PKF FRANCISCLARK

Chartered accountants & business advisers

# Corporate Services

Spring 2018

supporting you and your business

# Welcome to our Spring 2018 Corporate Services newsletter

Despite the slow progress of the Brexit negotiations, the UK economy continues to grow, albeit at a slower rate than previously, and also behind G7 and global growth generally. Forecasts for 2017 are for GDP growth of 1.8%, and the IMF is predicting growth to reduce to 1.5% in 2018. These are the lowest growth rates since 2012. The Office for National Statistics' (ONS) numbers of those in work increased sharply and wages rose at their fastest rate (2.4%) in almost a year. That leaves the UK's unemployment rate at a four-decade low of 4.3%. This, combined with inflation at 3.1%, was part of the picture that led the Monetary Policy Committee to increase the base rate in November 2017, the first time since July 2007. It also suggested that 'further modest increases' are likely to be needed over the next few years.

Businesses in the South West continue to perform well against this backdrop but will face a number of challenges in 2018 including recruitment, wage inflation (with inflation at 3.1% and wage growth at 2.4%, underlying earnings still remain negative), interest rate rises, foreign currency fluctuations and of course understanding the wider implications of Brexit arrangements.

Experian has reported on the most active legal and financial advisers in the South West's mergers and acquisitions (M&A) market in 2017 and we are delighted to have been the most active adviser - working on 53 deals. We also held our first Cyber seminars in November 2017 which were very well received and supported. We were also pleased with record numbers at our Finance Director (FD) seminars which ran across five locations; some of the topics covered are included in this newsletter.

**Glenn Nicol**
**Partner**

**Details of our 2018 FD seminars are listed on the back page of this newsletter. For further details and to reserve places, please visit our website: www.pkf-francisclark.co.uk/events.**

# Brexit - what should you be doing now?

The Brexit vote has undoubtedly increased uncertainty for businesses, which is never a positive attribute to business confidence. Nevertheless, regardless of your personal views on Brexit, it is imperative that businesses continue to plan ahead, seize opportunities and manage risk. So what should you be doing now?

In an uncertain world planning becomes more important. Businesses need to be undertaking contingency planning to assess some of the possible impacts of Brexit (both challenges and opportunities). This is about demonstrating leadership and risk management: what is the potential impact, and the likelihood of each possible outcome? Which ones are business critical? What actions need to be considered now to manage the situation?

An issue here is lead times - especially when management of customs duties and border logistics are concerned. Authorised Economic Operator (AEO) status may be appropriate. This status reduces border and customs obligations on a business. It is administered by HMRC and already has pretty long lead times to set up. Those lead times are only likely to increase as Brexit approaches and AEO status may become more vital to a greater number of businesses.

This is just one example. FDs need to go through a systematic process to establish the impact on their business. This is probably best done by going through the profit and loss account and assessing the potential impact of Brexit on a line by line basis. Whilst the impact of customs duties need to be considered, this is only part of the story and interest and exchange rates, labour supply, border logistics and working practices should be taken into consideration.

A key part of considering options is to review the supply chain. It may be appropriate to restructure the business into EU and non-EU operations and to structure the supply chain accordingly. This will have implications for the location and production facilities, warehousing and sales teams. Changes in business structure may be required and, as well as AEO status, it will be important to consider Inward Processing Relief for customs duties.

**PKF Francis Clark has a team focussing on Brexit implications for our clients and can help with the issues identified here. Stuart Rogers is leading on the business structuring implications, and Liam Dushynsky is concentrating on customs duties. However, in the first instance please speak to your usual contact should you require our assistance to consider the implications for your business.**

# Alternatives to the 100% trade sale

Having spent many years building up a business, most owner-managers expect to 'sell-up and retire' at some future date, where there is no natural succession in place. However, when it actually comes to that intended date, a simultaneous 'cliff-edge' termination of both ownership and day-to-day management may be impractical or not actually desired.

At the extreme there may not be any trade party that wants to buy the business, or alternatively many business owners would like to continue to work in some capacity, but not for a new owner - having been the boss and in control of their own destiny for many years.

Alternatives to both scenarios (as well as other situations such as when the current owners want to sell/exit at different times) may be achievable through a 'vendor initiated management buy-out' (VIMBO). This process can be 'controlled' by the current shareholders - as without their agreement, there won't be any transaction. Consequently, the owners can have a significant influence over the structure of a deal and the terms (even down to the price and when they get paid - obviously to the extent that it is acceptable to the MBO team and their funders).

In the current climate of economic and political uncertainty, with talk of capital taxes rising significantly with any other colour of government, there is the added risk that, whilst preparing the business for the 'perfect sale' in several years' time, the external world moves on and the net value received could be significantly lower.

However, business owners can mitigate these risks through alternatives to the 100% trade sale by using a VIMBO approach or even retaining an interest with a majority sale to a trade purchaser (if the latter will allow it).

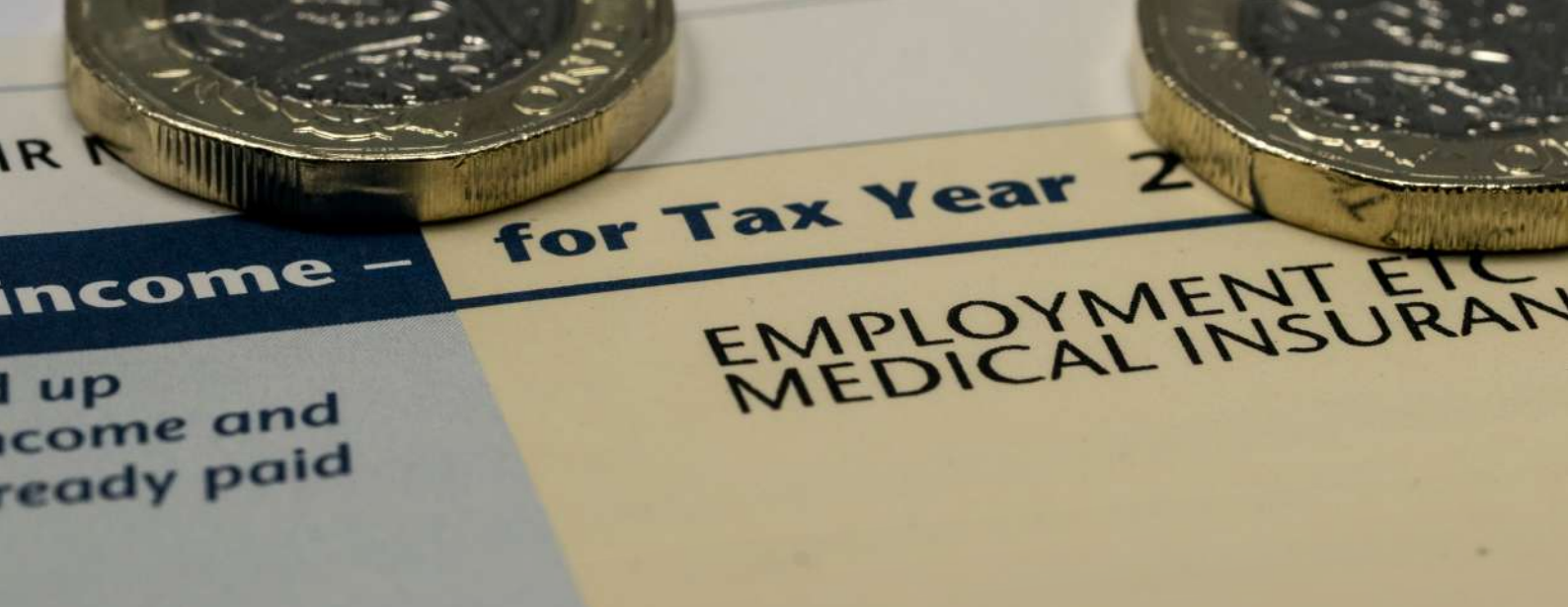
Business owners are therefore in a unique position of being able to take advantage of low interest rates at a time when significant amounts of cash are available, to crystallise some (or all) of the increase in value of their business under the current low capital tax rates and still potentially benefit from some future increase in the value of a business. In addition, any 'deferred' element can be structured to be 'IHT exempt' which avoids the scenario where they sell 100% to the trade and pay 10%-20% capital gains tax now, and potentially a further 40% on death on any cash still held.

# VAT

In our most recent round of FD seminars we looked at two recent cases. The first of these was the First Tier Tribunal case of a law firm, Brabners LLP, which related to the recharge of e-search fees and whether or not these could be treated as disbursements for VAT purposes. Although the case is appropriate to legal firms, the principles of disbursements are generic and could apply to all businesses who recharge costs. The second case was the European court decision in Mercedes Benz Financial Services which related to the VAT treatment of the Agility optional purchase scheme. The facts were specific to this agreement but provided a reminder of the difference in treatment of the outright purchase of a car and the leasing of a car for both the supplier and the purchaser.

We then looked at the 'Top 10 VAT tips, tricks, twists and trips'. This section provided a high level summary and aimed to include at least a few points that were relevant to each attendee. This included VAT planning tips such as ensuring that VAT is recovered on mileage allowances and the ability to make backdated claims in certain situations. A recap of the rules relating to bad debt relief was provided and when the relief can be claimed. The rules relating to the requirement to make a repayment to HMRC in respect of unpaid purchase invoices more than six months old were explained. The circumstances in which requests for payment can be issued were explained. Where requests for payment can be used, VAT does not need to be accounted for until payment is received. Turning to overseas trade, there is a requirement to register for VAT in other EU countries under the distance selling rules where B2C sales of goods are made from the UK in excess of certain limits. With the increase in online sales of goods and more sales of goods being made via online retailers, it is becoming common for stock to be held at locations outside the UK; the requirements for overseas VAT registrations in this situation were explained. The intricacies of buying or selling all or part of a business were explained, highlighting the problem areas and stressing that taking VAT advice early is key.

**As detailed in our Brexit article, Liam Dushynsky is one of our Brexit team and is leading on customs duties. If you have any other VAT queries please speak to your usual contact.**




# Auto enrolment and payroll update

Five years on from the introduction of auto enrolment (AE), together with many changes in payroll processing such as RTI, we look at the current issues in these areas and what you need to consider.

For AE the minimum contribution rate for employer contributions increases by 1% from April 2018 with the employee rate increasing by 2% at the same date. Considering this for your budget forecasts and communicating with employees is something to be considering now.

Many employers will be approaching the three year anniversary of AE implementation which means cyclical re-enrolment needs to be considered. Revisit any employees that opted out and ensure they are re-enrolled plus a new 'Declaration of Compliance' must be made to The Pensions Regulator.

As the AE market begins to mature, it is apparent that some AE schemes are faring better than others from a 'service and financial stability' point of view. If you are having issues or are worried about the sustainability of your pension provider, now may be a good time to consider other options.

Payroll compliance doesn't get any easier as time passes with RTI, AE, Gender Pay Gap reporting and the Apprenticeship Levy to consider as well as the upcoming GDPR legislation in May 2018. With fines being imposed for non-compliance and these potentially leading to investigations wider than just payroll, outsourcing this area could reduce risk and add efficiency to your business.

PKF Francis Clark offers a free 'payroll health check' and a fully outsourced AE compliance service should you wish to consider either of these areas. Please speak to your usual contact.

# Keeping on top of intercompany accounts

Group companies don't exist in isolation from one another. In addition to acting as trading partners, they may share resources in the form of staff or property, use collective purchasing power to obtain the best deals and keep costs down, maximise available cash through treasury management or loans, and mitigate the group's aggregate tax burden. Subsidiaries also provide funds to their parent in the form of dividends. All this needs to be reflected in each group member's accounting records.

The issue is that while it is easy to move assets and resources around a group on a continuing basis, at the year end all the intercompany balances need to be agreed, reviewed for recoverability and appropriately presented in the accounts. For a busy FD it can be easy to lose control over the recording process, resulting in a time-consuming reconciliation exercise at the year end. Good intra group 'housekeeping' helps to minimise the year-end burden, while making it easier for the group to identify and implement opportunities to distribute funds or streamline its structure.

For example, having regular, robust, intercompany reconciliations ensures that both parties have recorded transactions accurately. It is much easier to identify differences on a quarterly or monthly basis, especially if there is a large volume of activity. Having a standard format for reconciliations may also be useful, especially if the financial operations are not run by one individual or the group is becoming geographically diverse.

Try to clear down intercompany balances periodically. Apart from minimising the risk of recovery issues, this will also help to prevent complications when determining distributable (i.e. realised) profit. Unsettled intra group sales, whether they arise from trade or assets, may not fall to be treated as realised profit, especially if the debtor company doesn't have the means, or does not intend to pay. This in turn restricts the ability of a subsidiary to pay profit up to its parent by way of dividend.

If some of the group's activities are overseas or occur in foreign currency, keep on top of exchange rates used on intra group transactions. Many an intercompany reconciliation has faltered because no one kept a note of the exchange rates.

Consider separating longer term funding from short term trading balances. If balances simply build up over time in a sort of 'bucket', this could result in significant creditor balances repayable on demand, upsetting the company's solvency position. As well as reflecting more accurately the strategic and commercial realities, formalising longer term investment, including applying market rates of interest, will avoid the complexities of discounting under FRS 102.

Where intra group transaction routines are not robust or well-managed, it can result in the build-up of significant balances that cannot easily be settled and, in some cases, can only be eliminated through formal waivers.

# A robust strategy to prevent against cyber-attacks along with GDPR considerations is now a business necessity

With the new year comes new business planning, and with malware and 'phishing' attacks increasing month on month, combined with the imminent arrival of the new General Data Protection Regulation (GDPR), the matter of digital security should be high on the agenda of most boards.

Recent examples of cyber-attacks include the crypto-locker virus which is still bringing systems down globally. This, added to the fact that companies are bombarded with phishing scams every day, presents severe risks. These scams take the form of emails that try to persuade staff to download malicious attachments, click on suspicious links, provide personal details or other sensitive data. A targeted 'spear' phishing email campaign was blamed for instigating the recent cyber-attack that caused a major power outage in Ukraine.

Closer to home in the West Country, for Q1 2017, there was a reported loss due to cyber-crime of over £5,172,000, (source: Action Fraud) and this is just the tip of the iceberg as it is believed that the majority of cyber frauds go unreported.

Although the appointment of specialised consultants can be invaluable in offering practical advice, many boards still require assurance that they are doing all that is possible to protect themselves. The UK government is now pushing businesses towards its Cyber Essentials schemes in order that a company can assess and improve its digital defences. Should a company suffer a breach, the Cyber Essentials certification provides evidence that it has carried out basic steps towards protecting its business and data from internet based cyber-attacks, and therefore the scheme can mitigate fines from the ICO (Information Commissioner's Office). The UK government estimates that by undergoing this exercise, companies can protect themselves against an estimated 80% of cyber-attacks.

The certification covers five key areas:

- Secure configurations
- Firewalls
- Access controls
- Patch management
- Malware protection

IASME offers a certification route to demonstrate that you are preparing for the introduction of GDPR. This certification is available as a verified self-assessment or as an on-site audit.

Once the assessment is passed, a business will receive a certificate and also a website/email badge to show the 'GDPR ready' status as well as Cyber Essentials and IASME Governance, which are all embedded in the one assessment.

With regard to GDPR, the two-year implementation period ends in May 2018, yet the majority of UK businesses are unprepared. A new report from Trend Micro has revealed that the boards of UK companies are not treating the new EU GDPR with the seriousness that it deserves. This has resulted in an overconfidence when it comes to UK GDPR compliance.

Rik Ferguson, VP Security Research at Trend Micro commented, "The lack of knowledge demonstrated in this research by enterprises surrounding GDPR is astounding. Birth dates, email addresses, marketing databases and postal addresses are all critical customer information, and it's concerning that so many British businesses, despite their confidence, are unaware of that. If businesses aren't protecting this data, they aren't respecting the impending regulation, or their customers, and they definitely aren't ready for GDPR". (Source: EUGDPR).

Writing in City AM recently, Liz Brandt, the chief executive at Ctrl Shift said, "Many businesses are less than enthusiastic, treating GDPR as another red tape burden. Too many companies are sinking huge sums of money into just becoming compliant, while many others are ignoring the looming regulation altogether.

"This is a missed opportunity. GDPR is a chance for businesses to sail ahead of competitors - to become their industry's Netflix and leave rivals in the 'Blockbuster Bargain Bin'. It is also a significant opportunity for the UK economy to become more creative and productive".

PKF Francis Clark works with companies to help them protect their businesses against cyber attacks and keep their data safe. To find out more about this and the accreditation schemes, please contact Richard Wilding on **01803 320100** or at **cyber@pkf-francisclark.co.uk**

# Energy & Sustainability

The UK renewable energy market continues to develop and adapt in spite of an ever changing regulatory backdrop. From the low it experienced in 2015 with the Government's early closure of the Renewables Obligation (RO), this resilient industry has successfully responded in typical fashion as is evidenced with some notable highs.

With the recent recruitment of two senior energy experts into our awarding wining corporate finance team, PKF Francis Clark is continuing its support of the energy industry through the provision of leading commercial and financial advisory services at the development, primary and secondary phases of the market.

## Subsidy-free solar

In September, we witnessed the opening of the UK's first subsidy-free solar farm, complete with storage, by Anesco. While the site benefits from unique advantages which mean that this does not necessarily form a blue-print for subsidy free solar across the UK, it does still represent material progress in a technology which was only recently in disarray following the closure of the RO.

## Record electricity generation

Renewables' share of electricity generation was a record 30% in 2017 Q2, up 4.4 percentage points on the share in 2016 Q2, reflecting both increased wind capacity and wind speeds, as well as lower overall electricity generation.

## Subsidy free onshore wind

As a result of competition throughout the development and supply chain, innovative financing solutions and greater focus on offtake arrangements, we are witnessing the key steps necessary to enable subsidy-free onshore wind to become reality. While developers and construction companies conclude the build out of the last RO projects, the activity in preparing the next phase of subsidy free wind is very real.

## Offshore wind's success in the latest CfD auction

With the majority of capacity in September's second CfD allocation being allocated to offshore wind clearing at a strike price of £57.50/MWh, there is now unequivocal evidence that renewable energy at scale is good value for money when compared to fossil fuels and nuclear.

## Battery Storage

Growing system need for storage/flexibility as penetration of intermittent renewables grows has coupled with rapidly falling costs to drive growth. With Li-ion battery costs down an estimated 80% since 2010, deployment is anticipated to grow fast: from trivial levels of deployment on the system, to 0.6GW at the end of 2016 to up to 8-12GW by 2021 in some scenarios.

# Finance Directors' events feedback

In November 2017, over 300 Finance Directors and Controllers across the South attended our FD Directors' Update seminars held in Plymouth, Exeter, Taunton, Bournemouth and Bodmin. During the packed programme, PKF Francis Clark's experts provided key updates and focus on: The role of the FD; Financial Reporting - FRS 102.2 and IFRS; Intercompany Accounts; Cyber Security and the Cyber Essentials Schemes; VAT; Brexit; Business Tax; Auto Enrolment and Payroll; Energy - Opportunities to Create Investment Income; and MBOs - An Alternative to a Full Business Sale.

Some delegates feedback:

*"The overall content of the presentation was excellent".*

*"Excellent broad breadth - useful contacts".*

*"Excellent - best so far. I do go to others but this is the best by some distance - well done".*

# Forthcoming Finance Directors' events

Set out below are details of the next round of our Finance Directors' Update events, scheduled for June 2018:

| | |
|---|---|
| Thursday 7 June<br>8.45am -1.00pm | Somerset County Cricket Club<br>Taunton<br>Somerset<br>TA1 1JT |
| Monday 11 June<br>8.45am - 1.00pm | Boringdon Park Golf Club<br>55 Plymbridge Road<br>Plympton<br>Plymouth<br>PL7 4QG |
| Tuesday 12 June<br>8.45am - 1.00pm | AFC Bournemouth<br>Vitality Stadium<br>Bournemouth<br>Dorset<br>BH7 7AF |
| Wednesday 13 June<br>8.45am - 1.00pm | Exeter Racecourse<br>Exeter<br>Devon<br>EX6 7XS |
| Tuesday 19 June<br>8.45am - 1.00pm | The Alverton Hotel<br>Truro<br>Cornwall<br>TR1 1ZQ |

PKF Francis Clark experts in financial reporting, corporation tax, VAT, financial planning and funding and transactions will once again be examining the latest financial issues affecting your business. A full programme and invite will be distributed at the end of April. However, you are already able to book your place online at:

www.pkf-francisclark.co.uk/events

Alternatively, please contact:

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Events Co-ordinator
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