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R&D Capitalization: Where did we go wrong?

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Issues covered in the paper

1. The distinction between knowledge and a knowledge asset in the SNA sense. *(Not Further Discussed)*
2. How is R&D connected to the MNE’s global production chain?
3. Are national accountants able to ‘look through’ IP driven tax planning arrangements?
2. How does R&D enter the MNE?

This accounting scheme may still work at the MNE Group level.

• But can it still be applied at establishment level?
• The SNA fixed asset approach: does one size fits all?
2. How does R&D enter the MNE?

- Decisions on R&D programs are strategic and tend to occur high in the organizational structure;
- R&D input is indirect and upfront;
- Product development tends to interfere with entire supply chains;
- We know where R&D takes place but not necessarily where it is put into production.
2. How does R&D enter the MNE?

S.1 **Vertically integrated producer**

- **HO**
  - **R&D**
  - **Intermediate Deliveries (intragroup)**
  - **R&D a, b, ..**
  - **Producer A, B, ..**
  - turnover

S.2 **Factoryless goods producer**

- **FGP**
  - turnover
  - **R&D**
  - **Intermediate Deliveries**
  - **R&D a, b, ..**
  - **Contractor A, B, ..**
  - turnover
3. IP driven tax planning

Two examples:
1. Google: ‘Double Irish Dutch Sandwich’
2. Nike: ‘De Commanditaire Vennootschap’

....but the same kind of arrangement.
3. IP driven tax planning

Main elements:
1. R&L (brass-plate) in a low tax jurisdiction, often with a peculiar tax (and residency) status;
2. The R&L is legal IP owner but not in the business of IP creation;
3. Charges IP costs (produced, non-produced) to an affiliate in a high tax jurisdiction. This affiliate will typically report (high) turnover.
4. Both entities have the same parent in yet another jurisdiction.
Double Irish with a Dutch Sandwich

**Alphabet/Google Inc.**
- Controls Google Ireland Holdings
- Creates the IP
- Grants the rights of IP use outside the US to Google Ireland Holdings

**Google Ireland Holdings Unlimited Company**
- Controls Google Netherlands Holding B.V.
- Owns the rights of IP use outside the US
- Sub-licences IP rights to Google Netherlands

**Google Ireland Limited**
- Reports turnover from advertising
- Exploits and reports costs of IP

**Google Netherlands Holding B.V.**
- Controls Google Ireland Limited
- Is granted a sub-licence to the right of IP use
- Re-licences this sub-licence to Google Ireland Limited

**Google Asia Pacific**

**Royalty payments**
- 2016: 15 billion €
- 2016: 12 billion €
- 2016: 3 billion €
De commanditaire vennootschap

**Nike Inc.**
- Top of global Nike Group
- Creates IP
- Grants the rights of IP use outside in Europe to Nike Innovate CV

**Nike Innovate CV**
- Registered in the Netherlands.
- Owns certain IP within the Nike group
- Not seen as a resident institutional unit in the Netherlands

**Nike Europe Operations Netherlands B.V.**
- Reports turnover from selling sporting goods
- Legal and economic owner of inventory at European distribution centre
- Resident institutional unit in the Netherlands

**Nike Europe Holding B.V.**
- Holding company for Nike subsidiaries in Europe
- Operates distribution centre via Belgian branch
- Resident institutional unit in the Netherlands

Royalty payments
2015/16: 1 billion €

Dividend payments
2015/16: 575 million €

Dividend payments
2015/16: 377 million €

Other subsidiaries
3. IP driven tax planning

Accounting implications:

- IP assets and transactions may not show up in the accounts of any country
- Royalties on non-produced assets (marketing)
- The Bermuda triangle sink cannot be ignored, neither the Dutch Polder.

-> Bermuda GDP is 4.9 billion US $ while the Google R&L income is 14.9 billion €.
3. IP driven tax planning

Accounting implications:
• IP assets and transactions may not show up in the accounts of any country
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-> Bermuda GDP is 4.9 billion US $ while the Google R&L income is 14.9 billion €.
4. Conclusions and recommendations

**R&D in MNEs**
- Current SNA has little understanding for R&D ownership in MNEs. Further research is needed.

**IP and tax planning**
- Role of IP in tax planning -> problematic!
  - Observation and recording on strict national basis is not working
  - Key MNE units (R&Ls) are not present in source statistics
4. Conclusions and recommendations

**Possible ways forward:**

- Research the option of assigning R&D ownership to enterprise group or headquarters
- NSIs must co-operate on recording of MNE’s and sharing data.