



Quick summary

- From 1 April 2013 companies who carry out innovation and patent their ideas will benefit from a 10% tax rate on resulting profits (to be phased in over 5 years).
- Any UK company with qualifying intellectual property rights can elect into the regime.
- Companies who currently carry out innovation should seek to optimise their structure in order to maximise the value of the relief when it comes in.

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10% Tax Rate for companies who carry out innovation

In his 2012 Budget speech, the Chancellor confirmed that the government is to go ahead with introducing a new form of tax relief for companies who undertake innovation, to be known as the 'Patent Box'. The regime will provide an opportunity for companies that hold patent interests and use them in the business to significantly reduce their UK tax liabilities. This article briefly sets out the scope of the new rules and the potential benefits.

What are the benefits of Patent Box?

From 1 April 2013 the Patent Box will tax worldwide profits attributable to patents at 10% rather than the standard rate of corporation tax (currently 24%).

Not only will the new rules help companies to reduce their tax liabilities but also allow for more efficient use of losses and other reliefs.

Qualifying criteria

For company to qualify for the lower tax rate it must actively hold patents that have been granted by the UK or European patents offices, and receive income relating to those patents. What constitutes 'holding a patent' is widely drawn and can include partnerships, joint ventures, and other cost sharing arrangements involving patents.

The types of income that will benefit from lower tax rate include:

- Patent royalties and other income from licensing;
- Income from the sale of patents;
- Income from infringements; and
- Income from the sale of products which incorporate a patented invention.

When do the new rules apply?

The government has said that the new regime will come into effect from 1 April 2013. Transitional rules will apply which will mean that the 10% tax rate is phased in over a five-year period.



FIGURE 1
How the rules will work in practice

Patent Box will follow a three stage formulaic approach in order to identify the income which will benefit from the reduced tax rate:

1. Apportion the company's trading profits into qualifying (i.e. patents related) and non-qualifying (i.e. non-patent related) element.
2. Deduct 'routine trading profits' from the non-qualifying element to arrive at a 'residual profit' representing the return the company derives from its innovative activities.
3. Eliminate notional marketing royalties in order to arrive at Patent Box profit.

How will Patent Box profits be calculated?

In essence patents box will use a formulaic approach to calculate the amount of profits which will be subject to the 10% tax rate. A brief summary of the steps involved is shown in Figure 1, above.

The rules are complex and so companies are advised to seek specialist tax advice in order to ensure that they are benefiting fully from the relief.

Optimising the benefits

There are a number of key areas which should be looked at in order to ensure that the benefits of Patent Box are fully realised. These include:

- Identifying which revenues will qualify;
- Tracking revenue streams;
- Optimising internal admin and cost coding structures; and
- Minimising the degree to which patent profits are dependent on marketing royalties.

The new rules are intended to complement the existing R&D reliefs, which companies should also be encouraged to look as part of their overall tax strategy.

How we can help

Forbes Dawson can assist businesses in a number of ways.

Examples of where we can help include:

- Developing 'best practice' methodologies for tracking relevant patent income and expenditure;
- Optimising group structures to fit around the Patent Box rules;
- Identifying areas of the business where there is hidden value in relation to intellectual property;
- Securing clearances from HMRC on a company's claim methodology; and
- Preparing the calculations required by HM Revenue and Customs to be included with the company's tax return, together with supporting documentation.

This is in addition to the services we already offer in relation to R&D relief.

What's next?

Detailed legislation is in the process of being drafted, and we will provide an update on any significant developments.

In the meantime we are already working with clients to assess the potential tax savings. If your company could benefit please contact us for a free consultation.