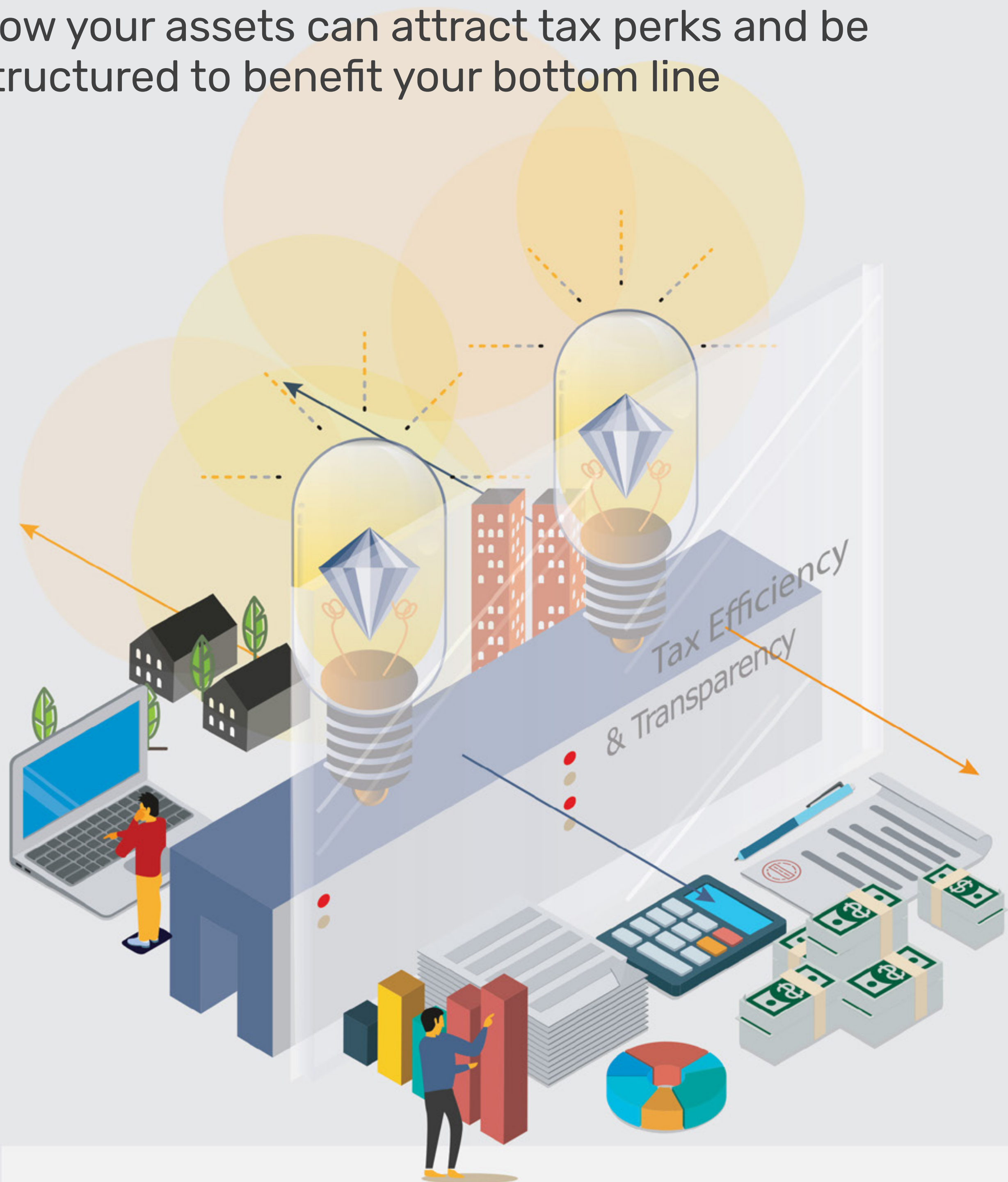
MAKING TAX-EFFICIENT USE OF YOUR ASSETS

How your assets can attract tax perks and be structured to benefit your bottom line



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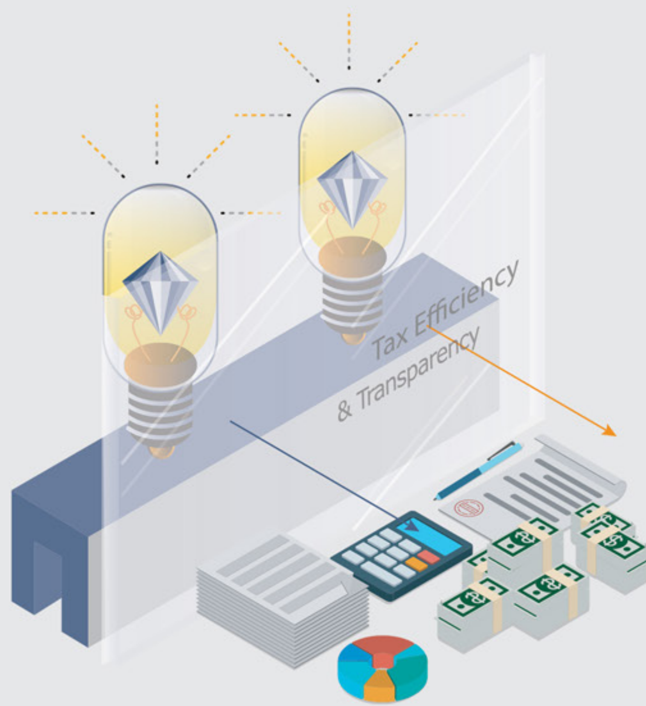
Tax Efficiency
& Transparency

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Introduction

As the saying attributed to Benjamin Franklin puts it: "In this world, nothing is certain except death and taxes!" However, for businesses that develop and exploit intellectual property (IP) assets, those inevitable tax bills can be reduced. This is because certain innovative activities and IP investments qualify for tax reliefs or deductions.

Your tax liabilities will be determined by three main considerations:

- How much taxable income you generate (as a result of your business activities);
- How many of your expenses are deductible against tax (some are, some aren't);
- What capital allowances you can claim (broadly, the tax equivalent of depreciation).

Tax planning aims to ensure your taxable income is not over-reported and make the best use of all the deductions you are entitled to claim to offset it.

It should be stressed at the outset that this guide is **not** a substitute for proper professional advice. Every company's situation is different. Accounting treatments that work for some companies are unsuitable for others; also, your entitlement to tax reliefs and deductions will vary depending on the activities in which you engage. Rather, this guide is intended to offer an overview of things you should be discussing with your accountant.

Chapter 1 sets the foundations by describing how IP investment is commonly taxed, and how research and development expenditure can be accounted for. Chapter 2 then looks at the specific incentives that are available linked to investment in IP, focusing in particular on offsetting elements of qualifying IP investment against tax and on R&D tax credits, which are likely to be relevant for the majority of innovative companies.

Chapter 3 considers how you can reduce the amount of tax you pay on the earnings you derive from your investment in IP. Singapore has introduced the IP Development Incentive (IDI), which offers reduced tax rates on directly IP-attributable income, including royalties. There are several conditions linked to this relief, including levels of investment made locally in innovation.

Where to locate and manage your IP is also a consideration for companies, especially as they grow. **Chapter 4** looks at how tax might feature in your decision-making process, depending on the varying locations of your IP, operations and production processes. If you move your IP assets, you will also encounter the challenges of transfer pricing, which is under increasing scrutiny. An accompanying guide in this series—***Uncovering your Hidden Value***, can assist you further by setting out how your intangibles might be valued.

Produced by **IPOS International**, these intellectual property management (IPM) business guides aim to deliver a suite of IP solutions for enterprises based on industry best practices. As the expertise and enterprise engagement arm of the Intellectual Property Office of Singapore (IPOS), IPOS International helps enterprises and industries use IP and intangible assets for business growth. Some of these engagements may be eligible for Enterprise Singapore (ESG) funding, such as the intangible asset audit and strategy development aligned with business goals. IPOS International 's business portal ***www.iposinternational.com*** also contains case studies and videos of enterprises leveraging IP to gain a competitive edge in their innovations. Should you have questions on IPM matters or wish to speak with our Intellectual Property Strategists, do email us at **enquiry@iposinternational.com** or call **+65 63308660**.

How does IP investment affect tax?

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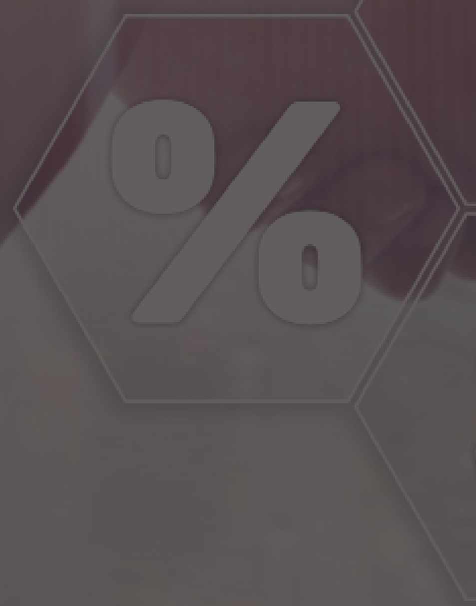

1. How does IP investment affect tax?

How is investment in IP reflected on my balance sheet?

Depending on the activity to which it relates, IP expenditure may be dealt with in your accounts in one of two ways, with differing tax implications. It may be expensed through the profit and loss account or capitalised as an intangible asset on the company's balance sheet.

Any intangible assets, like intellectual property, that you develop in-house can only be recognised (put on your balance sheet) if they conform to the strict criteria shown in the accompanying table. Where this is permitted, the cost of their development can be amortised (spread) over a specified number of years—the maximum for internally generated assets like patents, technologies and trade marks is five years.

In essence, the tax consequences of this accounting treatment are the same—either you can claim a one-off outright deduction against the expense in the year in which you incur it, or you spread this deduction over a period of time. The tax benefit is obtained by claiming writing-down allowances, explained below. However, there may be other benefits to capitalising development cost when permitted—principally, it aligns your costs more closely with their expected benefits, and mitigates the impact on your profits in the short term.

Summary of balance sheet criteria

	Criterion	Meaning	Test
1	**Identifiable**	Distinct from goodwill	*An asset is identifiable if it is capable of being separated from the company, or if it arises from contractual or other legal rights.*
2	**Controllable**	The company must control the asset	*An entity controls an asset if it has the power to obtain future economic benefits from it and prevent others from doing so.*
3	**Probability of future economic benefit**	There must be a legitimate expectation that the assets will drive future performance	*The economic benefits can be either enhanced revenues or cost savings.*

Unlike tangible assets, where the usual concept in accounting is to represent fair value, intangible asset expenditure can only be 'recognised' (put on the balance sheet) initially at cost—and to be recognised, that cost must be capable of being measured reliably. Things like the costs of introducing a new product or conducting business in a new location, or general administrative costs of doing business are not regarded as part of the cost of an intangible asset.

*More information on the accounting treatments applicable to IP rights are provided below and in the accompanying guide in this series—**Uncovering your Hidden Value**. Grants and other financial incentives are included in another guide—**Unlocking Your IP's Financing Potential**.*

Because of the 'probability' condition shown in the table above, expenses relating to the riskier **research** phase (of R&D) cannot be recognised as assets on the balance sheet. The same rule applies to other value-producing assets like branding and customer lists; this is because it is not considered possible to distinguish them from the general costs of developing your business.

The consequence of these rules is that your profits will be depressed by all this non-capitalisable expenditure in the accounting year in which it occurs, which will have an impact on your tax liability.

The relevant accounting standard which sets out the rules governing permitted capitalisation (balance sheet recognition) of intangible assets is set out in Statutory Board Financial Reporting Standard 38.

What are the implications of capitalising IP costs?

Pros		Cons	
✓	Introduces an asset onto the balance sheet to reflect investments being made in expectation of future benefits	✗	Can only be valued at cost; this may not be representative of the value to the business, which may be much higher
✓	Spreads the cost of eligible development over several years so the short-term impact on profitability is reduced	✗	Introduces an amortisation charge over several years, impacting future profitability
✓	Improves balance sheet optics	✗	Lenders (and sometimes investors) tend to be sceptical about the value of on-balance sheet intangibles because of the low likelihood of recovery

1. How does IP investment affect tax?

Pros		Cons	
✓	Amortisation reduces forward-looking tax burden	✗	Hardly any intangible assets can be revalued at market rates, as no transparent market is deemed to exist for them
		✗	Over time, the value of the assets will appear to reduce, when in reality it should grow

Are there ways in which I can offset these costs against tax?

Recognising that investment in IP is a costly business, Singapore provides several useful tax perks to help innovative companies with expenses associated with obtaining national and international protection for qualifying rights like patents, trade marks and designs.

“Tax perks last indefinitely but have to be claimed in a timely fashion”

Chapter 2 of this guide provides more detail on the available benefits. These are quite comprehensive, covering not only the costs you incur in protecting your IP assets but also what you may have to pay to acquire rights from third parties or license them from other organisations. There are also opportunities under the IDI scheme to pay a lower rate of corporation tax on incomes directly associated with IP you own that has been developed in Singapore, and you can also claim tax credits on qualifying R&D-related expenditure.

This is very helpful if you are paying tax—although since there is no cash equivalent, companies that are at an early stage of development might think these are not worth claiming. However, nothing could be further from the truth. Under Singapore tax law, these benefits can last for an indefinite period once they have been validly claimed if the company’s circumstances do not change.

What this means is that, while you may not feel the benefit now, these perks will reduce or even eliminate the tax liability you would otherwise face once you start to generate profits. This means you will have more cash available to continue investing in your business at the time it may need it most when you know that you have a successful business model. Alternatively, of course, you could share it with your supportive shareholders by way of a dividend!

While you can preserve the tax losses referenced above for an indefinite period, you only have a short period of time in which to claim your entitlement to them. There are very limited opportunities to amend tax returns that have already been submitted.

How can I gain tax perks from my investment in IP creation?

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2. How can I gain tax perks from my investment in IP creation?

What incentives are available to offset my costs?

Singapore has a range of schemes to stimulate investments likely to lead to IP creation through various tax deductions/capital allowances when qualifying activities are undertaken and appropriately documented.

“Tax perks are available on the costs of creating, buying or licensing IP”

Three main areas provide tax deductions which are specifically related to intellectual property assets. Even if you are not yet paying tax, these perks are worth claiming, as they can be preserved as tax losses and carried forward, subject to certain conditions set out in the Income Tax Act.

Under Singapore’s tax system, tax deductions are allowed until Year of Assessment 2025 on the following items:

- Protecting IP you have created in-house
- Licensing-in IP from third parties
- Buying IP from third parties

There are also incentives linked to qualifying upfront R&D investment and high-tech products and services. All of these are explained further in the following sections.

It is important to note that, under the current rules, the benefits available provide a reduction in a company’s current or future tax bill. Loss-making businesses do not have the option of cash conversion.

Outside of the taxation system, there is also ***RISC****—a Government cash grant fund to assist in setting up R&D centres, generally covering between 30% and 50% of total qualifying cost. The awards are discretionary and are made to certain projects deemed to be strategic by the Government. Further information on grants of this nature is available from the Economic Development Board (EDB Singapore).*

What tax perks are available to help me protect my own IP?

Recognising that IP protection can be an expensive business, especially when this is international in scope, there is a special tax deduction available to help offset the costs associated with filing for rights, both in Singapore and overseas.

“A 200% deduction is available on official and professional fees”

Under section 14A of the Income Tax Act, the first $100,000 of annual IP protection costs are eligible for an enhanced 200% tax deduction. Above this ceiling, you can still claim deductions, but at 100%. These perks apply to patents, trade marks,

designs and plant varieties you need to register for your trade or business and cover specified professional fees as well as official fees.

'Official' fees mean the sums you pay to Singapore's registries when applying for these different types of rights and their international equivalents. 'Professional' fees relate to advice you seek from advisers or people acting as your agent in the course of your application, described in more detail in the checklist below.

You do not need to submit supporting documents with your application, but you do need to prepare and retain information in case the Comptroller of Income Tax asks to see it. You will be required to keep records describing the IP, the countries in which it is registered, the registration costs (broken down by type) and confirmation of legal and economic ownership for at least five years.

It's important to be aware that if you subsequently sell any qualifying IP rights for which you have claimed enhanced tax deductions, a claw-back provision could apply, depending on when the sale happens. If circumstances arise where it would be preferable to dispose of these rights, consult your tax advisor.

CHECKLIST

Which activities can be offest against tax?

Category	✓	*Description*
You can claim against **official fees** relating to:		*Filing an application for a patent, trade mark, design or for a grant of protection for a plant variety.*
		A search and examination report on a patent application, or an examination report on an application for a grant of protection for a plant variety.
		Grant of a patent.
You can claim against **professional fees** relating to:		*Applying for any patent, registration of a trade mark or design, or grant of protection for a plant variety, in Singapore or elsewhere.*
		Preparing specifications or other documents in support of applications for any of the four specified types of IP rights in any country.
		Giving advice on validity or infringement of any of the four specified types of IP rights.

2. How can I gain tax efficiencies from my investment in IP creation?

Can I claim writing-down allowances on IP I buy from other people?

If you have a requirement to purchase intellectual property assets from a third party, it is good to know that there is a special writing-down allowance available to help offset your capital expenditure costs on these important assets.

"Provided you have 'legal and economic' ownership of IP rights you buy, you can write them down over 5, 10 or 15 years"

Under section 19B of the Income Tax Act, you can now elect to write down the IP rights you have acquired on a straight-line basis over a 5-, 10- or 15-year period. This is done using a one-off election submitted when you start claiming your allowances; it reflects the varying lifespans that IP rights may have.

There is a particular definition to 'acquiring' rights. Unless a waiver has been granted by the Economic Development Board, you need to have obtained both the legal and economic ownership of these rights to be eligible for writing-down allowances. The transfer of legal ownership will normally require an assignment: the economic ownership means that as transferee, you will be receiving the future economic benefits from the rights.

To claim these allowances, an additional declaration is required setting out the cost, which is used as the basis for the calculation. In addition, a third-party valuation report will be required if the capital expenditure involved is more than $500,000 (for a related party transaction) or $2m (for an unrelated party transaction). This needs to be produced by an independent specialist who is suitably qualified and experienced and is required to confirm that the cost is not greater than the open market price—if it is, the available allowance may be restricted.

CHECKLIST

What assets are eligible for writing-down allowances?

✓	*Description*
	Patents
	Copyrights
	Trade marks
	Registered designs
	Geographical indicators

✓	*Description*
	Integrated circuit layouts
	Plant varieties
	Trade secrets or information with commercial value (subject to exclusions in relation to customer lists and requirements and work process information: these are the same rules applied to deductions for licensing expenditure)

These writing-down allowances will cease if the IP expires or is not maintained or the company ceases the trade or business for which they were originally acquired. Also, if the company sells the IP rights, a balancing adjustment may be required if the sale proceeds are higher than the tax written-down value. Consult IRAS or your tax advisor if any of these circumstances apply to you.

Do tax perks apply when I license-in IP from other people?

Sometimes it may be necessary or desirable to license IP rights from third parties. If this applies to your business, the good news is that there are deductions available on the costs of doing so, provided they relate to a qualifying research and development project.

Under section 14 and 14D of the Income Tax Act, the first $100,000 of annual IP licensing costs are eligible for an enhanced 200% tax deduction. Above this ceiling, you can still claim deductions, but at 100%.

These perks apply to a wide range of IP, including patents, most copyright materials, registered designs, geographical indicators, integrated circuit layouts, trade secrets and plant varieties. There are some exclusions, most notably in respect of trade marks, which are set out in the following checklist.

CHECKLIST

Are the rights I am licensing eligible for tax perks?

✓	Exclusion	*Description*
	Trade marks	*Licensing of trade marks does not qualify for the enhanced 200% deduction. However, you can still claim 100% relief.*
	Copyright	*Any rights to the use of software are not eligible for tax deductions.*

2. How can I gain tax efficiencies from my investment in IP creation?

	Exclusion	*Description*
	Trade secrets and information that has commercial value	*This has some specific exclusions concerning customer lists and information on customer requirements. Information that is likely to assist in manufacturing or processing goods and materials does qualify, but other work processes (such as standard operating procedures) does not. Also, fees for compiling excluded information are not eligible.*
	Related party licensing	*You cannot claim a deduction for IP licensed from another part of your business.*
	'Double-dipping'	*If you have claimed a writing-down allowance under s19B of the Income Tax Act, you cannot claim deductions for licensing as well. Similarly, if you have obtained a grant or subsidy from the Government or a statutory board in relation to the IP, that part of your expenditure is not eligible.*
	Costs of ownership transfer	*If you have paid money to have the rights transferred to you, this expenditure is not eligible.*
	Legal fees	*The deduction relates to the actual cost of licensing, not to the cost of preparing the legal documentation associated with the licensing deal.*

This is not an exhaustive list—you should check the latest guidance with IRAS, or your tax advisor, to make sure you qualify.

What are the rules for R&D tax credits?

The requirements for qualifying for R&D tax credits are quite specific. Projects are required to have a clear objective, contain novelty and/or technical risk, and be a systematic, investigative and experimental study. Supporting documentation to demonstrate all of these steps needs to be produced and retained.

Qualifying R&D activity that is undertaken in a discrete project (one with clearly pre-defined start and end and objectives) can gain up to a 150% deduction if certain strict criteria are met. This rises to 250% for staff costs and consumables. To qualify, the project must satisfy all three of the criteria set out in the accompanying checklist.

CHECKLIST

Key criteria to qualify for R&D tax credits

No	Criterion	Test
1	Objective	*There must be a clear objective stated at the outset to acquire new knowledge, create new products or processes or improve an existing process.*
2	Novelty/ technical risk	*The R&D must involve a degree of novelty or technical risk (i.e. it must not be capable of being readily resolved by a competent professional).*
3	Systematic, Investigative and Experimental (SIE)	*The R&D process must be a systematic, investigative and experimental study in science or technology and be clearly defined and documented as such. This documentation must be structured and typically includes: plans, testing, the team, records, analysis, testing and evaluation.*

Routine data collection, sales and marketing activities, stylistic changes and projects in the social sciences and humanities would not qualify as R&D for these purposes. The scheme also excludes expenditure relating to government grant-funded schemes or separately covered by subsidies, depreciation, land and machinery (although capital allowances apply on the latter).

In Singapore in 2016, around 770 companies claimed enhanced R&D benefits, with SMEs making up about 85% of that total.

“There are strict rules governing projects that are eligible for R&D tax credit benefits”

To gain the maximum 150%, the qualifying expenditure needs to have been undertaken in or partly in Singapore and entirely in-house. If it has been outsourced, then the eligible amount for the additional 50% deduction (over the usual 100%) is applied to 60% of the fee paid for the outsourced R&D.

If all the R&D has taken place outside Singapore, then the additional 50% does not apply. If it has been done partly outside Singapore, then only the portion undertaken in Singapore is eligible, under the same conditions for outsourcing as noted above.

It is important to create and retain documentation for all stages of an R&D project that you believe qualifies for tax perk. IRAS will evaluate your claim and may request further information if required; there is also a technical advisory panel that can evaluate referred cases.

*The **Pioneer Tax Incentive** applies to companies manufacturing approved products or services which contain high technological content. This allows for tax exemption for 5-15 years on each qualifying project, followed by a reduced tax rate afterwards. Singapore's Economic Development Board (EDB) approves applications for this incentive.*

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