

Corporation Tax Treatment of Goodwill and Related Assets

23 July 2019

CORPORATION TAX TREATMENT OF GOODWILL AND RELATED ASSETS

There are special rules governing the treatment of goodwill and other intangible assets for corporation tax purposes. When the rules were first introduced with effect from 1 April 2002 the tax treatment was intended to broadly follow the accounting treatment. This meant that where a company acquired an intangible asset, it would be able to claim a corporation tax deduction on the amortisation debited in its accounts as part of its computation of trading profits for tax purposes.

INTANGIBLE ASSETS ACQUIRED BEFORE 1 APRIL 2002

Any asset acquired before 1 April 2002 is dealt with under the original capital gains tax rules which did not permit a corporation tax deduction for amortisation. Instead, when the intangible asset is sold, the cost is deducted in computing the gain or loss on disposal in the same way as any other chargeable asset.

There are special rules dealing with the situation where a company acquires an intangible asset from a related party, with the result that an intangible asset that was acquired or created before 1 April 2002 by the related party, the company acquiring the asset cannot treat that asset as a post-1 April 2002 asset. It will retain its capital gains tax status.

GOODWILL ACQUIRED AFTER 3 DECEMBER 2014

Until 3 December 2014 goodwill and other customer-related intangible assets were treated in the same way as other intangible assets such as patents and similar intellectual property for corporation tax purposes. Where goodwill and other customer-related assets are acquired from a related party on or after that date the company cannot claim a corporation tax deduction for amortisation of those assets.

GOODWILL ACQUIRED AFTER 7 JULY 2015

The rules were changed again with effect from 8 July 2015, so as to deny a corporation tax deduction for amortisation on any goodwill or other customer-related intangible assets acquired on or after that date.

CURRENT TREATMENT OF AMORTISATION OF GOODWILL

Amortisation continues to be available in relation to post-1 April 2002 goodwill and other customer-related intangible assets acquired between 1 April 2002 and 2 December 2014, and on goodwill and other customer-related intangible assets acquired from unrelated parties between 3 December 2014 and 7 July 2015.

TREATMENT OF OTHER INTANGIBLE ASSETS

It should be noted that all other intangible assets continue to be dealt with in accordance with the original version of the intangible assets regime, whereby a corporation tax deduction is available for amortisation on post-1 April 2002 intangible assets that do not relate to goodwill and other customer-related intangibles.

GOODWILL ACQUIRED AFTER 31 MARCH 2019 – FINANCE ACT 2019 CHANGES

Finance Act 2019 has now introduced, in a new Chapter 15A to CTA 2009, a measure of relief for amortisation on some goodwill and other customer-related intangible assets acquired on or after 1 April 2019. The rules are, however, complex and restrictive.

- The Chapter starts by identifying the types of intangible assets covered by the new rules, referred to as “relevant assets”. These are:
- Goodwill in a business or part of a business,
- An intangible fixed asset that consists of information which relates to customers or potential customers of a business or part of a business,
- An intangible fixed asset that consists of a relationship 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 or part of a business, or
- A licence or other right in respect of an asset within any of the above.

Instead of getting relief for the amortisation in the accounts, the rate of relief is fixed at a writing down rate of 6.5%.

This means that a measure of relief has been re-introduced for acquired goodwill, but only to the extent that it has a connection with other intellectual property that qualifies for relief.

Companies which have acquired goodwill over the period from 1 April 2002 will, therefore, need to track amortisation for goodwill under a number of different rules, where relief for amortisation will continue to apply in accordance with the rules in place when that goodwill was acquired.

PRE-FA 2019 RELEVANT ASSET

Relief is restricted on any “pre-FA 2019 relevant asset” so that no deduction can be claimed for amortisation, and when the asset is sold the debit on any loss on disposal will be treated as a non-trading debit. This means that the loss will not form part of the trading results of the company.

This part of the new legislation aims to ensure that companies do not structure acquisitions in a way that might convert a non-qualifying into a qualifying acquisition. There are four ‘cases’ in which a relevant asset will be treated as a pre-FA 2019 relevant asset.

THE FIRST CASE

This applies to an asset acquired or created in the period 8 July 2015 to 31 March 2019, and the asset was a chargeable intangible asset in relation to the company at any time in the period 29 October 2018 (the date of the Autumn Budget 2018) and 31 March 2019 (the day before the start date of the new provisions).

THE SECOND CASE

This applies to a relevant asset of a company (“C”), where another company acquired or created the asset in the period 8 July 2015 to 31 March 2019, it was a chargeable intangible asset in relation to that company at any time in the period 29 October 2018 and 31 March 2019, and C acquired the asset on or after 1 April 2019 otherwise than in case A or case B from a person who was a related party in relation to C.

Case A:

C acquired the asset from a company that was within the charge to corporation tax at the time of the acquisition, and the asset was not a pre-FA 2019 asset in the hands of that company immediately before the acquisition.

Case B:

C acquired the asset from a person (“the intermediary”) who acquired the asset on or after 1 April 2019 from a third person who was not at the time of the intermediary’s acquisition a

related party in relation to the intermediary, or, if the intermediary was not a company, to a company in relation to which the intermediary was a related party, and who is not, at the time of the acquisition by C, a related party in relation to C.

THE THIRD CASE

This applies where a relevant asset was created on or after 29 October 2018, a company (“C”) acquired the relevant asset on or after 1 April 2019 from a person (“the transferor”) who was a related party in relation to C at the time of acquisition, the value of the relevant asset derives in whole or in part from another asset (“the other asset”) which meets the “preserved status condition”.

The preserved status condition is met where the other asset was acquired or created by a company between 8 July 2015 and 31 March 2019, and was a chargeable intangible asset in the hands of that company at any time between 29 October 2018 and 31 March 2019 when that company and C were related parties, or that company and the transferor were related parties.

Where only part of the value of the relevant asset derives from the other asset, the relevant asset is apportioned into two separate assets.

THE FOURTH CASE

This applies where a company acquired the asset on or after 1 April 2019 directly or indirectly in consequence of, or otherwise in connection with, a disposal of a relevant asset by another person, and the asset disposed of would have been a pre-FA 2019 relevant asset in the hands of the company had the person transferred it to the company at the time of the disposal.

NO BUSINESS OR NO QUALIFYING IP ASSETS ACQUIRED

Where a company acquires a relevant asset on or after 1 April 2019 and the acquisition is not part of the acquisition of a business, and the company does not acquire any qualifying IP assets as part of the acquisition of the business for use on a continuing basis in the course of the business, a debit cannot be claimed for amortisation, and on disposal any loss on disposal will be treated as a non-trading debit.

A qualifying IP asset is an intangible fixed asset that falls into one of the following categories:

- a) a patent, registered design right, plant breeders’ right,

- b) a right under the law of a country or territory outside the UK corresponding to or similar to a right within the above,
- c) a licence or other right in respect of any of the above, except for software licences that permits use of that software, but does not permit manufacture, adaptation or supply.

Further, the asset cannot to any extent be excluded by Chapter 10 (which are broadly intangible assets for which there are special rules), and cannot be a pre-FA 2002 asset.

RELATED PARTY ACQUISITIONS

Where a relevant asset is acquired from a related party on or after 1 April 2019, a debit for amortisation is not available for corporation tax purposes. A loss on subsequent disposal of the asset will be a non-trading debit.

PARTIAL RESTRICTIONS ON DEBITS

There is a restriction on the amount that can be claimed as a debit where expenditure on relevant assets is more than six times the expenditure on qualifying IP assets. This is expressed as a formula, where the restriction applies when the result is less than 1 (the "relevant amount"):

$$\frac{A \times N}{B}$$

Where:

A is expenditure incurred by the company on acquisition of qualifying IP assets;

B is expenditure incurred by the company on acquisition of the asset concerned and any other relevant assets acquired with the business;

N is 6.

Where the result is less than 1, the allowable debit is reduced by the formula:

$$D \times RA$$

Where:

D is the amount of debit that would be brought into account disregarding this restriction;

RA is the relevant amount computed above.

For example, a company acquires goodwill for £200,000, and qualifying IP assets of £15,000.

The fixed rate of relief, ignoring any restriction, is $200,000 \times 6.5\% = £13,000$.

The restriction is calculated as follows:

$$(15,000 \times 6) / 200,000 = 0.45$$

The allowable debit is reduced by the formula:

$13,000 \times 0.45 = £5,850$, which is the allowable debit for goodwill for corporation tax purposes.

Where there has been a restriction, any debit on sale of the goodwill is apportioned so that part of the debit attributable to the restricted portion is treated as a non-trading debit. Following the above example, if the company sold the goodwill for £150,000, the position would be as follows.

Step 1

The tax written down value of the goodwill would be $200,000 - 13,000 = 187,000$ (ignoring the restriction of the corporation tax deduction). The debit on realisation is therefore £37,000. This is then multiplied by the RA restriction of 0.45, giving an allowable trading debit of £16,650.

Step 2

If the restriction had not been ignored, the restriction on the debits, the tax written down value would have been $200,000 - 5,850 = 194,150$. The debit on realisation would have been £44,150.

The non-trading debit is, therefore, $44,150 - 16,650 = £27,500$.

This means that full relief is available for the whole loss, but part of that loss is treated as a non-trading debit, which could restrict the availability of that loss.

CONCLUSION

The corporation tax treatment of goodwill has changed several times since the introduction of the intangibles regime in 2002. Where companies have been active in acquiring goodwill and other intangible assets over a number of years they need to track the amortisation of intangibles to treat each part correctly in accordance with the legacy position.

The new rules applicable for acquisitions from 1 April 2019 are complex, but in principle companies only need to consider whether relief for amortisation is available if the business purchase is from a third party and involves not only goodwill, but also other forms of intangible asset that fall within the definition of qualifying IP assets.

The information contained in this document is for information only. It is not a substitute for taking professional advice. In no event will Dixon Wilson accept liability to any person for any decision made or action taken in reliance on information contained in this document or from any linked website.

This firm is not authorised under the Financial Services and Markets Act 2000 but we are able in certain circumstances to offer a limited range of investment services to clients because we are members of the Institute of Chartered Accountants in England and Wales. We can provide these investment services if they are an incidental part of the professional services we have been engaged to provide.

The services described in this document may include investment services of this kind.

Dixon Wilson
22 Chancery Lane
London
WC2A 1LS

T: +44 (0)20 7680 8100
F: +44 (0)20 7680 8101
DX: 51 LDE

www.dixonwilson.com
dw@dixonwilson.co.uk