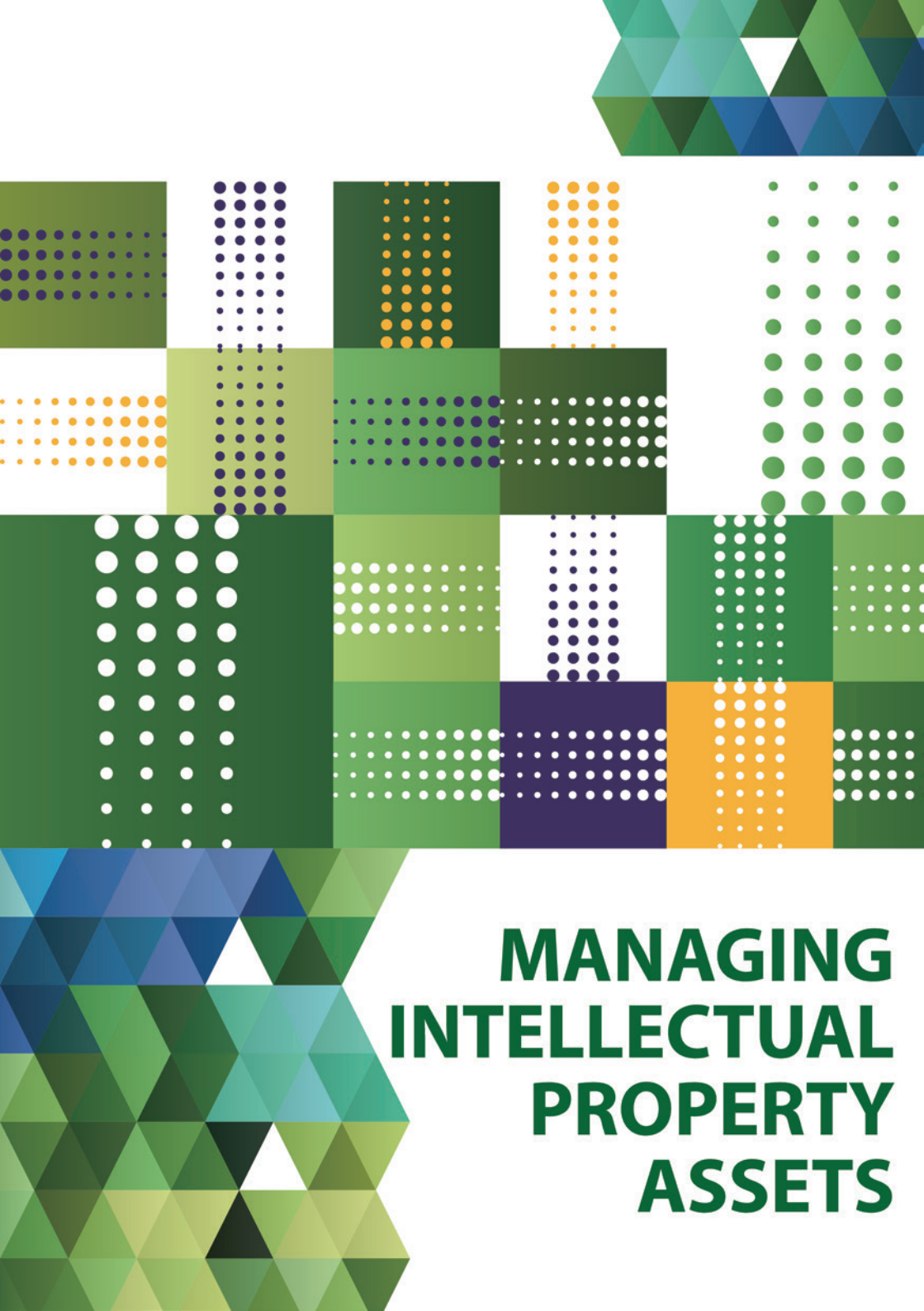

MANAGING INTELLECTUAL PROPERTY ASSETS

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MANAGING INTELLECTUAL PROPERTY ASSETS

Intellectual property ("IP") assets are becoming as important, if not more important than, tangible assets. It is essential to know how to manage your IP portfolio to optimize your IP investments and returns.

Managing IP assets involves not only a practical and diligent registration (if rights can only be enjoyed by way of registration) and maintenance programme but also a clear understanding of your business needs and foresight.

PRACTICAL CONSIDERATIONS

A good IP management policy should be incorporated into a business's daily practice and procedure and be part of the business culture. Here are some suggestions for IP managers:

(1) Be involved

To help identify potential problems at the earliest opportunity and minimise wasting valuable time and resources, you should be apprised of:

(a) research areas, new designs, inventions and marks to be undertaken,

(b) new production processes employed,

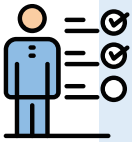
(c) new mark, packaging products or services launched,

(d) all technologies, proprietary processes or marks made obsolete, and

(e) old brands restored or revamped.

Ideally, you should be involved in approving all material stages of development, from conceptualisation, research, development, to finalisation.

(2) Understand the choice



To be able to advise how IP assets should be protected, you need to understand:

(a) why a certain product or service is designed, produced or offered the way it is,

(b) why a particular process is undertaken,

(c) why a particular name, brand, colour, slogan, logo/device or trade dress is chosen,

(d) the potential value of the IP created or licensed,

(e) the commercial life span of the relevant product or service, and

(f) your company's immediate, medium and long-term plans to develop the business utilising such IP assets.

Usually, a quick Internet search can help to gauge the commercial potentials and risks involved in continuing the development or application of the relevant IP subject.

(3) Identify the IP assets

You need to identify the nature of your IP assets. Patents, designs and trade marks require registration before exclusive rights in them will be granted and these rights are only territorial. Copyright will require a very good record of the process of creation to prove authorship and the date of creation not only for enforcement purposes but also to defend against any allegation of copying. With the advent of artificial intelligence, the degree of human input may determine the authorship and subsistence of copyright. It is important and necessary to keep a clear record of all human input (instructions) given to employ generative artificial intelligence in the process. Trade secrets will require strict compliance of security procedures to maintain the confidentiality and commercial value of the information. In addition to identifying the IP assets, you need to ask yourself which are the key assets, are they the business-drivers and can they be easily replaced, replicated or get around?

(4) Managing a registration programme

Where registration is required, you will have to decide what, when, how and where to register. Take trade mark for example, ideally, one should obtain the optimal protection by registering all the distinctive components of the mark in respect of all goods and services in all jurisdictions of actual and potential interests. However, there are always budget constraints and instead of filing for all possible registrations at the same time, you may have to do it in stages if time allows.

Even with the Madrid Protocol which facilitates the filing of one application in possibly over 100 countries in a time and cost effective manner, you still need to decide on the countries to which you wish to extend the application.

Where a composite mark is involved and there are budget considerations, you may have to decide whether it is adequate to initially register the mark as a whole rather than breaking it up into different distinctive elements and register those elements individually. You may need to prioritise the countries and the classes of goods and services to get the core registrations first. For example, if it is a new brand for clothing, the priority is likely to be as follows (in descending order of importance which of course depends on what the actual plans for the brand are):

(a) Class 25 registrations (clothing, headgear and shoes) in the countries of manufacture and markets for such products. If the brand will be the name of stores selling the branded products, then a Class 35 (retail services if the relevant country recognises them) in the countries of sale will be important too.

(b) Classes related to clothing such as Class 18 (covering leather goods, imitation leather goods, bags, umbrellas etc) in the countries of manufacture and markets.

(c) Other classes such as Class 14 for watches and jewellery; Class 9 for sunglasses.

(d) Class 3 (cosmetics, perfumery, personal care products etc) if the brand may develop a personal care and cosmetic line.

(e) Class 24 (bedding and linen) if the brand may expand into a lifestyle brand etc.

Following technological advancements, there has been a significant increase in trade mark applications covering virtual goods and uses in the Metaverse, hence Classes 9 (mobile applications, virtual goods etc), 35 (retail store services featuring virtual goods) and 41 (entertainment services in the Metaverse etc) should be considered.

While seeking trade mark registrations in stages, you must remain vigilant to police and oppose opportunists who may see the potential in your mark and try to file and obtain abusive registrations in hopes of selling them back to you at a profit in the future (trade mark squatting). You also need to review the need to expand your registrations at regular intervals. You should ensure that your business colleagues keep you apprised of plans and development of the brand ahead of actual expansion.

There are also ways to make cost savings. In Hong Kong (and in Mainland China and some other countries), you may consider multi-class applications. Overseas, you should consider the eligibility to file and the advantages of filing using the international (Madrid Protocol) and Community trade mark systems.

For designs and patents however, you may not have the luxury of filing in stages since the requirement of novelty demands that there must be no prior public disclosure of the design or invention before the date of filing. That said, you can take advantage of the priority dates afforded by international conventions such as the Patent Cooperation Treaty which allows time to file corresponding applications in member countries and

for patents, many months before deciding to proceed with the national phases. These will allow some time for your company to assess whether the commercial benefits and potentials justify the costs of (substantive) examination in the countries applied for.

(5) Coordination

This is particularly important for multinational corporations or companies where different departments or local operations may be able to make filing decisions. Preferably, all IP filings should be centralised or at least coordinated to avoid unnecessary duplications and possible conflicts. In case of enforcement, this should likewise be centralised or coordinated to make sure that the approach is consistent, and no unwitting admissions or compromises are made which may have long-term repercussions.

(6) Maintaining a portfolio

In Hong Kong and most countries, trade marks are renewed at intervals of 10 years. Discontinued brands, brands that were never developed or never really took off and markets no longer of interest are reasons not to renew. The same applies to patents and designs which are not fully utilized. In Hong Kong, registered designs are maintained every 5 years up to a maximum of 25 years, standard patents are renewed annually starting the 4th year up to 20 years and short-term patents being 8 years in maximum duration can be renewed for a second 4-year term.

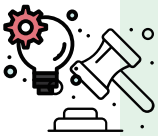
Basically, renewals depend on the requirements of the individual countries, some may require an annual renewal or evidence of use (usually for trade marks). Depending on how quickly the market changes, an audit should be conducted at appropriate intervals to review whether renewal resources should be reallocated. You should also explore the possibility of monetarizing IP assets which are and will not be actively used.

There should be a central docket system where all original registration certificates and their renewals should be kept together with evidence of first use and a detailed record of the date of conceptualization, creation, date of application, date of publication, date of registration, date of renewal, and date when the registration rights commence.

Depending on the type of rights and the jurisdiction, rights may commence from the date of application, date of publication or date of actual grant of certificate. For trade marks, information about the classes, goods and services of every mark registered in every country should also be recorded. Renewal dates and dates where evidence of use may have to be adduced should be diarized.

Where licences are granted, material particulars of the licences, including the name, place of incorporation and address of licensee, the nature of the licence (exclusive, non-exclusive, sole, partial or whole), scope (goods/services covered), channels of distribution and territories (careful territorial consideration should be given to online use), date of expiry, option to extend or first right of refusal (if any), date when notice may have to be given to terminate or extend etc. should be entered in the docket.

(7) Enforcement



It defeats the purpose of securing exclusive rights, either by incurring the cost of registration and maintenance or the cost of research and development in creating them, if you do not zealously protect them from infringement. Although you may not have all the resources you prefer to deal with all infringing acts, technical or otherwise, nor perhaps the desire to do so (some degree of infringement may be evidence of popularity and demand for your brand, product or service and perhaps tolerable), the decision should be made in accordance with clear objective criteria. You may take into account, for example, the extent of infringement, the adverse impact on your market and brand image or the desirability for the product, whether the infringer found is at the retail or wholesale level or is the source of infringement, the likelihood that other traders may be encouraged to infringe, whether defences of laches or acquiescence may be raised, whether dilution may be resulted and the value of the IP asset undermined. The objective criteria should be agreed by management with input from marketing and business and endorsed by legal. Such objective criteria or an enforcement policy is not cast in stone and should be reviewed frequently to meet dynamic market changes. Your company's sales and marketing teams are usually the first to become aware of infringements, look-alikes or parallel imports. They should be educated and reporting channels should be devised to bring these matters to proper attention. If infringement becomes rampant, it may be necessary to engage professional watching services to monitor the market.

Many IP right owners seem shy to admit the problem of infringement lest this may affect sales as consumer's confidence may be lowered. Yet, sometimes proper publicity not only sends a clear message to the market to deter actual or potential infringers but also restores consumer confidence. This will be enhanced by a robust enforcement programme to protect the integrity, quality assurance and image associated with the IP assets. Although legal departments are often viewed as a cost centre in companies, business units should be educated to acknowledge the value of enforcement to maintain the exclusivity and value of the IP assets.

(8) Review

It is important to have periodic reviews of the IP assets, their effectiveness and the mechanisms employed to protect them, to ensure that any rectifications and improvements required will be aptly made if necessary. It is equally important to review the expectations of the stakeholders to ensure that the right IP strategy is employed. This is where IP audit comes into play. An effective IP management policy increases the value of the business in IP asset creation, increases revenue through use and licensing of IP assets and decreases costs especially in reducing infringement risks.

You may refer to:

IP Audit and Due Diligence Booklet

https://www.ipd.gov.hk/filemanager/ipd/en/share/publications/IP-Audit-and-Due-Diligence-Booklet_2023-e.pdf

TAX CONSIDERATIONS

(1) General

A company's IP strategy should cover not only the creation and exploitation of IP, legal and regulatory compliance and enforcement but also tax planning. Effective tax planning and management can significantly enhance the financial benefits derived from IP assets. By understanding tax implications, businesses can structure their IP creation, ownership, investment and licensing activities to optimize deductions related to R&D expenditures, IP acquisition costs, licensing fees, and royalties, ultimately reducing their tax burden. This is particularly important in international contexts, where different jurisdictions may have varying tax rates, concessions and valuation methods.

(2) IP expenditures as deductibles

In Hong Kong, despite the general prohibition of deduction of expenditure of a capital nature, in order to promote the wider application of patent rights, rights to know-how, copyright, registered designs, trade marks, performer's economic rights, protected layout-design (topography) rights and protected plant variety rights, capital expenditures (including legal expenses and valuation fees) incurred in the purchase of such rights, for use in one's trade, profession or business in the production of chargeable profits, have been allowed.

(3) Patent box incentive

In 2024, to foster innovation and enhance Hong Kong's competitiveness as a regional IP trading center, and to encourage the industrial and research and development ("R&D") sectors as well as the creative industries to create and exploit IP, the Government has introduced the patent box tax incentive ("Concession") effective 5 July 2024. From the year of assessment 2023/24 onwards, taxpayers can elect to enjoy a 5% concessionary tax rate for Hong Kong-sourced taxable profits derived from use or sale of eligible IP, as compared to the normal profits tax rate of 16.5% (2024).

(4) Features of the patent box incentive

There are a few issues about the Concession which businesses should bear in mind:

(a) Hong Kong applies the nexus approach adopted by the Organisation for Economic Co-operation and Development in determining the extent of IP income that is entitled to the Concession. Only income derived from an eligible IP can qualify for the Concession based on a nexus ratio which is defined as the eligible expenditures (subject to a 30% uplift) as a proportion of the overall expenditures that have been incurred by a taxpayer to develop the eligible IP.

(b) Eligible IP only covers patent, plant variety rights and copyrighted software generated from an R&D activity.

(c) Applications for and registrations of patents and plant variety rights in Hong Kong or elsewhere are eligible, whilst a local registration in Hong Kong is also required for non-Hong Kong applications filed on or after 5 July 2026 and their corresponding registrations. In respect of a standard patent, local registration means registration through Hong Kong's original grant patent system and not re-registration. If the local registration is a short-term patent, a post-grant substantive examination request must be filed.

(d) In respect of copyright, only those software which is generated from an R&D activity. An R&D activity is: (i) an activity in the fields of natural or applied science to extend knowledge; (ii) a systematic, investigative or experimental activity carried on for the purposes of any feasibility study or in relation to any market, business or management research; (iii) an original and planned investigation carried on with the prospect of gaining new scientific or technical knowledge and understanding; or (iv) the application of research findings or other knowledge to a plan or design for producing or introducing new or substantially improved materials, devices, products, processes, systems or services before they are commercially produced or used.

(e) Eligible expenditures only include R&D expenditures that are directly connected to the eligible IP. This covers the expenditures on R&D activities that are (i) undertaken by the taxpayer (whether inside or outside Hong Kong), (ii) outsourced to unrelated parties to take place inside or outside Hong Kong; and (iii) outsourced to resident related parties to take place inside Hong Kong. Specifically, acquisition costs of the IP are not considered as eligible expenditures.

(f) If the R&D generates a family of eligible IPs, the taxpayer will have to apportion and allocate the relevant R&D expenditure to each of the eligible IPs on a just and reasonable basis.

(g) If the R&D involves acquisition of other IPs, or the taxpayer has outsourced part of the R&D to be undertaken by related parties outside Hong Kong, the amount of profits that can enjoy the Concession may be reduced proportionally.

(h) Where the taxpayer has undertaken part or all of the underlying R&D activities under a cost-sharing arrangement with other parties, the taxpayer's share of R&D costs could qualify as eligible expenditures for the Concession, subject to certain conditions.

(i) A loss incurred in relation to income benefiting from the Concession can be allowed to set off against assessable profits subject to a tax rate other than that provided under the regime so long as the amount of loss allowed is to be adjusted with reference to the tax rate difference.

(j) Any person entitled to derive eligible IP income from an eligible IP can enjoy the Concession without the need for any advance application. Such person must however elect for the Concession. Once the election is made, it is irrevocable and the taxpayer will not qualify for the normal two-tier profits tax rates for corporations (2023/24 - the first HK$2 million of profits will be taxed at 8.25% and the remaining profits at 16.5% tax rate).

(k) "Eligible IP income" means (i) income derived from an eligible IP in respect of the following whether in or outside Hong Kong: (1) the exhibition or use of, or a right to exhibit or use, the IP; or (2) the imparting of, or undertaking to impart, knowledge directly or indirectly connected with the use of the IP; (ii) income arising from the sale of an eligible IP; (iii) embedded IP income, i.e. if the price of a sale of a product or service includes an amount that is attributable to an eligible IP - such portion of the income from that sale as, on a just and reasonable basis, is attributable to the value of the IP; and (iv) amount of insurance, damages or compensation derived in relation to an eligible IP.

(l) To enjoy the Concession, it is essential that R&D expenditures and income derived from the eligible IP are properly tracked, traced and maintained. Such record of information must be sufficient to establish that the income concerned is eligible IP income and details of the eligible IP to which the income relates. There is a transitional

period of 3 years to allow time for taxpayers to adapt to the tracking and tracing requirements.

(m) The Concession will not apply in the event of abandonment, refusal, cancellation, revocation, lapse, withdrawal, or the absence of a request for substantive examination (where relevant), of the eligible IP or the corresponding local IP application or registration. In such situations, the Concession made in prior years will become taxable at the difference between the normal rate and the concessionary rate in the year of occurrence of the event.

Tax is a technical subject. The above only aims to provide an overview of the IP-related tax issues in Hong Kong to alert readers to consider the tax implications in its IP strategy and consult with tax advisors to implement effective tax planning and management.

ISSUES CONCERNING COLLABORATIVE INNOVATION

As economic and technological developments accelerate, technology becomes more complex and product life cycle shortens. It is unlikely that one company can have a real monopoly over all the technological fields. More and more businesses are finding collaboration as important as competition to react faster to market changes and new opportunities.

Advancement in technology and communication, digital disruption, artificial intelligence and the Internet of things, increase opportunities and make it easier for businesses to collaborate. Innovative activities have grown increasingly collaborative and transnational. Many businesses find the cost to create, acquire and maintain IP to be high and begin to shift away from traditional focus on ownership of IP to freedom to operate.

Collaboration is attractive because it can increase innovation capability and capacity, gain access to news skills and markets, better utilize resources, and share costs and risks. In reality, it is not so simple and special care must be given to related IP issues and management.

(1) Common IP-related issues for collaborative innovation

These include:

(a) What is the extent of the confidentiality obligations?

(b) What are the scope and goals of the collaboration?

(c) How to define and manage background IP?

(d) How to assess the value of the background IP a partner brings in?

(e) Who will own the output IP? If it is to be co-owned, what does it mean?

(f) What right of use will other partners have?

(g) How will the output IP generate more benefits and how will such benefits be shared?

(h) Do the partners have the right to develop derivative IPs and own them?

(i) What are the conditions of use or restrictions in respect of the background, output and derivative IPs?

(2) Is Collaboration Suitable for Me?

While collaborative innovation or IP seems attractive, not all companies are suitable to collaborate. Here are some questions you should ask:

(a) What are the goals to be achieved?

(b) Can those goals be achieved through your company's own resources?

(c) Is the nature of the product or technology involved suitable for collaboration?

(d) Does the lifecycle of the product or technology involved demand fast innovation?

(e) Is your corporate culture ready to share and collaborate?

(f) What is the duration expected?

(g) What is the exit strategy and consequences?

(3) Are There External Factors which Favour Collaboration?

You should ascertain:

(a) Who are the potential collaborators?

(b) Do potential collaborators share common objectives, values and vision?

(c) Are there government support and incentives?

(d) Would there be anti-competitive concerns?

Often, partners in collaborations between public and private institutions, established conglomerates and start-ups, customers and suppliers or between competitors have their own different priorities and objectives.

(4) Contract

Although to a good extent, IP laws regulate the rights of co-inventors, co-authors and co-owners, licensors and licensees, they are not complete. It is certainly advisable to have comprehensive contracts to clearly spell out the rights and obligations of collaboration partners to manage their expectations properly.

(5) Holistic Approach

There is no one size fits all approach for collaborative innovation. You must adopt a holistic approach. After all, is collaboration the solution? And is it best for your business competitiveness? You should be able to find the answers by asking yourself:

(a) What is the ultimate goal?

(b) How can your company achieve such goal cost effectively?

(c) What changes must be implemented to accomplish those goals and are they worthwhile?

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