Ryecroft Glenton
Chartered Accountants

Financial Journal *Issue 4* 2013

Chris Robson outlines the topics covered in this edition.

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Welcome to our final FJ of 2013...

With the end of the year approaching, I am delighted to introduce a wide range of interesting topics.

On the technical front, this edition of our FJ focuses on the significant change in pension provision known as Auto Enrolment which employers ignore at their peril.

We make no excuse for highlighting once again the enormity of the task being faced by businesses of all sizes and the eye watering penalties for slipping up with the implementation and ongoing administration of this new regime.

As well as including some important notes covering certain aspects of VAT and the taxation of property income, we report on our involvement in the CEO Sleepout which focused on raising awareness and substantial funds for homelessness in the North East.

Finally, I am pleased to report that our Corporate Finance division continues to build its presence both locally and nationally with a number of key successes. Carl Swansbury, our Director of Corporate Finance, provides some tips on acquiring a business. Carl's achievements were recognised in September when he was shortlisted for the "Young Dealmaker of the Year Award" for the second year running.

As always please do not hesitate to contact me or your Engagement Partner if you would like to discuss in further detail any of the issues covered in this edition of our FJ.

We look forward to working with you in the year ahead and in particular helping you to achieve your financial objectives for 2014.

Ian Smith looks beyond the contributions element of auto enrolment at the true cost of this new demanding legislation.

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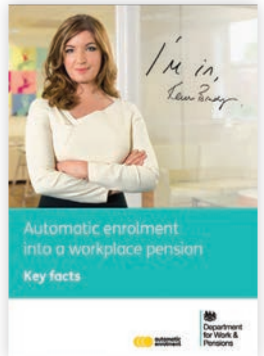
Auto enrolment
– how much will it cost you?



Many people believe auto enrolment is all about selecting and providing a pension to your workforce. While I would not deny some of this to be true, it is only a very small part of the legislation introducing mandatory pension provision for workers across the United Kingdom.

Providing a pension is only a small part of auto enrolment. **The largest part of auto enrolment relates to payroll and it will be the most significant change to how payroll is processed this century!**

Employers will have the burden and cost of not only paying pension contributions but also complying with complex administrative requirements… all with the potential for significant fines if they are dilatory or deliberately avoid these new requirements.

Fines

The pensions regulator has stated that it does not want to scare people by concentrating on the hefty fines it can levy against persistent offenders. **However, larger employers can be fined £10,000 per day**, although a more realistic figure for the average business in the UK is £500 per day.

Ironically, the pensions regulator's "softly softly" approach means that many employers are unaware fines can be levied!

Employers can also be fined **from £1,000** for any prohibited recruitment [where the business recruits, or offers to recruit, an individual if they opt out of auto enrolment] – this fine increases in increments up to £5,000 depending on the number of workers affected.

True cost?

Ignoring the fines, how much will auto enrolment ***really*** cost your business?

Most people understand that contributions are being phased in over the next four years and that the employer will be responsible for paying contributions of 1% - 3% on workers' qualifying earnings [qualifying earnings include normal gross pay, sick pay, maternity and paternity pay, bonuses, commission etc].

However, this is only the tip of the iceberg. The real cost to employers will be the additional administrative work, payroll software and payroll services that will be required to comply with the new requirements. There will also be the potential upset caused to employees.

In addition to preparing for auto enrolment, once it is implemented, some (depending on the work force) employers may have to assess workers on each and every pay run thereafter. All employers have to re-assess the entire workforce **every 3 years**.

Software providers such as Sage are already announcing a new "auto enrolment add-on", available at an **extra** cost and payroll bureaus across the country are busy calculating the extra cost of providing information to employers to enable them to comply with the complex legislative requirements.

How can we help?

Our focus is on helping you prepare for auto enrolment, understand your requirements and accurately estimate the financial impact of auto enrolment.

We now have a dedicated micro-website – www.ryecroft–glenton.co.uk\autoenrolment - which covers all the basics.

We will also be running a series of workshops in early 2014, covering key areas. Details will be available on the micro website during December.

If you would rather we took the pain out of this complex area, we can provide you with a comprehensive plan with timetable, assessment of workers, estimate of financial impact and options available (such as postponement) – please contact me for further information.

Carl Swansbury sets out some of the key points that need to be considered when aquiring a company.

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Tips on acquiring a company

Whether a business is looking to expand its existing operations, find a struggling business to turnaround or stepping into a new market for the first time, acquiring a company is one of the most common and effective ways to develop and grow any business. The process does, however, carry an element of risk and so acquirers need to keep a number of considerations in mind, some of which are summarised in this article.

1. Assets or shares?

While we're assuming for the purpose of this article that the acquisition will be of 100% of a company's share capital, the alternative, a trade and asset purchase, should always be considered.

While a share purchase may be the simplest route from a commercial standpoint, it does mean the business will be acquired "warts and all." If the target company has a lengthy trading history and/or is susceptible to hidden liabilities, an asset purchase allows the purchaser to cherry-pick the best assets and leave behind the liabilities. This can be highly attractive even if the legal practicalities of transferring each individual asset can be quite cumbersome. In addition, both acquisition structures carry potential tax implications and getting the right advice will be key.

2. The "A Team" of advisers

It is never too soon to get a specialist corporate finance adviser and lawyer involved. They can guide acquirers on the first approach to the target company and flag up show-stopping pitfalls before too much time and money has been invested.

Good legal and financial advice throughout the transaction will pay dividends. A missed liability or over-optimistic financial forecasts could be far costlier than any adviser's fees.

3. Exclusivity

Before incurring substantial due diligence costs, acquirers should make sure they have legally enforceable rights of exclusivity. These should lock out other potential purchasers during negotiations (and ideally for a time period afterwards if the deal collapses).

Depending on respective bargaining power, it may even be possible to obtain an indemnity from the seller to cover professional fees in the event the seller pulls out without valid reason. This will keep the seller focused on the transaction as they are certainly more likely to be committed to the deal if there is a risk of losing money.

4. Due diligence – the devil in the detail

It will be vital to know what is being bought.

Properly executed financial due diligence should give a full picture of how the company is performing now and how it is likely to perform in the future. Legal due diligence can uncover issues regarding employment matters, intellectual property rights and compliance with relevant legislation. Financial due diligence will focus on the quality of historical earnings and maintainable profits, future prospects of the business and balance sheet black holes. The purchaser should obviously have also carried out its own commercial due diligence.

The results of any due diligence gives the purchaser the opportunity to renegotiate the purchase price and demand warranties to cover any potential liabilities.

5. The warranties

Having completed due diligence, a good set of warranties will be needed to protect the purchaser in respect of the risks and liabilities being purchased.

In valuing the company, the purchaser will have made some key assumptions (for example, that the company is not subject to any litigation and that the accounts have been properly prepared) and it is vital that they are protected in the event that these are not true. By the acquirer's insistence on a comprehensive set of warranties, the seller will be motivated to disclose all possible problems.

Only by giving a certain level of disclosure can a seller protect itself from a warranty claim. Without negotiating a set of warranties, the acquirer risks forming an incomplete and inaccurate view of the company. It also denies itself the right of recourse to the seller in the event of an undisclosed liability.

6. The warrantors

Where there is a single seller, there is usually just one single warrantor. If there are several shareholders all selling their interests in the company, agreeing the identity of the warrantors can be more difficult.

Where shareholders have been one step removed from the day-to-day management of the company (such as institutional investors), they will be reluctant to give any warranties on matters in which they have not been actively involved. In such circumstances, where they do give such warranties, it is likely that they would seek to limit their liability to their actual knowledge on an individual (rather than a joint and several) basis.

Purchasers would be strongly advised to resist liability for warranties on an individual basis and ensure liability is given on a joint and several basis. This means that it will be possible to pursue any one or more of the warrantors for the whole liability in the event of a breach. It is then up to the shareholders to determine how they contribute to and share any such liability.

7. Holding back the money

It is important to remember that, regardless of the level of protection procured through due diligence and warranties, protection is only as good as the seller's creditworthiness or financial position. If the seller does not have the money to pay out on a claim, the purchaser will be left carrying the can.

Those buying from a large corporate structure may want to ask for a parent company guarantee to back up the warranties. For most transactions some part of the purchase price should be held back. If it is intended that any of the sellers are remaining with the business after completion, discuss the possibility of an earn-out structure or deferred consideration whereby part of the purchase price is paid upfront and the remainder held back until certain conditions have been satisfied. Similarly, the parties could agree to ring-fence part of the price. This is then held in an escrow or retention account for an agreed period of time during which the purchaser has the benefit of a secured pool of money to which it can have recourse in the event that any issues are discovered after completion.

8. How much to pay?

No issue will be more commercially and emotionally charged than the purchase price. There is no hard-and-fast rule on the best way to value a company and the method chosen will have as much to do with future plans as it does with the current status of the company. Multipliers of gross sales or post tax profits, book value, return on investment and capitalised earnings can each form a good basis for valuing a company, but ultimately the key drivers may be as simple as how badly the seller wants to sell and how determined the buyer is to buy.

9. Protecting the value of the company

Even before conducting due diligence on the target company, it is likely that the buyer will have a good idea as to where the value of the company ultimately lies.

Every company will have its key assets and any sensible buyer will work hard to ensure that the acquisition has as little impact on those assets as possible. It may be that the company's business is focused on a small number of vital customers. Legal due diligence should uncover whether there are any change of control clauses in the relevant contracts which could trigger termination rights for the customers on completion of the transaction. Even if no termination rights are triggered, ensuring customers are fully informed and happy with the new ownership could pay dividends in the future.

Perhaps even more important than the customers is the quality of the management team. Legal due diligence should reveal whether there are any potential change of control or golden parachute provisions in the employment contracts. Consideration should also be given to whether the management/workforce is to be incentivised as part of the transaction to safeguard the value of the company going forward. If the sellers play an important role in the day-to-day running of the business (and will be exiting as a part of the sale), make sure sufficient handover arrangements have been put in place prior to completion to ensure a smooth transition and minimise the loss of knowledge and impact on the value of the company.

10. Where's the money coming from?

It is rare to find a purchaser who can comfortably finance an acquisition out of its own resources.

Careful thought will need to be given as to where the funds are coming from. A purchaser may need to approach its bank for an extension of overdraft facilities or to secure a term loan – a far harder task in these difficult economic times.

Alternatively, an investment partner may offer up the additional cash, but regardless of whether this is another individual or a venture capitalist/institutional outfit, it is likely that such a partner will be pursuing its own agenda and want sufficient control and protections over management decisions and cash flows.

Institutional investors will be particularly concerned about their exit route as this is how they see a return on their investment. Be sure the buyer understands any investment partner's expectations and be aware that such funding gives rise to a new round of negotiations and legal documentation quite separate from the intended acquisition.

With funding still hard to source and all parties taking a far more cautious approach to any potential deal, it has never been more important to ensure that purchasers have a basic level of protection when looking to buy a company. By surrounding themselves with good advisers, establishing exclusivity and putting in the ground work early on, they will ensure that they are well placed to secure a good deal and avoid potential pitfalls further down the line during negotiations and/or after completion.

Andrew Wordsworth looks at a series of topical VAT issues.

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VAT as easy as 123

1. A change was made in the 2012 Budget which affected the VAT liability of "storage facilities" from 1 October 2012. HMRC have recently issued an information sheet which provides an indication of how far reaching these changes are likely to be. The information sheet confirmed that where a property was being used for "storage" there could be a VAT problem which could result in VAT being due to HMRC, backdated to 1 October 2012.

The new rules state that if a property, including rented property, is used for "storage," any income attributable to the landlord should have VAT added at the standard rate.

HMRC have stated that it is the responsibility of the landlord to ensure that they are aware of the use their properties are being put to. This would mean that should it be found that a property has been used for storage with no VAT charged, the extra amount due will be taken from the landlord, who would then need to attempt to recover this from his tenant.

There is more detail on this change in a longer article on our website.

2. There has also been a recent VAT case that may affect charities with investments.

Traditionally HMRC's view has been that any VAT incurred as part of the management of a charity's investments which relates to the non-business activity of investment is not recoverable.

The case has questioned HMRC's presumption with the tribunal agreeing with the appellant charity that while the investments themselves were non-business, the income received from them was used in all areas of the business, including the taxable parts. This made the related VAT "residual" and so recoverable as a part of the VAT partial exemption calculation.

This case opens up an opportunity for other charities and not for profit organisations (including schools, academies etc.) who have investment activities and taxable supplies but who do not recover the VAT on their investment activities.

3. Finally, a reminder that HMRC are to remove the concession in relation to the Road Fuel Scale Charge (RFSC) that applies for partially exempt businesses, from 1 January 2014.

This concession allowed partially exempt businesses to reduce the Road Fuel Scale Charge by applying their partial exemption (PE) recovery rate to them.

HMRC have however been informed that this concession must either be formalised and brought into legislation or removed. Following a consultation they chose to remove it. HMRC have published a document that sets out a new method of calculating the recoverable VAT that, they claim, provides a similar result to those realised under the concession.

This is:
VAT on RFSC + ((VAT charged on fuel purchased in period – VAT on RFSC) x PE Recovery rate)

Illustrating this by way of example:
- VAT on RFSC = £300.00
- VAT incurred on fuel purchased = £630
- PE recovery rate = 40%
- 300 + ((630 – 300) x 40%)
- 300 + (330 x 40%)
- 300 + 132 = £432 input tax recovery

If, as a result of the withdrawal of the concession, you feel that your partial exemption calculation no longer gives a fair and reasonable recovery it may be possible to apply to HMRC for a special method that matches your business model more closely.

If you feel that any of these points may affect you please do not hesitate to contact either your usual partner or Andrew Wordsworth in our VAT department who can advise on whether a special method can give you a better result.

Claire Charlton outlines this valuable tax relief.

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Rental Property

– Wear and Tear Allowance

Generous tax deductions are few and far between these days, but one which continues to be available is the "wear and tear" allowance in respect of residential property which is let on a furnished basis.

Broadly, a deduction may be claimed in arriving at taxable rental income each year, being 10% of the rents receivable in the tax year, subject to certain adjustments to prevent artificial inflation of claims. The deduction is intended to cover the cost of purchasing and replacing the property contents including furniture, appliances, kitchen equipment, curtains and floor coverings, linen etc. If the 10% allowance is claimed, the cost of replacing these items cannot be deducted from rental income, but the cost of repairing them can.

The allowance is not intended to cover the cost of replacing or repairing fixtures such as kitchen and bathroom fittings, windows and light fittings nor does it cover redecoration costs. Such expenses may be claimed as a deduction from rents in addition to the wear and tear allowance.

If the 10% wear and tear allowance isn't claimed, the alternative is the "renewals" basis which does not give a deduction for the initial cost of equipping the property, but does allow a deduction for the cost of subsequent replacements as and when those costs are actually incurred. Given the simplicity of the 10% annual deduction, and the fact that it usually results in a more favourable tax deduction in terms of both size and timing, it is generally the more popular choice. However, it is a "once and for all" choice; there can be no switching from one basis to another and all furnished let property belonging to the same landlord must be dealt with on the same basis.

This brings me to the question of what constitutes a furnished property. The legislation says that the property must have "sufficient furniture, furnishings and equipment for normal residential use." In other words, the tenants could simply move in and live there, albeit that they may choose to bring additional "luxury" items with them.

Furnished holiday accommodation, let on a short term basis, is subject to different tax deduction rules if it meets the criteria to qualify as a trade.

In preparing annual rental accounts for our clients, we make a careful review of all expenses incurred to ensure that deductions are maximised. If you are a landlord and have any queries about whether a particular expense will be deductible for tax purposes, or if you are thinking of setting up a furnished residential letting for the first time, please contact Claire Charlton.

Tony Glenton has the last word
with news of other events in 2013.

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The first Belsay Horse Trials were held this year in the picturesque setting of Belsay Hall/Castle and Gardens, having previously been held at the Linnels near Hexham.

Ryecroft Glenton were delighted to have supported the event as a sponsor. It was estimated that around 4,000 people attended over the weekend to watch just under 500 equestrian competitors, including Olympic silver medallist Nicola Wilson, take part in the dressage, show jumping and cross country. The event was considered to be a great success both by competitors and spectators.

Tony Glenton, Senior Partner of Ryecroft Glenton said: ***"We have been associated with Belsay for many years. The initiative to bring the horse trials to Belsay for the first time was something we wanted to support strongly. The setting is outstanding and the event will, I'm certain, become an increasingly important one in the horse trials calendar in the years ahead. Laura and Peter de Wesselow together with Edward Pybus are to be congratulated on an event which was beautifully organised and thoroughly enjoyed by participants and spectators in wonderful surroundings".***

Three of Ryecroft Glenton's senior team slept rough last month to raise money to fight homelessness across Tyneside, taking part in the CEO Sleepout at St James' Park on 17th October 2013.

The CEO Sleepout is a local event of national business significance. Organised by the Middlesbrough and Teesside Philanthropic Foundation, business leaders gave up a night of comfort to sleep rough despite the weather. The event was held in partnership with the Newcastle United Foundation. Managing partner Chris Robson and director of corporate finance Carl Swansbury joined corporate finance executive Abu Ali, who was one of the organisers of the CEO Sleepout. Abu's friend Lee Halpin died earlier this year while trying to raise awareness of homelessness.

Ryecroft Glenton managing partner Chris Robson said: ***"I admire Abu's determination to raise the issue of homelessness. Carl and I decided that we should do more than just donate and we wanted to experience it for ourselves. Carl, Abu and I have been amazed at the generosity and support we have received so far. The funds we have raised will all go to homeless charities on Tyneside and I hope as many people as possible will visit our justgiving page."***

Abu went to school with Lee Halpin, who was producing a documentary film about homelessness when he died while sleeping rough to understand for himself what it was like.

Abu said: ***"Lee was always a passionate campaigner and was determined to raise the issue of homelessness. It's so sad that he lost his life in doing so. I'm delighted to have such strong support from Ryecroft Glenton.So far, a very impressive total has been raised amounting to £4,165!!"***

You can still donate to the Ryecroft Glenton justgiving page by visiting
http://www.justgiving.com/RyecroftGlenton
Visit **http://www.ceosleepoutuk.co.uk/** for more information

Newcastle	***Morpeth***	***Rothbury***	***Whitley Bay***	***PFM***
32 Portland Terrace	55 Newgate Street	Barclays Bank Chambers	189 Park View	29 Portland Terrace
Newcastle upon Tyne	Morpeth	Rothbury	Whitley Bay	Jesmond
Tyne & Wear	Northumberland	Northumberland	Tyne & Wear	Newcastle upon Tyne
NE2 1QP	NE61 1 AY	NE65 7SS	NE26 3RD	NE2 1QP
Tel: 0191 281 1292	Tel: 01670 512 102	Tel: 01669 620 360	Tel: 0191 252 1849	Tel: 0191 281 6074
Fax: 0191 212 0075	Fax: 01670 510 385	Fax: 01669 622 854	Fax: 0191 297 1204	Fax: 0191 281 5396