EIP

What's in the Patent Box? An update

What is a 'Patent Box'?

The Patent Box is a taxation scheme proposed for the UK. Under the Patent Box scheme companies will be able to apply a 10% rate of corporation tax for net profits arising from patented products. The scheme is intended to apply from 1 April 2013. It is intended to encourage the commercialisation of patents in the UK.

Where are we now?

The Patent Box was initially suggested in 2009 by the previous Labour government. The present coalition Government announced they would be implementing the scheme in their Pre-Budget Report in November 2010. According to the UK Treasury, implementation will consist of three stages:

- Stage 1 – Set out objectives and identify options – implemented as an initial consultation from 29 Nov 10 to 22 Feb 11.
- Stage 2 – Determine the best option and develop a framework for implementation – ongoing consultation from 10 June to 2 September 2011; and
- Stage 3 – Draft legislation to effect the proposed change – proposed for autumn 2011.

Final implementation through legislation will occur before April 2013.

Current Proposals

The second consultation sets out the framework for implementation, building on a first round of consultation with business. A companion scheme of Research and Development tax credits is also proposed.

Qualifying Patents

It is proposed to apply the scheme to patents granted by the UK Intellectual Property Office (UKIPO) and the European Patent Office (EPO).

Supplementary Protection Certificates (SPCs) that extend these patents, regulatory data protection (also called 'data exclusivity') and certain plant variety rights will also be included.

Ownership

Benefits of the Patent Box will be accessible both through legal ownership and through the holding of an exclusive licence. This includes acquired patents although may require further active use criteria as set out below.

Partnerships, joint ventures and cost-sharing arrangements will also be accommodated.

Qualifying Income

The Patent Box will focus on products. The Patent Box will include worldwide income earned by UK businesses from products containing at least one invention covered by a currently valid qualifying patent. For example, it appears to cover worldwide income from a product that is covered by a UK or European patent, regardless of any patents in other jurisdictions. It will also include all royalties or licence fees received for use of an invention covered by a currently valid qualifying patent.

Sales of spare parts for qualifying products and damages in patent litigation may also be included. It is proposed to exclude services from the scheme. Whether spare parts will include consumables and whether products that result from a patented process will be included are subjects of ongoing consultation.

A formulaic approach to calculating qualifying income is set out in the consultation document (see chapters 4 and 5), which may be applied by a suitable accountant.

Active Use

The Government proposes a number of criteria to exclude non-practising entities (so-called 'patent trolls') from the scheme. The company claiming a Patent Box tax deduction must remain actively involved in the ongoing decision making connected with the exploitation of the patent.

How this will be achieved is not yet clear. Two options are proposed: a first based on a proportion of the value of the patent being met by development expenses; or a second based on a judgement in each case. It is likely an approach that is easy to administer will be chosen.

Commencement

To avoid problems determining the date of first commercialisation, it is proposed to phase in the benefit of the scheme, starting with 60% in 2013/14 and increasing to 100% by 2017/18.

By 2017/18 it is estimated the scheme will cost £1.1 billion per year.

It should be noted that the next UK general election will likely be held in spring 2015.

Conclusions

Reviewing the proposals, it is apparent that many actively-patenting companies could benefit from the scheme. Likewise, certain companies that are not actively patenting at the moment may benefit from implementing a patenting strategy. The inclusion of worldwide income and the need for only a single patent on a product make the scheme particularly attractive. To ensure that the qualification criteria apply to their circumstances, companies may wish to take an active role in the consultation process as set out here. It is also worthwhile monitoring the consultation process, so that companies can begin developing a strategy to take full advantage of this tax break.

HM Treasury Press Release