

## Preparing a Business for Sale - Tax Issues

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Selling a business for most entrepreneurs is a life changing event, involving extensive planning and negotiation on the realisation of their biggest single asset. It is also fair to say that on selling their business they are also faced with their biggest ever tax liability! Therefore managing tax related issues and the final tax liability deserves a proper investment of time, attention and planning.

### Start Early

When consideration is being given to the sale of a business, it is also the right time to look at any tax planning which can be undertaken to minimise tax leakage. Starting early in this process provides the opportunity to maximise important tax reliefs which are available on the disposal of a business such as Entrepreneurs relief.

The share ownership test for Entrepreneurs Relief requires 5% or more of the share capital and voting rights to be held by an employee or officer of the company for at least 12 months before disposal. Often pre-sale tax planning looks at trying to ensure the spouse also qualifies for Entrepreneurs Relief, and therefore obtain another £1million of gain at the favourable 10% capital gains tax rate. If this planning is missed or not undertaken at least 12 months before disposal, it could cost up to £80,000 in additional capital gains tax.

### Establish Exactly What is for Sale

All too often in transactions, there are capital assets within a company which need to be extracted for the retention of the vendor, or as a pre-requisite to the purchase. The most common asset to be removed from a transaction is freehold property. Planning around the extraction of a freehold property takes time, especially where the property is to be contributed into a Self Invested Personal Pension for the benefit of the vendor. The key to extracting the asset is to ensure that a material tax liability is not left behind in the company, which in turn can affect the sale proceeds.

It is key therefore to establish exactly what is for sale within the transaction and plan ahead for the valuation and extraction of any assets which are to be retained by the vendor, or parts of the business which need to be sold separately to achieve full value.

### Prepare for Due Diligence

The extent and depth of due diligence is down to the purchaser, but commonly the key areas include corporation tax, PAYE and VAT. The Due Diligence can cover everything from checking the compliance and submission of returns on a timely basis through to a detailed review of expenses and benefits policies for employees.

A good starting point is the last HM Revenue & Customs (HMRC) enquiry or inspection, to revisit any issues that were identified by HMRC and ensure they have been rectified. Issues arise on transactions where potential tax liabilities are identified late in the day and are a surprise to both the vendor and the purchaser. Do not underestimate the size of a tax liability which can be

identified, particularly when it is extrapolated over six years together with interest and penalties. Tax issues have the ability to de-rail a transaction so it is important that such issues are dealt with and a commercial, managed solution obtained for all parties.

## Tax Clearances

Tax clearances are often a new concept to entrepreneurs selling their business, especially if they haven't been through the process before. The benefit of applying to HMRC for tax clearance is to give the tax payer certainty over the filing position for their self assessment tax returns. The concept of tax payer certainty is an unusual one in a world of self assessment, but where the proceeds from a transaction are material, knowing the tax treatment enables the vendor to plan how to use the proceeds.

On the disposal of a business there are generally two tax clearances which are obtained from HMRC in advance of completion. The first ensures that the proceeds from the transaction are taxed as a capital gain, rather than taxed as income which would be subject to higher rates of taxation. The second clearance is in connection with deferred proceeds in a transaction, where the vendor may obtain shares or loan notes from the purchaser. This clearance delays the tax charge on an element of the shares which are exchanged into shares or loan notes from the purchaser until they are sold or encashed.

The tax clearance should be applied for to HMRC shortly after the deal terms have been agreed between the vendor and the purchaser. HMRC must reply within 30 days of receiving the clearance application, sometimes with further questions or additional information and so the clearance process needs to be built into the entire deal timetable.

## Summary

Careful tax planning through the disposal of a business can reduce the amount of tax payable by the vendor, enable the transaction to run smoothly and provide tax payer certainty. Get the tax planning wrong and you may lose out on important tax reliefs and potentially present yourself with a tax issue which could cause the deal to fall over.

In summary, the following main points should be addressed:

- ▶ Start tax planning early - to ensure all possible tax reliefs are obtained
- ▶ Establish what is for sale - identify and plan for assets which need to be removed
- ▶ Prepare for Due Diligence - to avoid unexpected tax issues
- ▶ Apply for tax clearances - to obtain tax payer certainty on the transaction

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