Tax Spotlight

Tax Implications of the Summer 2004 Survey of U.S. Food and Beverage Companies

Grant Thornton

Kevin Burns, Tax Partner and Chicago Consumer & Industrial Products Industry Leade,r takes a look at the tax implications of the recently completed Survey of U.S. Food and Beverage Companies.

Grant Thornton, a global public accounting, tax and business advisory firm, recently performed a survey of executives in the food and beverage business to gain an understanding of industry benchmarks, critical success factors and economic issues impacting the sector. More than 30 percent of Grant Thornton's clients are in the food and beverage industry segment. Perhaps even more interesting than the survey findings are the implications for tax planning strategies at food companies of all sizes.

Specifically, the survey revealed several key tax-planning opportunities showing up on the shelves.

Growth strategies

Consumer product loyalties are tenuous and food and beverage companies need to identify niches with pinpoint accuracy. A simple news story can sway demand in a day. That's why 45 percent said they believe the real key to unlocking this potential industry growth lies in consumer behavior research.

Correctly recognizing customer wants and needs is fundamental to business growth - and as consumers continue to gravitate to "better for you" products, 67 percent of survey respondents said they were planning to increase their product development spending in 2004 over 2003 levels.

In fact, research spending will be a catalyst for several important tax issues. The primary federal, state and local tax issue associated with new product development is the potential eligibility for research tax credits. Research tax credit specialists can help companies that dedicate capital to research qualify for and claim additional credits for developing or improving new or existing products, processes and technologies through the federal research and experimentation (R&E) tax credit.

The R&E tax credit is a 20 percent incentive credit designed to lower the cost of innovation. To qualify, there are specific criteria that must be met. The developed product has to be innovative with an element of risk - it could be a modification to a prior product, but it has to be significant in terms of research and testing. A serious examination of R&E tax credits may help recover significant tax dollars.

Basic meat and potatoes tax planning can help companies take advantage of what is called 'chargeback consulting' - making sure that any program is expensed effectively so proper expenses can be deducted. Also, companies can perform Tax Accounting Method Reviews that examine how well they are handling inventory or dealing with slotting fees or advertising expenses. In a nutshell, companies can use this expertise to examine their tax returns and detect where and if they should be accelerating or delaying deductions to get the greatest mileage out of their programs.

Companies looking to expand within the U.S. or overseas may want to consider state and local (SALT) and national tax incentives that can help build a new plant or create jobs in a new geographic market. This can be accomplished through a service that many state and local tax experts call credit and incentive negotiation.

Also, companies may need a quick assist on the increased bonus depreciation provisions of the Jobs and Growth Tax Reconciliation Act of 2003, which expire at year end. Companies are now able to take advantage of first-year bonus depreciation at 50 percent - available for alternative minimum tax - over the previous 30 percent, but companies may need help to confirm what qualifies as property placed in service before Jan 1, 2005.

To get a copy of the full survey, please call Kevin Burns at 312.602.8986.

Financing

As companies rebuild after the recession, 79 percent of surveyed executives said they expect their need for capital to rise over the next five years. Yet the difference in available funding between public and private companies is striking. While 70 percent of public companies and 78 percent of private firms predicted a need for more capital, only 40 percent of private firms said they were counting on the availability of reasonably priced lending, compared to 80 percent of public companies.

A host of services can be added to the mix to raise, locate or accelerate working capital that can help companies grow, invest and offset costs. Using aggressive cash management approaches can help find latent "lazy cash" and redirect it to support more growth with the same level of investment. Cash actually hides in many niches of a company's business processes - this is true for firms large and small. With guidance, a company can detect and put this cash to better use by expediting routine operations

Business Issues

This dynamic business sector still needs to add some major ingredients for success. Despite successful product rollouts in 2003, respondents are not as optimistic about sales in 2004, with 53 percent of respondents foreseeing more difficulty in this area through next spring.

One contributor to this uncertain outlook is the unstable commodities market. Over the past five years, commodity prices have skyrocketed resulting from increased foreign demand, droughts and other unusual crop situations on a global scale. Despite some crop recovery in the past year the majority of survey respondents believe the current trend in commodity pricing will continue, with 74 percent foreseeing an increase in prices over the coming year.

To better prepare, respondents are increasing education for their brokers and sales forces, and companies should review their tax options on these training expenses as part of their overall benefits plan. Businesses may want to look at the impact that hedging commodity prices may have on their tax accounting and treatment of gains and losses.

In further response to these shifting market conditions, 79 percent of the executves surveyed also said they anticipate a rise in merger, acquisition and restructuring in the industry in 2004. Seventy-six percent said they expect the trend to rise in 2005.

Employment

While the food and beverage industry is committed to faster growth and product development, only 45 percent of respondents expect the industry as a whole to add employees in 2004. However, more executives said they expect their own headcounts to rise. Fifty-nine percent plan to add employees in 2004 and 56 percent anticipate the same in 2005.

For companies adding jobs, the No. 1 tax issue is controlling healthcare costs. The best choice for today's companies is cafeteria plans - plans that allow employees to pick and choose their own healthcare coverage based on a menu of options.

In the best scenario, tax professionals and compensation and benefits consultants work hand-in-hand to help management select the right benefits offerings for their workforce. This is a continual process that requires full-time attention throughout the company's lifecycle. Ultimately, this isn't only a cost-savings issue. A company that pays proper attention to the cost and quality of its benefits offerings has the potential to become a leader in work-life issues.

For many middle-market food and beverage businesses, the best practices in benefit plan design are appetizing. With the right advice, firms of virtually any size can apply tactics and solutions from the most successful large-company cafeteria plans to best serve their employees and bottom line.

At Grant Thornton, we find opportunities for companies to grow faster. Our food and beverage industry clients are no exception. We see tax planning as a critical part of that recipe.

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Grant Thornton's consumer and industrial products industry practice provides efficient, responsive service to meet the accounting, audit and tax needs of mid-size retailers, manufacturers and distributors. Grant Thornton's industry-specific services include assurance services, tax compliance and consulting, Sarbanes- Oxley compliance, transaction support, due diligence, mergers and acquisitions, initial public offerings and other registration statements, and private placements. Grant Thornton International is the world's leading accounting, tax and business advisory organization dedicated to mid-size companies. Through its network of 585 offices in 100 countries, including 48 offices in the United States, partners of the member firms of Grant Thornton International provide personal attention and seamless service delivery to public and private clients around the globe. Grant Thornton's Web site is www.GrantThornton.com.