CPA IRELAND

Taxation considerations on the sale and purchase of a business – asset sale v share sale

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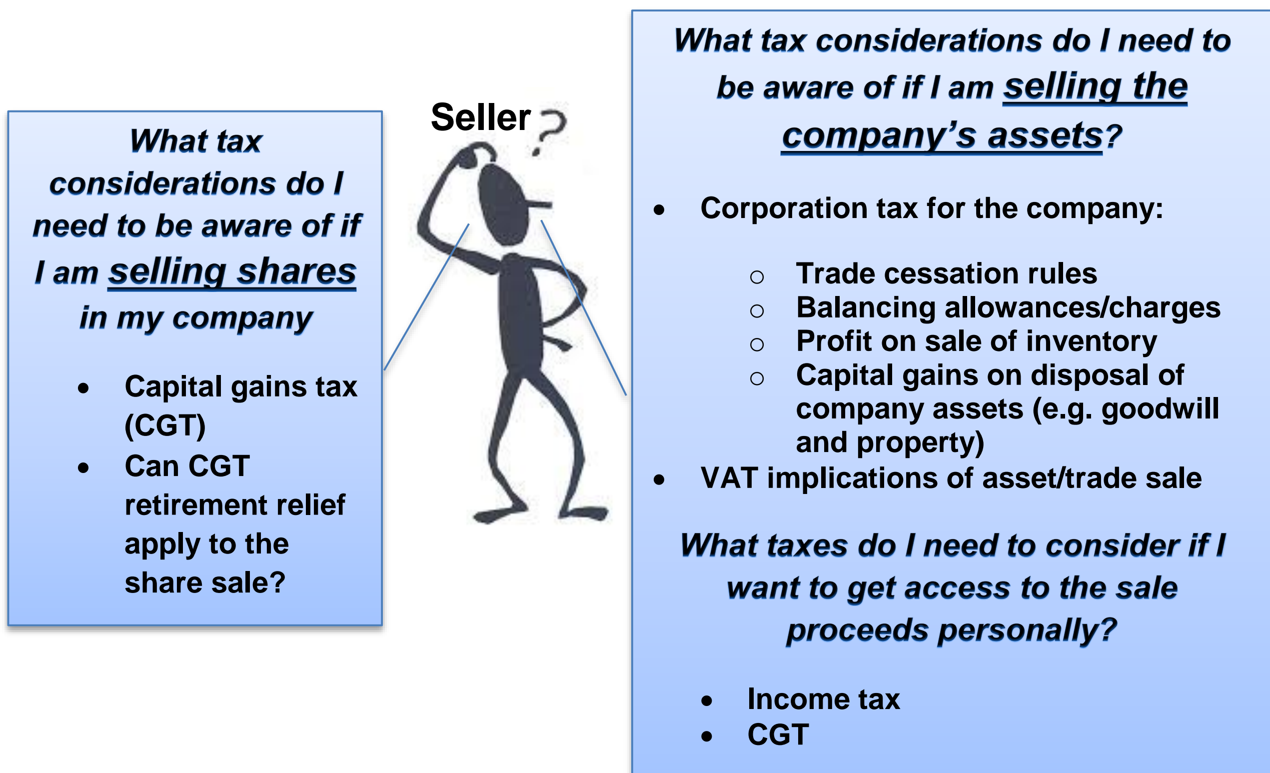
Depending on the type of business (i.e. sole trade, partnership or company), the sale of that business can be undertaken in a number of different ways. This article will concentrate on the tax implications for an individual who is the purchaser or seller of company shares versus the position where the assets of the company are purchased or sold. The advice that you provide in respect of the sale of a business will largely depend on whether you are advising the seller (sometimes referred to as the vendor) or the purchaser. This article will therefore look at these two perspectives separately. This article is of interest to students of Professional 2 Advanced Taxation.

Section 1 Advising the seller



1.1 Share sale

A major advantage of a share sale from the seller's perspective is that the proceeds of the share sale will be received by them personally. However, their CGT exposure will need to be considered.

Depending on the base cost of the shares that are being sold, there may be CGT due on the share sale. The base cost of the shares will either be the price paid for the shares (nominal value plus any share premium) or, where the shares were received by way of gift or inheritance, the market value used for capital acquisitions tax purposes will be relevant.

Where a shareholder is over the age of 55, the availability of retirement relief should be considered in order to reduce or eliminate any CGT due.

Recap of the main conditions for retirement relief – sale of shares

1. The individual must be aged 55 years or over at the time of sale.

2. The shares must be qualifying assets. That is, the shares must be held in a family trading company and the individual must have held the shares for a minimum period of 10 years. The individual must have been a working director of the company for 10 years, 5 years of which the individual must have been a full-time working director.

   The definition of a family company in relation to the individual disposing of the shares is one in which the individual owns at least 25% of the shares or a company in which the individual owns at least 10% of the company and the individual's family (in addition to the individual's holding) own at least 75% of the shares.

3. Where the shares are disposed of to anyone other than a child of the individual, a €750,000 limit applies to the value of the shares for retirement relief to apply. If the proceeds exceed €750,000, marginal relief may be available. Where the individual who is disposing of the shares is 66 or over, the €750,000 limit is reduced to €500,000.

1.2 Asset sale

1.2.1 Corporation tax implications

When a company sells its trade and assets, the trade of the company ceases. Therefore, the company cessation rules need to be considered. The date of sale will trigger the end of a tax accounting period and a corporation tax return will be due in respect of the accounting period to this date. Where the company was making losses in its final twelve months of trading, the availability of such losses for offset against capital gains arising on the sale should be considered in addition to the use of any remaining losses for terminal loss relief.

The creation of balancing allowances and charges need to be considered. These are calculated by comparing the tax written down value (TWDV) of the asset to the sales proceeds attaching to that asset. A balancing allowance will arise where the TWDV is more than the sales proceeds and it will reduce any corporation tax due. A balancing charge will arise where the TWDV of the asset is less than the sales proceeds. Balancing charges are limited to the amount of capital allowances previously claimed in respect of the asset but are effectively negative capital allowances which will increase any corporation tax due.

In addition, if inventory is being sold at a profit, then this will have implications for the corporation tax due for the final trading period of the company as the profit will be treated as a trading receipt.

When a company sells assets such as goodwill, property or plant and equipment the company's liability to corporation tax on the capital gains arising need to be considered. Usually, goodwill will be quantified by calculating the difference in the agreed price for the assets versus the value of the company's net assets. As such, any goodwill arising on the sale will have a nil base cost.

The base cost for any land and buildings which are sold will need to be established and the capital gain calculated. Any enhancement expenditure and costs of acquisition should be taken into consideration.

In respect of plant and equipment which is sold, where the sales proceeds exceeds the original cost of the asset a capital gain will arise. Where a capital loss arises, it will be reduced by any capital allowances previously claimed.

1.2.2 VAT implications

If assets (such as property, plant and equipment) are sold then VAT may be chargeable on the sale of those assets at the appropriate rate. However, where a transfer of a trade is taking place, it may be possible to claim the transfer of a business as a going concern exemption.

Recap on the VAT exemption for the transfer of a business

For the exemption to apply:

1. The purchaser must be registered for VAT, and
2. The purchaser must be entitled to 100% input VAT recovery, and
3. The transfer must constitute and undertaking or part of an undertaking which is capable of being operated on an independent basis.

1.2.3 Tax implications for shareholder(s) on extraction of funds from the company

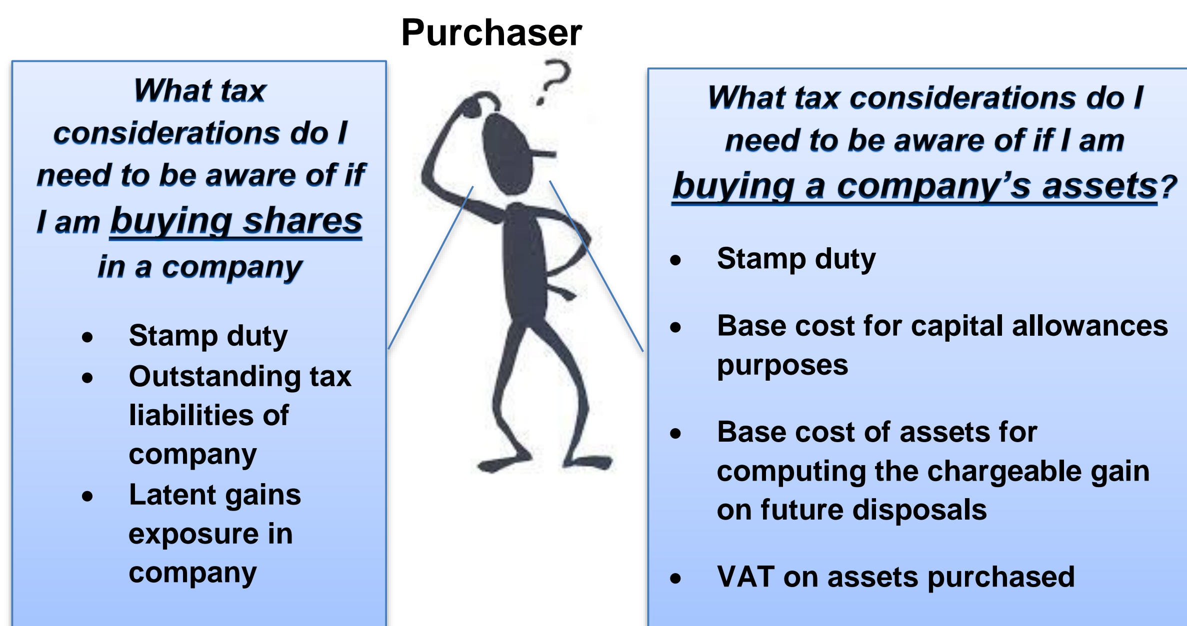
After all the taxes for the company have been quantified and paid the balance of monies available for extraction from the company to the shareholder(s) can be established. A number of extraction options are available.

The balance of monies can be extracted by way of salary. However, such a salary will be subject to income tax, USC and PRSI.

Alternatively, the monies can be paid out as a dividend to the shareholder(s). The company paying the dividend will need to ensure that it withholds dividend withholding tax (DWT) at the appropriate rate (20% where paid to Irish resident individuals) and the dividend will then be subject to income tax (with credit available for the 20% DWT), USC and PRSI in the hands of a shareholder.

Another option is for the shareholder(s) to liquidate the company and receive a cash distribution from the company. Such a cash distribution will be subject to CGT. The appropriate base cost to be used in calculating any CGT due will be either the price paid for the shares (nominal value plus any share premium) or where the shares were received by way of gift or inheritance, the market value used for capital acquisitions tax purposes will be relevant. It is important to note that retirement relief can be availed of, where the relevant conditions are met (see above) and where the company assets were sold not more than six months before the liquidation.

Section 2 Advising the purchaser



2.1. Share purchase

From the purchaser's perspective, the only tax that needs to be paid on the purchase of the company shares is stamp duty. The stamp duty rate applicable to the transfer of shares in a company is 1%.

A due diligence review is essential where a share purchase is being undertaken. Such a review should provide the purchaser with information regarding the tax compliance history of the company and detail any outstanding tax liabilities such as corporation tax, VAT and PAYE.

One of the major disadvantages associated with the purchase of shares in a company is the possibility of latent gains in respect of the company's assets (e.g. land and property included on the statement of financial position). When advising a purchaser on the purchase of shares in a company it is advisable that the exposure to latent gains is quantified before the deal is finalised as this could influence the price paid for the shares.

Tax warranties may be required in respect of the company's tax compliance history. Such warranties should be contained in the share purchase agreement.

2.2 Asset purchase

Stamp duty is an issue which needs to be considered carefully where an asset purchase is taking place. The rate of stamp duty on commercial property is 2%. Therefore, stamp duty at a rate of 2% will be due in respect of the purchase of land, commercial buildings and goodwill. Plant and machinery may transfer by delivery without a stampable document, therefore no stamp duty will be due for these assets.

For capital allowances purposes for plant and machinery and intangible assets (such as goodwill), the relevant cost will be the amount paid for these assets.

In respect of any future disposals of the assets acquired, the base cost for computing any capital gain will be the price paid for the assets at acquisition.

As noted above, where VAT on the transfer of a business exemption applies, no VAT will be charged on the assets transferring with the trade. Therefore, in this situation, there will be no VAT implications for the purchaser. Where the VAT exemption does not apply and VAT is charged on the transfer of the assets, the purchaser will need to consider registering for VAT in order to claim back any VAT charged as input VAT.