



Chartered Accountants
& Business Advisers

21 July 2006

Private & Confidential

Mr Stephen Hargreaves
Chairman & CEO
International Innovations Ltd
Level 25 Chifley Tower
2 Chifley Square
Sydney NSW 2000

Dear Stephen,

Private Ruling – application to all countries

We refer to the Notice of Private Ruling Authorisation Number 63585 (**the ruling**) dated 8 June 2006 issued to International Innovations Limited (**IIL**) in relation to the application of the income tax and capital gains tax (**CGT**) provisions and the capital allowances provisions of the *Income Tax Assessment Act 1997 (the 1997 Act)* should IIL grant a licence to exploit certain intellectual property to a company to be established in Europe (**Euro Co**).

In particular, the private ruling addressed the meaning of the phrase 'non-cash benefit' at Item 4 of the table in section 40-305 of the 1997 Act. The Commissioner of Taxation (**the Commissioner**) confirmed in the private ruling that a right that IIL obtained under the licensing agreement to receive future royalty payments from Euro Co would not be a non-cash benefit that IIL would be taken to have received under section 40-305 of the 1997 Act, notwithstanding that the right to receive the future royalty payments would have some value. In essence, the Commissioner confirmed that contractual rights were not of themselves non-cash benefits for the purposes of Item 4 of the table in section 40-305 of the 1997 Act with the consequence that, in the absence of any consideration provided by Euro Co to IIL for entering into the licensing agreement, merely entering into the licensing agreement would not of itself give rise to a balancing adjustment under Subdivision 40-D of the 1997 Act.

At the time of applying for the private ruling, it was anticipated that Euro Co would be a tax resident of either Switzerland or Germany. You have requested that we confirm that the private ruling will also apply should IIL grant a licence to exploit the intellectual property to a company in any other country.

Summary of the private ruling and licensing arrangements

The subject of the private ruling issued to IIL involves the application of the Australian income tax law to IIL at the time that IIL grants a licence to a foreign company on the terms and conditions set out in the application for a private ruling and in the private ruling itself. The terms and conditions of the licence agreement are summarised in the private ruling as follows:

- Euro Co will pay a percentage of the revenues it earns from exploitation of the intellectual property in the form of royalties to IIL
- The royalties will be payable monthly, in arrears
- The term of the licence to be granted to Euro Co will be for an agreed and finite period of time
- The terms and conditions of the licensing agreement will be negotiated on an arms length basis and any amounts payable or benefits provided or obtained under the agreement will be fully negotiated and reflect arm's length pricing principles
- Euro Co may sublicense authority to other parties to exploit the patent
- IIL will be able to terminate the agreement upon certain acts or omissions on Euro Co's behalf, including the failure to pay the required royalty amounts
- IIL will retain all proprietary rights to the patents and the intellectual property.

In addition, the private ruling reiterated that IIL may enter into other licensing agreements granting other companies the right to exploit the intellectual property in other countries or regions.

The private ruling will only bind the Commissioner if licences to exploit the intellectual property are in fact issued on the terms and conditions as advised to the Commissioner in the application for a private ruling and as included in the private ruling issued by the Commissioner. If IIL wishes to vary the terms and conditions of the licensing arrangements, IIL should consider whether the proposed changes would materially affect IIL's ability to rely on the private ruling.

The private ruling issued by the Commissioner covers the Australian tax implications arising when IIL grants a licence to a foreign company. The private ruling does not cover the tax implications arising in any other country when IIL issues a licence to a foreign company. The Commissioner cannot and will not rule on the way a foreign taxation law applies to a transaction or event.

Application of the private ruling to licences granted to companies resident in other countries

The Australian tax law will apply in the way described in the private ruling issued to IIL whenever IIL licences the intellectual property described in the private ruling on the terms and conditions and in the circumstances described in the application for the private ruling and as described in the private ruling issued by the Commissioner.

The country of residence of the licensee is not relevant for the purposes of determining the way the Australian tax laws covered in the private ruling, and in particular section 40-305 of the 1997 Act, apply at the time a licence is granted to a foreign licensee. Accordingly, in addition to a licensee in Germany or Switzerland, the Australian tax consequences as described in the private ruling will apply at the time a license is granted to a licensee in any other country, including the United States of America, China, Japan or elsewhere.

Note the country of residence of the foreign licensee may be relevant for other tax purposes, such as the application of the royalty withholding tax rules of a foreign country or the application of an international tax treaty to any payments made in accordance with a licensing agreement.



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If you have any queries or wish to discuss this matter further, please do not hesitate to contact me on (03) 9603 1719.

Yours sincerely

The PKF logo, consisting of the letters 'PKF' in a bold, blue, sans-serif font.

A handwritten signature in black ink that reads 'John Kelly'.

John Kelly
Partner

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