

Thinking in the box – but should it be the UK Patent Box or the Dutch Innovation Box?

11 June 2013

The popularity of patent box regimes is on the rise as countries compete to attract investment. The most recently introduced regime was the April 1 implementation in the UK. Hogan Lovells' tax team compares this new regime with the Netherlands' long-standing Innovation Box.

Who can benefit?

Both the UK and Dutch regimes are only available to corporate investors. In the UK, companies potentially qualify where they own or have a countrywide exclusive licence in respect of certain qualifying intellectual property (IP) rights and, in the case of group companies, either perform a significant amount of management activity in relation to the rights, or have created or developed the patented invention (or a product or process incorporating the patented item).

In the Netherlands, companies will qualify where they own self-developed intangible assets (i) with respect to which a patent is obtained or (ii) that originate from certain R&D activities. Development or further development by the Dutch taxpayer is required, though R&D activities may be outsourced provided the activities are supervised by, and performed for the risk and account of, the Dutch taxpayer.

What IP rights qualify?

The benefit of the UK Patent Box is limited to profits derived from patents granted by the UK Intellectual Property Office, the European Patent Office and certain EEA countries (and certain other medicinal or botanic innovation rights), in respect of which the company holding the rights or a group member has created or developed the patented invention (or a product or process incorporating the patented item).

The scope of the Dutch Innovation Box is, by contrast, wider insofar as the regime extends to profits derived from (i) both foreign and domestic patented intangibles as well as (ii) non-patented intangibles that result from R&D activities with respect to which an R&D statement is obtained from the Ministry of Economic Affairs (R&D intangibles). The regime can, therefore, apply either where it is not possible to apply for a patent (for example when it comes to software and trade secrets) or where there is no intention to make such an application. Any intangible asset can qualify as long as at least 30% of the expected income generated by that asset can be allocated to the patented IP right or R&D intangibles.

How to opt into the regime?

To benefit from the UK Patent Box, a qualifying company must make a one-off election, following which it will remain within the regime until such election is revoked. No new election can be made for five years after revocation.

By comparison, the Dutch Innovation Box applies on a product-by-product basis. Where a company wishes to opt into the innovation box for a specific qualifying intangible asset, it may do so retrospectively in its Dutch corporate income tax return as soon as a qualifying intangible asset starts generating income.

Rate of tax for qualifying income

In the UK, the rate of tax for qualifying income will be 10% once the benefits of the patent box regime have been fully phased in (from April 1 2017), whereas the standard rate of UK corporation tax is 23% (reducing to 20% by April 1 2015).

The headline rate of Dutch corporate tax is 25%, but the Dutch Innovation Box has a significantly lower effective tax rate of 5%, achieved by excluding 80% of the relevant tax base. This rate applies when the qualifying profits are more than a threshold of the recapture amount, which consists of production expenses plus losses in respect of the relevant intangible asset. This recapture occurs if such expenses and losses were previously deducted against the headline tax rate and the taxpayer receives qualifying income in respect of the qualifying intangible asset. This recapture does not, however, take place if the intangible asset is unsuccessful.

What types of IP income qualify?

In the UK, there are four types of “relevant IP income” qualifying for the patent box, broadly:

- (a) income from sales of items that are protected by qualifying IP rights or incorporate items protected by qualifying IP rights (regardless of the relative value of the items incorporated – the “golden screw” principle);
- (b) licence fees/royalties from agreements granting rights in respect of qualifying IP rights;
- (c) income from sales of qualifying IP rights or exclusive licences thereof; and
- (d) damages for infringement and other compensation.

“Notional royalties” calculated on an arm's-length basis may also arise where a company uses a patented process to provide a service.

In the Netherlands, all income and gains in respect of the qualifying intangible assets come within the scope of the innovation box. The only limitation is that the income must be attributable to the patented IP right or R&D Intangibles.

Calculation of IP profits/losses

In the UK, there are two methods for calculating profits. The standard calculation broadly requires the relevant IP income to be expressed as a percentage (X%) of gross income (excluding finance income), followed by a calculation of X% of the profits of the trade, less a 10% routine return and profits relating to marketing assets. The streaming method (usually elective but sometimes mandatory) involves allocation of expenses and profits on a just and reasonable basis, followed by deduction of routine and marketing returns. IP losses can also be generated within the patent box and such losses have to be set off against IP profits.

In the Netherlands, profits and gains must be allocated to the patented IP rights or the R&D Intangibles. This allocation is frequently agreed in advance with the Dutch tax authorities. If, for example, income is allocable to marketing activities this part of the income is regularly taxed at the full rate. IP losses are fully deductible against the headline tax rates (subject to a possible recapture).

The UK Patent Box regime is of potentially wide application and may offer significant tax savings, especially where companies are able to benefit from the "golden screw" principle. The Dutch innovation box also has a number of significant benefits, among others a wider scope and a significantly lower effective tax rate. A tailored review is required to determine which regime would be most beneficial in a specific case.

Karen Hughes (karen.hughes@hoganlovells.com) is a partner and Fiona Bantock (fiona.bantock@hoganlovells.com) is a senior associate of Hogan Lovells, based in London; and Anton Louwinger (anton.louwinger@hoganlovells.com) and Alexander Fortuin (alexander.fortuin@hoganlovells.com) are in the firm's Netherlands offices.

[Back to top](#)

ITR PREMIUM
Corporate · Indirect · Disputes · Compliance

ITR PREMIUM
Corporate · Indirect · Disputes · Compliance

ITR PREMIUM
Corporate · Indirect · Disputes · Compliance