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Transfer Pricing in case of Intangibles

info@sbcllc.ae

sbcllc.ae

What are Intangibles ?

Intangibles – Definition (as per OECD Guidelines)

- Not a physical asset (e.g., plant, machinery) or a financial asset (e.g., shares, loans).
- Capable of being owned or controlled by an entity.
- Used in the course of commercial or business activities.
- Has economic value arising from its use, transfer, or exploitation.
- The use or transfer would be compensated if it occurred between independent parties.
- Valuation is assessed based on comparable circumstances under the arm's length principle.

Common categories of intangibles include:

- Marketing intangibles
- Technology intangibles
- Data and algorithms
- Contractual or legal intangibles

Why are they Crucial in TP?

These assets are **hard to define, value, and locate**, given their non-physical nature. As a result, intangibles have become a central focus of tax authorities and transfer pricing disputes due to their potential for **profit shifting** across jurisdictions.

OECD Extracts

Paragraph 6.48 (Core DEMPE wording)

*"The arm's length principle and the principles of Chapters I–III require that all members of the group receive appropriate compensation for any functions they perform, assets they use, and risks they assume in connection with the **development, enhancement, maintenance, protection, and exploitation of intangibles**."*

Paragraph 6.32 (Objective of DEMPE analysis)

*"The determination of the entity or entities within an MNE group which are ultimately entitled to share in the returns derived by the group from exploiting intangibles must be based on an identification of the member or members of the MNE group which perform and exercise control over the **development, enhancement, maintenance, protection and exploitation of the intangibles**, and which assume the risks and bear the costs related to those functions.*

Key Focus Area

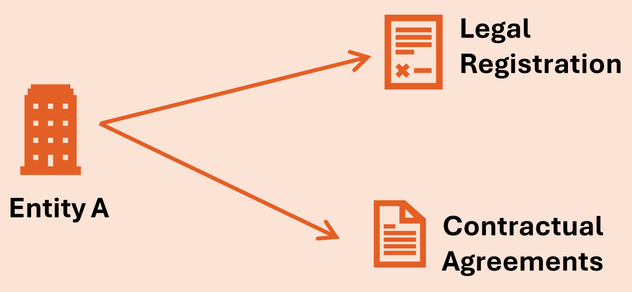
Intangibles are critical not only for their value but due to ownership, control, and risk complexities

- **Who owns** the intangible?
- Who **controls, performs** and **enhances** it?
- **Who assumes the risk** and **should be rewarded?**

1. Who owns Intangibles?

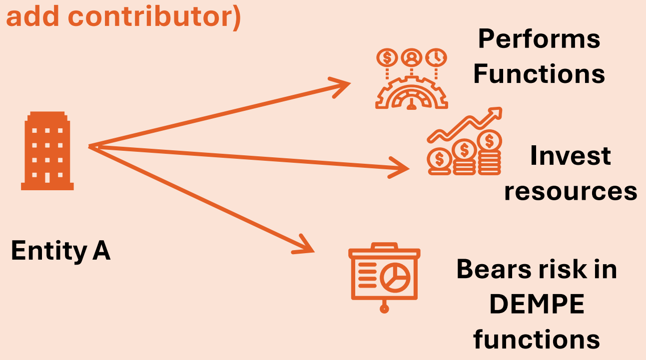
Ownership in TP is of two types: Legal (based on registration/contract) and Economic (based on functions, risks, assets)

Legal Ownership (Financial/on paper)



Legal ownership is determined through registration or contractual agreements and if no contract exists or differs from conduct, **actual control and decision-making** determine the legal owner.

Economic Ownership (Functional/ value add contributor)



Economic ownership refers to the person or entity that creates real value from an intangible — the one who performs key DEMPE functions, invests resources, and bears the related risks.

2. Who controls, performs and enhances the intangible ?

The entities that perform and control the DEMPE functions and related control activities for an intangible determine how value is generated and who is entitled to the resulting returns.

- **Development:** Designing and managing research programs reflects the Development function – driving & prioritizing new intangible creation
- **Enhancement:** Marketing and value initiatives reflect Enhancement, aimed at boosting existing intangibles' value and reach.
- **Maintenance:** Ongoing quality control reflects Maintenance, ensuring intangibles remain functional and retain their intended value.
- **Protection:** Decisions regarding patents and registrations illustrate Protection, safeguarding intangible property from infringement.
- **Exploitation:** Using intangibles to derive economic benefits (e.g., licensing or franchising) represents Exploitation, focusing on monetizing the asset

3. Who assumes risk and should be awarded?

- Risk control = reward entitlement
- Funding/asset-only entities earn routine returns
- Risk bearer decides, manages, and bears downside

- Residual profits go to entities controlling key risks
- Substance prevails over contracts
- Risk bearer must make key decisions and monitor risks

Stepwise Framework for Intangibles

Step 1	**Identify** the intangible used or transferred.
Step 2	Review the **contractual agreements** & establish legal ownership.
Step 3	Perform **DEMPE** functional analysis to identify economic owners.
Step 4	Verify **conduct vs contract** and financial capacity of risk-bearers.
Step 5	**Characterize** the actual controlled transactions
Step 6	Determine **Arm's Length Price** using suitable valuation or TP Method

Key FTA Emphasis Areas

- **Conduct over Contract:** Substance and control determine entitlement to returns.
- **Funding & Capacity:** Funders must prove financial ability and real risk assumption.
- **HTVI Focus:** Hard-to-value intangibles need reliable valuations and sensitivity testing.
- **Routine vs Non-Routine:** Funders earn routine returns; DEMPE performers receive residuals.
- **Options Realistically Available:** Document and test feasible alternatives for each party.

Overall Transfer Pricing framework for Intangibles

Section	Details
Key Transfer Pricing Considerations	- Identify which entities perform **DEMPE (Develops, Enhances, Maintains, Protects and Exploits)** functions and bear related risks. - Determine arm's length royalties or license fees for IP transfers or use. - Align legal ownership with economic substance and value creation. - Apply appropriate valuation methods (CUP, Profit Split, or DCF).
Documentation requirements	- Legal rights & registrations (patents, trademarks, licenses). - Maintain Master File and Local File if thresholds are met. - Ensure all intercompany agreements accurately reflect functions and control & DEMPE role mapping. - Valuation and comparability studies. - Funding agreements and proof of financial capacity
Potential Risks	- Tax adjustments or penalties for non-arm's length arrangements. - Double taxation due to mismatched profit allocation. - Increased audit focus from the UAE Federal Tax Authority (FTA) on intangible-heavy structures.

How Can SBC help?

Benchmarking Analysis: Comprehensive and periodic benchmarking studies are undertaken, supported by detailed financial analyses and appropriate economic adjustments, to ensure that all intercompany transactions consistently remain compliant with the Arm's Length Principle (ALP) and reflect market-aligned outcomes.

Documentation / Record Keeping Ongoing assistance is provided in the preparation, review, and maintenance of Transfer Pricing Policies, Intercompany Agreements, and robust supporting documentation, ensuring full alignment with UAE Transfer Pricing regulations and OECD Guidelines, as well as audit-ready record retention.

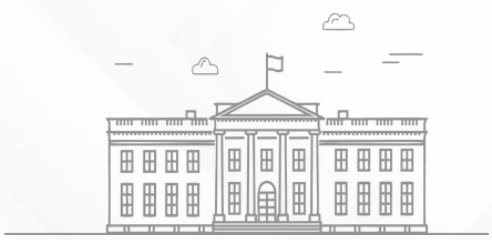
Monthly Handholding Support Regular and structured interaction is offered throughout the tax period, including continuous guidance and advisory support, to help entities proactively monitor transactions, address emerging TP issues, and maintain sustained compliance with ALP requirements.

Year-End TP Compliances End-to-end support is provided for year-end transfer pricing compliances, including the accurate preparation and timely filing of Disclosure Forms, Local Files, and Master Files, in strict accordance with applicable UAE TP regulations and deadlines.

SBC REGIONAL HEAD OFFICES

UAE
SBC LLC
202 & 309, Al Nasr Plaza Commercial Building, Oud Metha Metro Station Exit 1, Dubai, UAE

INDIA
SBC LLP
Suite 5, Level 3, Reliance Cyber Ville, Madhapur, Hitech City, Hyderabad – 500081



USA
SBC LLC
SBC LLC, 8 The Green, Suite A in the City of Dover, Delaware - 19901