

Innovation & Technology

'PATENT BOX' TAX RELIEF



UK 'PATENT BOX' TAX INCENTIVE

The 'Patent Box' was introduced into UK tax legislation with effect from 1 April 2013. It effectively reduces the rate of corporation tax payable on profits from patents and sales of patented products. The tax savings can be substantial.

The Patent Box complements existing, valuable tax incentives for Research and Development (R&D), by providing further tax incentives for the commercial exploitation of patented products and inventions. In principle, therefore, tax incentives are available for the whole of the innovation lifecycle.

Under this scheme, innovative companies effectively pay tax on their Patent Box profits at just 10%, instead of the main rate of corporation tax of 19% i.e. the tax liability on these profits is almost halved.

KEY FEATURES OF THE PATENT BOX

The Patent Box is a generous incentive. Broadly, the 10% tax rate applies to worldwide profits arising from the exploitation of UK patents, patents granted by the European Patent Office and patents granted by certain other EU member states, or from an exclusive licence over such patent rights.

The 10% tax rate is intended to be available irrespective of how the company exploits its patent rights. Eligible Patent Box profits can arise from:

- sales of patented products;
- sales of products incorporating patented items;
- sales of bespoke spare parts for such products;
- licence fees or royalties for granting rights over patents and other associated IP rights;
- income from the sale of patent rights or exclusive licences over patent rights;
- income received as damages for infringement or alleged infringement of patent rights;
- deemed 'notional royalty' income for patented tools and patented processes used to create non-patented services or products for sale;
- insurance payments in respect of patented products.

WHICH COMPANIES ARE ELIGIBLE?

Despite what you may have heard, the Patent Box is not just a tax break for large pharmaceutical companies; it is not 'sector specific'. All innovative companies generating profits from patents and patented products are eligible, whatever their industry sector.

To qualify for the Patent Box, a company/group must have created or made a significant contribution to the innovation underlying the patent or its commercial application, or to the development of a product incorporating the patented invention.

Special rules apply for groups of companies. In this context, it is important to note that passive patent-holding companies do not qualify for the 10% tax rate.

IMPORTANT POINTS AND OPPORTUNITIES

Some important planning points arise from the details of the Patent Box legislation:

- **The Patent Box is optional and does not apply automatically.**
It must actively be claimed in the company's corporation tax return.
- **Company/group structures can affect the amount of Patent Box tax savings.**
It may be appropriate to review existing corporate structures to ensure that the tax position is optimised.
- **Profits earned in the 'patent pending' period can qualify for the 10% tax rate.**
However, this will require appropriate consideration and action in advance of the patent being granted.

- **Interaction with R&D tax credits**
Some important changes were made to the UK Patent Box from 1 July 2016.

In essence, the new rules tie the Patent Box benefit more closely to underlying R&D expenditure and potentially limit the Patent Box relief for companies which have acquired patents or have subcontracted the underlying R&D to related parties. Companies that are potentially eligible for Patent Box are also required to 'track and trace' their R&D expenditure so that it can be identified with the relevant patent(s).

ACTION TO TAKE

In light of these points, companies that might qualify for the Patent Box are recommended to seek specialist tax advice at the earliest opportunity so that eligibility and appropriate planning may be considered.

It may also be appropriate for companies to revisit their IP protection and exploitation strategies. The potential Patent Box tax savings may offer a further justification for the costs of obtaining patents.

In particular, group companies should consider how the new Patent Box rules could affect them.

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