



# farming **finance**

## Limited companies yield big tax savings

### advice

MARTIN  
O'SULLIVAN



**S**INCE the barriers to dairy farmers incorporating their businesses were removed in 2008, there has been a steady stream of company formations resulting in the total number of farming companies now in their thousands.

The primary motivation for all those who incorporated was probably, without exception, the prospect of significant tax savings.

The question I will attempt to answer in this article is whether their expectations of generous tax savings have been realised.

I will answer that question in summary by saying that of the 70 or so limited companies that my firm is dealing with, not one of them has paid more tax than they would have paid had

they remained as sole traders. In fact, the tax savings in many cases have been quite staggering, particularly in 2014-2015 while milk prices were strong.

On reviewing many such files, I was scratching my head wondering how the tax could have been met if the farmer in question had remained a sole trader.

The problem with farm profit is that it is generally not there at the end of the year in the form of cash at bank, but rather it has been reinvested in buildings, livestock or plant and machinery, or has been applied to reducing debt.

This situation prompts the most commonly asked question, 'where is it?', when I'm sitting in front of a farmer reviewing his annual accounts and telling him he has earned a profit of

what appears to him to be an outlandish figure.

I can report that my job of informing my clients of their tax liability is infinitely easier where he or she is trading as a limited company. I will detail a number of cases to give an indication of the tax savings made.

### PRACTICES TO BE AVOIDED

Incorporation can have a lot to offer in terms of tax savings and also in terms of a suitable structure to accommodate the farmer and his successor(s).

However trading as a limited company involves two layers of compliance, namely compliance with good corporate govern-

ance which is overseen by the Companies Registration Office (CRO) and also tax compliance.

Good corporate governance means that the all dealings between the farmer and his company have to be at arm's length and have to pass the test of commercial reality.

Your dealings with your company can be no different to dealing with a total stranger. In recent years, farming company issues are probably one of the more frequent topics that my firm is consulted on and unfortunately, the level of corporate and tax compliance leaves a lot to be desired in some instances.

I will detail the most common practices that give cause for concern.

### FARM BUILDINGS

Buildings built by the company on land it has no freehold or leasehold title to is a common occurrence. Such situations can have legal and taxation consequences in the event of the company being wound up.

In all cases where buildings are likely to be erected, a long-term lease to the company of the farmyard and any adjacent

land that might be built upon in the future should be drawn up.

### HERD NUMBER AND BASIC PAYMENT

It is important when forming a company that the 'to do list' includes transferring the herd number and Basic Payment entitlements to the company.

In some instances, this has not occurred for a variety of reasons and Revenue could take issue. That said, legal opinion would suggest that if the company is clearly carrying on the farming activity, it is the beneficial owner of the BPS payment. Nevertheless, it is strongly advised that the herd number and BPS entitlements are transferred

### GOODWILL

Some accounting practitioners appear to hold the view that a farm business contains a marketable goodwill element.

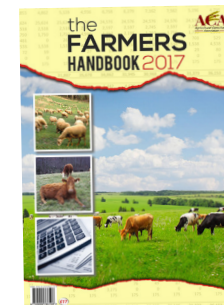
This may be the case with certain specialist producers who have carved out a niche market for their particular product and if their farm business was being sold as a going concern, it may attract some added value for

this reason. Such added value can be classified as goodwill.

However, a normal commercial farm is unlikely to carry any goodwill as nobody will pay any more for it than the collective asset market value.

Accordingly, any suggestion to sell notional goodwill to the company to create or augment a director's loan account where no realistic case can be made for the existence of goodwill in the first place should be questioned and a second opinion sought.

Martin O'Sullivan is the author of the *ACA Farmers Handbook*. He is a partner in O'Sullivan Malone and Company, accountants and auditors. [www.som.ie](http://www.som.ie). Ph: 051 640397



### CASE STUDY 1

#### PROFILE

This enterprise is based on an 80-cow dairy herd producing 420,000 litres of milk in 2015 with a small beef enterprise and a Basic Payment of €16,400. The taxable farm profit after capital allowances but before any remuneration to the owners in the form of rent or salary was €75,600. The farmer paid himself and his wife a combination of salary and rent of slightly in excess of €40,000 net. There is no off farm income.

#### TAX OUTCOME

The salary and rent when grossed up for tax purposes amounts to €51,000 approximately. The farmer and his wife paid personal tax, PRSI and USC of €10,782 and Corporation Tax of €3,075, making a total of €13,857. Had they operated as a sole trader, he would have paid a total of €18,567. There was a saving from trading as a company of €4,710.

#### COMMENT

While a saving of €4,710 is not insignificant, the farmer did incur additional accountancy charges of approximately €1,000 by trading as a company, thereby reducing the saving to €3,710. This could be regarded as a marginal case but the farmer is happy that by trading as a company, he has far greater control over his tax bill and is looking at the cumulative tax he will save over the coming years.

### CASE STUDY 2

#### PROFILE

This enterprise is based on a 180-cow dairy herd producing 990,000 litres of milk in 2015 along with a small beef enterprise and a Basic Payment of €26,600. The taxable farm profit after capital allowances but before any remuneration to the owner in the form of rent or salary was €136,000 approx. The farmer paid himself a combination of salary and rent of €30,000 net. His wife is employed off the farm and is paying tax at the 40pc rate.

#### TAX OUTCOME

The salary and rent when grossed up for tax purposes amounts to €39,000 approximately. The farmer paid personal tax, PRSI and USC of €8,053 and Corporation Tax of €12,125, making a total of €21,077. Had he operated as a sole trader, he would have paid a total of €59,629. There was a saving from trading as a company of €38,552.

#### COMMENT

In this particular case, the farmer is committed to a hefty debt repayment schedule and had he been trading as a sole trader, he simply would not have had the cash flow to pay the tax bill that would have arisen.



### CASE STUDY 3

#### PROFILE

This enterprise is based on a 60-cow dairy herd producing 360,000 litres of milk in 2015 and a Basic Payment of €13,200. The taxable farm profit after capital allowances but before any remuneration to the owner in the form of rent or salary was €43,600. The farmer is single and paid himself a combination of salary and rent of €18,000 net. There is no off-farm income.

#### TAX OUTCOME

The salary and rent when grossed up for tax purposes amounted to €22,000 approximately. The farmer paid personal tax, PRSI and USC of €4,023 and Corporation Tax of €2,700, making a total tax bill of €6,723. Had he operated as a sole trader, he would have paid a total of €11,297. There was a saving from trading as a company of €4,774.

#### COMMENT

By present-day standards, this is a relatively small enterprise and many farmers of this size may simply not consider trading as a company. However, the farmer in question considers a saving of €4,724 to more than justify him trading as a company and is more inclined to consider expansion as he feels that tax is not going to be a disincentive which he had always felt was the case when he was trading as a sole trader.