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Corporate Intangibles Research and Development Manual

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CIRD48140 - Intangible assets: avoidance: tax-driven transactions: circumstances where anti-avoidance rule may be in point

Cases where CTA09/S864 may apply

Introduction

In the nature of a rule like that in CTA09/S864 it is not possible to provide a comprehensive catalogue of the circumstances where it may be in point, but the examples below illustrate the sort of manipulation at which the provision is aimed.

Depression of carrying cost of purchased asset

It may be possible to depress artificially the value of intangibles held by a company by having it enter into commercially unfavourable arrangements with related parties (who need not be outside the UK tax net for this purpose).

For example, a company, having acquired goodwill as part of a business, could enter into a binding and fairly long-term contract with a fellow UK group member to be supplied with services required for the business at an excessive price. That would depress the profits of the business and so call into question the value of the goodwill (which is simply the difference between what was paid for the business and the total of the value of each of its identifiable assets minus its liabilities). That in turn could trigger an impairment review (see CIRD30550 (https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird30550)), leading to a substantial write-down in the goodwill.

Similar devices to depress the market value of intangibles prior to their disposal to a related party might also be possible.

Inflation of acquisition cost

The mirror image of these devices could equally be used to inflate the market value of the asset at acquisition, though the opportunities are more limited by the inflation also of the potential income charge on a related party vendor. But possibilities remain.

For example, an asset may be acquired by a partnership business from a third party and then sold to a related company at a price which reflects a transaction with another related company inflating the value of the asset (for example a licensing agreement in respect of a patent providing for very high rates of royalty).

Turning existing assets into assets within CTA09/PART8

Intangible assets acquired after commencement are within CTA09/PART8 and therefore qualify for tax deductions based on the sums written off assets in the accounts. An important exception to this provision is that assets acquired from related parties who held them prior to 1 April 2002 do not come within CTA09/PART8, (CIRD11500 (https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird11500)). One attempt to side-step this rule would be to pass the asset after commencement through a third person unrelated to either the original transferor or the company seeking the tax deductions. Another might be to break temporarily the relationship between otherwise related parties by artificial means. There is likely to be a strong case in these circumstances that these are arrangements a main object of which is to obtain tax deduction which would not otherwise be due.

A slightly more sophisticated manifestation of this ‘churning’ of pre-commencement assets might involve the post-commencement creation of substitute assets offshore. If such assets are subsequently transferred into the UK group, there is again likely to be a strong case that the transfer is part of arrangements a main object of which is to obtain a debit which would not otherwise have been due.

Cross-border transactions and structures

Multinational groups are in a position to influence and manipulate the value of specific intangible assets. In this context, the anti-avoidance rule is most likely to be in point where deductions for sums written off intangible assets are relievable against profits fully exposed to CT but either:

- the corresponding income stream from the asset is sheltered in some way from UK tax; or else
- the asset has been transferred to a UK group member in the knowledge that it is likely to generate considerably less taxable income than the CT deductions it will attract (as the cash flow projections which are likely to have been drawn up may demonstrate).

Whilst the transfer pricing rules will usually be the first port of call in respect of cross-border arrangements, valuation provisions are not always an adequate counter for avoidance. The anti-avoidance rule in S864 also needs to be considered where significant amounts of tax are at stake, and particularly where the value of what is being bought or sold cannot be reliably established by cogent evidence. It is possible for assets to be structured, and transactions designed, to exploit difficulties in applying open market valuation provisions.

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