Examining the impact of BEPS on the life sciences sector

Overview of select BEPS final reports and timing of implementation
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Overview of BEPS

In September 2013, G20 leaders endorsed the ambitious and comprehensive Action Plan on Base Erosion and Profit Shifting (BEPS), which identified 15 actions intended to end international tax avoidance. The plan was structured around three pillars: introducing coherence in the domestic rules that affect cross-border activities, reinforcing substance requirements in the existing international standards to align taxation with the location of economic activity and value creation, and improving transparency and certainty for businesses and governments.¹

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On 5 October 2015, just two years later, the Organisation for Economic Co-operation and Development (OECD) issued its final reports on these 15 focus areas. These were discussed and endorsed at the G20 Finance Ministers meeting on 8 October 2015.

The recommendations range from new minimum standards to reinforced international standards to common approaches and best practices.

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The BEPS reports are “soft law” documents and are not legally binding. Rather, countries will need to determine whether and how they will implement the recommendations. However, they are generally expected to be implemented by countries that are part of the consensus. All OECD and G20 countries have committed to consistent implementation in the areas of preventing treaty shopping, country-by-country reporting, fighting harmful tax practices and improving dispute resolution. In other areas, such as recommendations on hybrid mismatch arrangements and best practices on interest deductibility, countries have agreed to a general tax policy direction.²

Some of the measures are immediately applicable, such as the revised guidance on transfer pricing. Other measures require changes to bilateral tax treaties, and still others require domestic law changes before implementation. Here is a general timetable for effectiveness:

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Further development
- Follow-on work on several actions
- Framework for monitoring country implementation and involvement of additional countries

The output also includes analytical reports on Action 1 (digital economy), Action 11 (economic analysis) and Action 15 (multilateral instrument).

Impact of BEPS final reports on the life sciences sector

As with other multinational corporations, all of the BEPS actions have a potential impact on companies in the life sciences sector. However, specific actions may have a disproportionate effect on life sciences companies. In particular, these are Action 5 in the coherence pillar, Actions 7-10 related to substance and Action 13 related to transparency. These actions and their implications for the life sciences sector are explained in this report.
Examining the impact of BEPS on the life sciences sector
Countering harmful tax practices more effectively, taking into account transparency and substance

The OECD has been focused on harmful tax practices for over 15 years, beginning with the 1998 report *Harmful Tax Competition: An Emerging Global Issue*. The BEPS project reviewed this previous work with a focus on requiring substantial activity for any preferential regime and on improving transparency, including compulsory spontaneous exchange of information for certain tax rulings. This project is also closely tied to similar work being undertaken by the European Commission, which has participated in the OECD meetings and has adopted similar approaches, such as the nexus approach for intellectual property (IP) regimes.

The final report covers two main areas: harmful tax practices and transparency. In doing so, it touches on a wide variety of topics, including substance requirements for IP and other regimes; the determination of which IP regimes are allowable and which need to be phased out; what constitutes a harmful preferential regime; which ruling information is to be mandatorily exchanged and to whom; what qualifies as a “ruling”; and best practices for cross-border rulings (the process for granting rulings, terms and publication). Also note that transparency of certain rulings is covered under the master file requirements of Action 13, which is discussed further below.

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**Why is this action important to life sciences companies?**

This action matters because IP is important to the industry — many life sciences companies are using IP regimes and may be impacted by the changes, particularly the additional substance that the nexus approach requires. Regimes already assessed as potentially harmful by the Forum on Harmful Tax Practices (FHTP) include Belgium’s patent income deduction, Luxembourg’s partial exemption for income/gains derived from certain IP rights and the UK’s patent box.

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3. Belgium’s regime is expected to change to align the patent income deduction with the OECD nexus approach. The current regime will likely continue during a grandfathering period.
Details of Action 5

Harmful tax practices
Rulings, or the legal or administrative procedures under which a ruling was given, can be considered to have been issued under a harmful preferential regime if the regime, among other factors, does not require substantial activity. The final report determines that this substantial activity requirement used to assess preferential regimes should be strengthened to realign taxation of profits with the substantial activities that generate them. Several approaches were considered, and the consensus was to apply the “nexus approach.” The approach includes R&D activities carried out by the taxpayer itself and uses expenditure as a proxy for determining substantial activities, including outsourced R&D to unrelated parties.

If the regime is found to be harmful, the country will be given the opportunity to abolish the regime or remove the features creating the harmful effect. Additionally, the taxpayer could become subject to defensive measures taken by other countries to counter the effects of the harmful regime.

The FHTP has reviewed or is reviewing 43 IP and non-IP regimes in OECD member states and associate countries in the BEPS project (with the scope to be extended to third countries). The 16 IP regimes reviewed were identified as inconsistent with the OECD nexus approach. In response, countries have already agreed to changes or have stated that prospective regimes will conform to the OECD recommendations.

Transparency
Action 5 recommends disclosing summaries of specific rulings with affected tax authorities, in the absence of an existing compulsory spontaneous exchange agreement among the jurisdictions. The affected tax authorities include the jurisdiction of the:

- Direct parent
- Ultimate parent
- Related parties with which the taxpayer entered into a transaction covered by the ruling
- Related parties if the ruling gives rise to income from these parties benefiting from a preferential regime

The framework covers six categories of rulings that would be disclosed:

- Rulings related to preferential regimes
- Cross-border unilateral advance pricing arrangements (APAs) or other unilateral transfer pricing rulings
- Rulings adjusting profits downward
- Permanent establishment (PE) rulings
- Conduit rulings
- Any other type of ruling where the FHTP agrees in the future that the absence of exchange would give rise to BEPS concerns

Only rulings issued on or after 1 January 2010 that were still valid on 1 January 2014, or new rulings issued on or after 1 April 2016, would be subject to disclosure.

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4. The jurisdictions with these IP regimes are Belgium, People's Republic of China, Colombia, France, Hungary, Israel, Italy, Luxembourg, the Netherlands, Portugal, Spain, Spain-Basque Country, Spain-Navarra, Switzerland-Canton of Nidwalden, Turkey and the UK.

5. Some examples include the UK, which on 22 October 2015 set out the Government’s proposals for modifying the UK patent box regime in line with the recommendations published by the OECD. These proposals, which would take effect on 1 July 2016, would limit the benefits of the patent box according to a nexus fraction that is based on the amount of direct in-house and externally subcontracted R&D expenditure incurred by the claimant (plus, to a limited extent, R&D subcontracted to related parties and acquired IP). This fraction is applied to profits as calculated in the current regime. Further, Switzerland proposed introducing a license box at the cantonal level that is competitive and compatible with international standards. The license box will still undergo modifications that take the latest international developments into consideration, particularly the OECD developments related to the substantial activity requirement and the modified nexus approach. Lastly, Ireland introduced the Knowledge Development Box (KDB) from 1 January 2016, which was published in the recent Finance Bill. The KDB is aimed at incentivizing innovative R&D activities by taxing profits from patented inventions and copyright software at an effective rate of 6.25%. The KDB will be the first OECD-compliant tax regime adopting the nexus approach, which seeks to link the relief to the proportion of R&D in Ireland as a percentage of overall R&D expenditure inclusive of overall group R&D and amounts paid to acquire IP.
For countries with the necessary legal basis, the exchange of information under this framework will take place from 1 April 2016 for future rulings (generally within three months after the competent authority of the issuing state becomes aware of the ruling). The exchange of certain past rulings will need to be completed by 31 December 2016.

In addition to the industry considerations on IP-related rulings, the disclosure recommendation under Action 5 will also have a great impact on life sciences multinationals. Rulings on transfer pricing arrangements among the various members of the supply chain (i.e., manufacturers, principals and limited risk distributors), as well as rulings on the existence or nonexistence of permanent establishments resulting from commissionaire arrangements, are prevalent in the sector. Summaries of such rulings may be subject to disclosure under Action 5.

What actions are life sciences companies taking with respect to Action 5?

Companies are undertaking a comprehensive review of select rulings to analyze whether the ruling or regime is harmful and will need to be disclosed under Action 5. EY has developed a risk assessment framework that aims to identify the level of risk related to certain rulings, including recommendations on whether they should be renewed, withdrawn, renegotiated or further supported by transfer pricing documentation. In addition to the financial impact, companies are considering the reputational risks stemming from the transparency recommendations of Action 5.

Further, companies should review their supply chains in light of the recommended nexus approach and consider whether changes are needed to align current IP ownership and substance. For example, companies are undertaking reviews of functions related to IP to understand where activities are taking place – from strategic decision-making to funding of research and R&D activities (or oversight of third-party activities).
Examining the impact of BEPS on the life sciences sector
Preventing the artificial avoidance of permanent establishment status

The final report on Action 7 proposes changes to the PE definition in Article 5 of the OECD Model Tax Convention. The changes are intended to prevent the use of the following arrangements and strategies, which are viewed as an effort by a foreign enterprise to operate in another country without creating a PE:

- Commissionaire arrangements and similar strategies
- The use of specific preparatory or auxiliary activity exemptions, including the artificial fragmentation of so-called cohesive business activities into several smaller operations so that each part can benefit from specific-activity exemptions

The suggested changes require the amendment of tax treaties. About 90 countries have already started negotiating a multilateral instrument to implement the treaty-related BEPS measures and modify bilateral tax treaties. The multilateral instrument is expected to be opened for signature in 2016.

Why is this action important to life sciences companies?

Multinational companies in the life sciences sector commonly rely on PE exceptions in the OECD Model Tax Treaty to avoid a taxable nexus for various activities in their supply chains. For example, a principal company may hold title to inventory in a local jurisdiction through toll manufacturing, centralized warehousing or regional distribution activities. In addition, when initially entering a jurisdiction, a company may rely on a related representative office or third-party representation, which, under current rules, may not create a PE. The recommended tightening of the definition of PE in treaties may cause companies to have a taxable presence where they do not today.
Commissionaire arrangements

Life sciences companies often use a commissionaire or sales agent structure — an arrangement through which the “commissionaire” sells products in a state in its own name but on behalf of a foreign enterprise (principal) that owns the products. The commissionaire does not take title to the products, as a limited risk distributor would, and it is compensated for its services with a commission from the foreign enterprise principal. Under the current OECD Model Tax Treaty, a foreign enterprise principal that uses such an arrangement generally does not have a permanent establishment to the extent that the contracts concluded by the commissionaire are not binding on the foreign enterprise.

Under the final report for Action 7, sales and marketing models similar to commissionaire arrangements are likely to create the finding of a permanent establishment. In the final report, it will no longer matter that the contract is not in the name of the principal, as long as a person (other than an independent agent) habitually concludes contracts or habitually plays a principal role leading to the conclusion of contracts that are routinely concluded without material modification by the foreign enterprise. Currently, Article 5(5) of the OECD Model Tax Treaty relies on the formal conclusion of contracts in the name of the foreign enterprise, whereby it is possible to avoid the application of that rule by changing the terms of contracts without material changes in the functions performed in a state. Companies also try to avoid the application of Article 5(5) in situations where contracts that are substantially negotiated in a state are not formally concluded in that state because they are finalized or authorized abroad. The new language of “habitually playing the principal role” is meant to expand the “concluding contracts’’ requirement to capture these types of situations.

The final report also clarifies that independent agents shall not include a person who “acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related” (i.e., directly or indirectly controls more than 50% of the beneficial interest or shares). When commissionaire structures are seen in life sciences companies, the transactions are generally between related parties, suggesting that the independent agent exception would not be available under the new guidelines and that the foreign principal would have a permanent establishment.

The final report also specifically references an example related to the life sciences sector for when a sales agent would not be seen as creating a permanent establishment for the principal:

“[The phrase ‘or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise’] does not apply, however, where a person merely promotes and markets goods or services of an enterprise in a way that does not directly result in the conclusion of contracts. Where, for example, representatives of a pharmaceutical enterprise actively promote drugs produced by that enterprise by contacting doctors that subsequently prescribe these drugs, that marketing activity does not directly result in the conclusion of contracts between the doctors and the enterprise so that the paragraph does not apply even though the sales of these drugs may significantly increase as a result of that marketing activity.”

It should be noted that such changes to the OECD Model Tax Treaty are not intended to address BEPS concerns related to the transfer of risks between related parties through low-risk distributor arrangements.

Preparatory or auxiliary activity exemptions

The current OECD Model Tax Treaty provides a list of exceptions through which a permanent establishment is deemed not to exist where a place of business is used solely for those activities. They include:

- The use of facilities solely for storage, display or delivery of goods or merchandise belonging to the enterprise
- The maintenance of a stock of goods or merchandise belonging to the enterprise solely for storage, display or delivery
- The maintenance of a stock of goods or merchandise belonging to the enterprise solely for processing by another enterprise
- The maintenance of a fixed place of business solely for purchasing goods or merchandise or for collecting information for the enterprise
- The maintenance of a fixed place of business solely for carrying on, for the enterprise, any other activity of a preparatory or auxiliary character
- The maintenance of a fixed place of business solely for any combination of activities mentioned above, provided that the overall activity resulting from this combination is of a preparatory or auxiliary character

Multinational life sciences companies often rely on these exceptions when considering the various points in the supply chain where the principal companies have title to inventory in a local jurisdiction through toll manufacturing, centralized warehousing, regional distribution activities, etc. In certain cases, a few of these activities occur in the same local jurisdiction but, when looked at separately, meet one of the exceptions noted above.

In the final reports, activities that used to fall under any of the specific-activity exemptions may now give rise to a permanent establishment risk unless it can be shown that these activities are, as a whole, preparatory or auxiliary. Consider an example in the final reports that is relevant to the life sciences sector. In this scenario, storage and delivery activities are performed through a warehouse that represents an important asset, requires a number of employees and constitutes an essential part of the enterprise's sale and distribution business. The example concludes that such activities do not have a preparatory or auxiliary character.

The final reports also added an anti-fragmentation rule. Under this new rule, operating models that involve various group entities in the same jurisdiction performing “complementary business activities as part of a cohesive business operation” may give rise to a permanent establishment if these activities, when viewed as a whole, exceed what is considered preparatory or auxiliary. Thus, when companies have a few supply chain activities occur in the same local jurisdiction, they must be looked at all together when determining if the preparatory or auxiliary exception is met.

What actions are life sciences companies taking with respect to Action 7?

The timing of the recommended changes to the permanent establishment definition under Action 7 will depend on when treaties are negotiated in the relevant countries. Further, the OECD has not released guidance on the allocation of profits to a permanent establishment (if one is found). Further guidance is expected by the end of 2016.

Companies are reviewing their supply chains in connection with preparing the master and local files under Action 13 and are considering changes to the operating model to minimize permanent establishment risks. Some companies are examining the possibility of converting commissionaires/sales agents to limited risk distributors. It should be noted that limited risk distributors are out of scope for the BEPS project on Action 7; however, this does not eliminate the possibility that some jurisdictions may implement laws challenging the use of the limited risk distributor structures as well.

Companies are also taking a closer look at the preparatory and auxiliary nature of activities and considering where they otherwise had fragmentation of activities that may now form part of a cohesive business operation.

The industry should closely monitor any future guidance on allocating profits attributable to permanent establishments.
Actions
8-10

Examining the impact of BEPS on the life sciences sector
Aligning transfer pricing outcomes with value creation

The arm's-length principle is well-established, and the BEPS action items do not purport to change that.\(^8\) Countries use the principle as the cornerstone of transfer pricing rules, and the OECD report says it has proven useful as a practical and balanced standard for tax administrations and taxpayers to evaluate transfer prices between associated enterprises and to prevent double taxation.\(^9\) However, because of a perceived emphasis on contractual allocations of functions, assets and risks, the OECD believes that the existing guidance on the application of the principle has proven vulnerable to manipulation. Accordingly, the action items have focused on strengthening guidance on applying the arm's-length principle to align profits with the value created through underlying economic activities.

The final reports for Actions 8–10 have six interlinked topics:

1. Guidance for applying the arm's-length principle
2. Guidance on commodity transactions
3. Further work on transactional profit split is scoped
4. Guidance on intangibles
5. Guidance on low value-adding intra-group services
6. Guidance on cost contribution arrangements

The OECD views the recommended changes as shared interpretations of how Article 9, paragraph 1 of the OECD and UN Model Tax Convention should be applied. Accordingly, where these provisions are found in treaties, the shared interpretations between countries will have immediate application.

This section will focus specifically on items 1, 3 and 4 as they relate to the life sciences sector.

**Why are these actions important to life sciences companies?**

Supply chains at life sciences companies are complex, with IP licensed as necessary to support global operations. IP owners have been compensated as entrepreneurs earning residual returns. The commonly used transfer pricing methods to value IP include comparable uncontrolled pricing (CUP), transactional net margin (TNMM) and transactional profit split. Other functions (distribution, logistics and so forth) are compensated on a routine basis, such as a cost-plus service fee or resale minus distribution margin. In some cases, there is a division between the funding and ownership of IP and activities related to its use or exploitation. The action item recommendations focus more on decision-making related to IP, the allocation of risk based on control and the financial capability of such risk, as well as the development, enhancement, management, protection and exploitation (DEMPE) functions related to the IP.

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Details of Actions 8-10

Guidance for applying the arm's-length principle
As part of the discussion on applying the arm's-length principle, the OECD issued detailed guidance on analyzing risks as an integral part of a functional analysis. The discussion notes that cash boxes that provide funding, but cannot control the related financial risks, will attain no more than a risk-free return — or less if the transaction is commercially irrational. Many companies have structures designed around principals funding the development of intellectual property and earning the return on such IP. Risks are high in the life sciences industry when developing IP, and companies need to make sure that the exercise of control over these risks also lies with the principals. The OECD lays out a new six-step analytical framework, as summarized below:

Step 1: identify economically significant risks with specificity
Step 2: determine contractual assumption of the specific risk
Step 3: perform functional analysis in relation to risk
Step 4: interpret steps 1-3
Step 5: allocate risk
Step 6: price the transaction, taking into account the consequences of risk allocation

Risks are defined as the effect of uncertainty on the objectives of the business, and its significance depends on the likelihood and size of potential profits or losses arising from it. The risk (and related returns) should be allocated to the party that contractually assumes the risk unless it does not exercise control over the risk and does not have the financial capacity to assume the risk. To determine whether the contractual assumption of risk is aligned with the conduct of the parties and other factors, companies should analyze whether the parties follow the contractual terms and whether the party assuming the risk manages the risk and has the financial capacity to assume it.

Risk management is defined as the function of assessing and responding to risk associated with commercial activity. Risk management comprises three elements:

- The capability to make decisions to take on, lay off or decline a risk-bearing opportunity, together with the actual performance of that decision-making function
- The capability to make decisions on whether and how to respond to risks associated with the opportunity, together with the actual performance of that decision-making function
- The capability to mitigate risk by taking measures that affect risk outcomes

Control over risk requires the first two elements of risk management and the actual performance of risk mitigation. It is insufficient to merely perform risk mitigation or make decisions that shape the policy environment. The mere formalizing of decision-making in any form does not qualify as a decision-making function exercising control over a risk.

Financial capacity to assume a risk is defined as access to funding to take on the risk or to lay off the risk, to pay for risk mitigation functions and to bear the consequences of risk materialization.

It will be important for life sciences companies to assess which parties in the supply chain are performing these activities around risk.

Further work on transactional profit split is scoped
Briefly: the 2015 report confirms the use of the profit split method (PSM) as appropriate to align profits with value creation. Profit splits may be used to divide residual income after paying a cost-plus remuneration to limited-function entities. The profit split may be accomplished, for example, using production capacity, headcount and value of production. The draft guidance will be developed by the OECD’s Working Party 6 in 2016 and finalized in 2017.

Those in the life sciences sector should closely monitor this topic. Consider, for example, a company that has a non-US principal who uses a US contract manufacturer and US limited risk distributor (LRD) for sale into the US market. The US LRD earns a market return and most of the profits retained by the principal as IP owner. The concern may not come from Action 7 on the anti-fragmentation rule for permanent establishments. The real risk could be a challenge on the transfer pricing adjustment to use PSM rather than market return for the LRD.

Guidance on intangibles
Actions 8-10 also provide guidance for valuing and pricing intangibles, a very relevant topic for the life sciences sector. The definition of intangible remains the same as in the 2014 report — “not a physical or financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.” The report also notes that specific local market characteristics and group synergies are not intangibles but should be taken into account in comparable analysis.

The report’s new definition for marketing intangibles is “an intangible … that relates to marketing activities, aids in the commercial exploitation of a product or services, and/or has an important promotional value for the product concerned.” These can include things such as trademarks, trade names, customer lists and proprietary market data that can aid in marketing and selling goods or services to customers.
The economic return from IP and costs will be allocated to entities that perform and control the DEMPE functions. As discussed under item 1, the contractual assumption of risk associated with the DEMPE functions (financial or legal risk) means that financial consequences of the risk will be allocated to that enterprise as long as it functionally exercises control over the risk.

Another topic – hard-to-value intangibles (HTVI) – is also relevant to the life sciences sector, specifically when it involves intangibles that are not commercially viable at the time of the transaction. HTVI may be partially developed, may need to be exploited in a manner that is considered novel at the time of transfer and may involve highly uncertain financial projections. Also included are intangibles that are not HTVI but are integral to the development or enhancement of other intangibles, and IP transferred to an associated enterprise for a lump-sum payment and/or used in connection with or developed under a cost contribution or similar arrangement.

The impact to companies when HTVI is part of a transfer is to allow tax administrations to use ex-post evidence to evaluate ex-ante pricing arrangements (i.e., the use of hindsight). Certain circumstances and safe harbors may apply, such as if the taxpayer demonstrates that ex-ante projections at the time of transfer were reliable based on risks and reasonably foreseeable events, if the difference between financial projections and actual outcomes results in a change of compensation from the HTVI of less than 20%, if the commercialization period of five years has passed and the difference between financial projections and actual outcomes is not more than 20%, and if the HTVI transfer is covered by an advance pricing arrangement (APA).

What actions are life sciences companies taking with respect to Actions 8–10?

The reports on Actions 8–10 are getting a lot of consideration, particularly because intangible property plays a significant role in the life sciences sector. Companies are undertaking or reviewing RACI analyses of their supply chains to understand who exercises control over risk and who has the financial capacity to assume those risks, as well as control the performance of outsourced functions in relation to the DEMPE functions of the intangibles. Reviewing substance and critical people functions for IP owners is essential to assessing the potential risk to the company.

From that outcome, companies are undertaking stopgap analyses of their supply chains. In some instances, they are considering co-locating key value-adding functions in jurisdictions where IP is owned, which is connected to recommendations under Action 5 for the IP regimes.
Examining the impact of BEPS on the life sciences sector
Guidance on transfer pricing documentation and country-by-country reporting

Many in the industry are aware of the general recommendations under Action 13 for the master file, local file and template for country-by-country (CbC) reporting. The recommendation from the OECD is that the ultimate parent of the group with revenue of EUR750 million or greater should report the CbC forms for fiscal years starting in 2016, filing within 12 months from fiscal year-end. The jurisdictions that have adopted or drafted regulations to implement CbC reporting have generally followed these recommendations.

Like the Action 5 report, Action 13 calls for more transparency. One of the requirements is that summaries of certain rulings and APAs may need to be disclosed in either the master file or the local file, or both. The master file requires the listing and summary of rulings related to the “allocation of income among countries.” In the life sciences industry, these rulings include such matters as unilateral APAs, permanent establishment and principal rulings. But also consider how broad the definition of “allocation of income” could be construed so as to apply to other rulings involving investment in certain activities or regions as a way to shift income from other jurisdictions.

Summaries of rulings must be disclosed in the local file when the rulings relate to a material controlled transaction in a jurisdiction that is not party to the ruling and when the other jurisdiction has introduced transfer pricing documentation that requires the filing of an OECD-type local file. In addition to the summaries, the full ruling itself might be requested by jurisdictions that are subject to exchange of information under certain treaties.

With CbC, companies have raised concerns about how information on their complex supply chains, populated on the standard forms, will be viewed by various jurisdictions and potentially used for pricing comparison among countries with similar activities.

Life sciences companies are also concerned about how these new recommended disclosures might affect their reputation and risk of tax controversy, particularly around disclosing summaries of APAs and rulings.

What actions are life sciences companies taking with respect to Action 13?

Besides gathering the information to prepare the documentation, some companies are taking a strategic look at drafts of the reports to see how all three files fit together to tell the company’s story. In addition to Action 5, the risk assessment framework developed by EY covers the transparency aspects of Action 13. One of the recommendations from this framework might be to consider withdrawing from certain rulings because the filing of reports under Action 13 would commence with 2016 information, whereas withdrawing may not be applicable to Action 5 due to its retroactive nature.

Companies undergoing business change might also look at limiting controlled transactions (i.e., having a centralized supply point) to minimize the ruling summaries necessary under the local file. Lastly, companies are considering supporting their ruling positions and supply chains through further transfer pricing documentation.
Conclusion

While the BEPS reports are “soft law” and are not legally binding, they are expected to be implemented by countries that are part of the consensus. We are already seeing jurisdictions act on certain recommendations. The UK, Ireland, Switzerland and Belgium are looking to align their IP regimes based on the recommendations in Action 5, and multiple jurisdictions, including Australia, Spain and Mexico, are implementing recommendations under Action 13. Some recommendations under Actions 8–10 will have an immediate impact.

In light of this, companies where IP is important, such as those in the life sciences sector, are starting to review their supply chains with a focus on substance and critical people functions. They are seeking to address gaps where they may not align with the new recommendations for IP regimes or IP ownership and pricing in line with the DEMPE functions. This analysis also identifies the permanent establishment risks discussed under Action 7. In the jurisdictions where Action 13 is already implemented or is in progress, companies are not only considering how to draft the forms and reports, but they are also focusing on what information will be included – and with whom it will be shared – so they can mitigate any reputational or other business concerns.
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