

Intangibles Amortization Passes Amid Rate Increases

by Robert W. Wood • San Francisco

While we have cautioned in past issues that the Rostenkowski intangibles bill was no panacea (see *e.g.*, "Intangibles Bill Important, As Is Section 338," 2 *M&A Tax Rep't* 1 (August 1993), p. 1), now that the legislation has finally passed, it seems appropriate to review the major provisions of this portion of the new law. New Section 197 permits 15-year amortization of certain intangibles acquired and held in connection with a trade or business or an activity engaged in to produce income. While the intangible need not be acquired as part of a trade or business to be eligible, Section 197 generally does not apply to intangibles created by the taxpayer unless created in connection with a transaction that involves the acquisition of assets constituting a trade or business or a substantial portion thereof.

Even on this point, however, there are some refinements. Section 197 intangibles are considered created by a taxpayer even if produced for that taxpayer by someone else under a contract entered into before production of the intangible. However, there are exclusions for contracts entered into or renewed for the use of Section 197 intangibles, including licenses or permits granted by a governmental unit or agency, covenants not to compete entered into in connection with a transaction that involves the acquisition of assets constituting a trade or business or a substantial portion thereof, and franchises, trademarks, and trade names.

Although taxpayers may elect to apply the new provision to any Section 197 intangibles acquired after 7/25/91, there are anti-churning rules designed to prevent taxpayers from converting intangibles for which no depreciation or amortization deduction would have been allowed under prior rules into property qualifying for Section 197 treatment.

Defining Intangibles

The big question under the new provision is sim-

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ply what kind of intangibles qualify. Section 197 intangibles include:

- Goodwill and going concern value.
- Workforce, information base, know-how, customer-based intangibles, supplier-based intangibles, and similar items.
- Licenses, permits, and other rights.
- Covenants not to compete and similar arrangements.
- Franchises, trademarks, and trade names.

Some of these items are the subject of extensive definitions. The list of items that do not qualify under Section 197 is equally noteworthy:

- Interests in a corporation, partnership, trust, or estate.
- Interests in land.
- Interests under certain financial contracts.
- Interests in films, sound recordings, video tapes, books, or other similar property.
- Certain computer software.
- Interests in patents or copyrights.
- Leasehold interests of tangible personal property.
- Rights to receive tangible property or services.
- Interests as a debtor or creditor in indebtedness.
- Professional sports franchises.
- Purchased mortgage servicing rights.
- Rights of fixed term or duration.
- Certain transaction costs.

At least for now, certain questions about the availability of amortization for some intangibles have been laid to rest. ■