Kirkpatrick & Hopes

income & share ownership planning accountants

Initial Financial Healthcheck follow-up report

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Initial Financial Healthcheck follow-up report

Following our meeting earlier, as promised here is our report setting out the various opportunities for improvements in business and tax-savings ideas that we discussed.

Section A: Accounts

1. I will ask our Direct Debit company contact to call you to see if they can help you with their DD service, so you can collect in the money owed to you by customers more quickly and with less effort.

2. Let me know if you have more problems with the VAT accounting. We are Xero Accounting Software Partners and will be able to help you deal with such problems now and in future.

3. I suggest you start including Corporation Tax in your management accounts to give you a more accurate overall profit figure. I would use an assumed rate of 20% (calculated as 20% of profits BEFORE deducting and dividend payments).

Section B: Tax planning

4. We discussed how you and the other shareholders will take your money out of the company. You intend to take £100k a year each in salary, hopefully going up to £125k after next year.

   I would like to explore ways of potentially using dividends rather than salary. This would be the main focus of the next stage of our planning work as part of the income and succession planning work.

   This can save over £10k a year each in tax and National Insurance, as well as giving you significant cash flow benefits by paying tax much later.

5. We discussed how spouses and possibly children could benefit from share/dividend planning in future. This can be done for over 18s, and in certain circumstances even for under 18s. This can save up to £10k a year in tax for each child.

6. I attach a copy of our use of home spreadsheet to allow you to work out how much each of the shareholders can be paid (tax-free) for working from home. This may allow you to take several £000s out of the company tax-free every year.

7. I mentioned the LLP planning that you could use for new income streams (e.g. new services or customer groups, or trading in new territories) in future. This can reduce your effective tax rate from about 50% to 10% on the future value of that business. To illustrate, this could give you a long-term saving of up to £400k in tax on a business worth £1 million!

8. I can speak to your business partners separately about whether their personal finances/investments are optimised for tax with their spouses.

9. Employment status and IR35. It looks as if your consultancy payments to date may be questionable as possible 'disguised employment' under IR35. Beware of this for future self-employed/consultancy workers in the business.

10. We discussed the 10% Entrepreneur's Relief CGT tax rate and special Inheritance Tax exemption for company shares (Business Property Relief, BPR). I am sure you qualify for these now, and we would monitor this on an annual basis to ensure you get the full benefit, which together could mean a saving of close to 60% of the value of the company.

11. Child Benefit. I explained that this is reduced or lost from next year for households where either partner earns over £50k. The remuneration planning needs to take account of this to keep you and your life partner below that threshold if possible.

12. VAT:

    Cash accounting. This allows you to pay and reclaim VAT when you actually get paid and when you pay suppliers, rather than according to invoice dates. It can be a huge help to company cash flow. You can go into this scheme if turnover is less than £1.35 million. Once in the scheme, you can stay in until turnover reaches £1.6 million as a general rule.

    Flat rate scheme. This allows you just to pay a fixed percentage of your VAT inclusive total turnover (usually about 14% for consultancy businesses) but you cannot then reclaim the VAT on your costs (unless they are capital equipment costing more than £2,000).

13. Research and development (R&D) tax credits etc. You may be able to get tax relief of up to 225% of the actual costs you incur on qualifying R&D costs. The possible loss of this is obviously one of the factors we need to allow for in considering the use of dividends as part of the ISOP planning.

    Bear in mind the Patent Box rules that may allow you to reduce your company tax rate to 10% on certain patent-related income streams.

14. We discussed various employee tax planning points/tax free benefits, including:

- childcare vouchers
- tax-efficient company cars
- £4 a week tax-free working from home allowance
- £150 a year entertainment allowances
- bike to work scheme
- tax-free life insurance
- parking spaces
- suggestions schemes: up to £25 per suggestion, subject to conditions. See here for more detail: **http://www.hmrc.gov.uk/paye/exb/a-z/s/suggestion-schemes.htm.**

15. We can do a PAYE settlement agreement (PSAs) to allow the company to pay the tax and NI on any benefits that *are* taxable, for any employees for whom you would rather not have to pay tax on those benefits.

16. Let me know if you would like to find out more about ways to reduce Stamp Duty when you buy a new house.

17. You are not claiming interest relief on the money you borrowed a couple of years ago to buy your company shares. I recommend doing this on the current tax return and for last year's too. Let me know if you'd like us to do these tax returns for you.

18. Overdrawn directors' loan accounts. Based on the information I have, I recommend that this should be left as an overdrawn loan in the accounts. Any amounts outstanding on the year end accounts and not repaid within nine months of the end date of those accounts, will attract a 25% payment to the tax man. (However, you will get this 25% payment back nine months after the accounts year in which the loan is repaid.) We have various strategies that we can use to help manage this situation going forward.

Section C: General business

19. It sounds as if all your employees' employment contracts need updating. Note that it is usually better from a tax-planning point of view NOT to have employment contracts for directors (so they are not caught by national minimum wage rules).

20. We discussed the new NEST pension contribution rules being phased in from 2014 to 2016 for companies with fewer than 500 employees. This will increase your payroll costs by up to 1% per annum over the first three years. This is, in effect, a forced pay increase for your employees, so allow for it when you agree their pay rises!

21. £1,000 grants for IT equipment, iPads etc. Here's the Sustainable Routes website link: **http://www.sustainableroutes.co.uk/** to find out how to apply.

22. Credit checking and monitoring. I would recommend using this for current and potential clients. We use Barclays' Credit Focus system, but there are many such systems around, and very inexpensive.

23. Let me know when your website development is ready and we can perhaps find a way of putting a link to it on our site (e.g. as part of a testimonial).

Section D: Personal finances

24. You have an IFA who deals with advice on insurances, pensions, investments etc. I recommend that you have annual reviews with them to discuss all these issues and ideally to give you a cash flow forecasts of your likely income in retirement, so you know now what you need to save or what your business needs to be worth to give you the lifestyle that you want in retirement. It may be useful for us to have a joint meeting with as part of our ongoing monitoring of your financial affairs to make sure nothing 'falls between the cracks' in the advice that you get from your advisers.

25. It may be useful for you or your IFA to get a state pension forecast as part of your personal pension/savings planning. You can call 0845 3000 168 to get the forms (the online service wasn't working last time I looked).

26. Your Wills need doing! This is particularly important for unmarried couples and those with children. We would want to be closely involved with this (as should your IFA), again to ensure nothing is missed between your various advisers.

27. Your credit card etc. debts from the recent lean period in the business. I recommend that you make your IFA aware of this in case it affects their advice. Let me know if you'd like to ask our debt management adviser contact that we deal with to get in touch with you.

Business and exit planning in general

As previously discussed, I think the main issue here is getting complete clarity over the personal goals of shareholders (and any future shareholders) in terms of:

- exit plans: when to sell
- exit plans: how much they need from the sale
- income needs up to the sale
- roles in the business
- working hours, holidays etc.

I know you may be aware of some of this already, but I strongly recommend you get this information from everyone and ideally write it down somewhere!

Next time we meet I can show how our Build to Sell process (part of the succession planning work) may be able to help you pull all this together and produce a detailed action plan to guide you towards the eventual sale of the business.

I think that covers everything we discussed - sorry if it all looks a bit daunting! Obviously, we can help prioritise and manage the process of implementing all the necessary changes, perhaps over an extended period to make it manageable, but obviously focusing on the things that will give you the biggest, quickest financial benefit first.

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