Intangibles: What is in the Manual

- Local intangibles
  - Local entities may over time develop local intangibles, and need to be compensated.
- Know-how force attenuation
  - Usefulness of intangibles may decrease over time
  - A royalty of 3% 10 years ago may not be reasonable 10 years after.

Intangibles: What is not in the Manual

- Overpricing of intangibles
  - 1 airplane for 800,000,000 shirts
- There has been unfair exchange of value between developing and developed countries
  - Developing countries: full utilization of production factors, but low standard of living
  - Developed countries: partial utilization of factors, high standard of living
- Intangibles have been used to extract value from developing countries

Intangibles: What is not in the Manual

- Intangibles are a result of high leverage of capital in western countries – a disaster for developing countries
- With the participation of low tax jurisdiction in the game, developed countries are also becoming losers – BEPS project
- Calls for a return to the good old days
- Labor is the primary factor that contributes to value making

Intangibles: Different Profile in Value Chain

- Intangibles cannot be consumed separately
- Intangibles have to be compensated out of the sales price to the consumers
- If there is no market, there is no value
- Marketing intangibles:
  - Augment value but do not create value
  - Highly dependent on markets
- Trade intangibles:
  - May create or augment value

Intangibles: Holistic approach

- Transfer pricing
  - Put all intangible-related transactions in the framework of transfer of intangibles
  - Avoid the distortion caused by the form of transactions
- Withholding taxation
  - Withholding tax may be imposed on the transfer or the use of intangibles in China
- PE taxation
  - If MNEs claims they own the intangibles, and the intangibles are used in China, then there are PE taxation

Risks: What is in the Manual

– Generally respects the limited risk characterization of sole function entities, but
– Where multiple single function entities exist, they need to be viewed in combination in attributing risks and determining returns
– Risk-based approach is not appropriate where
  - Majority of the work force is located in China
  - Majority of tangible assets are located in China

Risks: What is in the Manual

- Will seek other alternatives:
  - Global formulary apportionment
  - Can accept TNMM but
    - Headquarters as the tested party
    - Group as a comparable

Risks: What is not in the Manual

- Generally dislike the notion of risk
  - Fluid term
  - Facilitate tax avoidance
- Risks do not generate profits, they are by-products of profits that enterprises have to deal with
- Risks should align with the functions and assets of the enterprises
  - Control risks – function
  - Financial capacity to assume risks - asset

China: Responsibility in Shaping the Rules

- China thinks large countries like BRICS should shoulder the responsibility of, and take the lead in shaping the rules for international taxation
- Small countries have no bargaining power against MNEs
- Believes that the positions proposed in Country Practice Chapter will benefits smaller countries as well
- An international consensus needs to be reached before smaller countries can benefit