

1 Intangible fixed assets: treating assets as “existing assets” etc

- (1) Schedule 29 to FA 2002 (gains and losses of a company from intangible fixed assets) is amended as follows.
- (2) In paragraph 13 (credits in respect of intangible fixed assets: introduction), in sub-paragraph (1) (credits brought into account under Part 3), after paragraph (a) (receipts recognised in determining profit or loss), insert –
 - “(aa) receipts in respect of royalties so far as the receipts do not give rise to a credit under paragraph 14 (see paragraph 14A),”.
- (3) After paragraph 14 (receipts recognised as they accrue) insert –

“Receipts in respect of royalties so far as not dealt with under paragraph 14

14A (1) So far as a receipt in respect of any royalty does not give rise to a credit under paragraph 14 (whether in the period of account in which it is received or in a subsequent period of account), a credit shall be brought into account for tax purposes.

 - (2) The amount of the credit to be brought into account for tax purposes is equal to so much of the amount of the receipt as does not give rise to a credit under paragraph 14.
 - (3) The credit shall be brought into account for tax purposes in the accounting period in which the receipt is recognised for accounting purposes.”.
- (4) In paragraph 82 (assets excluded to extent specified: research and development), in sub-paragraph (2) (provisions of Schedule not applying to asset so far as representing expenditure on research and development) –
 - (a) in paragraph (a) (Part 2 not to apply subject to exception relating to paragraph 14), at the end insert “or 14A (receipts in respect of royalties so far as not dealt with under paragraph 14)”, and
 - (b) in paragraph (b) (Part 3 not to apply subject to exception for paragraph 14), for “paragraph 14” substitute “paragraphs 14 and 14A”.
- (5) In paragraph 83 (assets excluded to extent specified: election to exclude capital expenditure on computer software), in sub-paragraph (3) (effect of election) –
 - (a) in paragraph (a) (Part 2 not to apply subject to exception relating to paragraph 14), at the end insert “or 14A (receipts in respect of royalties so far as not dealt with under paragraph 14)”, and
 - (b) in paragraph (b) (Part 3 not to apply subject to exception for paragraph 14), for “paragraph 14” substitute “paragraphs 14 and 14A”.
- (6) In paragraph 118 (application of Schedule to assets created or acquired after commencement, that is to say, on or after 1st April 2002) –
 - (a) in sub-paragraph (4) (application of sub-paragraph (1) subject to other

- paragraphs), at the end insert “and
- (c) paragraph 127A (assets whose value derives from existing assets treated as existing assets), and
 - (d) paragraph 127B (assets acquired in connection with disposals of existing assets treated as existing assets).”, and
- (b) in sub-paragraph (6) (nothing in paragraph 118 restricts application of Schedule in accordance with paragraph 119), at the end insert “, but see sub-paragraph (5) of that paragraph.”.
- (7) In paragraph 119 (application of Schedule to royalties), at the end insert –
- “(5) Nothing in this paragraph shall be read as authorising or requiring an amount to be brought into account in connection with the realisation of an existing asset within the meaning of Part 4.”.
- (8) After paragraph 127 (certain assets acquired on transfer of business treated as existing assets) insert –

“Assets whose value derives from existing assets treated as existing assets

127A(1) This paragraph applies where –

- (a) a company acquires an intangible fixed asset (“the acquired asset”) after commencement from a person (“the transferor”) who at the time of the acquisition is a related party in relation to the company,
 - (b) the acquired asset is created, whether by the transferor or any other person, after commencement,
 - (c) the value of the acquired asset derives in whole or in part from any other asset (“the other asset”),
 - (d) the other asset has not at any time on or after 5th December 2005 been a chargeable intangible asset in the hands of the company or a related party in relation to the company or the transferor, and
 - (e) the existing asset condition is met.
- (2) The existing asset condition is that, after commencement, –
- (a) the other asset has been an existing asset in the hands of the transferor at a time when the transferor was a related party in relation to the company, or
 - (b) the other asset has been an existing asset in the hands of any other person at a time when the other person was a related party in relation to the company or the transferor.
- (3) Where this paragraph applies the acquired asset shall be treated for the purposes of this Schedule as an existing asset in the hands of the company, but only so far as its value derives from the other asset.
- (4) If only part of the value of the acquired asset so derives –
- (a) this Schedule has effect as if there were a separate asset representing the part of the value not so derived, and
 - (b) the enactments that apply where this Schedule does not apply have effect as if there were a separate asset representing the part of the value so derived.

Any apportionment necessary for this purpose shall be made on a just and reasonable basis.

- (5) For the purposes of this paragraph the cases in which the value of an asset may be derived from any other asset include any case where—
 - (a) assets have been merged or divided,
 - (b) assets have changed their nature, or
 - (c) rights or interests in or over assets have been created or extinguished.
- (6) For the purposes of this paragraph the time at which an asset is created or acquired is the time at which it would be regarded as created or acquired for the purposes of paragraph 118 (application of Schedule to assets created or acquired after commencement).

Assets acquired in connection with disposals of existing assets treated as existing assets

- 127B(1) This paragraph applies where—
 - (a) a person disposes of an asset which, at the time of the disposal, is an existing asset in the hands of the person,
 - (b) a company which at the time of the disposal is a related party in relation to the person acquires an intangible fixed asset directly or indirectly in consequence of, or otherwise in connection with, the disposal, and
 - (c) the intangible fixed asset that is acquired would, apart from this paragraph, at the time of the acquisition be a chargeable intangible asset in the hands of the company.
- (2) Where this paragraph applies the intangible fixed asset that is acquired shall be treated for the purposes of this Schedule as an existing asset in the hands of the company.
- (3) For the purposes of this paragraph—
 - (a) “asset”, in relation to any disposal, means any asset for the purposes of the Taxation of Chargeable Gains Act 1992,
 - (b) a person “disposes of” an asset if, for the purposes of that Act, the person makes a part disposal of the asset or any other disposal of the asset,
 - (c) the time at which a disposal of an asset is made is the time at which it is made for the purposes of that Act.
- (4) For the purposes of this paragraph it does not matter—
 - (a) whether the asset that the person disposes of is the same asset as the one that the company acquires,
 - (b) whether the asset that is acquired is acquired at the time of the disposal or at any other time, or
 - (c) whether the asset that is acquired is acquired by merging two or more assets or is acquired in any other way.”.
- (9) In paragraph 143 (index of defined expressions), in the entry relating to existing asset, in the second column, for “paragraph 127” substitute “paragraphs 127 to 127B”.
- (10) The amendments made by this section have effect in relation to the debits or credits to be brought into account for any accounting period beginning on or

after 5th December 2005 (and, in relation to the debits or credits to be brought into account for any such period, shall be deemed always to have had effect).

- (11) For this purpose an accounting period beginning before, and ending on or after, that date is treated as if—
- (a) so much of that period as falls before that date, and
 - (b) so much of that period as falls on or after that date,
- were separate accounting periods.

Intangible Assets Regime Anti avoidance measures

Draft legislation

5 December 2005

1. A new measure to counter tax avoidance involving intangible assets held by companies was announced at PBR. Draft legislation is published today as part of this note. The legislation, which will take effect today (5 December 2005), will be included in Finance Bill 2006. The draft legislation will amend Schedule 29 Finance Act 2002 (the corporation tax regime governing the treatment of intangible assets).
2. The draft legislation is aimed at avoidance schemes designed to obtain relief under Schedule 29 for the value of companies' existing assets which were not intended to be within the scope of the Schedule. Schedule 29 specifically excludes the assets held by companies at the commencement of the new intangibles regime (1 April 2002) unless and until those assets are acquired by an unrelated party after that date.
3. In part, the proposed clause is designed to address avoidance schemes involving substantial advance payments of royalties. These schemes rely on an assumption that where such a payment is accounted for by the recipient as a realisation of an existing asset, the effect of Schedule 29 will be to bring the receipt in question into a realisation calculation within Part 4 of Schedule 29. The effect of this treatment would be to allow the accounting cost of the existing asset to be deducted against the receipt.
4. This is not the intention of Schedule 29. The Schedule included most royalties within its scope (overriding the more general exclusion of 'existing assets' in this instance) in order to modernise the timing rules which previously applied to royalties. But it was clearly not intended to allow relief for the cost of 'existing assets' (except for the specific categories of asset provided for in the Schedule).
5. Sub-clause (7) of the draft legislation inserts a new provision into paragraph 119 of Schedule 29 dealing with the treatment of royalties. The effect of the new provision is to put beyond doubt that a royalty receipt cannot be dealt with under Part 4 of Schedule 29 as a realisation of an 'existing asset'.
6. Sub clauses (2) and (3) ensure that, to the extent that royalty receipts would not give rise to taxable credits under paragraph 14(1) of Schedule 29, they give rise to taxable credits under new paragraph 14A when they arise. Realisations of assets within Schedule 29 are prevented from being within paragraph 14 and new paragraph 14A by paragraph 13(2).
7. Sub-clause (8) introduces new paragraphs 127A and 127B into Schedule 29. These provisions are targeted at avoidance schemes which also seek to generate tax deductions under Schedule 29 for the value of intangible assets held by groups of companies prior to the introduction of Schedule 29.
8. The schemes often involve lump sum licensing arrangements which seek to convert 'existing assets' into newly created assets that fall within Schedule 29. We do not accept that these schemes are effective. However, the new provisions put beyond doubt that where:
 - a licence is granted between related parties in respect of an 'existing asset', and
 - the licence is an intangible fixed asset in the hands of the licensee,

the licence is an existing asset and tax relief under Schedule 29 will not be available.

9. New paragraph 127A provides that where an asset created after commencement is acquired from a related party and that asset derives its value from an existing asset:

- in the hands of that related party;
- or in the hands of another related party of either the transferee or transferor company,

the newly created asset will be an existing asset and so will be excluded from Schedule 29.

10. 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 (sub-paragraph 4).
11. New paragraph 127B applies where there is a related party transaction involving the acquisition of an intangible fixed asset by a company and the disposal of an existing asset by a related person. The effect of the paragraph is to ensure that (where the acquisition of the intangible asset is directly or indirectly in consequence of, or otherwise in connection with, the disposal) the acquired asset is an existing asset for the acquiring company.
12. Paragraph 127B specifically addresses avoidance schemes where licences or other rights are granted between related parties in respect of 'existing assets'. For example, one company in a group grants a licence out of an existing trademark to another group company. The company granting the licence claims to have made a part disposal of an existing asset to which section 171 TCGA applies so that no chargeable gain arises. The company granted the licence maintains that it has acquired a newly created intangible asset falling within Schedule 29 so that relief is available for the cost of the licence as it is amortised.
13. The scheme seeks to convert an existing asset into a new asset and so generate additional tax deductions, contrary to the policy intention of Schedule 29. Paragraph 127B puts beyond doubt that the licence or other rights granted under these circumstances will remain an existing asset and that Schedule 29 will operate as intended.
14. The new provisions included in this draft legislation will have effect in relation to debits and credits brought into account on or after 5 December 2005. (For this purpose, the period from 5 December to the end of the current accounting period will be treated as a separate accounting period.) In the case of new paragraphs 127A and 127B, the effect will be that any intangible assets which may have succeeded in entering Schedule 29 as a result of the avoidance schemes targeted by these measures, will be treated as 'existing assets' from 5 December 2005. Further tax deductions will therefore no longer be available under Schedule 29 in respect of these assets.
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