

# ***PCG 2021/D4 (Finalised) - Intangibles Arrangements***

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! This draft was re-released as PCG 2023/D2 Intangibles Arrangements on 17 May 2023 for further consultation.

! There is a Compendium for this document: **PCG 2024/1EC** .  
This document has been finalised.



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# Draft Practical Compliance Guideline

## Intangibles Arrangements

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### **❗ Relying on this draft Guideline**

This Practical Compliance Guideline is a draft for consultation purposes only. When the final Guideline issues, it will have the following preamble:

*This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. Provided you follow this Guideline in good faith, the Commissioner will administer the law in accordance with this approach.*

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### What this draft Guideline is about

1. This draft Guideline<sup>1</sup> sets out our compliance approach to international arrangements connected with the development, enhancement, maintenance, protection and exploitation (DEMPE) of intangible assets<sup>2</sup> and/or involving a migration of intangible assets. A 'migration' refers to any transaction or transactions that allows an offshore party to access, hold, use, transfer, or obtain benefits in connection with intangible assets and/or associated rights. These arrangements are collectively referred to as 'Intangibles Arrangements' in this Guideline

2. This Guideline applies to Intangibles Arrangements and focuses on tax risks associated with the potential application of the transfer pricing provisions.<sup>3</sup> It also focuses on other tax risks that may be associated with Intangibles Arrangements, specifically the withholding tax provisions<sup>4</sup>, capital gains tax (CGT)<sup>5</sup>, capital allowances<sup>6</sup>, the general

<sup>1</sup> All further references to 'this Guideline' refer to the Guideline as it will read when finalised. Note that this Guideline will not take effect until finalised.

<sup>2</sup> Intangible assets being property, assets and rights that are not physical or financial assets, which are capable of being controlled for use in commercial activities, and are not restricted by any accounting or legal concepts or definitions – see paragraphs 6.6 to 6.8 of Chapter VI of the *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, as approved by the Council of the Organisation for Economic Co-operation and Development (OECD) and last amended on 19 May 2017; see section 815-135(2)(a) of the *Income Tax Assessment Act 1997*. All legislative references in this Guidelines are to the *Income Tax Assessment Act 1997* unless otherwise indicated.

<sup>3</sup> As outlined in Division 815.

<sup>4</sup> As outlined in Subdivision 12-F of Schedule 1 to the *Taxation Administration Act 1953* (TAA).

<sup>5</sup> As outlined in Parts 3-1 and 3-3.

<sup>6</sup> As outlined in Division 40.

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anti-avoidance rule (GAAR)<sup>7</sup> and the diverted profits tax (DPT)<sup>8</sup>. All of these tax risks are relevant to our compliance approach and are collectively referred to as ‘compliance risks’ in this Guideline.

3. This Guideline has been prepared to accompany the release and publication of Taxpayer Alerts TA 2018/2 *Mischaracterisation of activities or payments in connection with intangible assets* and TA 2020/1 *Non-arm’s length arrangements and schemes connected with the development, enhancement, maintenance, protection and exploitation of intangible assets*.

4. It is not the intention of this Guideline to limit, deter or prevent arm’s length dealings involving intangible assets. Rather it is intended that this Guideline will serve as a point of reference and assist you to understand arrangements which we see as representing a higher risk from a compliance perspective.

5. We use the framework set out in this Guideline to assess the compliance risks associated with your Intangibles Arrangements and tailor our engagement with you.

6. You can use the framework set out in this Guideline to understand:

- the compliance risks that may be presented by your Intangibles Arrangements
- the type of analysis we undertake to assess compliance risks, and the documents and evidence we expect you to have and maintain to substantiate your Intangibles Arrangements
- the level of engagement we would generally expect from you based on our assessment of the compliance risks of your Intangibles Arrangements, and
- how you can work with us to mitigate any compliance risks in relation to your Intangibles Arrangements.

7. The application of this Guideline allows us to differentiate risk and prioritise our compliance resources. This Guideline will also outline the ways in which we are likely to engage with you based on the level of risk of your Intangibles Arrangements.

### Structure of this Guideline

8. The guidance contained in this Guideline is divided into the following parts:

- Part One – Our Compliance Approach – provides an outline of our compliance approach for Intangibles Arrangements.
- Part Two – Our Risk Assessment Framework – provides an outline of our risk assessment framework, which explains how we assess the compliance risks of Intangibles Arrangements.

9. This Guideline does not limit the operation of the law.<sup>9</sup> The information provided in this Guideline does not replace, alter or affect our interpretation of the law in any way or relieve you of your legal obligations in complying with all relevant tax laws.

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<sup>7</sup> As outlined in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936).

<sup>8</sup> As outlined in sections 177H to 177R of the ITAA 1936. Further information concerning the application of the DPT is available in Practical Compliance Guideline PCG 2018/5 *Diverted profits tax*, Law Companion Ruling LCR 2018/6 *Diverted profits tax* and Law Administration Practice Statement PS LA 2017/2 *Diverted profits tax assessments*.

<sup>9</sup> For example, this Guideline does not limit the operation of Subdivision 284-E of Schedule 1 to the TAA, which sets out special rules about unarguable positions for cross-border transfer pricing.

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10. If your Intangibles Arrangements are subject to review, you can expect that we will test the conditions and tax outcomes of your arrangements. We are not limited by this Guideline when testing the actual conditions of your Intangibles Arrangements for compliance with Australia's transfer pricing rules. Similarly, we are not limited by this Guideline when testing the purpose of your Intangibles Arrangements under the GAAR or DPT provisions, for example.

### **Date of effect**

11. When finalised, this Guideline is proposed to apply both before and after its date of issue.

## **PART ONE – OUR COMPLIANCE APPROACH**

### **The ATO's role and compliance approach**

12. We review Intangibles Arrangements with a focus on identifying those that mischaracterise Australian activities connected with DEMPE of intangible assets. We are concerned that these arrangements may be non-arm's length or structured to avoid tax obligations, resulting in inappropriate outcomes for Australian tax purposes. Our concerns include whether functions performed, assets used and risks assumed by Australian entities in connection with the DEMPE of intangible assets are properly recognised and remunerated in accordance with the arm's length requirements of the transfer pricing provisions in the taxation law.

13. Australia's income tax law places an onus on taxpayers to self-assess their compliance with relevant tax laws, including the transfer pricing rules.

14. The transfer pricing rules under Subdivision 815-B require taxpayers to assess whether the conditions of their international arrangements reliably reflect 'arm's length conditions', such that no transfer pricing benefit is obtained. Former Division 13 of Part III of the ITAA 1936 and Subdivision 815-A of do not require taxpayers to self-assess but allow the Commissioner to make a determination regarding the arm's length nature of a taxpayer's international related party arrangements.

15. In some cases, Subdivision 815-B may require the identification of arm's length conditions with regard to arrangements or circumstances different from the form of your Intangibles Arrangements (the exceptions to the basic rule contained in subsections 815-130(2) to (4)). In these cases, we will have specific regard to relevant ATO views, such as Taxation Ruling TR 2014/6 *Income tax: transfer pricing – the application of section 815-130 of the Income Tax Assessment Act 1997*.

16. To the extent relevant and applicable, any action we may take in applying the transfer pricing provisions will be made so as best to achieve consistency with the relevant transfer pricing guidelines published by the OECD.<sup>10</sup> Of particular relevance are Chapters I, VI and IX of the OECD TPG.

17. Chapter I of the 2017 edition of the OECD TPG outlines the basic operation of the arm's length principle. Our risk assessment approach follows this principle, having

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<sup>10</sup> See paragraphs 815-20(2)(a) and 815-135(2)(a). Of particular relevance are the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD TPG). The 2017 (latest) edition of these guidelines is relevant to income tax years commencing on or after 1 July 2017; the 2010 edition is relevant to income tax years commencing on or after 22 July 2010; the 1995 edition is relevant to income tax years commencing on or after 27 July 1995.

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particular regard to the accurate delineation of Intangibles Arrangements through an understanding of their economically relevant characteristics.

18. Chapter VI of the 2017 edition of the OECD TPG outlines special considerations for intangibles. Our risk assessment approach follows the principles discussed in Chapter VI regarding the identification and ownership of intangibles, the undertaking and control of DEMPE activities in connection with intangibles, and transactions involving the use or transfer of intangibles (or the rights to exploit them).

19. Chapter IX of the 2017 edition of the OECD TPG provides guidance on analysing transfer pricing outcomes in relation to business restructuring situations, examples of which include sales of assets or the relocation of business operations (that is, the transfer of functions, assets and risks). Specifically, it prescribes a two-step framework, whereby the arm's length nature of the restructuring itself must first be assessed before determining arm's length conditions for any post-restructuring controlled transactions.<sup>11</sup> Our risk assessment approach has particular regard to these principles in arrangements where we consider there to have been a migration of intangible assets.

20. We are also concerned that parties to such arrangements may fail to properly comply with Australian income tax obligations such as those imposed by the CGT and capital allowance provisions. We are particularly concerned where intangible assets and/or associated rights are migrated to international related parties as part of non-arm's length arrangements and/or in a manner intended to avoid Australian tax.

21. We also review arrangements to identify those that mischaracterise intangible assets and/or activities or conditions connected with intangible assets. Our concerns include whether intangible assets have been appropriately recognised for Australian tax purposes and whether Australian royalty withholding tax obligations, under Subdivision 12-F of Schedule 1 to the TAA, have been met.

22. In some cases, we may also consider the application of other income tax provisions, such as the GAAR and/or the DPT<sup>12</sup>, particularly in circumstances where such arrangements lack evidence of commercial rationale and/or substance. Where a taxpayer has obtained a tax benefit in connection with an Intangibles Arrangement, and the other legislative conditions are met, the Commissioner may cancel the tax benefit. Where a taxpayer has obtained a DPT tax benefit in connection with an Intangibles Arrangement, and the other legislative conditions are met, the Commissioner may issue a DPT assessment. In these circumstances, we will have specific regard to our internal processes, relevant ATO views and further guidance, which are documented in Law Administration Practice Statement PS LA 2005/24 *Application of General Anti-Avoidance Rules*, PCG 2018/5 and PS LA 2017/2.

23. This Guideline does not alter or supersede the guidance and processes outlined in the materials referred to in paragraph 22 of this Guideline, and should be considered alongside these materials where relevant to your Intangibles Arrangements. It does not relieve you of your obligation to self-assess your compliance with all relevant taxation laws; rather, it is designed to explain how we assess the risk posed by Intangibles Arrangements, enabling you to self-assess and mitigate your compliance risk with respect to your Intangibles Arrangements.

24. The level of engagement you can expect from us will be based on our assessment of the compliance risks of your Intangibles Arrangements. We explain how we will assess

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<sup>11</sup> Section E.2 of Chapter IX of the 2017 OECD TPG includes commentary specific to business restructures involving intangibles.

<sup>12</sup> As outlined in Part IVA of the ITAA 1936.

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the compliance risks of your Intangibles Arrangements and how we will engage with you under the framework set out in this Guideline.

25. We will typically apply our risk assessment framework to your Intangibles Arrangements and identify compliance risks associated with these arrangements in the course of our engagement or assurance activities. Our primary objective in the course of these activities is to obtain the information and documents necessary to gain assurance that the tax outcomes associated with your Intangibles Arrangements accord with the requirements of the relevant tax provisions. This is also the case where you have approached us voluntarily to assure your Intangibles Arrangements.

26. We encourage you to engage with us if, having considered the compliance risks presented by your arrangements in accordance with our risk assessment framework, you consider that there is a potential compliance risk associated with your Intangibles Arrangements. Engaging with us early, including prior to entering into your Intangibles Arrangement, will assist us to cooperatively work with you to assure your arrangement or resolve any issues that may be associated with your Intangibles Arrangements.

27. The advance pricing arrangement (APA) program can provide certainty with respect to covered Intangibles Arrangements for an agreed period.<sup>13</sup> Where you are seeking entry into the APA program, we would expect documentation and evidence of the nature identified in this Guideline to be produced and maintained with respect to your Intangibles Arrangements.

28. If we review your Intangibles Arrangements, we may consider other factors beyond those contained in this Guideline, having regard to relevant facts and circumstances of your Intangibles Arrangements.

29. We are committed to working with you to resolve any issues associated with your Intangibles Arrangements as early and cooperatively as possible.

30. Where we are unable to resolve disputes that may arise in respect of your Intangibles Arrangements under our compliance approach, you will be able to access your review and objection rights, where and when relevant.

### ***Reporting your self-assessment***

31. If you are required to complete a reportable tax position (RTP) schedule, you may be asked to disclose:

- how your Intangibles Arrangements compare to each of the Risk Factors in Appendix 1 of this Guideline, specifically whether your Intangibles Arrangements exhibit Risk Factors that have been described as High, Medium or Low Risk Factors, and/or
- how your Intangibles Arrangements compare to the Examples of Arrangements in Appendix 2 of this Guideline, specifically whether you have entered into any arrangement or variation of an arrangement described in the High, Medium or Low Risk examples, or
- that you chose not to, or could not, self-assess your risk.

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<sup>13</sup> Refer to PCG 2018/5 for further information with respect to how DPT matters may be considered in an APA.

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### **Evidencing your self-assessment**

32. We may, in the course of our ordinary engagement and assurance activities, or any specific assurance activity relating to this Guideline, fact-check your self-assessment, having regard to our Documentation and Evidence Expectations as outlined in paragraphs 42 to 74 of this Guideline. If you are unable to provide adequate evidence to support your assessment, or we disagree with your assessment, we may undertake further engagement and assurance activity.

## **PART TWO – OUR RISK ASSESSMENT FRAMEWORK**

33. Our compliance approach will vary depending on the level of risk presented by your Intangibles Arrangements. This part is designed to explain how we assess the compliance risks of Intangibles Arrangements.

34. Our risk assessment framework includes an assessment of the risk of your Intangibles Arrangements based on:

- Risk Factors (set out in Appendix 1 of this Guideline) which outline features and Examples of Arrangements that we will use to inform our assessment of the compliance risks in your Intangibles Arrangements, and
- Documentation and Evidence Expectations (set out in paragraphs 42 to 74 of this Guideline), including the level of evidence that we will have regard to when assessing your Intangibles Arrangements against the Risk Factors to assess the level of risk posed by your arrangement.

35. The Risk Factors include High, Medium and Low Risk Factors and focus on:

- understanding and evidencing the commercial considerations and your decision making, in particular where you have restructured or had a change associated with your Intangibles Arrangements
- understanding the form of your Intangibles Arrangements
- identifying and evidencing the intangible assets and connected DEMPE activities of your Intangibles Arrangements
- analysing the tax and profit outcomes of your Intangibles Arrangements, and
- understanding the type of example arrangements we consider to be High, Medium or Low risk, which have been described in Appendix 2 of this Guideline.

36. We will have regard to each of the Risk Factors to inform our assessment of the compliance risks of your Intangibles Arrangements, including how we will engage with you. The Risk Factors serve as general guidance only and do not form an exhaustive list of features or examples of arrangements we may consider when assessing the level of risk posed by your Intangibles Arrangements.

37. The Examples of Arrangements, as detailed in Risk Factor E in Appendix 1 of this Guideline, and further set out in Appendix 2 of this Guideline, provide practical guidance to determine the level of risk presented by your Intangibles Arrangements. The examples are categorised into High, Medium and Low risk examples. Appendix 2 of this Guideline will be updated where new or emerging examples of arrangements are identified.

38. In the course of our engagement and assurance activities, we may seek information and/or documents regarding the facts and circumstances of your Intangibles



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Arrangements in order to validate or assess the Risk Factors as they relate to your Intangibles Arrangements. The information and documents that we would typically seek are outlined in paragraphs 42 to 74 of this Guideline. We would expect detailed documentation of the nature identified in this Guideline to be produced and maintained with respect to your Intangibles Arrangements.

39. If your Intangibles Arrangements exhibit one or more of the High Risk Factors, our compliance approach will likely include further engagement with you to assess the compliance risks of your Intangibles Arrangements. This may involve commencing a further review or audit. We will typically prioritise our resources to address Intangibles Arrangements that pose the highest level of risk. In these circumstances, our expectation is that you provide us with information and documentation, having regard to the Documentation and Evidence Expectations as outlined in paragraphs 42 to 74 of this Guideline, so that we can substantiate your Intangibles Arrangements.

40. While exhibiting Medium or Low Risk Factors may not exclude your Intangibles Arrangements from further review, they will influence our engagement with you. Improving your documentation and having contemporaneous evidence to substantiate your arrangement will also assist you to substantiate Medium or Low Risk Factors that your Intangibles Arrangements may exhibit and mitigate the level of compliance risk posed by your Intangibles Arrangements.

41. Where you are seeking entry to the APA program, we will have regard to the Risk Factors that your Intangibles Arrangements exhibit, including the documentation you have maintained according to our Documentation and Evidence Expectations. If your documentation does not substantiate your arrangement, it may limit our ability to provide you with greater certainty and/or engage in APA discussions. We will be open to entering into early engagement APA discussions with you and will be more likely to invite you to make a formal APA application where your Intangibles Arrangements exhibit the Low Risk Factors and you are able to substantiate your Intangibles Arrangements according to our Documentation and Evidence Expectations.

### **Documentation and Evidence Expectations**

42. This section outlines documentation and evidence we would generally expect when assessing the level of compliance risk posed by your Intangibles Arrangements according to our risk assessment framework. It sets out the type and level of documentation that we will have regard to when assessing your Intangibles Arrangements against the Risk Factors.

43. The documents outlined in this section are intended to serve as a general guide and should not be treated as an exhaustive list of the kinds of documents, evidence and matters we may take into account in the event we need to review your Intangibles Arrangements.

44. We recognise that certain documents identified in this section may not be relevant to the facts and circumstances of your Intangibles Arrangements or that it may be difficult for you to assess the degree of documentation that is required to assess the risk of your Intangibles Arrangements. The Risk Factors are designed to assist you in this regard.

45. The type and level of documentation we will expect from you will be influenced by the complexity of your arrangement. We will take into consideration your natural business systems and governance processes and systems to focus on documentation and evidence that can reasonably be expected to be created and relied on in your business, taking into account the compliance risks involved with your Intangibles Arrangements.

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46. The Documentation and Evidence Expectations outlined in this section will assist you in assessing whether you have maintained documentation that adequately supports and substantiates the position you have taken with respect to your Intangibles Arrangements and your risk assessment according to our risk assessment framework. The Documentation and Evidence Expectations outlined in this section may also assist you in supporting and/or verifying your transfer pricing documentation for the purposes of Subdivision 284-E of Schedule 1 to the TAA (refer to Taxation Ruling TR 2014/8 *Income tax: transfer pricing documentation and Subdivision 284-E*).

47. As a preliminary matter, we will typically review the following information in our possession, where relevant, including (and depending on) whether you have relevant international related party dealings, are a significant global entity (SGE) and/or have disclosed a relevant Category C reportable tax position<sup>14</sup>:

- Australian income tax returns
- general purpose financial statements
- International Dealings Schedules
- Country-by-Country reporting data exchanged automatically or by exchange of information request, including any available Masterfile, Local File Parts A and B and/or Country-by-Country Report
- information obtained from foreign jurisdictions through exchange of information processes, and
- other information obtained previously by the ATO in connection with any engagement or review, and other relevant information from third party / public sources or other government agencies.

48. The Documentation and Evidence Expectations outlined in this section are categorised as:

- understanding and evidencing the commercial considerations and your decision making
- understanding the legal form of your intangibles arrangements
- identifying and evidencing the intangible assets and connected DEMPE activities, and
- analysing the tax and profit outcomes of your intangibles arrangements.

#### ***Understanding and evidencing the commercial considerations and your business decisions***

49. In circumstances where you have restructured or had a change associated with your Intangibles Arrangements, we will typically require an understanding of the circumstances in which the restructure or change was entered into or occurred. We will typically require contemporaneous documents to verify the market value of any intangibles acquired or sold, identify and evidence any tax and commercial objectives considered and any other considerations connected with the decision to enter into the restructure or arrangement, including whether other or alternative arrangements were considered and the reasons why any alternative arrangements were not pursued. This information is

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<sup>14</sup> We refer to the self-assessment obligations referenced in paragraph 31 of this Guideline, as well as Category C reportable tax positions relating to TA 2018/2 (Question 25) and TA 2020/1 (Question 32).

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integral to, and an important part of, our assessment of the commerciality of your Intangibles Arrangements and potential compliance risks.

50. The evidence we may require includes:

- (a) internal or independent reviews, cost-benefit analyses, forecasts, projections, modelling, reports or advice commissioned or obtained in relation to your Intangibles Arrangements and associated commercial objectives – this could include quantifiable productivity gains, cost savings, synergistic benefits, location/jurisdiction-specific benefits, reduction of non-income tax costs, provision of connected government incentives and any other relevant costs and benefits associated with your Intangibles Arrangements
- (b) the documents created or provided by personnel or tax advisers disclosing anticipated or potential Australian tax effects of the Intangibles Arrangements, including financial models disclosing projected or potential tax impacts and slides or step plans in connection with developing arrangements
- (c) briefing materials, analysis and data produced in connection with the documents outlined in paragraph 50(a) of this Guideline, including those produced by or for internal and independent specialists
- (d) presentations and other papers prepared in relation to your Intangibles Arrangements and associated commercial objectives, including papers provided to the taxpayer's management team, board of directors or any other group or subgroup responsible for considering or making recommendations on the arrangements
- (e) minutes of board and other meetings at which all Intangibles Arrangements, including alternative arrangements not pursued, were considered and any correspondence with tax advisers or tax personnel in relation to preparing or revising the minutes
- (f) commercial, regulatory and tax advice obtained in connection with your Intangibles Arrangements
- (g) details of any changes to the transfer pricing policy in the relevant period, including the rationale for any such changes and the pricing and profit outcomes before and after the change event for all parties connected to your Intangibles Arrangements (for example, reports documenting functional analyses undertaken for relevant entities, correspondence exchanged between key decision makers regarding the benefits of certain structures, and actuarial reports of cost modelling), and
- (h) details of any changes to inter-company agreements and company policies in the relevant period.

### ***Understanding the legal form of your Intangibles Arrangements***

51. To assess the compliance risks presented by your Intangibles Arrangements, we must understand the specific transactions entered into as part of your Intangibles Arrangements. We will require the documents that disclose the detailed legal form of your Intangibles Arrangements to assist us in understanding your Intangibles Arrangements in totality.

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52. The evidence we may require to understand the legal form of your Intangibles Arrangements includes:

- (a) legal agreements, memoranda and like documents associated with your Intangibles Arrangements, including any amendments to, or restatements of, such documents
- (b) details of ownership of intangible assets, including whether ownership rights in the intangible asset may have been diluted
- (c) details of the planning in connection with setting up the legal arrangements or entering into legal documentation, for example, planning on choice of employees or officers to be appointed as directors of new entities and policies to protect intangible assets
- (d) guidelines, manuals, policies, procedures, specifications and like documents relevant to your Intangibles Arrangements that are developed and/or maintained by you, your global group, a related party or a third party under the direction of you, your global group or a related party. This includes any such documents that instruct and detail conduct of parties with any connection to the Intangibles Arrangements, the relevant intangible assets and the connected DEMPE activities, and
- (e) transfer pricing documentation including any specific or supplementary analysis or valuation and/or other reports produced for transactions which form part of your Intangibles Arrangements.

#### ***Legal agreements***

53. Obtaining the legal agreements, memoranda and other documents associated with your Intangibles Arrangements allows us to form a preliminary view of your Intangibles Arrangements, which includes all relevant intangible assets, associated activities and entities involved in the arrangements. This includes, for example, relevant asset purchase agreements, sale agreements, royalty or licensing agreements, associated contract research and development (R&D) service agreements with international related parties, including any amendments to, or restatements of, such agreements.

54. Where legal agreements are not yet drafted or are subject to change, we may require available draft or interim agreements, memoranda or like documents. If relevant agreements and documents are subject to change, this will impact our ability to determine the level of risk presented by your Intangibles Arrangements. In these circumstances we may be unable to provide you with greater certainty regarding your tax outcomes.

55. We may also request relevant agreements or other documents between other international related parties and, in certain circumstances, third parties to allow us to obtain a holistic understanding of your global group's Intangibles Arrangements. For example, where international related parties with which the Australian entity has entered into agreements have similar or dissimilar arrangements with other international related parties in connection with intangible assets.

#### ***Guidelines, manuals, policies and governance-like documents***

56. Obtaining your internal guidelines, manuals, policies, procedures, specifications, governance and like documents relevant to your Intangibles Arrangements allows us to establish whether you, your global group, or relevant international related parties have policies and work processes in place that are of relevance to your arrangements. This

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includes, for example, relevant group intellectual property management policies evidencing whether intangible assets are managed by a central team, R&D policies or other policies concerning the development, management and commercialisation of your intangible assets.

57. These facts and documents enable us to understand the broader circumstances surrounding your Intangibles Arrangements and inform our assessment of risk. For example, we may have concerns where your group intellectual property management and R&D policies appear to be inconsistent with your legal agreements or your actual conduct or dealings with other parties in relation to the intangible assets.

#### *Transfer pricing documentation*

58. Obtaining your transfer pricing documentation allows us to gain an overall understanding of the operation of your Intangibles Arrangements, including the identification of all relevant intangible assets, entities, activities and associated transfer pricing outcomes. This documentation allows us to assess the degree to which your transfer pricing analysis supports the arm's length nature of your Intangibles Arrangements, which would inform our risk assessment.

59. We may also compare your transfer pricing documentation with your group intellectual property management and R&D policies, legal agreements with international related parties and/or your actual conduct or dealings with other parties in relation to the intangible assets to better understand your Intangibles Arrangements.

#### *Country-by-Country reporting documentation*

60. If you are an SGE, we will also consider information provided as a part of any available Country-by-Country reporting documentation, such as agreements provided in Part B of your local file and master file documentation. We may request further information, such as the underlying data and records that you used to prepare your Country-by-Country reporting.

#### ***Identifying and evidencing the intangible assets and connected development, enhancement, maintenance, protection and exploitation activities***

61. The identification of relevant intangible assets and connected DEMPE activities is critical to assessing the level of compliance risks presented by your Intangibles Arrangements. As such, in addition to obtaining an understanding of the legal form of your Intangibles Arrangements, we will seek to identify and/or clarify relevant intangible assets and connected DEMPE activities in more specific detail. We will do so to clarify how your Intangibles Arrangements operate in substance and mitigate any uncertainty arising from your legal form documents.

62. We may also require specific documents and evidence to identify and clarify your intangible assets and DEMPE activities due to the:

- difficulties you may encounter in identifying and tracking intangible assets through the various stages of development, commercialisation and exploitation
- fact that certain intangible assets may be intrinsically connected or linked to certain other assets or DEMPE activities

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- ease with which certain intangible assets and DEMPE activities may be altered or moved, and
- complex nature of a multinational group's value chains connected with intangible assets and DEMPE activities.

63. These issues necessitate discussions with management and or the review of specific documentation to inform our risk assessment.

#### *Identifying intangible assets*

64. The documents and evidence we may require you to identify and clarify intangible assets relevant to your Intangibles Arrangements include documents which detail, describe and evidence the names/identifiers and functions of relevant intangible assets and the products, processes or other relevant commercial activities they are associated with. We will also seek to obtain evidence of the nature of relevant assets (for example, copyright, patent, design or model, plan, know-how, secret formula or process, trademark or other like property or right) and whether such assets have been registered. Our document and evidence expectations extend to know-how assets relating to business processes, interpretation of data, a valuable concept or business innovation not able to be registered.

65. The evidence we may require includes:

- intangible asset registers
- AASB Standard 138-compliant<sup>15</sup> financial statements and associated records or documents relevant to the recognition of intangible assets
- registration documents, such as those required by and produced for IP Australia
- internal or external database extracts or other relevant digital or physical records
- relevant reports, specifications or R&D stage-gate documents, particularly where intangible assets are in development or in a pre-commercialised state
- guidelines, manuals, policies, procedures and like documents relevant to the identification and recognition of relevant intangible assets of you or of members of your global group, including governance documents over approval of business plans where know-how is reflected in decision-making accountability, and
- any additional or like documents that may assist us in identifying and understanding relevant assets.

#### *Identifying development, enhancement, maintenance, protection and exploitation activities*

66. We may require contemporaneous documentation and evidence to clarify the DEMPE activities connected with your Intangibles Arrangements in more specific detail. We expect that the functions performed, assets used and risks assumed by relevant entities in connection with the DEMPE of intangible assets will be detailed in your transfer

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<sup>15</sup> Australian Accounting Standards Board [AASB] Standard 138 *Intangible Assets* as applicable to the reporting period in question. The current standard is available at: <https://www.aasb.gov.au/Pronouncements/Current-standards.aspx>. AASB 138 as applicable to earlier reporting periods can be found at: <https://www.aasb.gov.au/Pronouncements/Search-by-reporting-period.aspx>

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pricing documentation. We may seek to clarify this information, for example, by obtaining correspondence of persons involved in DEMPE activities or by identifying and interviewing specific personnel involved in DEMPE activities, relevant decision makers and approval points and any activities outsourced to third or related parties.

67. The evidence we may require includes:

- (a) organisational charts, including description of roles and responsibilities of individuals involved in DEMPE activities
- (b) correspondence of persons identified as involved in DEMPE activities
- (c) guidelines, manuals, policies, procedures and like documents relevant to you, your global group's or your international related parties' DEMPE activities
- (d) internal or external database extracts or other relevant digital or physical records relating to DEMPE activities
- (e) relevant reports, specifications or R&D stage-gate documents associated with DEMPE activities
- (f) documents associated with any R&D tax incentive claims lodged with the Department of Industry, Innovation and Science, and
- (g) any additional or like documents that may assist us in identifying and understanding your DEMPE activities.

*Evidencing intangible assets and development, enhancement, maintenance, protection and exploitation activities*

68. We may also seek to obtain evidence to substantiate aspects of your legal form documents, the nature of relevant intangible assets and aspects of DEMPE activities. We request this information to obtain assurance that the substance of your Intangibles Arrangements aligns with the legal form of the arrangement and consider whether there are any associated compliance risks.

69. We may require documents to ensure that the obligations outlined in your legal form arrangements are consistent with what is occurring in practice. We will analyse the functions performed by relevant entities in connection with the Intangibles Arrangements with reference to specific clauses in legal agreements, group policies, correspondence and/or transfer pricing documentation. We may also require information and documents, including email correspondence, which demonstrate that entities stated to manage, control and/or perform DEMPE activities and assume associated risks have the capability, financial capacity and assets to do so in substance.

70. The evidence we may require includes:

- (a) approvals, authorisations, correspondence and meeting minutes which demonstrate that the DEMPE activities undertaken by relevant entities are consistent with those specified in your legal form agreements, for example, directions and approvals received from entities that manage and control risks associated with DEMPE activities
- (b) meeting minutes, reports, scopes of work, internal or external database extracts or other relevant digital or physical records which demonstrate functions performed, assets used and risks assumed in connection with DEMPE activities

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- (c) documents detailing the assets and capabilities of relevant entities, including relevant employment contracts and key performance indicators, employee head count and qualifications, and planning documents
- (d) documents detailing the financial position of relevant entities and profit outcomes associated with your Intangibles Arrangements, including general purpose financial statements, accounts and annual reports
- (e) contemporaneous valuation reports, working papers and associated documentation where intangible assets and relevant functions have been transferred offshore, and
- (f) any additional or like documents that may assist us in identifying and understanding your DEMPE activities.

### ***Analysing the tax and profit outcomes of your Intangibles Arrangements***

71. We may require documents to assess the appropriateness of the tax and profit outcomes resulting from your arrangements, including the transfer pricing method and comparability studies applied, where relevant.

72. The evidence we may require includes:

- (a) comparability studies, valuations, projections and other analyses which have been obtained or applied to determine the nature and quantum of transactions executed under the arrangement, including any connected advice obtained from internal or independent specialists
- (b) any financial modelling or projections, including models of anticipated tax impacts of options or arrangements prepared by tax personnel or tax advisers
- (c) analyses, data and briefing materials underlying any valuations, projections, other analyses and connected advice obtained from internal or independent specialists that have been applied to determine the nature and quantum of transactions executed under the arrangement
- (d) evidence of actual cash flows in connection with the arrangement
- (e) financial, transactional and tax information for relevant domestic and offshore entities, including general purpose financial statements, accounts, annual reports, general ledger entries and other accounting or reporting documentation where relevant, and
- (f) tax information for relevant domestic and offshore entities including foreign income tax returns, foreign notices of assessment (or equivalent), foreign tax receipts and notices of refund (or equivalent), foreign tax instalment notices and running balance accounts (or equivalent), any advice or valuations obtained in relation to the potential tax consequences of proposed structures or transactions, any approvals of tax holidays or other reductions in tax and relevant correspondence from foreign revenue agencies.

### ***Simplified record keeping***

73. If you are eligible to apply any of the simplified transfer pricing record-keeping options under Practical Compliance Guideline PCG 2017/2 *Simplified transfer pricing*



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*record-keeping options*, we will have regard to the record-keeping obligations outlined in PCG 2017/2, where relevant.

74. PCG 2017/2 is not available to small taxpayers and distributors in relation to international related-party dealings involving royalties, licence fees or R&D arrangements. We note:

- The performance of DEMPE functions that materially contribute to the value of intangible assets, as described in this Guideline, will not fall within the definition of 'low value adding intra-group services' for the purposes of PCG 2017/2.
- Technical services considered under PCG 2017/2 also exclude the use of intellectual property, know-how, processes, systems or other like intangible assets or rights.

Status: **draft only – for comment****APPENDIX 1 – Risk Factors**

<b>Risk focus areas – Intangibles Arrangements</b>	<b>High risk factors</b>	<b>Medium risk factors</b>	<b>Low risk factors</b>
A. Understanding and evidencing the commercial considerations and your decision making, in particular where you have restructured or had a change associated with your Intangibles Arrangements	<ul style="list-style-type: none"> <li>• Your documentation and evidence does not substantiate the commercial considerations and associated decision making actually undertaken with respect to your Intangibles Arrangements.</li> <li>• Your documentation and evidence does not substantiate that there was due consideration and assessment of the commercial options realistically available as alternatives to your Intangibles Arrangements, disregarding any anticipated tax effects.</li> <li>• Your documentation and evidence does not substantiate any clear quantifiable, non-tax financial benefits of your Intangibles Arrangements.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence relating to the commercial considerations and associated decision making actually undertaken with respect to your Intangibles Arrangements is incomplete.</li> <li>• Your documentation and evidence relating to whether there was due consideration and assessment of the commercial options realistically available as alternatives to your Intangibles Arrangements is incomplete, disregarding any anticipated tax effects.</li> <li>• Your documentation and evidence relating to whether there are clear quantifiable, non-tax financial benefits of your Intangibles Arrangements is incomplete.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence substantiates the commercial considerations and associated decision making actually undertaken with respect to your Intangibles Arrangements.</li> <li>• Your documentation and evidence substantiates that there was due consideration and assessment of the commercial options realistically available as alternatives to your Intangibles Arrangements, disregarding any anticipated tax effects.</li> <li>• Your documentation and evidence substantiates clear quantifiable, non-tax financial benefits of the Intangibles Arrangements which outweigh anticipated tax effects.</li> </ul>
B. Understanding the form of your Intangibles Arrangements	<ul style="list-style-type: none"> <li>• The form of your Intangibles Arrangements is not substantiated by the documents or evidence, such as legal agreements, correspondence of relevant persons, your internal guidelines, manuals, policies, procedures, governance and like</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence relating to the form of your Intangibles Arrangements, including legal agreements, correspondence of relevant persons, your internal guidelines, manuals, policies, procedures, governance and like</li> </ul>	<ul style="list-style-type: none"> <li>• The form of your Intangibles Arrangements is substantiated by the documents, such as legal agreements, correspondence of relevant persons, your internal guidelines, manuals, policies, procedures, governance and like</li> </ul>

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	<p>documents relevant to your arrangement.</p> <ul style="list-style-type: none"> <li>• Your documentation and evidence does not substantiate that the form of your Intangibles Arrangements is consistent with the substance of your arrangements.</li> <li>• Your documentation and evidence does not substantiate your characterisation of any payments made under your arrangements, including recognising an amount in the nature of a royalty where relevant (for example, TA 2018/2 arrangements).</li> </ul>	<p>documents relevant to your arrangement is incomplete.</p> <ul style="list-style-type: none"> <li>• Your documentation and evidence relating to whether the form of your Intangibles Arrangements is consistent with the substance of the arrangement is incomplete.</li> <li>• Your documentation and evidence relating to your characterisation of any payments made under your arrangements, including recognising an amount in the nature of a royalty where relevant, is incomplete (for example, TA 2018/2 arrangements).</li> </ul>	<p>documents relevant to your arrangement.</p> <ul style="list-style-type: none"> <li>• Your documentation and evidence substantiates that the form of your Intangibles Arrangements is consistent with the substance of the arrangements.</li> <li>• Your documentation and evidence substantiates your characterisation of any payments made under your arrangements, including recognising an amount in the nature of a royalty where relevant (for example, TA 2018/2 arrangements).</li> </ul>
C. Identifying and evidencing the intangible assets and connected DEMPE activities of your Intangibles Arrangements	<ul style="list-style-type: none"> <li>• Your documentation and evidence does not identify the intangible assets connected with your Intangibles Arrangements with specificity.</li> <li>• Your documentation and evidence does not substantiate the DEMPE activities connected with your Intangibles Arrangements, including how such activities generate value.</li> <li>• Your documentation and evidence does not substantiate that the entities stated to primarily manage, perform and control DEMPE activities and assume associated risks have the necessary capability, financial capacity and/or assets to do so in substance.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence relating to the specific identification of intangible assets connected with your Intangibles Arrangements is incomplete.</li> <li>• Your documentation and evidence relating to the DEMPE activities connected with your Intangibles Arrangements, including how such activities generate value, is incomplete.</li> <li>• Your documentation and evidence relating to whether the entities stated to primarily manage, perform and control DEMPE activities and assume associated risks have the necessary capability, financial capacity and/or assets to do so in substance is incomplete.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence identifies the intangible assets connected with your Intangibles Arrangements with specificity.</li> <li>• Your documentation and evidence substantiates the DEMPE activities connected with your Intangibles Arrangements, including how such activities generate value.</li> <li>• Your documentation and evidence substantiates that the entities stated to primarily manage, perform and control DEMPE activities and assume associated risks have the necessary capability, financial capacity and/or assets to do so in substance.</li> </ul>

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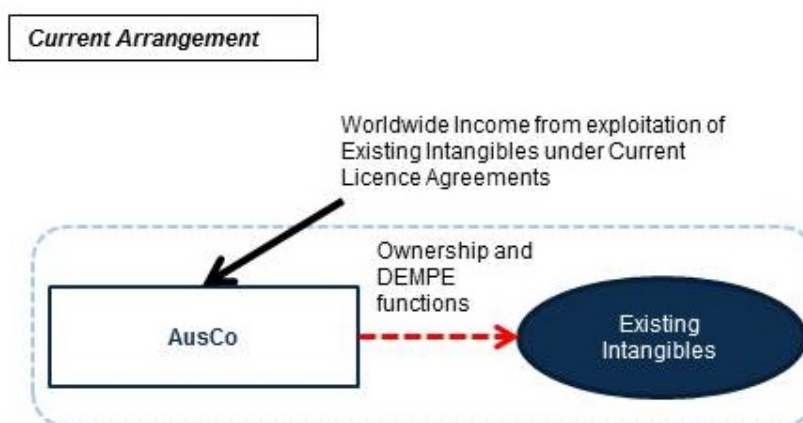
D. Analysing the tax and profit outcomes of your Intangibles Arrangements	<ul style="list-style-type: none"> <li>• Your documentation and evidence does not substantiate that the economic outcomes and benefits obtained by relevant entities in connection with intangible assets align with their contributions to DEMPE activities, having regard to functions performed, assets used and risk assumed.</li> <li>• Your documentation and evidence does not substantiate that the tax and profit outcomes are consistent with the commercial or economic substance of your Intangibles Arrangements.</li> <li>• Your documentation evidencing the determination of transfer pricing methods, valuations, projections and/or other analyses that have influenced the characterisation and quantum of transactions executed under your Intangibles Arrangements is not consistent with the anticipated tax and non-tax benefits actually considered in deciding to enter the arrangements, or relies on inadequate, non-contemporaneous and/or unreliable analysis or data.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence relating to whether the economic outcomes and benefits obtained by relevant entities in connection with intangible assets all align with their contributions to DEMPE activities, having regard to functions performed, assets used and risk assumed is incomplete.</li> <li>• Your documentation and evidence relating to whether the tax and profit outcomes are consistent with the commercial or economic substance of your Intangibles Arrangements is incomplete.</li> <li>• Your documentation and evidence relating to the determination of transfer pricing methods, valuations, projections and/or other analyses that have influenced the characterisation and quantum of transactions executed under your Intangibles Arrangements relies on incomplete analysis or data.</li> </ul>	<ul style="list-style-type: none"> <li>• Your documentation and evidence substantiates that the economic outcomes and benefits obtained by relevant entities in connection with intangible assets align with their contributions to DEMPE activities, having regard to functions performed, assets used and risk assumed.</li> <li>• Your documentation and evidence substantiates that the tax and profit outcomes are consistent with the commercial or economic substance of your Intangibles Arrangements.</li> <li>• Your documentation and evidence relies on adequate, contemporaneous and reliable analysis or data to determine transfer pricing methods, valuations, projections and/or other analyses that have influenced the characterisation and quantum of transactions executed under your Intangibles Arrangements.</li> </ul>
E. Understanding the type of example arrangements we consider to be high, medium or low risk, as described in Appendix 2 of this Guideline	<ul style="list-style-type: none"> <li>• Your Intangibles Arrangements exhibit features or characteristics of the high risk examples described in Appendix 2 of this Guideline or the arrangements described in TA 2018/2 or TA 2020/1.</li> </ul>	<ul style="list-style-type: none"> <li>• Your Intangibles Arrangements exhibit features or characteristics of the medium risk examples described in Appendix 2 of this Guideline.</li> </ul>	<ul style="list-style-type: none"> <li>• Your Intangibles Arrangements exhibit features or characteristics of the low risk examples described in Appendix 2 of this Guideline.</li> </ul>

Status: **draft only – for comment****APPENDIX 2 – Risk Factor E – Examples of Arrangements**

75. Appendix 2 of this Guideline provides examples of Intangibles Arrangements that we will use to assess the level of risk of your Intangibles Arrangements based on Risk Factor E of our Risk Factors Appendix 1 of this Guideline. The examples in this Guideline are categorised as High, Medium and Low risk.

76. The examples in Appendix 2 of this Guideline are provided to illustrate the kinds of matters we will generally consider in assessing the compliance risks relating to your Intangibles Arrangements. They highlight the circumstances in which we consider the different compliance risks that may be associated with your Intangibles Arrangements and the facts that may support this assessment. Any reference to a particular intangible asset, industry or commercial activity in the examples is anecdotal and does not limit the particulars of an arrangement to any one industry.

Level of risk	Examples of Arrangements
<b>High risk</b>	Example 1 – centralisation of intangible assets Example 2 – bifurcation of intangible assets Example 3 – non-recognition of Australian intangible assets and DEMPE activities Example 4 – migration of pre-commercialised intangible assets Example 5 – non-arm's length licence arrangements
<b>Medium risk</b>	Example 6 – centralisation of intangible assets Example 7 – transfer of rights to intangible assets via a Licence Agreement Example 8 – contract research and development arrangement Example 9 – cost contribution arrangement
<b>Low risk</b>	Example 10 – centralisation of intangible assets Example 11 – contract research and development arrangement Example 12 – cost contribution arrangement

**Example 1 – centralisation of intangible assets – high risk**

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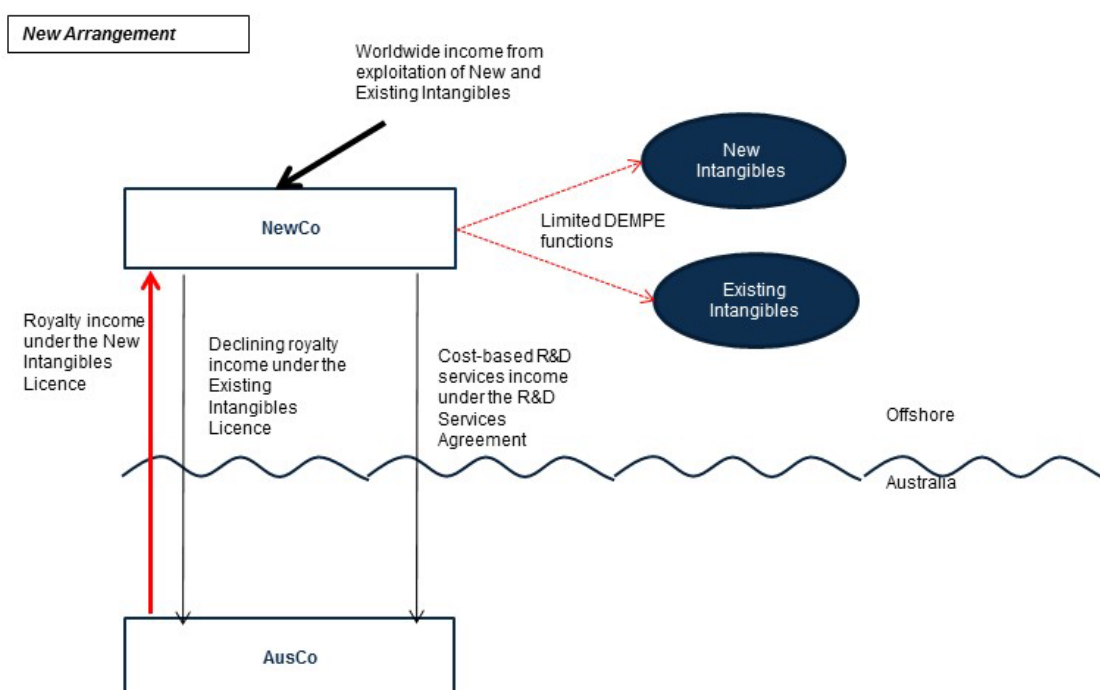
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**Current Arrangement**

77. AusCo is part of a global group that manufactures, markets and sells goods and provides services associated with those sales. AusCo and its international related parties exploit valuable intangible assets in undertaking their operations. The intangible assets include patents, know-how trademarks, copyright and other intangible assets or rights (Existing Intangibles).

78. AusCo owns, manages and controls DEMPE activities associated with the Existing Intangibles and assumes associated risks. AusCo derives royalties from its international related parties for the exploitation of the Existing Intangibles globally under current licence agreements between AusCo and its international related parties (Current Licence Agreements).

**Decision to centralise intangible assets**

79. AusCo and the global group decide that the Existing Intangibles and any new or future intangible assets that are created or developed (New Intangibles) should be centralised in a new entity (NewCo) to be located in a foreign jurisdiction. The New Intangibles will initially comprise adaptations of the patents, know-how, trademarks, copyright and other intangible assets or rights that form part of the Existing Intangibles. The documentation maintained or provided by AusCo does not substantiate the commercial rationale underpinning the decision to centralise.

80. As a result of the decision to centralise, AusCo enters into a licence agreement (Existing Intangibles Licence) with NewCo to transfer the rights to the Existing Intangibles to NewCo. The term of the Existing Intangibles Licence is based on a period determined to reflect the remaining useful life of the Existing Intangibles at the time. Under the Existing Intangibles Licence, NewCo will pay royalties to AusCo for the right to exploit and sub-licence the Existing Intangibles to other international related parties, including AusCo.

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*These royalties decline over the term of the Existing Intangibles Licence and are based on a formula designed to reflect the declining value of the Existing Intangibles over the term of the Existing Intangibles Licence. The documentation maintained or provided by AusCo does not substantiate the arm's length nature of the pricing of this arrangement.*

81. *The Current Licence Agreements between AusCo and its international related parties are terminated as a result of the decision to centralise. No payments were made to AusCo as a result of the termination. AusCo and its international related parties subsequently execute a master Licence Agreement with NewCo (New Intangibles Licence). Under this agreement, NewCo receives worldwide royalty income from the rights to exploit the Existing Intangibles and any New Intangibles developed.*

82. *NewCo and AusCo also enter into a contract R&D Services Agreement. Under this agreement, AusCo will provide R&D services to NewCo in relation to the New Intangibles in return for a fee determined with regard to the costs incurred by AusCo in the provision of the R&D services. Any New Intangibles that are developed as a result of the R&D undertaken by AusCo under the R&D Services Agreement will be owned by NewCo and AusCo's use of those New Intangibles will be subject to the New Intangibles Licence.*

#### *New Arrangement*

83. *In the first year following the centralisation of the intangible assets in NewCo, the functions performed, assets used and risks assumed by AusCo do not substantially change. AusCo continues to employ the same specialised staff and use its expertise and assets to manage, perform and control DEMPE activities associated with the New Intangibles. While the development of the Existing Intangibles ceased as a result of the New Arrangement, AusCo continued to perform and control the management and exploitation of the Existing Intangibles. The functions performed, assets used and risks assumed by AusCo under the R&D Services Agreement with NewCo results in the development of New Intangibles. The R&D Services Agreement states that the New Intangibles are owned by NewCo. The use of the New Intangibles is subject to the New Intangibles Licence, where AusCo and its international related parties pay royalties to NewCo. NewCo manages and performs limited DEMPE activities and assumes limited risks in connection with the Existing Intangibles or the New Intangibles.*

84. *In the second year following the centralisation of the intangible assets to NewCo, NewCo hires some additional staff and acquires additional assets to assist it in the management of DEMPE activities. These staff and assets are not sufficient to allow NewCo to wholly manage, perform or control the DEMPE activities connected with the New Intangibles and the Existing Intangibles and assume the associated risks. AusCo continues to undertake the majority of the DEMPE activities while receiving a cost-based remuneration under the R&D Services Agreement and declining royalties under the Existing Intangibles Licence. NewCo receives royalty income from AusCo and its international related parties for the use and exploitation of the Existing Intangibles and New Intangibles.*

#### *Risk assessment*

85. *The New Arrangement would be regarded as a High Risk Intangibles Arrangement.*

86. *There is a risk that AusCo's entry into the New Arrangement is not commercially rational and may not be consistent with AusCo's best economic interests having regard to the commercial options realistically available to it, disregarding anticipated or potential tax impacts. This risk is emphasised where AusCo has not maintained or is not able to provide documentation substantiating its decision-making regarding entering into the New*

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*Arrangement or does not recognise or provide documents referring to anticipated or potential Australian tax impacts considered in making the decision to centralise.*

87. *AusCo continued to perform and control DEMPE activities with respect to the Existing Intangibles and the New Intangibles, which in economic substance was inconsistent with terms and conditions of the various licences and the R&D Services Agreement between AusCo and NewCo under the New Arrangement. The New Arrangement does not appropriately recognise AusCo's contributions to the New Intangibles, either through a recognition of the intrinsic link between the Existing and New Intangibles or a recognition of the DEMPE activities performed by AusCo in substance in relation to the New Intangibles.*

88. *Had the New Arrangement not occurred, AusCo would have continued to own and derive income from the exploitation of the Existing Intangibles and the New Intangibles. AusCo would not have been required to pay royalties to NewCo for the use of the New Intangibles that AusCo developed after entering into the New Arrangement.*

89. *Understanding the (non-tax) commercial considerations for making and implementing the New Arrangement and the relevance of anticipated or potential tax impacts considered in connection with the decision to centralise, including any alternative options and their (non-tax) commercial value considered by AusCo and the global group prior to the decision to centralise, will be essential to our risk assessment. We may take the view that an independent entity dealing wholly independently in circumstances comparable to AusCo would not have entered into the New Arrangement. The New Arrangement required AusCo to dispose of its rights to current and future valuable intangible assets and associated income streams on non-arm's length terms.*

90. *As AusCo has not maintained or provided substantiating documentation, there is a risk that AusCo may not have appropriately priced its arrangements, including, but not limited to, not giving consideration to whether the Existing Intangibles Licence adequately compensates AusCo for the termination of the Current Licence Agreements.*

91. *While assessing the risk, we will consider the potential application of the transfer pricing provisions, including the exceptions to the basic rule within Subdivision 815-B, and the CGT or capital allowances provisions where relevant. Additionally, we will consider whether the arrangement was entered into or carried out for the dominant or principal purpose of obtaining a tax benefit. This may attract the operation of the GAAR in Part IVA of the ITAA 1936 and/or the application of the DPT.*

#### *Risk Factors and Documentation and Evidence Expectations*

92. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

- *understanding the (non-tax) commercial considerations of AusCo's decision to enter into the New Arrangement and the relevance of anticipated or potential tax impacts in implementing the New Arrangement, including the impact of the New Arrangement on AusCo's profitability and tax outcomes – this will include understanding AusCo's business decision-making processes, associated analyses and the global group's internal policies or guidelines governing its intangible assets and/or R&D processes and practices*



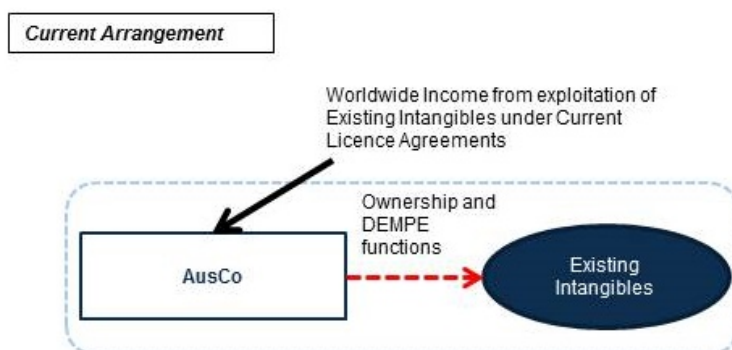
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- *identifying the Existing Intangibles and the New Intangibles with specificity and evidencing the DEMPE activities connected with these assets, as well as a comparison of the terms and conditions of the relevant agreements that AusCo entered into with NewCo – this will include understanding the link between the Existing Intangibles and the New Intangibles and the connected DEMPE activities*
- *identifying any relevant or comparable third-party arrangements entered into by AusCo or the global group regarding like intangible assets or R&D to understand their market behaviour and conduct with independent entities, and*
- *understanding the foreign tax implications of AusCo and its international related parties in connection with the arrangement referred to in this Example.*

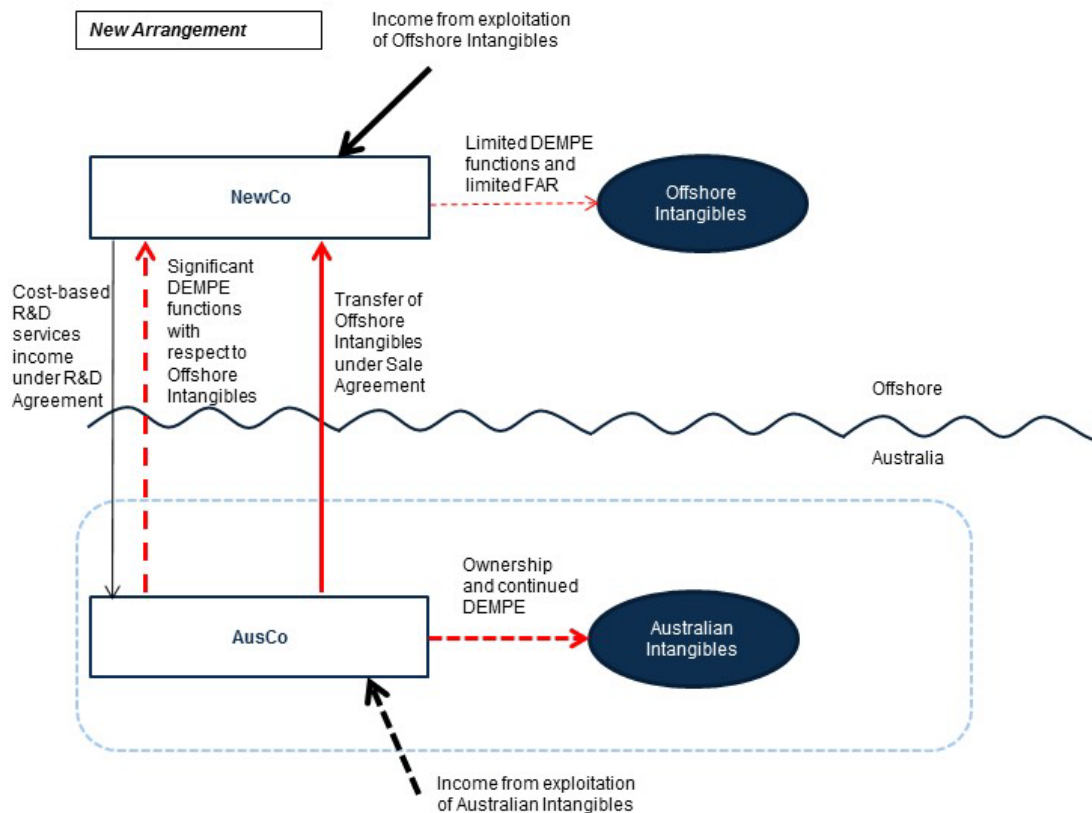
### **Example 2 – bifurcation of intangible assets – high risk**



#### **Current Arrangement**

93. AusCo is part of a global group that manufactures, markets and sells goods. AusCo and its international related parties exploit valuable intangible assets in undertaking their operations. The intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights (Existing Intangibles).

94. AusCo manages, performs and controls the DEMPE activities associated with the existing intangibles and assumes associated risks. AusCo derives royalties from the international related parties for the exploitation of the existing intangibles globally under current licence agreements between AusCo and the international related parties (current licence agreements).

Status: **draft only – for comment****New Arrangement**

95. AusCo and its global group decide that a new entity located in a foreign jurisdiction (NewCo) should exploit the Existing Intangibles in offshore markets by owning the relevant intangible assets (Offshore Intangibles).

96. As part of this decision, AusCo will continue to exploit the Existing Intangibles in Australia only and will own the relevant intangible assets and undertake the associated DEMPE activities as a result (Australian Intangibles).

97. The decision to transfer the Offshore Intangibles to NewCo (and bifurcate the Existing Intangibles into Australian Intangibles and Offshore Intangibles) is stated to be based on a desire to facilitate expansion into emerging markets and establish a global centre of expertise for new product development (New Arrangement). The documentation maintained or provided by AusCo does not substantiate the commercial rationale or does not recognise or provide documents referring to anticipated or potential Australian tax impacts considered in making the decision to transfer the Offshore Intangibles to NewCo.

98. To implement the New Arrangement, AusCo enters into a sale agreement (Sale Agreement) with NewCo, transferring the Offshore Intangibles to NewCo for an amount of consideration. This amount was determined by reference to a valuation that was undertaken by AusCo in relation to the Offshore Intangibles. The Sale Agreement provides that any entitlement to royalties connected with the Offshore Intangibles will be novated to NewCo. This includes the royalties AusCo received from the international related parties under the Current Licence Agreements. No payments are made to AusCo as a result of the termination. The documentation maintained or provided by AusCo does not

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*substantiate the arm's length nature of the pricing of all arrangements in connection with the restructure, including, but not limited to, the Sale Agreement and the decision to terminate and novate the Current Licence Agreements.*

99. *NewCo and AusCo also enter into an agreement where AusCo will provide R&D services to NewCo for cost-based remuneration (R&D Agreement). Under the R&D Agreement any new Offshore Intangibles that are developed as a result of the R&D undertaken by AusCo will be owned by NewCo.*

100. *At the time the New Arrangement is implemented, NewCo does not have sufficient assets or employ sufficiently qualified staff to wholly manage, perform or control the DEMPE of the Offshore Intangibles and assume the associated risks.*

101. *Some members of AusCo's management relocate to the jurisdiction of NewCo to facilitate the New Arrangement. However, AusCo continues to otherwise employ specialised staff and use its expertise and assets to manage, perform and control DEMPE activities associated with the Bifurcated Australian Intangibles and the Offshore Intangibles, and assume the associated risks. AusCo is remunerated for these activities with a cost-based service fee pursuant to the R&D Agreement with NewCo.*

102. *AusCo continues to own the Australian Intangibles, which allows it to manufacture, market and sell goods in the Australian market. AusCo continues to manufacture, market and sell goods associated with the Australian Intangibles in the Australian market and derive associated profits, but no longer receives royalties from international related parties for the exploitation of the Offshore Intangibles in undertaking similar functions offshore.*

103. *In subsequent years, AusCo continues to primarily manage, perform and control the DEMPE of both the Australian Intangibles and the Offshore Intangibles. There is limited new product development undertaken by NewCo independent of the DEMPE activities outsourced to, and managed and controlled by, AusCo in relation to the Offshore Intangibles.*

#### *Risk assessment*

104. *The New Arrangement would be regarded as a High Risk Intangibles Arrangement.*

105. *There is a risk that the New Arrangement has artificially bifurcated the Existing Intangibles into Australian Intangibles and Offshore Intangibles such that the New Arrangement is not arm's length in nature or is structured to avoid tax obligations.*

106. *Had the New Arrangement not occurred AusCo would have continued to own and derive income from the exploitation of the Existing Intangibles, including the bifurcated Offshore Intangibles. Understanding the commercial considerations underpinning the bifurcation of the Existing Intangibles into Australian Intangibles and Offshore Intangibles, the business need for the New Arrangement and the associated profit and tax outcomes will be essential to our risk assessment. The risk in this regard is emphasised where AusCo is not able to provide documentation substantiating its decision-making for entering into this arrangement or does not recognise or provide documents referring to anticipated or potential Australian tax impacts that were considered in making the decision to enter into the arrangement.*

107. *AusCo continued to manage and control the DEMPE activities of the Offshore Intangibles, which in economic substance was inconsistent with the form of the New Arrangement. We may take the view that an independent entity dealing wholly independently in circumstances comparable to AusCo would not have entered into the New Arrangement with NewCo, as it involved AusCo disposing of the Offshore Intangibles and associated income streams under non-arm's length conditions.*

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108. *We may also take the view that the distinction between the Australian Intangibles and the Offshore Intangibles and the separation of DEMPE activities in relation to these assets lacks commercial rationale and economic substance.*

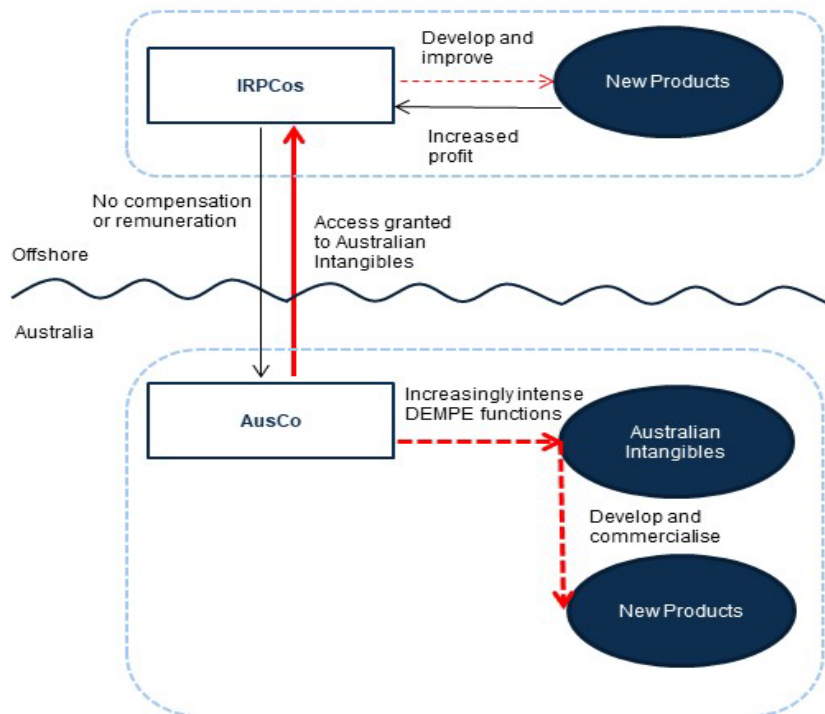
109. *As AusCo has not maintained or provided substantiating documentation, there is also a risk that AusCo may not have appropriately priced its arrangements, including not giving consideration to whether the AusCo was adequately compensated for the termination of the Current Licence Agreements or AusCo's sale under the Sale Agreement.*

110. *While assessing the risk, we will consider the potential application of the transfer pricing provisions (including the exceptions to the basic rule within Subdivision 815-B), the CGT provisions and the capital allowances provisions. Additionally, we will consider whether the arrangement was entered into or carried out for the dominant or principal purpose of obtaining a tax benefit. This may attract the operation of the GAAR in Part IVA of the ITAA 1936 and/or the application of the DPT.*

#### *Risk Factors and Documentation and Evidence Expectations*

111. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

- *understanding the (non-tax) commercial benefits and the anticipated or potential tax impacts of implementing the Bifurcation Arrangement and the decision-making process for implementing the New Arrangement*
- *identifying the Existing Intangibles, including the bifurcated Australian Intangibles and Offshore Intangibles with specificity– this will include understanding the intrinsic link between the Offshore Intangibles and the Bifurcated Australian Intangibles, as well as the valuation processes that were relied upon to determine the value of the Offshore Intangibles*
- *evidencing the DEMPE activities associated with the Bifurcated Australian Intangibles and Offshore Intangibles, as well as a comparison to the terms and conditions of the relevant agreements that AusCo entered into with NewCo as a result of the New Arrangement*
- *identifying any relevant or comparable third party arrangements entered into by AusCo or the global group regarding like intangible assets or R&D to understand market behaviour and conduct with independent entities, particularly the bifurcation of such intangible assets, and*
- *understanding the foreign tax implications of AusCo and its international related parties in connection with the arrangements referred to in this Example.*

Status: **draft only – for comment****Example 3 – non-recognition of Australian intangible assets and DEMPE activities – high risk**

112. AusCo is part of a global group that manufactures and sells goods and provides associated services. AusCo and its international related parties have historically recognised the use of minimal valuable intangible assets in undertaking their operations aside from certain trademarks and intangible assets associated with the global group's brand and product lines. A number of these trademarks are owned by AusCo and connected with products and services exclusively distributed in Australia. AusCo manages, performs and controls DEMPE activities connected with its Australian trademarks and assumes associated risks.

113. Over a number of years, AusCo's DEMPE activities increase in intensity, resulting in the development and commercialisation of a number of new and improved products and services. Several new identifiable intangible assets are developed from these activities. AusCo does not account for any additional intangible assets in its financial statements or register the relevant intangible assets for legal protection. The relevant intangible assets include patentable products and processes, know-how, copyright and other intangible assets or rights. These intangible assets and the Australian trademarks are developed, maintained, enhanced and owned by AusCo (Australian Intangibles).

114. AusCo does not formally recognise any Australian Intangibles or engage in annual review or analysis of its processes and activities associated with the Australian Intangibles. Likewise, AusCo's global group does not maintain a comprehensive contemporaneous R&D or intellectual property policy or other relevant processes or guidelines.

115. In the following years, a number of AusCo's international related parties are granted access to the Australian Intangibles and use these assets to develop and improve equivalent products and services in offshore jurisdictions. AusCo does not enter into any legal agreements for the transfer or licensing of these assets with its international related

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*parties or update its transfer pricing policy or documentation in connection with these dealings.*

116. *The profitability of AusCo's international related parties increases as a result of accessing and exploiting the Australian Intangibles and the functions performed, assets used and risks assumed by AusCo in connection with the DEMPE of the Australian Intangibles. AusCo does not receive compensation or remuneration from its international related parties in connection with their access to, and use of, the Australian Intangibles.*

#### *Risk assessment*

117. *This arrangement would be regarded as a High Risk Intangibles Arrangement.*

118. *There is a risk that the dealings entered into by AusCo may not be consistent with AusCo's best economic interests having regard to the commercial options realistically available to AusCo. AusCo granted access to and use of the Australian Intangibles to its international related parties where no agreements or form of remuneration were considered or recognised.*

119. *The absence of legal agreements between AusCo and its international related parties may impede AusCo's ability to protect its interests with respect to the Australian Intangibles. The lack of compensation or remuneration from the international related parties for access to and use of the Australian Intangibles may be inconsistent with arrangements that might reasonably be expected to be entered into between independent entities dealing wholly independently in comparable circumstances.*

120. *The effect of the arrangement is that AusCo has allowed its international related parties to exploit and derive benefits in connection with the Australian Intangibles for nil consideration. The arrangement fails to appropriately recognise DEMPE activities managed, performed and controlled by AusCo, development of Australian Intangibles from AusCo's activities and exploitation of assets developed by AusCo by AusCo's international related parties.*

121. *We may take the view that the conditions that operate between AusCo and its international related parties in connection with their commercial or financial relations are conditions that differ from arm's length conditions. Understanding the conditions that operate between AusCo and its international related parties in their commercial or financial relations compared to the conditions that operate between independent entities dealing wholly independently in comparable circumstances to that of AusCo and its international related parties will be essential to our risk assessment.*

122. *While assessing the risk, we will consider the potential application of the transfer pricing provisions including the exceptions to the basic rule within Subdivision 815-B. Additionally, we will consider whether the arrangement was entered into or carried out for the dominant or principal purpose of obtaining a tax benefit. This may attract the operation of the GAAR in Part IVA of the ITAA 1936 and/or the application of the DPT.*

#### *Risk Factors and Documentation and Evidence Expectations*

123. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

- *understanding the economic substance of AusCo's international related party arrangements – this will include obtaining contemporaneous*

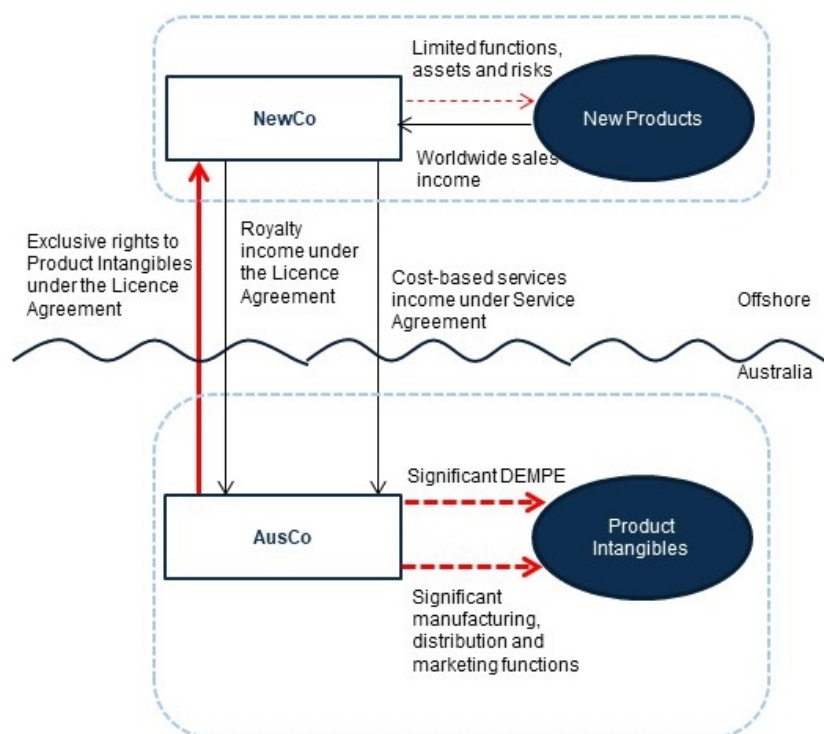


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*documentation to evidence the DEMPE activities connected with the Australian Intangibles and documents disclosing anticipated or potential tax impacts considered in relation to implementing the arrangements*

- *understanding how the international related parties exploit and utilise the Australian intangibles – this will include understanding the value and benefit of the Australian Intangibles*
- *in the absence of documentation to evidence the functions undertaken, assets held and risks assumed by AusCo, we may need to undertake interviews with key personnel within AusCo or its global group, and*
- *understanding the foreign tax implications of AusCo and its international related parties in connection with the arrangements referred to in this Example.*

**Example 4 – migration of pre-commercialised intangible assets – high risk**



124. AusCo is part of a global group that develops, manufactures, markets and sells products globally. AusCo and its international related parties engage in the DEMPE of valuable intangible assets in undertaking their operations. These intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights.

125. AusCo spent a number of years undertaking R&D in Australia to develop a new product range, which resulted in the development of pre-commercialised intangible assets (Product Intangibles). AusCo owns the Product Intangibles. AusCo considers the Product Intangibles to be strategically important to their business.

126. Prior to the Product Intangibles being commercialised, AusCo and the global group decide to incorporate a new entity in an offshore jurisdiction NewCo for the stated purpose of further developing, manufacturing and commercialising the new products associated

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*with the Product Intangibles (New Products). While AusCo has the capability and capacity to develop, manufacture and commercialise the New Products, the global group decides that NewCo should instead own the rights to the Product Intangibles. The documentation maintained or provided by AusCo does not substantiate the commercial rationale underpinning this decision or does not recognise the consideration of anticipated or potential tax impacts in making the decision.*

127. *As a result of this decision, AusCo and NewCo enter into a licence agreement (Licence Agreement). The Licence Agreement grants NewCo the exclusive rights to develop, manufacture and commercialise the Product Intangibles, including the associated New Products. Under the Licence Agreement, NewCo pays ongoing royalties to AusCo in relation to worldwide sales of the New Products. As a result of the Licence Agreement, the effective control of the Product Intangibles is transferred from AusCo to NewCo and, as a consequence, all of the worldwide income that will be received from the global commercial sales of the New Products will be derived by NewCo. The documentation maintained or provided by AusCo does not substantiate the arm's length nature of the pricing or terms of this arrangement.*

128. *At the time of entering into the Licence Agreement, NewCo does not have sufficient assets or employ sufficiently qualified staff to undertake the DEMPE activities which are undertaken by AusCo. NewCo subsequently enters into various service agreements (Service Agreements) with AusCo, under which AusCo agrees to provide services for the development, manufacture and distribution of the New Products. The Service Agreements remunerate AusCo with a cost-based service fee. The documentation maintained or provided by AusCo does not substantiate the commercial rationale or the arm's length nature of the pricing of this arrangement.*

#### *Post-transfer of the rights to the Product Intangibles*

129. *Following the transfer of the rights to the Product Intangibles to NewCo, the functions performed, assets used and risks assumed by AusCo do not substantially change. AusCo continues to employ specialised staff and uses its expertise and assets to manage, perform and control DEMPE activities associated with the Product Intangibles. The functions performed, assets used and risks assumed by AusCo in connection with activities covered by the Services Agreements with NewCo results in the commercialisation of the Product Intangibles. NewCo has limited relevantly qualified staff and manages and performs limited activities, owns limited assets and assumes limited risks in connection with the Product Intangibles.*

130. *Once the New Products are commercialised, AusCo manufactures, distributes and markets the New Products on behalf of NewCo under the Service Agreements. In undertaking these activities, AusCo employs specialised staff and uses its expertise and assets to manufacture and sell the New Products to the global market. However, AusCo only receives cost-based remuneration from NewCo in accordance with the terms of the Service Agreements and royalties from the commercial sales of the New Products. NewCo continues to have limited qualified staff, manages and performs limited activities, and assumes limited risks in connection with the manufacture, distribution and marketing of the New Products. NewCo derives the worldwide income from the sale of the New Products.*

#### *Risk assessment*

131. *The arrangement between AusCo and NewCo would be regarded as a High Risk Intangibles Arrangement.*



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132. *There is a risk that AusCo's entry into the Licence Agreement and Service Agreements with NewCo lacks commercial and economic substance or may not be an arrangement that independent entities dealing wholly independently in comparable circumstances to that of AusCo and NewCo would have entered into. This risk is emphasised where AusCo is not able to provide documentation substantiating its decision-making for entering into these arrangements or does not provide documents created or provided by personnel or tax advisers which disclose anticipated or potential tax impacts that were taken into account in connection with deciding to implement the arrangements.*

133. *AusCo owned and developed the Product Intangibles and had the capability, expertise and capacity to continue to develop, manufacture and commercialise them for market. The Product Intangibles were strategically important to AusCo's business. AusCo did not require NewCo as a partner to develop or commercialise the Product Intangibles. NewCo did not have the capability or capacity to develop or commercialise the Product Intangibles at the time the arrangements were implemented.*

134. *As a consequence of AusCo transferring the rights to control or use its Product Intangibles to NewCo, AusCo did not derive the worldwide income from the sale of the New Products.*

135. *AusCo also continued to manage and control the DEMPE activities of the Product Intangibles and performed the functions, used its assets and assumed the risks that were associated with the manufacturing, marketing and distribution of the New Products. NewCo had limited qualified staff, managed and performed limited activities, and assumed limited risks in connection with these activities. NewCo did not have the capability or capacity to manage and be responsible for the rights and obligations it had under the Licence Agreement in connection with the Product Intangibles and the New Products which were instead, in substance, controlled and managed by AusCo.*

136. *We may take the view that an independent entity dealing wholly independently in circumstances comparable to AusCo would not have entered into the Licence Agreement and Service Agreements with NewCo. Understanding the business rationale for transferring the rights to the Product Intangibles to a newly incorporated entity in a foreign jurisdiction with limited capability or capacity to undertake the associated DEMPE activities will be essential to our risk assessment.*

137. *As AusCo has not maintained or provided adequate substantiating documentation, there is also a risk that AusCo may not have appropriately priced its arrangements in connection with the restructure, including the pricing of the Service Agreements.*

138. *While assessing the risk, we will consider the potential application of the transfer pricing provisions, including the exceptions to the basic rule within Subdivision 815-B. Additionally, we will consider whether the arrangement was entered into or carried out for the dominant or principal purpose of obtaining a tax benefit. This may attract the operation of the GAAR in Part IVA of the ITAA 1936 and/or the application of the DPT.*

#### **Risk Factors and Documentation and Evidence Expectations**

139. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

- *understanding the decision-making of AusCo's transfer of its Product Intangibles to NewCo – this will include understanding any alternative options and (non-tax) commercial factors that were considered by AusCo or*

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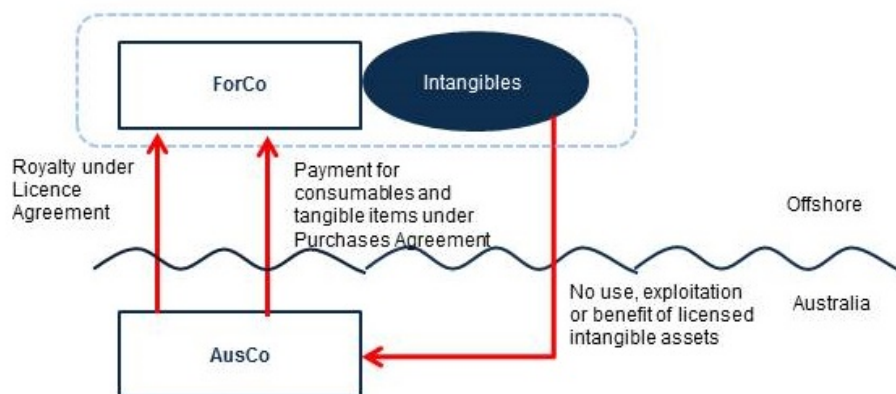
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*its global group in deciding to transfer the Product Intangibles, including any analysis of the costs and benefits of the arrangement compared with the other options including anticipated or potential tax impacts*

- *evidencing the DEMPE activities connected with the Product Intangibles and with the manufacturing and commercialisation of the associated New Products, including obtaining contemporaneous documentation to assess the DEMPE activities of AusCo and NewCo having regard to the terms and conditions of the Licence Agreement and the Service Agreements*
- *understanding AusCo and the global group's policy regarding R&D and intangible assets and the context of these policies with respect to any relevant or comparable third party arrangements regarding the development, manufacturing or commercialisation of comparable intangible assets and associated products, and*
- *understanding the foreign tax implications of AusCo and its international related parties in connection with the arrangements referred to in this Example.*

#### **Example 5 – non-arm's length licence arrangements – high risk**



140. *AusCo is part of a global group that manufactures and sells goods and provides associated services globally.*

141. *To enable AusCo to undertake its business, it enters into an agreement to acquire consumables and other tangible items from an international related party, ForCo (Purchases Agreement).*

142. *AusCo also enters into a licence agreement with ForCo (Licence Agreement), under which ForCo provides AusCo with access to certain intangible assets. The intangible assets include trademarks, manufacturing patents and copyrights. Some of these intangible assets are stated to relate to the use of the consumables and other tangible items purchased under the Purchases Agreement. Under the Licence Agreement, AusCo pays royalties to ForCo to access and use these intangible assets.*

143. *As part of its business operations AusCo does not exploit or use the intangible assets under the Licence Agreement. In substance, AusCo does not require the use of the licensed intangible assets in order to operate and exploit the consumables and other tangible items purchased under the Purchases Agreement. The licenced intangible assets*

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*also provide no benefit to AusCo's business. AusCo pays royalties to ForCo for the intangible assets under the Licence Agreement.*

144. *There is no mischaracterisation of intangible assets and/or activities or conditions connected with intangible assets under either the Purchases Agreement or the Licence Agreement with ForCo.*

#### *Risk assessment*

145. *This arrangement would be regarded as a High Risk Intangibles Arrangement.*

146. *There is a risk that the Licence Agreement between AusCo and ForCo is non-arm's length and that AusCo has obtained a transfer pricing benefit as a result of the deductions it has claimed for the royalties payable to ForCo under the Licence Agreement.*

147. *AusCo did not require access to the intangible assets to operate its business. AusCo did not access or use the intangible assets under the Licence Agreement or obtain valuable business benefits in connection with the licenced intangible assets. Specifically, AusCo did not require the use of the trademarks, patents and copyrights stated to be linked to the consumables under the Purchases Agreement. Understanding the benefits of the intangible assets to AusCo's business operations and the use of those assets will be essential to our risk assessment.*

148. *We may take the view that independent entities dealing wholly independently in circumstances comparable to AusCo and ForCo would not have entered into the Licence Agreement or that the arrangement between AusCo and ForCo is inconsistent with the substance of the arrangement.*

149. *While assessing the risk, we will consider the potential application of the transfer pricing provisions, including the exceptions to the basic rule within Subdivision 815-B in certain circumstances. Additionally, we will consider whether the arrangement was entered into or carried out for the dominant or principal purpose of obtaining a tax benefit. This may attract the operation of the GAAR in Part IVA of the ITAA 1936 and/or the application of the DPT.*

#### *Risk Factors and Documentation and Evidence Expectations*

150. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

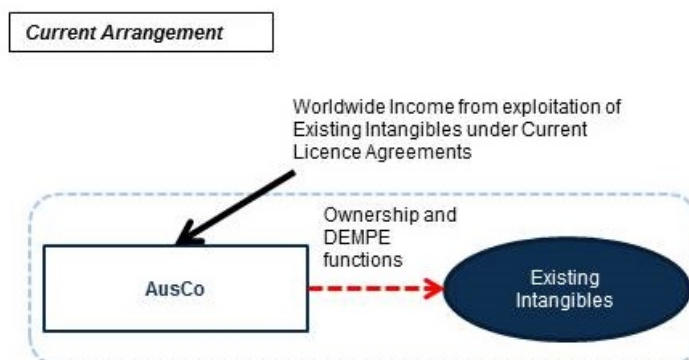
- *understanding the economic substance of AusCo's dealings with ForCo in the context of the terms and conditions of the Licence Agreement*
- *understanding the decision making in connection with entering into the Licence Agreement including consideration of any anticipated or potential tax impacts of entering into the Licence Agreement*
- *identifying the intangible assets with specificity and understanding whether, and how, AusCo exploits and utilises the intangible assets under the Licence Agreement*
- *understanding the value and benefit of the intangible assets to AusCo's business operations and the DEMPE activities associated with those intangible assets*

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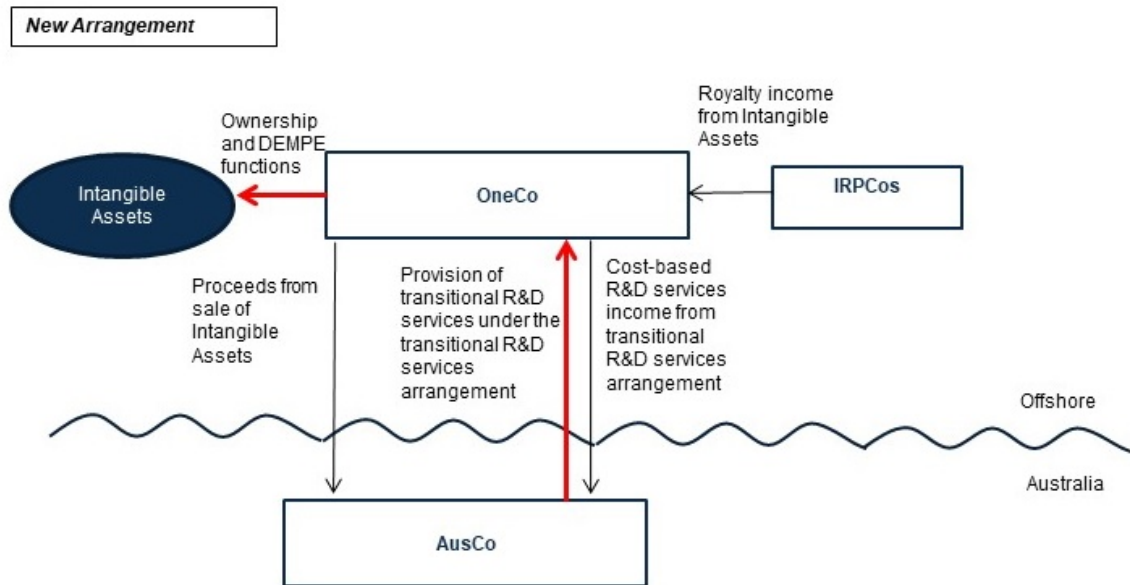

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- *understanding AusCo and the global group's policy regarding intangible assets and the context of these policies with respect to any relevant or comparable third-party arrangements, and*
- *understanding the foreign tax implications of AusCo and its international related parties in connection with the arrangements referred to in this Example.*

**Example 6 – centralisation of intangible assets – medium risk**

**Current Arrangement**

151. Similarly to Example 1 of this Guideline, AusCo undertakes manufacturing, marketing and distribution functions and owns, manages and controls DEMPE activities associated with a suite of valuable intangible assets, including patents, know-how, trademarks, copyright and other intangible assets or rights (Intangible Assets).

152. The Intangible Assets are used in the business of the global group to which AusCo belongs and AusCo derives royalties from its international related parties from the global exploitation of the Intangible Assets under current licence agreements between AusCo and the international related parties (Current Licence Agreements). Entities within the global group in other jurisdictions have also undertaken manufacturing, marketing and distribution functions and managed and controlled DEMPE activities associated with a suite of valuable intangible assets over a similar historical period. These other overseas entities also derive royalties from related parties within the global group, including Australia, from the exploitation of their intangible assets under licence agreements.

Status: **draft only – for comment***Decision to centralise intangible assets*

153. AusCo and the global group determine that the Intangible Assets should be centralised in an entity (OneCo) to be located in a foreign jurisdiction. AusCo's transfer of the Intangible Assets to OneCo forms part of a broader global centralisation under which intangible assets held by other international related parties are also transferred and centralised in OneCo.

154. AusCo and the global group consider a number of commercial and legal factors in making the decision to centralise, including considering alternative options, and determine that centralising their intangible assets in one entity has a number of commercial benefits which have been quantified. AusCo maintains or provides documentation to substantiate the commercial rationale underpinning its decision to centralise.

155. As a result of the decision to centralise, AusCo enters into a Sale Agreement with OneCo to transfer the Intangible Assets to OneCo. As part of the sale, the Current Licence Agreements between AusCo and its international related parties are novated to OneCo with OneCo as the licensor. AusCo undertakes an independent valuation to value the Intangible Assets prior to this sale and to ensure that the transfer is made on arm's length terms.

156. As a result of the sale, OneCo receives worldwide income from the exploitation of the Intangible Assets. AusCo maintains or provides some documentation to support the arm's length nature of the pricing and terms of all arrangements in connection with the restructure, including, but not limited to, the Sale Agreement and the novation of the Current Licence Agreements.

157. As part of the decision to centralise, AusCo decided that it was no longer commercially viable for it to continue with its manufacturing and R&D functions. As a result, AusCo decided to cease these operations and continue with its distribution functions only.

158. AusCo enters into a transitional R&D Services Agreement with OneCo. Under this agreement, AusCo will provide R&D services to OneCo in relation to the Intangible Assets in return for a fee determined with regard to the costs incurred by AusCo in the provision of the R&D activities. This arrangement is intended to operate as a transitional feature of the

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*centralisation to allow AusCo to assist OneCo with managing the Intangible Assets as OneCo builds up the necessary capability and expertise to undertake these functions. Any New Intangibles that are developed as a result of the R&D undertaken by AusCo under the R&D Services Agreement will be owned by OneCo. The documentation AusCo maintains or provides in relation to the arm's length nature of the pricing and terms of the R&D Services Agreement is incomplete.*

#### *New Arrangement*

159. *In Year 1 following the decision to centralise, AusCo performs R&D activities under the R&D Services Agreement under the direction and oversight of OneCo, which employs sufficiently skilled staff to manage DEMPE activities. AusCo receives remuneration for the functions it performs under the R&D Services Agreement.*

160. *By Year 2 following the decision to centralise, OneCo has employed additional staff and acquired additional assets to assist in the management of DEMPE activities for the Intangible Assets. These staff and assets are sufficient to allow OneCo to wholly manage, perform and control the DEMPE activities connected with the Intangible Assets and assume all associated risks. The R&D Services Agreement between AusCo and OneCo is terminated and AusCo ceases performing R&D services with respect to the Intangible Assets.*

#### *Risk assessment*

161. *The New Arrangement would be regarded as a Medium Risk Intangibles Arrangement.*

162. *We would expect that the documentation AusCo has maintained or provided demonstrates a genuine and substantiated (non-tax) commercial rationale to support the decision to centralise and how this decision was not affected by consideration of the anticipated or potential tax impacts of implementing the arrangements.*

163. *A risk that may arise with respect to this arrangement is the risk that the substance of the New Arrangement may not align with the form of the arrangement. The level of substance in OneCo's operations following the decision to centralise and OneCo's ability to demonstrate that it has built up the additional capacity necessary to manage, perform and control DEMPE functions connected with the Intangible Assets will inform the level of risk associated with the arrangement.*

164. *It is relevant to consider the independent valuation undertaken with respect to the Intangible Assets and the documentation maintained or provided by AusCo demonstrating the arm's length nature of the transfer of the Intangible Assets under the Sale Agreement and the arm's length nature of the terms of the R&D Services Agreement. It will also be relevant to consider the level of documentation maintained or provided by AusCo in relation to all arrangements in connection with the centralisation of the intangible assets.*

165. *While assessing the risk, we may consider the potential application of the transfer pricing provisions, including Subdivision 815-B, as well as the CGT provisions or the capital allowance provisions in relation to the Sale Agreement.*

#### *Risk Factors and Documentation and Evidence Expectations*

166. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. Consistent with the principles outlined in paragraphs 42 to 74 of this Guideline, the documentation and*

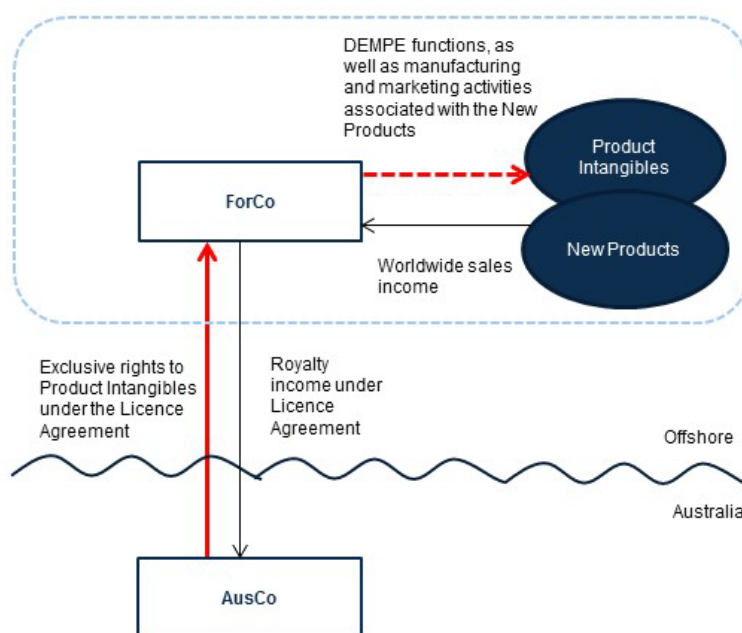


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*evidence requested will align with the level of risk associated with the arrangement. Our focus under this Example will be on:*

- *substantiating the (non-tax) commercial considerations of AusCo's entry into the New Arrangement, the options realistically available to the parties to the arrangement and any impact the New Arrangement has on AusCo's profitability and tax outcomes – this will include understanding AusCo's business decision-making processes and how the decision was not affected by consideration of anticipated or potential tax impacts of implementing the arrangements, associated analyses and the group's internal policies or guidelines governing its intangible assets and/or R&D processes and practices*
- *identifying the Intangible Assets and evidencing the DEMPE activities connected with the Intangible Assets- this will include an assessment of the conditions operating under the R&D Services Agreement and the substance of the New Arrangement following the decision to centralise, and*
- *documents to assess the appropriateness of the transfer pricing method and comparability studies applied, including the independent valuation undertaken on the intangible assets.*

**Example 7 – transfer of rights to intangible assets under a Licence Agreement – medium risk**



167. Similarly to Example 4 of this Guideline, AusCo is part of a global group that develops, manufactures, markets and sells products globally. AusCo and its international related parties engage in the DEMPE of valuable intangible assets in undertaking their operations. These intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights.

168. AusCo undertakes R&D activities to develop a new product range resulting in the development of early stage intangible assets (Product Intangibles). AusCo owns the Product Intangibles.

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169. *AusCo's ability to further develop and commercialise the Product Intangibles, including the capability and capacity to manufacture and market the products that may be associated with the Product Intangibles (New Products), is limited. AusCo requires a partner to continue with the development of the Product Intangibles so that they can be commercialised into New Products that are able to be manufactured and marketed to customers.*

170. *ForCo, a related party located in a foreign jurisdiction, has the capability to further develop and commercialise the Product Intangibles including the capacity to manufacture the New Products. AusCo decides that it is in its best interest to partner with ForCo to further develop and commercialise the Product Intangibles, otherwise it may have to cease further development of the Product Intangibles given its limited expertise and capability. AusCo maintains or provides documentation to substantiate the commercial rationale underpinning this decision.*

171. *As a result of this decision, AusCo and ForCo enter into a licence agreement (Licence Agreement). The Licence Agreement grants the exclusive rights of the Product Intangibles to ForCo for the development and commercialisation of the Product Intangibles and for the manufacturing and marketing of the associated New Products. Under the Licence Agreement, AusCo negotiates with ForCo to receive upfront, milestone and royalty payments based on an independent valuation of the Product Intangibles and associated New Products. The documentation AusCo maintains or provides in relation to the arm's length nature of the pricing and terms of all arrangements in connection with the restructure, including but not limited to, the Licence Agreement, is incomplete.*

172. *As a result of the Licence Agreement, ForCo assumes the risks associated with further developing and commercialising the Product Intangibles, including manufacturing and marketing the New Products. Any income generated from the commercial sales of the New Products will be derived by ForCo.*

#### *Post-Licence Agreement*

173. *ForCo, with its expertise and capability, manages, performs and controls the DEMPE activities connected with the Product Intangibles and assumes the associated risks. ForCo continues to develop the Product Intangibles and is able to commercialise them into New Products.*

174. *Once commercialised, ForCo manufactures and markets the New Products to customers, derives the worldwide income from the sale of the associated Products and pays to AusCo the amounts payable under the Licence Agreement.*

#### *Risk assessment*

175. *The arrangement between AusCo and ForCo would be regarded as a Medium Risk Intangibles Arrangement.*

176. *We would expect that the documentation AusCo has maintained or provided demonstrates a genuine and substantiated (non-tax) commercial rationale to enter into the Licence Agreement with ForCo.*

177. *A risk that may arise with respect to this arrangement is the risk that the substance of the Licence Agreement may not align with the form of the arrangement. The level of substance in ForCo's operations following the transfer of the Product Intangibles will also inform the level of risk associated with the arrangement and in particular ForCo's role in the management of the DEMPE activities and role in the commercialisation, manufacturing and marketing of the New Products.*



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178. Another risk that may arise in relation to this arrangement relates to whether the payments made by ForCo and AusCo under any arrangements in connection with the restructure are arm's length. This includes, but is not limited to, the Licence Agreement. It will be relevant to consider the documentation maintained or provided by AusCo in relation to the pricing and terms of this arrangement, including the independent valuation for the Product Intangibles and associated New Products, and how each of the upfront, milestone and royalty payments under the Licence Agreement were determined.

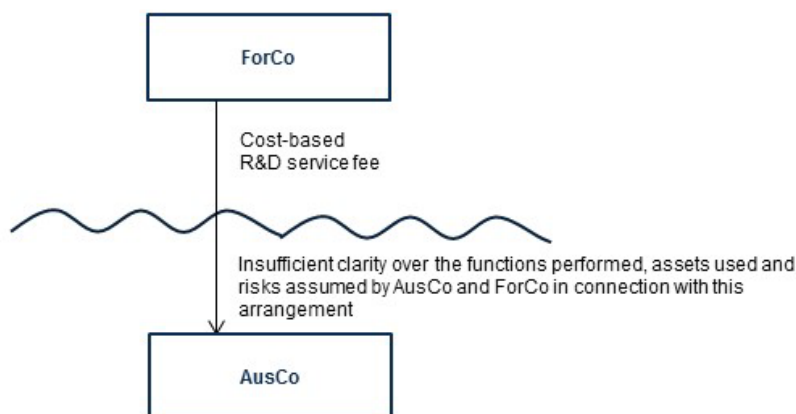
179. While assessing the risk, we may consider the potential application of the transfer pricing provisions, including Subdivision 815-B.

#### *Risk Factors and Documentation and Evidence Expectations*

180. In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:

- substantiating the (non-tax) commercial considerations of AusCo's entry into the Licence Agreement, including the impact they have on AusCo's profitability and tax outcomes – this will include understanding AusCo's business decision-making processes and how the decision to enter into the Licence Agreement was not affected by consideration of the anticipated or potential tax impacts, associated analyses and the group's internal policies or guidelines governing its intangible assets and/or R&D processes and practices
- identifying the Product Intangibles and evidencing the DEMPE activities connected with the Product Intangibles – this will include an assessment of the substance of the Licence Agreement, and
- documents to assess the appropriateness of the tax and profit outcomes resulting from your arrangements, including the transfer pricing method and comparability studies applied.

#### **Example 8 – contract research and development arrangement – medium risk**



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181. *AusCo is part of a global group that manufactures and sells goods and provides associated services globally. AusCo and its international related parties exploit valuable intangible assets in undertaking their operations. The intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights (Existing Intangibles).*

182. *ForCo, a related party located in a foreign jurisdiction, is the entity that has always undertaken, managed and been responsible for the DEMPE activities associated with the Existing Intangibles. ForCo derives worldwide income from the exploitation of the Existing Intangibles by the global group.*

183. *In connection with managing and controlling the DEMPE activities, ForCo is responsible for managing the global group's R&D operations. The R&D operations consist of R&D centres, located both within and outside of ForCo's jurisdiction, that perform contract R&D services for or on behalf of ForCo.*

184. *ForCo employs specialised staff and has the expertise and capability to manage the various contract R&D centres. While AusCo's R&D costs are relatively much less than the costs of the global group's total R&D operations, it does employ experienced and specialised staff to perform R&D activities.*

185. *AusCo is party to an R&D services agreement with ForCo, under which it is remunerated with a service fee (R&D Services Agreement). The documentation AusCo maintains or provides in relation to the pricing and terms of the R&D Services Agreement is incomplete.*

186. *Under this arrangement:*

- *The documentation maintained or provided by AusCo does not provide sufficient clarity around the specific functions performed, assets used and risks assumed by AusCo and ForCo in connection with the DEMPE activities associated with the Existing Intangibles.*
- *New intangible assets or improvements to the Existing Intangibles developed as a result of the R&D undertaken by AusCo will be owned by ForCo.*

#### *Risk assessment*

187. *The arrangement between AusCo and ForCo would be regarded as a Medium Risk Intangibles Arrangement.*

188. *The risks that arise from this arrangement are that the substance of the arrangement may not align with its form (that is, AusCo may, in fact, control certain DEMPE activities) and AusCo may not receive a return commensurate with its contributions to the Existing Intangibles or any new intangible assets developed under the arrangement. The extent of AusCo's actual involvement in DEMPE activities will inform the level of risk associated with the arrangement.*

189. *There is also a risk as to whether the payments made by ForCo to AusCo under the R&D Services Agreement are arm's length and are commensurate with the functions performed, assets utilised and risks assumed by AusCo and ForCo in relation to DEMPE activities performed under the R&D Services Agreement. It will be relevant to consider the documentation maintained or provided by AusCo in relation to the pricing and terms of this arrangement.*

190. *While assessing the risk, we may consider the potential application of the transfer pricing provisions, including Subdivision 815-B.*

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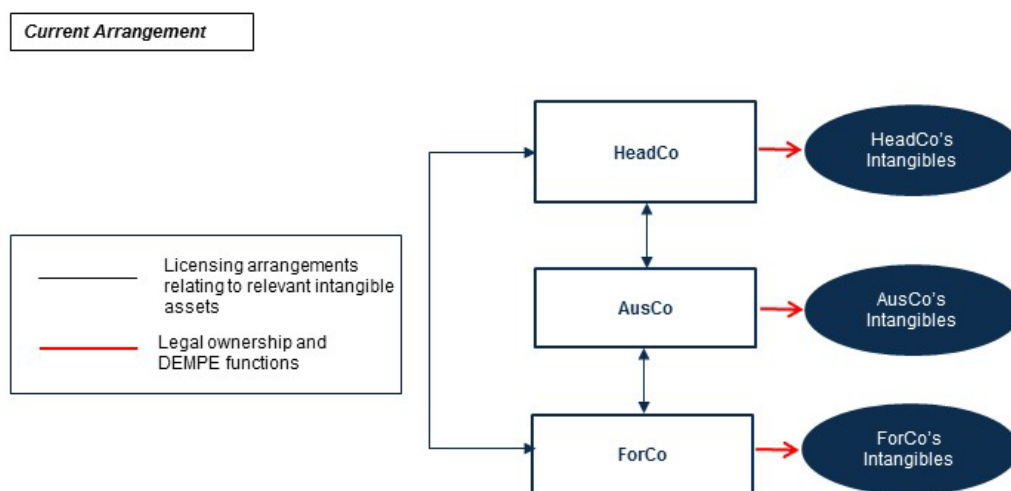

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### *Risk Factors and Documentation and Evidence Expectations*

191. In assessing the risk, we will request certain documentation, taking into account the *Risk Factors and Documentation and Evidence Expectations*. While the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:

- substantiating documentation which clarifies the analysis and information contained in the legal form documents and any additional materials provided to us
- understanding and evidencing the relevant DEMPE activities being undertaken by ForCo and the extent of any DEMPE activities undertaken by AusCo, and
- documents to assess the appropriateness of the tax and profit outcomes resulting from your arrangements, including the transfer pricing method and comparability studies undertaken.

### **Example 9 – cost contribution arrangement – medium risk**



### **Current Arrangement**

192. AusCo is part of a global group headed by HeadCo, located in a foreign jurisdiction. HeadCo's subsidiary, ForCo, is located in another foreign jurisdiction. AusCo, HeadCo and ForCo act as regional heads for the global group. The regional heads exploit a suite of valuable intangible assets comprising AusCo's Intangibles, HeadCo's Intangibles and ForCo's Intangibles in undertaking business operations in their respective regions.

193. AusCo manages and controls DEMPE functions associated with its Intangibles. AusCo derives royalties from its international related parties HeadCo and ForCo under licence agreements for the exploitation of its Intangibles in each of HeadCo's and ForCo's respective regions.

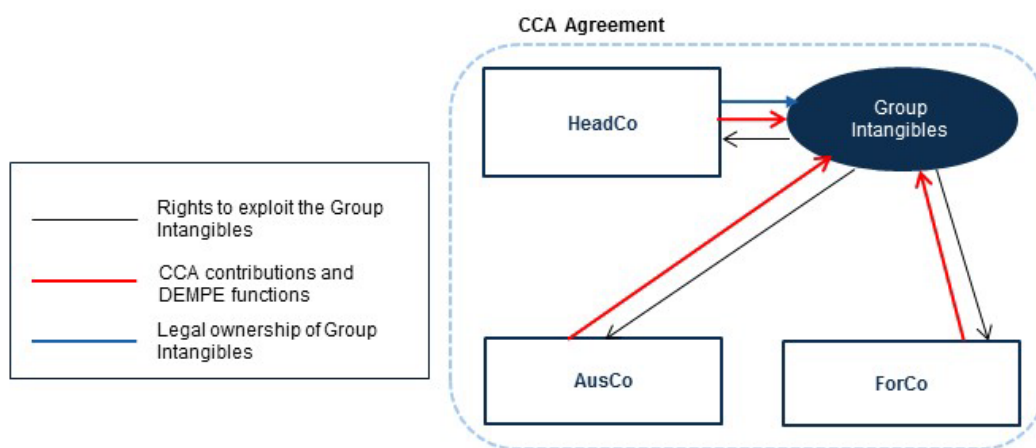
194. ForCo manages and controls DEMPE functions associated with its Intangibles. ForCo derives royalties from its international related parties HeadCo and AusCo under

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*licence agreements for the exploitation of its Intangibles in each of HeadCo's and AusCo's respective regions.*

195. *HeadCo manages and controls DEMPE activities associated with its Intangibles, which comprise the majority of the global group's intangible assets. HeadCo derives royalties from AusCo and ForCo under licence agreements for the exploitation of its Intangibles in each of AusCo's and ForCo's respective regions.*

New Arrangement



#### Cost contribution arrangement

196. *AusCo, HeadCo and ForCo decide to enter into a cost contribution arrangement (CCA) to pool their expertise and share the risks of improving each of their respective Intangibles for the mutual benefit of all participants. AusCo maintains or provides documentation to substantiate the commercial rationale underpinning the decision to enter into the CCA.*

197. *Under the terms of the CCA:*

- *AusCo, HeadCo and ForCo each contribute their Intangibles to the CCA, with all three participants making adjustments to their contributions, as required, to align them with their share of expected benefits. An independent valuation was undertaken for each of AusCo's, HeadCo's and ForCo's Intangibles.*
- *All R&D costs incurred globally are initially borne by HeadCo, and the costs are then allocated between the three regional heads based on the proportion of group sales each regional head makes in their respective region.*
- *At the end of the income year, a balancing adjustment, based on the allocation of costs, is made where necessary to align each of HeadCo's, AusCo's and ForCo's share of costs with their share of expected benefits.*
- *All intangible assets developed under the CCA are to be legally owned by HeadCo, with AusCo and ForCo each granted a perpetual, royalty-free licence to exploit the developed intangibles in their respective regions.*

198. *Each of HeadCo, AusCo and ForCo employs specialised R&D staff, who use their expertise in performing their functions. The activities and risks borne by AusCo per the*

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*CCA agreement accurately reflect the substance of its R&D contribution (based on an assessment of its functions, assets and risks). AusCo's proportionate share of costs is consistent with the expected benefits to be received by AusCo under the CCA agreement as compared to HeadCo and ForCo.*

199. *The documentation AusCo maintains or provides in relation to the arm's length nature of the pricing and terms of the CCA is incomplete. AusCo, HeadCo and ForCo terminate their pre-existing cross-licensing agreements as a result of entering into the CCA.*

#### *Risk assessment*

200. *The arrangement between AusCo, HeadCo and ForCo would be regarded as a Medium Risk Intangibles Arrangement.*

201. *We would expect the documentation AusCo has maintained or provided substantiates the commercial rationale underpinning its decision to enter into the CCA, having regard to all the relevant facts and circumstances.*

202. *There is a risk that the terms of the CCA may not be consistent with what independent enterprises in comparable circumstances would have entered into. This risk may arise where the value of AusCo's pre-existing contributions and current contributions have been incorrectly valued, including where the economic outcomes and benefits obtained by AusCo under the CCA do not align with its contributions to DEMPE activities, having regard to functions performed, assets used and risks assumed by AusCo as compared to HeadCo and ForCo.*

203. *It will be relevant to consider the documentation that has been maintained or provided by AusCo in relation to the pricing and terms of the CCA, in order to determine whether AusCo is able to demonstrate that its proportionate share of the overall contributions (taking into account any balancing payments already made) to the CCA is consistent with its share of the overall expected benefits to be received under the arrangement. In addition, it will be important to consider whether AusCo and the parties to the CCA are able to demonstrate that they have the necessary capability, financial capacity and/or assets to in substance manage and control the DEMPE activities and assume associated risks as agreed in the CCA.*

204. *While assessing the risk, we may consider the potential application of the transfer pricing provisions, including Subdivision 815-B of the ITAA 1997, and the CGT provisions in relation to AusCo's entry into the CCA (where relevant).*

#### *Risk Factors and Documentation and Evidence Expectations*

205. *In assessing the risk, we will request certain documentation, taking into account the Risk Factors and Documentation and Evidence Expectations. Whilst the typical documentation and evidence that we will seek is outlined in paragraphs 42 to 74 of this Guideline, our focus under this Example will be on:*

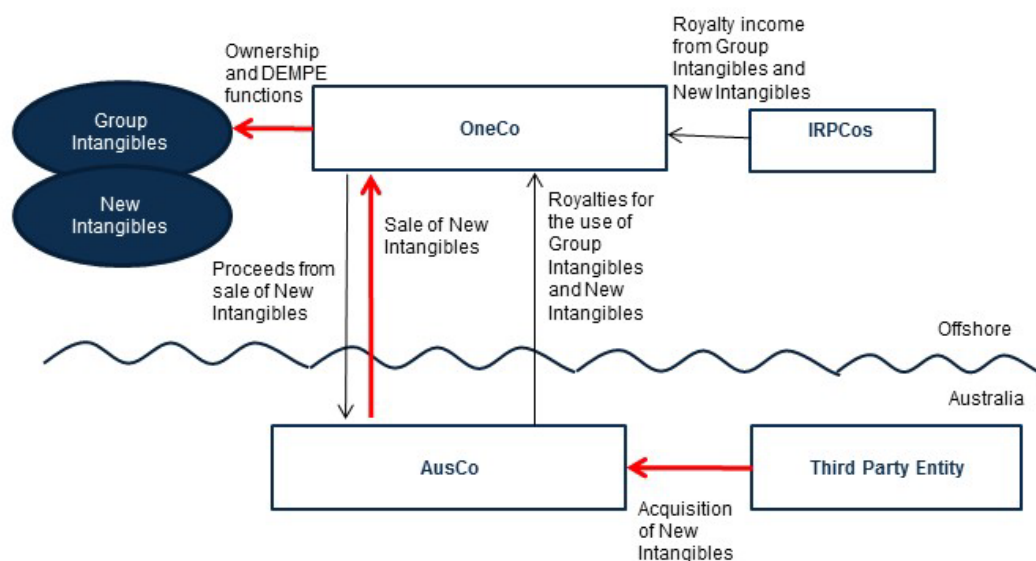
- *substantiating the (non-tax) commercial considerations of AusCo's entry into the CCA compared to any anticipated or potential tax effects of the CCA and the alternative options realistically available to AusCo – this may include understanding AusCo's business decision-making processes and associated analyses*
- *substantiating documentation to assist with determining whether AusCo's pre-existing and current contributions to the CCA and the economic*

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*outcomes and benefits obtained by AusCo are arm's length, having regard to the functions performed, assets used and risks assumed by all the participants to the CCA, and*

- *documents to assess the appropriateness of the tax and profit outcomes resulting from the arrangements, including the transfer pricing method, comparability studies applied and the independent valuation undertaken in relation to the arrangements.*

**Example 10 – centralisation of intangible assets – low risk**



206. *AusCo is part of a global group that develops, manufactures, markets and sells products globally. AusCo and its international related parties exploit valuable intangible assets in undertaking their operations. These intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights (Group Intangibles).*

207. *The Group Intangibles are centralised in a foreign related party, OneCo. OneCo has always owned, managed and controlled all DEMPE activities associated with the Group Intangibles. OneCo has material operations, including many specialised staff with the expertise and skill to manage, perform and control DEMPE activities with respect to the Group Intangibles.*

208. *AusCo does not perform development, enhancement, maintenance or protection activities with respect to any of the Group Intangibles, including R&D activities. AusCo pays a royalty to OneCo under a Royalty Agreement for the right to license and exploit the Group Intangibles in its ordinary business operations. The royalty paid under this agreement is determined as a percentage of sales. Both AusCo and OneCo comply with their Australian withholding tax obligations. AusCo maintains or provides documentation substantiating the arm's length nature of the royalty paid under this agreement.*

**Acquisition and transfer**

209. *AusCo acquires business assets from a third-party Australian entity. The acquired assets include intangible assets (New Intangibles). The New Intangibles are considered to complement the global group's existing Group Intangibles. The purchase price for the*

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*assets includes a value attributable to the New Intangibles, determined by an independent valuation of the New Intangibles, carried out just prior to the acquisition.*

210. *Shortly after AusCo acquires the New Intangibles, it transfers the New Intangibles to OneCo. The price at which OneCo purchases the New Intangibles from AusCo is not materially different to the independent value that was attributable as part of the purchase price when AusCo acquired the New Intangibles.*

211. *The decision to transfer the New Intangibles reflects the fact that OneCo has the appropriate expertise, staff and infrastructure to continue to own, manage and perform DEMPE functions with respect to the New Intangibles and that AusCo does not have the appropriate expertise, staff and infrastructure to perform DEMPE functions with respect to the New Intangibles. Following the transfer, AusCo does not perform any control functions relating to the maintenance, development, enhancement or protection of the New Intangibles. AusCo does exploit the New Intangibles in its ordinary business operations following the transfer and AusCo and OneCo amend their existing Royalty Agreement to include and factor in the New Intangibles to the Group Intangibles licensed by AusCo under the Royalty Agreement.*

212. *AusCo maintains or provides documentation substantiating the arm's length nature of the updated terms and pricing of the Royalty Agreement.*

#### *Risk assessment*

213. *The arrangement between AusCo and OneCo would be regarded as a Low Risk Intangibles Arrangement.*

214. *We would expect that the documentation maintained or provided by AusCo demonstrates a genuine and substantiated (non-tax) commercial rationale to support its decision to transfer the New Intangibles to OneCo. The commerciality of this decision can be supported by the level of OneCo's qualified staff and capability, the capacity of its operations and the expertise OneCo has to continue to perform DEMPE functions with respect to the New Intangibles, as compared with AusCo's absence of such staff, capability and capacity. These factors inform our assessment of the level of risk in this arrangement. We would expect AusCo to have prepared contemporaneous documentation demonstrating the relevant functions performed by OneCo.*

215. *It will be relevant to consider the amount attributable to the New Intangibles at the point at which AusCo acquired the New Intangibles and at the point at which the New Intangibles are transferred to OneCo. The arm's length nature of these transactions can be supported by the independent valuation undertaken just prior to acquisition of the New Intangibles by AusCo and AusCo's sale of the New Intangibles to ForCo.*

216. *We would also expect that the documentation and evidence maintained or provided by AusCo demonstrates the arm's length nature of its Royalty Agreement, both pre- and post-transfer of the New Intangibles, having regard to the pricing and terms of this arrangement. We would expect this documentation to substantiate the appropriateness of the tax and profit outcomes resulting from the arrangement, the transfer pricing method and comparability studies applied. It will be relevant to consider this documentation to determine whether the terms of the Royalty Agreement are consistent with those between independent parties, dealing wholly independently of one another in comparable circumstances to that of AusCo and OneCo.*

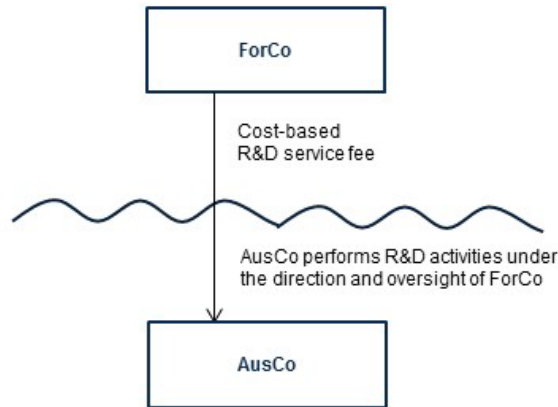
217. *When assessing the risk we would expect specific consideration be given to the transfer pricing provisions, including Subdivision 815-B.*



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**Example 11 – contract research and development arrangement – low risk**

218. Similarly to Example 8 of this Guideline, AusCo is part of a global group that manufactures and sells goods and provides associated services globally. AusCo and its international related parties exploit valuable intangible assets in undertaking their operations. The intangible assets include patents, know-how, trademarks, copyright and other intangible assets or rights (Existing Intangibles).

219. ForCo, a related party located in a foreign jurisdiction, is the entity that has always undertaken, managed and been responsible for the DEMPE activities associated with the Existing Intangibles. ForCo derives worldwide income from the exploitation of the Existing Intangibles by the global group.

220. In connection with managing and controlling the DEMPE activities associated with the Existing Intangibles, ForCo is responsible for managing the global group's R&D operations. The R&D operations consist of primary R&D centres which are located within ForCo's jurisdiction and several secondary R&D centres located outside of ForCo's jurisdiction, which perform R&D services for or on behalf of ForCo.

221. AusCo is party to an R&D services agreement with ForCo, under which it is remunerated with a service fee (R&D Services Agreement). AusCo maintains or provides documentation substantiating the arm's length nature of the service fee and the terms of the R&D Services Agreement.

222. Under the R&D Services Agreement:

- AusCo performs the R&D services under the direction and oversight of ForCo
- provision of the R&D services requires knowledge and use of the Existing Intangibles, and
- new intangible assets or improvements to the Existing Intangibles developed as a result of the R&D undertaken by AusCo will be owned by ForCo.

223. ForCo employs specialised staff and holds the necessary expertise and capability to manage the various contract R&D centres and undertake DEMPE activities. AusCo does not manage and control the risks associated with the relevant DEMPE activities, and performs R&D activities under the close supervision of ForCo. AusCo's R&D staff conduct



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*their R&D activities solely within scope of work orders received from ForCo and are monitored by relevant staff employed by ForCo, attending regular management and milestone reviews in connection with their project work.*

#### *Risk assessment*

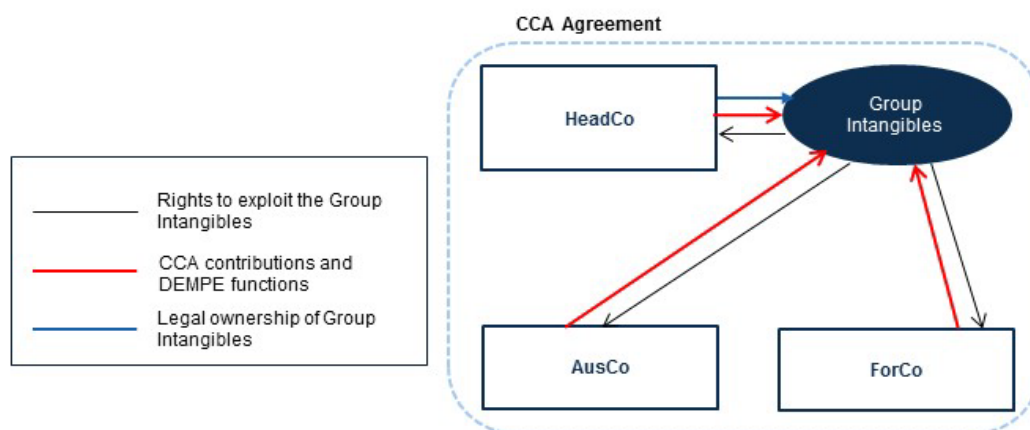
224. *The arrangement between AusCo and ForCo would be regarded as a Low Risk Intangibles Arrangement.*

225. *We would expect that the documentation and evidence maintained or provided by AusCo demonstrates the arm's length nature of the service fee received under the R&D Services Agreement and the terms of this arrangement. We would expect AusCo has prepared contemporaneous documentation substantiating the functions performed and risks assumed by AusCo and by ForCo with respect to the R&D activities governed by the R&D Services Agreement. This evidence demonstrating alignment between the substance and form of the R&D Services Agreement informs our assessment of the level of risk in this arrangement.*

226. *We would also expect the documentation and evidence maintained or provided by AusCo to substantiate the appropriateness of the tax and profit outcomes resulting from the arrangement, the transfer pricing method and comparability studies applied. It will be relevant to consider this documentation to determine whether the terms of the R&D Services Agreement are consistent with those between independent parties, dealing wholly independently of one another in comparable circumstances to that of AusCo and ForCo.*

227. *When assessing the risk we would expect specific consideration be given to the transfer pricing provisions, including Subdivision 815-B.*

#### **Example 12 – cost contribution arrangement – low risk**



228. *Similarly to Example 9 of this Guideline, AusCo is part of a global group headed by HeadCo. HeadCo's subsidiary, ForCo, is located in another foreign jurisdiction. AusCo, HeadCo and ForCo act as regional heads for the global group. The regional heads exploit a suite of valuable intangible assets, comprising patents, know-how, trademarks, copyright and other intangible assets or rights, in their ordinary business operations (Group Intangibles).*

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229. *AusCo, HeadCo and ForCo are party to a CCA under which they contribute resources and perform activities associated with the DEMPE of the Group Intangibles for the mutual benefit of all participants. AusCo, HeadCo and ForCo all have the qualified staff, capacity and capability to contribute the assets and services they agree to provide under the CCA.*

230. *Under the CCA, AusCo, HeadCo and ForCo jointly manage, direct and control activities associated with the DEMPE of the Group Intangibles and allocate R&D activities, managing these activities and the associated risks according to the terms of the CCA. HeadCo is the legal owner of the Group Intangibles and also owns, registers and protects all new intangible assets developed under, and associated with the CCA.*

231. *AusCo, HeadCo and ForCo perform R&D activities and make contributions to the CCA based on an allocation key. Both AusCo and ForCo obtain from HeadCo the right to exploit all intangible assets associated with the CCA in their respective jurisdictions. At the end of the income year, a balancing adjustment, based on the allocation key, is made where necessary to align each of HeadCo's, AusCo's and ForCo's share of costs with their share of expected benefits. AusCo maintains or provides documentation substantiating the arm's length nature of the pricing and terms of the CCA.*

#### *Risk assessment*

232. *The arrangement between AusCo, HeadCo and ForCo would be regarded as a Low Risk Intangibles Arrangement.*

233. *We would expect AusCo to have prepared contemporaneous documentation substantiating the alignment between its contributions under the CCA and its expected benefits, taking into account the extent and nature of functions performed, assets used and risks assumed by AusCo in connection with the intangible assets covered by the CCA as compared to the extent and nature of functions performed, assets used and risks assumed by HeadCo and ForCo.*

234. *We would also expect that AusCo's documentation and evidence substantiates the arm's length nature of the pricing of the arrangement, including all balancing adjustments made, allocations made to each entity and the basis of the allocation key adopted. The evidence pointing to an arm's length allocation of costs, contributions and benefits between AusCo, HeadCo and ForCo informs our assessment of the level of risk in this arrangement.*

235. *It will be relevant to consider the documentation and evidence maintained or provided by AusCo to determine whether the terms of the CCA are consistent with those that would be expected to operate between independent entities dealing wholly independently of one another in comparable circumstances to that of AusCo, HeadCo and ForCo.*

236. *When assessing the risk, we would expect specific consideration be given to the transfer pricing provisions, including Subdivision 815-B.*

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**Commissioner of Taxation**

19 May 2021

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## Your comments

237. You are invited to comment on this draft Guideline. Please forward your comments to the contact officer by the due date.

238. A compendium of comments is prepared when finalising this Guideline, and an edited version (names and identifying information removed) may be published to the Legal database on [ato.gov.au](http://ato.gov.au)

Please advise if you do not want your comments included in the edited version of the compendium.

**Due date:** 16 July 2021

**Contact officer:** Contact officer details have been removed following publication of new draft guideline.

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## References

### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations:*

LCR 2018/6

TR 2014/6

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### *Legislative references:*

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- ITAA 1997 815-130
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- ITAA 1997 815-130(3)
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### ATO references

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reduction  
International issues ~~ Transfer pricing ~~ Profit shifting

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