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Transfer Pricing of Intellectual Property: Legal, Economic, and Taxation Approaches under OECD, EU, and Austrian Frameworks

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Abstract

The purpose of the study is to shed light on the taxation and transfer pricing of intellectual property within multinational enterprises (MNEs) which allocate income from IP assets across jurisdictions. The analysis is based on a doctrinal legal approach, supported by a comparative analysis of OECD Guidelines, EU directives (ATAD, DAC6), Austrian national law, and some additional relevant initiatives within the field concerned. The research finds that traditional transfer pricing methods, such as the CUP and TPSM, face limitations when applied to hard-to-value intangibles. The DEMPE framework and the OECD's Modified Nexus Approach have emerged as central tools in allocating profits appropriately. The thesis concludes that a coordinated international approach to IP transfer pricing is crucial to prevent base erosion and profit shifting.

Keywords: intellectual property, intangibles, transfer pricing, controlled transactions, intra-group transactions, arm-lenghth principle, IP structuring, OECD Guidelines, DEMPE, HTVI, BEPS, ATAD, DAC6.

Ziel der Masterarbeit ist es, die Besteuerung und Verrechnungspreisgestaltung von geistigem Eigentum innerhalb multinationaler Unternehmensgruppen (MNEs) zu beleuchten, die Einkünfte aus IP-Vermögenswerten grenzüberschreitend zuweisen. Die Analyse basiert auf einem dogmatisch-rechtlichen Ansatz und wird durch eine vergleichende Analyse der OECD-Leitlinien, der EU-Richtlinien (ATAD, DAC6), des österreichischen Steuerrechts sowie weiterer relevanter Initiativen ergänzt. Die Untersuchung zeigt, dass traditionelle Verrechnungspreismethoden wie die CUP- und die TPSM-Methode bei schwer bewertbaren immateriellen Wirtschaftsgütern an ihre Grenzen stoßen. Das DEMPE-Konzept sowie der modifizierte Nexus-Ansatz der OECD haben sich als zentrale Instrumente zur sachgerechten Gewinnzuordnung erwiesen. Die Arbeit kommt zu dem Schluss, dass ein international koordinierter Ansatz bei der Verrechnungspreisgestaltung von geistigem Eigentum entscheidend ist, um Gewinnverkürzung und Gewinnverlagerung (BEPS) zu verhindern.

Schlüsselbegriffe: geistiges Eigentum, immaterielle Werte, Verrechnungspreise, kontrollierte Transaktionen, konzerninterne Transaktionen, Fremdvergleichsgrundsatz, IP-Strukturierung, OECD-Leitlinien, DEMPE, HTVI, BEPS, ATAD, DAC6.

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Table of abbreviations

I. ALP — Arm's Length Principle

II. APA — Advance Pricing Agreement

III. ATAD — Anti-Tax Avoidance Directive

IV. BEFIT — Business in Europe: Framework for Income Taxation

V. BEPS — Base Erosion and Profit Shifting

VI. CCA — Cost Contribution Agreement

VII. CFC — Controlled Foreign Company

VIII. CIT — Corporate Income Tax

IX. CPM — Cost Plus Method

X. CUP — Comparable Uncontrolled Price

XI. DAC — Directive on Administrative Cooperation

XII. DEMPE — Development, Enhancement, Maintenance, Protection and Exploitation

XIII. DST — Digital Services Tax

XIV. EBITDA — Earnings Before Interest, Taxes, Depreciation and Amortization

XV. EStG — Einkommensteuergesetz (German Income Tax Act)

XVI. GAAR — General Anti-Abuse Rule

XVII. HTVI — Hard-to-Value Intangibles

XVIII. IRS — Internal Revenue Service

XIX. KStG — Körperschaftsteuergesetz (German Corporate Income Tax Act)

XX. MNA — Modified Nexus Approach

XXI. MNE — Multinational Enterprise

XXII. OECD — Organisation for Economic Co-operation and Development

XXIII. PE — Permanent Establishment

XXIV. R&D — Research and Development

XXV. RPM — Resale Price Method

XXVI. TNMM — Transactional Net Margin Method

XXVII. TP — Transfer Pricing

XXVIII. TPSM — Transactional Profit Split Method

I. Introduction

Intellectual Property is an extremely attractive research topic. IP emerges out of creativity of the person's mind. As we know, it includes creative works of literature and art, images, designs, inventions, and much more. IP law in this case plays a vital role as it protects creators from unauthorized use or reproduction by granting creators exclusive rights over their work. It incentivises innovation, as they are fairly rewarded and their efforts are recognized accordingly. Legal entities in technology, innovation, and entertainment sectors highly rely on IP as the basis for their business model. It adds substantial value and improves their competitive advantage. Also, no pharmaceutical manufacturing can be successful without the existance and proper protection of IP. Moreover, IP is one of deciding factors on tax planning for business enterprises, which often raises complex issues in transfer pricing.

Generally, the main categories of IP include patents, which grant inventors exclusive rights over their inventions; copyrights, which mainly protect creative works of literature, music, and notably software; trademarks, which secure brand identifiers like logos and distinctive signs; and trade secrets and know-how, which refer to confidential business information such as proprietary formulas or production methods.

At the beginning of the research, it is important to mention that the exact legal classification of IP assets is a key determinant for their tax treatment. Apart from being uniformly called IP, this notion also refers to a broader term called "intangibles". It may additionally include other categories, such as goodwill and ongoing concern value, group synergies, as well as market-specific characteristics. [1] This is highly relevant for transfer pricing purposes and will be examined more in detail in chapter IV.

According to article 12 of the OECD Model Tax Convention, royalties are defined as: *"payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience."* [2] Under this definition, most payments for the licensing or use of IP are classified as royalties, which are typically subject to withholding tax in the source state, unless reduced or eliminated by a tax treaty. This master's thesis will focus on uncovering the taxation of royalties and capital gains.

[1] OECD, Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022 (OECD Publishing 2022) ch VI, sub-sections A.4.6–A.4.8.

[2] OECD, Model Tax Convention on Income and on Capital: Full Version 2017 (OECD Publishing 2019).

The nature of the IP and the transaction determine, how the income can be treated: as royalty under article 12, business profit under article 7, or capital gain under article 13, each of which entails a different source of taxation, withholding tax treatment, and reporting obligation. Royalty payments are repeated or periodic payments for limited-use rights; capital gains — one-time payments for full ownership or long-term economic rights over the IP; business income — if the IP is actively used in the course of a business (for example, embedded in a product or service). This distinction is critical for the future analysis in this work, because tax treaties apply different rules to different income types, especially in determining which country has the right to tax and what tax rates apply.

Each country's law rules the creation, ownership, protection, and exploitation of IP. For example, Austria classifies IP assets for tax purposes under the Income Tax Act [3] and Corporate Tax Act. [4] While domestic law defines what qualifies as IP and how it can be transferred or licensed, its classification for international tax purposes must align with treaty definitions and OECD guidance. Thus, countries interpret their domestic law relying on international standards. The OECD Model Convention and Transfer Pricing Guidelines are not binding but serve as soft law frameworks. The OECD Model is the basis for most bilateral treaties, which ensures a degree of consistency in classifying IP income.

However, countries may deviate in implementation. Some interpret "royalties" more broadly (e.g. India, U.S.), while others follow the OECD strictly [5]. Transfer pricing rules like the arm's lenghth principle or DEMPE framework, derived from OECD guidelines, are incorporated into most countries' domestic law through legislation and case law. Thus, the OECD provides harmonization, while national law implements these norms.

Also it is important to clarify, who is the subject of the tax rules. Generally, such categories are the following: natural person, possibly self-employed or an entrepreneur; legal entity, corporation/MNE. This thesis focuses on the application of transfer pricing rules to transactions involving IP among legal entities, in particular multinational enterprises engaging in commercial activity. The analysis is mostly limited to cross-border situations, where at least two tax jurisdictions are involved, thus triggering the need for compliance with international legal frameworks such as those outlined in the OECD Transfer Pricing Guidelines, as well as relevant EU and national Austrian legislation.

In the context of transfer pricing, an intangible, according to OECD guidance, is "something which is not a physical asset or a financial asset, which is capable of being owned or controlled

[3] Einkommensteuergesetz 1988 (EStG), BGBl Nr 400/1988.
[4] Körperschaftsteuergesetz 1988 (KStG), BGBl Nr 401/1988.
[5] Rajendra Nayak and Monique van Herksen, "Global Experts Debate Landmark Indian Ruling on Software Taxation" (Kluwer International Tax Blog, 8 October 2021).

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". [6] Basically, transfer pricing rules are based on the arm's length principle defined in Article 9 of the OECD Convention and Transfer Pricing Guidelines, which states that transactions between associated enterprises must be priced as if they were between independent parties in the open market. This principle ensures that taxable profits are appropriately allocated and prevents artificial shifting of income. [7] MNEs often structure their operations so that IP assets are relocated to low-tax jurisdictions, receiving royalties or licensing fees, and claiming deductions in higher-tax countries. These practices raise critical concerns regarding tax base erosion. Moreover, the abovementioned provisions require that income must be allocated based on the actual conduct and functions performed, assets used, and risks assumed—commonly referred to as the DEMPE analysis. [8] This concept will be analyzed in Chapter V.

One of the real-life examples essential to ignite the interest in the topic is the *US vs Coca Cola case*. The dispute focused on royalties paid by Coca-Cola's foreign subsidiaries to the parent company located in the U.S. The Court supported the IRS arguing that the royalties were understated, which reduced taxable income in the U.S. Even though Coca-Cola used a transfer pricing method agreed upon in prior tax rulings, the IRS claimed that this method no longer reflected the arm's length principle. [9]

In addition to the legal acts named, to reduce and desirably eliminate aggressive tax planning strategies, the lawmakers have adopted at the international level the OECD/G20 Base Erosion and Profit Shifting (BEPS) Action Plan, notably Action 8–10 (Aligning Transfer Pricing Outcomes with Value Creation) and Action 5 (Harmful Tax Practices), which introduce tighter rules on intangible asset valuation and transparency. Within the EU, such measures were harmonized through the Anti-Tax Avoidance Directive (ATAD I and II). [10] CFC rules included thereinto target passive income from intangibles, interest limitation rules, and hybrid mismatch rules, all of which are highly relevant to the tax treatment of IP in cross-border structures.

[6] OECD, Transfer Pricing Guidelines (n 1) ch VI, para 6.6.
[7] Jérôme Monsenego, Introduction to Transfer Pricing (Wolters Kluwer 2023) ch 1, 5–49.

[8] Karol Dziwinski, The DEMPE Concept and Intangibles (Wolters Kluwer 2022) ch 2, s 2.2, 75–85.
[9] United States v Coca-Cola Co, US Tax Court, Docket No 31183-15 (18 August 2024).
[10] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries [2017] OJ L144/1.

Additionally, DAC6 (Directive on Administrative Cooperation) requires intermediaries and taxpayers to disclose certain cross-border arrangements that bear hallmarks of aggressive IP tax planning, such as royalty payments routed through preferential regimes. [11]

Another crucial component of EU tax law in this area is the State Aid, through which the European Commission has challenged advance pricing agreements and IP-related tax rulings that result in selective advantages, potentially violating EU internal market rules .

Having described the key concepts and legislation highly important to this master's thesis, needless to highlight that this paper will critically assess how intellectual property is classified, valued, and taxed. It will examine the interaction between transfer pricing and the taxation of intellectual property, focusing on both international and EU instruments, with brief reference to Austrian law. Particular attention will be given to how these frameworks co-exist. The goal is to assess whether current legal mechanisms effectively ensure that income derived from intellectual property is taxed where value is created, and to identify potential gaps and inconsistencies that require further improvement and development.

Thus, the questions raised before the start of the research were the following:

- how do multinational enterprises apply transfer pricing principles to intellectual property in practice?
- what are the main features of OECD, EU, and Austrian transfer pricing and IP taxation frameworks relevant for IP?
- how do these legal frameworks interact and influence the taxation of IP income?
- what are the strengths and challenges of current transfer pricing rules related to intellectual property?

The research methodology combines doctrinal legal analysis with comparative study. Primary sources, such as OECD Transfer Pricing Guidelines, relevant tax treaties, EU and national legislation, are examined. Secondary sources include academic literature and practical case studies to illustrate application and challenges in real world scenarios.

[11] Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements [2018] OJ L139/1.

II. Taxation of IP Income: National Approach. Focus on Austrian law

2.1 Taxation of income from commercial activities and corporations derived by resident taxpayers under Austrian law

Austria has a strong legal framework for IP which encompasses several national laws. Each of them focuses on a specific category of IP rights. Firstly, the Urheberrechtsgesetz 1968 (Copyright Act, further—UrhG)[12] protects literary, artistic, and scientific works. While the law itself obviously does not define taxation rules for these IP rights, it provides the basis for their commercial exploitation. Section 19 UrhG mentions that the creator's moral rights like authorship and integrity of work are non-transferable, while sections 24–28, however, mention that economic exploitation rights which include reproduction, adaptation, and distribution, can be licensed exclusively or non-exclusively, or assigned.

Importantly, as we know, software is protected under copyright law. Under the EU Directive on the Legal Protection of Computer Programs implemented in Austria, economic rights in software may be licensed or assigned, with the author's moral rights remaining inalienable. If software is developed in employment, the economic rights usually vest in the employer by law (Art. 2(3) of the Directive, § 40b UrhG). In the context of transfer pricing, software is often licensed intra-group. Also, at the EU level, the copyright area is harmonized through other directives such as InfoSoc Directive 2001/29/EC and Digital Single Market Directive 2019/790, which standardize copyright exceptions and licensing rules across Member States.[13] Copyright is inherently personal and non-transferable.

Secondly, the Patent Act 1970 (Patentgesetz, PatG)[14] governs the protection of inventions that are new, involve an inventive step, and are industrially applicable. It defines the scope and duration of patent rights in Austria. On the EU level, the Regulation No 1257/2012 and Agreement on a Unified Patent Court support the implementation of the Unitary Patent System, which simplifies cross-border patent protection in participating Member States.[15] Section 33 PatG states that both the patent application right and the granted patent can be transferred fully or partly through agreement, inheritance, or court order. According to § 43 PatG, rights over this IP become effective

[12] Urheberrechtsgesetz 1968 (BGBl 111/1936, as amended by BGBl I 111/2010).
[13] Guglielmo Maisto, Taxation of Intellectual Property under Domestic Law, EU Law and Tax Treaties (IBFD 2018) ch 10, 229–237.
[14] Patentgesetz 1970 (BGBl 259/1970).
[15] Maisto, Taxation of Intellectual Property (n 14).

against third parties only upon entry in the Patent Register, thus requiring the new owner to be registered.

Thirdly, the Trademarks Act 1970 (Markenschutzgesetz, MSchG)[16], defining trademarks, sets out procedures for registration, use, and enforcement. It aligns with the EU Trade Mark Regulation 2017/1001[17] and the Trademark Directive 2015/2436[18], ensuring consistency in how trademark rights are granted and protected across the EU. According to §10 MSchG, ownership may be transferred wholly or partially, e.g., by sale, merger, or inheritance. Similar to patents, article 20 EUTMR and §11 MSchG state that such transfer is legally effective even without register entry, although effectiveness against third parties, like licensees, successors, or creditors, requires registration in the Trademark Register. §34 MSchG explicitly mentions that use of the trademark by a licensee is considered equivalent to use by the owner, which is important to avoid revocation for non-use. At the same time, according to article 25 EUTMR, an EU trade mark may be licenced for some or all of the goods or services, and for the whole or part of the Union.

Next, the Design Protection Act 1990 (Musterschutzgesetz)[19] protects the appearance of products, such as shapes, colors, and surface patterns. Its EU counterpart is the Community Design Regulation 6/2002,[20] which allows for the registration of designs valid throughout the EU and ensures harmonized protection standards.[21] As formal details are similar to trademarks, rights are protected post-registration. Transfer and licensing, often bundled with trademarks, can take place, typically requiring no mandatory register.

Trade secrets are safeguarded by the Unfair Competition Act 1984 (Gesetz gegen den unlauteren Wettbewerb),[22] particularly in cases of unauthorized acquisition or disclosure of confidential business information like secret formulas or production methods. At the EU level, the Trade Secrets Directive 2016/943[23] harmonizes rules on lawful acquisition, use, and protection of trade secrets. No formal ownership or registration is required. Rights are enforced via confidentiality and anti-disclosure provisions, and transfer/licensing is contract-based, governed by general civil and competition law. Their valuation is difficult due to secrecy and lack of comparables, and their legal protection affects risk attribution in TP models.

[16] Markenschutzgesetz 1970 (BGBl 260/1970).
[17] Regulation (EU) 2017/1001 of the European Parliament and of the Council of 14 June 2017 on the European Union trade mark [2017] OJ L154/1.
[18] Directive (EU) 2015/2436 of the European Parliament and of the Council of 16 December 2015 to approximate the laws of the Member States relating to trade marks [2015] OJ L336/1.
[19] Musterschutzgesetz 1990 (BGBl 49/1990).
[20] Council Regulation (EC) No 6/2002 of 12 December 2001 on Community designs [2002] OJ L3/1.
[21] Maisto, Taxation of Intellectual Property (n 14).
[22] Bundesgesetz gegen den unlauteren Wettbewerb 1984 (UWG) (BGBl 448/1984).
[23] Directive (EU) 2016/943 of the European Parliament and of the Council of 8 June 2016 on the protection of undisclosed know-how and business information (trade secrets) against their unlawful acquisition, use and disclosure [2016] OJ L157/1.

While the above mentioned laws define and protect IP rights, Income Tax Act deals with the taxation of income derived from IP. This includes royalties, licensing fees, capital gains from the sale of IP rights, and income from the exploitation of copyrighted works or patents. The income from IP may be classified as business income, self-employment income, or income from capital, depending on the legal and contractual arrangements.[24]

In international tax law, particularly for royalty payments from IP rights, "beneficial ownership" is a highly important term, which means that the person or entity actually enjoys the benefits of the income like royalties, has the right to use or dispose of the income freely (not just forwarding it to someone else), is not just an intermediary, like an agent or nominee. This concept is not always the same as legal ownership — a person may be listed as the recipient of royalties, but not be the true economic owner.[25]

OECD Model Convention Article 12 clarifies that only the beneficial owner of royalties is entitled to treaty benefits. Additionally, Interest and Royalties Directive exempts certain intra-group royalty payments from withholding tax within the EU, but only if the recipient is the beneficial owner.

For example, Company A in Austria pays royalties for the use of a patent to Company B in a low-tax country. Company B immediately transfers 95% of the royalties to Company C, the true economic owner in another jurisdiction. In this case, Company B is not the beneficial owner. Austria, as the source state, may deny treaty benefeficial lowering of withholding tax because Company B does not qualify as the beneficial owner.

In Austria, the taxation of income derived from IP depends on the legal form of the taxpayer. A distinction must be made between individuals, who are subject to personal income tax under the Einkommensteuergesetz (further EStG), and legal entities, which fall under the Körperschaftsteuergesetz (further KStG).

Before we dive into taxation of corporations, taxation of business income for individuals will be briefly examined. Provisions of §23 EStG define what counts as "Einkünfte aus Gewerbebetrieb" (income from trade or business). It lists three main categories of business income. Firstly, income from an independent, sustainable activity with profit intent, excluding agriculture or self-employment. Secondly, profit shares and specific remunerations of partners in partnerships, and capital gains as defined in § 24 EStG. Thus, royalty payments or other types of income related to IP fall under the scope of business income, plus payments connected to business. Additionally, progressive tax rate applies according to §33.

[24] Maisto, Taxation of Intellectual Property (n 14).
[25] Dziwinski (n 8) ch 1, s 1.5, 47–52.

In Austria, self-employed individuals and small business owners can determine their taxable profits using a simplified method known as Einnahmen-Ausgaben-Rechnung under § 4(3) EStG, provided they are not legally required to keep formal accounts and have not opted to do so voluntarily. This cash-based method calculates profit as the difference between actual income received and expenses paid. However, once a business exceeds an annual turnover of EUR 700,000 for two consecutive years, it must switch to full double-entry bookkeeping and determine profits under § 4(1) EStG. This method is based on the net equity comparison and follows the principles of proper commercial accounting, requiring a more comprehensive and accrual-based approach. Any costs directly connected to royalty income—such as legal fees, R&D expenses, or licensing costs—may be deducted as business expenses under § 4(4) EStG, reducing the taxable base accordingly.

Alternatively, under § 17 EStG, a flat-rate deduction method (Durchschnittssatz) is available to certain professional groups, having freelence or business imcome, including writers, lecturers, scientists, teachers, and artists under § 22 Z 2. In this case, they must meet the turnover and bookkeeping requirements and not be subject to income tax under employment law. This method allows them to deduct 6% of their revenues (up to €13,200) instead of itemizing actual expenses.

In addition, the alienation (sale or transfer) of intellectual property rights is considered to be business income under § 23 EStG, and the proceeds from such a sale are subject to taxation as part of the overall income.

While most income falling under §§ 22, 23, or 28 EStG is taxed at the progressive personal income tax rates outlined in § 33 EStG, an important exception exists for patented inventions. § 38 EStG provides for a reduced tax rate for the income derived from the exploitation of patents. To qualify for this beneficial regime, the income must stem from a registered patent, the inventor must be recorded in the Austrian Patent Register as the rightful owner, the invention must be actually used by a third party (e.g., a company paying a royalty) in a territory where patent protection exists. The rule also applies to the sale of a patent. Under these conditions, the income attributable to the exploitation of a patented invention will be taxed at half of the taxpayer's average income tax rate. For example, if the inventor's average tax rate is 30%, the patent-related income will be taxed at only 15%.[26]

Moreover, § 38 EStG may also be applied to employment income under § 25 EStG in cases where an invention is created by an employee. If the employer grants a special remuneration to the employee-inventor, this income may also benefit from the halved tax rate, provided that the invention and its use meet the same criteria outlined above.

[26] Maisto, Taxation of Intellectual Property (n 14).

Furthermore, as far as the taxation of IP income for corporations is concerned, in contrast to individuals, corporations—such as Aktiengesellschaften (AG), Gesellschaften mit beschränkter Haftung (GmbH), private foundations, and associations with legal personality—are subject to corporate income tax under the Körperschaftsteuergesetz (further KStG). These entities are taxed on all forms of income, including income derived from the exploitation or alienation of intellectual property.

Generally, both EStG and KStG apply to corporations in Austria. The KStG is the main law that governs how legal entities are taxed in Austria. It tells us who is subject to corporate income tax (Körperschaftsteuer), the tax rate, special rules for group taxation, exemptions, and dividend taxation. The EStG contains the general rules on how to calculate taxable income—these rules are used for both individuals and corporations. For example, how profit is determined (e.g., net equity comparison in § 4(1) EStG), what counts as business income, which expenses are deductible (§ 4(4)).

Under § 7(2) KStG, the basis for corporate taxation is the income calculated according to the general rules of the EStG, particularly § 4(1), which establishes the net equity comparison as the standard method of profit determination. All income from IP—whether licensing, royalties, or sale—is classified as business income under § 23 EStG. The applicable tax rate for corporations is a flat 23%, as per § 22 KStG, regardless of the type or origin of income. Notably, the preferential tax treatment under § 38 EStG with the halved tax rate for patent-related income does not apply to corporations.

A key feature of Austrian tax law is that, in accordance with commercial accounting rules, corporations are not permitted to capitalize self-created intangible assets, including internally developed IP. This applies to R&D costs, personnel expenses, and material expenditures incurred in the process of creating intangible assets. As a result, such expenses must be recognized as expenses in the year they are incurred, thereby immediately reducing the taxable profit.[27] These costs are not added to the balance sheet as assets, which means that the sale of the self-created IP results in a full increase in taxable profit, since the asset had no prior book value.

By contrast, purchased IP rights may be capitalized on the balance sheet and depreciated over time, following the ordinary rules for asset amortization. This distinction—between internally generated and acquired IP—is crucial for tax planning.

Finally, corporations may also deduct ongoing expenses related to the management, defense, and exploitation of IP rights, including legal fees and marketing costs, as ordinary business

[27] Maisto, Taxation of Intellectual Property (n 14).

expenses. The sale or licensing of IP constitutes a taxable event, and the income is treated as ordinary business income under § 23 EStG, subject to the flat 23% corporate tax rate.

2.2 Taxation of income from IP derived by non-resident taxpayers. Country-specific anti-avoidance rules targeting IP structuring

According to EStG § 1(3), individuals without residence or habitual abode in Austria are limited-tax liable. They pay tax only on Austrian-source income. Legal entities, like corporations, without a legal seat or effective management in Austria are also subject to limited tax liability. Moreover, under § 98(1)(6) EStG, non-residents must pay Austrian tax on income from leasing property rights connected to immovable assets in Austria. This includes, for example, rights to exploit intellectual property (IP) that is either used within Austrian territory or registered in Austrian public registers. This also includes royalties for phonogram use, film distribution rights, payments for know-how (even if not copyright-protected), and literary royalties. [28] As a rule, a person with limited tax liability can only be taxed if there is a sufficient connection to Austria. However, income from the sale (alienation) of IP rights is not covered here in this provision—only ongoing lease/license income.

Royalty payments for the use of intellectual property made to non-resident recipients are subject to a 20% withholding tax (WHT). This rule is set out in § 99(1)(3) of EStG and applies whether the IP is used in Austria or if the payer is an Austrian resident. WHT is triggered at the moment a royalty is paid or made available to the non-resident rightsholder. The obligation to withhold and transfer this tax to the Austrian tax authorities lies with the Austrian payer.

Austria has signed DTTs with many countries, which often reduce or eliminate the 20% WHT on royalties. These treaties override domestic law if applied correctly. Most treaties reduce the rate to 10% or less, even 0%, depending on the treaty partner and whether the beneficial owner requirements are met. To benefit from a reduced DTT rate, the non-resident recipient must prove tax residency in the treaty country and beneficial ownership of the royalties.

As the Austrian Ministry of Finance clarifies, there are two methods for applying DTT relief. Firstly, exemption at source. The Austrian payer applies the reduced WHT rate directly after the advance approval from the Austrian tax office (Zentraler Antrag auf Entlastung, ZS-Formular)[29].

Secondly, a refund method when a payer withholds 20% at payment. The recipient then applies for a refund from the Austrian tax office by submitting a treaty relief claim. For example, an

[28] Maisto, Taxation of Intellectual Property (n 14).
[29] Austrian Ministry of Finance, Relief from Austrian Withholding Taxes under Double Taxation Conventions (DTC).

Austrian company pays €100,000 in royalties to a Cyprus-based IP holding company for the use of a trademark. Under Austrian law, a 20% WHT (€20,000) must be withheld. However, Austria–Cyprus DTT[30] establishes the 0% royalty WHT rate, if the Cypriot company is the beneficial owner.

Provisions of § 99(2) sentence 2 allow EU/EEA residents to deduct directly connected expenses before withholding tax is calculated, if they notify the Austrian payer. This leads to a net taxation system, where WHT is not calculated on the gross income, but on the net amount (after deduction of expenses). The withholding tax rate becomes 25% instead of 20%, but only on the reduced base.

This option is only available to entities or individuals that are tax resident in an EU or EEA state, and provide written documentation of the directly related expenses before receiving the payment.

For example, a German company earns €10,000 in royalties from Austria. It spent €3,000 on legal and admin costs to manage the IP. Instead of paying 20% of €10,000 (€2,000), the company can request tax assessment and pay tax on €7,000. This net-based taxation results in a tax rate of 25% on net income (instead of 20% of gross). So, 25% of €7,000 = €1,750, which means less than €2,000, so this option is beneficial.

Pursuant to the EU Interest and Royalties Directive, royalty payments made between related corporations within the EU/EEA are exempt from withholding tax under § 99a EStG, provided that the royalty payer is either a corporation fully taxable in Austria or maintains a permanent establishment there. Accordingly, Austria has transposed the Directive into its national law.

Additionally, the Corporate Tax Act contains a rule which is to a certain extent comparable to a CFC legislation[31]. This rule is contained in §10 and §10a through which Austria implemented the Parent-Subsidiary Directive[32].

Basically, dividend income can be exempt from tax for corporations if certain criteria are met. under § 10 (1). For example, dividends received by an Austrian corporation are tax-free if it holds a minimum 10% share in a foreign corporation for at least one year.

If a foreign corporation is low-taxed and derives passive income, § 10a applies. Under these rules, the passive income of the foreign entity is attributed to the controlling Austrian corporation and taxed in Austria (Hinzurechnungsbesteuerung). Low taxation is deemed to exist if the effective tax burden of the foreign corporation does not exceed 12.5%, calculated according to Austrian tax

[30] Austria–Cyprus Double Taxation Convention (DTC), available via Austrian Ministry of Finance.
[31] Maisto, Taxation of Intellectual Property (n 14).
[32] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (Parent-Subsidiary Directive) (consolidated version 2022).

rules. Passive income includes, among others, interest, royalties, dividends, and capital gains from shares, income from finance leasing, financial activities. The CFC rules apply if the Austrian corporation, alone or together with associated entities, holds more than 50% of the voting rights, capital, or profit participation in the foreign company. The rules do not apply if the foreign entity carries out substantial economic activity supported by staff, assets, and premises.

Furthermore, a so-called "method switch" applies to certain international or portfolio shareholdings where the foreign entity's main activity is the generation of passive income. In such cases, income is not exempt but taxed in Austria, with a credit for foreign tax paid. To prevent double taxation, capital gains on the sale of such foreign entities are exempt to the extent that the underlying income has already been taxed in Austria.

As for the selling of IP (capital gain), Austria may tax it—but only in specific cases. If taxed, it means this IP is registered in Austria, or the asset is used in a business with a permanent PE in Austria, or the right is considered Austrian-sourced income under § 98 EStG. If none of those apply (e.g., IP is sold by a foreign company to another foreign company, and it is not used or registered in Austria), Austria generally has no taxing rights.

Under most DTTs concluded by Austria, capital gains from the sale of intangible property are only taxable in the seller's country of residence, unless the property is connected to a PE in Austria. If a Cyprus-based company sells a trademark used globally but not registered or exploited in Austria, Austria cannot tax the capital gain under the Austria–Cyprus DTT.

If Austria is entitled to tax the capital gain (e.g., the IP is exploited through a PE in Austria or was developed/registered there), then the gain will be taxed as business income under the rate of 23%. For example, an Austrian software company sells a self-developed software platform to a US-based buyer for €500,000. If the IP was developed and registered in Austria, Austria has taxing rights. The Austrian seller includes the gain in its corporate income tax return.

If instead a Cyprus company with no Austrian PE sells Austrian-registered IP to a third party, Austria might claim taxing rights under § 98 EStG (source-country taxation). But under the Austria–Cyprus DTT, the gain might be exempt in Austria, unless connected to a PE.

III. Practical Application

3.1 Common tax planning structures using IP

As we already know, according to the OECD Model Convention, the exclusive right to tax royalty income is granted to the state in which the beneficial owner is resident. However, many OECD member states include provisions in their tax treaties that also permit source taxation, allowing the state where the royalty income originates to impose tax.[33]

Recalling some important characteristics of intangibles mentioned previously, they often possess certain key features: they serve as revenue-generating business assets, are highly mobile, and can be transferred at relatively low costs compared to tangible fixed assets. Another notable characteristic is their firm-specific nature, which makes it difficult to apply the arm's length principle due to the frequent absence of comparable market intangibles. Consequently, when IP is transferred within a corporate group, companies often have considerable discretion in determining the transfer price of the IP itself or the royalty rates for its use under licensing arrangements. This flexibility can be exploited to shift profits to low-tax jurisdictions while minimizing tax exposure in high-tax countries.[34]

However, companies can justify themselves. For instance, the IP may be still under development at the time of transfer, or there is uncertainty surrounding future income. It is often challenging to quantify the precise benefit derived from the IP, also when it is combined with other assets.

Generally, the existing tax planning structures can be described as centralized and decentralized. These structures result in varying tax implications and determine who holds legal ownership of the intellectual property. Each of them will be explained separately next.

The first structure is the centralized one, the modes of which are deferentiated the following way: licence model and franchising/service model. Intra-group licensing means that instead of selling the IP, the parent company licenses it to a subsidiary. The parent keeps ownership but allows the subsidiary to use the IP in exchange for royalty payments. This structure centralizes ownership and allows income to flow to jurisdictions with lower tax rates. The royalty payments are deductible for the subsidiary (often in a high-tax country) and taxable for the parent (ideally in a low-tax country). This shifts profits to where they are taxed less. However, royalty rates must be

[33] Agreement between the Federal Republic of Germany and the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital (Germany–China DTA), signed 10 June 1985, in force 3 April 1986, BGBl II 1986, 840, art 12(2).
[34] Dziwinski (n 8) ch 1, s 1.1, 1-10, 30-39.

at arm's length. In addition, WHT may be imposed at the subsidiary level. However, this is often circumvented in practice through the application of the Interest and Royalties Directive or by inserting intermediary companies in jurisdictions without withholding tax. This approach is particularly effective when the intellectual property is already situated in a low-tax country.[35]

Whether the main entity will be entitled to receive all residual profits generated by the intangibles owned depends purely on its functions, financial assets, and risks. For example, a multinational group created a holding company in Luxembourg. The R&D team in Germany develops software, but the IP is assigned to the holding company, which licenses it back to the German operating company. Royalties are paid by Germany to Luxembourg, where the effective tax rate is lower.

Another example, a Dutch holding company owns a trademark. It licenses the trademark to its German operating subsidiary for €10 million/year. The German company deducts the royalties, reducing its taxable profit in Germany, while the Dutch parent pays low tax on the royalty income thanks to the innovation box regime in the Netherlands. Except for Luxembourg and Netherlands, other common jurisdictions are also Ireland, Switzerland, Singapore. However, the risks are related to anti-abuse rules (CFC rules, substance requirements). Also, OECD BEPS Action 5 requires substantial economic activity where IP income is taxed.

However, another method involves, vice versa, transferring ownership of intellectual property from a parent company to a subsidiary in a low-tax jurisdiction. It is a one-time sale between related entities. Once the IP is owned by a company in a low-tax country, the future income generated by the IP (e.g., through licensing) will be taxed at a lower rate. The sale must be at "arm's length" — i.e., the price should reflect what unrelated parties would have paid. If the IP has appreciated, the parent might be taxed on the capital gain (difference between book value and transfer price). For example, a U.S. tech company develops a valuable software product. It sells the rights to that software to its Irish subsidiary for $100 million. Ireland has a corporate tax rate of 12.5%, which is much lower than the U.S. rate. From then on, global sales of that software generate income in Ireland, not in the U.S.

Another structure pertains R&D contracts. In this case, for example, the parent company (usually in a high-tax country) performs R&D services for a subsidiary based in a low-tax country. The subsidiary becomes the legal owner of the resulting IP, even though it did not do the research itself. The parent receives a fee (taxable at the parent level), but the real profits from the IP (via licensing or sales) go to the subsidiary and are taxed in the low-tax jurisdiction. However, the contract R&D fee must reflect a fair cost-plus markup. The subsidiary must bear the risks of the

[35] Dziwinski (n 8) ch 1, s 1.1, 1-10, 30-39.

R&D. If a Swiss company hires its U.K. parent to conduct R&D for a new manufacturing process. The U.K. company performs the research, bills Switzerland for £5 million (cost + 10%), and Switzerland becomes the legal owner of the new patents. Later, Switzerland licenses the IP to other affiliates and pays tax on the income at Switzerland's low tax rate. However, one more option for MNEs to develop intangibles is collaboration with third-party contractors. Performing relevant R&D works in order to quickly adapt to the new trends might not always be possible only within the group.

Moreover, MNEs may use a franchising/service model, where the IP holding company not only licenses intangibles, but also bundles them with support services and provides with know-how. This model allows better application of the IP in operational subsidiaries but the main issue is that it raises transfer pricing challenges due to the combined pricing of intangibles and services.

Contrary to the centralized model, a decentralized business model relies on diverse group companies using intangibles for their processes, e.g., manufacturing or distribution, but they are also the owners of such intangibles. These entities are not subordinate to a central principal but hold comparable decision-making power, risks, and responsibilities. As they independently perform important functions, including R&D and IP development, there is no need in complex licensing structures. Thus, companies can also enter a cost contribution agreement (CCA). Under a CCA, two or more related companies jointly fund the development of IP. Each contributes money or resources proportionally and gains a share of ownership and benefit.[36] Because each party owns part of the IP, there is no need to pay royalties to each other. This avoids recurrent cross-border payments and simplifies taxation. Each party must contribute based on expected benefits and in line with what unrelated parties would agree to.[37] For example, a French pharmaceutical company and its U.S. affiliate agree to co-develop a new drug. The French company provides 60% of the R&D funding, while the U.S. firm provides 40%. Under the CCA, each owns that percentage of the future patent rights and can exploit them in their respective markets without paying royalties to the other.

Except for the structures mentioned before, it is also important to talk about preferential tax regimes, exploitation of tax arbitrage, hybrid mismatch structures, although the last two are not specifically relevant today. As for patent/innovation box regimes, such regimes provide lower effective tax rates on income derived from IP like patents accordingly, and software copyrights. This opportunity is created to incentivize local research and attract new businesses locating IP in the country.

[36] Dennis Josef Rudolf Nijssen, Cost Contribution Arrangements in a Changing International Tax Environment (PhD thesis, Maastricht University 2020) ch 1, 3–7.
[37] OECD, Transfer Pricing Guidelines (n 1) ch VIII, para 8.1–8.69.

According to the relevant recent data found by Tax Foundation, patent box regimes are relatively widespread in Europe. Currently, 13 of the 27 EU Member States have a patent box regime, namely Belgium, Cyprus, France, Hungary, Ireland, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Slovakia, partially Spain, including Albania, Serbia, Switzerland, Turkey, and the United Kingdom outside of the EU. The reduced tax rates provided range from 1.75 percent in Malta to 12.5 percent in Turkey. However, between 2018 and 2020, Andorra gradually eliminated its patent box regime. In 2021, Italy abolished its patent box and replaced it with a super-deduction allowing a 230% deduction of eligible research and development expenses. Conversely, in 2022, Portugal expanded its corporate income tax exemption on patent-related income from 50% to 85%.[38]

Thus, recent policy trends point toward a tightening of IP box regimes and increasing pressure for harmonization. The EU has proposed a common framework for fair and effective taxation of IP income, as part of the broader BEFIT (Business in Europe: Framework for Income Taxation) initiative, which could limit the scope of aggressive tax planning using IP boxes in the future. This initiative will be examined deeper in Chapter V.

In order to limit the frivolous exploitation of the regime and avoid harmful IP-based tax planning, the Modified Nexus Approach (MNA)[39] was introduced as part of the BEPS Action 5. As of the latest peer review, all IP regimes that remain in force in EU MS and several third countries are marked as "not harmful", provided they adhere to the MNA, thus proving to be effective. Basically, BEPS Action 5 requires that there should be “substantial research activity” in the specific country actually carried on in order to access the preferential patent box regimes.[40] Lower tax must be granted to the IP if it is located in the jurisdiction where the value is originally created, without being artificially transfered away from such in favor of jurisdictions offering a preferential tax regime. So, intangible asset mobility, if separated from R&D and IP location prevents the company from obtaining IP box tax benefits. Firms may relocate IP not based on business logic but for tax benefits.

However, as the currently available research on this topic has revealed, this approach has its flaws. One of them is that patent boxes reward the output (e.g., IP income), not the input (actual R&D expenditures).[41] Modified Nexus Approach aims to ensure IP income is taxed where substantial R&D occurred. Despite this improvement, other challenges remain. Companies that already hold patents benefit the most, even if little R&D is done locally. Moreover, reality is that

[38] Izabella Sara, Alex Mengden, Patent Box Regimes in Europe (2024), Tax Foundation (23 April 2024).
[39] OECD, ‘Action 5: Agreement on Modified Nexus Approach for IP Regimes’ (OECD 2015).
[40] OECD, "Harmful Tax Practices – Peer Review Results - Update (as of January 2025).
[41] Jessica M Müller, Christoph Spengel and Daniela Steinbrenner, “IP Box Regimes and Multinational Enterprises: Does Nexus Pay Off?” (2022) 14 World Tax Journal 75.

it might be difficult for tax authorities to trace R&D expenditures, track IP ownership, and audit income allocations. Another problem is that MNEs still are able to allocate income to low-tax patent box jurisdictions, often using intragroup licensing or CCAs. This is because the Modified Nexus Approach looks at which company carries out the R&D, not where the R&D takes place. This means that companies can still move some of their income to another country, for example, one with a patent box regime that does not follow the MNA rules. In other words, companies can shift IP income to favorable jurisdictions by structuring who officially performs the R&D, even if the bulk of the actual research is done in a different country. Except for that, the publication by International Monetary Fund[42] mentions that profit shifting by multinationals in the past also led to a small overall impact on domestic innovation activity, the effect of BEPS Action 5 reform is still uncertain, and impact on Total R&D per Dollar Spent was 0. So, when MNEs used tax strategies and benefited from IP regimes, it did not increase the amount of R&D that was done for every dollar spent, did not make R&D spending more productive. That data does not seem to be optimistic.

Finally, a practical imaginary example will be provided. LuxPharma S.A. is a pharmaceutical company headquartered in Luxembourg, where it conducts its in-house R&D. The company develops a new patented drug for cancer treatment. Patent was registered with the Benelux IP Office in 2024. In 2025, LuxPharma launches the product across the EU and licenses the technology to an Italian distributor. Total revenue from the patented product was €10 million. Under Article 50ter LITL,[43] Luxembourg allows a partial exemption of up to 80% of net eligible income from qualifying IP assets, subject to nexus rules. LuxPharma determines that its nexus ratio is 75%, thus, only €7.5 million of IP income qualifies. 80% of €7.5 million are €6 million which are exempt from tax. These savings are reinvested into R&D for a new vaccine technology. The remaining €1.5 million is taxed at Luxembourg's standard corporate tax rate.

Next, briefly mentioning hybrid mismatches. These structures emerge when jurisdictions provide different tax treatment. For example, a group sets up an IP holding in a country that allows a deduction for royalty payments, while the receiving jurisdiction either does not tax royalties or defers taxation.[44] In hybrid mismatch cases, double non-taxation appears to be highly beneficial for companies. However, due to active improvements in fighting tax avoidance, this structure is

[42] International Monetary Fund, Fiscal Monitor, April 2024: Expanding Frontiers—Fiscal Policies for Innovation and Technology Diffusion (IMF 2024).
[43] PWC, "Luxembourg – Corporate – Tax credits and incentives" (PwC Tax Summaries, 14 July 2025).
[44] Körperschaftsteuergesetz 1988, § 14 (5th section: "Sondervorschriften für hybride Gestaltungen").

now prohibited under OECD BEPS Action 2.[45] Anti-Tax Avoidance Directive in the EU has neutralized many hybrid mismatch benefits, which will be detalized in the next Chapter.[46]

In practice, the Google Inc. case shows how hybrid entity mismatches can lead to double non-taxation. The subsidiary was incorporated in Ireland but managed and controlled from Bermuda. Under U.S. tax law, which bases corporate residency on the place of incorporation, the company was considered an Irish resident. However, Irish tax law determines residency based on where the company is actually controlled, so Ireland treated it as a Bermudan resident. As a result, neither the U.S. nor Ireland taxed the company's income. Since Bermuda does not levy corporate income tax, the income remained untaxed altogether.[47]

Similarly, the "Double Irish" and "Single Malt" are now closed, but are nevertheless historically important tax planning structures that allowed multinational companies to significantly reduce their global tax bills by exploiting mismatches in the tax residency rules of different countries. Both strategies relied on IP ownership and intra-group licensing, but took advantage of specific jurisdictional nuances.

Briefly, as far as "Double Irish" is concerned, this structure typically involved two Irish companies. One of them was a tax resident outside of Ireland (for example, Bermuda), another one was an Irish tax resident paying royalties to the first. This arrangement worked by means of a U.S. company transferring IP to an Irish-incorporated company that is tax resident in a zero-tax jurisdiction, like Bermuda or Cayman Islands. A second Irish-resident company licenses that IP and collects revenue from international sales (e.g., in Europe). This second company pays massive royalties to the offshore Irish-incorporated company, reducing its Irish taxable profits to near zero. The offshore Irish company accumulates untaxed profits in Bermuda or another tax haven if applicable. Netherlands could be used to transfer profits directly to the Irish company in the tax haven, extending the scheme to a double Irish with a Dutch sandwich. It was highly beneficial because the profit earned in Ireland was almost completely offset by deductible royalty payments. Royalties go to a non-taxed Irish-incorporated/Bermuda-resident entity.[48] Luckily, OECD BEPS reforms and US tax reforms (GILTI) put pressure on these schemes.

For "Single Malt" it functioned similarly. The scheme involved an Irish company and a Maltese tax-resident company. It exploited Ireland–Malta tax treaty mismatch on residency and taxation

[45] OECD, Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 Final Report (OECD 2015), International Organizations' Documentation IBFD.
[46] Gerrit K Fibbe and Ton Stevens, 'Hybrid Mismatches Under the ATAD I and II' (2017) 26(3) EC Tax Review, 153-166.
[47] Błażej Kuźniacki and others, 'Preventing Tax Arbitrage via Hybrid Mismatches: BEPS Action 2 and Developing Countries' (WU International Taxation Research Paper Series No 2017-03, 2017).
[48] Navodhya Samarakoon and Paul R. Organ, Doubling Down on Tax Avoidance: The Effect of Double Irish Closure on the Profit Shifting of U.S. Multinational Companies, International Tax and Public Finance (2025).

rights. Hence, a company was incorporated in Ireland but tax resident in Malta. Under the Ireland–Malta tax treaty, neither Ireland nor Malta taxed the royalties: Ireland did not tax because the company was not an Irish tax resident. Malta did not tax because no income was sourced from Malta. This created "stateless income", meaning royalty income was untaxed anywhere. Thus, income could escape taxation entirely. Like the Double Irish, it was used to shift billions in profit out of reach of tax authorities.

Even though those two schemes are not in operation anymore, it is immensely important to get acquainted with them and for that purpose, a further study with a more detailed fact base is highly recommended. Despite the fact that the US was aware of the Double Irish scheme, the EU Commission was the one which forced Ireland to terminate it as of January 2015, allowing users like Apple, Google,[49] Facebook[50] until 2020 to comply. Apple was accused of receiving illegal state aid from Ireland, noting its effective corporate tax rate had dropped from 1% in 2003 to 0.005% in 2014.[51] This case will be examined in Chapter V of this thesis. The Single Malt strategy, similarly used by Microsoft (LinkedIn) and Allergan, was exposed in 2017.[52]

[49] Edward Helmore, 'Google says it will no longer use "Double Irish/Dutch sandwich" tax loophole', The Guardian (1 January 2020).
[50] Thomas Hubert, Intellectual property, liquidations and tax: The Facebook double Irish subsidiary that refuses to die, The Currency (23 May 2022).
[51] European Commission, 'State aid: Ireland gave illegal tax benefits to Apple worth up to €13 billion' (European Commission Press Release, 30 August 2016).
[52] Dominic Coyle, 'Multinationals turn from "Double Irish" to "Single Malt" to avoid tax in Ireland' The Irish Times (14 November 2017).

IV. OECD Transfer Pricing Guidelines and the Taxation of IP

4.1 Scope and role of OECD Transfer Pricing Guidelines (2022 edition)

In response to widespread base erosion and profit shifting, the OECD introduced the BEPS Actions to ensure that multinational enterprises are appropriately taxed. These measures aim to counter IP-based aggressive tax planning by implementing anti-avoidance rules. As part of this broader initiative, later on the OECD updated its guidance on transfer pricing to reflect the challenges posed by the expansion of intangible assets across jurisdictions and profit shifting strategies.

The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations were first implemented in 1995, with the intent to minimise conflicts between MNE and public administrations in transactions involving Transfer Pricing (TP) around the world. The revised Guidelines followed the OECD/G20 BEPS Project, particularly Actions 8–10, which addressed the transfer pricing of intangibles, risk, and high-risk transactions. These Actions were first fully incorporated into the 2017 edition of the Guidelines and remain integral to the current version. Rather than existing as standalone rules, BEPS 8–10 reshaped the application of the arm's length principle by introducing a stronger focus on economic substance and value creation, especially through the DEMPE framework for intangibles and the requirement that risk be effectively controlled and borne.

In parallel, other BEPS Actions, such as Action 2 on hybrid mismatches, Action 3 for Controlled Foreign Company, Action 5 on harmful tax practices, 6 on treaty abuse, 12 for mandatory disclosure rules, and Action 13 on transfer pricing documentation and country-by-country reporting, existing separately, complement the Guidelines by addressing related transparency and anti-abuse concerns within the broader international tax architecture.

This latest version of Guidelines provides the revised approach towards hard-to-value intangibles (HTVI) and considerations for financial transactions. HTVI will be examined deeper in part 3 of this chapter. Even though they are not legally binding instruments, the Guidelines have become the widely recognised international reference standard for governments and MNEs, especially in interpreting transfer pricing rules based on Article 9 of the Model Convention, as well as illustrating methods that can be used to determine the ALP of a transaction.

Diving into a brief overview of the Guidelines'structure, they are divided into ten chapters, each covering a focal part of Transfer Pricing. The first chapter lays the conceptual foundation of transfer pricing by explaining the arm's length principle. The second chapter delves into the topic of transfer pricing methods and utlines the five accepted methods for determining an arm's length

price: traditional transaction methods (Comparable Uncontrolled Price (CUP) Method, Resale Price Method,Cost Plus Method), and transactional profit methods (Transactional Net Margin Method (TNMM), Profit Split Method (PSM)). The Guidelines emphasize that no method is inherently preferable, but rather it must be chosen based on the specific transaction, the quality of available data, and how comparable the circumstances are. The chapter also offers guidance on selection criteria, practical challenges, and reliability of adjustments.

The third chapter provides detailed guidance on conducting a comparability analysis, which underpins all transfer pricing evaluations. It distinguishes between the search for comparables and the broader analysis, which includes understanding the economically relevant characteristics of the controlled transaction: the characteristics of property or services, functional analysis (functions, assets, and risks), contractual terms, economic circumstances, and business strategies.

In practice, the comparability analysis follows a nine-step process. The chapter stresses the importance of functional analysis and proper documentation to support the pricing method selected.

Chapter four deals with measures to avoid and resolve transfer pricing disputes, particularly mutual agreement procedures (MAP) and advance pricing arrangements (APA). It discusses both unilateral and bilateral/multilateral APAs, their legal frameworks, and practical benefits. The chapter encourages cooperation between taxpayers and tax administrations to mitigate double taxation and enhance certainty. The fifth chapter focuses on documentation reflecting the outcome of BEPS Action 13. It introduces the three-tiered documentation structure.

Most interestingly and importantly, the sixth chapter was substantially revised as part of BEPS Action 8. It defines intangibles for transfer pricing purposes, includes both legally protected intangibles (e.g., patents, trademarks, copyrights) and economically valuable intangibles (e.g., customer lists). Key topics also include the elaboration of the DEMPE framework, economic vs. legal ownership, valuation techniques, transfer of partially developed intangibles. Annex II provides detailed guidance with numerous examples on HTVI, focusing on information asymmetries and ex post outcome testing as a means to assess whether the initial pricing assumptions were reasonable.

Chapters seven to nine address specific issues related to intra-group transactions. Chapter VII focuses on intra-group services, Chapter VIII covers CCAs, Chapter IX examines the transfer pricing implications of business restructurings, and Chapter X deals with intra-group financial transactions, such as intercompany loans. It also provides guidance on whether the pricing of these transactions aligns with the principles outlined in Chapter 1, including how to determine risk-free and risk-adjusted rates of return.

Importantly, the OECD advises conducting a thorough functional analysis to fairly identify entities within an MNE that perform essential functions, provide or contribute key assets, and bear risks related to intangibles. This ensures profit allocation aligns with economic reality.

As it was mentioned in the introduction part, conceptually, intangibles can encompass both rights clearly defined by law, such as patents and trademarks, and broader categories. These broader categories, despite not being clearly legally defined, can carry economic value that independent parties would compensate for. This subtle nuance must be considered in any transfer pricing analysis involving the use or transfer of intangibles. In each situation particular facts and circumstances have to be examines. So, in addition to traditional intangibles like patents, trademarks, and know-how, there are other concepts that often arise in discussions of business value but are treated differently for transfer pricing purposes.

Firstly, as mentioned in part VI of the Guidelines, goodwill and ongoing concern value represent the value of a business beyond the sum of its identifiable assets. Goodwill can refer to various things: the reputation of the business, customer relationships, or the expectation of future trade. Ongoing concern value relates to the idea that a fully operating business may be worth more than just the sum of its parts. However, neither goodwill nor ongoing concern value is typically considered a separate intangible for transfer pricing purposes because they cannot be easily transferred or separated from the business as a whole.

Market-specific characteristics—such as high consumer demand in a wealthy country or low labor costs in a developing one—can influence the pricing of goods and services. These factors are not intangibles either, but they are important comparability factors that should be taken into account in transfer pricing analyses.[53]

4.2 Transfer pricing methods relevant for IP

Overall, there are five recognised methods that can be used to determine whether the conditions established in transactions between related parties are consistent with the arm's length principle. The methods are divided into two categories: the traditional transaction methods and the transactional profit methods. The first category consists of the CUP method, the RPM, and the CPM. The second category includes the TNMM and the TPSM.

As a general introduction to traditional and transactional profit methods, it can be stated that in order to test or establish the arm's length conditions relating to the tested transactions, the CUP

[53] OECD, Transfer Pricing Guidelines (n 1) ch VI, para 6.28–6.30.

method compares prices, the RPM compares gross margins, the CPM compares gross profit markups on costs, the TNMM compares net margins and, lastly, the TPSM compares the allocation of profits between the parties. All these methods are characterized in detail in Chapter II of the Transfer Pricing Guidelines, where this categorization is basically introduced.[54]

A further important distinction is that some of these methods are one-sided while others are two-sided. Quite logically, one-sided methods (i.e., RPM, CPM and TNMM) apply to one party to the tested transaction and test the results against those derived by unrelated parties engaged in comparable transactions. The "tested party" should be the party with a less complex functional profile. As a result, the other party will be entitled to any remaining actual profit from the transactions concerned.

Two-sided methods, in contrast, are effectively applied to both parties to the tested transaction. They determine either an arm's length price to be used by each party (i.e., CUP method) or an allocation of relevant profits from the transactions between the parties (i.e., TPSM).

In order to select the most appropriate method, the accurate delineation and recognition of the actual transaction are of vital importance. Within this analysis, several factors must be taken into account, among which the functional analysis is the most important. It seeks to understand the nature of the transaction by examining the functions performed, assets used, and risks assumed by each party involved. The functional analysis will also help in determining whether a change over time in the functional profile of the parties involved in the tested transactions requires a modification to the TP method applied or the selection of another; determining whether any adjustments are necessary in order to apply the TP method in a reliable manner. Provision 6.145 of the Guidelines[55] clearly state that the transfer pricing methods most likely to prove useful in matters involving transfers of one or more intangibles are the CUP method and the transactional profit split method TPSM.

The Comparable Uncontrolled Price (CUP) method is a traditional transaction method used in transfer pricing to assess whether the pricing in a transaction between related parties complies with the arm's length principle. Under this method, the price charged in a controlled transaction is compared with the price charged in a comparable uncontrolled transaction (i.e., a transaction between independent enterprises under similar circumstances). OECD Guidelines 2022 (Chapter II) confirm that the CUP method is the most direct and reliable method where a high degree of comparability exists.

[54] Michael Lang, Giammarco Cotani and Raffaele Petruzzi, Fundamentals of Transfer Pricing (Wolters Kluwer 2021) ch 1.
[55] OECD, Transfer Pricing Guidelines (n 1) ch VI, para 6.145.

The method can be applied using internal comparables (within the same group) or external comparables (third-party transactions). To apply the CUP method, it is important to identify a comparable uncontrolled transaction involving the same or similar goods/services under similar circumstances, compare the price charged in that transaction with the controlled transaction price, make adjustments for material differences (e.g., in volume, contractual terms, or market conditions), if possible and reliable.

The CUP method is particularly useful when there is a high degree of comparability between the controlled and uncontrolled transactions. There are internal comparables available (i.e., the same company sells similar goods/services to both related and unrelated parties). The products or services are standardized or commoditized, meaning they are not affected by unique intangibles (e.g., raw materials, publicly traded goods, generic software licenses). Any differences in the comparability factors (e.g., volumes, contractual terms, credit terms, geographic markets) can be reliably adjusted.[56]

For example, Company C, located in Germany, manufactures generic pharmaceutical products and sells them both to Company D, a related distributor in France; and to Independent Distributors in Italy and Spain under identical contractual terms. The products are identical, sold in similar volumes, and under similar market conditions. In this case, internal CUPs exist, and only minor adjustments may be needed (e.g., for transportation costs). The CUP method is highly reliable here and provides a strong basis for transfer pricing. Despite being conceptually straightforward, the CUP method can be difficult to apply in practice due to the strict comparability requirements. High comparability threshold means that minor differences in product characteristics, functions, or markets may lead to pricing discrepancies that are hard to adjust. Especially, this is the case for the use of unique or valuable intangibles: these often make transactions incomparable. There can be often lack of reliable comparables, especially for services or intangibles. The OECD Guidelines Chapter VI emphasize that the CUP method is often not appropriate for transactions involving unique and valuable intangibles due to the absence of comparable uncontrolled transactions. For instance, if a company licenses a proprietary software or a patented technology, it's difficult to find a comparable license agreement with an unrelated party that involves a similarly valuable intangible. Adjustments for differences in brand recognition, marketing strategy, or legal protections may be impossible to quantify reliably.

So, careful research gives understanding of some examples on where CUP Method might not be appropriate, especially if there are differences in the application and use of such intangibles or in case of fundamental differences of product characteristics. Company A manufactures

[56] Lang, Cotani and Petruzzi (n 54) ch 3.

refrigerators under two trademarks. “Freezer”, sold via unrelated distributors (low-end segment); “Freeze Premium”, sold through Company B, a related entity, in the high-end market. Though technically identical, the two product lines are marketed under different trademarks to reach distinct customer segments. The price difference reflects the marketing intangible and customer perception, which cannot be reliably adjusted for. Therefore, CUP is inappropriate, and a Transactional Net Margin Method (TNMM) or Transactional Profit Split Method (TPSM) may be more suitable.

The CUP method can be reliably applied where the product or service includes only routine or non-unique intangibles, or where the impact of intangibles on pricing is negligible or comparable. For example, mass-market trademarks (e.g., a local or generic detergent brand used in multiple markets), regional mineral water brand sold under a common label in several countries, generic software license (e.g., common business productivity software sold under standard terms).

The CUP method is not reliable when the transaction involves unique and valuable intangibles because there are no sufficiently comparable uncontrolled transactions, and any price difference cannot be reliably adjusted. Rolex watches sold under the Rolex trademark. Patented technology licensed within a group. Proprietary or custom enterprise software license. Trade secrets used in production (e.g., Coca-Cola formula). R&D service arrangements involving know-how. Use of global brands with strong marketing presence (e.g., Apple, Louis Vuitton). Rolex is a strong brand with high reputation and marketing intangibles that materially affect price, and there are no suitable comparables. The patent is unique; the pricing cannot be compared with unrelated party transactions due to the lack of comparables. The software is non-standardized and highly tailored, with no reliable comparables.

Similarly, CUP cannot apply to patents if the patents are unique, highly valuable, or industry-leading. The patents represent core business IP (e.g., a new cancer drug formula or iPhone Face ID algorithm). The comparability factors (duration, exclusivity, market, geographic scope) differ materially. No reliable third-party license transactions exist or they are not publicly available. For example, a biotechnology company licenses a groundbreaking genetic therapy patent to its affiliate. There are no unrelated-party transactions involving that patent or similar ones. CUP cannot apply — so it is better to use TPSM or TNMM instead. Even in the case of the licensing of similar patents, differences in the stage of development, geographic rights, duration, or degree of exclusivity may materially affect value.

Thus, the CUP method is generally most suitable when internal comparable transactions are available and there are no significant differences in product features or economic conditions that could materially impact pricing—or when such differences can be reliably adjusted for. In these

cases, all relevant information is typically accessible, allowing for a clear identification of any material differences between related-party and third-party transactions.

The Transactional Profit Split Method (TPSM) is particularly appropriate when both parties to a controlled transaction contribute unique and valuable intangibles, perform integrated activities, or share significant economically relevant risks. Differently from one-sided methods (like TNMM, RPM, or CPM), TPSM, it takes into account the financial results of both parties to the transaction, aiming to allocate profits (or losses) in a way that reflects the value each party contributes.[57]

Except for both parties contributing unique intangibles (e.g., proprietary technology, brand, or know-how), this method is applicable when the business operations are highly integrated, so it is hard to evaluate each entity in isolation. In such a case, the parties share or assume significant, economically interdependent risks, so it is either difficult or impossible to identify reliable comparables or to evaluate the contribution of just one side of the transaction. TPSM ensures that the residual profit is not arbitrarily assigned to one entity, but is instead split according to value creation.

For example, company A (Country X) provides software and know-how, and company B (Country Y) contributes unique hardware and a qualified workforce for manufacturing self-driving cars. Given that both parties provide unique and valuable assets, and the operations are highly integrated, the TPSM is appropriate. A contribution analysis would consider their respective roles in determining the profit split.

There are two main approaches to applying TPSM. This method can be implemented using several different analytical frameworks, depending on the nature of the contributions and available data: contribution and residual analysis. Under the contribution method, the total profits from the controlled transactions are split directly between the parties based on the relative value of their contributions. This may involve functional analysis, financial data review.

Residual analysis is a two-step method appropriate where part of the contributions can be reliably benchmarked (routine functions), and the residual profit is allocated based on the relative value of the parties' unique or non-benchmarkable contributions. For example, routine marketing and distribution functions may receive a benchmarked return, while residual profit from intangible assets developed jointly is split based on relative contributions. Moreover, TPSM is flexible. It can be used ex ante (for advance pricing agreements or internal planning) or ex post (to test if the actual profit split is arm’s length).

Lastly, company A and Company B (affiliates) engage in joint product development. Company A also works with an unrelated Company C, where profits are split 70/30. If the same ratio is

[57] Lang, Cotani and Petruzzi (n 54) ch 4.

applied between A and B under comparable conditions, the split is likely at arm's length and can be used under TPSM with external comparables.

In some cases—especially where contributions involve long-term investments, such as R&D efforts or infrastructure development—a profit split can be based on relative investment amounts rather than functions alone. This approach is suitable when the return is delayed or intangible-based, contributions are not immediately profitable but critical for long-term value, and investment amounts can be reliably measured and linked to value creation.

4.3 Hard To Value Intangibles

Hard to Value Intangibles (HTVI) can have significant impacts on transfer pricing for multinational enterprises (MNEs) operating across various tax jurisdictions. Their uncertain valuation and lack of reliable comparables at the time of transfer make it difficult for MNEs and tax professionals to apply standard arm's length pricing methods. This leads to an increased risk of audits, transfer pricing adjustments, and disputes across tax jurisdictions. As it was already mentioned, the Guidelines have introduced the Annex II for Chapter VI HTVI incorporating the OECD's report on Guidance for Tax Administrations on the Application of the Approach to Hard-to-Value Intangibles, developed under BEPS Action 8. According to the TP Guidelines section 6.189,[58]an intangible is considered HTVI if:

a) no reliable comparables are available at the time of the transaction, and
b) there is substantial uncertainty about the projections of future cash flows or valuation assumptions.

Common characteristics of HTVIs include the following:

- the intangible is only partially developed at the time of the transfer;
- it is not expected to be commercially exploited for several years;
- it is part of a larger development/enhancement project;
- there is no track record of similar intangibles;
- the transaction is structured as a lump-sum payment.the intangible is transferred under a Cost Contribution Arrangement (CCA) or similar framework. Even if development costs are split under a CCA, the final value of the intangible may still be uncertain, justifying HTVI classification.

For instance, Company A, based in Country X, and Company B, located in Country Y, are both members of the ABC Group. Company A manufactures electric engines for the automotive sector

[58] OECD, Transfer Pricing Guidelines (n 1) ch VI para 6.189 and Annex II to Chapter VI.

and has developed proprietary know-how related to this process. It plans to transfer this know-how to Company B. Although the current economic benefits of the intangible are limited due to the early stage of the industry, its value is expected to rise as electric engines increasingly replace traditional technologies.

Tax authorities often lack access to critical business information, and it creates information asymmetry. This imbalance can hinder their ability to challenge a taxpayer's valuation, especially when discrepancies arise between forecasted and actual results.

The OECD recommends income-based valuation techniques, such as the discounted cash flow (DCF) method, as the preferred approach for valuing HTVIs. Tax authorities may refer to ex post outcomes (i.e., actual results after the transfer) to assess the reliability of ex ante (pre-transfer) pricing. Section 6.190–6.193 of the OECD Guidelines provides that tax authority may not seek an adjustment if no reliable comparables or cash flow projections were available at the time of transfer, the intangible meets the criteria like partial development, novel exploitation. Also, if the ex ante valuation is over five years old**,** the difference between ex ante and ex post values is less than 20%**,** the taxpayer provides robust evidence that the discrepancy was due to unforeseeable circumstances and developments.

In order to better illustrate how this works in practice, one of the recent cases should be mentioned, namely, *Sweden vs Twilio Sweden AB*.[59] The Twilio case highlights how complicated valuation of hard-to-value intangibles in transfer pricing can be. Identifying the real transaction and considering all relevant intangibles is a key challenge.

Talking more about the facts of the case, Twilio Sweden AB, a Swedish subsidiary of the US-based Twilio Group, had developed valuable intangible assets—particularly proprietary software, technology platforms, and customer-related intangibles—prior to being acquired by the Twilio Group in 2016. After the acquisition, a license agreement was signed between Twilio Sweden AB and the US parent entity. Under this agreement, Twilio licensed its IP, including proprietary software and technology. The economic and strategic control of these intangibles effectively shifted to the US entity. Twilio Sweden was compensated with a limited, low-risk return, despite the IP continuing to be legally owned by it. The Swedish Tax Agency (STA) argued that the actual control, decision-making, and risk-taking associated with the intangibles were no longer performed by Twilio Sweden. Under OECD BEPS DEMPE framework (Development, Enhancement, Maintenance, Protection, Exploitation), the US entity carried out the key DEMPE functions. Therefore, the Swedish subsidiary should not retain the full residual profits from the intangible assets. The STA proposed a recharacterization of Twilio Sweden's role to that of a

[59] Sweden v Twilio Sweden AB (Administrative Court of Appeal, Case No 17-22, KRNG 22 February 2024).

contract R&D or service provider, rather than the economic owner of the IP. The Administrative Court and the Court of Appeal both upheld the Tax Agency's position. The court found that the license arrangement was not at arm's length. Twilio Sweden no longer bore the risks or made strategic decisions related to the IP. The residual profits derived from the intangibles should be attributed to the US parent company. Thus, the court reallocated the profits and increased the taxable income of Twilio Sweden AB to reflect an arm's length outcome, consistent with the OECD Transfer Pricing Guidelines. Comparable Uncontrolled Price (CUP) was used in this case with adjustments, though the court found they did not enhance comparability. More importantly, the Court stated that there was a discrepancy between formal agreements and economic reality. This difference in interpretation has significant implications for the valuation of the intangibles involved, meaning that not all transferred intangibles were explicitly listed in the agreement between the parties of this case. Implicitly transferred assets—like trade secrets and customer databases—were disputed.

Finally, it is useful to summarize, which challenges MNEs and tax professionals might encounter while dealing with HTVIs. Tax authorities may question transfer pricing arrangements if post-transfer profits are much higher than forecasted. This can lead to taxation being adjusted retroactively, as well as to penalties and increased liabilities. Secondly, MNEs face high compliance responsibilities, preparing detailed valuation reports and assumptions, conducting regular reviews of pricing strategies, attempting to find comparables for HTVIs. Due to increased scrutiny, MNEs must carefully monitor the location and ownership of intangible assets, the structure and timing of transfers, potential exposure to double taxation and cross-border disputes, because different jurisdictions may valuate HTVI distinctly. This can lead to double taxation risks.

4.4 The DEMPE functions

The DEMPE framework—standing for Development, Enhancement, Maintenance, Protection, and Exploitation—was introduced by the OECD as part of the BEPS (Base Erosion and Profit Shifting) initiative, specifically in the guidance on intangibles within Actions 8–10.[60] It represents a significant shift in how multinational enterprises (MNEs) are required to analyze and allocate profits derived from intangible assets.

Prior to the implementation of BEPS, transfer pricing analyses primarily relied on legal ownership and contractual arrangements to allocate profits among related entities. This formalistic approach, however, often failed to reflect the real economic substance of transactions and allowed

[60] OECD, Transfer Pricing Guidelines (n 1) ch VI, para 6.34–6.59.

MNEs to shift profits to low-tax jurisdictions simply by structuring contracts in a favorable way, even when little or no real economic activity occurred there. The DEMPE framework requires a detailed functional analysis that considers which entities within an MNE perform key functions, use relevant assets, and assume the associated risks with respect to intangible assets. In this way, the emphasis shifts from mere legal ownership to economic substance.

Each element of DEMPE has a specific meaning. Development means creating intangible assets, such as developing a new software platform, designing a medical device, or conducting pharmaceutical R&D. Enhancement relates to improving the performance, usability, or value of an existing intangible—for example, upgrading a search engine algorithm, enhancing an existing product formula, or adding features to a mobile app. Maintenance are activities that preserve the utility or legal integrity of intangibles—like managing a trademark portfolio, conducting software bug fixes, or regularly refreshing customer databases. Protection, obviously, means safeguarding the legal rights tied to the intangible, including registering trademarks, defending patents, managing IP litigation, or enforcing licensing agreements. Finally, **e**xploitation is actively using the intangible to generate income, such as licensing a patented technology to affiliates, using brand reputation in global marketing, or selling products that incorporate IP like smartphones with proprietary software.

By applying the DEMPE framework, tax authorities and MNEs can determine how to allocate profits based on real economic contributions rather than on ownership titles alone. Importantly, entities that contribute substantially to any DEMPE function—regardless of whether they legally own the intangible asset—should be compensated in line with their value-creating role. This ensures that the profits from intangibles are aligned with where genuine business activity takes place. To ensure that returns from intangibles are allocated in line with value creation, the OECD provides a six-step process.

Firstly, it is important to clearly determine which intangibles are involved in the transaction and what economically significant risks are associated with their development, enhancement, maintenance, protection, and exploitation. Secondly, analyse legal ownership and contracts. Then, review who holds the legal title (e.g., via registrations or licenses) and what the contracts say about ownership, risk assumption, and functional responsibilities. Next, examine which entities perform the important functions, use assets, and manage risks related to the DEMPE of intangibles. Outsourced activities are relevant only if the principal entity controls and assumes the associated risks. Also, validate that the actual behaviour of the parties matches what the contracts state, especially regarding risk assumption and control. An entity that assumes risk must also control the risk and have the financial capacity to bear it. Taking into account legal ownership, contractual rights, and actual conduct (functions, assets, risks) is also crucial, determining what the controlled

transaction truly consists of. Lastly, allocate returns based on each party's contribution to the DEMPE functions—only those that create or manage value are entitled to a share in the resulting income.[61]

It is important to know that a legal owner of an intangible (e.g. patent holder) that does not perform or control DEMPE functions will not be entitled to more than routine compensation (e.g. cost reimbursement or interest-like return). Conversely, a group member that contributes significantly to DEMPE may be entitled to a greater share of the returns, even if it is not the legal owner. Also, anticipated returns (ex ante) should be determined when the transaction is entered into. However, actual outcomes (ex post) may differ, but compensation must reflect arm's length risk assumptions based on the accurately delineated transaction.

Overall, the DEMPE model reflects a broader principle of the BEPS project: to combat artificial profit shifting by requiring alignment between value creation and profit allocation. It recognizes that value is often created by functions and risks spread across multiple jurisdictions, not merely where legal ownership resides.

[61] Dziwinski (n 8) ch 2, 75–115.

V. EU Legal and Regulatory Framework

5.1 Anti-Tax Avoidance Directives (ATAD I & II)

The Council of the EU adopted the Anti-Tax Avoidance Directive (ATAD I) on July 12, 2016, aiming to coordinate the implementation of anti-BEPS rules across Member States. Unlike the OECD's BEPS project, ATAD is a binding EU-level initiative. On May 29, 2017, ATAD II was adopted to expand the scope of hybrid mismatch rules to include non-EU jurisdictions. It introduced measures addressing hybrid permanent establishments, hybrid transfers, hybrid financial instrument mismatches, reverse hybrid and imported mismatches.[62] The ATAD establishes five core rules: Interest Limitation Rule (Article 4), Exit Taxation (Article 5), General Anti-Avoidance Rule GAAR (Article 6), Controlled Foreign Company (CFC) Rule (Articles 7 & 8), Hybrid Mismatches (Article 9). All of them will be briefly analyzed further on.

Under article 4 of ATAD II,[63] Interest Limitation Rule is a rule that limits how much interest a company can deduct from its taxable profits — in order to stop aggressive tax planning using debt (like shifting profits via intra-group loans). A company can only deduct interest up to 30% of its EBITDA (Earnings Before Interest, Tax, Depreciation, and Amortization). This is calculated before taxes and interest — so it reflects how profitable the business is. Only the "exceeding borrowing costs" are limited. That means interest expenses that are more than the interest income.

For example, a company has EBITDA €1,000,000, interest income = €100,000, interest expenses = €400,000. Exceeding borrowing costs = €400,000 – €100,000 = €300,000. 30% of EBITDA = €300,000. So the company can deduct €300,000, and the remaining €100,000 is not deductible now, but may be carried forward (if allowed by the country). De minimis rule however exists: every company can deduct up to €3 million of exceeding interest costs fully, even if that is more than 30% of EBITDA. Also, some interest expenses are excluded from this rule: standalone entities — companies with no group or related companies may be exempt, EU Public Infrastructure Loans—loans for long-term infrastructure projects in the EU can be excluded, banks and insurance companies can be excluded due to the special nature of their business.

Next, Exit Taxation (Article 5 of ATAD) applies when a company moves assets or its tax residency to another country, and as a result, the original country loses the right to tax those assets. In that case, the original country charges an "exit tax" — a tax on the unrealized gains (i.e. profits that haven't yet been made but would be if the asset were sold). It applies when a company moves

[62] KPMG International, EU Anti-Tax Avoidance Directive – Member State Implementation Overview (August 2022).
[63] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries [2017] OJ L144/1.

an asset (like IP, equipment, shares) from its head office to a permanent establishment (PE) in another country, or vice versa — from a PE to the head office, or between two PEs in different countries, or when a company moves its tax residence to another country. It only applies when the original country loses the right to tax the asset after the move.

For example, a company in Germany moves IP to its branch (PE) in Ireland. Germany will lose the right to tax future gains from that IP. So, Germany applies exit tax on the market value minus the book value of the IP (i.e., unrealized capital gain). This ensures Germany still collects tax as if the asset had been sold. The country receiving the asset must treat it as having the market value when it arrives (not just the original book value). This avoids double taxation (once on unrealized gain, and again on actual gain later). If the asset comes back within 12 months, no exit tax is applied. This only works if the transfer is temporary, and it is for specific purposes like providing collateral, meeting regulatory capital requirements, managing liquidity, etc.

General Anti-Abuse Rule (GAAR) under article 6 allows tax authorities to ignore fake or artificial setups that companies create mainly to avoid paying taxes. If a company creates an arrangement mainly to gain a tax benefit, and it is not a genuine business arrangement, then the tax authority can disregard it when calculating corporate tax. Not genuine arrangement means the arrangement is not based on real economic or commercial activity, it only exists on paper to lower taxes, e.g. moving profits to a tax haven, or creating shell companies, then issuing fake loans, or transferring ownership artificially. Let us say a company sets up a small subsidiary in a low-tax country, moves all its profits there by charging fake “royalties” to itself, the subsidiary has no real activity — just a mailbox. The tax authority can apply GAAR to ignore this arrangement, and tax the profits in the real country where the business happens.

A Controlled Foreign Company (CFC) under articles 7 and 8 is a foreign subsidiary or PE where an EU parent company (or its related companies) owns more than 50% of the voting rights, capital, or profits, and the CFC pays less tax than it would have paid in the parent company’s country — i.e., its actual tax is too low compared to what the parent country’s tax rules would say. If a company is treated as a CFC, then the parent company in the EU is taxed on the CFC’s income (even if that income hasn not been distributed). There are two ways countries can apply this tax: with the Model A or Model B.

Model A – categorical approach (passive income focus), which means that the CFC charge applies to undistributed income derived from certain passive income types, like interest, royalties and other intellectual property income, dividends and capital gains on shares, financial leasing, insurance, banking, and other financial activities. If the CFC has real substance (i.e., real economic activity, employees, assets), Model A does not apply. A country may choose not to apply CFC rules if one-third or less of the income is passive income.

Model B uses a transactional approach, which means the CFC charge only applies if the income arises from arrangements that are not genuine and are mainly designed to get tax benefits. An arrangement is considered not genuine if the CFC does not really own the assets or risks generating the income, and key people managing those assets or risks are elsewhere (e.g., in the parent company's country). Small companies can be excluded if their accounting profits are less than €750,000 and non-trading income is under €75,000, or accounting profits less than 10% of operating costs.[64]

For example, a German parent owns 100% of a subsidiary in Country X. The subsidiary pays only 5% corporate tax (much lower than Germany's 30%). The subsidiary earns €1 million in royalties from intellectual property but does not have real operations (just a mailbox). Under Model A, Germany could tax the German parent on those royalties as if they had been earned in Germany. Under Model B, Germany would tax the income only if it finds that the subsidiary's arrangement is non-genuine (no real substance or functions).

Lastly, hybrid mismatches under article 9 happen when two related companies in different countries treat the same thing differently for tax purposes, causing no tax paid anywhere (non-taxation), or the same expense deducted twice (double deduction), as was already mentioned in the previous chapter of the Master's thesis. These mismatches often happen because tax laws in different countries do not line up perfectly. This rule works two ways.

Firstly, if double deduction happens (same cost deducted twice), the investor country (where the parent company is) denies the deduction first (primary rule), or, if that is not done, the payer country (where the expense is incurred) denies the deduction (secondary rule).

Secondly, if deduction without inclusion happens (expense deducted but no income taxed anywhere), the payer country denies the deduction first, or, if that is not done, the payee country includes the payment as taxable income. One of the most common types of hybrid mismatches are, for example, financial instrument mismatch (different countries treat a financial instrument differently — e.g., one calls it debt (with interest deductible), another calls it equity. Also, hybrid entity mismatch (an entity is seen as a company in one country and taxed separately, but as part of the owners, no separate tax, in another), branch mismatch (a permanent establishment (PE) is treated differently in the PE country vs. the home country, causing mismatches).

[64] KPMG International, EU Anti-Tax Avoidance Directive – Member State Implementation Overview (August 2022).

5.2 DAC6 and Mandatory Disclosure Rules

A major concern underpinning DAC6 is the lack of transparency and absence of disclosure obligations in aggressive cross-border tax planning. Jurisdictions without mandatory disclosure rules may offer a competitive edge, motivating the EU to adopt a harmonised approach. This effort builds on the recognition that many tax planning schemes are designed by intermediaries, as highlighted by leaks such as the Lux Leaks, Malta Files, and the Panama Papers.[65] While many intermediary services are legitimate, these cases exposed the use of complex structures for tax avoidance or evasion. DAC6 thus aims to provide tax authorities with early access to information on potentially aggressive arrangements, enabling timely enforcement and countermeasures.

DAC6 was adopted by the EU on 25 June 2018, entered into force on the same date, and was required to be transposed into national law by 31 December 2019. Reporting obligations have applied since 1 July 2020, with retroactive effect for arrangements implemented from 25 June 2018 onwards. Its overarching objective is to promote transparency and discourage aggressive tax planning within the internal market. To this end, DAC6 introduced a mandatory disclosure regime for cross-border arrangements, placing reporting obligations on intermediaries (such as tax consultants, lawyers, and financial institutions), or taxpayers when intermediaries are either exempt or not involved. German data shows that as of 31 March 2023, the Bundeszentralamt für Steuern (BZSt) received 26,921 DAC6 disclosures, around 76.5% by intermediaries.[66]

The Directive relies on a set of 19 "hallmarks"—defined characteristics that render an arrangement reportable. These hallmarks are listed in Annex IV of the Directive, grouped into five categories (A to E), with some requiring satisfaction of the main benefit test (MBT)—i.e., that one of the main benefits of the arrangement is a tax advantage—while others are automatically reportable, irrespective of intent. Jumping into the hallmarks relevant to IP and HTVIs, Hallmark E.2 directly refers to transfer of hard-to-value intangibles. It covers arrangements involving the cross-border transfer of HTVIs between associated enterprises. The hallmark is automatically reportable, with no requirement to meet the MBT. It reflects OECD Transfer Pricing Guidelines and BEPS Action 8–10 concerns and captures intangible transfers where no reliable comparables exist for valuation, and future projections or valuation assumptions are highly uncertain. This applies particularly to intangibles in early development phases, such as software prototypes, pharmaceutical patents, or algorithms that have not yet reached commercialisation. For example,

[65] Bart Peeters and Lars Vanneste, 'DAC 6: An Additional Common EU Reporting Standard?' (2020) 12(3) World Tax Journal.
[66] European Commission, ‘DAC6’, Taxation and Customs Union – Directive on Administrative Cooperation.

when a group transfers a biotech patent—whose future profitability is still speculative—to an entity in a low-tax jurisdiction, the arrangement falls within the scope of Hallmark E.2.[67]

The legal definition under DAC6 closely mirrors Chapter VI of the OECD Transfer Pricing Guidelines. Thus, internally developed intangibles that are not capitalised (and hence not visible on the balance sheet), as well as goodwill or going concern value, may still qualify. As both taxpayers and tax administrations face challenges in valuing HTVIs reliably, all such transfers are reportable, even when they are not tax-motivated.

A guidance example involves a non-EU group transferring IP and associated DEMPE functions to a Dutch affiliate. Despite the inclusion or absence of a price adjustment clause, the arrangement is deemed reportable solely on the basis of the HTVI transfer. Importantly, the guidance clarifies that transferring DEMPE functions alone may suffice to trigger a reportable arrangement. This raises the question of whether relocating key personnel involved in IP (e.g., a senior R&D officer) would also fall under Hallmark E.2—a question left open, but implied to be affirmative under a substance-over-form approach. Basically, the group E hallmarks are devoted to transfer pricing matters.

Hallmark E.2 applies even if HTVIs are part of a broader asset transaction, such as a corporate merger, asset deal, or liquidation, where the intangible constitutes a minor component (e.g., minor patents, employee inventions). In all such cases, reporting remains mandatory.

Hallmark E.3 targets intra-group transfers of functions, risks, or assets—including IP—that cause a decline in projected EBIT (Earnings Before Interest and Tax) of the transferor by more than 50% over three years post-transfer. This hallmark is automatically reportable, regardless of tax motives. The guidance clarifies key implementation points. In case of universal succession (e.g., merger, liquidation), the EBIT of the legal successor is not the relevant basis. The hallmark also applies to already liquidated entities or those with negative EBIT. Larger HTVI transfers are often captured under both E.2 and E.3, especially if their transfer causes significant EBIT impact. As EBIT reduction often accompanies major reorganisations, careful contemporaneous documentation is essential even where the arrangement is assessed as non-reportable, due to the high audit risk and complex interpretation of the hallmark.

Also, Hallmark C.1 covers deductible cross-border payments, such as royalties, made to entities in non-cooperative jurisdictions, stateless entities, or preferential regimes, such as patent boxes. This hallmark is reportable even without a tax motive, and particularly relevant when MNEs redirect royalty streams to tax-favoured locations in IP restructurings.

[67] Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements [2018] OJ L139/1 (DAC 6).

Hallmark B.2 applies to the conversion of income into forms taxed more favourably. In an IP context, this includes, for example, reclassifying an out-of-court settlement into a licence payment or royalty. Even informal changes aimed at exploiting favourable tax rates may trigger disclosure obligations.

The reportable tax arrangements must be reported within 30 days to the competent national authority. The reporting period begins either: on the day on which the arrangement is made available for implementation, or as soon as the arrangement can be implemented, or when the first step towards implementation is taken. The decisive factor is which of the above events occurs first. The EU has also developed a joint communication network (Common Communication Network, CCN) via which the mandatory automatic exchange of information in relation to reportable cross-border arrangements takes place.

Interestingly, the Directive refers variously to "associated enterprises" (E.2) and "intra-group transfers" (E.3), without consistent definitions. While the Commission has clarified that these terms are to be interpreted consistently (based on Article 3(24) DAC), differences in Member State transpositions may lead to uncertainty, especially regarding branch-to-branch transfers (e.g., head office to permanent establishment), which may not qualify under E.2 or E.3 in some jurisdictions.

More and more cases emerge related to the application of the Directive, yet specifically about HTVIs are expected to be. In its landmark ruling Orde van Vlaamse Balies and Others v Vlaamse Regering Case C-694/20, 8 Dec 2022,[68] the CJEU held that lawyers subject to legal professional privilege (LPP) are exempt from reporting cross-border tax arrangements under DAC6 if doing so would breach their confidentiality obligations. Requiring such lawyers to notify other intermediaries of their reporting obligations, as DAC6 previously mandated, violates the clients' right to confidentiality under Article 7 of the EU Charter for Fundamental Rights—as it reveals the very existence of legal advice. Instead, Member States must ensure lawyers can invoke LPP without any notification duty, or else pivot the reporting obligation onto the taxpayer or other intermediaries.

[68] Orde van Vlaamse Balies and Others v Vlaamse Regering Case C-694/20, EU:C:2022:963, Judgment of 8 December 2022.

5.3 State aid and IP tax rulings

The notion of state aid is defined in article 107(1) of the TFEU: "Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the internal market."[69] So, a measure must cumulatively meet four conditions: be granted by the State or through State resources, confer an advantage, be selective, affect trade between Member States and distort (or threaten to distort) competition. A measure confers an advantage if it relieves an undertaking, directly or indirectly, of charges that are normally borne from its budget, thereby improving its financial position. In tax matters, this means a reduced taxable base or preferential tax rate, favourable interpretation of tax law by tax authorities through a tax ruling, a derogation from the normal tax system that reduces the undertaking's tax burden. Secondly, selectivity refers to whether the measure favours certain undertakings or categories of undertakings, as opposed to being generally applicable. In tax cases, the three-step test developed by the CJEU is applied to assess selectivity. Firstly, it is necessary to identify the reference framework (the "normal" tax system) – what is the general rule in the national tax system? Secondly, determine if the measure derogates from that framework – does it treat certain undertakings more favourably than others in comparable legal and factual situations? Thirdly, assess whether the derogation is justified by the nature or logic of the tax system – is the differentiation necessary and inherent to achieving the objective of the tax system? If the measure benefits only certain undertakings and the differentiation cannot be justified, it is selective. [70]

To illustrate the notion of selectivity and state aid in general, it is necessary to dive into the Apple case as one of the prominent cases in this sphere. The CJEU found that Apple's Irish tax rulings allowed for a non-market-based allocation of profits, which selectively favoured Apple subsidiaries compared to other companies under Irish tax law.

The Apple case, European Commission v. Ireland (C-465/20 P), has reignited the debate over how EU state aid rules interact with national tax systems, especially in the context of advance pricing agreements (APAs) and transfer pricing. The judgment of the Court of Justice of the EU, which sided with the European Commission and overturned the 2020 General Court ruling, confirms that member states do have broad autonomy over their tax systems—but only within

[69] Case C-465/20 P Commission v Ireland and Apple Sales International ECLI:EU:C:2024:724.
[70] Guglielmo Maisto, Taxation of Intellectual Property under Domestic Law, EU Law and Tax Treaties (2020) ch 3, 44–49.

limits. This decision, however, raises concerns because it appears to contradict the Court's own recent jurisprudence.

The Commission's 2016 decision had concluded that Ireland granted unlawful state aid to Apple through two APAs issued in 1991 and 2007, allowing its subsidiaries Apple Sales International (ASI) and Apple Operations Europe (AOE) to pay significantly less tax. The Commission claimed this was because Ireland failed to properly apply the arm's-length principle, which is a central concept in transfer pricing, and because it did not allocate Apple's IP income to its Irish branches. The General Court had annulled the Commission's decision in 2020, partly because it found the Commission relied too heavily on OECD guidance rather than on Irish law, which at the time did not explicitly incorporate the arm's-length principle or the OECD's Authorised OECD Approach (AOA). But the CJEU's new judgment reversed that outcome, effectively accepting the Commission's approach and reinstating the original decision. As a result, Ireland must recover EUR 13 billion in unpaid taxes from Apple.

To clarify a little bit more, the Apple Group is structured as follows: the US-based Apple Inc. is the parent company. It wholly owns Apple Operations International (AOI), which, in turn, possesses Apple Operations Europe (AOE), and AOE is the owner of Apple Sales International (ASI). Although both AOE and ASI are incorporated in Ireland, crucially, they are not considered Irish tax residents (para 4 of the Judgement). This distinction allowed Apple to exploit gaps in the international tax framework.

A cost-sharing agreement existed between Apple Inc. and the Irish-incorporated subsidiaries (ASI and AOE). Under the CSA, the shared costs mainly concerned R&D for technology used in Apple's products. Apple Inc. retained legal ownership of the group's intellectual property. ASI and AOE received royalty-free licenses to use the IP for manufacturing and sales activities. As participants in the CSA, ASI and AOE bore financial risks, including the R&D expenses (para 6–7).

Both ASI and AOE had branches in Ireland, which were nonetheless responsible for real business activities: ASI's Irish branch handled procurement, sales, and distribution of Apple-branded products. AOE's Irish branch was responsible for manufacturing and assembling certain computer products in Ireland (para 9–11).

In the 1990s and 2000s, Ireland's tax authority issued rulings Advance Pricing Arrangements (APAs) to define how ASI's and AOE's profits would be calculated for tax purposes. For example, 2007 revised APA stated for ASI, taxable profit was a fixed percentage of operating costs, excluding intra-group charges. For AOE, profit meant operating costs plus a fixed percentage of turnover, where that percentage represented the IP return from the branch's technology (para 12–22).

In August 2016, the European Commission concluded that these tax rulings reduced the tax base of ASI and AOE artificially. They resulted in Apple paying much lower taxes in Ireland than other companies would have paid under normal Irish corporate tax rules. The rulings were selective because they applied only to Apple Group entities, not to other taxpayers. These rulings derogated from the reference system—that is, the ordinary Irish corporation tax rules—without valid justification. Thus, the Commission ruled that the rulings were incompatible State aid under Article 107(1) TFEU (para 23–32). More details on selectivity explained by the CJEU are depicted in para 294–309, 379 of the judgement.

The CJEU begins by emphasizing that even in tax matters that are not harmonised by EU law, Member States must comply with EU State aid rules. This means a Member State cannot adopt tax measures that amount to unlawful State aid and thus distort competition within the internal market (para 73).

Additionally, the Commission cannot impose foreign concepts or frameworks that do not exist under the national tax law. It must respect the fiscal autonomy of Member States, especially since direct taxation is largely a national competence. National tax law is the primary source. The reference system is defined exclusively by the applicable national law of the Member State in question. This means the Commission must take the national tax rules as they are to determine what the normal taxation regime is (para 78–83).

The Commission found that the Irish tax authorities granted Apple a selective advantage by reducing the profits taxable in Ireland for ASI and AOE. This occurred because profits generated from Apple's IP were not attributed to the Irish branches. Even if Ireland had some grounds for allocating profits elsewhere outside of Ireland, the tax rulings approach led to the outcomes that did not align with a market-based (arm's length) standard. Hence, the profit allocations to the Irish branches were artificially low, resulting in lower tax bases and effectively selective tax advantages (para 85).

The General Court stated that the Commission had applied an "exclusion" approach by allocating profits for tax purposes to the Irish branches based on the fact that the head offices of ASI and AOE had no employees or physical presence to ensure their control and management. This "exclusion" was also found inconsistent with the arm's length principle. The CJEU examined this and stated that the ALP was properly applied by the Commission based on Irish tax law.

The Commission used the ALP to check if the profits allocated to the Irish branches for their trading activity corresponded to profits those branches would have made under market conditions, accounting for how assets, functions, and risks are shared between branches and the rest of the company. Irish tax legislation stipulates that the profits attributed to a branch of a non-resident company should reflect the amount the branch would have generated on an arm's length basis, as

if it were a separate and independent entity performing comparable functions, using similar assets, and assuming similar risks.

For that purpose, the tax authorities should compare the functions performed, assets used, and risks assumed by the head offices and the Irish branches. The Commission concluded that the lack of active or critical functions and risks in the head offices combined with the central role of those functions and risks being performed by the branches justified allocating IP-related profits to the Irish branches (para 123–125).

Crucially, it was not merely the absence of employees or physical presence in the head offices that led to the Commission's conclusion but the combined factual findings about functions and risks. Irish tax law requires a functional analysis of the branch itself, identifying the activities, assets, and risks directly connected to the branch. It is important for the correct profit allocation, as it must accurately reflect how functions, assets, and risks are genuinely divided between the branch and the rest of the company not being the Irish resident (para 129).

The Court confirmed that the profits related to IP exploitation should have been allocated to the Irish branches based on their actual functions, assets, and risks, excluding any influence from Apple Inc. itself. This follows from the Apple Group's decision to transfer IP-related costs and risks to the Irish branches under a Cost-Sharing Agreement (para 284, 286).

Ireland, ASI, and AOE blamed the Commission for violating the principle of legal certainty by relying on a new and unforeseeable interpretation of Article 107(1) TFEU, which was not predictable at the time the tax rulings were granted in 1991 and 2007. Additionally, Ireland contended that the Commission failed to respect the principle of legitimate expectations, as it ordered the recovery of aid despite the considerable time that had passed. The principle of legal certainty requires that laws be clear, precise, and predictable so that affected parties can understand their legal position. However, legal certainty cannot be invoked if the Commission did not clearly breach its duty of diligence or manifestly fail in supervising State aid. Also, because supervision of State aid is mandatory under EU law, undertakings cannot legitimately expect that unnotified aid is lawful. Moreover, the Commission had not been aware and properly notified of those tax rulings. The contested tax rulings had not been notified to the Commission, which was unaware of their existence. Ultimately, the Court dismissed the appeal, upholding the General Court's judgment (para 322–366).

The Apple judgment stands in tension with previous case law, especially, for example, Fiat Chrysler Finance Europe v. Commission and Ireland.[71] In Fiat, the CJEU emphatically rejected the Commission's use of external benchmarks like the OECD guidelines unless those rules are

[71] Case C-885/19 P and C-898/19 P Fiat Chrysler Finance Europe v Commission and Ireland (Judgment of 8 November 2022, ECLI:EU:C:2022:859).

explicitly incorporated into national law. The Court stated that transfer pricing rules must be assessed under the national legal framework, not under an external, harmonized standard. Also, Commission v. Luxembourg[72] – the Amazon case. The Court again stressed that OECD standards are not binding unless incorporated into a member state's legal system. This supported the idea that selectivity assessments must respect national tax sovereignty.

Yet in Commission v. Ireland, the Court accepted the Commission's assumption that Irish law effectively included the arm's-length principle and AOA. Observers have found this outcome surprising and controversial, because the Court appeared to side-step its own previous holdings by not revisiting the General Court's procedural handling of these issues. However, the Fiat ruling still stands, and the CJEU in Apple did not address the clear contradiction between the two cases. This unresolved tension creates significant legal uncertainty for tax authorities and multinational enterprises. They are now left guessing how strictly OECD guidance will be treated as a benchmark in future state aid investigations and whether national tax discretion truly remains protected.

5.4 EU-level proposals affecting IP taxation: BEFIT, Digital Services Tax

Throughout the 20th century, a country could tax a company's profits only when the company had a sufficient physical presence there—such as a fixed place of business, because expanding a company's activities and sales in a country typically required a corresponding increase in physical footprint, such as offices, staff, or equipment. However, the rise of the digital economy has significantly challenged this model. Unlike traditional businesses, digital companies can deliver a broad range of services in foreign markets without being physically present—or with only a minimal presence—in the customer's country. These companies also tend to scale rapidly across borders without the need for extensive physical infrastructure, a phenomenon often referred to as "scale without mass."

Digital Services Taxes (DSTs) are tax measures imposed by countries to ensure that large digital businesses contribute to taxation in markets where they generate value, even without a physical presence. In March 2018, the European Commission put forward a proposal for a digital services tax (DST) as a temporary solution, acknowledging that a global agreement under the OECD's Inclusive Framework would take time to materialise.[73] The proposed DST would apply

[72] Case C-457/21 P Commission v Luxembourg and Amazon.com, Inc. (Judgment of 14 December 2023, ECLI:EU:C:2023:998).
[73] European Commission, Proposal for a Council Directive on the Common System of a Digital Services Tax on Revenues Resulting from the Provision of Certain Digital Services COM (2018) 148 final, 2018/073 (CNS).

a 3% tax on revenues generated from digital services where user participation plays a central role—specifically, online advertising, digital platforms facilitating user interactions (digital intermediation services like marketplaces), and the sale of user data. In contrast, digital services with limited user contribution, such as video streaming or online gaming, were excluded. As of 2025, 18 countries have implemented DSTs.[74]

For example, Austria levies a 5% DST on online advertising revenues generated from Austrian users. The digital tax is regulated in the Austrian Digital Tax Act 2020.[75] The tax applies to companies with global revenues exceeding €750 million and Austrian digital ad revenues of at least €25 million. The tax is geo-targeted—only advertising specifically directed at Austrian users (based on IP addresses, content, or format) is taxable. Companies without a permanent establishment in Austria must still register, submit annual returns, and keep detailed records, including advertising data and user location.

The rise of DSTs stems from a geographic mismatch between the users of digital platforms—often located in East and Southeast Asia—and the location of value creation, primarily in North America. In 2020, 40% of internet users were in East and Southeast Asia, while 40% of value creation in information industries came from North America.[76] This has raised questions about where profits should be taxed.

However, DSTs are controversial. They create risks of double taxation, distort trade, and often target U.S.-based digital giants, leading the United States to push for their repeal—either through multilateral agreements (e.g., OECD's Pillar One – Amount A) or retaliatory trade measures. The U.S. recently launched a 2025 review of DSTs under President Trump, highlighting their discriminatory impact, such as Austria's DST, which applies thresholds that capture mainly large American platforms.[77] Even if a multilateral treaty is adopted, not all DSTs may be repealed, and countries may continue to introduce or maintain them, undermining tax certainty and cooperation.

To address these issues, experts recommend shifting focus from DSTs to broadening existing consumption taxes (like VAT/GST) to include digital goods and services. This approach aligns taxation with where consumption occurs, avoids revenue-based distortions, and promotes neutrality between digital and traditional commerce.

Furthermore, on 12 September 2023, the European Commission proposed a new tax system called BEFIT (Business in Europe: Framework for Income Taxation). This system aims to make corporate taxation simpler and more consistent across the EU for large multinational groups. The

[74] Pieter Bayert, European Parliamentary Research Service, Balancing on Two Pillars: The Global Corporate Tax Reform (EPRS, June 2024) PE 762.346.
[75] Federal Ministry of Finance Austria, Digital Tax Act.
[76] Tax Foundation, 'Digital Taxation Around the World' (20 April 2021).
[77] Cristina Enache, Digital Services Taxes in Europe (Tax Foundation, 6 May 2025).

main goal is to reduce the differences between national tax rules, lower the administrative burden for companies, and prevent tax avoidance within the EU. At its core, BEFIT establishes the concept of a "BEFIT group" under Article 3, which is formed when two or more companies or permanent establishment, directly or indirectly controlled by a common ultimate parent entity, meet a 75% ownership or profit rights threshold. This structure ensures that the tax base is no longer calculated in isolation by each entity but rather aggregated at the level of the ultimate parent entity (Article 1). This aggregated tax base is then redistributed among the group's members through a formulary apportionment mechanism.[78]

Large groups that operate in the EU and have global revenues of €750 million or more will be obliged to follow the new BEFIT rules. This includes both EU-based and non-EU-based companies. Smaller groups can only choose to follow BEFIT if they prepare consolidated financial statements, thus, their participation is voluntary. Previous plans to unify tax rules (like the CCCTB) failed due to political disagreements.

Due to BEFIT functioning, profits will be calculated in the same way for all. Each group company will calculate its taxable profits starting from its financial statements and applying the same EU-wide rules (e.g., what income is taxable, what expenses are deductible, how assets are depreciated). All the profits and losses of the companies in the group will be added together into one single EU-wide tax base. In the beginning, the combined profits will be split among countries based on the average taxable profits of each company over the past 3 years.

Later on, a new sharing method based on a formula (like how many employees or how much sales each company has in a country) will be introduced. Each EU country can apply its own tax incentives or rules to its share of the profits.[79]

So, this initiative offers simpler transfer pricing rules for transactions between companies inside the BEFIT group, some transactions with related companies outside the group. This should reduce tax disputes and compliance work. However, the OECD Transfer Pricing Guidelines will still apply to companies outside the BEFIT group.

BEFIT will be administered by the parent company of the group filing a single BEFIT Information Return with its local tax authority. Each group company will also file a tax return for its own share of the profits, including any country-specific adjustments. BEFIT Teams, made up of tax officials from different EU countries, will check that the system is being applied correctly across borders. If all EU countries agree on the proposal, BEFIT would start applying in 2028.

[78] European Commission, Proposal for a Council Directive on Business in Europe: Framework for Income Taxation (BEFIT) COM(2023) 532 final.
[79] Stijn Blaakman and Jasper Korving, 'The Tax Base in BEFIT and Pillar Two: Harmony, Dissonance, or Off-Key?' (2024) 52 Intertax 361-386.

BEFIT also proposes a risk-based traffic light system under Articles 45 and 51 for managing transfer pricing compliance. If a BEFIT group member's intra-group transactions increase by less than 10% compared to the average of the previous three years, the transaction is presumed to comply with the arm's length principle—placing it in the "low-risk zone". Conversely, if the increase is 10% or more, the excess amount is presumed not to comply with the arm's length standard and may be excluded from the allocation calculation. This approach gives tax authorities a streamlined, data-driven tool to identify anomalies without the burdens of traditional case-by-case transfer pricing analysis.

One of the key drivers behind the BEFIT initiative is the recognition that current tax rules are ill-equipped to address modern digital business models, particularly those relying heavily on intangible assets. As a result, the existing framework often fails to guarantee fair and transparent taxation. By introducing a unified system, BEFIT aims to eliminate tax-driven distortions, thereby enhancing the overall competitiveness of the EU's single market.

5.5 OECD's Pillar One and Pillar Two: relevance to IP-heavy business models

Pillar One and Pillar Two were agreed upon in October 2021 with the support of over 140 countries, including all EU Member States. Although the agreement outlined the main principles, the following months were spent developing detailed rules and guidance to ensure both pillars could be properly implemented.[80]

Pillar One introduces a significant shift in international corporate taxation by reallocating taxing rights to market jurisdictions—that is, the countries where consumers are located—regardless of whether a MNE has a physical presence there. The goal is to make sure that the countries where customers are located get a fair share of the taxes, even if a company has no physical presence there. It applies to MNEs with global revenues over €20 billion, profit margins above10%.

The Amount A states that 25% of the profits above the 10% margin are reallocated to market jurisdictions where the MNE earns more than €1 million in annual revenue.[81] This shift applies even in the absence of a physical or tax presence in those countries. For example, if a company earns €100 billion with a 15% profit margin, 25% of the excess 5% (i.e., €1.25 billion) may be taxed in the countries where it makes sales. It ensures large MNEs, especially digital platforms and global consumer brands, pay taxes where users or customers are located, not just where the

[80] Pieter Baert, Balancing on Two Pillars: Global Corporate Tax Reform (European Parliamentary Research Service Briefing, European Parliament 2024) PE 762.346.

[81] Baert (n 74).

company is headquartered. The rules exclude extractive industries (e.g., mining, oil, gas) and regulated financial services.[82]

Pillar One was partially designed to replace unilateral DSTs imposed by countries like Spain, France, Italy, Austria, and the UK. These countries agreed to withdraw their DSTs once Pillar One takes effect. Until then, DST liabilities will be credited against future Pillar One obligations, as part of a temporary truce with the United States. This arrangement was set to last until 30 June 2024. Although the timeline and details of removing DSTs are still being negotiated.[83]

Because Pillar One reallocates taxing rights based on group-level profit, it requires modifications to existing bilateral tax treaties. The OECD has proposed a Multilateral Convention to facilitate this change. A signature ceremony was planned for mid-2024, with Pillar One expected to enter into force in 2025 in participating jurisdictions.

Pillar Two stands for a global minimum effective corporate tax rate of 15%. It aims to limit harmful tax competition between countries by ensuring that MNEs pay a minimum level of tax, regardless of where they operate. Pillar Two applies to multinational groups with: annual consolidated revenue above €750 million, and operations in more than one country. Pillar Two relies on two interlocking mechanisms to ensure the 15% minimum tax is effectively applied.

Firstly, the Income Inclusion Rule (IIR) – the primary rule which states that the ultimate parent entity (headquarters) must check whether each of its subsidiaries (constituent entities) is paying at least a 15% effective tax rate in the countries where they operate. If not, the parent's country applies a "top-up tax" to bring the group's overall effective tax rate in those jurisdictions up to 15%. A substance-based carve-out allows MNEs to deduct a portion of payroll and tangible assets from the top-up calculation, reducing the tax burden for activities with genuine economic substance. This ensures that real economic presence (like factories or employees) is not penalized, unlike intangible-based profits.

Secondly, if the IIR does not apply, other countries where the MNE operates can apply the Undertaxed Profits Rule (UTPR) to ensure the minimum tax is still paid. In such cases, top-up tax is distributed among those countries, based on a formula reflecting the MNE's employees and tangible assets in each jurisdiction. The UTPR helps prevent tax avoidance via corporate inversions, where companies move headquarters to low-tax countries.

The OECD also introduced the QDMTT, giving source countries the first right to collect the top-up tax. If a country adopts a QDMTT, it can retain the revenue locally, rather than allowing it

[82] Ilsu Erdem Ari, 'Does the OECD's Pillar One Solution Effectively Tax the Digital Economy? A Study of the Legal and Economic Incidence of Amount A' (2024) LSE Law Review.
[83] Pieter Baert, Balancing on Two Pillars: Global Corporate Tax Reform (European Parliamentary Research Service Briefing, European Parliament 2024) PE 762.346.

to flow to the parent or other jurisdictions via IIR or UTPR. This gives low-income and emerging economies a direct incentive to adopt the rules.[84]

Pillar Two was adopted by EU through Council Directive (EU) 2022/2523, which entered into force on 31 December 2023. The IIR is in effect in 2024. The UTPR will apply from 2025. Other countries implementing Pillar Two include Australia, Japan, the UK, Norway, and South Korea. The US has not directly implemented Pillar Two but already has similar provisions. However, political tensions exist, especially regarding the application of the UTPR to US companies.[85] Ironically, many of the initial revenue gains may arise in low-tax countries, as they will be pressured to apply the 15% rate themselves.

[84] Victoria J Perry, 'Pillar 2: Tax Competition in Low-Income Countries and Substance-Based Income Exclusion' (2023) Fiscal Studies. The journal of applied public economics, 44(S1), 23–36.
[85] Pieter Baert, Balancing on Two Pillars: Global Corporate Tax Reform (European Parliamentary Research Service Briefing, European Parliament 2024) PE 762.346.

VI. Conclusion

This Master's thesis has examined the taxation of IP in the context of transfer pricing, with a particular focus on the OECD, EU, and Austrian legislation. It has provided a structured analysis of how MNEs apply TP rules to IP transactions and how these rules interact with each other in practice. Notably, the thesis highlights that for TP purposes, "intangibles" can be interpreted broader than simply trademarks, designs, patents, and secrets.

This research confirms that the OECD Transfer Pricing Guidelines, including the DEMPE framework, remain a highly important reference point for MNEs and legal professionals globally. They offer a comprehensive system for allocating profits according to where economic value is created. Nevertheless, these rules encounter challenges in practice

al application, specifically due to uniqueness and easily relocatable nature of IP, combined with the fact that it is not easy to valuate them because of limited information availability.

The European Union's legal framework referred to in this thesis, notably ATAD, DAC6, and the State Aid rules, play an immense reinforcing role. ATAD targets BEPS through measures like

CFC rules and interest limitation. DAC6 emposes early disclosure obligation of potentially aggressive cross-border arrangements. Meanwhile, State Aid prohibits distortions in the internal market fighting with unequal and unjustified preferential tax treatment by scrutinizing favourable tax rulings of Member States. These EU instruments operate in both substantive and procedural alignment with OECD standards despite of their soft law nature.

Thus, the EU often transforms OECD principles into binding harmonized rules for its Member States. However, although EU Member States are required to implement EU tax directives and generally adhere to OECD recommendations, they obviously and naturally retain significant autonomy over their national tax systems, as analyzed earlier in relevant case law. As a result, legal and tax advisers might still identify gaps or mismatches that allow for the creation of new BEPS tools. Within the EU, countries like Ireland, Luxembourg, and the Netherlands, as well as non-EU jurisdictions, such as Bermuda and the Cayman Islands, continue staying attractive to MNEs due to favorable tax regimes. A similar trend can be observed in the digital economy, where the absence of a unified EU digital tax has led Member States to introduce individual national digital services taxes. This fragmented approach further increases the risk of legal uncertainty, double taxation, or regulatory arbitrage. At the national level, Austria aligns with EU and international standards. The Austrian Income Tax Act and Corporate Income Tax Act integrate OECD principles, yet retaining domestic classifications and thresholds. Austria's implementation of ATAD and DAC6 has improved compliance and transparency.

Academic hypotheses set up previously have been largely confirmed. The OECD and EU frameworks do provide a coherent legal basis but are not always effective. Enforcement gaps, valuation difficulties, and lack of harmonization at the global level remain major challenges. However, further research would still be needed into the taxation of non-traditional and data-driven intangibles, as the global economy continues shifting to digitalisation. The forthcoming implementation of Pillar One and Pillar Two under the OECD's Framework will redefine profit allocation and minimum taxation standards, raising important questions about their impact on IP taxation, especially for digital MNEs. Moreover, the future of IP taxation may involve a more detailed and unified valuation approaches for hard-to-value intangibles, possibly via international cooperation on valuation standards. Also, coordinated global frameworks to reduce treaty mismatches, especially in the classification of IP income as royalty, business income, or capital gain, are of high importance. And, no doubt, a more detailed further research is recommended for each specific intangible/IP right in the context of national law(s), as this master's thesis is only a general introduction and guide into the field. For example, software is gaining importance and popularity recent years and requires a deeper practical analysis.

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