FAMILY BUSINESS

Family Business Winter Update

December 2020

BRINGING FORWARD THE CONVERSATIONS ABOUT LONG-TERM SUCCESSION AND STRATEGY

While most leaders of a family business will be highly cautious to relinquish authority over their business or make rash decisions to accelerate ownership transition, consideration should be given to the alternative of postponing the inevitable moment.

Surprisingly, owners of high value private businesses often delay succession planning, leaving their businesses exposed should they become unexpectedly incapacitated in future.

Why transition ownership now and not after my lifetime?

Transfers during an owner's lifetime have a number of potential advantages:

a. **Governance Controls:** the transfer of ownership interests can be made pre-conditional on the family members agreeing to the terms of a shareholders' agreement. This can address the thorny issues that will face the next generation in their stewardship of the business as well as retaining overall control in the owner during their lifetime, potentially avoiding scope for disagreements down the line. Issues addressed will typically include:
   - future share transfer restrictions and pre-emption rights,
   - dividend and investment policy,
   - executive remuneration principles,
   - family member employment policies, and
   - decision making involving board representation, overall control and family councils.

b. **Next Generation Integration:** it is essential that the next generation who will take over the business is not left ill prepared to manage the business in future. An owner will need to carefully consider how best to introduce family members into management, boardroom and stakeholder discussions so that they are integrated when the time comes to take over.

c. **Financial Planning:** the value of a business owner's estate is often dominated by the business asset itself. If children receive shares as part of an inheritance at an unexpected point in future, they may find themselves in a situation facing a large inheritance tax liability but without liquid cash reserves to discharge the burden. This can force them into selling some or all of their shares in the business. Such forced sales can result in the business falling out of family hands and tends to result in poor realisation of value where the sale process does not take place in a controlled manner or happens at an inopportune time.

d. **Stakeholder Communication:** large businesses rely on key stakeholders (banks, significant customers and suppliers) to operate and such key stakeholder relationships tend to be long term in nature. By transferring ownership during one's lifetime, there is an opportunity to control the narrative with stakeholders, and to pre-empt any concerns they may have about a transition of ownership. As the owner is available to maintain control through governance arrangements notwithstanding the passing of economic ownership interests, this transition can be managed gradually. Thus important business relationship issues can be addressed before passing control on to the next generation entirely.

e. **Succession law rules:** a major factor for some families is seeking to minimise the risks of a dispute relating to the terms of a will. A child who is dissatisfied by the provision made in a will can initiate court action under the Succession Act 1965 seeking to have the terms of the will varied in his or her favour. The costs of such cases are usually borne by the estate, irrespective of the outcome, so there is little risk of a costs deterrent to such an action. If transfers of property are made more than three years before death, generally no challenge can be made, and the prior transfer period may be shorter in many other cases.

How will this impact me from a tax point of view?

Owners may be reeling with the issues faced from COVID-19 in 2020 and the diminution caused to the value of their businesses, particularly in sectors badly hit by lockdowns including industry and construction. However, lower valuations arising from this turbulence may also present an opportunity to transfer some or all of an owner's shares in their business to the next generation in a cost efficient manner. An inter-generational transfer of shares will give rise to considerations under three heads of tax, stamp duty, capital gains tax (CGT) and capital acquisitions tax (CAT).

In many cases, businesses will have experienced strong growth since foundation, with a low base cost, so the prospect of triggering a substantial CGT charge on the deemed disposal that is treated as made if shares are gifted to children can be daunting. Depending on the age of the owner however, it may be possible to avail of retirement relief which would eliminate any CGT charge. If that is not available, then other avenues might be explored such as utilising any CGT losses forward.

It is important to have careful regard to tax valuation rules. Normal minority discount rules apply in valuing assets for the purposes of CGT and stamp duty. However the CAT code imposes a method of valuation for the transfer of shares between family members that can result in an artificially high value being attributed for CAT purposes. It forbids the application of the minority discount rules that would usually be applied in establishing open market value. While that is clearly bad news, the good news is that many businesses may qualify for Business Property Relief, so that the value of shares/assets transferred is reduced by 90%, and CAT is only imposed on 10% of the value. An effective CAT rate of 3.3% is an attractive proposition, and there can be benefit in securing a transfer at that rate with uncertainty ahead as to what changes may be made to the tax code to redress the demands on the exchequer arising from COVID-19 and Brexit.

What steps do I need to take?

a. Transfer Restrictions: an owner will need to consult with their adviser to ensure that there are no impediments to transferring their shareholding interests. Restrictions could be in the form of pre-emption rights in the constitution of the company or any shareholders' agreement, change of control restrictions in company contracts or charges or other encumbrances given to the individual's or the company's finance providers.

b. **Controls Going Forward:** an owner will need to decide whether to make any transfer conditional on the recipients signing up to a shareholders' agreement to govern their future relationship, and whether to retain owner control during their lifetime.

c. **Valuation:** it will be necessary to obtain a third party expert valuation of the company for tax purposes.

d. **Family Communications and Financial Planning:** an owner will need to communicate her/his intentions to their family and ensure that the owner and the proposed recipients have the financial resources to meet any tax obligations that will arise.

e. **Stakeholder Engagement:** once the decision to transfer has been made, an owner will need to consider which key stakeholders should be informed in advance / following transfer and how best to introduce the next generation into the ongoing relationship to ensure continuity.

STATUTORY SICK PAY

In Ireland there is currently no statutory entitlement to sick pay. An employee who is unable to work due to illness or injury will usually be entitled to receive Illness Benefit from the State, after six days of absence. As part of Budget 2021, the Government announced that it will reduce this waiting period to three days from February 2021. In March 2020, the Government introduced the COVID-19 Enhanced Illness Benefit which provides for a payment of €350 per week for any worker who is advised to self-isolate by a doctor or who has tested positive for COVID-19. This is currently due to operate until 31 March 2021. The Oireachtas Special Committee on COVID-19 Response issued its final report in October 2020 which recommended the establishment of a statutory sick pay requirement for low-paid workers, such as those working in nursing homes and meat factories. In September 2020, the Labour Party brought forward the Sick Leave and Parental Leave (Covid-19) Bill 2020, which proposed that after four weeks service, employees would be entitled to 30 days of paid sick leave in any 12 month period where the employee is incapable of working due to illness or injury. The Government voted to postpone debate on the Bill for six months pending a consultation, indicating that it planned to introduce its own bill on the matter, arguing that the Labour Party's proposals placed an undue burden on employers.

On 11 November 2020, the Department of Enterprise, Trade and Employment launched a public consultation process on the introduction of a statutory right to paid sick leave for all employees.

The Department is encouraging all employees and employers to engage with the consultation and to complete questionnaires (available here) by 18 December 2020. In circumstances where the Tánaiste and Minster for Enterprise, Trade and Employment, Leo Varadkar TD, has made a commitment to bring Ireland in line with other OECD countries by providing for a statutory entitlement to sick pay, it would appear that change is imminent. Our briefing on this topic is available here.

CHANGES TO FAMILY LEAVES

The Parental Leave Acts 1998 and 2019 govern the law relating to (i) parents' rights to take leave to care for their children and (ii) force majeure leave, which relates to exceptional leave required in emergency situations. From 1 September 2020, qualifying employees are entitled to take 26 weeks' unpaid parental leave, compared to the previous 22 weeks' leave, for the purposes of caring for a child up to the age of 12 years old (or where the child has a disability or a long-term illness, parental leave may be taken up to the child's 16th birthday).

Parent's leave was introduced in Ireland by the Parent's Leave and Benefit Act 2019. All parents are entitled to two weeks' leave during the first year after the birth or placement of their child in the case of adoption. Parent's Benefit is paid in respect of this leave by the State to employees with sufficient Pay Related Social Insurance contributions. Employers may top up the State benefit but are not required to do so. From April 2021, the entitlement to parent's leave and Parent's Benefit will increase to five weeks which can be taken during the first two years after the birth or placement of their child. Employers should ensure they are familiar with the provisions of the legislation and develop a parent's leave policy or incorporate this entitlement into existing family leave policies, if they have not already done so. Employers should prepare to update policies in April 2021 when the proposed changes will come into effect.

COVID-19 UPDATE

Ireland's Plan for Living with COVID-19

On 15 September 2020, the Government launched its new six to nine month Resilience and Recovery 2020-2021: Plan for Living with COVID-19. The Plan for Living with COVID-19 is a five level framework of restrictions, with level five being the most restrictive level, similar to the restrictions that were imposed in Ireland in March 2020. Our briefing on the Plan for Living with COVID-19 is available here.

Currently Ireland is at level three of the Plan, with reduced restrictions to come into effect on 18 December 2020 until 6 January 2021.

Notably, under all five levels of the Plan, employees are advised to continue to work from home if possible. Employers are therefore advised to continue to support their employees with working remotely to the extent possible. Significantly from the point of view of employees being available to work, either remotely or by attending the workplace, schools, early learning and childcare services continue to remain open as they are deemed essential. Our briefing on Handling Employee Requests to Work Remotely Abroad is available here.

Where employees are required to attend the workplace, employers are reminded of their obligations under the newly published Work Safely Protocol published on 20 November 2020 (the "November Protocol"). The November Protocol replaces the May 2020 Return to Work Safely Protocol and reflects the most up to date Government and public health advice including the Plan for Living with COVID-19. The November Protocol's primary emphasis is on the need for continued monitoring and review of health and safety practice and procedures in the workplace along with providing access to employers and workers to up to date information. Our briefing on the November Protocol is available here.

Employers have general duties to take steps and implement measures to safeguard the safety, health and welfare at work of employees and others at a workplace, as far as reasonably practicable, under the Safety, Health and Welfare at Work Act 2005. These obligations are in addition to common law duties of care. Exposure to COVID-19 presents an additional health risk to employees and other persons at a workplace and employers are required to take additional measures to safeguard its employees and others in order to discharge their duties under the 2005 Act. The November Protocol sets out the additional measures that employers should take in this regard. Central to the November Protocol is an obligation to respond and adapt processes quickly where gaps arise. Employers are therefore advised to frequently review the health and safety measures in place in their workplace, and in particular to address any concerns raised by employees.

Where an employee demonstrates a reluctance or an unwillingness to attend the workplace, the employer should be mindful of the statutory protections in place for employees. The employer should engage with the employee to fully understand their concerns with a view to identifying a workable solution. If an employee is concerned about their own health and safety or that of their colleagues, they may seek to invoke the protection of the 2005 Act or the Protected Disclosures Act 2014. Our detailed briefing on this issue is available here.

The Health and Safety Authority (the "HSA") reportedly carried out over 5,000 workplace inspections between May and September this year, the majority of which were COVID-19 related inspections. The volume of inspections seems likely to rise with news that the Oireachtas Special Committee on COVID-19 Response, in its Report, recommended an increase in the number of HSA inspectors to ensure enforcement and compliance with Covid-19 safety measures. Our briefing COVID-19: What to Expect from a Health and Safety Authority (HSA) Inspection provides helpful guidance to employers facing such an inspection of their workplace.

Extension of suspension of redundancy provisions

The suspension of redundancy provisions relating to temporary lay-off and short-time work introduced in March 2020 is currently in place until 31 March 2021.

Prior to March 2020, under the Redundancy Payments Acts 1967 – 2014, if an employee was laid-off or put on short-time for (i) four or more consecutive weeks, or (ii) six or more weeks within a 13-week period of which not more than 3 are consecutive, the employee was entitled to notify their employer in writing of their intention to claim a statutory redundancy payment assuming they satisfied the qualifying criteria, for example, having at least two years' continuous service. On giving notice, an employee would be entitled to a statutory redundancy payment if their employer could not give them counter-notice within seven days of the employee's notice. The employer's counter-notice should be to the effect that within four weeks of the employee's service of notice of intention to claim, the employee will be offered at least 13 weeks' work with the employer without lay-off or short-time.

It is important to be aware that an employee's right to claim a redundancy payment has not been removed, but merely deferred for a specified period for those employees on temporary lay-off and short-time. Employers should therefore continue to be mindful of an employees' rights to claim statutory redundancy payments, and the cost of these payments to employers, once such entitlements are reinstated.

EWSS

The EWSS has been in operation since 1 September 2020 and replaced the COVID-19 Temporary Wage Subsidy Scheme, which had been in place since March 2020. The EWSS has the following two elements:

- It provides a flat-rate subsidy to qualifying employers based on the numbers of paid and eligible employees on the employer's payroll; and
- It charges a reduced rate of employer PRSI of 0.5% on wages paid to eligible employees.

In order to be eligible for the EWSS, an employer must be able to demonstrate that:

- their business is expected to experience a 30% reduction in turnover or orders between 1 July and 31 December 2020 looking at the period as whole rather than on a monthly basis; and
- this disruption is caused by COVID-19.

The rate of the weekly EWSS subsidy the employer will receive per eligible employee is as follows:

GROSS WEEKLY PAY	SUBSIDY
>€1,462	No subsidy
>€400 <€1,462	€350
>€300 <€400	€300
>€203 <€300	€250
>€151 <€203	€203
<€151	No subsidy

These rates will run until 31 January 2021. The EWSS will operate until 31 March 2021 (rates from 1 February 2021 to be confirmed) and will be replaced from 1 April 2021 until the end of 2021 with a variant of the EWSS. The most up to date guidance on the EWSS is available from Revenue here.

BUDGET 2020 FOR EMPLOYERS (NON-COVID-19)

The following are the key (non-COVID-19) take-aways for employers from Budget 2021.

Welfare supports

- There is to be no change to the main benefit rates.
- The State pension age will remain at 66.
- Illness Benefit will now be available after three days out of work, rather than six. It is expected that this will come into effect from the end of February 2021.
- Parent's Benefit is to be extended by three weeks and can be taken within the first two years of the birth of a baby or its placement with a relevant parent in the case of adoption. This is expected to come into effect from April 2021.

Tax

- No changes to income tax, USC or PRSI rates.
- The ceiling of the second USC band will be increased from €20,484 to €20,687 to support those on the increased minimum wage.
- The weekly income threshold for higher rate of employer PRSI to increase from €394 to €398.

To read our Summer Update, click here.

KEY CONTACTS

If you would like to discuss the foregoing, or require any assistance please do not hesitate to contact a member of our team or your usual Arthur Cox contact.

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