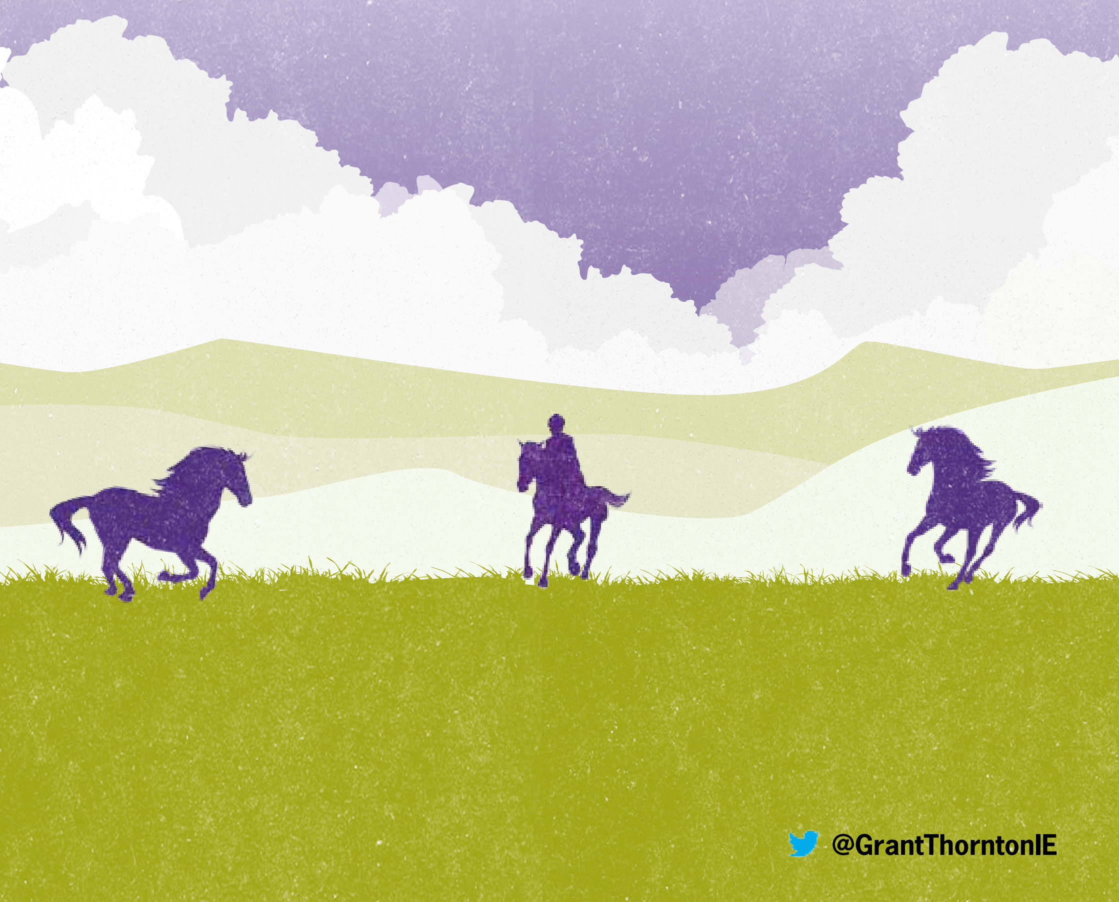
Grant Thornton

An instinct for growth™

Front runner across the sport

Clearing the hurdles



@GrantThorntonIE

Overview

This booklet provides a high level overview of some of the current key areas that people involved in various aspects of the equine industry are likely to encounter. There have been recent legislative changes introduced in the areas of taxation and financial planning discussed below and hence for optimal business planning/structuring purposes it is important that businesses give these areas some thought and focus.

This booklet does not aim to be a comprehensive guide, rather it highlights the main areas that businesses operating in this industry should consider and seek further advice on as needed.

Incorporation – impacts of operating via a sole trader v company structure

With the Irish corporation tax rate being one of the lowest in the EU at 12.5% but the top rate of personal tax being 55%, more and more farming sole traders /partnerships are considering the benefits of trading through a company. However it is not a 'one size fits all' option – the decision to incorporate should be made on a case by case basis and only after considering all taxes, bank debt, cashflow projections and of course family interests.

Key benefits

Managed tax costs - sole traders/partners are liable on their taxable profits, irrespective of whether they actually need that level of after tax income to fund their lifestyle. In a company it is only the salary drawn down that is liable to income tax. The balance of trading profits can be retained in the business and should be liable to corporation tax at 12.5%.

Increase in working capital - sole traders fund their working capital costs from their after tax income so potentially only 45% of profits remain for re-investment. Corporates likewise, fund the company's working capital from after tax income but in this case approximately 87.5% of profits may be available for reinvestment.

Pension funding - a company provides greater scope for pension funding for directors; and limited liability protection - the limited liability status of a company affords the protection of personal assets as you cannot be held personally liable for debts beyond the amount of capital contributed.

Key negatives

Increased compliance cost – cost of incorporation and annual compliance cost for the company.

Transfer of trade and funds - the trade, and potentially the assets of land/buildings, now belong to the company. Your access to funds will be either through salary, dividend, company loan or liquidation.

Tax costs - all tax heads must be considered (income tax, capital gains tax, VAT, stamp duty, succession planning) so as to ensure the relevant tax reliefs are available to minimise any tax cost of transferring from a sole trader structure to a corporate structure.

Department payments - department payments, grants and subsidies must be paid to the company.

In summary there is scope for flexibility in relation to profits earned by companies – funds can be retained in the company as working capital to be drawn down in future years, contributed into a pension or withdrawn on liquidation.

Capital investment – timing of relief and maximising claims

Working capital consists of the accumulated after tax profits retained by the sole trader or company plus any debt finance available to the business. Investment for growth and expansion is funded from working capital. However, the cashflow impact of such investment needs to be considered given that capital expenditure is not tax deductible in full in the year that it is incurred. Instead a capital allowance for offset against taxable profits is granted as follows:

- in the case of expenditure incurred on farm buildings and land improvement, the 'farm buildings allowance' is granted at 15% for six years and 10% in the seventh year; and
- in the case of plant and machinery, including motor vehicles* the allowance is 12.5% over eight years.

**An important qualification is that there is a limit on the allowable expenditure on motor vehicles. This limit also applies to lease/hire payments.*

It is important that sufficient focus is given to capital allowances claims to ensure, where possible, the expenditure being incurred can be identified and the relevant claims maximised. Effective capital allowance management can unlock substantial tax savings.

Succession – beneficial agricultural relief

Succession planning must always be given due consideration, especially the benefits of dealing with asset transfers during a lifetime rather than leaving all assets via a will. This area is particularly relevant to consider in light of the recent changes introduced in Finance Act 2014 regarding the qualifying criteria that beneficiaries need to satisfy in order to claim agricultural relief.

Agricultural relief is a 90% reduction in the market value of agricultural property for Capital Acquisition Tax (CAT) purposes which arises in a gift or inheritance tax situation. Hence a beneficiary in receipt of agricultural property worth €3 million that qualifies for the relief will only be deemed to have received €300,000 for the purposes of calculating their CAT liability.

In order to qualify for agricultural relief under previous legislation, an individual must have qualified as a 'farmer' on the valuation date i.e. 80% of their assets were agricultural assets and retain the the agricultural property for a period for six years (ten years in the case of development land).

The changes that have been introduced in Finance Act 2014 require that as well as satisfying the 'farmer' test at the valuation date, the property must be actively farmed in the six year period post the valuation date. This now makes the 'farmer' test more onerous to satisfy and increases the risk of potential clawbacks of agricultural relief, if not managed and reviewed on an annual basis.

The three alternatives for the beneficiary are:

- hold an appropriate agricultural qualification and for a period of not less than six years farm the land on a commercial basis and with a view to realisation of profits;
- for a period of six years commencing on the valuation date will spend not less than 50% of his/her normal working time farming the land on a commercial basis and with a view to realisation of profits; or
- lease the majority of the land for six years to an individual who meets either of the conditions above.

These new changes mean that in order to effectively transfer agricultural property from one generation to the next the timing of this and use of the property for the subsequent six years needs to be considered.

VAT – current focus

From 1 January 2015 following proceedings brought against Ireland at EU level businesses operating in the equine industry should re-consider the VAT rates applicable as the VAT rate chargeable will in most cases now depend on the “VAT status” of the purchaser.
The changes should not have an impact on the operation of the flat rate addition scheme.

Flat rate farmers as defined under VAT law, with existing or new income streams, should consider the impact these income streams may have on their status as a flat rate farmer and if required what options may be available to negate any negative impact.

Similarly racehorse trainers, who can effectively avail of a 2.3% VAT rate should also consider their VAT status and the impact existing or new income streams may have on the availability of the 2.3% rate and if necessary consider what options may be available to ensure the rate is retained.

Businesses may also wish to consider the VAT impact of moving horses into and out of training, the resulting VAT claw-back or VAT refund due and the VAT consequence of selling a horse while in training.

Pension planning – be prepared

It is fair to assume that very few of us would survive living off a state pension of €11,976 per year. On top of this, we are now faced with the reality that there will also be an income gap between the date most of us are scheduled to retire, age 65, and the date the state pension kicks in, age 67 or 68. Therefore, we need to understand where our finances currently stand and have a plan in place to fund for the years we won't have a regular or adequate income.

The attractive tax relief at marginal rate on pension contributions is still available which means setting up a pension plan is a very tax efficient way of saving for the lifestyle you want in later years. By claiming tax relief, a contribution of €200 per month will only cost you €120 and the earlier you start to contribute to a pension the more time your fund has to grow. Under pension arrangements you benefit from tax free growth of the funds and on retirement you are entitled to a portion of your fund tax free. Therefore, it makes perfect sense to redirect some of your savings into a pension plan to avail of these benefits.

Whether you are a cautious or high risk investor, there are many options available to you and you can choose a strategy which falls in line with your appetite for risk and to meet your expectations. It is of upmost importance that you are comfortable with your investment strategy regarding your pension contributions.

Contact

We would be delighted to meet with and advise you on any of the above topics or other tax related items that maybe relevant to you or your business same. Please feel free to contact any member of our team.

Sasha Kerins
Director, Tax
T +353 (0)1 6805 689
E sasha.kerins@ie.gt.com

Kevin Devenney
Director, Tax
T +353 (0)1 4366 481
E kevin.devenney@ie.gt.com

Oliver O'Connor
Director, Financial Counselling
T +353 (0)1 6805 679
E oliver.oconnor@ie.gt.com

Brendan Murphy
Manager, Tax
T +353 (0)1 4366 462
E brendan.murphy@ie.gt.com

Elaine O'Gara
Manager, Tax
T +353 (0)1 6805 616
E elaine.ogara@ie.gt.com

24-26 City Quay, Dublin 2

@GrantThorntonIE

www.grantthornton.ie

Offices in Dublin, Belfast, Cork, Galway, Kildare and Limerick.

Grant Thornton
An instinct for growth™