Support for research and innovation: The Patent Box

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Patent Box

• Reduces corporation tax rate from 28% to 10% for the income from patents

• Very few details at this stage
  – Apply to income from patents granted after April 2013
  – There will be consultation before introduction in the 2011 Finance Bill
  – Treasury estimate revenue cost at £1.3bn

• Stated aim of the policy: “strengthen the incentives to invest in innovative industries and ensure the UK remains an attractive location for innovation”
Why Government supports innovation

• Market failures:
  
  – External benefits: ideas are difficult to own; others benefit from results without bearing costs. As a result the market provides insufficient incentives for investment
  
  – Financial market failures: difficult to secure external finance for risky and intangible projects

• These market failures are largest in the area of basic science

• Without market failures it is not clear why government should intervene
Well targeted policy?

- Policy targets income from ideas, not the activity that generates new ideas
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- Income is a function of both the quality of the idea and the market power of the firm
Increased incentives to invest in innovation?

- Large time lag between a new idea and the income stream from patents
  - Small incentives for marginal projects
  - No affect on financial constraints

- Increased development & commercialisation activities to create more income
  - Low external benefits

- Will the UK be a ‘more attractive location’?
  - Incentives to locate the income from patents in the UK
  - Unlikely that the research underlying eligible patents will need to have been conducted in the UK
Who will benefit?

- In theory all firms which create income from patents

- In practice a few large firms hold the majority of patents
  - In 2005, of all the patent applications filed by UK headquartered firms to the European Patent Office, the 4 largest firms accounted for over a fifth
  - Likely that these firms are also most able to create large income streams
Costs

• Large deadweight costs
  – Subsidising activity that would have happened already
  – Firms attributing more income to patents

• Cost in forgone revenue: Treasury estimate £1.3bn
  – Coming at a time of large cuts elsewhere, including to science and research and higher education budgets