Intellectual Property - Luxembourg

Administrative Court rules on the IP Income Tax Regime

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Background
***Zeilt* decision**
***Zinc alloy* decision**

Background

Under the framework of the Lisbon strategy for growth and employment in the European Union, Luxembourg added Article 50*bis* to the Income Tax Act 1967 at the end of 2007.

Based on this regime, Luxembourg undertakings and Luxembourg branches of foreign companies can benefit from an exemption of 80% on revenue (ie, royalty fees) derived from patents, trademarks, designs and domain name rights, as well as from copyright on software, to the extent that such rights have been established or acquired after December 31 2007. The exemption brings the effective tax rate for such revenues to approximately 5.85%.

The Article 50*bis* regime has been further clarified by the Luxembourg Administrative Court, the highest administrative jurisdiction in Luxembourg which rules on appeal procedures brought against judgments of the Administrative Tribunal.

On July 30 2014 the Administrative Court handed down its judgments in the *Zeilt* and *Zinc Alloy* cases, holding that:

- revenues from trademark rights are eligible under the Article 50*bis* regime from the date of the trademark application (rather than the date of definitive registration);
- licence fees are eligible revenues under the Article 50*bis* regime only when a licensee actually exploits the eligible IP rights on a given market – this is not the case where the licensee simply affixes the trademark on goods and sells them on to a licensor which is an intra-group company; and
- cartoon characters do not benefit from design protection and fall outside the scope of the Article 50*bis* regime.

These clarifications show that companies should carry out a more detailed analysis of eligible revenues – particularly from an IP law viewpoint – before relying on the Article 50*bis* regime.

Zeilt decision

In *Zeilt Productions Sàrl* the Luxembourg tax administration refused to grant an exemption to the revenues of Luxembourg company Zeilt Productions Sàrl, which produced the Oscar-winning animated short movie *Mr Hublot*. The revenues were derived from unregistered designs related to several cartoon characters.

The tax administration considered that only designs for which an application has been filed are eligible for the 80% exemption, as the filing of an application allows for objective verification of the existence of the rights.

Zeilt challenged this refusal before the Luxembourg Administrative Tribunal. On November 6 2013 the tribunal handed down its judgment holding that nothing in Article 50*bis* prevented the granting of the 80% exemption to revenues derived from designs for which no application had been filed. The tribunal correctly based its judgment on Article 1.2.a) of the EU Community Designs Regulation (6/2002), which confers protection on unregistered designs from the date when they are made available to the public.

However, the Administrative Court overturned the judgment and held that the characters constituted copyright-protected works (which do not fall within the scope of the Article 50*bis* regime), rather than design-protected works.

According to the Benelux Convention on Intellectual Property and EU Regulation 6/2002, a 'design' is

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the "appearance" of a "product", whereby 'product' means "any industrial or handicraft item".

The Administrative Court considered that computer-created characters are not industrial or handicraft items, and thus not products whose appearance can be protected as a design.

Therefore, the court had a restrictive interpretation of the terms 'design' and 'product' – an interpretation which is not supported by the broad definition of these concepts in the Benelux Convention on Intellectual Property (or EU Regulation 6/2002), which explicitly includes less evident items such as "get-up, graphic symbols and typographic typefaces". Further, according to the Office for Harmonisation in the Internal Market and other design search registries, various cartoon characters (eg, the Teenage Mutant Ninja Turtles) enjoy design protection.

In the proceedings before the Administrative Court, the Luxembourg state (representing the tax authorities) argued that an undertaking seeking to benefit from the Article 50*bis* regime must prove the new and individual character of a design. This position cannot be upheld in the light of *Karen Millen* (Case C-345/13, June 19 2014), in which the European Court of Justice held that the rights holder of a design "is not required to prove that it has individual character... but need only indicate... what, in his view, are the element or elements of the design concerned which give it its individual character".

***Zinc alloy* decision**

In order for the Article 50*bis* regime to apply, the eligible IP rights must have been "established" or "acquired" by the Luxembourg undertaking or branch after December 31 2007.

The tax administration issued Circular 50*bis*/1, wherein it clarified that for trademarks the date of establishment may be earlier if the undertaking concerned has already commercialised the relevant products (ie, zinc alloys) under the sign concerned without filing an application for registration.

This point of view was challenged in a case which arose when the Luxembourg tax authorities refused to grant the 80% exemption to a Luxembourg company for revenue derived from a name and a logo that was used before December 31 2007, but for which Benelux and Swiss trademark registrations was filed only after that date.

On June 27 2013 the Administrative Tribunal handed down a judgment in this case. The tribunal held that Article 50*bis* did not prohibit the granting of the 80% exemption to undertakings that used a sign before December 31 2007 but filed a registration application only afterwards.

The Administrative Court held that the date of the application for the trademark registration is the date on which trademark rights are established (even when these are definitively acquired only on the date of registration) and also the start date for the eligibility of trademark-related revenues under the Article 50*bis* regime.

However, the court refused to consider the relevant trademark licence fees as eligible revenues under the Article 50*bis* regime. It held that the licensee only affixed the trademark on the zinc alloys and then sold them to the licensor, which was an intra-group company. According to the court, the licence fees do not constitute remuneration for the right to use the trademark. In this respect, the court had a restrictive interpretation of the 'right to use' the trademark – that is, the use of the trademark for the licensee's own purposes for the commercialisation of the products on the market covered by the trademark.

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