HOW TO APPLY
INTELLECTUAL PROPERTY (IP)
BOX REGIME

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About Speaker

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Disclaimer

- This presentation is **NOT a legal advice**. It is **a legal information**.
- The difference between legal information and legal advice is important.
- Legal information can help you understand the law and legal options in general.
- Legal advice is specifically about your situation and can help you to decide what to do.
- If you need a legal advice, you should talk to a lawyer.

About IP Box

IP Box Regime (known also as a patent box, innovation box or IP box) is a corporate tax regime used by many countries to incentivize research and development activities by taxing revenues deriving from licenses, royalties, patents, sale or transfer of qualified IP assets differently offering lower taxes compared to other commercial revenues.

Intellectual Property

Intellectual Property (IP) is a commonly used term which includes mind creation results such as software programs, innovative algorithms and formulas, inventions, trade-secrets and know-how, manufacturing practices, marketing concepts, artistic works, designs, images, names and inventions used in commerce. It is one of the most valued assets a company can have.
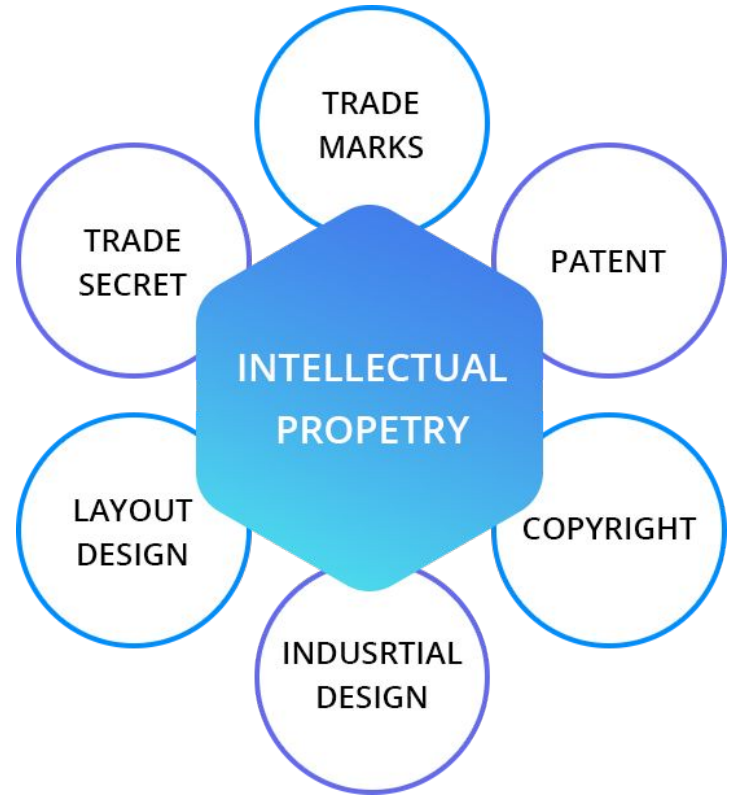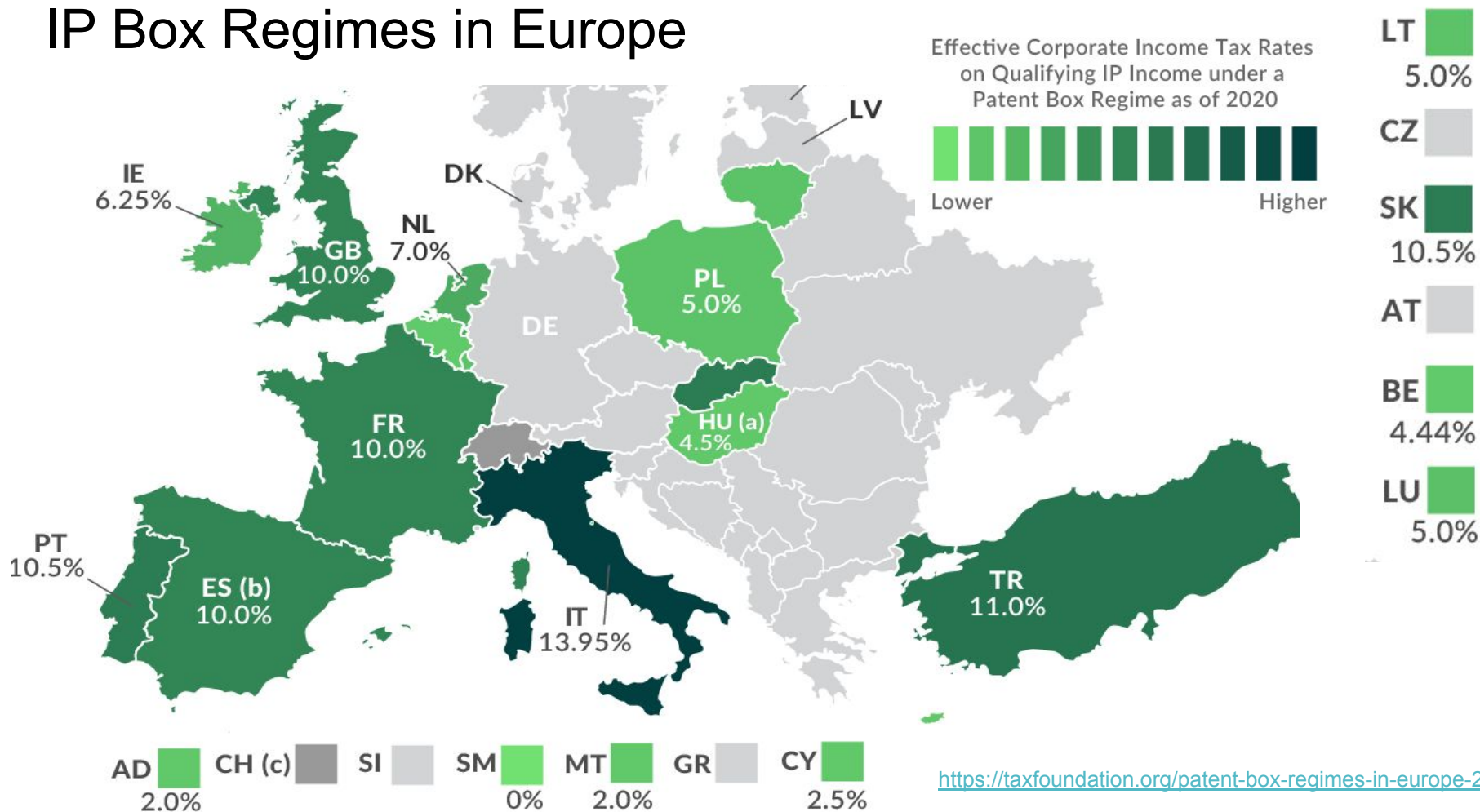
History

Ireland introduced for the very first time a scheme in its Corporation Tax on 1970s that gave the first incentive to total tax relief to respect royalties and other income from licenses patented in Ireland.
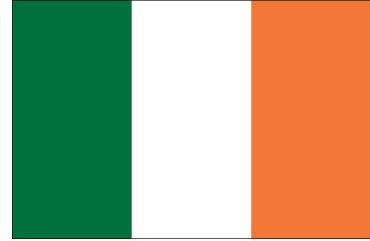
France decided to adopt Ireland's example in 2001 by reducing tax rate of revenues gained from IP licensing or the transfer of qualified IP. Later IP Box Regime started being a financial "trend" for many European countries such as Belgium, France, Hungary, Luxembourg, Netherlands, Spain, Switzerland, Cyprus, Malta and others.

IP Box Regimes in Europe

Effective Corporate Income Tax Rates on Qualifying IP Income under a Patent Box Regime as of 2020

Lower — Higher

Country	Rate
LT	5.0%
CZ	
SK	10.5%
AT	
BE	4.44%
LU	5.0%

IE 6.25%
DK
LV
NL 7.0%
GB 10.0%
PL 5.0%
DE
FR 10.0%
HU (a) 4.5%
PT 10.5%
ES (b) 10.0%
IT 13.95%
TR 11.0%

AD 2.0%   CH (c)   SI   SM 0%   MT 2.0%   GR   CY 2.5%

https://taxfoundation.org/patent-box-regimes-in-europe-2020/

IP Box Regimes in Europe

	Qualifying IP Assets			IP Box Tax	Default Corporate Tax
	Patents	**Software**	**Other**		
Andorra	X	X		2%	10%
Belgium	X	X		4.44%	29.58%
Cyprus	X	X	X	2.5%	12.5%
France	X	X		10%	32.02%
Hungary	X	X		0% or 4.5%	9%
Ireland	X	X	X	6.25%	12.5%
Italy	X	X		13.95%	27.9%

IP Box Regimes in Europe

	Qualifying IP Assets			IP Box Tax	Default Corporate Tax
	Patents	**Software**	**Other**		
Luxembourg	X	X		4.99%	24.94%
Malta	X	X		1.75%	35%
Netherlands	X	X	X	7%	16.5% to 25%
Poland	X	X		5%	19%
Portugal	X			10.5%	21%
San Marino	X	X		0% or 8.5%	17%
Slovakia	X	X		10.5%	21%

IP Box Regimes in Europe

	Qualifying IP Assets			IP Box Tax	Default Corporate Tax
	Patents	**Software**	**Other**		
🇪🇸 **Spain** **- Federal** **- Basque Country** **- Navarra**	X	X		10% 7.2% 8.4%	25%
🇨🇭 **Switzerland**	X			Depends on canton, up to 90% exemption	Depends on canton; 11.9% to 21.6%
🇹🇷 **Turkey**	X			11%	22%
🇬🇧 **United Kingdom**	X			10%	19%

Harmful vs Not Harmful IP Box Regimes

The IP assets may not have a fixed geographical nexus and can be relocated without significant cost. **85% of multinational companies use this flexibility to reduce overall tax burden by allocating valuable IP assets to a company residing in a country with a low corporate tax.**

As a result, IP Box regimes that can facilitate base erosion and profit shifting (BEPS) and therefore have the potential to unfairly impact the tax base of other jurisdictions.

Organisation for Economic Co-operation and Development

Harmful vs Not Harmful IP Box Regimes

On the basis of the features of the regime, IP regimes are found to be either: **harmful** (because they do not meet the nexus approach), **not harmful** (when the regime does meet the nexus approach and other factors in the review process), or **potentially harmful** (when the regime does not meet the nexus approach and/or other factors in the review process, but an assessment of the economic effects has not yet then place).

Organisation for Economic Co-operation and Development

https://www.oecd.org/tax/beps/harmful-tax-practices-peer-review-results-on-preferential-regimes.pdf

Nexus Approach

Nexus approach is the substantial activity requirement developed for IP Box regimes. **The nexus approach requires a link between the income benefiting from the IP Box regime and the extent to which the taxpayer has undertaken the underlying R&D that generated the IP assets.** The level of the qualifying profits is positively correlated to the extent that R&D activities are performed by the same entity.

Nexus Approach

In simple terms, if a company wants to benefit from IP Box regime then R&D activities should be largely undertaken by that same company. The company must have a local substance within the country territory.

Companies claiming benefits under the IP Box regime are obliged to maintain proper books of account, as well as records of income and expenses for each intangible asset.

Qualifying Profit (QP)

Qualifying profit (QP) is defined as the proportion of the overall income (OI) derived from the qualifying asset, corresponding to the fraction of the qualifying expenditure (QE) plus the uplift expenditure (UE) over the overall expenditure (OE) incurred for the qualifying intangible asset.

$$QP = OI \times \frac{QE + UE}{OE}$$

QI - Qualifying Income   QE - Qualifying Expenditure
UE - Uplift Expenditure   OE - Overall Expenditure

Overall Income (OI)

Overall income includes but is not limited to:

- royalties or other amounts resulting from the use of qualifying intangible assets

- license income for the operation of qualifying intangible assets

- any amount received from insurance or as compensation in relation to qualifying intangible assets

- income from the disposal of qualifying intangible assets, excluding profits of a capital nature

- embedded income of qualifying intangible assets arising from the sale of products or services, or from the use of procedures that are directly related to the assets

On calculating overall income, direct costs include:

- all costs incurred, either directly or indirectly, wholly and exclusively for the purpose of earning the income from qualifying intangible assets

- the amortization of the cost of the assets

- notional interest on equity contributed to finance the development of the assets (being a notional interest tax deduction allowed by Cyprus tax provisions)
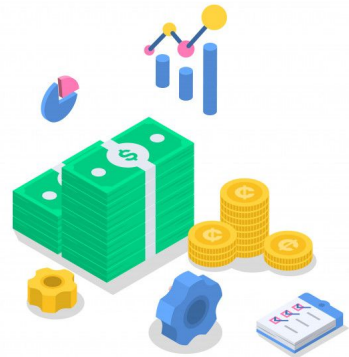
Qualifying Expenditure (QE)

Includes but is not limited to:

- wages and salaries
- direct costs
- general expenses relating to installations used for R&D
- commission expenses associated with R&D activities
- costs associated with R&D that have been outsourced to non-related persons

Does NOT include:

- costs for acquisition of intangible assets
- interest paid or payable
- costs for acquisition or construction of immovable property
- amounts paid or payable directly or indirectly to a related person to conduct R&D activities, regardless of whether such amounts relate to cost sharing agreements
- costs that cannot be proved directly connected to specific qualifying intangible asset

Uplift Expenditure and Overall Expenditure

Uplift Expenditure (UE) is added to the qualifying expenditure, which will be equal to the lower of:

- 30% of the qualifying expenditure
- the total cost of acquisition of the qualifying intangible assets, plus the cost of outsourcing to related parties of any R&D activities in relation to such assets

Overall Expenditure (OE) relating to qualified intangible assets is defined as the sum of:

- the qualifying expenditure
- the total cost of acquisition of the qualifying assets, plus the cost of outsourcing to related parties of any R&D activities in relation to these assets, incurred during any tax year

Qualifying Intangible Assets (QIA)

- patents, as defined in the Patents Law

- computer software

- other IP assets which are legally protected and fall within one of the following categories:

  - utility models, intellectual property assets which provide protection to plants and genetic material, orphan drug designations and extensions of protections for patents

  - non-obvious, useful and novel, where the person utilizing them in furtherance of a business does not generate annual gross revenues in excess of €7,500,000 from all intangible assets (€50,000,000 in case of a group of companies), which are certified as such by an appropriate authority, in Cyprus or abroad.

Cyprus IP Box - Principal Features

- 80% exemption of qualified profit from exploitation of IP assets

- 0% tax on the gain from disposal of IP assets as a capital nature transactions

- Up to 20 years amortization period

Cyprus has a large community of IT companies with founders that migrated from Ukraine, Belarus and Russia

Poland Patent Box
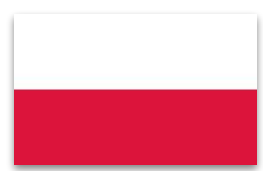
Since 1st January 2019 Poland offers plenty of support instruments for investors conducting R&D activity: R&D tax relief, Patent Box, government R&D grants as well as several programmes co-financed with EU funds.

Patent Box provides a 5% tax rate of QI from QIP rights (instead of 19% tax rate).

R&D tax incentive in CIT entitles taxpayers to make additional deduction of expenditure related to R&D activities from the tax base (up to 150%).

Advance Tax Ruling

An advance tax ruling is a tool for multinational corporations and for individual taxfilers for clarifying and confirming particular taxation arrangements. A written interpretation of tax laws is issued by tax authorities to corporations and individuals who request clarification of taxation arrangements.

An advance tax ruling binds tax authorities to comply with the tax arrangements set out in the ruling.

Example of Calculation

	Case 1	Case 2	Case 3
Overall Income (OI) from qualifying IP	€1,000,000	€1,000,000	€1,000,000
Cost of acquisition of asset	N/A	€300,000	€300,000
R&D costs, incurred internally	€500,000	N/A	N/A
R&D costs, outsourced to non-related parties	N/A	€200,000	N/A
R&D costs, outsourced to related parties	N/A	N/A	€200,000
Overall Expenditure (OE)	€500,000	€500,000	€500,000
R&D costs, incurred internally	€500,000	N/A	N/A
R&D costs, outsourced to non-related parties	N/A	€200,000	N/A
Qualifying Expenditure (QE)	€500,000	€200,000	N/A
30% of the qualifying expenditure	€150,000	€60,000	0
Total cost of acquisition + cost of outsourcing to related parties	0	€300,000	€500,000
Uplift Expenditure (UE)	0	€60,000	0

Example of Calculation

$$QP = OI \times \frac{QE + UE}{OE}$$

	Qualifying Profit (QP)	Notional Deduction (80% of QP)
Case 1: €1,000,000 x [(€500,000 + €0) / €500,000]	€1,000,000	€800,000
Case 2: €1,000,000 x [(€200,000 + €60,000) / €500,000]	€520,000	€416,000
Case 3: €1,000,000 x [(€0 + €0) / €500,000]	€0	€0

As a result, the effective corporate tax rate will be:

Case 1: Taxable profit will be decreased by €800,000 notional expense – **2.5%**

Case 2: Taxable profit will be decreased by €416,000 notional expense – **7.3%**

Case 3: No notional expense applies – **12.5%**

Cyprus IP Box Tax Calculator

License and royalties from QIA:	€1,000,000
Services with embedded QIA:	€500,000
Direct cost for generating income from QIA:	€300,000
Overall Income (OI) from QIA:	**€1,200,000**
R&D costs incurred internally:	€100,000
R&D costs outsourced to non-related parties:	€300,000
R&D costs outsourced to related parties:	€0
Cost of asset acquisition:	€100,000
Overall Expenditure (OE):	**€500,000**
R&D costs incurred internally:	€100,000
R&D costs outsourced to non-related parties:	€300,000
Qualifying Expenditure (QE):	**€400,000**
30% of the Qualifying Expenditure:	€120,000
Cost of acquisition and outsourcing to related parties:	€100,000
Uplift Expenditure (UE): minimum from the two above	**€100,000**
Qualifying Profit (QP) = OI * (QE + UE) / OE:	€1,200,000
Deduction = 80% * QP:	€960,000
Taxable Profit (TP) = OI - Deduction:	€240,000
Payable Tax (PT) = TP * 12.5%:	€30,000
Effective Tax Rate = PT / OI * 100% :	**2.5%**

https://ipbox.com.cy/calculator/

Other Issues To Consider

- Profit distribution / Dividends

- Substance Arrangement

- Controlled Foreign Corporation (CFC)

- Accounting

- Employment Taxation

- Migration Issues

- Cost of Living

Thank You!

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