Calibrate Law

BRIEFING NOTE:

TAX ISSUES FOR BUSINESSES

The Tax Team at Calibrate Law comment on some of the tax issues we expect to see coming to the fore as we emerge from lockdown.

LOAN RESTRUCTURINGS AND RELEASES

Many businesses are likely to have suffered a fall in revenue and need additional working capital in the short term. However, for businesses in the travel, tourism, entertainment, retail and consumer sectors we can expect a long-term structural resetting of revenue to lower levels. To pass this on to their suppliers will likely require some level of consensual or Court driven restructuring. This in turn will have a knock-on effect into other sectors.

From a tax point of view, the release of a loan obligation can generate taxable income in the borrower, particularly when the loan comes from a private equity fund or similar. This can mean that at just the time the business needs maximum support it is hit with an unwanted (and avoidable) tax charge.

The key outtake here is to take tax advice on any debt for equity swap, loan release or restructuring before the structure is finalised. There are relatively easy ways to achieve the desired tax outcome, provided advice is taken at the right time.

EQUITY RESETS AND MANAGEMENT INCENTIVES

As people begin to look to the future, the earnings trajectory and capital structure of many businesses will have changed fundamentally. As such it will be necessary to update management incentive structures to ensure they still encourage the behaviours their owners want in their executive management teams without being either too generous or impossible to achieve.

As such there will be a need to carry out “resets” of old schemes or replace them with new schemes – both of which should be undertaken tax efficiently. This is an area where it is very easy to end up with big tax costs inadvertently on retiring an old scheme early, changing key performance hurdles or putting in place a new scheme which is not as tax efficient as the one it replaced. A crucial point is around agreeing tax valuations for new equity incentives - we are happy to help with any tax planning issues around long-term incentive schemes, including providing tax valuations

RECLAIMING TAX OVERPAID ON EARN OUTS

Many deals have an element of deferred or contingent consideration often based on the future profitability of the business. These often look forward over a number of years. For deals done prior to Covid-19 these forecasts may now be unrealistic and as such this additional consideration may now be very unlikely to arise. However, the capital gains tax due on all ascertainable consideration, even if contingent or deferred, is paid in full up front.

You can approach HMRC to arrange a repayment in these circumstances and we have considerable experience in assisting clients to claim repayments and in arranging for payments of tax on certain consideration to be deferred.

BEING SUCCESSFUL IN DISTRESSED ACQUISITIONS

On the plus side, we expect there will be opportunities for people to acquire fundamentally good businesses at attractive prices. From the last recession a common theme is that those who buy well in distressed transactions need to be able to move quickly and be flexible - accepting that in order to secure good assets they may have to take a commercial view on risk issues, particularly tax risks.

HMRC CHALLENGE

Whilst HMRC and the Government currently remain very supportive of businesses, at some stage the pendulum will swing and consideration will turn on how recoup the costs of the bail out. The tax burden will subsequently increase with an expectation that certain groups who previously benefited, such as self-employed workers can expect to see tax rises. Furthermore, as ever the wealthy and asset rich will surely be expected to take their share of the load.

As such it is imperative to get your tax affairs in order and make use of generous tax reliefs whilst they remain available. We would also recommend making use of this lock down period to get personal tax returns in early – remember the 12-month period for enquiries runs from the date of submission.

INCORPORATION

If the Treasury does increase the National Insurance burden on the self-employed and with trading profits over the next few years likely to be lower and with working capital stretched, partner drawings are likely to be reduced and subject to high effective tax rates. This could fundamentally decrease the material attractiveness of the LLP/partnership business model. If so, is now the time to incorporate your business and move from a self-employed or partnership/LLP structure back to a corporate business model.

EMI OPTIONS

There are a growing list of technical points which HMRC will need to iron out – for example if you are furloughed do your EMI options lapse because you no longer meet the requirement to work at least 25 hours a week or 75% of your time for your employer company?

RESIDENCE

The difficulties in undertaking international travel will generate issues around corporate residence, where for example directors are forced to attend offshore board meetings from the UK rather than flying overseas to attend in person. Could this increase the risk of HMRC claiming the company in question has become UK tax resident or at least has a taxable presence in the UK? Equally where people are stuck in the UK when they otherwise planned to leave, how will the UK statutory residence test be applied for such individuals? Whilst HMRC has issued some limited guidance around Covid-19 and the exceptional days rule there are many other points of detail where they have not provided guidance, particularly around the position for people who planned to emigrate this year and have had their plans delayed.

CRYSTALLISING TAX LOSSES AND REVIEWING VALUATIONS FOR INHERITANCE TAX PURPOSES

There is little good news in what has happened, but from a tax point of view it is worth considering whether you can crystallise any tax losses, say with negligible value claims or otherwise to shelter other taxable income and gains.

From an Inheritance Tax perspective there is also a qualifying relief where the proceeds obtained on the sale of certain investments, such as quoted shares and securities, are lower than anticipated (provided the sale occurs within 12 months of the death of the individual in question or within four years in the case of land). As such anyone dealing with the administration of an estate should take tax advice as the timing and order in which assets are realised can influence the eventual tax liability.

NEXT STEPS

We have extensive experience of helping clients with strategic tax advice. If you would like to discuss what options might work for you, please get in touch.

If you have any questions arising from this briefing note or would like to discuss how it may affect you or your business, please contact pc@calibrate-law.com

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