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Internationally traded IP right and VAT planning – Taiwan, Japan and OECD perspectives

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Eternity Law Firm, Taipei Taiwan Transferring foreign-registered intellectual property (IP) right

Both company T ("T Co.") and company J ("J Co.") are incorporated and tax-resident in Taiwan. In 2022, J Co. accepted T Co.'s offer to transfer the right to its patent, which is registered in Japan ("Japanese patent right"), to T Co. for a price of US\$1 million. After the patent transfer, T Co. will license that patent right to its Vietnamese subsidiary, company V ("V Co."), which will use it in manufacturing consumer products in Vietnam.

Tax issues

1. Will the sale of the Japanese patent right incur value added tax ("VAT") liabilities? If so, in which country?
2. If there is potential risk of VAT double taxation, what can T Co. and J Co. do to minimise this risk?

Taiwan's tax ruling requires VAT filing in Taiwan

According to the Taiwan Finance Ministry (MOF)'s 2014 Tax Ruling No. 10304022020,¹ in a case where two local enterprises purchase and transfer an intellectual property right ("IP right") registered in another country, the seller is obliged to file for a VAT taxable service, because provision of intangible property is deemed a service and it is being provided and consumed in Taiwan. The sale of a foreign-registered IP right will be considered neither as trading foreign property nor as export-related services, which are VAT-exempt. Accordingly, J Co. is required to file a VAT return and pay VAT to the Taiwanese tax authorities. It seems that the Taiwan MOF ruling adopts a subjective test that VAT taxation depends on the residency of seller and buyer. Taiwan's eligible VAT rate is 5%.

Japanese VAT laws tax IP rights at the registered jurisdiction

Unlike the Taiwanese regulation, Article 6, paragraph 1, no. 5 of the Enforcement Rules under the Japanese Consumption Tax Law (i.e. VAT Law) stipulates that registered IP rights, such as patents, trademarks and (here) integrated circuit layouts, are deemed to be property located in the jurisdiction where they are registered.² If the IP rights are registered in Japan, transferring their ownership is subject to Japanese VAT taxation. In other words, IP rights registered in other jurisdictions are considered overseas assets and transactions in them are exempted from Japanese VAT. Japan's eligible VAT rate is now 10%.

OECD VAT Guidelines also have different rules

Not only do Taiwan and Japan have different rules on the same transaction, but the Organisation for Economic Co-operation and Development (OECD)'s International VAT/GST Guidelines also indicate different VAT treatment when interpreting the "destination principle".³ According to Guidelines 3.2 and 3.3, internationally traded intangibles will generally be taxed in the jurisdiction where the buyer is resident, which should be named in the contract. However, if the buyer satisfies the conditions to be regarded a "multiple location entity", then the jurisdiction in which that

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intangible is “*actually used*” will have the VAT taxing right. The term “actually used” covers usage, delivery and sharing of costs. However, the OECD guidelines are only reference material; they are not directly binding on Member States. So, taxability would depend more on the VAT regulations of the countries related to the transaction.

How to avoid double VAT taxation by contract arrangement

To sum up, this analysis shows very possible double VAT taxation in this case because Taiwan and Japan, and even the OECD, have adopted different rules on VAT relating to internationally traded intangibles. In this case, J Co. would be liable to charge T Co. 10% VAT in Japan, and 5% VAT in Taiwan, with filings in both countries. This double taxation is an unnecessary cost that would follow from failing to make proper contractual arrangements in advance.

A possible option to avoid this unwelcome double taxation is for the contract subject/seller to be J Co.’s Japanese branch, which would file a VAT return in Japan; then for T Co. to charge costs to V Co. for using this patent right in Vietnam. This arrangement will then satisfy Taiwan, Japan and the OECD VAT guidelines.

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- 1 Chinese version of the Ministry of Finance ruling, see: <https://reurl.cc/rDZ53y>
- 2 In Japanese; see: <https://elaws.e-gov.go.jp/document?lawid=363CO0000000360>
- 3 See: www.oecd.org/tax/consumption/international-vat-gst-guidelines-9789264271401-en.htm