CHAPTER 16

INTANGIBLE FIXED ASSETS

This chapter outlines the tax treatment of IFAs looking at:
- trade v non-trading IFAs;
- relief for losses on non-trade IFAs;
- disposal of IFAs and rollover relief on disposal;
- special rules for groups;
- related parties;
- anti-avoidance and "existing assets";
- profits from patents.

16.1 Introduction

The rules for IFAs held by companies changed on 1 April 2002. For IFAs acquired or created since that date, the tax treatment follows the accounting treatment (subject to certain exceptions).

16.2 Intangible Fixed Assets

The term “Intangible Fixed Asset” has the same meaning as it has for accounting purposes. In particular it includes intellectual property which means any patent, registered trademark, design or copyright etc. It also includes goodwill, again as defined for accounting purposes. CTA 2009, s.712 & 713; CTA 2009, s.715

IFAs include fungible assets. A fungible asset is defined as an asset which can be dealt in without identifying the particular assets involved. An example would be a milk quota in the dairy farming industry. Fungible assets of the same kind (e.g. successive acquisitions of milk quotas) held by the same person in the same capacity are treated as indistinguishable parts of a single asset. CTA 2009, s.858

Certain assets are expressly excluded from the provisions. Where an asset is excluded, an option or other right to acquire or dispose of such an asset is also excluded. CTA 2009, s.801

Assets entirely excluded include: CTA 2009, ss.803–809
- rights over tangible assets,
- oil licences,
- financial assets,
- rights in companies, trusts etc, and
- assets held for non commercial purposes etc.

Assets excluded except in respect of royalties include: CTA 2009, ss.810–813
- assets held for any mutual trade or business,
• film and sound recordings, and
• computer software treated as part of the cost of the related hardware.

Assets excluded from the provisions to the extent specified are:

• those that represent research and development expenditure – as these costs are subject to special R&D provisions, and CTA 2009, s.814
• If the company so elects, capital expenditure on computer software – an election would mean that amortisation would be disallowed; however it enables the company to claim capital allowances instead. CTA 2009, s.815

16.3 Trade and Non-Trade IFAs

It is important to classify IFAs according to whether they relate to a trade, a property business, or are non-trading.

Trading expenses (debits) and income (credits) form part of trade profits as they are accrued to the profit and loss account. CTA 2009, s.747

Expenses and income relating to a property business are treated as part of the profit of that property business. CTA 2009, s.748

Non-trading expenses and income are pooled. If the non-trading income exceeds non-trading expenses then there is a non-trading gain (IFA). CTA 2009, s.751

If non-trading expenses exceed non-trading income then there is a non-trading loss on IFAs.

16.4 Relief for Non-Trading Loss on IFAs

A claim can be made to set the whole or part of the non-trading loss on IFAs against the company’s total profits for that period. The company has two years from the end of the loss making chargeable accounting period to make this claim. CTA 2009, s.753

To the extent that the loss has not been used in a current year claim, it will be carried forward as a non-trading debit (expense) to the next accounting period. In other words, it is offset against non-trading IFA credits (income) of the following year. If a net non-trading loss arises in this later year then this is dealt with as above (set off against total profits).

16.5 Impact on Tax Computations

Royalty payments and receipts are accounted for on an accruals basis. Their treatment will depend on whether the assets are used or held for trade purposes or not. CTA 2009, ss.721 – 728

Patent and copyright royalties are paid gross between UK companies. Remember that all figures that appear in the tax computation must be gross figures.

For goodwill purchased and other IFA assets acquired or created on or after 1 April 2002, the company is allowed a deduction for the amortisation or impairment charged in the accounts. Alternatively it can claim a straight line deduction of 4% on cost. CTA 2009, s.729; CTA 2009, s.730
International Accounting Standard No 38 (IAS 38) does not allow a company to amortise goodwill; therefore goodwill will be stated in the balance sheet at fair value and subject to an annual impairment review.

When a company first adopts IAS 38 it may be required to increase the carrying value of goodwill. The amount of the increase will be a taxable credit (income), but this is restricted to the amount of debits taken against profits in previous periods in relation to the goodwill. CTA 2009, s.872

If the full amount of the increase was not taxable, the carrying value plus the taxable credit becomes the tax written down value for tax purposes. Future impairments will be deductible based on the tax written down value rather than the accounting value. CTA 2009, s.873

16.6 Realisation of IFAs

Realisations of assets result in income gains or losses. However, rollover relief may be available. CTA 2009, s.733

A realisation is defined as any transaction resulting in, in accordance with generally accepted accounting practice: CTA 2009, s.734

i. the asset ceasing to be recognised in the company's balance sheet; or

ii. a reduction in the accounting value of the asset, usually where part of the asset is sold or otherwise realised.

Transaction is defined as including any event giving rise to a gain recognised for accounting purposes.

Proceeds of realisation are those recognised for accounts purposes less incidental costs of realisation. CTA 2009, s.739

Where an asset has been written down for tax purposes the gain is the difference between the proceeds and the TWDV. If no amounts have been written off for tax then the full cost may be brought in. CTA 2009, ss.735 – 736

In the case of a part realisation the amount deducted is adjusted pro rata to the accounting value attributable to the realisation and the accounting value before realisation. CTA 2009, s.737

We use the following formula:

\[
\text{Cost or TWDV before realisation} \times \frac{\text{Reduction in Accounting Value}}{\text{Previous Accounting Value}}
\]

Reduction in accounting value is the difference between the accounting value immediately before the realisation and that immediately after the realisation.

Previous accounting value is the accounting value immediately before the realisation.
Illustration 1

An intangible fixed asset has a book value of £2,200. It is partly realised for £1,650. The book value of the retained part is £825. The amount written off for accounting purposes is then £1,375. The tax written down value is £1,800.

Calculate the accounting profit and adjustment required.

The profit on disposal per the accounts would be:

```
<table>
<thead>
<tr>
<th></th>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds</td>
<td>1,650</td>
</tr>
<tr>
<td>Net Book Value sold (2,200 – 825)</td>
<td>(1,375)</td>
</tr>
<tr>
<td>Accounting profit</td>
<td>275</td>
</tr>
</tbody>
</table>
```

The taxable profit on disposal is calculated as:

```
<table>
<thead>
<tr>
<th></th>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds</td>
<td>1,650</td>
</tr>
<tr>
<td>TWDV sold (1,800 × 1,375/2,200)</td>
<td>(1,125)</td>
</tr>
<tr>
<td>Taxable credit</td>
<td>525</td>
</tr>
</tbody>
</table>
```

Therefore, the profit shown in the accounts will need to be increased by £525 – £275 = £250 for tax purposes.

16.7 Rollover Relief for IFAs

As we have seen, if an IFA is sold then any gain arising will be an income gain.

Illustration 2

A Ltd purchased goodwill from an unrelated party on 1 May 2014 for £250,000 and sold it for £300,000 on 1 January 2015. Its year end is 31 December.

The amortisation charged in the accounting period to 31 December 2014 in the accounts is £15,000. This would have been deductible for tax purposes.

The written down value of the goodwill for tax and accounting purposes as at 1 January 2015 is:

```
<table>
<thead>
<tr>
<th></th>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>250,000</td>
</tr>
<tr>
<td>Less: Amortisation to date</td>
<td>(15,000)</td>
</tr>
<tr>
<td></td>
<td>235,000</td>
</tr>
</tbody>
</table>
```

The sale takes place in the accounting period ended 31 December 2015 and the income gain will be:

```
<table>
<thead>
<tr>
<th></th>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds of sale</td>
<td>300,000</td>
</tr>
<tr>
<td>Less: WDV</td>
<td>(235,000)</td>
</tr>
<tr>
<td>Income gain</td>
<td>65,000</td>
</tr>
</tbody>
</table>
```

Where a company reinvests the proceeds of sale in another IFA it can claim rollover relief. The proceeds need to be reinvested in the period 12 months before to 36 months after the sale of the old IFA. CTA 2009, ss.755 – 758
Illustration 3

Continuing the illustration of A Ltd. The company buys a business from an unrelated party with goodwill worth £400,000.

The amount rolled over will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds reinvested in new asset (goodwill)</td>
<td>£300,000</td>
</tr>
<tr>
<td>Less: Cost of original asset (goodwill)</td>
<td>(£250,000)</td>
</tr>
<tr>
<td>Amount rolled over</td>
<td>£50,000</td>
</tr>
</tbody>
</table>

Note that we use the original cost in this calculation, not the WDV.

Income gain | £65,000 |
Less: Amount rolled over | (£50,000) |
Taxable gain (IFA) | £15,000 |

A claim for rollover relief can be made to reduce the income gain in the Profit and Loss account by £50,000, leaving a credit in its tax computation of £15,000. This credit represents a reversal of the amortisation charged to date.

The cost for tax purposes of the new goodwill going forward will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of new IFA</td>
<td>£400,000</td>
</tr>
<tr>
<td>Less: Income gain rolled over</td>
<td>(£50,000)</td>
</tr>
<tr>
<td>Cost for tax purposes</td>
<td>£350,000</td>
</tr>
</tbody>
</table>

The effect of the rollover is to reduce the cost of the IFA for tax purposes. This will have the effect of reducing the deductible amortisation or impairments in future years, and increasing the income gain on realisation. Hence we are just deferring the income gain to a later year.

In the illustration above, the cost of the asset for accounts purposes is £400,000. If this asset is amortised over 10 years the debit would be £40,000 per year. However, the cost for tax purposes is only £350,000, so the amortisation for tax purposes (the IFA debit) will only be £35,000 per year. In the tax computation £5,000 must be added back each year so over 10 years an extra £50,000 is taxable, which is the income gain deferred. CTA 2009, s.729

If only part of the proceeds are reinvested, the amount available for rollover is the amount by which the proceeds reinvested exceeds the cost of the old asset. CTA 2009, s.758(3)

Illustration 4

Assume A Ltd above decides to reinvest only £270,000.

Calculate how much relief would be available and the cost of the new asset going forward.

The amount rolled over will again be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount reinvested in new asset</td>
<td>£270,000</td>
</tr>
<tr>
<td>Less: Cost of old asset</td>
<td>(£250,000)</td>
</tr>
<tr>
<td>Amount rolled over</td>
<td>£20,000</td>
</tr>
</tbody>
</table>
The taxable income gain for the year will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income gain</td>
<td>65,000</td>
</tr>
<tr>
<td>Less: Amount rolled over</td>
<td>(20,000)</td>
</tr>
<tr>
<td>Taxable gain (IFA)</td>
<td>45,000</td>
</tr>
</tbody>
</table>

The cost for tax purposes of the new asset going forward will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of new IFA</td>
<td>270,000</td>
</tr>
<tr>
<td>Less: Income gain rolled over</td>
<td>(20,000)</td>
</tr>
<tr>
<td>Cost for tax purposes</td>
<td>250,000</td>
</tr>
</tbody>
</table>

**Pre-2002 asset rolled over into IFA**

Special rules apply where the asset sold was acquired or created before 1 April 2002. IFAs that existed before this date stay within the capital gains tax regime; however, they **do not stay within the capital gains tax rollover relief rules**.

On disposal, the asset will give rise to a capital gain which can be rolled over under the new rules in relation to intangible fixed assets.

This is achieved by making certain amendments to the rollover provisions that we looked at above. CTA 2009, s.898

As with the realisation of IFAs, to establish whether the **full proceeds** of disposal of a pre-2002 IFA **have been reinvested**, we compare **net proceeds** to the cost of the new asset. CTA 2009, s.898

If there is **full reinvestment** on realisation of an IFA, we have seen that the amount of the income gain that can be rolled over on realisation of an IFA is the **proceeds compared to the cost** of the acquired IFA.

On disposal of a **pre-2002 IFA**, the amount of the capital gain that can be rolled over is the **net proceeds less** the difference between net proceeds and the chargeable gain i.e. the **indexed cost**. CTA 2009, s.898 & s.758(2)

If there is **not full reinvestment**, the amount of the income gain that can be rolled over on realisation of an IFA is the **cost of acquisition of the new IFA compared to the cost of the IFA that has been sold**.

If the IFA being disposed of is a **pre-2002 IFA**, the only difference is that we compare the cost of the new IFA to the **indexed cost of the pre-2002 IFA**. CTA 2009, s.898 & s.758(3)

**Illustration 5**

X Ltd sells goodwill it has held since December 1991 for £300,000, paying solicitors’ fees of £30,000 in relation to the sale. The goodwill originally cost £55,000. Indexation allowance is 20%. X Ltd is considering the following investments in a new IFA:

a. £280,000
b. £220,000
The gain arising will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds</td>
<td>£300,000</td>
</tr>
<tr>
<td>Less: Expenses</td>
<td>(30,000)</td>
</tr>
<tr>
<td>Net proceeds</td>
<td>£270,000</td>
</tr>
<tr>
<td>Less: Cost</td>
<td>(55,000)</td>
</tr>
<tr>
<td>Net proceeds</td>
<td>£215,000</td>
</tr>
<tr>
<td>IA (55,000 × 20%)</td>
<td>(11,000)</td>
</tr>
<tr>
<td>Chargeable gain</td>
<td>£204,000</td>
</tr>
</tbody>
</table>

**Option a)**

There is full reinvestment as the new asset costs £280,000 which is higher than the net proceeds on realisation of £270,000.

The capital gain which can be rolled over is calculated as:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net proceeds</td>
<td>£270,000</td>
</tr>
<tr>
<td>Less: Indexed cost (55,000 + 11,000)</td>
<td>(66,000)</td>
</tr>
<tr>
<td></td>
<td>£204,000</td>
</tr>
</tbody>
</table>

The full gain is rolled over.

The TWDV for IFA purposes of the new asset is £280,000 – 204,000 = £76,000, which as before, will give lower amortisation and impairments and a higher income gain on realisation in future years.

**Option b)**

There is not full reinvestment as the new asset only costs £220,000.

The capital gain which can be rolled over is calculated as:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of new IFA</td>
<td>£220,000</td>
</tr>
<tr>
<td>Less: Indexed cost (55,000 + 11,000)</td>
<td>(66,000)</td>
</tr>
<tr>
<td></td>
<td>£154,000</td>
</tr>
</tbody>
</table>

The remaining gain (204,000 – 154,000) of £50,000 is taxable in the year of disposal.

The TWDV of the new asset going forward is £220,000 – 154,000 = £66,000.

### 16.8 Groups

For IFA purposes, groups are essentially the same as those defined for capital gains purposes. [CTA 2009, s.765 & 766](https://www.legislation.gov.uk/pacts/uk/ta/2009/cta/765) Transfers of IFAs within a group are tax-neutral, provided that the asset is a chargeable IFA before and after the transfer. [CTA 2009, s.775](https://www.legislation.gov.uk/pacts/uk/ta/2009/cta/775)

**Rollover relief is available on a group wide basis** provided that the company that buys the new asset is within the same group at the time of purchase and is not a dual resident investment company. In addition the new asset must be bought from outside the group. [CTA 2009, s.777](https://www.legislation.gov.uk/pacts/uk/ta/2009/cta/777)

Rollover relief is also available where a company acquires a controlling interest in another company and as a result the company joins the gains group, and that
company holds IFAs. For the purposes of a rollover claim the purchasing company is treated as buying the underlying IFA at the lower of: CTA 2009, ss.778 & 779

- tax written down value of the IFA, and
- cost of the controlling interest.

The purchasing company can make a rollover claim provided it and the company with the underlying IFA sign the claim. As a result the TWDV of the underlying asset will be written down to the extent of the claim.

16.9 Companies Leaving a Group

Where a company leaves a group within six years of an IFA intra-group transfer and still holds the IFA, it is treated as having sold and repurchased the IFA at market value on the date of the transfer. The resulting debit or credit will be treated as arising to the transferee company immediately before it leaves the group. CTA 2009, s.780

There is an exception to the degrouping charge if the transferor and transferee were part of the same subgroup at the time that the asset was transferred and leave the group at the same time. CTA 2009, s.783

A degrouping charge can also be rolled over if the company reinvests in a new IFA within 12 months before and 3 years after the degrouping charge arises, which is the date the company leaves the group. The re-allocated charge can also be rolled over if the relevant conditions are met. CTA 2009, s.791

Where a degrouping charge arises the company about to leave the group together with another group member can jointly elect to treat the degrouping charge or any part of it as arising in that other group company. The gain will be treated as a non-trade credit arising in that other company immediately before the first company leaves the group. CTA 2009, s.792

Payments within the group in relation to rollover or degrouping charges are not taxable so long as they do not exceed the amount of the relief. CTA 2009, s.799

16.10 Related Parties

For IFA purposes, a person (A) is related to a company (B) if: CTA 2009, s.835

- A is a company and controls, or holds a major interest in, B,
- A is a company and B controls, or holds a major interest in, A,
- A is a company, and A and B are under the control of the same person,
- B is a close company, and A is a participator or the associate of a participator in B, or
- B is a close company, and A is a participator in another company that has control or holds a major interest in B.

Control means the power to ensure that the company's affairs are conducted in accordance with your wishes. CTA 2009, s.836
Major interest is where A and one other person together control B, and each hold at least 40%. CTA 2009, s.837

If parties are related, there are several rules that apply:

1. The transfer of an IFA between them is treated as taking place at market value. CTA 2009, s.845

   Note that this rule is overridden if the transfer takes place within a gains group. CTA 2009, s.848

2. Relief is restricted in respect of goodwill and certain assets linked with goodwill where the assets are acquired from an individual who is a related party (see below). CTA 2009, s.849D

3. Rollover relief cannot be claimed if an IFA is partly realised and an interest in it is acquired by a related party. CTA 2009, s.850

4. If a royalty payable to a related party has not been paid within 12 months of the end of the accounting period, and the royalty receivable has not been charged to corporation tax, the royalty is not deductible until it has been paid. This would happen if the recipient was an individual or a non-resident company. CTA 2009, s.851

Note also that transactions with related parties cannot turn pre-FA2002 IFAs into new IFAs. A pre-FA2002 IFA acquired from a related party will continue to be a capital asset. CTA 2009, s.893

16.11 Relevant Assets Acquired from a Related Party

Corporation tax relief in respect of goodwill and certain customer related intangible assets linked with goodwill is restricted where the assets are acquired directly or indirectly from an individual who is a related party in relation to the company, or from a firm where any member of the firm is a related party in relation to the company. CTA 2009, s.849B(1)

The restriction applies to assets acquired by the company on or after 3 December 2014.

No deduction is allowed for debits relating to amortisation of the intangible asset. CTA 2009, s.849D(2)

However, relief is available for any debit made on any subsequent realisation of the asset but it is treated as a non-trading debit and will not be included in the calculation of trading losses, which limits how any debit can be relieved. CTA 2009, s.849D(2)

Relevant assets are:

• goodwill;
• information relating to customers or potential customers;
• a relationship with one or more customers;
• unregistered trade marks; and
• a licence or other right in respect of an asset listed above.

CTA 2009, s.849B(2)

For example, if a sole trader incorporates a business into a company in which he owns 100% of the shares, the new company will not be able to claim corporation tax relief for the amortisation of the internally generated goodwill transferred to the company on incorporation. This means that there will be no difference in the treatment of goodwill for businesses that do not incorporate and businesses that have always operated via a company, neither of which can obtain relief for internally generated goodwill, and businesses which decide to incorporate.

The rules apply to all acquisitions of goodwill from related parties, not just internally generated goodwill. For example, the rules apply if the related party had originally acquired the goodwill from an independent third party, but in this case some corporation tax relief may still be available to the company as a trading deduction. Where the asset is acquired from a related party as part of a transfer of a business, an apportionment calculation must be carried out which prevents a proportion of amortisation being deducted in relation to any accounting value recognised which was internally generated by the individual, but enables a trading deduction on amortisation for the value of relevant assets acquired by the company derived from the previous third party transaction. On a subsequent realisation it will also be necessary to split the asset between trading and non-trading debits. This effectively limits the relief available to the company to what would have been available to the related party, if they had been entitled to relief for intangible assets. If the asset is acquired on a standalone basis, no amortisation debits can be brought into account, even if that asset was originally acquired from a third party, and any debit on disposal will be treated as a non-trading debit.

16.12 Change of Accounting Policy

When a company changes its accounting policy, this will result in a difference between the value at which an IFA is carried in a company’s accounts at the end of one accounting period, and the value at which it is shown in its accounts at the beginning of the next. CTA 2009, s.871

In particular the rules deal with the move from UK GAAP to IAS which we looked at earlier.

The resulting debit or credit is brought into account for tax purposes for the accounting period in which the change of accounting treatment takes effect.

Where the accounting value of the old asset and its tax written down value were not the same, the debit or credit is proportionately increased or reduced using the formula: CTA 2009, s.872(4)

\[
\text{Accounting difference} \times \left(\frac{\text{Tax value}}{\text{Accounting value}}\right)
\]

Where there is a credit, the amount of the credit that is brought into account for tax purposes is restricted to the aggregate amount of relevant tax debits that have previously been brought into account in respect of that asset.

Illustration 6

A company acquired an IFA for £100,000. Rollover relief of £20,000 was claimed on acquisition of this asset. For accounting purposes the asset was amortised over 10
years and no fixed rate election is made under s.730. After 5 years the asset is revalued due to a change in accounting policy, the new value being £150,000.

Value of asset

<table>
<thead>
<tr>
<th>Accounting</th>
<th>Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>£</td>
<td>£</td>
</tr>
<tr>
<td>Cost</td>
<td>100,000</td>
</tr>
<tr>
<td>Rollover relief</td>
<td>(20,000)</td>
</tr>
<tr>
<td>Amortisation</td>
<td></td>
</tr>
<tr>
<td>5yrs @ 10,000</td>
<td>(50,000)</td>
</tr>
<tr>
<td>5yrs @ 8,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>50,000</td>
</tr>
</tbody>
</table>

The revaluation gain in the accounts is the revalued amount of £150,000, less net book value in the accounts of £50,000, so £100,000.

The credit to be brought into account for tax purposes is calculated as:

\[ 100,000 \times \frac{40,000}{50,000} = £80,000 \]

However, this will be restricted to tax debits previously claimed, in this case £40,000. This will give the IFA a TWDV of £40,000 + £40,000 revaluation gain, so £80,000.

Similar rules apply if the carrying value is adjusted for a revaluation or an impairment. CTA 2009, s.723 & 729

16.13 Anti-Avoidance and “Existing Assets”

Anti avoidance measures are in place to stop companies taking advantage of the rules relating to IFAs that were in existence at 1 April 2002.

The rules deal with two avoidance schemes as follows.

- Schemes involving substantial advance payments of royalties. These schemes rely on an assumption that the payment is accounted for by the recipient as a realisation of an existing asset, the effect being to bring the receipt in question into a realisation calculation within the IFA rules. The effect of this treatment would be to allow the accounting cost of the existing asset to be deducted against the receipt.

  The effect of the anti-avoidance provision is to put beyond doubt that a royalty receipt cannot be dealt with under the IFA rules as a realisation of an ‘existing asset’. CTA 2009, s.896

- Schemes involving lump sum licensing arrangements which seek to convert ‘existing assets’ into newly created assets that fall within the IFA rules. CTA 2009, ss. 893 – 894

The rules provide that where an asset created after 1 April 2002 is acquired from a related party and that asset derives its value from an asset which has been an ‘existing asset’ in the hands of a related party of the transferee or transferor, the newly created asset will be treated as an existing asset. Therefore, tax relief under the IFA rules will not be available. Where only part of the value of an asset is derived from an existing asset, the acquired asset will be treated as a separate existing asset to the extent that its value is so
derived. An apportionment rule (to be applied on a just and reasonable basis) provides for these circumstances.

16.14 Tax Avoidance

There is a specific anti-avoidance provision where there are “tax avoidance arrangements”. CTA 2009, s.864

Arrangements are defined widely as including any scheme, agreement or understanding, whether or not legally enforceable. There is tax avoidance if the main object, or one of the main objects, of the arrangements is to enable a company to avoid having to bring into account a credit, to reduce the amount of the credit brought into account, or to bring a debit into account.

If this paragraph applies, all debits and credits in respect of intangible fixed assets are to be brought into the tax computation as if no tax avoidance arrangements had been made.

16.15 Commencement of the Rules for IFAs

The legislation applies to intangible fixed assets acquired or created from 1 April 2002. CTA 2009, s.882

An asset acquired or created partly before and partly after 1 April 2002 is treated as two assets. The expenditure on the purchase or creation of the asset is apportioned on a just and reasonable basis.

Internally generated goodwill is treated as created under the old rules if the company carried on the business before 1 April 2002.

16.16 Election for Special Treatment of Profits from Patents (Patent Box Companies)

For profits made from 1 April 2013, a company may elect that any relevant intellectual property (IP) profits related to a trade of the company, for an accounting period for which it is a qualifying company, are effectively chargeable at a lower rate of corporation tax. CTA 2010, s.357A

A qualifying company is one which at any time in the accounting period:

• holds any qualifying IP rights, or
• holds an exclusive licence in respect of any qualifying IP rights. CTA 2010, s.357B

The qualifying IP that is covered by these rules includes:

• a patent granted in the UK or Europe,
• a right similar to the above, granted under the law of a specified EEA state,
• a supplementary protection certificate, and
• plant variety rights. CTA 2010, s.357BB
The relief is being **phased in** over 5 years, and will give an **effective rate** of corporation tax on relevant IP profits of **12% in FY 2015**, until it is fully in place at an effective rate of **10% in FY 2017**.

The aim is to provide an additional incentive for companies to retain and commercialise existing patents, and to develop new innovative patented products.

The relief is given by allowing a **deduction** to be made in **calculating the trade profits** for the period as follows:  

\[
\text{Relevant IP Profits} \times \frac{\text{Main Rate of CT} - \text{IP Rate of CT}}{\text{Main Rate of CT}}
\]

The IP Rate of CT is **10%**.

In FY 2015, the main rate is 20% giving a deduction of 50% of the relevant IP profit against trade profits for the year. If you then tax the remaining 50% of the relevant IP profits at the main rate of 20%, this would give an effective rate of 10%.

However, as mentioned above, this relief is being **phased in over 5 years**. This works by **reducing** the amount of **relevant IP profits** used in the above calculation as follows:  

<table>
<thead>
<tr>
<th>Financial year</th>
<th>% of IP profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td>60%</td>
</tr>
<tr>
<td>2014</td>
<td>70%</td>
</tr>
<tr>
<td>2015</td>
<td>80%</td>
</tr>
<tr>
<td>2016</td>
<td>90%</td>
</tr>
</tbody>
</table>

If a company does not have a March year end, the relevant IP profits must be apportioned between the relevant financial years on just and reasonable basis.

The relevant IP profits used in the calculation for the deduction are **all profits attributable** to qualifying patents and IP, whether it is received as royalties, or embedded in the sales price of products, from services or underlying processes.

This will potentially benefit a wide range of companies which receive patent royalties, sell patented products, or use patented processes as part of their business. It applies to both **existing and new IP, and acquired IP** if the company has **further developed** the IP.  

The election for special treatment of profits from patents must be made within 12 months of the filing date of the return for the first accounting period for which the company wishes to elect into the regime. An election will apply equally to all trades of the company and will remain in force until it is revoked.

**Illustration 7**

A company has relevant IP profits for the year ended 31 March 2016 of £250,000. Total tax adjusted trade profits for the period are £980,000.

**Calculate the corporation tax payable by the company for the year ended 31 March 2016.**

The company will receive a deduction in calculating the trading profits for the period of:
80% x £250,000 x (20% — 10%)/20% = £100,000

Trade profits 980,000
Less: Patent Box deduction (100,000)
TTP 880,000

Corporation tax payable
880,000 @ 20% 176,000

If we look at the relevant IP profits, we can see that £100,000 effectively did not suffer tax and £150,000 was subject to tax at 20%.

£100,000 @ 0% 0
£150,000 @ 20% 30,000

This gives an effective rate of tax on relevant IP profits for FY 2015 of:

30,000/250,000 = 12%. 
EXAMPLES

Example 1

Theo Ltd purchased goodwill on 1 March 2010 for £500,000 and sold it for £800,000 on 31 December 2015. At 31 March 2015 the goodwill had a book value of £350,000.

Theo Ltd has a March year end and has not made an election under s.730 CTA 2010.

You are required to show:

a. The debit or credit in respect of the sale of the goodwill assuming no reinvestment of the proceeds;

b. The position if Theo Ltd buys a trademark from Pisci Ltd for £600,000;

c. The position if, instead of buying the trademark, Theo Ltd purchases 100% of the shares in Pisci Ltd. The balance sheet of Pisci Ltd shows IFAs with a written down value of £950,000;

d. The position if instead of option b) or c) Theo Ltd purchases a building from Pisci Ltd for £700,000. The building will be used in the trade of Theo Ltd;

e. Assuming that Theo Ltd buys the trademark in option b) above on 1 April 2016, show the amortisation that can be claimed in the year to 31 March 2017 if the accountants decide to write the trademark off over 10 years on a straight line basis. No election is made under s.730 CTA 2009.
ANSWERS

Answer 1

a. The sale takes place in the accounting period ended 31 March 2016. The income gain will be:

<table>
<thead>
<tr>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds of sale</td>
</tr>
<tr>
<td>Less: WDV (same as accounts)</td>
</tr>
<tr>
<td>Income gain</td>
</tr>
</tbody>
</table>

b. There is a partial reinvestment of the proceeds.

\[
\begin{align*}
\text{Amount reinvested} & \quad 600,000 \\
\text{Less: Cost of old IFA} & \quad (500,000) \\
\text{Amount rolled over} & \quad 100,000
\end{align*}
\]

Note that we do **not** take account of the amounts written off the cost in this calculation.

The gain for the year will be:

\[
\begin{align*}
\text{Income gain} & \quad 450,000 \\
\text{Less: Amount rolled over} & \quad (100,000) \\
\text{Taxable income (IFA)} & \quad 350,000
\end{align*}
\]

c. There is full reinvestment of the proceeds.

The amount rolled over will be:

\[
\begin{align*}
\text{Proceeds reinvested} & \quad 800,000 \\
\text{Less: Cost of old IFA} & \quad (500,000) \\
\text{Amount rolled over} & \quad 300,000 \\
\text{Income gain} & \quad 450,000 \\
\text{Less: Amount rolled over} & \quad (300,000) \\
\text{Taxable income (IFA)} & \quad 150,000
\end{align*}
\]

d. No rollover is possible as a building is not an IFA.

e. 

\[
\begin{align*}
\text{Amortisation in accounts} & \quad 600,000/10 = £60,000 \\
\text{Tax written down value} & \quad 600,000 - 100,000 = £500,000 \\
\text{Tax deduction for amortisation} & \quad 500,000/600,000 \times 60,000 = £50,000
\end{align*}
\]