
Patent Box - an update

Previous rules

Under the previous patent box rules, as long as a UK company owns a UK or European patent (or exclusive rights to that patent), all worldwide sales derived from that patent going into the UK company may be included in the three step patent box calculation:

1. Allocate taxable profits to either a patent box stream or a non-patent box stream
2. Reduce this by an element of normal profit (known as the routine return deduction)
3. Reduce this for an element of profits relating to brand (known as the marketing asset return).

The result is known as Relevant Intellectual Property (IP) Profits to which the reduced patent box tax rate (10%) applies once a company-wide election has been made.

There are detailed eligibility requirements – for example, the company must have made a significant contribution to the creation or development of the patented item or a product incorporating this item.

However, under the previous rules, there is no requirement for a connection to be made between the underlying R&D carried out and the patent itself. Thus, as long as the patent is held by the UK entity, it does not matter where in the world, or by whom, the R&D activities that led to the patent are conducted, provided an active ownership condition is satisfied.

New rules

The basic calculation for patent box retains the same three key steps, but the modified rules will insert an additional calculation.

The new rules are based on a more complex formulae based approach linking relevant R&D expenditure to the patent or patented item.

Impact of new calculation

This new R&D fraction could significantly reduce any patent box benefit for companies who outsource their R&D to other group companies. For example, IP holding companies that manage the IP of the group but do not directly undertake the R&D. Plus, to be able to calculate the new fraction, companies will need to 'track and trace' their R&D spend and map the data to their IP.

Transitional rules and grandfathering

Where a company has elected into the patent box and IP that already exists at (ie the 'priority' date is before) 1 July 2016, it will be able to benefit from the previous rules without applying the modification until 30 June 2021 (when everyone will have to apply the new fraction). However, even under the transitional rules, companies will need to start tracking and tracing their current R&D to their IP in preparation for the new rules.

New IP created after 30 June 2016 (even if the company is already elected into the patent box under the previous rules) may come under the new rules. Some companies may, therefore, be running calculations under both the old and new rules until 30 June 2021 – adding a further layer of complexity.

Checklist to consider

- Does a UK company own UK or EU patents (or exclusive rights to those patents)?
- Has the company incurred relevant R&D expenditure relevant to the developed IP?
- If relevant R&D is incurred by a group company other than the IP owner, could the business be restructured going forward?

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Next Steps

If you think that you may qualify for this relief then we can help. As you can see the rules are quite complex and difficult to navigate. If you wish to discuss the possibility of exercising a claim for Patent Box relief, please do not hesitate to get in touch.

For further information

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