DOLINKA, VANNOORD & COMPANY
A PROFESSIONAL LIMITED LIABILITY PARTNERSHIP
Certified Public Accountants

Self-Created Intangibles No Longer Qualify for Favorable Capital Gains Tax Rates

Effective for asset dispositions in 2018 and beyond, the TCJA states that certain intangible assets can no longer be treated as capital gain assets, as they were in the past. Instead, any gain on the sale of these assets will be taxed at ordinary income tax rates, which even under the new tax regime are significantly higher than capital gains tax rates. They include:

- Patents
- Inventions
- Models and designs (whether or not they are patented)
- Secret formulas or processes

On a positive note, it appears that Congress did retain the narrow exception provided by Section 1235 that allows some inventors (individuals) and investors (partners in partnerships) the opportunity to still receive capital gain treatment when transferring "all substantial rights" to a patent. Unfortunately, Section 1235 does not apply to self-created non-patent property (e.g. inventions, models or designs [unpatented], or secret formulas or processes); it narrowly applies only to patents. This makes it important for individual inventors or their investors to structure the ownership of their patents in a way that may allow the flexibility to utilize Section 1235's benefits at some point in the future.

Also, taxable gain on the sale of intangibles that are not specifically identified above (such as goodwill, workforce in place, trademarks, customer-based intangibles, and supplier intangibles) can still be taxed at favorable capital gains rates.

Therefore, to minimize a seller's tax liability, it is important, upon a sale of assets, to identify each type of intangible being sold and the portion of the total sales price being allocated to each.

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