

Abolition of income tax relief for patent royalties

Who is likely to be affected?

Individuals and other persons subject to income tax rules who claim relief for payments of patent royalties.

General description of the measure

The measure will introduce legislation to abolish the relief for payments of patent royalties.

Policy objective

This measure will support fairness in the tax system by protecting the Exchequer from potential loss of tax as a result of avoidance arrangements exploiting the relief. It will support HM Revenue & Customs' (HMRC) anti-avoidance strategy to protect revenues and deter and counter tax avoidance.

Background to the measure

The measure was announced on 5 December 2012.

Detailed proposal

Operative date

The measure will have effect for payments made on or after 5 December 2012.

Current law

Payments of patent royalties by individuals and other persons are relievable against other income of the same year in accordance with Chapter 4 of Part 8 of the Income Tax Act (ITA) 2007. The relief applies only to payments which are not deducted in calculating income tax liability from any source (for example, a trade).

Proposed revisions

Legislation will be introduced in Finance Bill 2013 to amend Part 8 of ITA to abolish the relief.

Summary of impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
	negligible	negligible	negligible	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2013. This measure supports the Exchequer in its commitment to protect revenue.					
Economic impact	The measure is not expected to have any significant economic impacts.					
Impact on individuals and households	The proposed change will impact only a small number of individuals and households who pay patent royalties other than as part of a trade or profession. The amount of additional administrative burden is thought to be negligible.					
Equalities impacts	The proposed change is not expected to have a disproportionate impact on any protected equality groups.					
Impact on business including civil society organisations	<p>The measure is expected to impact on a handful of businesses that market avoidance and tax planning arrangements exploiting the relief, by closing such opportunities.</p> <p>The businesses will need to understand the effect of the changes to advise the small number of their clients that may be affected, but the Government believes that the change will not otherwise impact on their business operation.</p> <p>Overall, the impact to business and civil society organisations is expected to be negligible.</p>					
Operational impact (£m) (HMRC or other)	It is not anticipated that implementing this change will incur any significant additional costs or savings for HMRC or other public sector delivery organisation.					
Other impacts	<p><u>Small firms impact test:</u> Small firms are unlikely to be affected as patent royalties paid as part of a trade are deductible in computing the profits of that trade.</p> <p>Other impacts have been considered and none have been identified.</p>					

Monitoring and evaluation

HMRC will monitor income tax returns and avoidance disclosures to ensure that the legislation operates as intended.

Further advice

If you have any questions about this change, please contact Judith Diamond on 020 7147 3422 (email: judith.diamond@hmrc.gsi.gov.uk).

1 Abolition of income tax relief for patent royalties

- (1) Chapter 4 of Part 8 of ITA 2007 (reliefs: annual payments and patent royalties) is amended in accordance with subsections (2) and (3).
- (2) In section 448 (relief for individuals), in subsection (1)(b) omit “or 903(5)” and “and patent royalties”.
- (3) In section 449 (relief for other persons), in subsection (1)(b) omit “or 903(6)” and “and patent royalties”.
- (4) Accordingly, that Act is amended as follows –
 - (a) in section 2 (overview of Act), in subsection (8)(c) omit “and patent royalties”,
 - (b) in section 24 (reliefs deductible at Step 2), in subsection (1)(b) omit “and patent royalties”, and
 - (c) in the heading for Chapter 4 of Part 8 of that Act omit “AND PATENT ROYALTIES”.
- (5) The amendments made by this section have effect in relation to payments made on or after 5 December 2012.

EXPLANATORY NOTE

ABOLITION OF INCOME TAX RELIEF FOR PATENT ROYALTIES

SUMMARY

1. This clause abolishes income tax relief for certain payments of patent royalties.

DETAILS OF THE CLAUSE

2. Subsection 1 provides that subsections (2) and (3) amend Chapter 4 of Part 8 of ITA 2007 (ITA) which provides income tax relief for payments of patent royalties.
3. Subsection 2 amends section 448(1)(b) ITA by removing the reference to section 903(5) ITA and the words ‘and patent royalties’. Section 903(5) ITA contains the requirement for individuals to deduct an amount representing basic rate income tax from payments of patent royalties. By removing these references the subsection has the effect of abolishing the relief for payments of patent royalties made by individuals.
4. Subsection 3 similarly amends section 449(1)(b) ITA by removing the reference to section 903(6) and the words ‘and patent royalties’. Section 903(6) contains the requirement for persons other than individuals to deduct an amount representing basic rate income tax from payments of patent royalties. By removing these references the subsection has the effect of abolishing the relief for payments of patent royalties made by other persons such as trustees, personal representatives and non-resident companies within the charge to income tax.
5. Subsection 4 makes consequential amendments to ITA to remove redundant references to patent royalties.
6. Subsection 5 commences the provision from 5 December 2012. Relief will therefore not be available for payments of patent royalties made on or after that date.

BACKGROUND NOTE

7. The relief which is abolished relates only to payments of patent royalties which are not deductible in calculating income from any source, such as trading. Where patent royalties are deductible in calculating income from any source they will continue to be relieved in that way.
8. The relief is being abolished to counter known avoidance and to simplify the income tax code.