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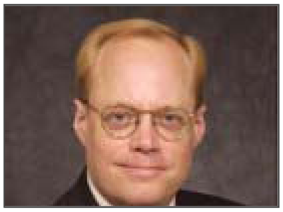

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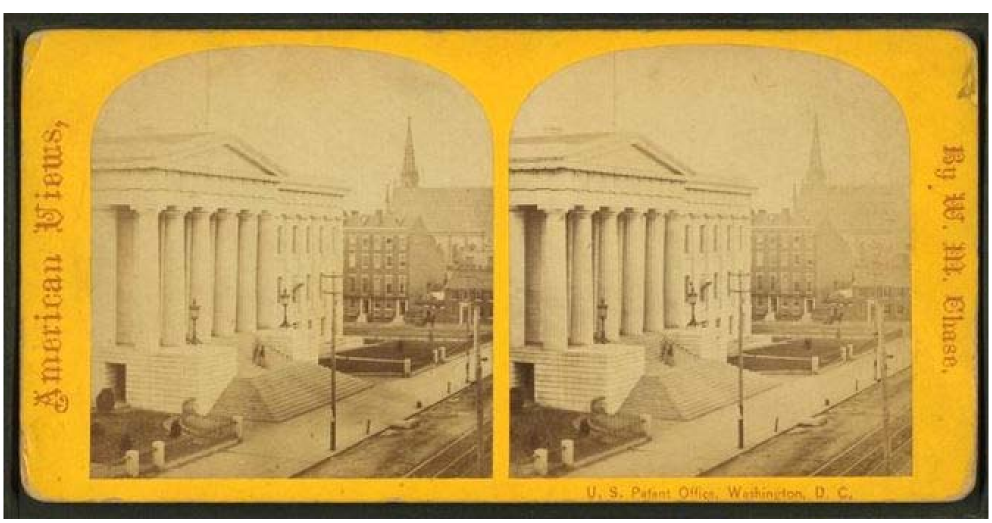
Patent Boxes Come To Ireland & UK, Why Not U.S.?

The last five years of IRS crackdowns on offshore income and bank accounts could make you think having *anything* offshore is illegal. It isn't, although the only way to have stress-free foreign accounts is full disclosure and reporting. You must distinguish between individuals and companies, especially public ones. Many things possible for big companies are not for individuals.

Individual Americans must pay U.S. tax on their worldwide income. Although they may claim foreign tax credits for taxes paid elsewhere, they can still end up with high U.S. taxes. But U.S. companies with patents and other intellectual property get a much better deal. Companies with IP often consider where it should be located. For example, the Netherlands, Belgium, France, the U.K., Ireland, Switzerland, Spain and even China can be appropriate jurisdictions for patent entities.

Although patents are the most appropriate type of IP, designs and copyrights can also be eligible. Even trademarks and trade names can work in some cases. Why do this? Think of it as splitting up income. Suppose that a company owns IP and produces and sells a product using it. How do you judge whether the revenue is from the IP, from manufacturing, or from sale?



It comes from all of them in many cases, and that invites putting the IP somewhere—quite legally—in which the IP revenue is taxed at a low rate. Pick a place that encourages R&D and other activities that will improve the IP. Some countries encouraging this activity require the R&D to be conducted in their own country.

What are the revenue sources from IP? The owner may derive income from licensing the IP, selling products or providing services using it. Licenses and sales may be to related parties, unrelated parties or both. In related party transactions, valuation is key.

Is the effort worth it? Say your company's U.S. tax rate on its profits is 35%, but the rate on IP profits in country X is 10%. That's a 25 cent savings on every dollar. Even considering fees to set it up and a contingency fund to fight the IRS if need be over valuation, the savings can be huge. The tax incentives are powerful, and IP offshoring is exploding.

Just look across the Atlantic. In the U.K., HM Revenue & Customs started patent boxes in 2013, taxing them at only 10%. Ireland has just announced an end to the double Irish tax deal, but with grandfathering. In fact, the double Irish will close in January 2015, but companies in place can keep their structures until December 31, 2020. This phase-in seems a shrewd move to keep the Irish economy moving. Besides, there will be new tax deals to be had in Ireland.

Ireland's Finance Minister Michael Noonan is introducing a patent box to encourage intellectual property held in Ireland. It should especially appeal to tech groups, which may get additional incentives to store data there. And what about the U.S.?

A special tax incentive for IP has been considered in the U.S. One proposal would require R&D activity in the U.S., making it more limited than many countries. Yet this U.S. proposal has not come to fruition, and some say it is time for the U.S. to implement a patent box tax regime to encourage domestic manufacturing. The U.S. is at a strategic disadvantage since many countries attract industry and jobs by taxing income from intellectual property sourced there at a lower tax rate.

IP offshoring to significantly reduce a company's effective tax rate can be a bonanza. The U.S. should learn that intellectual property and taxes go together, even in Apple v. Samsung + other IP suits. Plus, for inventors and flow-through entities, IP can produce capital gain rather than ordinary income. What's not to like?

Contact me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.