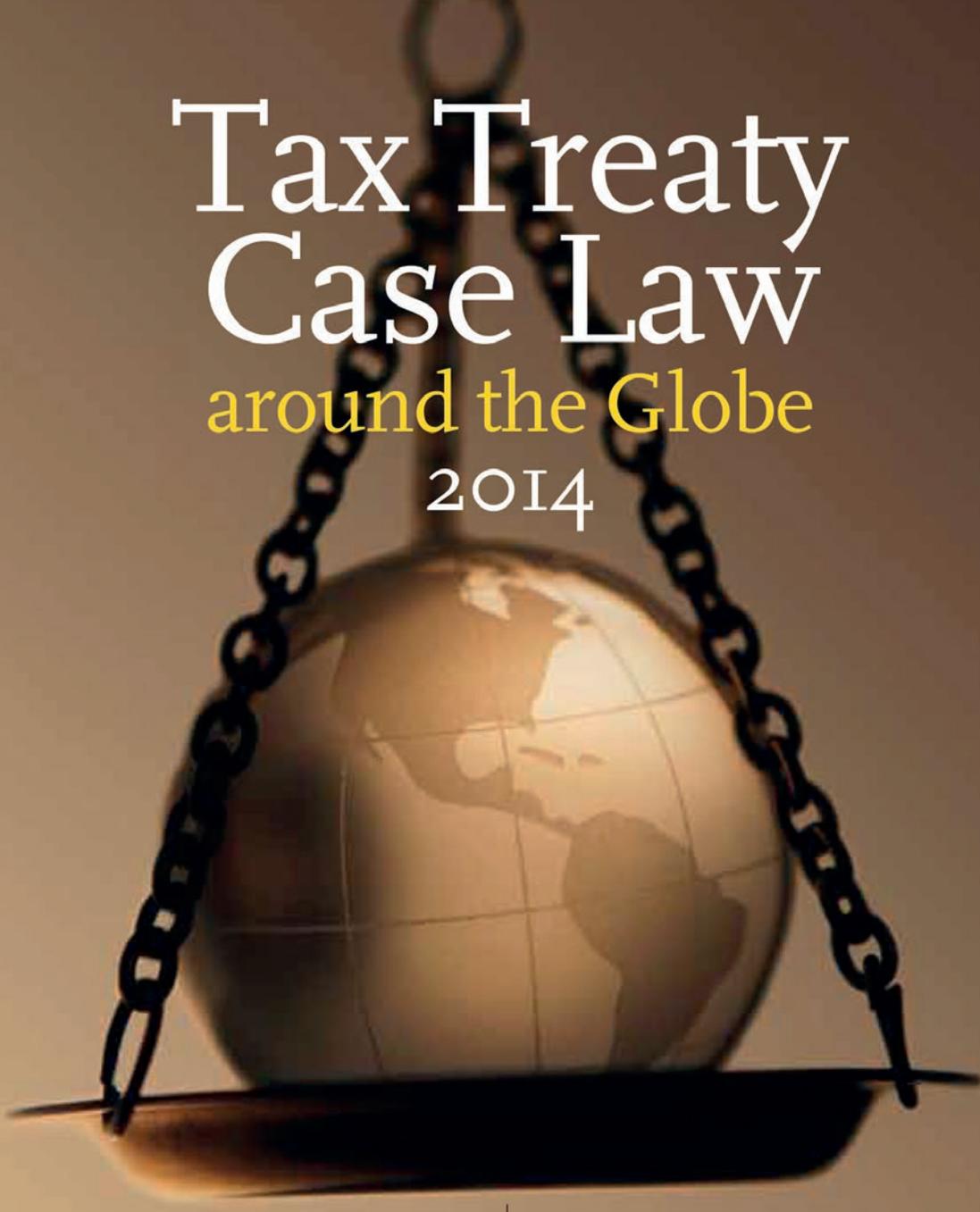


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Spain: Distribution Agreements between Independent Parties, Royalties and Use of Secret Comparables To Fix the Royalty

Adolfo Martín Jiménez and José Manuel Calderón Carrero

18.1. Introduction

This note will comment the judgment by the Central Administrative Court of 3 October 2013, R.G. 2296/2012,^{1,2} which refers to the powers of the Tax Administration to recharacterize private contracts – in this particular case payments for purchases of goods were partially converted into royalty payments – and the use of secret comparables to fix the amount of the royalties and the price for the goods. One of the specific features of this case is that it refers to a contract between independent parties. For the purposes of the Spanish domestic legislation on associated companies, the parties were not associated parties. For the purposes of article 9 of the OECD Model, they were not associated parties either since they were not in the same group or under common control (even if there may be a special relationship within the meaning of article 12(4) of the OECD Model, although this issue is irrelevant in the specific case commented).

18.2. Facts of the case

The facts refer to a tax audit covering the Spanish non-resident income tax for years 2005-2007 of the Spanish distributor of a well-known soft-drinks brand. The distributor, as explained above, was not an associate company for the purposes of domestic or treaty law with the US parent company of the soft-drinks group or the subsidiaries of such a group in different countries. The main relevant facts can be summarized as follows:

1. The Central Administrative Court (hereinafter “TEAC”) is an administrative body and not a real court of justice. Its decisions can be appealed before the *Audiencia Nacional* (AN), a real court of justice located in Madrid (the decisions of the AN can still be appealed before the Supreme Court).

2. For another commentary of this case, see E. Martínez-Matosas, I. Durán & J.M. Calderón Carrero, *Spanish Court Rules on Withholding Taxes for Deemed Royalty Payments*, Tax Notes International, p. 933 et seq. (10 Mar. 2014).

- X, the Spanish distributing company, had a contract with ABCD C, a US company, whereby X was allowed to use some trademarks belonging to ABCD C in order to elaborate, distribute and sell in a certain territory (presumably Spain) soft drinks identified with the brands X could use.
- X also had another contract with W, a Swiss company, whereby the latter permits X to use the trademark M8 to elaborate, distribute and sell in a certain territory (presumably Spain) soft drinks identified with such a trademark.
- In both cases, the parties had agreed that the use of the trademarks, labels, designs, cans and bottles and other intangibles did not give rise to any payment.
- In both cases, X had the obligation to prepare the soft drinks with “concentrates” that, in the first case, had to be purchased from ABCD C, from another entity of the group (ABCD E) or from providers authorized by them or, in the second case, from W. Those providers fix the prices and conditions for the sale of concentrate to X. As a matter of fact, the payments for the purchase of the concentrates were made to two different entities. In the first case (purchases from ABCD C), payments were made to a subsidiary of ABCD C which, the case explains, “was set up in a tax haven and had a ‘permanent establishment’ in Ireland, the PE acted in these cases as a supplier of the concentrate”. In the second case (purchases from W), payments were made directly to W (a Swiss entity).

The Spanish Tax Administration thought that the use of the trademarks was not for free. Under article 12(2) of the Spanish Non-Resident Income Tax Law, all assignments of goods or rights are presumed to be onerous unless a proof to the contrary is provided by the taxpayer. This provision was used by the Tax Administration as a legal basis to affirm that the assignment of the trademarks was not for free, as the contracts explicitly stated. As a matter of fact, the Tax Administration held that the price paid for the use of the trademark was incorporated in the prices paid for the concentrates. This part of the price was a royalty, subject to taxation in Spain at the domestic withholding tax rates (25%) in the case of payments to the Irish branch of the tax haven subsidiary of ABCD C or to the withholding tax rate of the Spain-Switzerland Tax Treaty (5%) for payments made to W.

The taxpayer (X) appealed the tax assessments first before the Tax Administration and then before the TEAC. Apart from procedural arguments, the taxpayer argued that:

- The contract between X and ABCD C, on the one hand, and X, on the other, was not entered into by associated companies and was not a franchise agreement as the tax inspectors seem to interpret. The contract only authorizes X to temporarily use the trademarks for the purposes of bottling, distribution and sale of the soft drinks and did not give X the right to make use of the intangible in itself or exploit it. As a consequence, this was not a license of a trademark but a contract of distribution.
- The contract does not stipulate any payment for the right to use of the trademark and the accounts of X only record payments for the purchase of concentrates, not for the use or right to use trademarks. These elements lessen the effects of the legal presumption that payments for the assignment of goods or rights are always paid.
- This is the first time that the Tax Administration holds this argument against the taxpayer since in previous tax audits the contracts between the same parties were not challenged (principle of legal certainty and estoppel).
- The method of valuation of the royalty part of the contract was illegal since, for that purpose, the tax inspectors have used information obtained from other taxpayers in tax audits and such information was not communicated or shown to X (“secret comparables”).
- Last, regarding the withholding tax rate, it does not make sense to apply the domestic rate for the payments to the entity resident in a tax haven. In this case, the reduced rates of either the double tax treaty with Ireland (it seems that it could be proved that the entity had its residence in Ireland and not the tax haven) or with the United States (the place of residence of the entity that owned the intangible deemed to be used by X) should apply.

18.3. The ruling by the TEAC³

18.3.1. Unbundling a single payment in different legal concepts: Royalties and business profits

First, the TEAC began by somehow correcting the conclusions and legal basis of the assessments to the taxpayer. For the TEAC, article 13 of the Spanish General Tax Law on the principle of recharacterization according to the legal nature of the acts of the parties should have been used in the case ad hoc. The TEAC explained that the principle of characterization permits the Tax Administration to decide on the true nature for tax law purposes of the facts and contracts. The TEAC found support in some decisions by the Spanish Supreme Court, which ruled the following:

- “the characterization of contracts must rest upon the true obligations of the parties, regardless of the name used by them” (judgment of 28 May 1990, cited the judgment of 25 June 2008); and
- “characterization consists on fixing the real facts to compare them with the abstract hypothesis of the norm ... this legal provision seeks to subject to tax the true economic capacity shown by the facts that are characterized as corresponds to their true legal nature or substance, disregarding therefore the external form or denomination used to manipulate the tax consequences of the act or contract ... as long as the characterization is a strictly legal operation, done with legal criterions, it cannot be said that the administrative powers have been misused” (judgment of 28 May 2011, 1451/2006).

From that case law, the TEAC drew the conclusion that the contract between X and the non-resident entities of the soft-drinks group should be studied by taking into account the true nature of the obligations assumed by the parties, regardless of the label used by them and the fact that they were not associated parties. That is to say, the TEAC corrected the legal basis of the assessment by the tax inspector (which, as explained, used the presumption of compensation of article 12(2) of the Non-Resident Income Tax Law) and explained that the fact the parties were not associated enterprises was irrelevant since neither the Tax Administration nor the TEAC itself were using the Spanish domestic law provision that sets out the arm’s length principle or article 9 of the double tax conventions applicable in the case.

The TEAC referred to the Spanish legislation on trademarks (Law 17/2001) and, in particular, to article 34(3) that establishes that “when a third party

3. For purposes of this contribution, only the arguments on substance are relevant and procedural issues will therefore not be discussed.

uses a trademark with the consent of the owner it will be presumed that the trademark is also being used by the latter”. For the TEAC, it is clear that the trademarks belong to ABCD C and are being used by X, as permitted by the contract between both parties.

For the TEAC, it is indubitable that the trademarks were used in Spain; the question was therefore whether or not that use was remunerated. It is obvious that the concentrates bought by X had an economic value, as well as the soft drinks made with the concentrates also have such a value. This value obviously increases if the drinks are commercialized under a given trademark. And it is precisely the added value of the trademark that permits to earn more income than if the drinks were marketed without such a brand or with a trademark with less value or prestige, as well as justifies the substantial marketing expenses aimed at keeping or even increasing the value of it. For the TEAC, from the wording of the contract, it was clear that ABCD C did not simply authorize X to commercialize soft drinks derived from the concentrates supplied, but the contract also permitted X to prepare, package, distribute and sell the soft drinks “with the trademarks”. Therefore, it is natural to inquire whether the payments for the concentrate also covered payments for the use of the trademark.

Despite the fact that X and the owners of the trademark were not associated entities, the TEAC invoked paragraph 6.17 of the OECD Transfer Pricing Guidelines and paragraph 11.6 of the Commentary on Article 12 of the OECD Model (2010) to justify that in package deals prices may need to be disaggregated to apply the appropriate tax treatment to each part.^{4,5}

4. *OECD Transfer Pricing Guidelines for Multinationals and Tax Administrations* para 6.17 (OECD 22 July 2010), International Organizations’ Documentation IBFD: “*The compensation for the use of intangible property may be included in the price charged for the sale of goods when, for example, one enterprise sells unfinished products to another and, at the same time, makes available its experience for further processing of these products. Whether it could be assumed that the transfer price for the goods includes a licence charge and that, consequently, any additional payment for royalties would ordinarily have to be disallowed by the country of the buyer, would depend very much upon the circumstances of each deal and there would appear to be no general principle which can be applied except that there should be no double deduction for the provision of technology. The transfer price may be a package price, i.e. for the goods and for the intangible property, in which case, depending on the facts and circumstances, an additional payment for royalties may not need to be paid by the purchaser for being supplied with technical expertise. This type of package pricing may need to be disaggregated to calculate a separate arm’s length royalty in countries that impose royalty withholding taxes*” [emphasis added on the part of the paragraph used by the TEAC to justify its decision].

5. *OECD Model Tax Convention on Income and on Capital: Commentary on Article 12* para. 11.6 (22 July 2010), Models IBFD: “In business practice, contracts are encoun-

For the TEAC, it was clear that the intangible (a very well-known trademark in the soft-drinks industry) was an important element of the contract between the parties and even if the contract was one of distribution, this is not an obstacle to conclude that it can also involve the assignment of a limited right to use a valuable trademark. As a matter of fact, the TEAC held, it can be derived from the contract that X is entitled and obliged to use the trademark to bottle and package the concentrates purchased to the companies of the group ABCD C. The facts that there are limits to the use of the trademark (it cannot be used except to identify soft drinks made with the concentrates and the concentrates cannot be commercialized under another trademark) was considered irrelevant.

Such a right to use the trademark was not ancillary to the sale of concentrates, rather, the TEAC held, was a substantial and principal part of it since if X were not entitled to use such a renowned trademark it would not have had a total turnover as high as the one it had. In fact, the tax inspectors attributed to the use of the trademark a weight equivalent to, in the example of two specific flavours of the concentrate, 61.17% of the price paid for concentrates of flavour A and of 46.18% in case of flavour B.

The TEAC took note that the tax inspectors also showed that ABCD C, apart from supplying concentrates and controlling the quality of the products, pays 50% of the marketing expenses of the trademark (not of the product). It is the policy of the group not to market specific products but to make publicity of the trademark itself. For the tax inspectors and the TEAC it would be irrational in economic terms to make expenses in Spain without obtaining any income from the trademark in Spain.

tered which cover both know-how and the provision of technical assistance. One example, amongst others, of contracts of this kind is that of franchising, where the franchisor imparts his knowledge and experience to the franchisee and, in addition, provides him with varied technical assistance, which, in certain cases, is backed up with financial assistance and the supply of goods. *The appropriate course to take with a mixed contract is, in principle, to break down, on the basis of the information contained in the contract or by means of a reasonable apportionment, the whole amount of the stipulated consideration according to the various parts of what is being provided under the contract, and then to apply to each part of it so determined the taxation treatment proper thereto.* If, however, one part of what is being provided constitutes by far the principal purpose of the contract and the other parts stipulated therein are only of an ancillary and largely unimportant character, then the treatment applicable to the principal part should generally be applied to the whole amount of the consideration” [emphasis added on the part of the paragraph used by the TEAC to justify its decision]

In this context, and using the precedent of a similar case decided by the *Audiencia Nacional*, the TEAC ruled that a part of the price paid for the concentrates was in fact a royalty subject to tax in Spain.⁶ The TEAC also made clear that in this case, paragraph 10.1 of the Commentary on Article 12(2) of the OECD Model (2010) is not applicable since the contract between X and the companies of the ABCD group is not limited to “payments made solely in consideration for obtaining the exclusive distribution rights of a product or service in a given territory”. X is not limited to “distribution” of the product, it also elaborates it in such a form that the product purchased is different from the product sold. The trademark is linked to the identity of the product sold and not to the concentrate purchased; this concentrate is not commercialized to the final consumer in an independent form.

As a consequence, the TEAC concluded that the part of the payment made by X to the companies of the ABCD group in excess of the market value of the concentrates is a royalty for the purposes of the domestic definition of royalties (article 13(1)(f)(3) of the Non Resident Income Tax Law and the royalty article of the applicable double tax conventions. The TEAC also rejected that the principle of legal certainty and the doctrine of estoppel could prevent the Tax Administration from acting according to the laws in force even if in the past the acts of the Tax Administration did not question the same contract because improper behaviour or misapplication of the law was not detected. Therefore, a change of criterion by the Tax Administration, if it is sufficiently reasoned, cannot be limited by those principles.

18.3.2. Calculating the amount of (recharacterized/deemed) royalties and the use of secret comparables

After having found that part of the price paid for the purchase of concentrates was a royalty, the TEAC proceeded to verify if the method used to calculate the amount of the royalty was valid. Since the tax inspectors could not find internal comparables of the company whereby the group permitted the use of the trademark to other independent companies, they chose two magnitudes to fix the value: the retail prices of the soft drinks (per flavour and specific product) and the cost of concentrates of private-branded (white label) products. The tax inspectors obtained information about

6. ES: AN, 30 Sept. 2009, 187/2007, also regarding a franchise contract in the field of soft drinks, although the specific contract had some relevant differences with the case considered by the TEAC.

those magnitudes from companies in the same sector; however, the taxpayer argued in the first administrative appeal that the following data were not revealed to them:

- The identity of the companies from whom the data were obtained.
- The selection criterion the tax inspectors followed (why those companies and not others?).
- The product the entities manufacture and the flavours.
- The raw materials, technology, expenses and quality control procedures used by those companies, as well as the volume of production.

The taxpayer argued that if the data were not revealed, it could not be known whether or not the comparables were homogeneous and if the amount of the royalties was correct. The answer by the Tax Administration was that they could not reveal such data for confidentiality reasons.

The TEAC, however, used paragraph 3.36 of the OECD Transfer Pricing Guidelines and the OECD Document on Comparability (later used to modify chapter III of the OECD Transfer Pricing Guidelines) to conclude that the use of secret comparables could affect the right of defence of the taxpayer and provoke a serious problem of defencelessness.^{7,8} The TEAC added that it is consolidated doctrine that tax assessments must be motivated and, when secret comparables and data are used, that motivation does not exist because the taxpayer does not have access to all the data that underpin the tax assessment, which means that there is no possibility of contradicting such data.⁹ This obviously affects the right of defence of the taxpayer and cannot be admitted. In valuation procedures, the Tax Administration, the

7. OECD Transfer Pricing Guidelines, *supra* n. 4, at para. 3.36: “Tax administrators may have information available to them from examinations of other taxpayers or from other sources of information that may not be disclosed to the taxpayer. However, it would be unfair to apply a transfer pricing method on the basis of such data unless the tax administration was able, within the limits of its domestic confidentiality requirements, to disclose such data to the taxpayer so that there would be an adequate opportunity for the taxpayer to defend its own position and to safeguard effective judicial control by the courts.”

8. OECD Ctr. for Tax Policy and Admin., *Comparability* (OECD July 2010), International Organizations’ Documentation IBFD, especially para. 8 et seq. (it is interesting that this document does not completely reject the use of secret comparables in all situations, although this nuance is not mentioned by the TEAC).

9. *See*, for instance, the Rulings by the TEAC of 14 Mar. 2008, RG 133/06, 11 Sept. 2008, RG 1510/07 and 4 Dec. 2008, RG 1462/07.

TEAC pointed out, can only use data that can be revealed to the taxpayer and are not regarded as confidential. If the companies (and products) whose data are used as a basis to motivate the tax assessment are not known by the taxpayer, it is impossible for him and the court to know whether or not their situation is comparable to that of the taxpayer. The TEAC therefore annulled the tax assessment.

It was not necessary, then, to resolve the issue of whether the tax treaty and the royalty rates thereof with Ireland or the United States were applicable.

18.4. Comments

18.4.1. General remarks on TEAC's decision: Unbundle or not to unbundle and the use of OECD materials (outside their field of natural application)

The case is very interesting in the context of article 12 of the OECD Model but also, even if it refers to the relationship between independent parties, from a transfer pricing perspective. This section comments on the TEAC's decision in a case not involving dependent parties and section 18.4.3. will take into account the differences between a context of related and unrelated parties. The use by the TEAC of international soft law also deserves some comments that, for systematic reasons, will be included in section 18.4.2.

As to article 12 of the OECD Model, the case clarifies when a right to use a trademark is conferred upon another person. First, the TEAC rightly defended an approach that requires establishing the facts and real transactions undertaken. This is not a substance-over-form analysis within the meaning of traditional anti-abuse norms or doctrines or the application of the disregard doctrine in paragraph 1.64 et seq. of the OECD Transfer Pricing Guidelines. It is simply a (re)characterization of the transactions actually undertaken by establishing the legal facts and their tax consequences, regardless of the names/labels used by the parties. As will be explained below, the issue of recharacterization arises in cases of transactions between related or unrelated parties, however, if a transfer pricing correction between the former is needed, the approach may not be the same as in the cases of the latter.

It is true, however, that in order to defend the separation of transactions and the existence of royalties, the TEAC, in addition to the Commentary

on Article 12 of the OECD Model, could have also made use of the OECD work on intangibles: the need to separate the different elements involved in some kind of combined transactions is expressly dealt with in paragraph 117 of the OECD Revised Discussion Draft on Transfer Pricing Aspects of Intangibles (30 July 2013). The document refers to the need to resort to available comparables to check whether a transaction should be combined or segregated. As it is evident from the judgment by the TEAC, even in third-party situations, it may not be easy to find comparables for these cases because of the tendency to attribute higher prices to goods in order to avoid withholding taxes for royalties. The problem, however, as explained below, in transactions between dependent parties is not only one of distribution of the price in the different components of the transaction, but also an issue of valuation according to the complex techniques the OECD has developed for transactions between associated parties.

Second, it is also clear from the case that “use of a trademark” is not only use with a view of commercial exploitation of the brand in order to license it to third parties but also use of the trademark by a distributor to manufacture products and sell them under that brand. In the authors’ view, this interpretation by the TEAC is correct and fully in line with the Commentary on Article 12 of the OECD Model (2010) even if it may create certain risks in case of distribution (and other) agreements. As the OECD Commentary on Article 12 explains, payments to obtain rights of distribution are not royalties. In line with them, Example 9 of the OECD’s Revised Discussion Draft on Transfer Pricing Aspects of Intangibles (30 July 2013) defends that no royalty is expected to be paid when a marketing and distribution entity obtains no right for transfer pricing purposes in trademarks or similar intangibles in distributing a branded product supplied by the entity entitled to the intangible return.¹⁰ But in the case considered, it appears that the contract was more than a simple distribution agreement with a (very limited) right to use the trademark for marketing purposes (use of the trademark on resale). In fact, it appears that the obligational content of the contract was not so different from a franchise agreement in which it is fully justified to disaggregate the price paid for the different parts of the transactions involved (in fact, it can be argued that the contract had three components: (i)

10. R.L. Doernberg, *Taxation Silos: Embedded Intangibles and Embedded Services*, 110 Tax Notes 10, p. 1191 (13 Mar. 2006), cites that in Revenue Ruling 75-254 the IRS ruled that income from a trademarked product should not be disaggregated for sourcing the income on a sale to a distributor; the IRS reasoned, according to Doernberg, that “the sale of a trademarked product carries with it the right to use the trademark on resale” and, in this case, because there was no specific grant of trademark rights by the seller to the distributor, no imputed royalty was appropriate. That logic was present, Doernberg continued, in the section 482 regulations (i.e. for transfer pricing purposes).

price paid for the goods; (ii) a transfer of know-how and (iii) payments for the use of the trademark).¹¹ This is not a case either where an intangible is incorporated in the product sold to the distributor and then resold, but rather a situation where the product was manufactured by the distributor with a right to use the intangible (the valuable trademark) in the production and distribution process.¹²

It is interesting that the TEAC and the Tax Administration did not refer, except by passing, to the issue of marketing intangibles since the Spanish distributor was only reimbursed 50% of the costs of the marketing expenses for the promotion of the (very well-known) brand and whether that cost had any impact upon the rest of economic magnitudes of the contract. Even if this issue is dealt with in paragraphs 6.36-6.39 of the OECD Transfer Pricing Guidelines, the OECD's Revised Discussion Draft on Transfer Pricing Aspects of Intangibles (30 July 2013) explains that in a case where the distributor assumes marketing expenses, this should have an impact on the remuneration paid to the owner of the intangible, either as a reduction in the royalty rate or the purchase price of the product.¹³ As a matter of fact, Example 10 of the OECD's Revised Discussion Draft is very similar to the case considered by the TEAC. This example recognizes that when the distributor that assumes manufacturing functions has made significant efforts (far beyond what independent companies would have made) to promote a trademark, this should have an impact on a reduction of the royalty rate.

It is likely that the TEAC did not enter into this issue because the valuation was annulled, based on the use of secret comparables, but the Tax Administration should have taken marketing expenses into account. It is not clear from the facts whether the marketing intangible and promotional efforts were relevant to fix the price paid for the concentrates (although, as explained, in this case it should have been used to calculate the amount of the royalty).

Additionally, there is another issue that is relevant. As mentioned above, the OECD's Revised Discussion Draft on Transfer Pricing Aspects of

11. On franchise agreements, see e.g. OECD, *Revised Discussion Draft on Transfer Pricing Aspects of Intangibles* (30 July 2013) para. 118.

12. The situation is therefore different from that considered in paragraph 122 et seq. of the OECD's *Revised Discussion Draft*, id.

13. See OECD, *supra* n. 11, at sec. B.4., paras. 94-96. On this issue, see also e.g. IN: Delhi Income Tax Appellate Tribunal, 14 June 2013, *Reebok India v. Addl. CIT*, where the court ruled that assumption by a subsidiary of marketing expenses above those that would have been assumed by an independent distributor can give rise to a right of compensation. See also id., 16 Aug. 2013, *BMW India Private Limited v. ACIT* (ITA 5454/Del/2012).

Intangibles (30 July 2013) proclaimed its independence from article 12 of the OECD Model and its Commentary.¹⁴ However, as this case shows, the considerations on intangibles in the OECD's Revised Discussion Draft and the Transfer Pricing Guidelines can be relevant to shed light on the application of article 12 of the OECD Model with regard to contractual relations between independent parties, especially when these contracts have been manipulated to obtain a tax benefit. It is interesting in this context that the work of the OECD in the field of transfer pricing could provide a sort of uniform standard to deal with cases of manipulation of the facts and legal consequences by the parties. It is clear in this regard that, for the TEAC, the OECD work provided such a standard to judge whether or not the contract between the companies of the group selling the concentrates and licensing the use of the trademark to an independent party was to be recharacterized. Whether or not this is a consequence that should be specifically dealt with by the Commentary on Article 12 of the OECD Model is for the OECD to evaluate. Even if it may be thought that this issue should be dealt with in the Commentary on Article 1 of the OECD Model, it may make sense to refer to it in the context of article 12 of the OECD Model in order to clarify when a distribution agreement does not give rise to royalties and when a royalty is inherent to the contract signed by the parties, especially in order to avoid excessively aggressive behaviours by tax administrations with regard to (independent or associated) distributors. In this respect, the decision to disaggregate a single contract into different components should not be taken by tax administrations without a good reason to support their conclusion, with due regard to the position of the parties and the profitability of companies situated in a similar position to the distributor (the oversimplification

14. OECD, *supra* n. 11, at para. 47: "The guidance contained in this Chapter is intended to address transfer pricing matters exclusively. It is not intended to have relevance for other tax purposes. For example, the Commentary on Article 12 of the OECD Model Tax Convention contains a detailed discussion of the definition of royalties under that Article (paragraphs 8 to 19). The Article 12 definition of 'royalties' is not intended to provide any guidance on whether and if so at what price, the use of transfer of intangibles could be remunerated between independent parties. It is therefore not relevant for transfer pricing purposes. Moreover, the manner in which a transaction is characterized for transfer pricing purposes has no relevance to the question whether a particular payment constitutes a royalty or may be subjected to withholding tax under Article 12. The concept of intangibles for transfer pricing purposes and the definition of royalties for the purposes of Article 12 of the OECD Model Tax Convention are two different notions that do not need to be aligned. It may occur that a payment made between associated enterprises may be regarded as not constituting a royalty for the purposes of Article 12 and nevertheless be treated for transfer pricing purposes as a payment made in remuneration for intangibles to which the principles of this Chapter apply ... It may also occur that a payment properly treated as a royalty under Article 12 of a relevant treaty may not be made in remuneration for intangibles for the purposes of this chapter." See also paragraph 104 of the OECD Revised Discussion Draft on Intangibles.

of the TEAC decision in this respect is somewhat surprising). But as will be explained below, it may also make sense in this context to differentiate between cases involving associated parties and independent parties since their situation is not completely equal.

In that respect, one of the main practical consequences of the decision by the TEAC may be that companies operating in Spain should review contracts involving the use of an intangible aside with the provision of services or goods, no matter whether or not the other contracting party is an associate company, if no specific consideration is provided in the contracts for the use of the intangible. A more aggressive policy of the Spanish Tax Administration on this issue cannot be discarded.

18.4.2. A note on the use of the OECD's soft law by the TEAC

As explained, the use of soft law by the TEAC also deserves some words. The TEAC did not hesitate to resort to the OECD Transfer Pricing Guidelines (it is not clear if it was the 2010 version) in a case where there were no associated companies, it also used the 2006 OECD document on comparables – which was only incorporated in the Guidelines in 2010 – so the TEAC does not seem to object to a retroactive application of the 2010 Guidelines to years before they were released (the years examined for the taxpayer were 2005-2007). It is also of great interest that the TEAC used the OECD documents to hold that the right of defence of the taxpayer – a constitutional right in Spain – was violated by the Tax Administration by using secret comparables to fix the price of the royalty paid.

The TEAC also applied the Commentary on Article 12, specifically paragraph 10.1 on distribution agreements, which was added in 2008, to interpret a tax treaty that had entered into force well before such paragraph was added to the OECD Model (the 1966 Spain-Switzerland Tax Treaty). This dynamic use is particularly curious since the TEAC applied the 2008 Commentary to interpret also the domestic concept and not only the tax treaty definition of royalties.

None of those two different uses of soft law deserves, as a matter of principle, any reproach if a certain degree of caution is exerted. As explained, the use of the OECD Transfer Pricing Guidelines or, in general, the OECD's transfer pricing materials by analogy in a case between independent companies seems correct due to the specific features of the case, but it may be

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