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HMRC internal manual

Corporate Intangibles Research and Development Manual

From: [HM Revenue & Customs](#)
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CIRD275500 - Patent Box: using the Value Fraction in exceptional circumstances CTA10/s357BLH(3)

Patent Box: new regime: When the R&D fraction is considered to be incorrect (using the 'Value fraction' in exceptional circumstances)

s357 BLH (3) CTA 2010.

There is an alternative approach to calculating a company's Research and Development fraction (R&D fraction) which a company can elect to apply

in exceptional circumstances. The R&D fraction is increased to a figure which represents a just and reasonable assessment. This is known as the Value fraction. It works by allowing a company to increase the normal R&D fraction where the original calculation is not commensurate with the contribution level of the taxpayer to the R&D activity. In other words, where the R&D fraction of a taxpayer does not reflect the true value in their intellectual property which has been derived from their own or third party subcontracted R&D activity. (This is referred to in the OECD guidelines as the 'rebuttable presumption' ie it is presumed that the R&D fraction, as defined at [CIRD274200](https://www.gov.uk/hmrc-internal-manuals/cird274200) (<https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird274200>) gives a true figure for the company's contribution to the IP but this presumption can be rebutted if that is not in fact correct. This term does not actually occur in the legislation but is in common use).

Exceptional circumstances could include, for instance, a complete or partial write down of acquired IP in the company's financial statements or other instances of an exceptional nature where a company can demonstrate that it engaged in greater value creating activity than is reflected in the R&D fraction such as where there has been loss or damage to equipment or data meaning that work needed to be contracted out.

It is generally expected to be an unforeseen circumstance. HMRC would not reject an application just because the circumstances are foreseeable – there might be other factors – but if the circumstances are foreseeable, it might be harder to establish that they are exceptional.

Because the value fraction only applies in exceptional circumstances, it will generally only be appropriate to apply it to one, or possibly to a few, sub-streams.

How does a company qualify to use the value fraction?

Before a company can elect to use the value fraction it must meet, at a minimum, the following requirements:

- The company first uses the R&D fraction to establish the presumed amount of income that could qualify for tax benefits.
- The R&D fraction as described in [CIRD274200 \(https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird274200\)](https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird274200) must equal or exceeds 0.325 (when converted to a decimal). This is because the R&D fraction must be at least $\frac{1}{4}$ (or 25%) before the 1.3% uplift before the Value fraction can be considered. The Value fraction must represent, on a just and reasonable basis, the proportion of the value of the relevant qualifying IP rights which is properly attributable to R&D undertaken at any time by the company itself or on its behalf by persons not connected.
- The company must be able to demonstrate that because of exceptional circumstances the application of the R&D fraction would result in an outcome that was inconsistent with the principle of the OECD approach. For example, the company could provide evidence such as valuations of the devalued acquisition, or other specific examples of what has happened.

How to make an election to apply the Value fraction rather than the R&D fraction.

If a company believes that it qualifies for the Value Fraction then it may elect for this treatment. An election can be made in writing as part of the Corporation Tax computation. There is no need to notify HMRC in advance of completing a company return. The company must make an election to HMRC on or before the last day where an amendment to the company's tax return could be made under paragraph 15 of Schedule 18, FA1998 (usually 2 years). The election should also be included in the company's corporation tax computation and subjected to iXBRL tagging.

In electing to apply the value fraction rather than the normal R&D fraction, the company is, in its self-assessment, asserting that this is the correct figure to use as part of its computation of tax and should provide robust documented evidence that demonstrate the effective of the R&D fraction and the level of substantial activity

Reporting to the OECD

- In all circumstances HMRC is required to make an annual anonymous aggregate report of the number of companies electing to use the Value fraction to the Organisation for Economic Co-operation and Development (OECD), as well as to complete an Exchange of Information with the relevant overseas country. This information is to be shared under the spontaneous Exchange of Information agreement with the Group parent's country of residence if not in the UK.

HMRC will therefore always consider whether the reasons behind the use of the Value fraction and may ask for additional information to support its use.

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