Equine tax planning in the recession

How can tax planning help the equine industry in the current recession?

The carry back of losses

Following the Pre-Budget Report (PBR) of November 2008, trading losses can be carried back against former trading profits of the same trade – going back to 2006/7 and 2005/6. The loss must be incurred in the year to 2008/9 for an unincorporated business and after 23 November 2008 for an incorporated business. It is not necessary to wait until the 2008/9 Return submission. Standalone claims can be actioned from Budget Day (22 April 2009).

'Net realisable value' – what is that when markets collapse?

A key factor in calculating the level of losses in the equine tax industry is stock values. The stock of horses at the balance sheet date has to be valued at the lower of cost and net realisable value (NRV). But how can the NRV of any equine stock be determined at the moment? It has been said that in the current economic storm, how can anything be valued accurately, especially if that 'thing' has four legs?

The prompt preparation of accounts

The key tax planning action point is to look at the preparation of accounts for the current financial period and, where possible, employ a professional valuer to support any HMRC enquiry into the tax loss and drop in stock value. Important factors to accelerate the loss will be the prompt preparation of accounts in order to arrive at the guide to profitability. The principle of the PBR tax relief is that if a previously profitable business that paid tax on its profit is now struggling, it can now achieve tax relief by the carry back of current tax losses against earlier profits – and recover the tax paid thereon. If a business is possibly struggling, a positive cash-flow advantage for any business is to sell stock. Obviously, if you are selling stock it makes sense to sell the weaker bloodlines and to keep the stronger lines for future profitability.

Another obvious concern is that the business balance sheet will reflect a more prudent reflection of stock valuation in these complex times.

Subsequent sales of stock at high prices

Concerns might arise for the taxpayer if the horses are subsequently sold for more money than the NRV of the stock value. Where the correct valuation of stock has been made and has resulted in a future profit on sale, then tax will be paid on that increased profit. There are many who would say that they should be so lucky as to enjoy paying tax on the subsequent uplift in tax values!

Concerns over 'negative equity'

The problem of the write down of stock values in the accounts is that this could result in negative equity showing in the balance sheet. The resulting insolvent position would, of course, bring problems of 'trading insolvently' for companies. This would mean that the directors would be in breach of their duties as directors. Obviously, the tax refund that is due as a result of the carry back

of losses will be an asset (a debtor) of the company and should be brought into the accounts.

The problem of 'legs'

The equine industry involves a large amount of part ownerships. A 'leg' is, not surprisingly, one-quarter of the horse – a 'fetlock' is humorous terminology for a small share. On the basis that stock should be valued at the lower of cost NRV, the majority of shares in horses have been valued at a finite amount. But, what now with falling values?

In the interests of consistency, the value should be used in each set of accounts that it belongs in. However, how will that consistency be achieved? The keys have to be communication between part owners and attempts at consistency and transparency.

Summary

In order to look at the maximum use of tax losses, it is essential that accounts are produced promptly and there is a careful review of stock values.

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