

*The commission on tax report 2009 made recommendations that the tax exemption for patent royalties should be discontinued. During the last thirty-seven years, there have been numerous calls for the abolition of the patent royalty exemption. They've all failed. Why? Simple - it works, argues **Richard O'Connor**, partner with Cruickshank Intellectual Property Attorneys. It remains the only real fiscal incentive for Irish manufacturing to engage in commercially-focused research and development activities.*

PATENT ROYALTY EXEMPTION: REWARDING INNOVATIVE IRISH BUSINESSES

Ireland is brimming with entrepreneurs and businesses with the skills and competencies required to develop hugely innovative products and services that can compete on a global stage. Key to capitalising on these assets and supporting indigenous businesses is tax support. The Irish Government has outlined its plans to develop Ireland's innovation and commercialisation ecosystem as one of the strongest in Europe. Marketed internationally as 'The Innovation Island', its success is dependent on creating an environment supportive to research, development, commercialisation and innovation. A fundamental success factor in transforming Ireland into a smart economy is the availability of schemes such as the patent royalty exemption scheme, as it seeks to encourage and reward a commercial return on research and development.


However, there are various reports in the media calling for the abolition of the patent

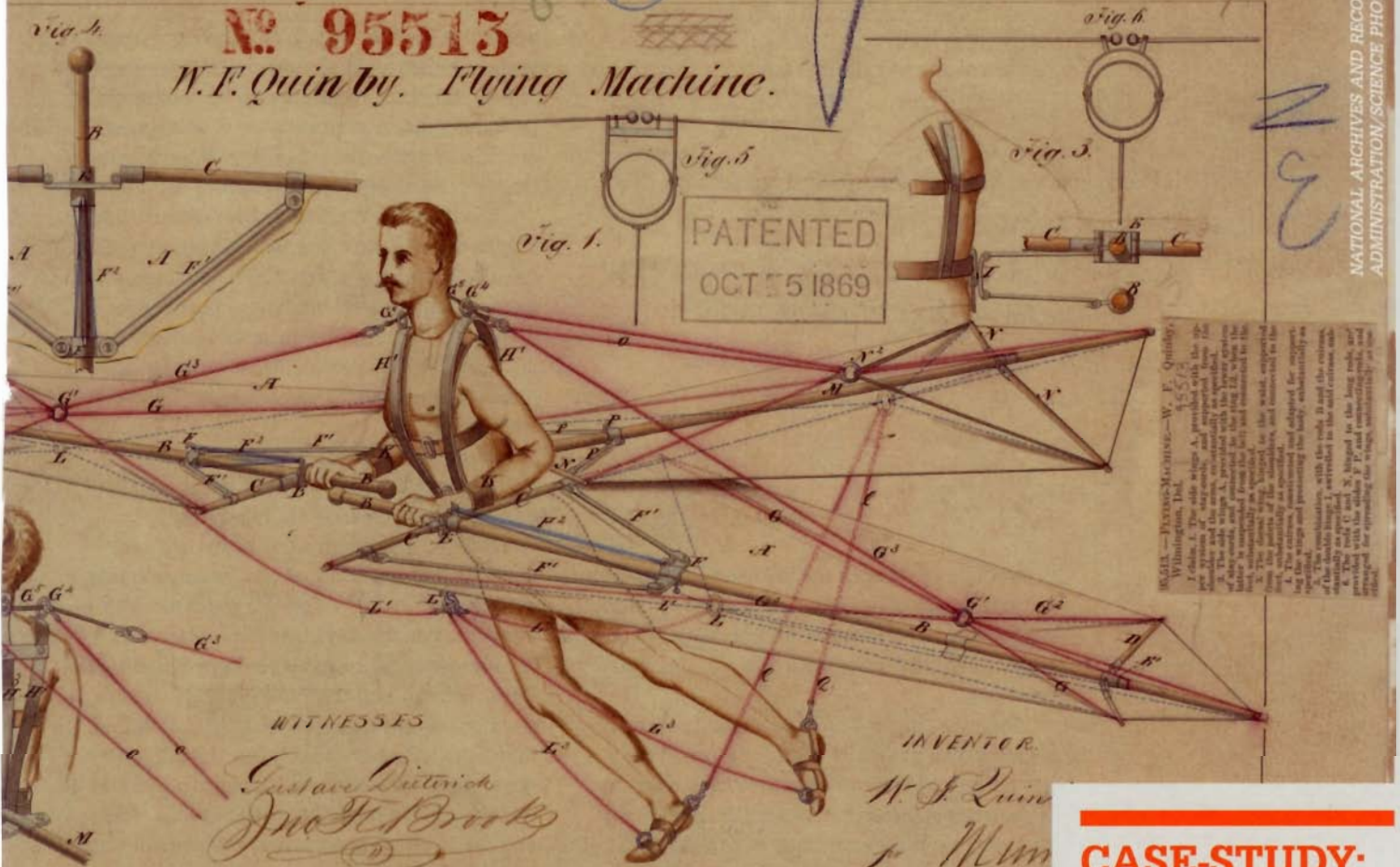
royalty exception, citing claims that it's superfluous because of the R&D Tax Credit Scheme and that it is open to abuse. The truth is that the patent royalty exemption is unique in that it is not a reward for investing in R&D, rather it rewards the successful commercialisation of R&D, thus generating more taxes, growing the Government coffers and creating more jobs - and as the saying goes, "a rising tide lifts all boats".

The benefit derived from the patent royalty exemption depends on the commercial success of the patented technology. Therefore, this initiative is about encouraging Irish businesses to invest time and resources into R&D that will yield profits. It only costs the Government money if the patented technology is a success and these costs are offset by increased taxes.

THE NEED FOR PATENT ROYALTY EXEMPTION Research and development is about creating new knowledge, generating new



Design  *Class 17*
No. 95513
W. F. Quinby. Flying Machine.



CASE-STUDY: A MAN AND HIS PEN

There are many different circumstances in which the patent royalty tax exemption comes into play. There are implications for an individual, for an organisation and for the people involved in the innovation process within the organisation. To succinctly outline the value of the patent royalty exemptions, consider a man that invents a new pen. He patents this pen and licenses the patent to a global pen manufacturer. This manufacturer makes the sales and agrees to pay 1¢ for every unit sold. The manufacturer sells 1,000,000 pens, and the inventor receives €10,000, which is paid tax free. He can earn up to €125,000 at a zero rate, and pay tax at a reduced rate up to €400,000. While the R&D may have stopped with the invention, the rewards of commercialisation will continue while the product sells.

processes and ideas. This is hugely important and the first step in the innovation life-cycle. However, the patent royalty exemption is designed to bring focus on the next step, which actively encourages businesses to bridge the gap between R&D and commercialisation. It encourages them to not simply engage in R&D activity, but also to successfully commercialise their technology and create the maximum return on investment. Invention alone does not lead to financial returns. Businesses must leverage their ideas, processes and patentable activities with a view to creating long-term and recurring revenue. This is the key distinction of the patent royalty scheme: it rewards the commercialisation process and delivers long-term benefits to Irish businesses.

TAPPING INNOVATION Irish companies often fail to tap the true potential of their intellectual property (IP). Whether traditional manufacturers or service providers that can be classified as

manufacturing e.g. treatment of food, they should consider their IP. More often than not, established Irish companies often undervalue the work they do. In fact, they are often unaware that the work they are carrying out is technically R&D, and they are most likely involved in the innovation process. This lack of awareness represents lost opportunities for businesses that have developed products or processes that should be patented. Ultimately, these businesses are losing out on the associated benefits of patents, including competitive advantage, recurring licensing fees and tax credits.

There is no simple formula to getting started. However, for businesses that want to begin the process of capitalising on their accumulated knowledge, processes and potentially patentable activities, the first step is to call in the experts. A patent and IP firm is an invaluable resource in the early stages of accessing a company's intellectual property. The firm will help an

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organisation to unlock the value and profits from patents. It can offer professional advice in terms of the significant financial and taxation benefits to be had from leveraging intellectual property correctly.

Many businesses have developed patentable technology and are not aware of it. And why would they be? Most businesses have never seen a patent application form and often presume that only a radical innovation will qualify. This is not the case and is often the reason many businesses are unaware that there's a very good chance they've created something patentable and therefore valuable. This may be a new invention. It may even be a process that has significant cost saving implications.

PATENT ROYALTY EXEMPTION The patent royalty tax exemption must be regarded as a substantial component of Irish tax-based support for R&D and one that helps raise the level of R&D tax based supports in Ireland. There are a large number of innovative companies that are involved in R&D activities but do not qualify for relief

under the R&D Tax Credit Scheme e.g. companies without clearly defined research and development expenditure budgets. However, by patenting and protecting their technology, these companies are able to realise some benefit from their efforts through the patent royalty scheme.

The R&D Tax Credit Scheme relates to tax credits given on an incremental increase in R&D spend. This is an important relief and removes many of the financial burdens of pursuing an innovation strategy. However, this scheme is limited to, and relates exclusively to, expenditure on R&D. When the investment stops, the credits stop.

On the other hand, the patent royalty exemption is a tax relief on the income of the invention. This means twenty years after the technological innovation has been patented, the company or individual can continue to reap the financial rewards. This is a big distinction and reiterates the symbiotic nature of the Irish Government's tax-based incentives. The R&D Tax Credit Scheme and the Patent Royalty Scheme must be viewed as complementary rather than mutually exclusive components of R&D tax-based supports in Ireland. The former is aimed at removing some of the financial burdens of R&D, and the latter is aimed at encouraging innovation by promoting long-term rewards.

Incentivising businesses and entrepreneurs is crucial to encourage them to engage in R&D activities and review their IP. Tax reliefs like the patent royalty exemption give the additional encouragement required to convince organisations to undertake the often costly and arduous task of R&D. The notion that successful and commercially viable R&D has residual financial implications will focus the nature of innovation towards products, services and processes that can be patented, allowing Irish businesses to exploit and profit from their IP domestically and internationally. ☺



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Recognising the lost opportunities in many Irish manufacturing businesses, Cruickshank offers a free innovation audit service called IP Free 60. The service offers participating companies a free one hour consultation with a Cruickshank Intellectual Property expert, who will assess patents, trademarks and other IP held by the company; gauge the participant's current position; outline the potential pitfalls and, crucially, tell users how they can profit from their IP.