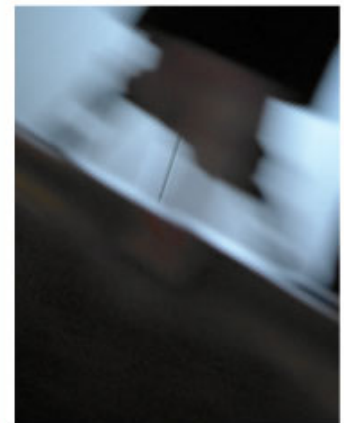
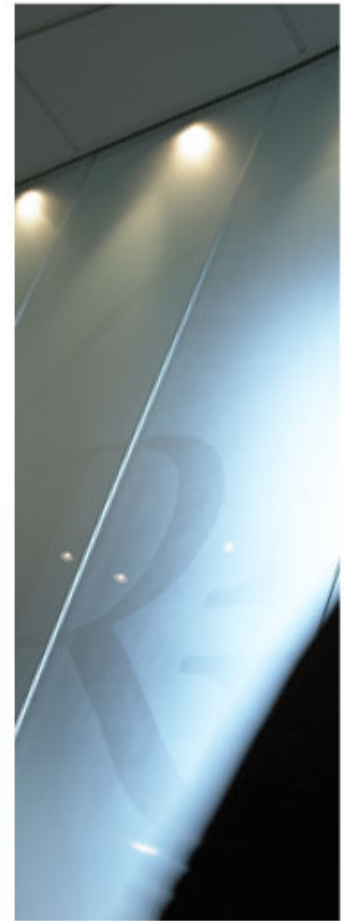




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Wealth Transfer in the 'Perfect Storm': Legal and Taxation Considerations

25 May 2011

John Cuddigan
Partner -Tax

- **Wealth Transfer**
 - Perfect storm for wealth transfer?
 - Current (new) risks for wealth transfers in light of ‘post-boom’ environment?
 - Current opportunities due to asset values/ taxation law (but with use of control/ protection structures in appropriate cases)?

- **Wealth Transfer – Preparation**

- **Legal and Tax Considerations on Disposing of Businesses and other Assets and Investments**

- **Wealth Transfer Structures – Options?**



Perfect Storm for Wealth Transfer?



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“an event where a rare combination of circumstances will aggravate a situation drastically” - Wikipedia

- Credit crunch – effects on business development
- Reduction in asset/ business values
- Wealth Erosion through collapse of ‘safe haven’ share investments/ CFDs/ property syndicates
- ‘middle generation’ debt burden/ creditor exposure
- Government cut-backs – health costs in future

All point against wealth transfer?



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- **Creditor attack risk to settlor/ transferor**
 - **S74 Land and Conveyancing Law Reform Act 2009** – *“any conveyance of property [after 1/12/2009] made with the intention of defrauding a creditor or other person is voidable by any person thereby prejudiced.”*
 - **S59 Bankruptcy Act 1988** – *“Any settlement of property not, ... in good faith or for valuable consideration, shall ... within 2 years ... be void against the official assignee”/ (5 years on voidable basis)*
 - **S211 NAMA Act 2009** – Power of NAMA to set aside a disposal where the disposal had the effect of defeating or delaying acquisition by NAMA of eligible asset
 - **ARF/ Pension Schemes** – Now open to creditor attack?

Impact of family law settlements – UK and Irish precedent?



- **Creditor attack risk to Transferee(s)**
 - **Asset insolvency and cash flow insolvency** – Exposure of family assets to funding impossible ‘debt mountain’ – Generation Y legacy from property boom
 - **Cash flow solvency/ asset insolvency** – Risk of ‘cash sweep’ where wealth passes to indebted next generation even where debt being serviced
- **Matrimonial/ Spendthrift**
 - **Exposure of Business Assets** – In light of negative equity in property assets, business assets/ cash benefits being increasingly called upon to fund matrimonial settlements
 - **‘Character Issues’** – risk of depletion of assets in wrong hands – of more concern now

All above in addition to normal risk that the next generation are not ready to take a transfer/ capable of running a business!



Wealth Transfer – Current Opportunities – Limited Window?



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- Capital tax rates still relatively low despite recent increases – likely to continue?
- Asset Values reduced by 50 – 60% from peak
- Elimination/ Reduction in capital taxes reliefs flagged in Commission on Taxation Report/ National Development Plan – Budget 2012
 - Cap on business property relief (gift tax/ IT) and reduction in value – 90% to 75%?
 - Cap on retirement relief for CGT?
 - Pension Levy
 - Asset Values reduced by 50 – 60% from peak

**Sufficient to favour wealth transfer now? –
balancing act between tax efficiency and
managing risks**



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Wealth Transfer – Current Opportunities?



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Example – transfer of business/ farm to child:

(Assumed that business fully qualifies for retirement relief/
business property relief)

Year	Market value	CGT/ gift tax rate	Business relief rate	Cap on business relief/ retirement relief	Tax Payable (excl stamp duty)
Jan 2009	€12M	22%	90%	n/a	€144K
Jan 2010	€8M	25%	90%	n/a	€96K
Jan 2011	€6M	25%	90%	n/a	€67K
<i>Jan 2012?</i>	<i>€6M</i>	<i>30%</i>	<i>75%</i>	<i>€3M</i>	<i>€800K/ €900K</i>
<i>Jan 2012?</i>	<i>€8M</i>	<i>30%</i>	<i>75%</i>	<i>€3M</i>	<i>€1.4 – 1.5M</i>

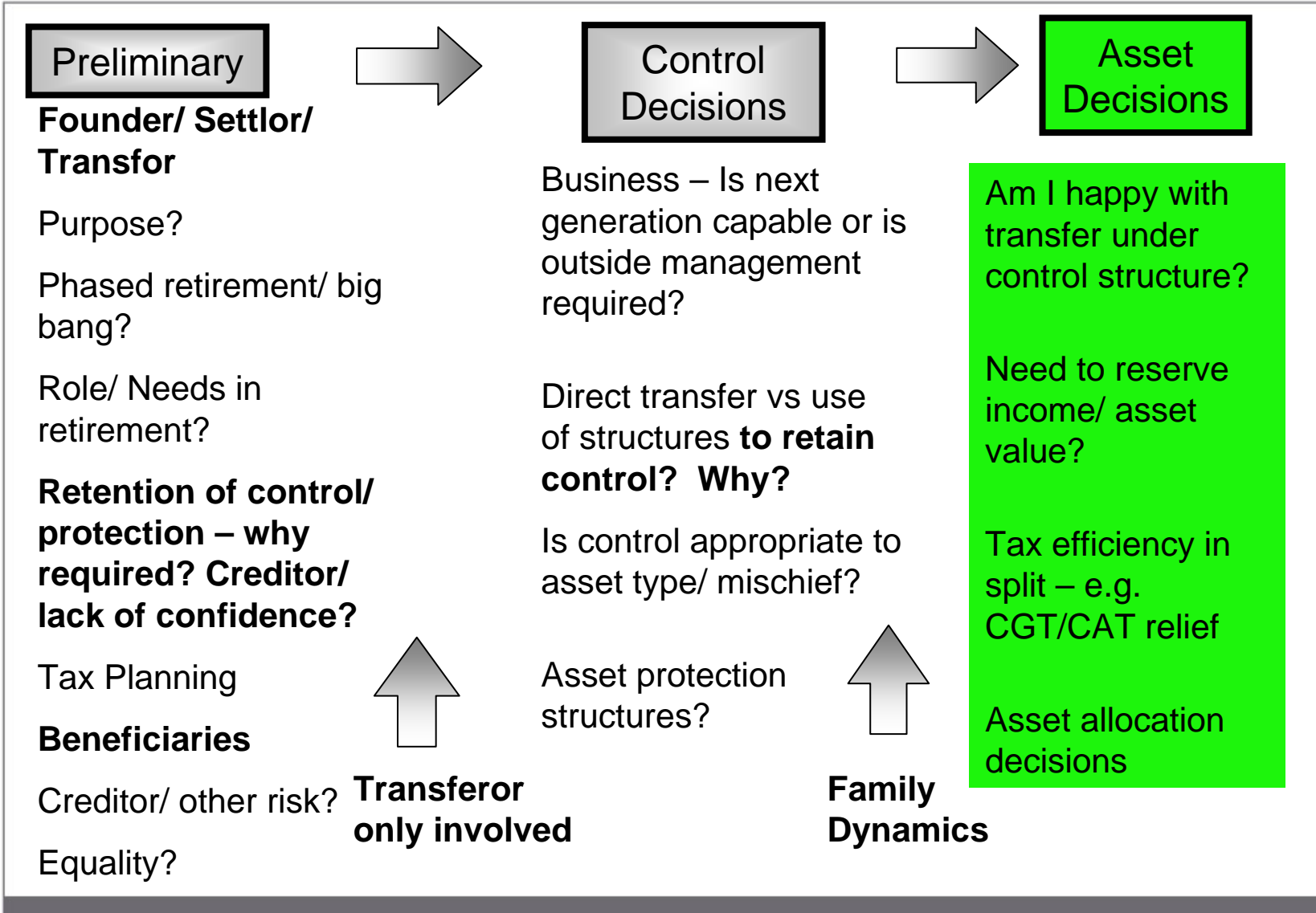


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Wealth Transfer – Possible Approach/ Preparation



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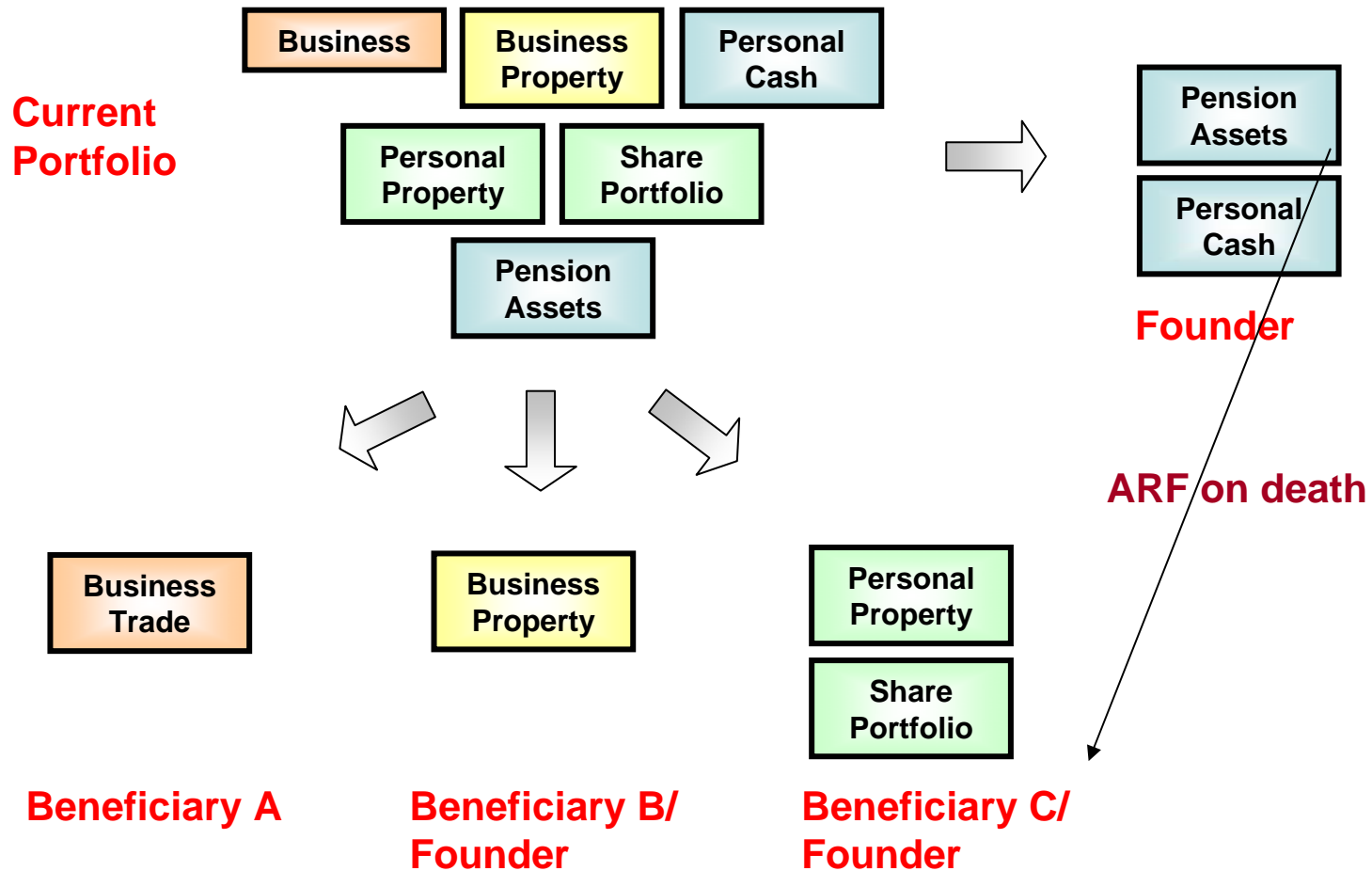


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Wealth Transfer – Asset Split?



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Wealth Transfer – Transferring the Business – Preparation Steps



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- **Separation of Business and Other Assets required?** – Tax efficient partitioning of business and non-business assets possible where need to separate trading/ other assets for equality between beneficiaries
- **Cash withdrawal from Business?** – Tax efficient means to extract cash (over and above pension entitlements) in a genuine retirement/ succession transaction – can assist with equality motive.
- **Planning to maximise tax reliefs on transfer** – Reorganisation of assets to maximise CGT retirement reliefs/ business relief/ agricultural relief – effected prior to transfer
- **Retaining Control – manner of achieving this?** – Use of ‘golden shares’/ growth shares/ non-voting shares/ staggered transfer of shares?
- **Minimising Risk/ Impact of Attack?** – terms of shareholders’ agreement – buyout provisions/ delayed payment mechanisms? – cf ‘*anti-deprivation rule*’



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Wealth Transfer – Effecting Transfer of Business



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- **Documentation** - Focus on details of paperwork to ensure commercial and taxation objectives are realised
- **Shareholder/ Control arrangements** –to assist with control objectives and minimisation of risks of attack from third parties. *Founder has more leverage power before rather than after transfer!*
- **Pension funding/ other extraction of cash and assets by Founder** – Need to ensure that these requirements are met at or prior to transfer of business. – Creditor risk of transfers being overturned?



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Wealth Transfer – Personal and Investment Asset Considerations



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- **What should be transferred?** Primary purpose is to ensure sufficient assets available to founder and spouse for lifetime
- **Testing of Beneficiaries/ Taxation?** Tax advantages may accrue from early transfer of value of assets/ benefit of ‘testing’ the beneficiary
- **How should assets be transferred?** Direct transfer of assets to beneficiary may result in loss of control/ lack of asset protection/ loss of resources
- **Use of Control Structures** – Can offer tax benefits of early transfer and retention of control and management of assets/ asset protection
- **Transactional tax issues** – use of capital losses to minimise costs of transfer / thresholds/ future impacts?



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- Pensions are significant source of wealth – greater flexibility in light of FA 2011
- Available to founder to (1) give independent source of wealth to business and (2) to achieve equality through leaving assets of ARF to other children – latter now diluted due to ‘notional annual distribution’ from ARFs of 5%
- Creditor risks? Thinking up to early 2010 was that all pensions were ring-fenced against attack from creditors – ARFs certainly open to attack/ annuities?



Wealth Transfer (Lifetime) – Control Structures (examples)



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- **Lifetime Domestic Trusts** – Permit assets to be put beyond transferor's control and allow for flexibility of benefits/ protection of assets
- **Family Partnerships** – Essentially limited or general partnerships entered into between transferor and family with management control retained/ assets
- **Offshore Structures** – Trusts, companies or foundations – commercially robust/ tax compliant

Appropriate structure will be dictated by whether asset protection structure is necessary in light of particular circumstances or whether tax efficiencies are paramount



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Family Partnership Structure



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- **Structure** - Partnership agreement entered into between transferor, spouse and children with control of management retained by transferor and spouse/ limited liability can be incorporated through LP
- **Commercial rationale** - Permits cash gifts/ investment assets contributed to be locked into legal structure/ retention of existing asset value for transferor/ retention of control for transferors
- **Sharing of Income/ Gains** - Can permit transferor and spouse to retain right to income from partnership assets/ other partners can be given gains
- **Tax Benefits** –
 - Tax transparent – income and gains assessable directly on partners entitled
 - Future asset growth accrues to children partners – eliminates gift and inheritance taxes on future growth



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Domestic Trust



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- **Structure –**
 - Various types of trust possible – e.g. income settlements/ discretionary trusts (which can incorporate income settlements)
 - Trustees will be appointed by transferor/ settlor
- **Commercial rationale –**
 - Assets relatively protected (assuming no challenge to settlement by Transferor) where beneficiaries not entitled to capital and just income
 - Control over assets maintained
- **Taxation –**
 - Transfer of assets into trust gives rise to tax implications (mainly CGT/ stamp duty – low asset values give opportunity to minimise) and also gift tax (benefit dependent)
 - Settlement of cash not subject to CGT or stamp duty
 - Future asset growth may create new tax liabilities
 - Benefits may give rise to CGT and gift/ inheritance tax – need to manage



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Offshore structures



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- Use of offshore trusts and other structures not illegal. Non-disclosure of tax liabilities is!
- Number of different structures – e.g. offshore trusts, offshore companies, foundations, cell companies
- Taxation implications will differ as between different structures
- **Why go offshore?**
 - Enhanced asset protection in certain cases through more sophisticated structures – e.g. foundations (these take a form of a company but without shareholders and beneficiaries with entitlements – until appointment made)
 - Tax deferral arrangements possible?



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- Many of foregoing strategies can also be employed in the context of passing property by will (the family partnership excluded) – less ability to control however
- In addition, asset protection can be achieved by framing will in particular way to ‘skip’ a generation if necessary through use of trust provisions in will
- Constant review of wills is now advisable in light of changing economic picture

Useful Gift Tax Exemptions to Consider



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- Benefits to children for education, maintenance and support where part of normal expenditure of parent and where *'reasonable having regard to the circumstances of the [grantor]'*
- Dwelling house exemption – available under certain conditions
- Tax free thresholds of grandchildren - €33K each (return must be filed once 80% of threshold reached) or more with use of annual small gift exemption



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