PKF Littlejohn LLP

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Accountants & business advisers

Tax Insights

Patent Box Regime

Have you secured corporate tax relief on your inventions yet?

If you've a patented invention, the Patent Box Regime can help you balance the books. Read on to discover how.

What is the Patent Box Regime?

First introduced in 2013, the Patent Box Regime is a tax incentive designed to enable UK companies to apply for a lower tax rate for profits earned from patented inventions and certain other intellectual property rights.

The Patent Box Regime can reduce the rate of tax on these profits from the main rate of 20% to as low as 10%. However, most qualifying companies will usually enjoy a reduced rate of somewhere between the two.

Why it changed

As a result of complaints from other EU member states, the old regime has been phased out and replaced with a more compliant structure, which began in July 2016.

Although participants under the old regime will continue to benefit under the old rules until their expiry in 2021, the reform offers a new basis to claim the 10% Corporate Tax rate to those with qualifying IP rights.

Do I qualify for Corporate Tax relief?

To benefit from the 10% Corporate Tax relief, you must have qualifying income derived from qualifying patents (broadly, those registered in the UK or EU).

That means you must have made a significant contribution to the invention specified in your patent, or the development of a product incorporating the patent.

This prevents relief being available for patents that are acquired and held passively. There are further rules dealing with changes in ownership of a company that has developed qualifying patents, which could deny relief.

Income qualifying for the regime:

- Licensing and royalty income.
- Sale of patented items (or those that incorporate a patent)
- Infringement income, damages and other compensation

New methods of calculating & streaming

Before the reform, companies were only required to calculate two streams of income: one for IP income and the second for non-IP income.

Under the new regime, it's now necessary to stream every individual IP right or, where appropriate, by patented product or product family.

Although this may add extra administrative work, it won't dilute the patent box benefit in any way.

In terms of calculating IP profits, you'll need to follow a three-stage process:

1. Identify sales income and attributable profits or losses (as above)
2. Remove routine profits
3. Remove the profits attributed to marketing assets

The Nexus Fraction

With the new regime, an additional step known as the 'Nexus Fraction' has to be performed.

This ensures that only profits derived from R&D activities carried out by the company will be allowed in a claim.

The fraction of profits allowed will depend on the level of qualifying and non-qualifying expenditure that is incurred directly by the UK company.

What you should do now

Under the new Patent Box Regime, companies can obtain significant savings over an extended period and feel assured that the current regulations seem here to stay.

To maximise the benefits of the relief available, companies should consider the following matters:

- Whether electing to carry back any existing IP into the old regime would be more favourable than the current regime (the time limit is two years from the end of an accounting period that ended before 1 July 2016)
- Ensure systems can deal with streaming of income and expenditure for each individual patent
- Review group structure to ensure that R&D activities are taking place in the UK company holding the IP and consider restructuring where necessary

Our expert team can help you with the complex rules surrounding the Patent Box Regime.

To find out more, please contact us.

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