FB 2015 – goodwill and other intangible assets, restriction to relief

Large Corporate **OMB**

01 November 2015

CIOT and ATT comment on clause 32 of the Finance Bill

The CIOT has written to the Finance Bill Committee commenting on clause 32 of the Finance Bill which will prevent corporation tax deductions, such as amortisation and impairment debits, for goodwill and other intangible assets linked to customers and customer relationships. The change will apply on goodwill purchased – usually as part of a business acquisition – after 8 July 2015 (summer Budget day). It follows a similar change, being the removal of the corporation tax deduction for goodwill acquired by a company on the incorporation of a business. This was introduced by Finance Act 2015 and took effect from 3 December 2014.

The CIOT does not agree with the stated rationale for this change. The government note says:

> ‘This measure removes the tax relief that is available when structuring a business acquisition as a business and asset purchase so that goodwill can be recognised. This advantage is not generally available to companies who purchase the shares of the target company. The current rules allow corporation tax profits to be reduced following a merger or acquisition of business assets and can distort commercial practices and lead to manipulation and avoidance.’

Although we agree that the availability of relief on purchased goodwill provides – from a buyer’s perspective – some advantage in being able to do an asset acquisition (compared with a share acquisition) since the write-off for goodwill is available, our experience is that sellers rarely entertain an asset disposal when significant goodwill is involved. This is because sellers invariably want to sell the shares in a company, either to take advantage of the substantial shareholdings exemption (SSE) available to corporates or to claim a lower rate of capital gains tax available to individuals (business asset taper relief or entrepreneurs’ relief). A sale of assets would result in the goodwill disposal being taxed, or taxed at a higher rate, whether it is pre- or post-2002 goodwill.

Whereas the seller can achieve an immediate lower tax bill for a sale of shares, a buyer can only write off the cost of the goodwill acquired over a number of years. There is already, therefore, an overall bias in the tax system in favour of share sales rather than asset sales. Thus the existing relief does not distort commercial practices. Indeed, rather than removing an artificial incentive to buy assets rather than shares, the proposed change increases the bias towards share transactions by removing any tax relief in the buyer’s hands for goodwill.

As well as objecting to the proposed change on the ground of its complexity, the CIOT said that, in terms of overall structure of the tax system, it was difficult to understand the rationale behind making this change in isolation. The CIOT noted several other aspects of the intangible assets regime that could, and should, be considered for reform.

This was a missed opportunity for consultation in an area where there is scope for reform and improvement; the change will introduce further complexity to the tax system; and, if the government is minded to remove the relief, there are other possible approaches that would offer greater simplicity and coherence within the tax system.

The full text of the CIOT's briefings can be found on parliament.uk here and here.

When is an obligation unconditional?

The ATT has considered the point that the clause will deny a corporation tax deduction unless the acquisition of the goodwill occurred before 8 July or was acquired 'in pursuance of an obligation, under a contract, that was unconditional before that date'. Clause 32(13) indicates that 'an obligation is unconditional if it may not be varied or extinguished by the exercise of a right (whether under the contract or otherwise)'.

An ATT member sought assistance on how the unconditional obligation provision would be interpreted in the context of a particular client. Briefly, their corporate client had made an offer for the acquisition of goodwill, which had been accepted in May 2015. The offer was, however, conditional on approval of the business transfer being obtained from the relevant regulatory authority, without which the company would not have been able to operate the business whose goodwill it had contracted to purchase. As of 8 July 2015, there was no indication from the regulatory authority as to whether the required approval would be forthcoming, even though it had been formally applied for in the middle of June. The question was whether the awaited response from the regulatory authority meant that the obligation was still conditional as of 8 July 2015.

The ATT contacted HMRC on behalf of the member. The specialist officer concerned was as helpful as they could be but explained that they were unable to comment on the interpretation of draft legislation. They indicated that the point might be addressed in guidance. The ATT accordingly submitted a note to HMRC setting out the circumstances. The note also raised the more general point on how the provision would be applied if the contract could be varied by reference, for example, to a final valuation at completion.

The ATT also assisted the member to prepare written evidence for submission by their client to the Finance Bill Committee. The submission on the unconditional obligation point can also be found on parliament.uk.