

# Proposals on Intellectual Property Tax Deduction

## PURPOSE

This paper sets out the Government’s proposals to amend the Inland Revenue Ordinance (Cap. 112) (“IRO”) to implement the 2025-26 Budget initiative to expand the scope of profits tax deduction for capital expenditure incurred for the purchase of intellectual property (“IP”) or the rights to use IP, so as to promote the development of IP trading. Comments from relevant stakeholders are invited to facilitate our finalisation of the legislative proposals.

## BACKGROUND

### *Policy Objective*

2. The “Outline of the 14th Five-Year Plan for National Economic and Social Development of the People’s Republic of China and the Long-Range Objectives Through the Year 2035” promulgated in 2021 supports Hong Kong to develop into, amongst others, an international innovation and technology (“I&T”) centre, an East-meets-West centre for international cultural exchange and a regional IP trading centre.

3. To promote Hong Kong as an IP trading centre, one key strategy as identified by the then Working Group on IP Trading<sup>1</sup> is to support IP creation and exploitation. Amongst others, tax incentives have been recognised as a policy tool for encouraging the industrial and research and development (“R&D”) sectors, creative industries and IP users to engage in IP trading activities in order to meet their strategic needs of upgrading and moving up the value chain. IP trading activities like buying/selling and licensing will lead to more creation and exploitation of IP through, for example, acquisition of background or upstream IP or the licensing of IP for derivative use and commercialisation.<sup>2</sup>

---

<sup>1</sup> The Working Group on IP Trading was set up by the Government in March 2013 to advise on the overall strategy to promote Hong Kong as a premier IP trading hub in the region. It was chaired by the then Secretary for Commerce and Economic Development and comprised representatives from various bureaux/departments, industry stakeholders and experts from different fields. Its report released in 2015 ([https://www.ip.gov.hk/filemanager/ip/en/content\\_47/IP\\_Trading\\_Report-Final.pdf](https://www.ip.gov.hk/filemanager/ip/en/content_47/IP_Trading_Report-Final.pdf)) contained 28 recommended measures under four strategic areas (namely, enhancing the IP protection regime; supporting IP creation and exploitation; fostering IP intermediary services and manpower capacity; and pursuing promotion, education and external collaboration efforts) for further developing Hong Kong as an IP trading hub in the region.

<sup>2</sup> See paragraphs 5.19 et seq. of the Report of the Working Group on IP Trading.

### ***Existing Tax Deduction Regime for IP***

4. Under Hong Kong's tax regime, an enterprise's recurring expenditure that generates revenue (commonly known as "revenue expenditure") is generally deductible when computing profits tax. As such, an enterprise's revenue expenditure for the use of IP (such as royalties, licence fees and other forms of regular payments which are revenue in nature) is deductible for determining profits tax liability. If an enterprise develops its IP in the ordinary course of business, the revenue expenditure so incurred, such as rent, salaries and promotion cost, is also deductible as ordinary business expenditure.

5. It has long been the Government's taxation policy and principle that we do not tax capital receipts, and that by symmetry deduction of capital expenditure is not allowed. Nevertheless, certain exceptions have been made over the years under the IRO for different policy reasons.

6. Under section 16E of the IRO, capital expenditure on the purchase of patent rights and rights to know-how is fully deductible in the year in which it is incurred. In addition, deduction of capital expenditure on purchase of specified IP rights ("SIPRs") is allowable under section 16EA of the IRO to be spread over five succeeding years on a straight-line basis starting from the year of purchase. Currently, there are six types of SIPRs, namely copyright, registered designs, registered trade marks, protected layout-design (topography) rights, protected plant variety rights and performer's economic rights.

### ***2025-26 Budget Speech***

7. The 2025-26 Budget Speech announced that the Government will review the relevant tax deduction arrangements for various expenditures, including the lump sum licensing fees for acquiring the rights to use IP, and related expenses incurred on purchase of IP or the rights to use IP from associates, so as to accelerate the development of IP-intensive industries and promote the development of IP trading in Hong Kong.

8. Following the Government's internal review, we propose to implement the two proposals detailed in the ensuing paragraphs.

## PROPOSALS ON IP TAX DEDUCTION

### *Proposal 1: Allowing tax deduction of the acquisition cost of certain IP from associates*

9. Under section 16EC(2) of the IRO, no deduction is allowable in respect of any patent right, right to know-how, or SIPR acquired by a person wholly or partly from an associate. This is a safeguard measure implemented since 1992 to tackle possible tax avoidance.

10. Tax deductibility of the acquisition cost of IP will affect corporations' consideration to move IP into or out from Hong Kong. Multinational corporations may wish to centralise the management of IP in Hong Kong. Allowing them to claim tax deduction for the acquisition cost of IP acquired from their associated entities outside Hong Kong can encourage the bring-in of new IP into Hong Kong. In cases involving domestic transactions where the associates are also Hong Kong entities, deduction of IP acquisition cost can facilitate domestic intra-group transfer of IP and encourage bona fide mergers and acquisitions to suit common business practices. Both scenarios will help generate more business activities as well as demand for associated professional services (such as legal and accountancy services), whilst creating job opportunities and additional revenue for the Government. Moreover, corporations are more likely to transfer IP to their associates best positioned to commercialise the IP, leading to greater exploitation of IP, which will in turn be conducive to driving more creation of IP and enhanced R&D, thereby reinforcing Hong Kong's role as a regional IP trading centre and international I&T centre. We therefore propose to suitably relax the safeguard measure under section 16EC(2) of the IRO and expand the scope of the profits tax deduction for capital expenditure incurred for the purchase of IP to include acquisitions from associates.

### Safeguard Measures Against Abuse

11. To align with the said policy objective and to prevent associates from looping the same IP within the group to claim tax deduction, as well as to prevent associates from shifting offshore losses into Hong Kong for setting off against the assessable profits of Hong Kong companies, we propose to introduce the following safeguard measures against abuse –

- (a) no deduction is allowable if the main purpose or one of the main purposes of the acquisition of the IP is to obtain a tax benefit<sup>3</sup>. In

---

<sup>3</sup> Tax benefit means an avoidance, postponement or reduction of a liability to pay tax chargeable under the IRO.

determining whether there are good commercial reasons for carrying out the transaction and whether there exists a main purpose for avoidance of tax, all relevant facts and circumstances would be considered. For avoidance of doubt, if tax benefit is only an incidental consequence of the transaction, the obtaining of tax benefit will not be regarded as a main purpose; and

- (b) in the case of domestic intra-group transfer of IP –
  - (i) the transfer should be subject to the requirements on the transfer pricing rules and transfer pricing documentation by way of carving out such transfers from the domestic transaction exemption provided under section 50AAJ of the IRO. For avoidance of doubt, the exemption on transfer pricing documentation for eligible enterprises and eligible transactions below a certain threshold under sections 58C(1) and 58C(4)(b) respectively of the IRO remains applicable to entities with domestic intra-group transfer of IP; and
  - (ii) to prevent group companies from obtaining excessive tax deduction by arranging domestic transfer of IP with inflated price among themselves, the full amount of the sales proceeds received by the IP transferor, less the amount of deduction (in respect of the IP) not yet allowed, will be treated as a trading receipt chargeable to profits tax in the hands of the IP transferor<sup>4</sup>. Nevertheless, since the associate being transferred with the IP is eligible for tax deduction of its acquisition cost of the IP, the tax position of the whole group will remain the same.

12. Other anti-abuse provisions under section 16EC of the IRO, including disallowing deduction for the acquisition of IP used by a licensee outside Hong Kong in section 16EC(4)(b) of the IRO, remain applicable. Hong Kong adopts a territorial source principle under which the profits derived from offshore activities with a source outside Hong Kong would not be chargeable to profits tax in Hong Kong. Accordingly and in accordance with the tax symmetry principle, no deduction should be granted for expenditures incurred in the production of such offshore profits. Section 16EC(4)(b) of the IRO is necessary to uphold the aforementioned principles.

13. Nevertheless, Hong Kong taxpayers would still be eligible for tax deduction if they have used by themselves the IP rights in cross-border activities

---

<sup>4</sup> For a transfer of IP between non-associates, the sales proceeds, capped at deductions previously allowed, would be brought to tax. That is, no tax would be imposed on the capital gain.

for production of profits chargeable to tax in Hong Kong. For example, a Hong Kong company acquires the proprietary interest of a trade mark registered both in Hong Kong and in the Chinese Mainland, contracts a manufacturer in the Chinese Mainland to produce goods bearing the Hong Kong registered trade mark by granting to the manufacturer a licence for the use of the Chinese Mainland-registered trade mark. The Hong Kong company then sells the goods in Hong Kong producing profits chargeable to tax in Hong Kong. The said Hong Kong company would, subject to the satisfaction of other relevant conditions, be eligible for tax deduction in respect of the capital expenditure incurred on the purchase of the Hong Kong registered trade mark.

#### Requirement for Third-Party Independent Valuation Report

14. To ensure that the acquisition cost is at an arm's length price and to prevent inflating the purchase price of IP for claiming excessive tax deduction, especially between associates, a **third-party independent valuation report by an appropriate valuer**<sup>5</sup> would be required if the acquisition cost of the IP exceeds a certain threshold. Detailed requirements are as follows –

- (a) a third-party independent valuation report is required when the capital expenditure incurred in the acquisition of the IP is equal to or greater than **\$3 million** for a related party transaction;
- (b) the valuer must be **independent** of any party to the transaction and has qualifications and experience that are relevant to the valuation of IP; and
- (c) whilst the valuation report need not be submitted together with the tax return, the taxpayer must provide the said valuation report to substantiate its deduction claim upon request by the IRD.

#### ***Proposal 2: Allowing tax deduction for upfront licence fees for the right to use IP in a licensing arrangement***

15. As mentioned in paragraph 4 above, licence fees that are revenue in nature are generally deductible for determining profits tax liability. However, upfront licence fees (i.e. a lump sum payment to be paid initially) which are regarded as capital in nature are not allowed for deduction. There has been feedback from the industry that the practice of charging an upfront licence fee is actually quite common especially among tech companies for the use of patents, given the huge capital investment made (and the wish of the creators to recoup

---

<sup>5</sup> An appropriate valuer should possess relevant qualifications, the details of which (including such examples) would be set out in a future guidance note.

the investment as early as possible). To further encourage the development and commercialisation of IP, we propose to allow tax deduction for upfront licence fees incurred for the right to use IP in a licensing arrangement. In other words, expenditures on licence fees, **irrespective of capital or revenue in nature**<sup>6</sup>, so long as they are incurred in the production of assessable profits, would be allowable for tax deduction.

### Forms of Licences to be Included

16. Forms of licences for allowing the tax deduction will include the following –

- (a) exclusive licence<sup>7</sup>;
- (b) sole licence<sup>8</sup>; and
- (c) non-exclusive licence<sup>9</sup>.

### Types of IP to be Included

17. For the types of IP involved in the licensing arrangements, we propose to confine the tax deduction to the **eight types of IP** under the existing tax deduction regime for IP. These eight types of IP are patent rights and rights to know-how, and SIPRs as mentioned in paragraph 6 above.

### Deduction Period

18. Allowing tax deduction in full in one go may create unnecessary distortion of the tax position of the licensee. To minimise the financial impact, we propose that the tax deduction be **evenly spread over the licensing term** so as to align with the accounting treatment on amortisation of the licence. If the licensing arrangement is amended subsequently, the remaining deduction is to be spread over the remaining term of the licensing period, while in the case that the aggregate of deduction claimed exceeds the revised licence fee, there shall be claw-back of the tax deduction.

---

<sup>6</sup> Revenue expenditures for the use of IP (such as royalties and periodic licence fees) are all along deductible under section 16(1) of the IRO.

<sup>7</sup> An exclusive licence refers to a licence under which the licensee is the only person authorised to exploit the IP, and even the IP owner cannot exploit the IP.

<sup>8</sup> A sole licence refers to a licence under which the licensee is the only person that is granted a licence to exploit the IP, while the IP owner retains the right to exploit the IP.

<sup>9</sup> A non-exclusive licence refers to a licence that may be granted to more than one licensee, while the IP owner may also exploit the IP.

## Claw-back Arrangement

19. We also propose that there will be claw-back of the tax deduction in the event of **termination or assignment** of all or any part of the IP licensing rights. To align with the existing tax treatment on sales proceeds of IP under sections 16E(3) and 16EB of the IRO, only the amount of the deduction previously allowed is to be recouped, as there is no capital gains tax in Hong Kong. Any excess of proceeds from the termination or assignment of any IP licensing rights over the unallowed amount will be treated as taxable receipts to the extent that the excess should not exceed the amount of the deduction allowed.

## Upfront Licensing Income is Chargeable to Profits Tax

20. In addition, to ensure that tax symmetry is maintained so that Hong Kong can tax the upfront licensing income for which deduction has been allowed to the licensee, we propose to add a deeming provision to treat any sums, not otherwise chargeable to profits tax under the IRO, received by or accrued to a Hong Kong licensor in relation to the right to use IP as trading receipts chargeable to profits tax.

## Anti-avoidance Provisions

21. Similar to other tax deduction items, tax deduction for capital expenditure involving IP is prone to abuse. Hence, we propose to put in place the following measures to guard against possible tax avoidance –

- (a) the Commissioner of Inland Revenue (“CIR”) will be empowered to determine, where the circumstances so warrant, **the arm’s length price** of which a tax deduction is claimed, and a provision will be added to empower CIR to **request the submission of a valuation report** from the licensee to substantiate its claim; and
- (b) the CIR will be empowered to **allocate the consideration** when the licence to use IP is acquired, assigned or terminated with any other dealings.

## **LEGISLATIVE TIMETABLE**

22. There is a need to amend the IRO to implement the above proposals. Our target is to introduce the relevant Amendment Bill into the Legislative Council within 2026.

## **VIEWS SOUGHT**

23. Views are invited on the above two proposals as set out in paragraphs 9 to 21 above. Please send your views to the Commerce and Economic Development Bureau (“CEDB”) by email (iptax\_consultation@cedb.gov.hk) on or before 31 March 2026.

24. Submissions received will be treated as public information, which may be reproduced and published in whole or in part and in any form for the purposes of this consultation exercise and any directly related purposes without seeking permission of or providing acknowledgement to the respondents.

25. It is voluntary for any respondent to supply his or her personal data upon providing comments. The names and background information of the respondents may be posted on the websites of CEDB and other relevant government bureaux or departments, referred to in other documents published for the same purposes, or transferred to other relevant bodies for the same purposes. If you do not wish your name and/or your background information to be disclosed, please state so when making your submission. For access to or correction of personal data contained in your submission, please write to CEDB via the above means.

**Commerce and Economic Development Bureau  
Inland Revenue Department  
Intellectual Property Department  
January 2026**