BIA consultation submission: Review of the corporate intangible fixed assets regime

May 2018

UK BioIndustry Association

Introduction

The BioIndustry Association (BIA) welcomes the opportunity to input into the HMRC and HM Treasury's review of the corporate intangible fixed assets regime.

The BIA is the trade association for innovative life sciences in the UK. Our goal is to secure the UK's position as a global hub and as the best location for innovative research and commercialisation, enabling our world-leading research base to deliver healthcare solutions that can truly make a difference to people's lives.

Our members include:

- Start-ups, biotechnology and innovative life science companies
- Pharmaceutical and technological companies
- Universities, research centres, tech transfer offices, incubators and accelerators
- A wide range of life science service providers: investors, lawyers, IP consultants, IR agencies

We promote an ecosystem that enables innovative life science companies to start and grow successfully and sustainably.

There are many features of the UK which make it an attractive place to start and grow an IP-rich business. There are many factors, but the UK tax system is one of them, given the ability to benefit from R&D tax credits, the patent box, venture capital schemes and EMI share option schemes is very helpful.

Intellectual Property (IP) – primarily patents – are the essential basis of the value of a life science company. Significant investment in R&D is required to take a scientific concept or discovery through to commercialisation. This can exceed £1 billion over a period of 10 to 20 years. Due to their complexity, medicinal products and other life science innovations are typically protected by a suite of patents, some of which will be developed by the company itself whilst others may be purchased or licensed from other sources. How these assets are dealt with by the tax regime is therefore an important consideration and the BIA welcomes this review and its focus on ensuring the UK has an internationally-competitive intangible fixed assets regime.

Responses to consultation questions

1-6[1]. What types of asset are typically affected by the pre-FA02 rule [and what would be the impact of bringing them within the IFA regime]?

For many of our member companies, their focus is on developing their IP, which is expensed, rather than meeting the accounting tests to be capitalised for accounting purposes. However, there remain instances where transactions might involve IP that pre-dates April 2002. As more time elapses from the transition, this creates more complexity and uncertainty. The legislation introduced in 2002 has been effective and we would welcome the opportunity for simplification by abolishing the pre-2002 rules such that they are removed entirely from the statute.

7. In what situations do companies pay more for a business than the fair value of the individual assets, and what does this difference represent?

Given the complexities of valuing highly specific intangible assets in an emerging growth sector such as the biotechnology industry, there are numerous situations where the overall benefit of an acquisition is not reflected in the value of individual assets, e.g. competitive bid situations, where off-patent assets are involved, or where there is no settled industry view, such as whether a marketing authorisation for a pharmaceutical product has no value or a very significant value. When purchase amounts are tested against valuation methods used for accounting standard purposes, there can often be differences.

8. How has the scope of the 2015 restriction – which extends beyond goodwill to customer-related intangibles – impacted on your business? Please explain both the positive and negative impacts, and provide specific examples where possible.

We would support the view that that the absence of relief for customer-related intangibles creates complexity and a friction for transactions by introducing a further boundary to the regime that does not align with accounting treatment. Valuing these intangible assets into their component parts is difficult and expensive. It is also subjective and this creates uncertainty in determining the tax impact of a transaction. In our experience, the tax position of the vendor has more impact to the nature of a transaction and so we have seen less evidence of the rules for intangibles having a distorting effect.

9. To what extent could changes be made in this area in a way that deals with the issues that motivated the removal of relief in 2015?

N/A given our responses to questions 7 and 8.

10. To what extent does the IFA de-grouping charge cause difficulties with M&A transactions in practice? Please provide specific examples where possible.

It is often the case that new intangibles are created through platform technology or member companies decide to develop medicines or technologies in different therapeutic areas. Smaller companies in this sector generally have a dependency on having to collaborate with other companies to bring a new product

[1] All questions:
1: What types of asset are typically affected by the pre-FA02 rule?
2: What difficulties or benefits has the need to distinguish between pre- and post-FA02 assets caused for your business? How has the significance of these issues changed over time? If possible, please provide details of any extra administration and cost this imposed.
3: What would be the impact (positive or negative) of allowing pre-FA02 assets to come within the IFA regime?
4: If pre-FA02 assets were brought within the IFA regime, at what value should they be recognised, and why?
5: How significant would the transitional issues around capital losses and other reliefs be in practice, and what do you consider would be the best way of addressing this potential unfairness?
6: Do you anticipate any other transitional issues? If so, please provide details.

through to regulatory approval. This is because of the exceptionally high cost of development. To achieve this it is not uncommon for the company to want to separate certain IP rights from the residual. This can commonly give rise to potential degrouping charges. This has resulted in early stage companies adopting complex group structures resulting in unhelpful cost and complexity or companies deciding to restructure or demerge with the same impact. Demerging a company in this sector is particularly problematic in having to separate rights for preference shareholders arising from venture capital.

Degrouping for intangibles puts this sector at a disadvantage to others (for example, real estate) for whom degrouping was essentially removed in 2011.

11. Do you consider that the IFA de-grouping charge could be modified to eliminate such difficulties? How could this be achieved affordably, while preserving the Exchequer's ability to claw-back deductions given in excess of the economic cost?

In order to achieve affordability, we suggest either:

a) a restriction on the types of IFA, so that brand and customer related intangibles are excluded, but patent rights and related know-how are not subject to degrouping charges; or

b) a clearance mechanism is introduced in order to prevent tax-motivated planning

12. In what circumstances do companies typically elect for fixed rate relief?

Whenever tax deductions are otherwise not available. This is a valuable form of relief for the industry; see our response to question 7 above.

13. Do you consider that the UK's approach to the elective fixed rate relief deters international businesses from locating intangibles in the UK?

In our industry there is a need to locate people in the UK in order to carry out R&D, and therefore create IFAs in the UK. The siting of goodwill in the UK, or elsewhere, is not a common topic for consideration.

14. Should the way in which fixed-rate relief is given under the IFA regime be changed? How would this impact on business decisions?

N/A given our responses to Q12 and Q13.

15. What are the benefits to the UK of international businesses holding intangible assets in the UK?

Intangible assets only have a value for accounting purposes if they represent a commercially viable proposition. Therefore, ultimately, those intangibles should turn into revenues and consequent tax receipts for the UK with a consequential positive impact on employment.

The US tax system allows for the share acquisition of a company to be treated as an acquisition of the underlying assets through the use of section 338 elections. As a result, tax is triggered on a deemed market value disposal of the assets, but the assets are then tax amortised in the future. This can provide long-term tax benefits to the acquirer, but accelerates the tax receipts. The introduction of a similar system in the UK would be very welcome in providing flexibility and enhancing the competitiveness of the UK.

16. How could the IFA regime be made more cost-effective?

See our comments to Q11. Aggressive tax planning regarding internally generated patent IP and related know-how is not common in our view and therefore relaxations to the degrouping rules could be made for these forms of IFA without opening the floodgates to such tax planning.

17. Do you have any comments on the assessment of equality and other impacts summarised above?

No.

For any further information on the contents of this submission please contact Dr Martin Turner, Policy and Projects Manager, by emailing mturner@bioindustry.org.