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BUSINESS SUCCESSION PLANNING

Business Succession Planning is a critical strategy for ensuring the continuity, sustainability, and growth of businesses.

By implementing a formal succession plan, identifying potential internal candidates, and investing in their development, the business will hopefully ensure a smooth leadership transition and continued growth. Without planning, a business faces potential disruption when the founder(s) either wishes to exit voluntarily or exit is because of death. In addition, business owners should plan for any CGT (Capital Gains Tax) implications and how they may be mitigated. This document looks at both the CGT tax relief for the disponer available in the event of a business disposal and the CAT implications for the beneficiary in the event of a gift or inheritance of a business. The questions both parties should ask are. What are the reliefs available? How do these reliefs work? What are the qualifying requirements for such reliefs?

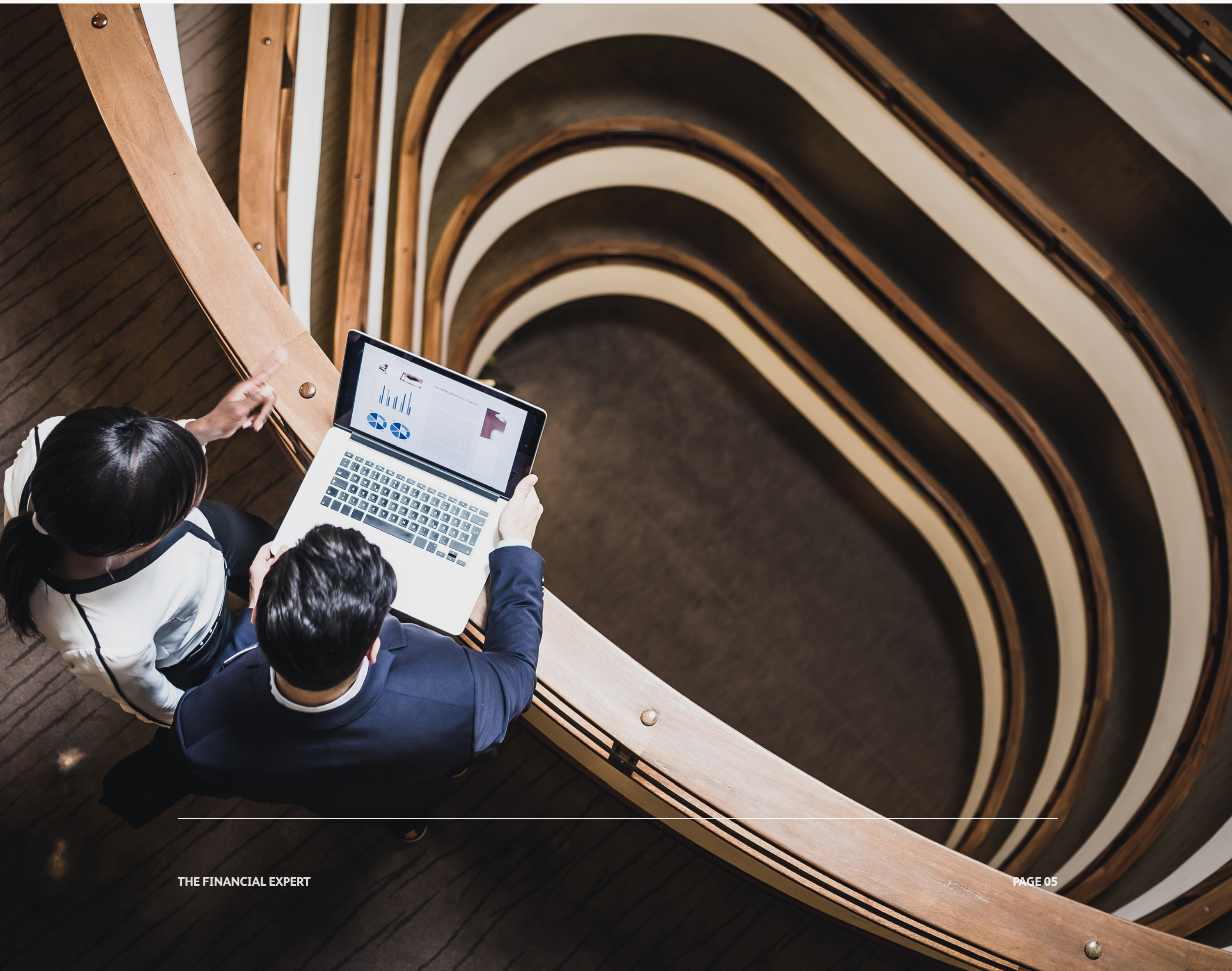
This is an enormous and very complex area, and this document is not nor is it ever intended to be, an exhaustive analysis of this area. Instead, its purpose is to simply give an overview of the potential tax implications and reliefs available for both disponer and recipient in the event of a business disposal. This document should be useful for Financial Advisors whose business owner clients will, at some stage, start to think about an Exit Strategy and Succession Planning. Why? Simply because if there is no advance planning, then, potentially the business dies with them. For this reason alone, Succession Planning is a topic that should be high on business owners-agendas. Hand in hand with Business Succession Planning goes tax planning as in the event of a business disposal there could well be significant tax implications for both the disponer and the recipient. These tax implications can be mitigated with careful planning and the use of existing reliefs. We should not assume that all business owners are aware of the available reliefs and their application. It is not the role of the Financial Advisor to give advice in respect of these reliefs. However, it is important as financial advisors that we are aware of these reliefs. The use of reliefs provides the following benefits.

1. **Tax Efficiency:** By reducing or eliminating CGT liability, business owners can transfer their assets without incurring prohibitive tax costs, preserving more value within the family or for the business's future.
2. **Encouragement of Succession Planning:** The relief encourages older business owners to plan for the future, ensuring that businesses are handed over smoothly and without financial strain.
3. **Support for Business Continuity:** Particularly for family-run businesses, the reliefs help maintain operations across generations, which can be critical for local economies and employment.

Obviously, as Financial Advisors, our role does not involve tax advice. However, in our role as advisor we may be involved in arranging life cover or pensions to assist in Succession Planning and as such, this will often involve meetings/ communication with the client's accountant and tax advisor, where the various tax reliefs and their interactions would be discussed. Thus, a basic knowledge of these tax reliefs is desirable. To start with: what are the available reliefs and to whom do they apply?

AVAILABLE RELIEFS

- Retirement Relief (The Disponer)
- Entrepreneur Relief (The Disponer)
- Business Relief (The Beneficiary)
- Agricultural Relief (The Beneficiary)
- Favourite Nephew/Niece Relief (The Beneficiary)



RETIREMENT RELIEF

Retirement Relief (RR) is a provision under Irish tax law that allows individuals who are disposing of business assets to potentially reduce their CGT liability.

Despite its name, the relief does not require the individual to actually retire from business activities. The primary aim is to encourage older business owners to pass on their business assets, thereby facilitating smoother succession and preserving business continuity. RR (subject to qualifying conditions) applies to the disposal of either a business or a farm (see point 2 below).

To qualify for RR, several conditions must be met:

- **Age Requirement:** The individual must be at least 55 years old at the time of the disposal of the asset. There is no upper age limit for claiming the relief, although the amount of relief available can vary depending on age.
- **Qualifying Business Assets:** The assets must have been owned and used by the individual in their trade, profession, or occupation for a minimum of 10 years prior to disposal. These assets typically include business premises, farmland, and shares in a family company.
- **Type of Disposal:** The disposal can be to a family member or a third party. However, the level of relief varies based on the recipient of the asset. The amount of relief available depends on whether the transaction relates to a Family Transfer or Non-Family Transfer. When the disposal is made to a child *(which includes ,inter alia, a child of a deceased child, child of the civil partner as well as a nephew or niece who satisfy certain conditions and , in certain circumstances a foster child)* the relief is more generous. Currently for individuals under the age of 66, there is no limit on the value of assets that can qualify for full CGT relief. For those aged 66 and above, the relief is capped at €3 million and any excess value above this threshold will be subject to CGT at the standard rate of 33%. Where a transaction relates to a Non-Family Transfer, the relief is less extensive. For individuals under 66, the relief is available for disposals up to €750,000. For those aged 66 and above, the limit is reduced to €500,000. Gains exceeding these limits are taxable at the standard CGT rate. Revised thresholds are due to come into force from 01/01/2025.

Revised Thresholds 2025 The current thresholds on disposals of qualifying assets are due to change on 01/01/2025. For ease the table below shows both current thresholds and expected changes from 01/01/2025:

Disposal to:	Current Rules:	Changes- effective 1 January 2025
Child	• Unrestricted relief from 55 up to 65 years • From 66 years onwards relief restricted to 3m	• Up to 69 years for disposals over €10m there is a clawback period of 12 years after which the CGT will be abated. • from 70 years onwards relief restricted to €3m
Person other than a child	• Full relief on disposal of qualifying assts of up to €750k from 55 up to the age of 65 • From 66 years onwards the cap is reduced to €500k	• €750k is extended to 69 years • From 70 years onwards cap is reduced to €500k

The relief can also be extended to certain assets owned personally by the disponer **that were used in the course of the company's business where they are disposed to the same person at the same time, as the disposal of the shares in the family company. This in essence replicates the position which can apply for gift and inheritance tax business relief.**

ENTREPRENEUR RELIEF

CGT (Capital Gains Tax) "Entrepreneur Relief" (ER) applies on the sale of certain assets subject to satisfying certain conditions.

Since 1 January 2017, under Section 597AA of the Taxes Consolidation Act 1997, the rate of "CGT" under ER is 10%. The amount of qualifying "chargeable business asset gains", (see below) on which an individual can obtain the benefit of CGT ER is a lifetime cap of €1m.

To qualify as a "relevant individual", the chargeable business asset must have been beneficially owned by the individual for a continuous period of three years in the five years immediately prior to the sale of those chargeable business assets.

What are the main conditions that need to be satisfied by an individual to claim CGT ER?

For ER to be available, the main conditions to be satisfied by an individual are:

A. the asset(s) disposed of must be a "chargeable business assets"; and

B. The individual making the disposal must be a "relevant individual" and if that individual is disposing of a shareholding, that person must also be considered a "qualifying person".

Chargeable business assets are generally:

Assets owned by a sole trader and used in their trade, including goodwill, once the business operated is a "qualifying business". A share of assets owned by an active partner in a trading partnership should also qualify; and

Shares held by an individual in a trading company that operates, wholly or mainly, a qualifying business or in a holding company of a qualifying group (discussed below), once the shareholding held is 5% or more of the issued ordinary share capital of the relevant company (even though the entire shareholding does not need to be sold).

The business of the holding of investments and/or development land as well as the businesses of development or letting of land are not qualifying businesses for the purposes of this relief. Consequently the assets of such businesses do not come within the scope of this relief.

Unfortunately, any previous period of ownership of the assets by a spouse/civil partner is not aggregated in determining the continuous period of three years; nor does any period of ownership as a sole trader prior to the incorporation of a business.

Any period during which the individual owned shares in or was a director or employee of a company that qualified for CGT reliefs under restructuring provisions, may be considered for the purpose of the three-year ownership and director or employee requirements.

Two questions that are often asked are:

What is the difference between ER and RR?

Is there any interaction between ER and RR as both reliefs relate to the sale or transfer of assets?

The answer is that where RR applies to a sale or transfer of "qualifying business assets" by an individual, any gain arising is relieved wholly or partly from CGT whereas ER reduces the rate of tax at which CGT is payable up to the €1m lifetime limit for chargeable business asset gains.

ER has a lifetime limit of €1m on chargeable business asset gains since 1 January 2016, so any prior sales or transfers of any chargeable business assets on which gains arose and on which no or reduced CGT may have been paid due to CGT RR applying, are aggregated in determining whether the €1m threshold has been exceeded and, if so, 33% tax is applied to the excess.

BUSINESS RELIEF FOR THE BENEFICIARY?

Business Relief (BR) is a provision under Irish tax law that reduces the taxable value of relevant business assets by 90% of that value for CAT purposes.

It applies to gifts and inheritances taken on or after 23rd January 1997. However, for the relief to apply, the beneficiary must meet one of the following ownership/control tests:

1. The shares themselves or together with other shares in the company, held in the absolute beneficial ownership of the beneficiary, give the beneficiary control of 25% of the voting power over all matters relating to the company,

or

2. ii) The beneficiary controls the company, or the company is controlled by the beneficiary and their relatives, *

or

3. iii) The beneficiary holds at least 10% of the issued capital of the company and has worked full time in the company for five years prior to the gift/ inheritance.

*Relatives of a person include their spouse or civil partner, their children or the children of their civil partner, mother, father, aunt/ uncle; and any children or grandchildren of any of the forgoing. In addition, all spouses or civil partners of relatives are included for the purposes of determining control.

Control includes - having over 50% of the voting power, or owning more than 50% of the shares, or being in a position to control the board of directors.

What about Unincorporated Businesses?

Relevant business property also includes property consisting of a business (sole trader) or an interest in a business (share in a partnership).

A business that is wholly or mainly concerned with dealing in land, shares, securities or currencies or the making or holding of investments is excluded. The relief will apply where the business or part of the business is transferred, but not simply where an asset that had been part of the business is transferred – this is subject to CAT.

General Qualifying Conditions

Along with the conditions that apply to the business and the beneficiary to qualify for BR, there are some other general conditions worth noting:

1. **Disponer**
   The property must have been owned by the disponer for a period of five years prior to a gift or two years in the case of an inheritance.

1. **Claw-back of Relief**
   If within six years of the gift or the inheritance of business property:

- the business ceases to qualify, or the property is sold or compulsorily acquired and not replaced within one year with other business property the entire relief will be clawed back.

AGRICULTURAL RELIEF FOR THE BENEFICIARY?

First a brief overview of this relief. It is given in respect of certain agricultural property taken by a "farmer". The relief reduces the market value of the agricultural property by 90% for gifts and inheritances taken on or after the 23rd of January 1997.

The market value of the agricultural property as so reduced is then termed "agricultural value" in the Act and is substituted for market value in the calculation of tax.

In addition to the relief available on the value of farmland, buildings and stock, agricultural relief (AR) can be claimed where a gift of, say, cash from an investment-based estate is gifted to a qualifying 'farmer' on the basis that the asset is converted to qualifying agricultural property within two years of the date of the gift or inheritance.

What this means in effect is that the asset gifted does not have to be agricultural property, but once the gift is made subject to it being converted to qualifying agricultural property by a qualifying farmer, AR can still be claimed on the gift or inheritance where the recipient is a qualifying farmer. It must be noted that if a gift or inheritance does not qualify for AR it may still qualify for BR provided that the conditions are met particularly that a farming business is being passed on **including, in certain circumstances, farm land which is the subject of a conacre letting. One point to note is that on foot of amending legislation in Finance Act 2020, a gift or inheritance tax return (IT38) must be filed, where AR or BR is being claimed, notwithstanding that the taxable value of the gift or inheritance is below the 80% requirement threshold for filing this return**.

Now a look at some specific Revenue Guidelines.

The market value of the agricultural property as so reduced is then termed "agricultural value" in the Act and is substituted for market value in the calculation of tax.

Budget 2025 Amendment to CAT Agricultural Relief Postponed

A new measure was announced in Budget 2025 which required that the donor meet a six year 'Active Farmer' test for the beneficiary to benefit from AR. It was intended as a measure to narrow the relief to benefit farmers i.e. to safeguard AR for the genuine active farmers and the next generation of farmers. However this measure has now been postponed. There will be no changes until proper consultation and engagement with the agricultural sector.

Revenue Guidelines for Agricultural Relief

With effect from 1st January 2015 changes were made to the conditions for AR from CAT which are designed to confine the relief to genuine farmers and ensure productive use of the agricultural property.

For gifts and inheritances taken on or after 1st January 2015 the beneficiary must satisfy the following additional conditions:

1. Have an agricultural qualification (a qualification of the kind listed in Schedule 2, 2A or 2B of the Stamp Duties Consolidation Act 1999) or obtain such a qualification within four years and farms the agricultural property for a period of not less than six years on a commercial basis and with a view to the realisation of profits.

or

2. Spends not less than 50% of his or her normal working time farming agricultural property on a commercial basis with a view to making a profit for a period of not less than six years commencing on the valuation date. "Normal working time" (including on-farm and off-farm working time) has been defined by Revenue as 40 hours per week. This will enable farmers with off-farm employment to qualify for the relief provided they spend a minimum of 20 hours working per week, averaged over a year, on the farm.

Alternatively, where the beneficiary leases the agricultural property, the individual to whom the property is leased must also satisfy conditions 1. or 2. above.

The relief can be withdrawn in certain circumstances:

A. If, within six years of the 'valuation date', the beneficiary ceases to qualify as a farmer as set out above and does not lease the land to a qualifying lessee who will farm the land for the remainder of the six-year period.

B. If, within six years after the date of the gift or the inheritance lands are sold or compulsorily acquired in the lifetime of the donee or successor, and the agricultural property is not replaced within a year following a sale, or within six years following a compulsory acquisition where the land was compulsorily acquired on or after 25th March 2002.

If the gift or inheritance consists of development land and is disposed of in the period commencing six years after the date of the gift / inheritance and ending ten years after the date, there will be a partial claw back of AR.

FAVOURITE NEPHEW/ NIECE RELIEF

Favourite nephew/niece relief entitles a beneficiary who is a child of the disponer's brother or sister or a child of the civil partner of the disponer's brother or sister to be treated as a 'child' of the disponer, provided certain conditions are met. Where the relief applies, the niece or nephew is entitled to the Group A threshold instead of the Group B threshold.

The relief applies to a niece or nephew who has worked substantially on a full-time basis for the disponer for the period of five years ending on the date the disponer ceases to have a beneficial interest in possession in the business. The relief will only apply to assets used in connection with the business. Note that farming is a business for the purposes of the relief. In order to qualify for the relief, the beneficiary must have worked a minimum number of hours in the disponer's business, i.e.

- 15 hours per week in a small business, i.e. a business carried on exclusively by the disponer, the disponer's spouse or civil partner and the nephew/niece.
- 24 hours per week in a larger business, i.e. where there are other employees.

As outlined earlier in this paper the relief (Group A threshold) will only apply to business assets. If there is an inheritance/gift of both business and non-business assets, the Group A threshold will apply to the business assets and the Group B threshold will apply to the non-business assets. As only benefits within the same Group threshold aggregate, the beneficiary aggregate, the beneficiary will have two separate thresholds if the benefit consists of both business and non-business assets.

BUSINESS SUCCESSION PLANNING IN THE EVENT OF DEATH

This paper has looked at the reliefs available for a ‘planned business succession’, however the unexpected death of a shareholder in a private limited company or partnership can cause problems for both the surviving shareholders/partners and the deceased’s next of kin. It is our role as Financial Advisors to bring this to the attention of our business owner clients.

In doing so, we highlight the potential issues and give a possible solution. Now the business owner(s) can make an informed decision. The first logic step in this process is to highlight the potential problems arising on death.

Let us first look at the surviving shareholders and the problems that can arise which are:

- **Loss of control.** If the deceased owned more than 50% of the company, the other shareholders would now find themselves having to work with a new controlling shareholder, possibly the deceased’s spouse or one of his children. There could be disagreements about how the business should be run, particularly if the new shareholder had no experience of the business.
- **Refusal to sell.** The ideal outcome for the surviving shareholders may be to buy back the deceased’s shareholding from his next of kin. But what happens if they refuse to sell?
- **Lack of liquid capital.** Even if the deceased’s next of kin are willing to sell, the surviving shareholders simply may not have sufficient liquid capital to buy the shares from them. The surviving shareholders could borrow the necessary funds but they would then be faced with the burden of loan repayments for years to come.
- **Shares pass to outside party.** If the deceased’s next of kin want to sell and the other shareholders are financially unable to buy, then the deceased’s next of kin may be have to sell the shares to an outside third party, possibly a competitor or someone totally inexperienced in the business.

Now to the deceased shareholder's next of kin and the problems that can arise:

- **An illiquid asset.** If the shares are not sold, the next of kin may be left holding a 'paper asset' producing little or no income. The position could be even more serious if the shares also give rise to an immediate inheritance tax liability for dependants.

- **No ready market for shares.** The company's Articles of Association may give the other shareholders the right to block the sale of the shares to any outside party. The next of kin could therefore be forced into a 'fire sale' of the shares to the other shareholders at a low price in the absence of any other realistic offer for the shares.

Potential Solution

Having identified and discussed the problems arising on death the next step is to offer a potential solution. The solution is quite simple i.e. a life Insurance policy that would, in the case of a limited company provide, liquid capital on the death of a shareholder to enable

- The deceased's shares to be bought back **(including, subject to company law conditions and tax issues, by way of company buy back of its shares)** from his estate or next of kin and allow the surviving shareholders to maintain ownership and control of the business going forward.

The policy can be either:

- Personal Shareholder Protection
- Corporate Shareholder Protection

What about unincorporated bodies i.e. partnerships?

The problems associated with the death of a partner are the same as those with the death of a shareholder. The solution again is life cover. However, in this situation as there is no body-corporate, life cover can only be arranged on a personal basis and can be either.

- Own Life in Trust
- Life of Another

CONCLUSION

A quick look at Statista.com website gleaned the following interesting statistics.

In 2023 there were approximately 309,000 SME's operating in Ireland with the vast majority (281,305) being micro sized enterprises employing between 0 and 9 people. There were 23,461 small businesses employing between 10 and 49 employees and 3,843 medium sized businesses.

These figures will of course have changed but they give an idea of the number of businesses that, if they have not already done so already will in the future be looking at the whole area of business continuity/succession planning and the attendant tax implications.

Will these business owners require advice and guidance? Will we as Financial Advisors have a part to play in this process? Almost certainly, yes. Whilst we as Financial Advisors will not be involved in providing tax advice it is hard to see how we will not be involved in this process. It may be to simply open the discission and highlights the areas for consideration or it may well be that we are involved with the roundtable discussions involving accountancy/tax advisors. Financial Advisors and financial products will often have a role to play

in Business Succession Planning e.g. shareholder/partnership insurance, S72 and S73 policies or pension planning as a method of cash extraction from a business. These conversations will invariably take place in conjunction with accountancy/tax advice. Thus, a basic knowledge of the tax implications for both disponer and recipient re business transfers is important. As outlined earlier both the recipients of either a gift or an inheritance and the disponer of any property will usually seek professional accountancy/tax guidance relating to potential tax implications (CAT/CGT). Therefore, it is important that we as Financial Advisors have a basic grasp of the reliefs available and the qualifying criteria as we will have business owner clients who if not now will at some time in the future need advice/assistance regarding succession planning. However, to be clear, it is not our role as Financial Advisors to give tax advice. If not, tax advice what could be the role of the Financial Advisor in Business Succession Planning? It could be the prompting of a discussion to bring the issues and opportunities relating to Business Succession Planning to the attention of our business owner clients. Alternatively, if it is already a topic under discussion then we as financial advisors could find ourselves working in conjunction with accountants/tax advisors specifically in the use of insured products in assisting in Business Succession Planning. In these discussions, we as Financial Advisors should be seen as essential to the whole process of Business Succession Planning. To ensure that this is the case we need a working knowledge of this area, and this document is designed as an introduction to what is unfortunately a complicated field and highlights the importance of accountancy/tax advice. It should not be used as the basis for accountancy/tax advice. It is a Discussion Document only.

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