



Smart decisions. Lasting value.

Selling your Business

How to maximise value and avoid pitfalls

10 February 2022



Overview

The sale of a business is a landmark occasion for a vendor – early preparation can maximise value and tax-efficiency. Today we consider the steps a vendor and the business itself can take to meet these objectives.

Preparing yourself as vendor for a sale

- Identity the key tax reliefs that may be available on a sale.
- Timely planning to enable you to avail of these reliefs and maximise value.

Preparing the business for sale

- Building and identifying value with a view to maximising the sale price.
- Incentives for employees – will they share in the proceeds?
- Pre-sale reorganisations?

Also, many of the key tax reliefs may be under threat. Is 2022 the year to claim them? Remember too that selling your business is a process that takes time, so early engagement is critical.

Vendor Preparation

Key Tax Reliefs



Key tax reliefs

CGT Reliefs

- Retirement Relief
- Entrepreneur Relief
- Holding Company Exemption

Cash Extraction

- Pension contributions
- Ex-gratia payments ('Golden Handshake')

Retirement Relief

Where Retirement Relief applies, it exempts from CGT:

- Proceeds of up to €750,000 – reduces to €500,000 at age 66.
- Where sold/transferred to your children there is no upper limit to age 66, then €3m thereafter – might be especially relevant for gifts.

Conditions

In the case of a company being sold:

- Trading company (or holding company of a trading group).
- Vendor aged 55+.
- Family company – 25% shareholding, OR 10% if family controls 75%.
- Vendor has owned the shares for at least 10 years.
- Working directorship requirements for ten years (five as full-time).
- Bona fide test.

Retirement Relief - Pinchpoints

Careful planning is advised in order to maximise Retirement Relief claims – also consider in context of other reliefs. Some key pinchpoints include:

- Are there any non-qualifying assets within a company that may deny/dilute relief?
- What if proceeds are likely to exceed €750,000?
- Married couples – structuring shareholdings to maximise relief. Problematic after age 55.
- Interaction with Entrepreneur Relief – can you claim both?
- Property owned personally but used by the company – can qualify with careful structuring.
- What if you have a holding company – how to structure disposal?
- What if vendor is approaching age 66?

Entrepreneur Relief

A reduced CGT rate of 10% on the first €1million gains on disposals of qualifying business assets.

Conditions

In the case of a company being sold:

- Must have owned the shares being sold for the previous 3 years.
- Must have held at least a 5% shareholding for a continuous 3-year period (at any stage).
- Must have worked for the company in a managerial/technical capacity on a full-time basis for a continuous 3-year period within the previous 5 years.
- Must be a trading company or the holding company of a trading group.

Entrepreneur Relief - Pinchpoints

As with Retirement Relief, advance planning is advisable. Some pinchpoints that can arise:

- Married couples and maximising relief – early planning advisable. Critically, ownership periods don't amalgamate.
- Group structures with non-qualifying subsidiaries:
 - Rental company
 - Dormant companies
- Property held personally but used by company – won't qualify.
- Interaction with Retirement Relief.

Holding Company Exemption

Advantages of holding companies:

- Can receive dividends from subsidiaries without giving rise to additional tax.
- Sale of shares in a trading subsidiary can qualify for a CGT exemption, provided:
 - Holding company owns at least 5%
 - For at least a 12-month period
 - Subsidiary is resident in Ireland/EU/DTA country
 - Subsidiary is a trading company, or the group as a whole is a trading group
 - Subsidiary does not derive majority of its value from Irish land & buildings
- Holding company then has the gross proceeds of share sale/dividends to reinvest, potentially enabling greater long-term wealth creation.
- In multi-shareholder structures, holding shares through personal holding companies can also facilitate the tax-efficient distribution of profits (and sales proceeds), thereby potentially leading to more harmonious decision-making.

Holding Company - Challenges

How to ultimately extract the proceeds of the share sale from the holding company ('Hold Co')?

- Take ongoing dividends from Hold Co – subject to Income Tax but only on the element you extract. Reinvest the rest inside the company.
 - Ultimately liquidate Hold Co – CGT at up to 33%.
 - Might still qualify for Retirement/Entrepreneur Relief if you carried on a new trade post-sale.
- But if you didn't, then those reliefs may not be available – there might be an element of trade-off, forgoing the CGT reliefs for the benefit of gross reinvestment.
- If you just want the proceeds in your own hands upfront:
 - Consider selling the holding company, if possible.
 - Can you get the Retirement/Entrepreneur Relief if buyer buys the trading company and you immediately liquidate Hold Co? Maybe, but careful structuring required.

Hybrid Solution?

It may be possible to put in place a hybrid structure to take advantage of a number of these reliefs.

Example

Jim and Mary own a trading company ('Trade Co') valued at €10m.

Put a holding company in place; holding company acquires 80% of Trade Co by share-for-share. Only tax cost should be Stamp Duty of €80k.

Jim and Mary retain 20%.

Company subsequently sold for €10m:

- Jim and Mary receive €1m each. Pay 10% CGT (Entrepreneur Relief).
- Holding Company receives €8m tax-free.

Complex issues and careful advance planning required.

Pensions & Ex-Gratia Payments

Pensions & ex-gratia payments can serve a number of purposes:

- Tax-efficient withdrawal of cash from the company.
- Reduces value of company; in some cases, helps meet conditions for key CGT reliefs or maximises utilisation of such reliefs.

Pensions – tax advantages:

- Contributions should be tax-deductible.
- Tax-free growth inside the pension fund.
- Tax-efficient withdrawal on retirement: 25% lumpsum, balance to ARF. Can pass through your Will tax-efficiently.

Ex-gratia termination payments:

- On resignation/retirement from directorship or employment.
- Different formulae apply, based on salary and service levels. Potentially a year's salary for each 15 years' service.
- Absolute maximum €200,000.
- Formulae linked with pensions – consider both in tandem.

Reliefs under Threat – Time to Act?

Commission for Taxation reviewing all of these reliefs.

ESRI paper from May 2021 questions efficiency of these reliefs notably Entrepreneur Relief.

Department of Finance Tax Strategy Group reviews in 2020 & 2021 questioned if Entrepreneur Relief meets policy objectives.

UK Treasury critical of UK Entrepreneur Relief (similar to Irish relief) and in 2020 cap on relief scaled back from Stg£10m to Stg£1m.

Key Dates:

- Budget: October 2022.
- Finance Act: November/December 2022.

Time to act?

Company Preparation



Pre-sale Restructuring – Relevant?

In many cases, the preferred course of action can be for the vendor to sell the shares in a company directly to the purchaser. In some cases however, complexities can arise. For example:

- The company owns premises which the purchaser does not wish to acquire.
- The company may have investment assets which the purchaser may not want and which may also compromise a claim for key CGT reliefs.
- The company may be carrying on more than one trade, or perhaps the purchaser only wishes to acquire part of a trade.
- It might be desirable to sell a ‘clean’ new company without any history, thereby reducing Due Diligence requirements.

In other circumstances, rather than sell the trading company the vendor may be attracted to the benefits of a holding company structure – might it be possible to implement one pre-sale?

Pre-sale Restructuring 1: Three-Party Swap

There are a number of ways of restructuring companies where not all of the assets are to be sold. One popular method is a Share-for-undertaking ('three party swap'), which entails:

- An undertaking (typically the trade) being transferred ('hived out') to a new company ('New Co')
- In return, New Co does not pay anything to the existing company; instead, it issues shares in itself to the shareholders of the existing company.
- Net result is that the individual shareholders now own two separate companies, one of which ('New Co') contains only the assets/business that the purchaser wishes to purchase.
- They then sell New Co to the purchasers and retain the other company.
- This type of restructuring can also be useful to facilitate/maximise CGT reliefs even where the entire company is being sold, e.g. to split out non-qualifying assets, or to bring qualifying proceeds (Trade Co) within the threshold for Retirement Relief.

Three-Party Swap – Tax Treatments

Tax legislation contains a range of reliefs, which may be availed of if the restructuring is executed in line with the legislative requirements:

- No tax on the execution of the restructuring:
 - Stamp Duty relief for New Co on acquiring the assets (Section 80, SDCA1999).
 - CGT relief for the individual shareholders (Section 587, TCA1997). Instead, a portion of their original base cost in the existing company transfers to their shares in New Co.
 - CGT relief for the transferor company (Section 615, TCA1997). Instead, New Co deemed to acquire assets at same base cost and same date as transferor company.
 - Not treated as a dividend for tax purposes.
- Preservation of key CGT reliefs:
 - Ownership periods and working periods across the two companies can be amalgamated for Retirement Relief/Entrepreneur Relief purposes.

Pre-sale Restructuring 2: Group Structures

Individual shareholders may wish to receive some or all of the proceeds through a holding company, thereby availing of CGT exemption (Section 626B, TCA1997).

Is it too late to do this? Maybe not:

- Holding Company would be deemed for CGT purposes to acquire the shares in the trading company at current market value so, if no further uplift on sale, no capital gain might be realised.
- Any further uplift would be taxed – however, if the holding company is put in place now, then by the time sale is completed, 12 months may have elapsed and Section 626B may apply.

Hybrid structures (as illustrated above) can be put in place to allow for a split in proceeds between individual shareholder and holding company. But must be done in a timely manner.

Additional complexities can arise if multiple shareholders involved.

Implementing Group Structures – Tax Treatments

There are a number of ways of implementing a group structure but typically at its core is a 'Share-for-share Exchange'.

If done in line with legislation, this can attract a range of tax reliefs.

No tax on execution:

- No CGT for the individuals who transfer their shares to the holding company. But Hold Co must get control (or make the offer conditional on getting control) of target company, i.e. more than 50%.
- No Stamp Duty for holding company. But must be acquiring 90% of target company, also subject to a two-year clawback so Stamp Duty is a more difficult relief to obtain. However, ultimately Stamp Duty on shares is generally 1% so might be a bearable cost?

Preservation of key CGT reliefs:

- Ownership and working periods generally amalgamate for purposes of Retirement/Entrepreneur Relief.

Incentivising Employees

Where a business is being prepared for sale, you may wish to consider incentivising employees and enabling them to share in the benefit. This is a complex area but some thoughts:

- You could simply pay them a 'farewell bonus' on sale – generally subject to Income Tax.
- Phantom Share Scheme – essentially a bonus calculated by reference to the share price. Should be subject to Income Tax but potentially a good way to reward them for a higher than expected sale price.
- Share Option Schemes? Again, Income Tax but might meet commercial objectives.
- KEEP? – A form of Option Scheme that potentially qualifies for CGT treatment.
- A Restricted Share Scheme if you are looking at say a 3-5 year horizon for sale. A mix of Income Tax (but reduced by up to 60%) and CGT.

Commercial Issues – Maximising Value

If considering a sale, important to do the preparatory work to maximise value from transaction.

- Get the presentation right – e.g. maximise efficiencies and address deficiencies so that the business is at its strongest when being presented to potential purchasers.
- Identify any issues that need to be corrected or ironed out, e.g. any tax issues, potential claims, HR problems, banking issues. These are relevant both from a value perspective and also in the context of preparing for a Purchaser Due Diligence.
- Analyse the likely value of your business and a realistic sales price. Preparing in advance will enable you to go to the market on your terms and better prepared, rather than waiting for and reacting to offers.
- Impact of Covid on value? Relevant to some businesses at the moment.
- Consider your attitude to how the consideration is funded, e.g. earnouts or deferred consideration? Being flexible might get a deal across the line but are you willing to take risks?

Summary



Summary

Selling a business is a big milestone and potentially a one-off opportunity to realise significant value in a tax-efficient manner:

- There are a number of reliefs that can greatly reduce the tax costs while also facilitating further wealth-creation post-sale in a tax-efficient manner.
- Could these reliefs be in danger and is 2022 to time to sell?
- Selling a business can be a lengthy process so early engagement is advisable. And, even if you are not yet considering selling, it is advisable to regularly review whether you meet the conditions for key tax reliefs and take any actions that might maximise use of them down the line.
- Commercial objectives will also have to be considered. These should drive the process and then look to get the best tax result to fit.
- Finally, good legal advice is always a pre-requisite when selling a business....

Thank You

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