIBLES IS DERIVED FROM, AMONG OTHER THINGS, THE COMPANY'S LEVELS OF ADVERTISING, MARKETING AND PROMOTION EXPENDITURES (AMP).

The concept initially gained prominence in the late 1980's and particularly in a docketed Tax Court case involving the sale of vacation destinations by a US distributor on behalf of a prominent foreign travel and vacation entity. The transfer price for the destination package was not directly at issue, but the level of AMP incurred by the US distribution entity for these sales was scrutinised. The IRS sought either to (1) disallow a portion of the AMP under the notion that it was incurred on behalf of the foreign trademark owner, or (2) deem a service fee for the marketing efforts performed by the US distributor on behalf of the foreign trademark owner. While the case was settled by the parties prior to litigation, this case foreshadowed the issues of today.

Subsequently in 1994, the IRS issued final transfer pricing regulations under IRC Section 482 wherein it addressed the

juxtaposition between the foreign owner of a trademark and the economic costs incurred by its US affiliate to promote and exploit that item of intangible property in its territory'. In examples then referred to as the 'Cheese Examples', one can extrapolate a number of scenarios between the foreign parent trademark owner, Fromages Freres, and its affiliated US distributor, such as where: (1) the US distributor was simply given a set transfer price and the development of the US market was at the risk and economic cost of the US distributor; (2) the foreign parent indirectly subsidised the development of the US market through a reduced transfer price; and (3) the foreign parent provided the distributor with a rebate of a portion of the distributor's AMP based on sales volumes. Following the theories in the above Tax Court case<sup>2</sup>, the Cheese Examples could require a return for the

distributor's investment in the marketing intangibles either in the form of a service fee arrangement with an appropriate profit markup or more robust operating margins to reflect the return for the developed marketing intangible.

The DHL Tax Court case decided in 2002 became the next significant step in the evolution of the marketing intangible concept. This case addressed the IRS' attempt to impute a trademark royalty for the use of the DHL tradename by DHL's foreign affiliates. At issue was the taxpayer's assertion that a royalty should not be imputed from these foreign affiliates because they bore the economic investment for the development of the DHL trademark. While marketing intangibles surrounding the DHL tradename were not directly discussed, the DHL Tax Court case stood for the proposition that for items of intangible property, the party who bore the economic burdens of the investment should bear the economic rewards. The aggregate levels of AMP, as well as certain other expenses that were incurred by the DHL foreign affiliates, were considered for purposes of this economic investment, although there was no real analysis of the accounting codes that made up the AMP nor what component of the underlying costs were directed to trademark development or surrounding intangibles. In effect, the Tax Court followed the money in order to match income with expense. Here, the Trial Judge espoused his 'bright-line' test which notes that, while every licensee or distributor is expected to expend a certain amount of cost to exploit the items of intangible property to which it is provided, it is when the investment crosses the 'bright line' of routine expenditures into the realm of non-routine that, economic ownership, likely in the form of a marketing intangible, is created<sup>3</sup>.

The marketing intangible issue is most recently considered in the Glaxo case in the US Tax Court<sup>4</sup> where the IRS has asserted a tax deficiency in amounts approximating almost US\$20bn for all open tax years. The underpinning to the IRS claim was that Glaxo's US affiliate was the economic owner of the US marketing intangible through its investment in a marketing strategy conceived and directed by Glaxo US executives. This investment arguably resulted in a fully integrated business and led to the success of its products in the US market. Critical facts, however, included that all items

of intellectual property were owned by Glaxo UK as well as the marketing platform and strategy was developed by Glaxo UK. As a distributor, Glaxo US earned an approximate 16% operating profit margin. However, the IRS was not satisfied with this amount. Accordingly, the IRS asserted that the US affiliate was entitled to operating income commensurate with its investments. While this case was settled for approximately US\$3.4m, it serves as a precursor for the IRS to continue challenging this issue on audit.

The theories described above continue to be raised in most tax audits and are presently under consideration by the US Tax Court in current pending cases. Numerous unanswered questions remain. While there may be merit in the DHL 'bright line' test, from a practical point of view, it is so industry and company specific, that it may be impossible to consistently apply in most cases. Similar companies within the same industry may have vastly different approaches to their marketing philosophies, product launches, and/or product dependence or interdependence. This could create very different levels of AMP and different 'bright lines.' This may even occur within the same companies and for



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similar product categories. These expenditures can also be impacted by the product's position in other countries, the timing of product launches, and the competitors and their products, each of which impacts the 'bright line' benchmarking and comparability standards.

The OECD added another twist to the international view of marketing intangibles when it included a discussion of their impact on the allocation of profits to either headquarter or permanent establishment<sup>5</sup> and did not clarify the concept of marketing intangibles when it establishes that they include, inter alia, the name and logo of a company and a brand<sup>6</sup>. The draft lends a hand to the quest for marketing intangibles by sympathising with the decentralised allocation of 'global' marketing intangibles as key entrepreneurial risk taking functions. The OECD draft is also an analogous application of the OECD Transfer Pricing Guidelines to permanent establishment/headquarter cases.

Thus, similar principles may be applied to company to company transactions. Even more, the draft speculates that key entrepreneurial risk taking functions are unlikely to be dispersed within the enterprise, but are concentrated either at the permanent establishment or the headquarter where marketing intangibles are specific to a permanent establishment's host country<sup>8</sup>. These ideas may well be taken by tax administrators as an invitation to identify something specific about an international marketing intangible and to establish some key entrepreneurial risk taking functions in the distribution country.

## Europe

European tax authorities have observed the marketing intangibles debate that was taking place in the US. The German Government has seized the opportunity offered to it by the judicial development of the concept of business opportunity developed in case law before the turn of the last millennium<sup>9</sup>. Today, it is understood that a business opportunity is an asset. Consequently, if there is no asset, there can be no business opportunity. As a result, failed AMP investments cannot lead to an asset nor to a business opportunity. At the same time, important questions remain open such as when to attribute a business opportunity

to a specific group entity among several, or how to value and establish a business opportunity. The spending of resources, such as money, is a widely recognised - though not unambiguous - criterion for the allocation of a business opportunity to an (distributor) entity. This is the link with the rather indiscriminate identification of (alleged) marketing intangibles that is so tempting to tax administrators.

The landmark Federal Tax Court decision of 17-2-1993<sup>10</sup> reveals a taxation concept competing with the allocation of marketing intangibles to a distributor. In the 1993 Aquavit decision, the center of the controversy were AMP expenses incurred by the German distributor when opening and penetrating the German market for the foreign produced branded spirits. Rather than attributing a deemed marketing intangible and a corresponding return to the distributor, the court disallowed the excessive AMP expenses and instructed the tax office to tax them as dividends in disguise. Financially it makes a difference whether excessive AMP expenses are taxed as hidden profit distributions or whether those expenses are capitalised as investment an adequate return being allocated on top of it.

Both the deeming and allocation of a marketing intangible and the disallowance of excessive AMP expenses are based on a more general principle of arm's length taxation, namely, the postulate that each entity ought to earn a return 'commensurate' with the functions exercised, risks taken and the assets actually held by the entity.

The Dutch and French tax authorities are also enamored with the issue. While the concept initially surfaced corporate in restructurings, it has lately become an issue under audit as to whether the distributors have been sufficiently awarded for their development of the market. It is becoming predictable that upon restructurings, that tax authorities first raise the issue that the margin allocated to foreign activities are too high, and to pre-empt that that discussion, might fail to yield the desired result of retaining revenue. The next determination is that marketing intangibles or goodwill are being transferred to the foreign country. As marketing intangibles are an economic, nearly synthetic, concept this development is likely to be countered in litigation by the civil law concept of legal ownership of legally recognised intangibles at some point.

In audit cases, the French tax authorities have been keen to protect their tax base by pointing at the legal protection granted to trademarks and patents and they might demand a return to the legal ownership for that term even where all AMP was incurred by the foreign distributors. Taxpayers are, therefore, caught between these tax authorities defending their tax bases and may suffer double taxation over this issue.

Transfer pricing is a legal concept driven by economics and proportionality between functions performed, risks incurred and earnings made. The boundaries of this proportionality are provided by comparables, largely from public databases. As the European countries all largely adhere to a continental system of recording, where costs are classified by type of expenses, reliable data of profit margins are lacking and comparables must be reviewed from an operating profit level and ratios must be consulted, such as the Berry Ratio or ratios of operating expenses to gross receipts or gross profit margins, to derive a realistic sense of comparability. However, as most European tax authorities prefer the traditional transaction transfer pricing methods, absent the application of such a method there is little authority or defense against adjustments by tax authorities.

The discussion and issue are likely to peak soon as the European Court of Justice has been chipping away at the domestic tax bases by breaking down domestic tax rules that discriminate against foreign taxpayers.<sup>11</sup> Because European tax authorities are seeking for a last anchor to base their access to revenue on, transfer pricing, intangibles and marketing intangibles, seem to be ideal for that purpose. One way to attempt to minimise exposure on the marketing intangibles front is to carefully define and allocate ownership of client lists, responsibilities for follow up with clients and potential after sales activities, marketing and merchandising responsibilities and in particular responsibilities for AMP spend in clear language contractual arrangements between related parties. This requires more than mere contract drafting and *de facto* adherence to contract requirements. So far, the judiciary generally appears to be quite formalistic, and not in favour of creative economic theories that would merit allocation of income elsewhere than where it legally and contractually belongs.

## Asia Pacific

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In Japan, there exists no judicial precedents or regulations of tax authorities for the marketing intangibles issue, nor are there yet the same vigorous debates on the issue as in the US. However, an officer responsible for international taxation at the National Tax Agency (NTA), (Director, International Taxation) delivered a lecture on the present situations and problems of international taxation at a meeting held in June, 2004 and referred to intangibles in general, and marketing intangibles specifically.<sup>12</sup> This is presumably the only instant where the tax authorities have expressed their views on this issue. Some of the views are set forth below, wherein the Director stated:

“In Japan, it is generally thought that an intangible, irrespective of whoever has legal rights thereto, belongs to not the registered owner thereof but to the party who has developed or enhanced the value of the intangible. This is an important point.”<sup>13</sup>

In the Instructions of the Commissioner dated June 1, 2001 (the ‘Guidelines of Administrative Processes for Transfer Pricing’), the NTA, declared, “The Agency shall exert its efforts to properly administer examinations of transfer pricing or audits for APAs by reference to the OECD Transfer Pricing Guidelines whenever necessary,” and clarifies that it will make the OECD Guidelines a base for its administration. The OECD Guidelines may also work as a guideline for the treatment of marketing intangibles. Further, the Director refers to the draft US Treasury Regulations, Section 1.482-4 (f)(4), and comments that “The United States has placed emphasis on the status of legal owners, but we have an impression that the attitudes of Japan and the United States are getting closer.” Hence, the Director believes that the arm’s length consideration for a contribution by one controlled taxpayer that develops or enhances the value, or may be reasonably anticipated to develop or enhance the value, of an intangible owned by another controlled taxpayer shall be determined in accordance with the applicable rules under section 482 of the Internal Revenue Code.

Lastly, the Director stated that, “On the premise that an intangible belongs to the party who has developed or enhanced the value of the intangible, it must be determined

who is the party who has developed or enhanced the value of the intangible.” It can be considered that this party is the one who has made a decision to develop or enhance the value of the intangible, managed risks thereof, provided services therefore and bore the costs thereof. “Hence, even if a parent company, for the purpose of unifying the management of all manufacturing patents and trademarks of its group companies unilaterally, holds the entire legal rights thereof, ... if the brand value is enhanced through marketing activities by a subsidiary, we consider that for taxation purposes, the interest in the intangibles in connection with the manufacture and sale thereof shall belong to the subsidiary and the benefits corresponding to the economic value of the intangibles belong to the subsidiary.”<sup>14</sup> Emphasis Added.

These passages clearly imply that while there is no direct Japanese jurisprudence on this subject, the thinking of the NTA and the IRS regarding marketing intangibles fairly parallels each other and this issue may likely result in similar audit issues in Japan, as in the US.

Australia’s reaction to the ‘marketing intangibles’ issue is more well-developed. The Australian Tax Office (ATO), issued on its website, on January 25, 2006, a new Guideline entitled ‘International Transfer Pricing – Marketing Intangibles, examples to show how the tax office will determine an appropriate reward for marketing activities performed by an enterprise using trademarks or tradenames it doesn’t run.’<sup>15</sup> The ATO makes reference to a number of its earlier rulings in which it has dealt with this issue.<sup>16</sup> Key matters which are determination of the ATP approach are:

- the contractual arrangements between the owner of the trade name and the market;
- whether the level of marketing activities performed by the marketer exceeds that performed by comparable independent enterprises;
- the extent to which the marketing activities would be expected to benefit the owner of the trade name and/or the marketer; and
- whether the marketer is properly compensated for

its marketing activities by a ‘normal’ return on those activities or should share in an additional return on the trade name.

Some scenarios that may possibly be under examination are:

- Where a related party distributor acting in Australia is reimbursed as to 100% of all of its marketing spend on behalf of the foreign parent and also receives a marketing service fee based upon a percentage of its marketing spend, the distributor is regarded as an agent being reimbursed for its promotional expenditure by the owner of the marketing intangible.
- Where the Australian taxpayer obtains no rights to use the trade name other than in marketing and distributing a branded product, it is anticipated that the ATO would not expect the Australian taxpayer to be charged a royalty in addition to the transfer price of the product. Where the marketing spend, compared to arm’s-length comparables is ‘normal’, it is likely that the ATO would not propose an adjustment to the distributor because the distributor would be receiving an arm’s length return.
- Where a distributor incurs marketing expenditure above and beyond what independent enterprises are assessed to do and has no right of recovery or reimbursement from the foreign parent so that the profits are lower than what unrelated parties would accept, it will be considered to have assumed a significantly greater and higher risk than the arm’s-length party.

In latter circumstance, it is anticipated that the ATO would propose to increase the taxable income of the distributor by applying, in substitute for the taxpayer’s transfer pricing methodology, a residual profit split methodology where it would attribute a basic return for the functions, assets and risks of each of the parent and Australian subsidiary and split the residual profit on the basis of the value of the intangible assets relevantly owned by the parent and the subsidiary. Presumably, the subsidiary’s intangible assets will constitute the contractual rights it has from the long-term distribution agreement which would need to have been valued at the time of entry into

the original Agreement. The ATO is thought unlikely to accept (presumably in retrospect) a reimbursement by the foreign principal of the Australian subsidiary's marketing spend because it would not be consistent with the legal arrangements between the parties.

The ATO's scenarios do not securely set out how it would quantify the adjustments it was proposing nor how it would distinguish between routine or non-routine marketing spend. In the ordinary course of the self assessment tax system, any amounts of marketing spend would not be immediately apparent to the ATO and would be expected to have been paid to arm's length providers in the first instant. However, where the AMP was 'excessive' or above a 'normal arm's-length range' it was likely to have created or developed an 'asset' for the local distributor which could be separately identified, valued carved out from the 'property' belonging to the legal owner and, either subject to tax in its own right, attributed to a royalty, or reducing the transfer price.

The ATO has not further indicated if it would determine, in the limited circumstances, an increase in the value of the intangible property. It is also unclear if the ATO is looking to attack or bifurcate the royalty payments from the transfer prices. The ATO currently recognises this as an emerging issue.

Most recently China has indicated a growing interest in the marketing intangibles issue as they follow the global trends in transfer pricing.<sup>17</sup> The likely outgrowth of this announcement is that the State Tax Administration (SAT) may wish to seek more income allocated to Chinese affiliates of foreign companies (called wholly Owned Foreign Enterprises or WOFEs) for expanding market share in China through AMP expenditures. Concomitantly, the SAT may also challenge royalty rates to foreign affiliates where brand recognition of its products is being developed locally in China by the WOFE. Particularly vulnerable in China are companies who have been unknown to the Chinese market, but are currently launching product into the marketplace.

The SAT is seeking input globally about how to address marketing intangibles. Most prominently, they may be following the lead of the US IRS and the ATO in this area. Not only is the SAT addressing the technical tax issues

surrounding marketing intangibles, but how to properly document the transaction. And, with the elimination of many tax holidays and incentives in a drive for revenue these issues are at the forefront, particular as multinational companies restructure their Chinese WOFE.

Indirect taxes in China may also be largely impacted by the role of marketing intangibles. For example, a royalty is subject to a 10% withholding tax and a 5% business tax. Because the royalty may be part of the cost base of the affiliate for either tax or customs, there may exist some double counting of the tax base.

## **Economic benchmarking challenges**

These disparities in approach, as well as the difficulties with the issue itself, make economic benchmarking extraordinarily difficult. First, one must actually review the precise accounting codes for what comprises the AMP. Factually, this may establish the company's routine versus the non-routine expenditures, however, there are difficulties in both characterisation and timing, such as for product launches. The amount of these expenditures may cross certain thresholds, or ratios set by either the taxing authority, taxpayer, or industry analysts, yet may be factually considered routine given the specific product, market, and timing of the launch. Even if this is all accomplished, economic benchmarking still remains a challenge.

What makes this economic benchmarking challenging is that there is no real database that addresses pure marketing intangibles. One can consider various rates of return on the cost of the investment, but that is not entirely reflective of a market value for intangible property. One can also extrapolate certain knowledge by reviewing the relationship of gross receipts to operating expenses to establish ratios to be applied to the taxpayer, but that analysis may be imprecise because operating expenses of all types are usually aggregated. Public companies are not required to disclose their AMP, and even for those who do, there is no way to determine the percentage of these expenses devoted to intangible property enhancement.

The idea that there are clear industry standards that establish what a distributor should spend on AMP can

be problematic. The financial statements of companies within an industry may classify and define AMP expenses differently. One company may define spending as advertising while another company defines similar spending as media or distribution. Other items, such as market studies or promotional brochures may be classified under completely different accounting codes.

Contributing to the difficulty is the uncertain definition of what exactly constitutes marketing intangibles. In addition to trademarks and trade names, marketing intangibles can be company specific, but may include customer lists and knowledge of distribution channels.<sup>18</sup> Customers are not 'intangible' but, on the other hand, are certainly not, *stricto sensu*, under the control, or ownership of, the company.<sup>19</sup> Yet, it is undeniable that customers (and more in general, all customer relationships) are a key value driver and one of the main indicators of growth potentials.

The lack of transparency and consistency in reporting practices for AMP spending makes it difficult to identify true benchmark levels of normal advertising expenses. There are a number of databases that are commonly used to conduct comparables analysis and benchmarking of financial data within industries, including Compustat, Disclosure, Moody's, Worldscope, Global Vantage, and Amadeus, among others. Although the database providers may attempt to standardise data across companies, they are faced with the same challenges regarding transparency and consistency as practitioners when reviewing company documents.

In compiling the financial data of the companies, the database providers also make certain decisions regarding classification and organisation that may not easily align themselves with the needs of the practitioner analysing AMP expenditures. For example, the Compustat database defines Advertising Expense as follows: "This item represents the cost of advertising media (radio, television, newspapers, periodicals) and promotional expenses. This item excludes selling and marketing expenses." Expenditures that relate to the creation of marketing intangibles may not be captured by this line item. However, the category of Selling, General, and Administrative Expense is defined, as one would expect, far more broadly

and includes 27 separate items, such as salaries and related costs, R&D, engineering, legal expenses, marketing, and others in addition to advertising. Using this item as a proxy would surely overstate the investments in marketing intangibles. Further, most contemporary databases that address trademark royalties (e.g. RoyaltySource and RoyaltyStat) contain information on license agreements between unrelated parties, but do not provide sufficient elements to segregate the remuneration paid for the intangible property (e.g. trademark) from the one paid, for instance, for ancillary services.

The level and nature of AMP spending can be also impacted by a variety of business factors, including management policies, market share, characteristics of the market, and the timing of product launches. The annual reports and SEC documents of public companies, as well as the database providers, generally do not provide the necessary level of detail that would be required to reconcile these management considerations and classification differences.

An additional challenge to an analysis of marketing intangibles is that AMP spending generally has spillover effects to or from other products or product lines. Also, the effects of AMP spending are distributed over time and so the accounting practice of expensing such AMP investments in the current period can create distortions in determining economic profits. This is most evident when dealing a product launch, where there may be a sharp increase in spending prior to the launch of a product or product line, followed by subsequent decreases to more stable spending levels. It might be appropriate to segregate out the spending related to the product launch, or at least ensure that the data being considered covers a sufficient time period such that the lifecycle dynamics can be properly addressed. This requires estimations of the useful life of AMP spending.

In analysing marketing intangibles for transfer pricing purposes one should consider, among others, the following questions:

- Will certain costs and expenditures result in an economically valuable asset?

- How do you distinguish developmental (i.e. non-routine) from non-developmental (i.e. routine) expenses?
- How are allocation keys established for applicable expense codes?
- What is the expected use of the asset by the entity?
- What is the expected useful life of the marketing intangible and how is this economically determined?
- Are there any legal or regulatory restrictions?
- What are the effects of obsolescence or other external economic factors?
- What is the level of maintenance expenditures?
- What are the customs ramifications of marketing intangibles expenses and/or royalties?

It is also important to consider the nature of the relationship between the related party manufacturer and the local distributor. Even assuming that it is possible to estimate a normal level of AMP spending for a particular industry, and that the distributor in question spends at a greater rate than this routine level, a critical factor is whether the intercompany arrangements are such that the distributor is assuming risks consist with an entrepreneurial role. If the intercompany arrangements are such that the distributor is effectively guaranteed a routine profit level regardless of the level of its marketing expenditure, then the question of whether these expenditures are above a normal level is not relevant because any resulting profits would be attributable to the manufacturer that is assuming the entrepreneurial risk.

### What does the future hold?

If one follows the normal trend that has been experienced in transfer pricing over the past years, this concept could likely become the subject of serious debate among taxing authorities as the grapple for an MNC's global profit such that economic modeling will become in vogue. If the item of intangible property (i.e., the trademark) is owned within the same legal entity, the AMP expenses can be perceived as enhancing the intangible's value and that value should

be reflected within its operating margin positively or negatively as the case may be. If the intangible is owned by another affiliate, the taxpayer will be perceived as the owner of the local marketing intangible, in whole or in part, based on the contributions of the other affiliate and the taxpayer. Here, the taxpayer's contributions will be considered only to the extent its AMP exceeds the 'bright line' test and constitutes non-routing intangibles.

These facts will signal a real need to engage in planning to assure that any perceived marketing intangible is consistent with the taxpayers' business realities. It is here that a more refined and documented definition of the company's marketing intangible is needed for a more reliable economic analysis. Most important is that the relationship between the parties regarding the expenditures for the development of the marketing intangible must be documented within the parties' distribution and/or license agreement.

If an entity is intended to make investments in developing marketing intangibles, the nature and degree of expected spending should be clearly documented. An attempt should also be made to demonstrate that these activities differ than those undertaken by the distribution comparables, keeping in mind the data and information challenges discussed previously. The intercompany pricing policies should reflect that the entity is making additional investments and assuming additional risks and therefore should reasonably expect to have the potential for non-routine benefits should the intangible-developing activities prove successful. On the other hand, if an entity is not expected to be permitted to realise the potential benefits from local activities designed to develop, maintain, or expand marketing intangibles, the intercompany pricing policies should be such that the entity is not assuming the risk and expense of developing those marketing intangibles.

### Conclusion

These issues are nonetheless complex and become more so when the taxpayer fails to properly document these issues. In this latter scenario, the applicable taxing authority

is able to project its own view of the taxpayer's market, investment, and ultimately marketing intangible which at times can be totally at odds with the taxpayer's facts and commercial realities. And, if the matter is resolved adversely to the taxpayer, it will have to live with that result for subsequent tax years. Prudent taxpayers should take control of this issue by defining itself the marketing intangible in the context of its business, marketplace and investment, and documenting it in a legal agreement between the related parties.

**Notes:**

- <sup>1</sup> Reg. 1.482-4 (f) (3) (iv), Exs. 2, 3, 4. (1994).
- <sup>2</sup> DHL Corporation, TCM 1998-461, aff'd in part, rev'd in part 285 F.3d 1285, 89 AFTR2d 2002-1978 (CA-9, 2002).
- <sup>3</sup> Unfortunately, the Trial Judge did not embellish on this test to provide practical guidelines to this theory because he essentially held that the taxpayer failed to meet its burden of proof. Stated otherwise, he was concerned that DHL did not expressly identify those costs that were actually incurred in the development of the DHL tradename and whether those costs were truly earmarked for such development.
- <sup>4</sup> GlaxoSmithKline Holdings (Americas) Inc., v. Commissioner, T.C. No. 5750-04. GlaxoSmithKline Holdings (Americas) Inc., v. Comm'r., T.C. No. 6959-05. Note: The Glaxo Docket No. 5750-04 covers years 1989-1996 while the Glaxo Docket No. 6959-05 covers years 1997-2000.
- <sup>5</sup> OECD, Discussion Draft on the Attribution of Profits to Permanent Establishment – Part I (General Considerations), 2nd August 2004, s. 221, 239 et seq.
- <sup>6</sup> OECD, *ibidem* s. 239
- <sup>7</sup> OECD, *ibidem* s. 240
- <sup>8</sup> OECD, *ibidem* s. 241
- <sup>9</sup> In 2002 the German Ministry drafted guidance to address potential abuses caused by business restructuring that shifts risk and intangible ownership to affiliates in low-tax jurisdictions. See BNA Transfer Pricing Report, Vol 11 No 10 of September 18, 2002.
- <sup>10</sup> Federal Tax Gazette II 1993, p. 457
- <sup>11</sup> Most recently in the Bosal case (deductibility of expenses made for foreign participations) and likely in the Marks and Spencer case (allocation of foreign losses to domestic tax base).
- <sup>12</sup> See, Hiroki Yamakawa Present Situations and Problems of International Taxation, [(Sozei-Kenkyu (Tax Study) (August-October, 2004)].
- <sup>13</sup> *Id.*
- <sup>14</sup> *Id.*
- <sup>15</sup> Australian Taxation Office, Taxpayers and Tax Agents Guide NA 1456-11, 2005. See [www.atogov.au](http://www.atogov.au)
- <sup>16</sup> See TR 94/14 at para 235 and 334; TR 97/20 at para 1.13 and 2.23; and TR 98/11 at para 5.39 and 5.43
- <sup>17</sup> 'SAT Studying Marketing, Licensing Intangibles, Practitioners Say', 16 No. 6 BNA Transfer Pricing Report 175 (July 11, 2007)
- <sup>18</sup> See Levey, Shapiro, Cunningham, Lemlein and Garofolo, 'DHL: Ninth Circuit Sheds Very Little Light on Bright Line Test,' 13 J. of International Taxation 10 (Oct. 2002).
- <sup>19</sup> SFAS 131 deals with accounting for such items in specific industries: health maintenance, hospitality and publications.





