



# ***PCG 2023/D2 (Finalised) - Intangibles arrangements***

 This cover sheet is provided for information only. It does not form part of *PCG 2023/D2 (Finalised) - Intangibles arrangements*

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



Status: **draft only – for comment**

# Draft Practical Compliance Guideline

## Intangibles arrangements

### ❶ 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 Intangibles Arrangements involving international related parties. In this Guideline, 'Intangible Arrangements' refer to cross-border arrangements relating to the development, enhancement, maintenance, protection and exploitation (DEMPE) of intangible assets<sup>2</sup>, or the Migration of intangible assets that we have seen. A 'Migration' refers to any restructure

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<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> For the purpose of this Guideline, intangible assets refer to 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 20 January 2022; see also section 815-135(2)(a) of the *Income Tax Assessment Act 1997*.

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or change associated with your intangible assets that allows another entity to access, hold, use, transfer or benefit from the intangible assets.

2. This Guideline focuses on our compliance approach (primarily when we are more or less likely to apply resources to consider the potential application of the general anti-avoidance rules (GAARs) or the transfer pricing rules) with respect to:

- arrangements we have seen involving Migration of intangible assets, and
- arrangements we have seen involving mischaracterisation of Australian activities connected with the DEMPE of intangible assets.

3. This Guideline does not affect our compliance approach to other tax issues that might arise in connection with Intangibles Arrangements (for example, tax risks outlined in Taxpayer Alerts TA 2018/2 *Mischaracterisation of activities or payments in connection with intangible assets*<sup>3</sup> or TA 2022/2 *Treaty shopping arrangements to obtain reduced withholding tax rates*<sup>4</sup>).

4. For the avoidance of doubt, our compliance approach with respect to the proposed multinational tax integrity measure (*Denying deductions for payments relating to intangible assets connected with low corporate tax jurisdiction*)<sup>5</sup> is not covered by this Guideline.

5. Where the basic rule in section 815-130 of the ITAA 1997 applies, transfer pricing in respect of, and valuation of, an intangible asset are dependent on the facts and circumstances of individual arrangements. It is therefore outside the scope of this Guideline to determine the level of compliance risks associated with the transfer pricing of all related party dealings which arise in connection with properly characterised Intangibles Arrangements.

6. In this Guideline:

- Any reference to 'you' refers to the relevant Australian entity who is a party to the Intangibles Arrangement.
- All legislative references are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

### How to use this Guideline

7. We use the Risk Assessment Framework set out in this Guideline to assess the compliance risks associated with your Intangibles Arrangements and tailor our engagement with you.

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

- the kinds of compliance risks that may be presented by your Intangibles Arrangements
- the features of Intangibles Arrangements we consider to present greater compliance risk
- the evidence we are likely to ask you to produce in relation to your Intangibles Arrangements, including the level of engagement we would

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<sup>3</sup> In relation to the mischaracterisation of activities or payments in connection with intangible assets.

<sup>4</sup> In relation to treaty shopping arrangements to obtain reduced withholding tax rates.

<sup>5</sup> See the Exposure draft and explanatory material issued in March 2023 at [Multinational tax integrity – denying deductions for payments relating to intangible assets connected with low corporate tax jurisdictions](#)

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generally expect from you based on our assessment of the compliance risks of your Intangibles Arrangements.

9. This Guideline is not an exhaustive list of factors or example arrangements which may attract our attention in relation to the potential application of the transfer pricing rules or the GAARs.

## Structure of this Guideline

10. This Guideline is divided into the following parts:

- Part One – Our compliance approach – provides our compliance approach for Intangibles Arrangements.
- Part Two – Our risk assessment framework –explains how we assess the compliance risks of Intangibles Arrangements.
- Part Three – Our evidence expectations – provides an outline of the types and level of evidence that we will have regard to when examining your Intangibles Arrangements.

## Date of effect

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

Status: **draft only – for comment****PART ONE – Our compliance approach****The ATO's role and compliance approach**

12. This Guideline does not limit the operation of the law.<sup>6</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. However, we will have regard to our risk assessment framework and identify compliance risks associated with these arrangements in the course of our engagement or assurance activities.

13. Australia's income tax law places an onus on taxpayers to self-assess their compliance with relevant tax laws. 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*.

14. To the extent relevant and applicable, any action we may take in applying the transfer pricing provisions will be made so as to best achieve consistency with the relevant transfer pricing guidelines published by the OECD.<sup>7</sup> This includes our risk assessment approach in relation to the application of transfer pricing provisions. Of particular relevance are Chapters I, VI and IX of the OECD Transfer Pricing Guidelines.<sup>8</sup>

15. We also review Intangibles Arrangements to ensure they properly comply with other Australian tax obligations such as those imposed by the capital gains tax (CGT) and capital allowance provisions.

16. We may also consider the application of the GAARs (including the diverted profits tax (DPT))<sup>9</sup>, particularly in circumstances where an arrangement (or a part of an arrangement) lacks substance or probative evidence of the stated non-tax or commercial rationale. In these circumstances, we will have specific regard to our administrative processes and published guidance including Law Administration Practice Statements PS LA 2005/24 *Application of General Anti-Avoidance Rules* and PS LA 2017/2 *Diverted profits tax assessments*, and Practical Compliance Guideline PCG 2018/5 *Diverted profits tax*.

17. If your Intangibles Arrangement is rated high risk based on our risk assessment framework, we are likely to prioritise our resources to further engage with you to assess the compliance risks of your Intangibles Arrangement. This may involve commencing a further review or audit.

18. If your arrangement is rated low risk, we are unlikely to prioritise our resources to further examine or audit your arrangement, particularly where we have verified your

<sup>6</sup> For example, this Guideline does not limit the operation of Subdivision 284-E of Schedule 1 to the *Taxation Administration Act 1953* (TAA), which sets out special rules about unarguable positions for cross-border transfer pricing.

<sup>7</sup> See, for example, paragraphs 815-20(2)(a) and 815-135(2)(a). Of particular relevance are the relevant edition of the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD Transfer Pricing Guidelines).

<sup>8</sup> Broadly, these chapters cover:

- the basic operation of the arm's length principle (Chapter I)
- the special considerations for Intangibles, including the identification and ownership of intangibles and DEMPE activities (Chapter VI), and
- guidance on analysing the transfer pricing outcomes in relation to business restructuring situations (Chapter IX).

<sup>9</sup> As outlined in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936).

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self-assessment. However, where your Intangibles Arrangement meets the requirements to achieve a low risk rating, but there is evidence that it has been incorrectly priced, the application of this Guideline will not necessarily preclude that Intangibles Arrangement from further compliance activity (refer to paragraph 5 of this Guideline).

19. If your arrangement is rated medium risk, while we may also engage further with you to assess the compliance risks of your Intangibles Arrangement, it is likely that we will not prioritise our resources to review your arrangements over arrangements which have been rated as high risk.

20. While being rated medium or low risk may not exclude your Intangibles Arrangement from further engagement or review, they will likely influence how we will engage with you including where we assess or verify the evidence that you have produced and maintained to substantiate your Intangibles Arrangements.

21. Where you are seeking entry to the advance pricing arrangement (APA) program, we will have regard to your risk rating in accordance with our risk assessment framework.<sup>10</sup> We would also expect evidence of the nature identified in this Guideline to be produced with respect to your Intangibles Arrangements both when you are seeking entry to the APA program, as well as during the APA period.

22. 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 there is a potential compliance risk associated with your Intangibles Arrangements. Engaging with us early, including prior to entering into your Intangibles Arrangements, will assist us to cooperatively work with you to assure your arrangement or resolve any issues that may be associated with your Intangibles Arrangements.

23. 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.

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

24. You may be required to report your risk rating for each Intangibles Arrangement or on another basis. For example, you may have other disclosure requirements if you are required to complete a reportable tax position schedule.

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

25. We may engage with you to verify your self-assessment, having regard to your application of our risk assessment framework and our Evidence Expectations (as outlined in Part Three and Appendix 2 of this Guideline).

26. We may also prioritise our resources to further examine or audit your Intangibles Arrangements where we are unable to obtain evidence to substantiate your self-assessment against our risk assessment framework.

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<sup>10</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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## **PART TWO – Our risk assessment framework**

27. This Part is designed to explain how we assess the compliance risks of Intangibles Arrangements.

28. Our risk assessment framework will assist you to determine your risk rating under this Guideline. As outlined in Part One of this Guideline, your risk rating will influence our engagement with you.

29. Our risk assessment framework includes an assessment of the risk of your Intangibles Arrangements based on risk factors set out in Risk Assessment Framework Tables 1 and 2 in this Part, which cover the features of arrangements that we consider indicate compliance risks.

30. In this risk assessment framework:

- Risk Assessment Framework Table 1 should be used to assess the compliance risks in relation to a Migration of your intangible assets
- Risk Assessment Framework Table 2 should be used to assess the compliance risks associated with your Australian DEMPE activities; in particular, any risks of mischaracterisation and non-recognition of Australian DEMPE activities.

31. Your self-assessment will include an assessment of your Intangibles Arrangements against each of the risk factors in the applicable table to determine if your arrangement is considered to be high, medium or low risk (risk rating) with respect to that risk.

### **How to self-assess your compliance risk**

32. You should apply our risk assessment framework to **each** Intangibles Arrangement that you have during the income year:

- for existing arrangements, before tax returns for the relevant income year are lodged, or
- where a new arrangement is entered into during an income year, at the time it is entered into.

### ***Identifying Intangibles Arrangements in applying the risk assessment framework***

33. In some circumstances, you may have more than one dealing or arrangement connected with the same intangible asset, for example, you may have both a contract research and development (R&D) service agreement as well as a licensing agreement with the owner of the intangible assets. In those circumstance, in applying the risk assessment framework, you should treat all your dealings or arrangements in connection with the same intangible assets as one Intangibles Arrangement.

34. We recognise that some intangible assets may be naturally grouped together by your business, for example, all intangible assets associated with a particular product. In such circumstances and where appropriate, you can adopt the grouping according to your business systems and governance systems and consider the dealings and transactions related to the group of intangible assets as one Intangibles Arrangement in applying the risk assessment framework.



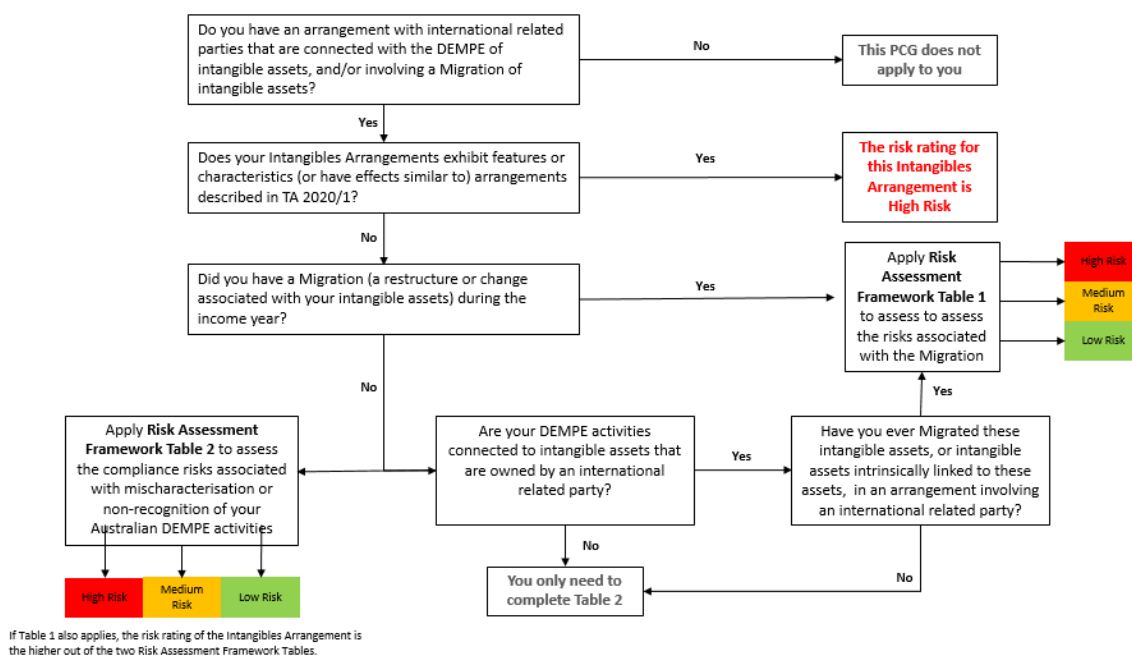
Status: **draft only – for comment****Using examples of Intangibles Arrangements to assess your compliance risks**

35. Appendix 1 of this Guideline provides examples of Intangibles Arrangements that are considered to be high, medium and low risk.

36. The high risk examples in Appendix 1, as well as Taxpayer Alert TA 2020/1 *Non-arm's length arrangements and schemes connected with the development, enhancement, maintenance, protection and exploitation of intangible assets*, indicate the kinds of arrangements that pose the highest level of compliance risk and have a higher likelihood of attracting the potential application of the exceptions to the basic rule contained in Subdivision 815-B and/or the potential application of the GAARs.

Arrangements that exhibit features, characteristics or have an effect similar to that of the high risk examples will attract a higher level of scrutiny.

37. The low risk examples are arrangements that pose the lowest level of compliance risk because they exhibit features or characteristics that we would regard as low risk.

**Diagram 1: Applying the risk assessment framework****The risk assessment framework**

38. If you have one or more Intangibles Arrangement, complete the risk assessment framework in relation to **each** one. The risk assessment framework is also depicted in Diagram 1 of this Guideline.

39. Answer the following questions to apply the risk assessment framework to each of your Intangibles Arrangements:

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**1. Does your Intangibles Arrangement involve an international related party?**

If **no**, the risk assessment framework and compliance approach set out in this Guideline does not apply to this Intangibles Arrangement.

**2. Does your Intangibles Arrangement exhibit features or characteristics of (or have effects similar to) the arrangements described in TA 2020/1?**

If **yes**, your Intangibles Arrangement is considered to be high risk and you do not need to complete the rest of the risk assessment framework to determine your risk rating in relation to this Intangibles Arrangement.

**3. Did you have a Migration of your intangible assets during the income year?**

A 'Migration' refers to any restructure or change associated with your intangible assets that allows another entity to access, hold, use, transfer, or benefit from the intangible assets.

- If yes, apply Risk Assessment Framework Table 1
- If **no**, apply Risk Assessment Framework Table 2 – refer to the first part of Risk Assessment Framework Table 2 to determine whether you also need to apply Risk Assessment Framework Table 1.

### ***Risk rating***

40. For each of your Intangibles Arrangements, your risk rating is determined by the number of points you score in either Risk Assessment Framework Tables 1 or 2 of this Guideline:

- high risk – 25 points or more
- medium risk – 19 to 24 points
- low risk – less than 19 points

41. The risk rating under each Risk Assessment Framework table reflects the assessment of the compliance risks posed by an Intangibles Arrangement with respect to a Migration of intangible assets or the mischaracterisation or non-recognition of Australian DEMPE activities respectively.

42. If you achieve a different risk rating under the 2 tables, the higher risk rating would be the overall risk rating for an Intangibles Arrangement.

### ***Definition of terms used in the risk assessment framework***

43. The following terms are used in the risk assessment framework. A reference the singular is also a reference to plural:

- **Relevant Entity** means
  - In Risk Assessment Framework Table 1, the international related party referenced in Question 1 for the type of transaction or change that applies to your Intangibles Arrangement.

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- In Risk Assessment Framework Table 2, the international related party referenced in Question 1 of Risk Assessment Framework Table 2.
- Where the party to the transaction or change is a branch of the Relevant Entity, this term refers to that branch of the Relevant Entity.
- **Relevant Intangible Assets** (used in Risk Assessment Framework Table 1 only) means the intangible assets which are the subject of your transaction or arrangement that you have identified in Question 1 of Risk Assessment Framework Table 1.
- **International related party** is as defined in the instructions to the International Dealings Schedule for the relevant income year, and also includes an entity which is part of your tax consolidated group or multiple entry consolidated group and satisfies that definition.
- **Specified jurisdiction** is as defined in the instructions to the International Dealings Schedule for the relevant income year.

#### **Risk Assessment Framework Table 1 – risk factors – Migration of your intangible assets**

44. Complete Risk Assessment Framework Table 1 to assess the compliance risks in relation to a Migration of intangible assets.<sup>11</sup>

##### ***Risk Assessment Framework Table 1: Risk factors for Migration of intangible assets***

#### **A. Restructure or Change**

1. Add **5 points** if any of the following applies to you.

You have restructured, or had a change associated with, intangible assets held by you or from which you benefit (whether in legal form or in substance), where:

- You have legally or beneficially transferred, assigned or otherwise made available the intangible assets to an international related party (Relevant Entity).
- You have entered into an arrangement (whether or not in writing) where you have licensed, granted rights or access to, or otherwise made available the intangible assets to an international related party (Relevant Entity).
- You have entered into a cost contribution agreement (or a similar agreement) with an international related party (Relevant Entity) relating to the intangible assets under which that entity obtains rights or access to the intangible assets.
- You have:
  - written off some or all of the intangible assets, or discontinued your development, enhancement or maintenance activities in respect of the intangible assets, and
  - an international-related party (Relevant Entity) is provided with, or otherwise obtained access to, intangible assets including any work-in-progress results of your development or enhancement activities.
- You have otherwise changed your Intangible Arrangements where the functions, assets or risks relating to activities contributing to the DEMPE of the intangible assets has been transferred to an international related party (Relevant Entity) – for example<sup>12</sup>, there has been a change in your activities such that you are no longer

<sup>11</sup> A 'Migration' refers to any restructure or change associated with your intangible assets that allows an international-related party to access, hold, use, transfer or obtain benefit from the intangible assets.

<sup>12</sup> These examples are illustrative only and are not intended to be exhaustive.

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	considered to be an ‘entrepreneur’ and have become a ‘distributor’ or ‘service provider’.
2.	<p>Add <b>5 points</b> if, in connection with, or following the restructure or change identified in Question 1, you have entered into an arrangement with a Relevant Entity that involves your continued use of or benefit from the Relevant Intangible Assets (or intangible assets that relate to the Relevant Intangible Assets), or you continue to be involved in the development, enhancement, maintenance or protection of the Relevant Intangible Assets (or intangible assets that relate to the Relevant Intangible Assets).</p> <p>Examples include but are not limited to:</p> <ul style="list-style-type: none"> <li>the use of such intangible assets in the manufacturing, marketing or distribution of products or rendering services connected to or otherwise utilising the Relevant Intangible Assets</li> <li>the performance of R&amp;D activities in connection with such intangible assets in Australia</li> <li>the licensing or entry into a cost sharing agreement granting you the right to use such the intangible assets.</li> </ul>
<b>B.</b>	<b>Substance of the Relevant Entity</b>
3.	<p>Following the restructure or change identified in Question 1, which category best describes the activities of the Relevant Entity in connection with the Relevant Intangible Assets?</p> <p>Where there is more than one Relevant Entity in your Intangibles Arrangement, include the score for the Relevant Entity with the highest number of points.</p> <p><b>Category 1 (assign 15 points):</b></p> <ul style="list-style-type: none"> <li>The Relevant Entity is newly established or in the initial stages of establishing operations.</li> <li>The Relevant Entity has no or very few staff or it does not currently have qualified staff with the expertise or skills to independently manage, perform or control the DEMPE activities connected to the Intangible Assets.</li> <li>DEMPE activities connected to the Intangible Assets continue to be or are primarily conducted by persons located Australia (including operating through a branch).</li> <li>The Relevant Entity has no, or very limited, capacity<sup>13</sup> to assume the risks associated with the DEMPE activities in relation to the Intangible Assets.</li> <li>The Relevant Entity completely or predominantly outsources DEMPE activities.</li> </ul> <p><b>Category 2 (assign 9 points):</b></p> <ul style="list-style-type: none"> <li>The Relevant Entity employs qualified staff, and has the ability to independently perform, manage and control some of the DEMPE activities connected to the Relevant Intangible Assets, however, is not currently able to wholly manage, perform and control the DEMPE activities connected to the Relevant Intangible Assets, including the assumption of the associated risks. This includes circumstances where the Relevant Entity is anticipated to transition to a position where it has qualified staff, capacity and capability to perform, manage and control all of the DEMPE activities in the future.</li> </ul> <p><i>However, in circumstances where the qualified staff employed by Relevant Entity to perform such activities in relation to the Relevant Intangible Assets are predominantly the same staff who had previously performed the same activities in Australia (but relocated, were contracted to, or became employed by the Relevant Entity), the category would be Category 1.</i></p>

<sup>13</sup> Including financial capacity.

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<ul style="list-style-type: none"> <li>The Relevant Entity outsources some DEMPE activities<sup>14</sup> but there is not a high degree of oversight and supervision from the Relevant Entity (refer to Example 11 of this Guideline for examples of high degree of oversight and supervision).</li> </ul> <p><b>Category 3 (assign 0 points):</b></p> <ul style="list-style-type: none"> <li>The Relevant Entity has always managed, owned and controlled DEMPE activities in relation to the Relevant Intangible Assets and employs staff with the relevant expertise and skills.</li> <li>All DEMPE activities are undertaken by the Relevant Entity OR Australian associates perform services (such as contract R&amp;D) for the Relevant Entity under a high degree of oversight and supervision from the Relevant Entity (refer to Example 11 of this Guideline for examples of high degree of oversight and supervision).</li> </ul> <p>4. Deduct <b>5 points</b> if the Relevant Entity is resident in the jurisdiction which is also the jurisdiction in which the products or services related to the Relevant Intangible Assets are predominantly sold.</p>	<p><b>C. Tax outcomes of the Intangibles Arrangement</b></p> <p>5. Add <b>10 points</b> if one or more of the following applies:</p> <ul style="list-style-type: none"> <li>the Relevant Entity or the Relevant Intangible Assets are subject to a preferential tax regime considered to be harmful according to the OECD Forum on Harmful Tax Practices</li> <li>the Relevant Entity has a tax holiday, exemption or concession in relation to income from the Relevant Intangible Assets or more broadly</li> <li>the Relevant Entity is resident or is a branch in a specified jurisdiction</li> <li>the Relevant Entity has available to it R&amp;D offsets or credits or amortisation or depreciation deductions in relation to the Relevant Intangible Assets, or significant tax losses, that are anticipated to substantially offset or shelter the income derived (or expected to be derived) by the Relevant Entity from the Relevant Intangible Assets</li> <li>the Relevant Entity is a foreign hybrid company under Division 830, and a member of your tax consolidated group or multiple entry consolidated group</li> <li>the Relevant Entity has different income tax treatment in two or more jurisdictions.<sup>15</sup></li> </ul> <p>6. Add <b>10 points</b> if:</p> <ul style="list-style-type: none"> <li>as a result of the restructure or change to your intangible assets, excluding capital gains<sup>16</sup> from the disposal of the intangible assets, your taxable income is, or might reasonably be expected to be, less than it would have been if the restructure of, or change associated with, the Relevant Intangible Assets had not been entered into, or</li> <li>the restructure or change is recognised as an acquisition of the Relevant Intangible Assets in a foreign jurisdiction for tax purposes, but is not recognised or taxed as a disposal in Australia for tax purposes.</li> </ul>
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### Risk Assessment Framework Table 2 – risk factors – other Intangibles Arrangements

45. Complete this table if, during the income year, you had an Intangibles Arrangement connected with the DEMPE of intangible assets that did not involve a Migration of intangible assets in the current year.

<sup>14</sup> Including where you, or your Australian-related parties, are performing services (such as R&D) for the Relevant Entity.

<sup>15</sup> For example, the entity is viewed as opaque (for example, taxed as a company) in a jurisdiction but is viewed as flow-through or disregarded in one or more other jurisdictions.

<sup>16</sup> Including your gains from a balancing adjustment event in relation to a depreciating asset under Division 40.

Status: **draft only – for comment*****Risk Assessment Framework Table 1: Risk factors for mischaracterisation of DEMPE activities in connection with Intangibles Arrangements***

<b>Risk factors</b>	
<b>Past Migration – complete Risk Assessment Framework Table 1 in relation to the Migration of your intangible assets</b>	
<p>If your Intangibles Arrangement relates to, or is intrinsically linked to, intangible assets or products in connection with intangible assets that have previously been held (legally or beneficially) by you, also complete Risk Assessment Framework Table 1 of this Guideline in relation to the Migration if it involved an international-related party.</p> <p>In applying Risk Assessment Framework Table 1 of this Guideline to assess the compliance risks in relation to the Migration, answer each question based on the circumstances as at the time of the Migration.</p>	
<b>A. Your overall characterisation</b>	
1.	<p>If:</p> <ul style="list-style-type: none"> <li>• you do not own the intangible assets and an international related party (Relevant Entity) holds the intangible assets legally or beneficially, or</li> <li>• you own the intangible assets where an international related party (Relevant Entity) is granted access to, or use of, the intangible assets without entering into a legal agreement with you for the transfer, cost and benefit sharing, or licensing of these assets</li> </ul> <p>assign the following risk score depending on how many of the following apply to you (that is, <b>1 – 10 points; 2 – 15 points; 3 – 20 points</b>)</p> <ul style="list-style-type: none"> <li>• you conduct or perform R&amp;D activities in connection with those intangible assets in Australia</li> <li>• you perform business activities or functions which might reasonably be expected to enhance or add value of those intangible assets in Australia. Examples include manufacturing activities, marketing activities, installation, customisation or other support services for digital products, conducting regulatory functions to seek market access and authorisation.</li> <li>• You perform other development, enhancement, maintenance or protection (DEMP) activities in connection with those intangible assets in Australia.</li> </ul>
<b>B. Substance of the Relevant Entity</b>	
2.	<p>Which category best describes the activities of the Relevant Entity in connection with the intangible assets referred to in Question 1 of this Risk Assessment Framework Table?</p> <p>Where there is more than one Relevant Entity in your Intangibles Arrangement, include the score for the Relevant Entity with the highest number of points.</p> <p><b>Category 1 (assign 15 points):</b></p> <ul style="list-style-type: none"> <li>• The Relevant Entity is newly established or in the initial stages of establishing operations.</li> <li>• The Relevant Entity has no or very few staff or it does not currently have qualified staff with the expertise or skills to independently manage, perform or control the DEMPE activities connected to the intangible assets.</li> <li>• DEMPE activities connected to the intangible assets continue to be or are primarily conducted by persons located in Australia (including operating in through a branch).</li> <li>• The Relevant Entity has no, or very limited, capacity<sup>17</sup> to assume the risks associated with the DEMPE activities in relation to the intangible assets.</li> <li>• The Relevant Entity completely or predominantly outsources DEMPE activities.</li> </ul>

<sup>17</sup> Including financial capacity.

Status: **draft only – for comment****Category 2 (assign 9 points):**

- The Relevant Entity employs qualified staff, and has the ability to independently perform, manage and control *some* of the DEMPE activities connected to the intangible assets; however is not currently able to wholly manage, perform and control the DEMPE activities connected to the intangible assets including the assumption of the associated risks. This includes circumstances where the Relevant Entity is anticipated to transition to a position where it has qualified staff, capacity and capability to perform, manage and control all of the DEMPE activities in the future.

*However, in circumstances where the qualified staff employed by Relevant Entity to perform such activities in relation to the intangible assets are predominantly the same staff who had previously performed the same activities in Australia (but relocated, were contracted to, or became employed by the Relevant Entity), the category would be Category 1.*

- The Relevant Entity outsources some DEMPE activities<sup>18</sup>, but there is not a high degree of oversight and supervision from the Relevant Entity (refer to Example 11 of this Guideline for examples of high degree of oversight and supervision).

**Category 3 (assign 0 points):**

- The Relevant Entity has always managed, owned and controlled DEMPE activities in relation to the Relevant Intangible Assets and employs staff with the relevant expertise and skills.
- All DEMPE activities are undertaken by the Relevant Entity OR Australian associates perform services (such as contract R&D) for the Relevant Entity under a high degree of oversight and supervision from the Relevant Entity (refer to Example 11 of this Guideline for examples of high degree of oversight and supervision).

**C. Tax outcomes****3. Add 5 points if:**

- the Relevant Entity or the Relevant Intangible Assets are subject to a preferential tax regime considered to be harmful according to the OECD Forum on Harmful Tax Practices
- the Relevant Entity has a tax holiday, exemption or concession in relation to income from the Relevant Intangible Assets or more broadly
- the Relevant Entity is resident or is a branch in a specified jurisdiction
- the Relevant Entity has available to it R&D offsets or credits, amortisation or depreciation deductions in relation to the Relevant Intangible Assets, or significant tax losses, that are anticipated to substantially offset or shelter the income derived (or expected to be derived) by the Relevant Entity from the intangible assets
- the Relevant Entity is a foreign hybrid company under Division 830, and a member of your tax consolidated group or multiple entry consolidated group, or
- the Relevant Entity has different income tax treatments in 2 or more jurisdictions.<sup>19</sup>

<sup>18</sup> Including where you, or your Australian-related parties, are performing services (such as R&D) for the Relevant Entity.

<sup>19</sup> For example, the entity is viewed as opaque (for example, taxed as a company) in a jurisdiction but is viewed as flow-through or disregarded in one or more other jurisdictions.

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## **PART THREE – Our evidence expectations**

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46. Appendix 2 of this Guideline sets out the types of evidence that we are likely to have regard to when examining your Intangibles Arrangements and would typically expect taxpayers to be able to produce to substantiate their arrangements.

47. The evidence outlined in Appendix 2 of this Guideline is intended to serve as a general guide and should not be treated as an exhaustive list. It is not the intention of this Guideline to unnecessarily impose burdensome requirements on you in respect of the evidence required to substantiate your Intangibles Arrangements. However, setting out the kinds of information and documents we are likely to request may assist you to mitigate the level of compliance risk posed by your Intangibles Arrangements and ensure that any engagement with us is as efficient as possible.

48. We recognise that certain evidence identified in Appendix 2 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 evidence that is expected. In these circumstances, your substantiation should focus on whether there is sufficient information to enable us to verify the information and to reach a proper assessment of your Intangibles Arrangements.

49. The type and level of evidence we expect from you will be influenced by the complexity of your business and the extent to which your Intangibles Arrangements contribute to that business. We will also consider your business systems and governance processes, including any appropriate materiality thresholds that you apply or follow in your business in relation to the management or governance of your, or your global group's, intangible assets, to focus on evidence that can reasonably be expected to be created and relied on in your business.

50. The expectations outlined in this Part and Appendix 2 should not be viewed as replacing or substituting the requirements for transfer pricing documentation under 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*). Notwithstanding that, our Evidence Expectations may assist you in being able to support and verify your transfer pricing documentation for the purposes of Subdivision 284-E of Schedule 1 to the TAA.



Status: **draft only – for comment**

## APPENDIX 1 – Examples of Intangibles Arrangements

51. This Appendix provides examples of Intangibles Arrangements to illustrate the kinds of matters we will generally consider in assessing the compliance risks relating to your Intangibles Arrangements. The application of the risk assessment framework is also included to illustrate how the framework applies to arrangements. They highlight the circumstances in which we consider the compliance risks that may be associated with your Intangibles Arrangements and the facts that may support this assessment.

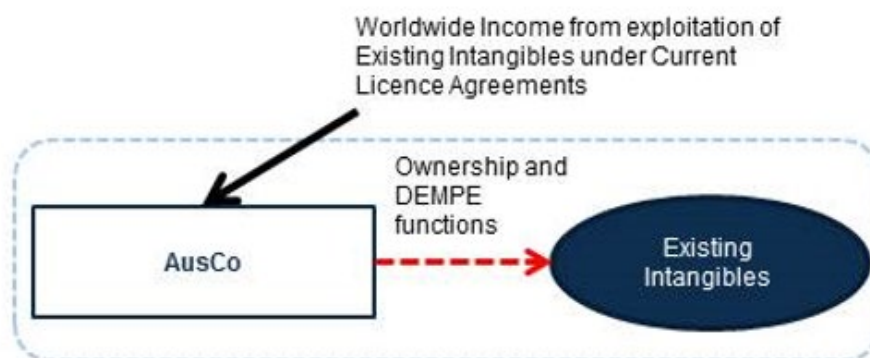
52. It is important to note that any reference to a particular intangible asset, industry or commercial activity in the examples is anecdotal and does not limit the particulars of an example arrangement to any one industry.

**Table 1: Examples of arrangements and the level of risk**

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 – Migration of pre-commercialised intangible assets Example 6 – transfer of intangible assets to a foreign hybrid entity
<b>Medium risk</b>	Example 7 – centralisation of intangible assets Example 8 – transfer of rights to intangible assets under licence agreement Example 9 – contract research and development arrangement
<b>Low risk</b>	Example 10 – centralisation of intangible assets Example 11 – contract R&D arrangement Example 12 – cost contribution arrangement Example 13 – service arrangement involving intangible assets

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

**Diagram 2: Example 1 – overview of current arrangement**



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#### *Current arrangement*

53. *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, trade marks, copyright and other intangible assets or rights (Existing Intangibles).*

54. *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).*

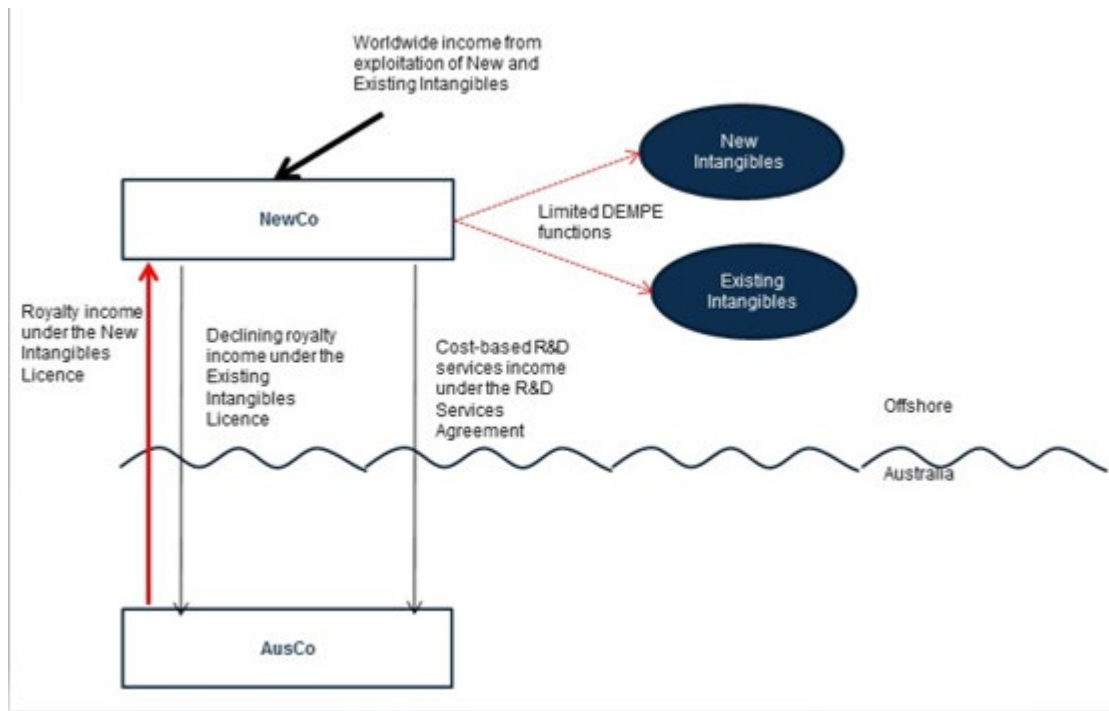
#### *Decision to centralise intangible assets*

55. *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, trade marks, copyright and other intangible assets or rights that form part of the Existing Intangibles.*

56. *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. 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.*

57. *The Current Licence Agreements between AusCo and its international related parties are terminated. 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.*

58. *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.*

Status: **draft only – for comment****Diagram 3: Example 1 – overview of new arrangement****New arrangement**

59. 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 result 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.

60. 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 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.

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Status: **draft only – for comment**


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*Risk assessment*

61. This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.

**Table 2: Example 1 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	<ul style="list-style-type: none"> <li>AusCo has licensed Intangibles to NewCo</li> <li>AusCo continues to perform and control DEMPE activities for NewCo</li> </ul>	10 (5 + 5)
Substance of the Relevant Entity	NewCo is a newly established entity with few employees	15
Tax outcome of the Intangibles Arrangement	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	10

62. The total risk score in relation to the New Arrangement is 35.<sup>20</sup> The New Arrangement would be regarded as a high risk Intangibles Arrangement.

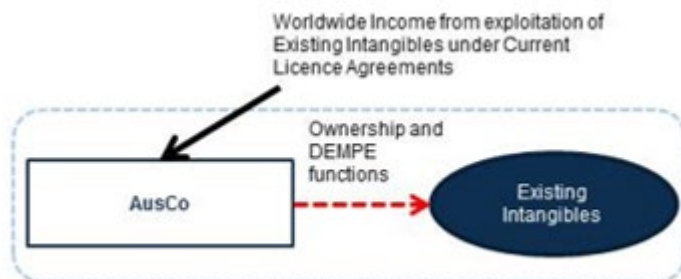
63. AusCo continued to perform and control DEMPE activities with respect to the Existing Intangibles and the New Intangibles. The New Arrangement does not appropriately recognise AusCo's contributions to the New Intangibles, either through a recognition of the intrinsic link between the Existing and New Intangibles or a recognition of the DEMPE activities performed by AusCo in substance in relation to the New Intangibles.

64. 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.

65. 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.

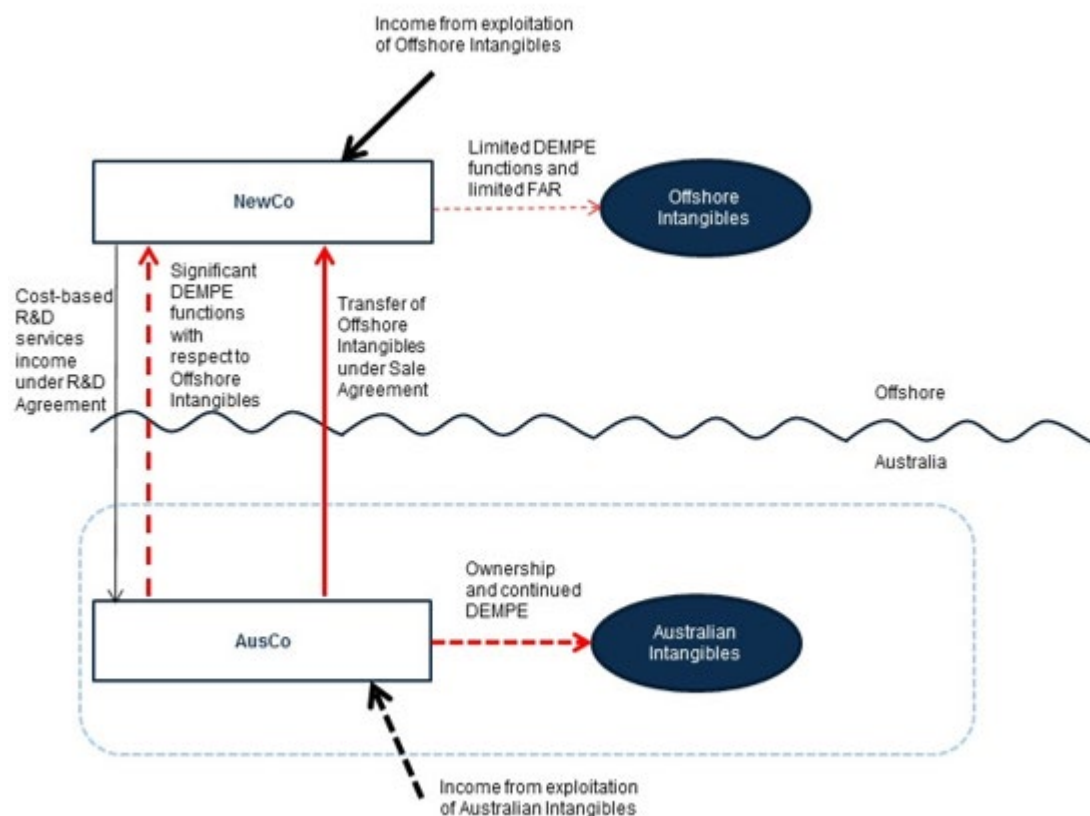
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<sup>20</sup> If one or more tax attributes listed at Question 5 of Risk Assessment Framework Table 1 of this Guideline applies, the risk score will be higher.

Status: **draft only – for comment****Example 2 – bifurcation of intangible assets – high risk****Diagram 4: Example 2 – overview of current arrangement****Current arrangement**

66. 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, trade marks, copyright and other intangible assets or rights (Existing Intangibles).

67. 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).

**Diagram 5: Example 2 – overview of new arrangement**

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*New arrangement*

68. *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).*

69. *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).*

70. *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). While AusCo has prepared transfer pricing documentation that focuses on determining whether the cost-based R&D services income received under the R&D arrangement is arm's length; it is not able to evidence the commercial rationale in making the decision to transfer the Offshore Intangibles to NewCo.*

71. *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.*

72. *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.*

73. *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.*

74. *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.*

75. *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.*

76. *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.*

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*Risk assessment*

77. This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.

**Table 3: Example 2 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	AusCo has transferred Offshore Intangibles to NewCo; post-transfer, AusCo provides R&D services to NewCo	10
Substance of the Relevant Entity	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. The relocation of staff who had previously performed the same activities in Australia would not result in this being in a category other than Category 1.	15
Tax outcomes of the Intangibles Arrangement	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.	10

78. The total risk score in relation to the New Arrangement is 35. The New Arrangement would be regarded as a high risk Intangibles Arrangement.

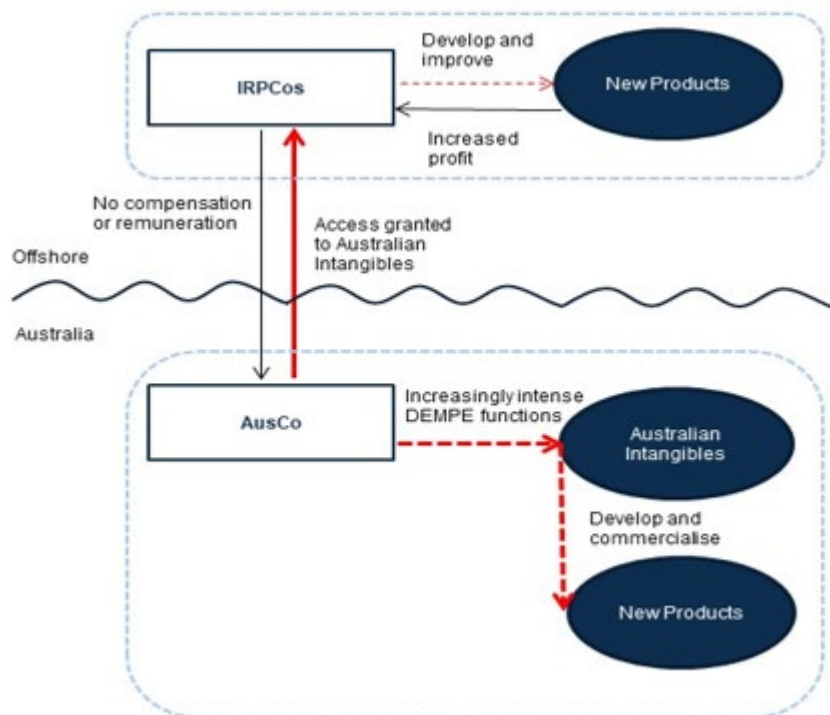
79. There is a risk that the New Arrangement has artificially bifurcated the Existing Intangibles into Australian Intangibles and Offshore Intangibles such that the New Arrangement is not arm's length in nature or is structured to avoid tax obligations. The risk in this regard is emphasised where AusCo is not able to provide evidence substantiating its decision-making for entering into this arrangement or does not recognise or provide evidence referring to anticipated or potential Australian tax impacts that were considered in making the decision to enter into the arrangement.

80. 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.

81. 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.

82. 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.



Status: **draft only – for comment****Example 3 – non-recognition of Australian intangible assets and DEMPE activities – high risk****Diagram 6: Example 3 – overview of arrangement**

83. 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 trade marks and intangible assets associated with the global group's brand and product lines. A number of these trade marks 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 trade marks and assumes associated risks.

84. 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 trade marks are developed, maintained, enhanced and owned by AusCo (Australian Intangibles).

85. 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.

86. In the following years, a number of AusCo's international related parties (IRP Cos) 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



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

87. *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*

88. *This is not a Migration of intangible assets. According to Risk Assessment Framework Table 2 of this Guideline, the risk assessment is as follows.*

**Table 4: Example 3 – application of risk assessment factors**

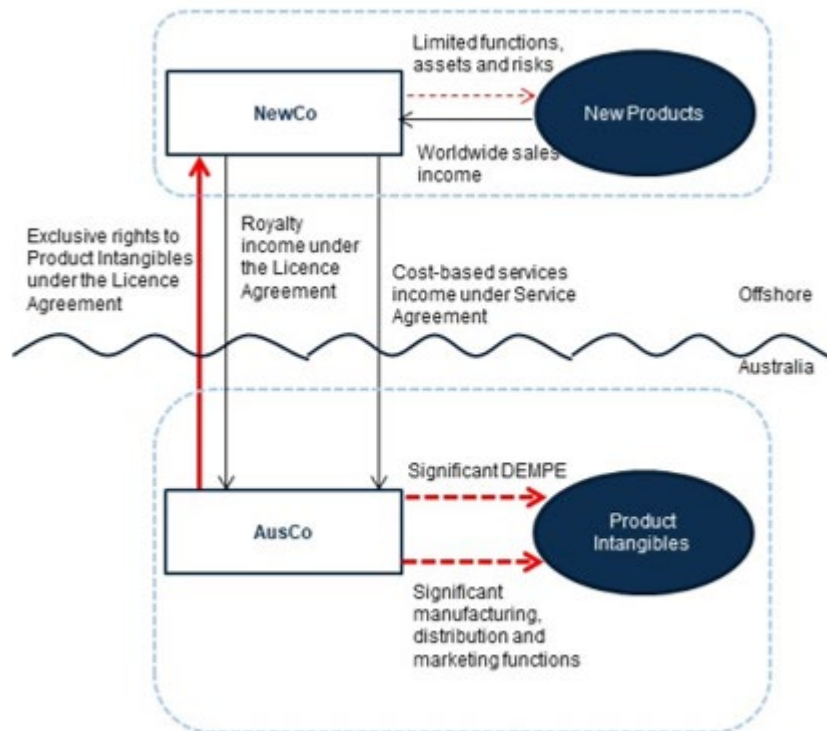
<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Overall characterisation of AusCo	AusCo performs DEMPE activities, including development of new Intangible assets <b>and</b> its related parties were granted access to AusCo's intangible assets without a legal agreement	20
Substance of the Relevant Entity	IRP Cos—Given that AusCo performs and controls the DEMPE activities associated with these intangible assets, IRP Cos' substance in relation to these intangible assets would be best described as Category 1	15
Tax outcomes of the Intangibles Arrangement	No specific tax outcomes are noted	0

89. *The total risk score for this arrangement is 35. This arrangement would be regarded as a high risk Intangibles Arrangement.*

90. *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.*

91. *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.*

92. *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.*

Status: **draft only – for comment****Example 4 – Migration of pre-commercialised intangible assets – high risk****Diagram 7: Example 4 – overview of arrangement**

93. 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, trade marks, copyright and other intangible assets or rights.

94. 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.

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

96. 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.

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Status: **draft only – for comment**


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97. 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.

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

98. 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.

99. 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*

100. This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.

**Table 5: Example 4 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	AusCo and NewCo enter into a licence agreement in relation to the Product Intangibles. Afterwards, AusCo continues to provide development, manufacturing and distribution services in relation to New Products	10
Substance of the Relevant Entity	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	15
Tax attributes – Relevant Entity	NewCo is a resident of a specified country	10
Tax outcomes of the Intangibles Arrangement	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	10

101. The total risk score for this arrangement is 45.

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102. In subsequent years, Risk Assessment Framework Table 2 of this Guideline will also be relevant in assessing the risks associated with mischaracterisation of Australian activities connected with DEMPE of the intangible assets. In summary, the risk score under this Table will also result in a high risk rating – a total of 45 points, based on overall characterisation (20 points as AusCo continues to manufacture, market and perform other DEMPE activities in connection with the New Products and Product Intangibles); substance of NewCo – Category 1 (15 points); and tax attributes of NewCo (10 points).

103. The arrangement between AusCo and NewCo would be regarded as a high risk Intangibles Arrangement.

104. There is a risk that AusCo's entry into the Licence Agreement and Service Agreements with NewCo lacks commercial and economic substance, is structured to avoid tax, 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 evidence its decision-making for entering into these arrangements.

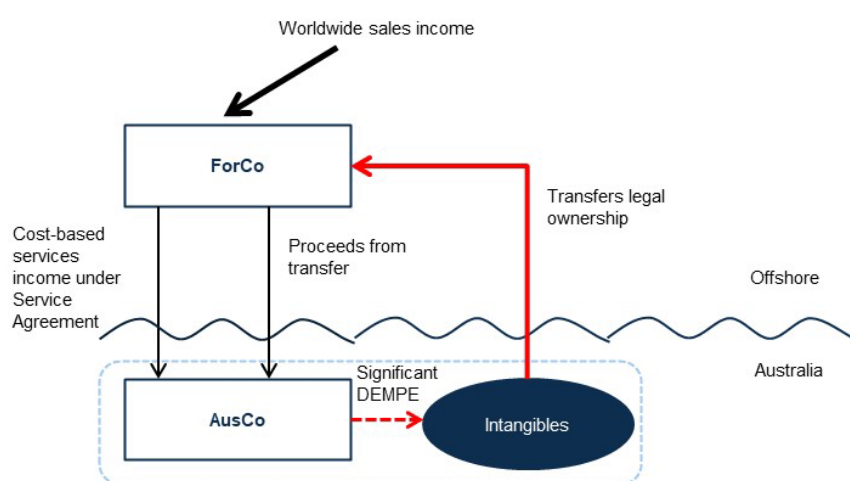
105. AusCo owned and developed the Product Intangibles and had the capability, expertise and capacity to continue to develop, manufacture and commercialise them for market. The Product Intangibles were strategically important to AusCo's business. AusCo did not require NewCo as a partner to develop or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

106. 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.

107. 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.

### Example 5 – Migration of pre-commercialised intangible assets – high risk

**Diagram 8: Example 5 – overview of arrangement**



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Status: **draft only – for comment**


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108. *AusCo is an Australian company that was recently incorporated. AusCo's founder, an Australian tax resident, is a software designer and developer and is in the process of developing a source code for a new software application. AusCo employs a small team of software developers in Australia to assist the founder with developing the new software application. AusCo manages, performs and controls all DEMPE activities associated with the intangible assets and assumes associated risks. AusCo, however, has not valued the intangible assets and it has also not registered the intangible assets for legal protection.*

109. *As AusCo's business grows, the founder considers expanding AusCo overseas. AusCo opens an offshore office and incorporates ForCo in that foreign jurisdiction. Prior to commercialisation, AusCo transfers the legal ownership of the intangible assets associated with the software application via a sale agreement to ForCo. At the time of the transfer of the intangible assets ForCo had no or limited qualified employees and no evidence around its business decision and commercial rationale to transfer the intangible assets.*

110. *Post transfer of the intangible assets, the founder frequently travelled to ForCo and changed their residency status for Australian tax purposes. ForCo also became the global headquarters for the business. The software application was subsequently commercialised and was available to download on global distribution platforms, generating income from in-application purchases and advertising which was derived by ForCo.*

111. *While the founder is involved in the development and enhancement of the software application including the ongoing maintenance and programming updates, AusCo, via its team of employees continue to manage and perform DEMPE activities under a Service Agreement with ForCo. In return, AusCo receives cost-based remuneration for the development activities under the Service Agreement.*

#### *Risk assessment*

112. *This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.*

**Table 6: Example 5 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	<ul style="list-style-type: none"> <li><i>AusCo transfers the legal ownership of the intangible assets associated with the software application via a sale agreement to ForCo</i></li> <li><i>AusCo, via its team of employees continue to manage and perform DEMPE activities under a Service Agreement with ForCo</i></li> </ul>	10 (5 + 5)
Substance of the Relevant Entity	<i>At the time of the transfer of the intangible assets ForCo had no or limited qualified employees and no evidence around its business decision and commercial rationale to transfer the intangible assets</i>	15
Tax outcomes of the Intangibles Arrangement	<i>As a consequence of the restructure, AusCo did not derive the sales and advertising income from the commercialisation of the software application</i>	10

113. *The total risk score for this arrangement is 35. The arrangement between AusCo and ForCo would be regarded as a high risk Intangibles Arrangement. The risk score will further increase if ForCo exhibits one of the tax attributes listed in the risk assessment framework.*

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Status: **draft only – for comment**

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114. *In subsequent years, Risk Assessment Framework Table 2 of this Guideline will also be relevant in assessing the risks associated with mischaracterisation of Australian activities. The risk rating under this Table will not impact the risk rating under Risk Assessment Framework Table 1 of this Guideline, which is in relation to the initial Migration.*

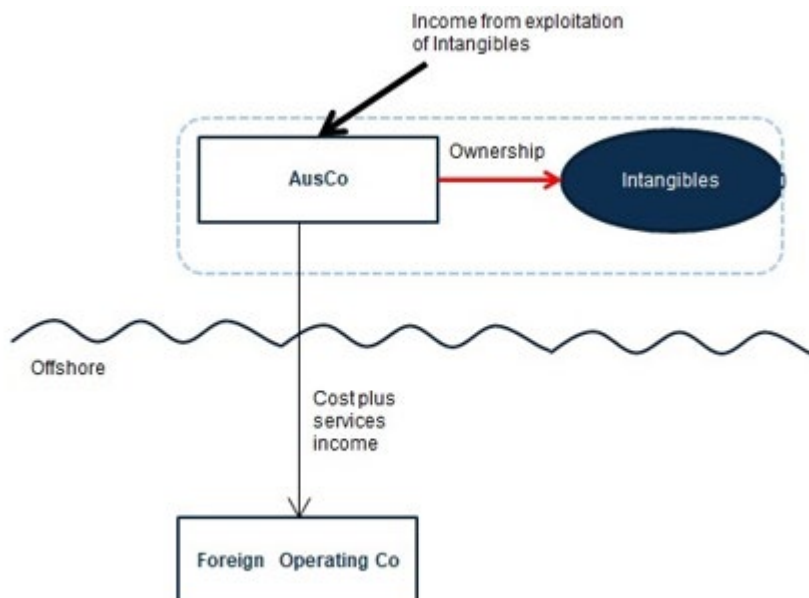
115. *There is a risk that AusCo's decision to transfer the ownership of the intangible assets to ForCo, an entity with no employees at the time of transfer, and the subsequent entry into the Service Agreement with ForCo is not commercially realistic and is unlikely to be an arrangement that independent entities dealing wholly independently in comparable circumstances to that of AusCo and ForCo would have entered into.*

116. *AusCo also continued to manage and control DEMPE activities post transfer of the intangible assets and had the capacity to commercialise the software application. AusCo did not require ForCo to commercialise the intangible assets. Understanding the business rationale for transferring the ownership of the intangible assets to ForCo and ForCo's capacity, including the founder's role, to undertake the associated DEMPE activities will be essential to our risk assessment.*

117. *We will consider the potential application of the transfer pricing provisions, (including the exceptions within Subdivision 815-B of the ITAA 1997) 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.*

#### **Example 6 – transfer of intangibles assets to a foreign hybrid entity – high risk**

**Diagram 9: Example 6 – overview of current arrangement**



#### **Current arrangement**

118. *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*

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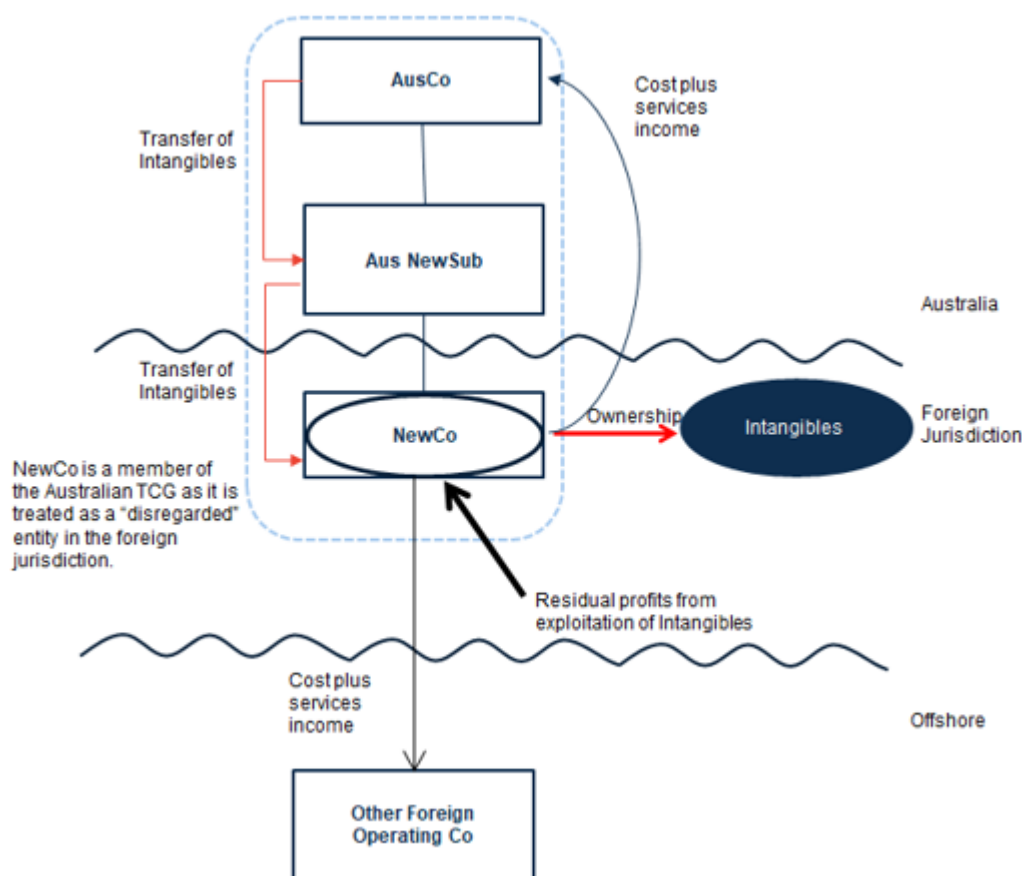
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include technology, customer relationships, brand, and other intangible assets or rights (Intangibles).

119. AusCo has historically owned, managed and controlled DEMPE activities associated with the Intangibles and assumes associated risks. AusCo derives the world-wide sales income from third parties for the exploitation of the Intangibles through direct sales and through licensing or distribution agreements entered into with international related parties. AusCo also has contract services agreements with international related parties to perform certain activities.

**Diagram 10: Example 6 – overview of new arrangement**



#### *New arrangement*

120. AusCo decides that the Intangibles should be centralised in a new entity, NewCo, in a foreign jurisdiction.

121. The transfer of the Intangibles to NewCo involves the following steps and features:

- A wholly-owned subsidiary entity in Australia, Aus NewSub, is established. Aus NewSub owns 100% of NewCo, an entity in the foreign jurisdiction.
- Under the laws of the foreign jurisdiction, NewCo can be treated as a 'disregarded' entity. As a result, under the tax laws of the foreign jurisdiction, NewCo's immediate holding company, Aus NewSub, is considered to be a 'regarded' entity and NewCo is treated as a permanent establishment of Aus NewSub.



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- *For Australian tax purposes, NewCo satisfies the requirements of Division 830 and is considered to be a ‘foreign hybrid company’ and a partnership for Australian tax purposes. As all its membership interests are held by Aus NewSub, a wholly-owned subsidiary of AusCo, NewCo is eligible to join the AusCo Tax consolidated group.*
- *AusCo, Aus NewSub and NewCo form a tax consolidated group (AusCo TCG).*
- *The Intangibles are assigned to NewCo. A market valuation is undertaken by AusCo to determine the value of the Intangibles.*
- *As the entities are all members of the AusCo TCG, under the single entity rule, there are no CGT consequences for the transfer of Intangibles from AusCo to NewCo.*

122. *Following the transfer of the Intangibles to NewCo, NewCo receives the worldwide sales income from the exploitation of the Intangibles. The existing contracts and agreements with the international related parties associated with the Intangibles are novated from AusCo to NewCo. NewCo also enters into a contract service agreement with AusCo, with AusCo now performing sales distribution, R&D, and other services on behalf of NewCo. Other international related parties previously undertaking certain activities for AusCo continue to perform the same activities, under new agreements entered into with NewCo. AusCo and other entities in the global group receive a routine return for their activities, while NewCo now retains all of the residual profits.*

123. *As NewCo is a member of the AusCo TCG operating in a foreign jurisdiction, its operations and presence are considered to be a foreign branch of the AusCo TCG and the income attributable to NewCo is returned as non-assessable non-exempt income under section 23AH of the ITAA 1936.*

124. *Under specific tax rules in the foreign jurisdiction, Aus NewSub, as the ‘regarded’ entity, is eligible to claim amortisation deductions in that foreign jurisdiction for the value of the Intangibles over a period of time.*

#### *Risk assessment*

125. *This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.*

**Table 7: Example 6 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
<i>Restructure or change</i>	<i>AusCo assigns intangible assets to NewCo and subsequently enters into a service agreement with NewCo in relation to the intangible assets</i>	<i>10</i>
<i>Tax attributes – Relevant Entity</i>	<i>NewCo satisfies the requirements of Division 830 of the ITAA 1997 and is considered to be a ‘foreign hybrid company’ and a partnership for Australian tax purposes Amortisation is available in the foreign jurisdiction in relation to the intangible assets</i>	<i>10</i>
<i>Tax outcomes of the Intangibles Arrangement</i>	<i>Had the New Arrangement not occurred, AusCo would have continued to own and derive income from the exploitation of the Intangibles, as opposed to a routine service return</i>	<i>10</i>



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	<i>Further, while the intangible assets are recognised as being acquired in the foreign jurisdiction, no CGT gains were recognised in Australia</i>	
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126. *The total risk score for the New Arrangement would be 30.<sup>21</sup> It would be regarded as a high risk Intangibles Arrangement.*

127. *There is a risk that AusCo's entry into the New Arrangement is not commercially rational and may not be consistent with the substance of the group's arrangement, or is structured to achieve particular tax outcomes in Australia or the foreign jurisdiction. The tax outcomes include the avoidance of CGT on the transfer of the Intangibles and the non-inclusion of the worldwide sale income in AusCo. There is also a tax risk that the profits associated with the Intangibles have not been appropriately attributed between AusCo and its foreign branch under Australia's transfer pricing rules.*

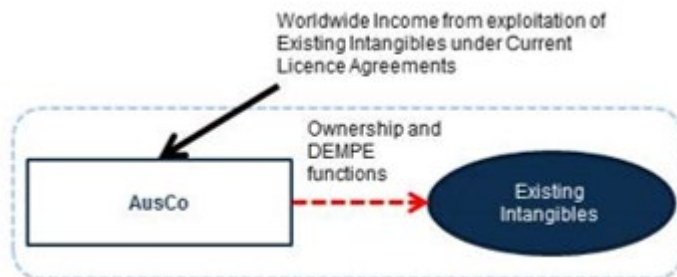
128. *This risk is emphasised where AusCo does not maintain documentation meeting the Evidence Expectation.*

129. *The New Arrangement does not materially change the way DEMPE activities are performed within the global group, other than resulting in additional deductions available in the foreign jurisdiction and shifting the worldwide sales income (residual profit) from AusCo to the foreign jurisdiction. Other international related entities continue to perform the same activities pre- and post-restructure, with the only change being the counterparty of their intercompany agreements.*

130. *Had the New Arrangement not occurred, AusCo would have continued to own and derive income from the exploitation of the Intangibles, as opposed to a routine service return.*

131. *We will consider the potential application of the transfer pricing provisions, specifically Subdivision 815-C, in relation to the attribution of profit between AusCo and its foreign branch. 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.*

<sup>21</sup> To the extent that AusCo continues to perform DEMPE activities without close oversight or supervision from NewCo, the categorisation for the substance of NewCo may be Category 1 or 2, resulting in a higher risk score.

Status: **draft only – for comment****Example 7 – centralisation of intangible assets – medium risk****Diagram 11: Example 7 – overview of current arrangement****Current arrangement**

132. 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, trade marks, copyright and other intangible assets or rights (Intangible Assets).

133. 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.

**Decision to centralise intangible assets**

134. 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. OneCo is located in a jurisdiction which is the global group's largest market in terms of product sales.

135. 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 documentation to substantiate the commercial rationale underpinning its decision to centralise.

136. 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.

137. As a result of the sale, OneCo receives worldwide income from the exploitation of the Intangible Assets. AusCo maintains some documentation to support the arm's length

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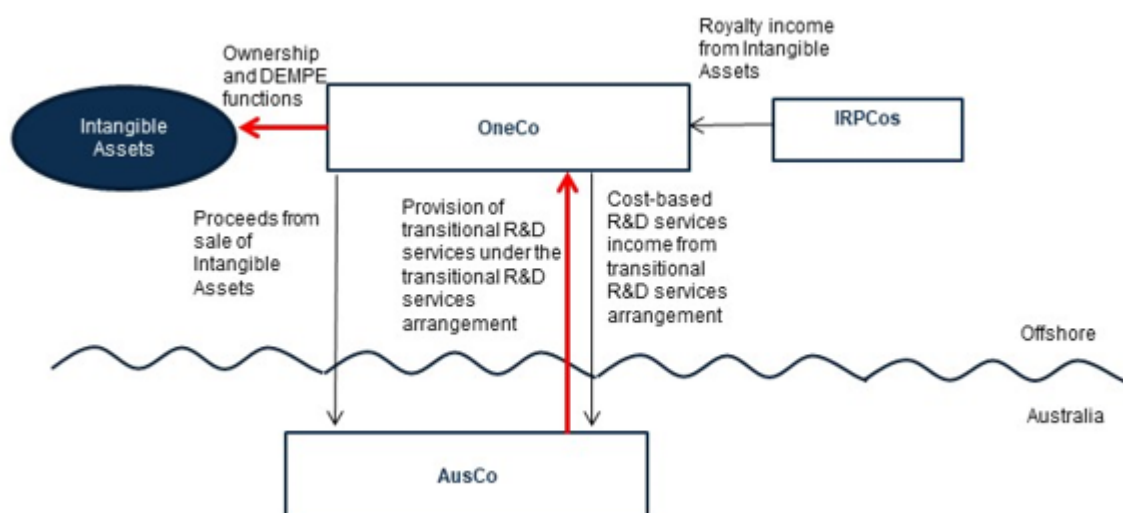
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*nature of the pricing and terms of all arrangements in connection with the restructure, including, but not limited to, the Sale Agreement and the novation of the Current Licence Agreements.*

138. *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.*

139. *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 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.*

**Diagram 12: Example 7 – overview of new arrangement**



#### *New arrangement*

140. *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.*

141. *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.*

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*Risk assessment*

142. This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment in relation to the Migration is as follows.

**Table 8: Example 7 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	AusCo enters into a Sale Agreement with OneCo to transfer the Intangible Assets to OneCo and also novates Current Licence Agreements with international related parties to OneCo. Afterwards, AusCo enters into a transitional R&D service agreement with OneCo and continues to distribute products associated with the Intangible Assets	10
Substance of the Relevant Entity	<ul style="list-style-type: none"> <li>Risk Assessment Framework Table 1 would be applied as at the time of the restructure or change. In Year 1, the substance of the Relevant Entity in relation to these intangible assets best fit 'Category 2', given ForCo has qualified staff to manage DEMPE activities, but AusCo has a continued involvement in intangible assets it has previously developed</li> <li>OneCo is located in a jurisdiction which has the largest market in terms of customer revenue from the products</li> </ul>	4 (9 – 5)
Tax outcomes of the Intangibles Arrangement	As a result of the sale, OneCo, instead of AusCo, receives worldwide income from the exploitation of the Intangible Assets. This will be balanced with the expenses AusCo no longer incurs in relation to the Intangible Assets as a result of the sale	10

143. The total risk assessment score of the New Arrangement is 24. It would be regarded as a medium risk Intangibles Arrangement.

144. A risk that may arise with respect to this arrangement is 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.

145. In addition, Risk Assessment Framework Table 2 of this Guideline should also be completed to assess the risks associated with the non-recognition of Australian DEMPE activities in the ongoing arrangement. Under Risk Assessment Framework Table 2 of this Guideline, the outcome can be summarised as follows:

- overall characterisation – 10 points (New Intangibles are not owned by AusCo and it ceased activities other than distribution and transitional R&D services)
- substance of the Relevant Entity – 9 points (Category 2).

146. Based on these 2 risk factors, the Intangibles Arrangement would be considered medium (19 points) under Risk Assessment Framework Table 2 of this Guideline. In subsequent years, once the transitional R&D activities cease, and the degree of OneCo's substance with respect to the Intangible Assets increase, the risk score assigned to Questions 2 and 3 of Risk Assessment Framework Table 2 of this Guideline may be

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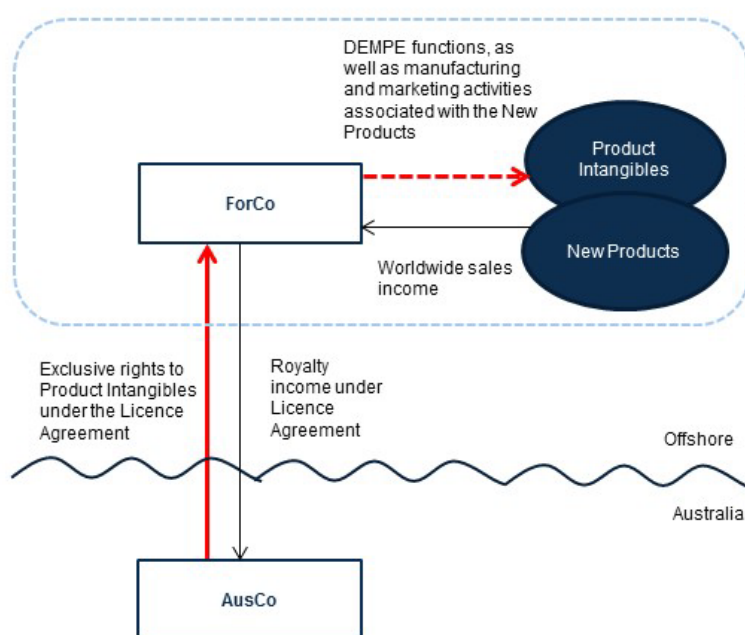
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*reduced, resulting in a lower risk rating with respect to the risk associated with non-recognition of Australian DEMPE activities.*

147. We may consider the potential application of the transfer pricing provisions as well as the CGT provisions or the capital allowance provisions in relation to the Sale Agreement. Where relevant, the potential application of Part IVA of the ITAA 1936 (including the DPT) may also be considered.

### **Example 8 – transfer of rights to intangible assets under a licence agreement – medium risk**

**Diagram 13: Example 8 – overview of arrangement**



148. 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, trade marks, copyright and other intangible assets or rights.

149. 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.

150. 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.

151. 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

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*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.*

152. *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.*

153. *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*

154. *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. 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.*

155. *AusCo distributes the New Products in Australia under an agreement with ForCo.*

#### *Risk assessment*

156. *This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.*

**Table 9: Example 8 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	<i>AusCo and ForCo enter into a licence agreement in relation to Product Intangibles</i> <i>AusCo distributes New Products once Product Intangibles have been commercialised</i>	10
Substance of the Relevant Entity	<i>ForCo, with its expertise and capability, manages, performs and controls all the DEMPE activities connected with the Product Intangibles and assumes the associated risks</i> <i>However, if the substance of the Relevant Entity is inconsistent with the form of the arrangement, the risk score would be higher for this question</i>	0
Tax attributes of Relevant Entity	<i>If one of the tax attributes listed at Question 5 apply to ForCo, 10 points would apply</i>	10
Tax outcomes of the Intangibles Arrangement	<i>AusCo would not have had the capacity to further develop the Product Intangibles without the partnership</i> <i>On the assumption that the payments made by ForCo and AusCo under any arrangements in connection with the</i>	0

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	<i>restructure are arm's length, AusCo's taxable income would not be less than if the restructure or change did not occur</i>	
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157. *The total risk assessment score for this arrangement is 20.*

158. *As demonstrated in this Example, if either of the following factors applies, the arrangement between AusCo and ForCo would be regarded as a medium risk Arrangement:*

- *one of the tax attributes listed at Question 5 in Risk Assessment Framework Table 1 of this Guideline apply to ForCo – for example, ForCo is a resident of a specified jurisdiction, or*
- *the substance of ForCo is inconsistent with the form of the arrangement – for example, despite ForCo having specialised staff and capability, it does not wholly perform, manage and control the DEMPE activities involved in the commercialisation, manufacturing and marketing of the New Products.<sup>22</sup>*

159. *A risk that may arise with respect to this arrangement is that the substance of the Licence Agreement may not align with the form of the arrangement. As shown in the application of the risk assessment framework in this Example, the level of substance in ForCo's operations following the transfer of the Product Intangibles will inform the level of risk associated with the arrangement.*

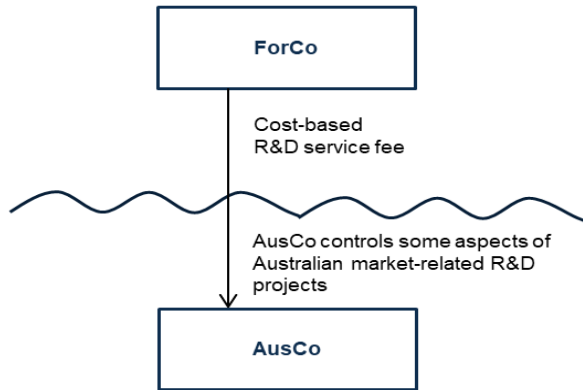
160. *The tax attributes of ForCo are also an indicator of the risk that the arrangement might have been driven by tax outcomes. In assessing this risk, we will consider any evidence demonstrating a genuine and substantiated (non-tax) commercial rationale to enter into the Licence Agreement with ForCo.*

161. *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, such as the pricing and terms of the Licence Agreement.*

162. *We may consider the potential application of the transfer pricing provisions. Where relevant, the potential application of Part IVA of the ITAA 1936 (including the DPT) may also be considered.*

<sup>22</sup> For completeness, it is noted that if there is a lack of substance consistent with a 'Category 1' categorisation under Question 5 of Risk Assessment Framework Table 1 of this Guideline, this will result in a further increase of risk score and the arrangement may be regarded as high risk.



Status: **draft only – for comment****Example 9 – contract research and development arrangement – medium risk****Diagram 14: Example 9 – overview of arrangement**

163. *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, trade marks, copyright and other intangible assets or rights (Existing Intangibles).*

164. *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.*

165. *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.*

166. *ForCo employs specialised staff and has the expertise and capability to manage the various contract R&D centres. AusCo is an established R&D centre within the global group and employs experienced and specialised staff to perform R&D activities.*

167. *AusCo is party to an R&D services agreement with ForCo (R&D Services Agreement), under which it is remunerated with a service fee.*

168. *Under this arrangement:*

- *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.*
- *As an established R&D centre within the global group, AusCo in fact controls certain DEMPE activities performed as part of the R&D Services Agreement. In substance, notwithstanding formal reporting lines to ForCo, AusCo personnel are considered subject matter experts for certain Australian-focused projects and often make key decisions in relation to these R&D projects without the input or oversight of ForCo personnel.*



Status: **draft only – for comment***Risk assessment*

169. This is not a restructure or change of intangible arrangements. According to Risk Assessment Framework Table 2 of this Guideline, the risk assessment is as follows.

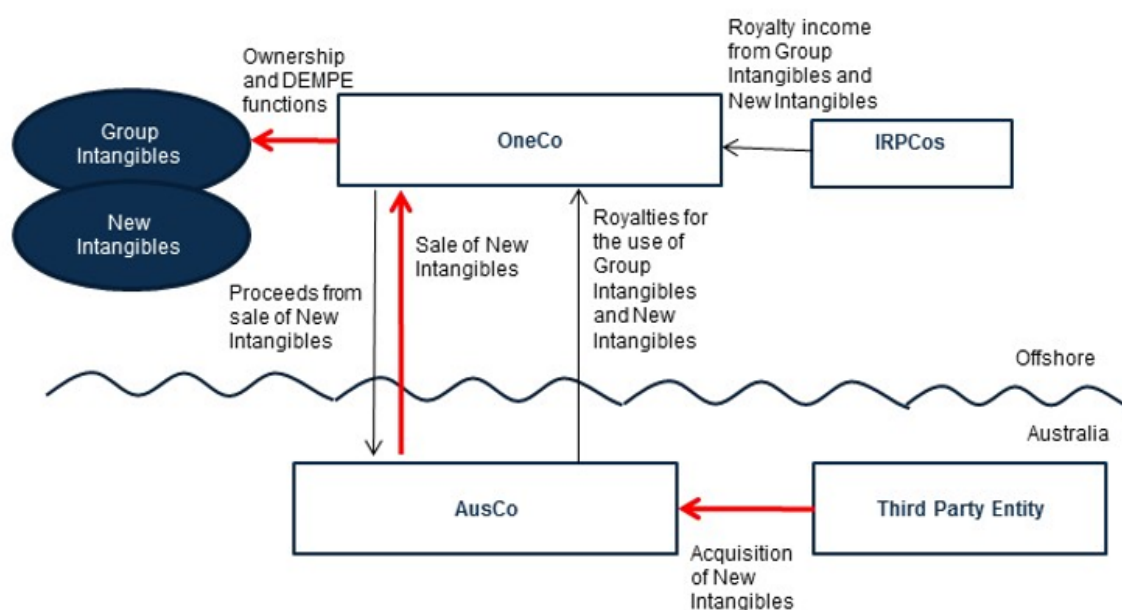
**Table 10: Example 9 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Questions 1 and 2	AusCo performs R&D activities in relation to an Intangible Asset it does not own	10
Substance of the Relevant Entity	ForCo has specialised staff and the capability, but AusCo in fact controls certain (though not all) R&D activities	9

170. The total risk assessment score for this arrangement is 19. The arrangement between AusCo and ForCo would therefore be regarded as a medium risk Intangibles Arrangement.

171. 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, including under the R&D Services Agreement. The extent of AusCo's actual involvement in DEMPE activities will inform the level of risk associated with the arrangement.

172. We may consider the potential application of the transfer pricing provisions.

**Example 10 – centralisation of intangible assets – low risk****Diagram 15: Example 10 – overview of arrangement**

173. AusCo is part of a global group that develops, manufactures, markets and sells products globally. AusCo and its international related parties exploit valuable intangible

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*assets in undertaking their operations. These intangible assets include patents, know-how, trade marks, copyright and other intangible assets or rights (Group Intangibles).*

174. *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.*

175. *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 evidence that substantiates the arm's length nature of the royalty paid under this agreement.*

#### *Acquisition and transfer*

176. *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 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.*

177. *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.*

178. *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.*

#### *Risk assessment*

179. *This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.*

**Table 11: Example 10 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Restructure or change	<p>Shortly after AusCo acquires the New Intangibles, it transfers the New Intangibles to OneCo</p> <p>AusCo exploits the New Intangibles in its ordinary business operations following the transfer</p>	10

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<i>Substance of the Relevant Entity</i>	<i>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</i> <i>AusCo is not involved in the DEMPE activities of Group Intangibles post-transfer</i>	<i>0</i>
<i>Tax outcomes of the Intangibles Arrangement</i>	<i>None of the tax attributes or outcomes in Risk Assessment Framework Table 1 applies</i>	<i>0</i>

180. *The total risk assessment score for this arrangement is 10. The arrangement between AusCo and OneCo would be regarded as a low risk Intangibles Arrangement.*

181. *It will be relevant to consider the valuation of 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. It will also be relevant to consider the pricing and terms of AusCo's Royalty Agreement, both pre- and post-transfer of the New Intangibles.*

182. *When assessing the risk, we would expect specific consideration be given to the transfer pricing provisions.*

183. *For illustration purposes, we note that if the arrangement is assessed under Risk Assessment Framework Table 2 of this Guideline, the risk assessment will be as follows:*

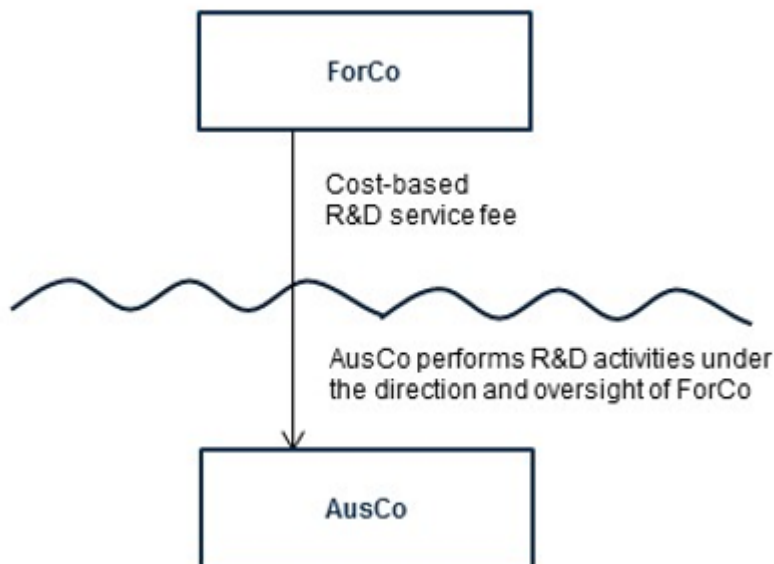
- overall characterisation – 0 points (AusCo only exploits the New Intangibles but otherwise has no further involvement in the DEMPE of New Intangibles)*
- substance (low risk) – 0 points given the degree of substance of OneCo, and*
- tax outcomes – 0 points as none of the attributes apply to New Intangibles post-transfer or to OneCo.*

*The overall risk rating is low (0 points) under Risk Assessment Framework Table 2 of this Guideline.*

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**Example 11 – contract research and development arrangement – low risk***Diagram 16: Example 11 – overview of arrangement*

184. 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, trade marks, copyright and other intangible assets or rights (Existing Intangibles).

185. 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.

186. 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.

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

188. 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.

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Status: **draft only – for comment**


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189. 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 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*

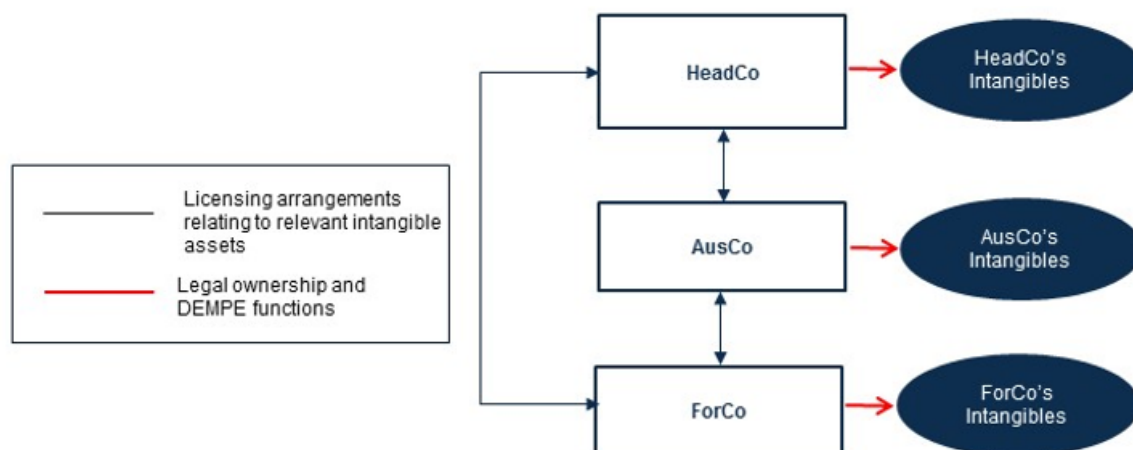
190. This is not a restructure or change of intangible arrangements. According to Risk Assessment Framework Table 2 of this Guideline, the risk assessment is as follows.

**Table 12: Example 11 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
Characterisation – AusCo	AusCo performs R&D activities in relation to Intangible Assets not owned by AusCo and exploits the Intangible Assets in its operations (but does not otherwise enhance or add value to the Intangible Assets)	10
Substance of the Relevant Entity	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	0

191. The total risk assessment score for this Intangibles Arrangement between AusCo and ForCo is 10. It would be regarded as a low risk Intangibles Arrangement.

192. We would expect specific consideration be given to the transfer pricing provisions.

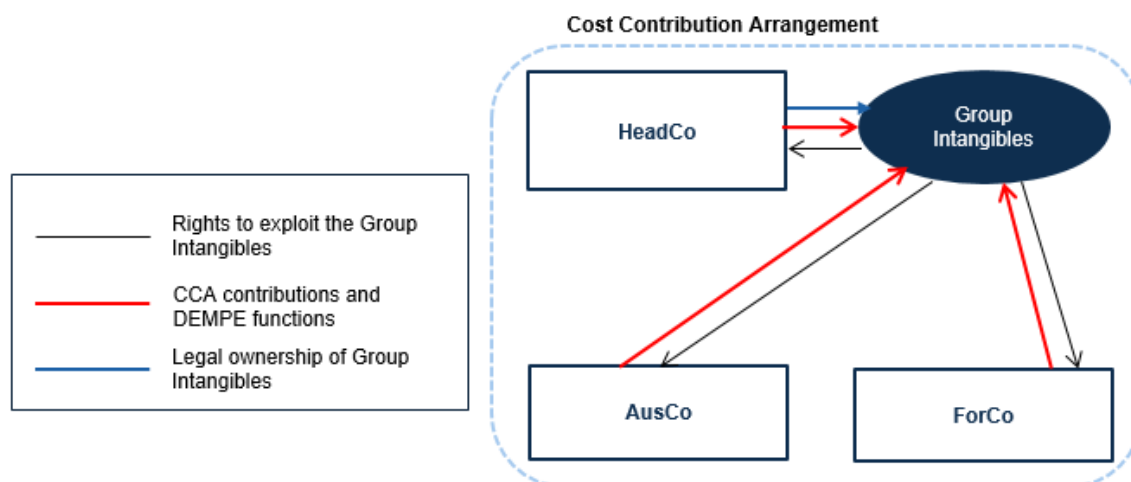
Status: **draft only – for comment****Example 12 – cost contribution arrangement – low risk***Diagram 17: Example 12 – overview of current arrangement**Current arrangement*

193. 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.

194. 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.

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

196. 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.

Status: **draft only – for comment****Diagram 18: Example 12 – overview of cost contribution agreement****Cost contribution arrangement**

197. 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.

198. 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 having economic ownership of the developed intangibles in their respective regions.

199. 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 CCA 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 as compared to HeadCo and ForCo.

200. AusCo, HeadCo and ForCo terminate their pre-existing cross-licensing agreements as a result of entering into the CCA.

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Status: **draft only – for comment**


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*Risk assessment*

201. *This is a Migration of intangible assets. According to Risk Assessment Framework Table 1 of this Guideline, the risk assessment is as follows.*

**Table 13: Example 12 – application of risk assessment factors**

<b>Risk assessment factor</b>	<b>Application of criteria</b>	<b>Score</b>
<i>Restructure or change</i>	<i>AusCo's contribution of intangibles into a CCA is a restructure or change covered by Risk Assessment Framework Table 1. AusCo continues to exploit or use the Relevant Intangible Assets (being AusCo's Intangible Assets)</i>	<i>10</i>
<i>Substance of the Relevant Entity or Entities</i>	<i>Both HeadCo and ForCo are Relevant Entities for the purposes of applying the risk assessment framework ForCo and HeadCo both have specialised staff who use their expertise in performing, managing and controlling the DEMPE activities they are responsible for</i>	<i>0</i>
<i>Tax outcomes of the Intangibles Arrangement</i>	<i>Given that AusCo's proportionate share of costs is consistent with the expected benefits to be received by AusCo under the CCA as compared to HeadCo and ForCo, it does not appear that AusCo's taxable income is, or might reasonably be expected to be, lesser than if the restructure or change has not been entered into</i>	<i>0</i>

202. *The total risk assessment score for this arrangement between AusCo, HeadCo and ForCo is 10. The arrangement would be regarded as a low risk Intangibles Arrangement.*

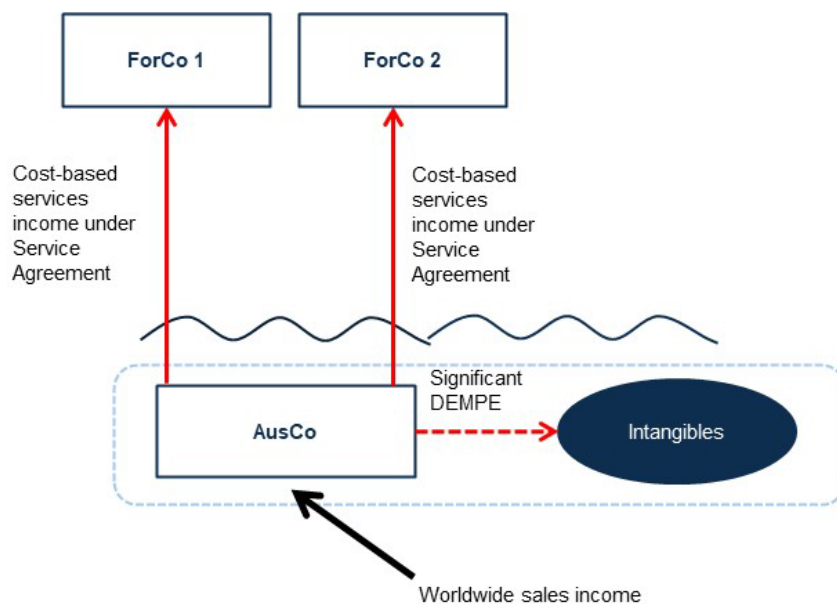
203. *If, under the CCA, the contribution by AusCo is extensive whereas the relative contribution by either HeadCo or ForCo is of limited value, this will impact the rating for the substance risk factor and the arrangement may be regarded as a high risk Intangibles Arrangement. These will include:*

- situations where the parties to the CCA are not able to demonstrate that they have the necessary capability, financial capacity or assets to, in substance, manage and control the DEMPE activities and assume associated risks as agreed in the CCA, or where the intangible assets contributed by them are of limited value relative to the expected benefits to be received by them, especially when compared to AusCo's contribution and expected benefits*
- circumstances where independent parties dealing wholly independently would not have entered into a similar arrangement under such conditions.*

204. *Examples of high risk Intangibles Arrangement include Arrangement 2 (Example 1) in Taxpayer Alert TA 2020/1. We also refer to Taxation Ruling TR 2004/1 Income tax: international transfer pricing – cost contribution arrangements for more extensive discussions of compliance risks associated with cost contribution arrangements.*

205. *Where relevant, we may consider the potential application of the transfer pricing provisions, and the CGT provisions in relation to AusCo's entry into the CCA. For higher risk CCA arrangements, the potential application of Part IVA of the ITAA 1936 (including the DPT) will also be considered.*



Status: **draft only – for comment****Example 13 – service arrangement involving intangible assets – low risk****Diagram 19: Example 13 – overview of arrangement**

206. AusCo is an Australian-headquartered company with subsidiaries in offshore locations, ForCo 1 and ForCo 2. AusCo’s founder, an Australian tax resident, developed a software product that has been commercialised and distributed globally. AusCo employs 15 staff, ForCo 1 employs 3 staff and ForCo 2 employs 2 staff.

207. AusCo owns the intangible assets associated with the software product and under the direction of the founder, AusCo manages, performs and controls all of the related DEMPE activities and assumes associated risks. Worldwide income from the distribution of the software products is derived by AusCo.

208. ForCo 1 and ForCo 2 provide support activities to assist AusCo. ForCo 1 and ForCo 2 receive cost-based remuneration from AusCo under Service Agreements. AusCo maintains evidence substantiating the arm’s length nature of the pricing and terms of each of the Service Agreements.

**Risk assessment**

209. Risk Assessment Framework Table 2 of this Guideline applies as this is not a Migration of intangible assets. However, since AusCo owns the intangibles assets and no related parties are exploiting the intangible assets without legal agreements, neither Question 1 or 2 of this Table applies and the risk rating is nil.

210. The arrangements between AusCo and its subsidiaries would be regarded as a low risk Intangibles Arrangement.

211. When assessing the risk, we would consider the transfer pricing provisions.

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## **APPENDIX 2 – Evidence expectations**

212. 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) or Country-by-Country reporting entity (CBCRE) or have disclosed a relevant Category C reportable tax position<sup>23</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 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.

213. The Evidence Expectations outlined in this Appendix focus on:

- evidencing the commercial considerations and your business decision making
- evidencing the legal form and substance of your Intangibles Arrangements
- identifying and evidencing the intangible assets and connected DEMPE activities, and
- evidencing the tax and profit outcomes of your Intangibles Arrangements.

### **Evidencing the commercial reasons and your decision-making process**

214. In circumstances where you have restructured or had a change associated with your Intangibles Arrangements, we will typically require an understanding of the broader circumstances in which the restructure or change was entered into or carried out. We will typically require information, including contemporaneous documents, to:

- verify the market value of any intangibles acquired or sold
- evidence any other considerations connected with entering into the restructure or arrangement, including whether other or alternative arrangements were considered and the reasons why any alternative arrangements were not pursued
- evidence and verify any tax and non-tax or commercial objectives achieved under the arrangement.

This information is integral to our assessment of the commerciality of your Intangibles Arrangements and potential compliance risks.

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<sup>23</sup> We refer to the self-assessment obligations referenced in paragraph 24 of this Guideline, as well as Category C reportable tax positions relating to TA 2020/1 (Question 32) or other questions relevant to your Intangibles Arrangement.

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215. The evidence we may require includes:

- 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 or jurisdiction specific benefits, reduction of non-tax costs, provision of connected government incentives and any other relevant costs and benefits associated with your Intangibles Arrangements
- the documents created or provided by tax 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
- briefing materials, analysis and data produced in connection with the documents outlined in the first dot point of this paragraph, including those produced by or for internal and independent specialists
- presentations and other papers prepared in relation to your Intangibles Arrangements and associated commercial objectives, including papers provided to your management team, board of directors or any other group or subgroup responsible for considering or making recommendations on the arrangements
- 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
- commercial, regulatory and tax advice obtained in connection with your Intangibles Arrangements
- 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
- details of any changes to inter-company agreements and company policies in the relevant period.

### **Evidencing the legal form and substance of your Intangibles Arrangements**

216. 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 information and documents that evidence the detailed legal form of your Intangibles Arrangements to assist us in understanding your Intangibles Arrangements in totality.

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

- legal agreements, memorandums and like documents associated with your Intangibles Arrangements, including any amendments to, or restatements of, such documents
- details of ownership of intangible assets, including where ownership rights in the intangible asset may have been diluted
- where a restructure has occurred, details of the planning in connection with setting up new legal arrangements or entering into new legal documentation, for example, planning the choice of employees or officers to be appointed as directors of new entities and policies to protect intangible assets
- guidelines, manuals, policies, procedures, specifications and like documents relevant to your Intangibles Arrangements that are developed 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
- transfer pricing documentation including any specific or supplementary analysis or valuation or other reports produced for transactions which form part of your Intangibles Arrangements.

### ***Legal agreements***

218. Obtaining the legal agreements, memorandums 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 R&D service agreements with international related parties, including any amendments to, or restatements of, such agreements.

219. Where legal agreements are not yet drafted or are subject to change, we may require available draft or interim agreements, memorandums 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.

220. 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***

221. Obtaining your internal guidelines, manuals, policies, procedures, specifications, governance and like documents relevant to your Intangibles Arrangements allows us to establish whether you and your associates have policies and work processes in place that are relevant to your arrangements. This includes relevant group intellectual property

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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.

222. 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***

223. 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.

224. We may also compare your transfer pricing documentation with your group intellectual property management and R&D policies, legal agreements with international related parties 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***

225. If you are an SGE or CBCRE, 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 Masterfile 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 DEMPE activities***

226. 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 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 documents and evidence establishing the legal form of your arrangements (legal form documents).

227. 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
- ease with which certain intangible assets and DEMPE activities may be altered or moved, and

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- complex nature of a multinational group's value chains connected with intangible assets and DEMPE activities.

228. These issues may require discussions or interviews of relevant personnel or the review of specific documentation to inform our risk assessment.

### ***Identifying intangible assets***

229. The evidence we may require you to maintain to identify and clarify intangible assets relevant to your Intangibles Arrangements include documents which detail the names or 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, trade mark 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.

230. The evidence we may require includes:

- intangible asset registers
- AASB Standard 138-compliant<sup>24</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 DEMPE activities***

231. 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 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 personnel involved in DEMPE activities, relevant decision makers and approval points and any activities outsourced to third or related parties.

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<sup>24</sup> Australian Accounting Standards Board [AASB] Standard 138 *Intangible Assets* as applicable to the reporting period in question. The current standard is available at [Current standards](#). AASB 138 as applicable to earlier reporting periods can be found at [Search by reporting period](#).

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232. The evidence we may require includes:

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

#### ***Evidencing intangible assets and DEMPE activities***

233. 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 will 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.

234. We may require documents to ensure that the obligations outlined in your legal form documents are consistent with what is occurring in practice. We may analyse the functions performed by relevant entities in connection with the Intangibles Arrangements with reference to specific clauses in legal agreements, group policies, correspondence or transfer pricing documentation. We may also require information and documents, including email correspondence, which demonstrate that entities held out to be managing, controlling or performing DEMPE activities and assuming associated risks, have the capability, financial capacity and assets to do so in substance.

235. The evidence we may require includes:

- 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
- 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
- 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

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- 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
- contemporaneous valuation reports, working papers and associated documentation where intangible assets and relevant functions have been transferred offshore, and
- any additional or like documents that may assist us in identifying and understanding your DEMPE activities.

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

236. 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.

237. The evidence we may require includes:

- 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
- any financial modelling or projections, including models of anticipated tax impacts of options or arrangements prepared by tax personnel or tax advisers
- 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
- evidence of actual cash flows in connection with the arrangement
- 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
- 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**

238. 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 record-keeping options*, we will have regard to the record-keeping obligations outlined, where relevant.



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Status: **draft only – for comment**

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239. 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 intragroup services' for the purposes of PCG 2017/2.
- Technical services considered under PCG 2017/2 also exclude the use of intellectual property, knowhow, processes, systems or other like intangible assets or rights.

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**Commissioner of Taxation**

17 May 2023

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Status: **draft only – for comment**

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## Your comments

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

241. 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 June 2023

Contact officer details have been removed as the comments period has ended

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Status: **draft only – for comment**


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## References

### *Previous draft:*

PCG 2021/D4

### *Related Rulings/Determinations:*

TR 2004/1; TR 2014/6; TR 2014/8

### *Legislative references:*

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- ITAA 1997 815-20(2)(a)
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### *Other references:*

- Australian Accounting Standards Board Standard 138
- OECD, 2015, Aligning Transfer Pricing Outcomes with Value Creation, Actions 8 10 – 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris
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### ATO references

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