

Topic review: intangibles for companies

(Lecture B1142 – 17.43 minutes)

The treatment of intangibles by companies has seen several changes over the past few years especially in relation to goodwill and other customer related assets. This summary reviews the areas that have changed and also looks at some aspects of the intangible legislation where queries can arise.

Types of intangibles

The legislation defines an intangible asset as having the meaning that it has for accounting purposes and including internally-generated intangible assets and intellectual property.

'Intellectual property' is then specifically defined to mean any:

- patent, trade mark, registered design, copyright or design right, plant breeders' rights or rights under section 7 of the Plant Varieties Act 1997;
- right under the law of a country or territory outside the United Kingdom corresponding or similar to a right within the above bullet;
- information or technique not protected by a right within the first two bullets but having industrial, commercial or other economic value, or
- licence or other right in respect of anything within the preceding bullets.

Goodwill, including internally generated goodwill, is also included within the definition of intangibles but then the legislation notes that this is subject to any indication to the contrary – these contrary indications are set out in more detail below.

Accounting for intangibles

As the legislation is based on the treatment of intangible assets in the accounts of the company it is worth looking at the accounting treatment of intangibles under different accounting standards.

There are essentially three broad categories of intangible assets:

- those that are separately acquired;
- those that are internally generated, and
- those that are acquired as part of the acquisition of a business combination (which include goodwill).

Intangibles that are separately acquired will generally satisfy the recognition tests in UK and international accounting standards and will be recognised at cost.

Internally generated intangibles cannot be recognised as assets under FRS 105 and only in limited circumstances under FRS 102 and international accounting standards.

The last category, intangible assets acquired as apart of a business combination are included in the goodwill arising on acquisition under FRS 105. FRS 102 and international accounting standards allow their separate recognition where the fair values can be measured with sufficient reliability and then they are recognised at fair value.

Negative goodwill, that is where the fair value of the assets and liabilities acquired on a business combination is greater than the cost of the acquisition is recognised as a credit on the balance sheet under FRS 102 and FRS 105 but under international accounting standards it is credited to profit and loss.

It is important therefore on a business combination to ensure that the breakdown of intangible assets is fully reviewed to establish any that can be recognised separately from goodwill. If these assets are not restricted under the rules for goodwill and other customer related assets, then relief for any amortisation may be available.

Partnerships and intangibles

Another area where the accounting can have an impact on the treatment of intangibles is for partnerships. The corporate intangible regime does not have specific rules on partnerships that hold intangibles but on general principles it would be assumed that the look through approach would be taken to determine the profits and losses to be apportioned to a corporate partner.

However, the accounting treatment can impact on this as the company accounts may show the holding in the partnership as an investment (as in the case of an LLP) rather than the company's share of the underlying assets including intangible assets. In *Armajaro Holdings Ltd* [2013] UKFTT 571 (TC) it was found as the company showed the holding in the partnership as an investment it was not entitled to a deduction for the amortisation.

For a discussion of the treatment of partnerships and intangibles see 'Encountering intangibles: some practical suggestions' by Gregory Price in Tax Journal 16 May 2018.

Goodwill and customer related assets – restrictions on debits

When the corporate intangible regime was first introduced in 2002 there was no restriction on the debits relating to goodwill and other customer related intangibles. However, HMRC felt that the regime was too generous to allow relief for goodwill in the company following incorporation of a sole trade or partnership together with entrepreneur's relief on the incorporation gain at 10% so they introduced restrictions on the debits allowed.

Specific types of assets are covered and these are:

- goodwill in a business or part of a business;
- information which relates to customers or potential customers of a business or part of a business;
- a relationship (whether contractual or not) between a person carrying on a business and one or more customers of that business or part of that business;
- an unregistered trademark or other sign used in the course of a business;
- a licence or other right in respect of any of the above assets.

The restrictions have changed over time and are summarised in the table below.

Date	Summary of treatment of goodwill and other customer related assets
Acquired or created on or after 1 April 2019	Relief only available if acquisition includes qualifying intellectual property (IP), fixed at 6.5%, restricted to 6 x qualifying IP acquired
Acquired or created on or after 8 July 2015 and before 1 April 2019	No relief under the post 2019 rules if acquisition between 8 July 2015 to 31 March 2019
Acquired or created on or after 3 December 2014 and before 8 July 2015	No relief where the acquisition was from a related individual or partnership
Acquired on or after 1 April 2002 and before 3 December 2014	Relief for debits in relation to the assets or at fixed rate if election made

So, when the intangible asset is acquired is key to the tax treatment for debits along with who the acquisition was from i.e. a related or a third party. The debits are not lost altogether but will only be available as non-trading debits on realisation of the asset.

In summary the rules for current acquisitions are that relief is at a fixed rate of 6.5% of the cost of the asset and the amount of relief may be partially restricted if the expenditure on qualifying IP multiplied by six is less than the expenditure on goodwill or customer-related asset.

Qualifying IP assets means a:

- patent
- registered design
- copyright or design right
- plant breeders' right
- right under

If goodwill or a customer-related intangible asset is transferred to the company, on or after 1 April 2019, from a related individual or from a partnership where a partner is related to the company, then relief is only available if that asset was acquired in a third party acquisition by the transferor and is transferred to the company along with the business.

The relief is again at a fixed rate of 6.5% and will only be available when there is a business acquisition that includes the acquisition of qualifying IP. The relief may be proportionately restricted to the notional accounting value of the goodwill or customer-related asset. Interestingly as detailed above FRS 105 does not allow the recognition of separate intangibles so the accounting treatment may be relevant here.

Acquisition or creation of goodwill

As a general rule, an intangible asset is treated as acquired or created on or after 1 April 2002 to the extent that expenditure on its acquisition or creation is incurred on or after that date.

The most notable exception to the general rule on when an asset is created or acquired relates to goodwill.

The general rule continues to apply in the following situations:

- where the goodwill is acquired by a company on or after 1 April 2002 from a person that is not a related party in relation to the company;
- where the goodwill is acquired by a company from a person that is a related party but is also a company, in respect of which the goodwill is goodwill that is already within the corporate intangible regime; and
- where the goodwill is acquired by a company from an intermediate person, who acquired it on or after 1 April 2002 from a qualifying third person.

In any other circumstances it will be necessary to consider when the goodwill was created; either by the company itself or by a related party from whom the company acquires the goodwill.

Where the business to which the goodwill relates was carried on, either by the company concerned or a related party (considered at the time the goodwill is acquired by the company), at any time before 1 April 2002, it is deemed to have been created before 1 April 2002. In any other situation it is deemed to have been created on or after 1 April 2002.

Although the intangible rules have been in place for a long time now this is always an area to watch on incorporation of a business and also any subsequent sale of the company as pre-2002 goodwill will fall within the rules for chargeable assets.

De-grouping changes on intangibles

There were also some recent changes to the de-grouping rules for intangibles. Where a company ceases to be a member of a group on or after 7 November 2018, a degrouping charge will not arise where the company leaves the group as a result of a share disposal by another company where that share disposal qualifies for the substantial shareholding exemption (SSE). This is as long as the disposal of share is not an arrangement under which the recipient is to dispose of the shares to another person.

The treatment of intangible assets when a degrouping charge arises as a result of a share disposal is therefore now similar to the treatment of assets under the chargeable gains regime but the difference is that with chargeable gains assets the degrouping charge accrues but can be relieved by available exemptions and reliefs such as SSE. The company acquiring the asset therefore effectively realises a market value uplift without a tax charge. The treatment for intangible assets is that the deemed realisation and reacquisition at market value is viewed as having not taken place and the transfer of the asset remains on a tax neutral basis.

For an examination of intangible assets and hive downs see 'Hive downs' by James Tryfonos in Tax Adviser on 1 May 2019.

Contributed by Joanne Houghton