Business Matters

News & Information from Alexander Sloan, Chartered Accountants

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Valuing your business

According to the latest research, nearly half of entrepreneurs planning to sell their business are unaware of how much it is worth. The problem is particularly marked for the smallest businesses, with only 37% having a clear idea of the sale value of their assets.

Perhaps these figures should not be surprising. It could be said that valuing a business is as much an art as a science. There is no precise formula that applies to all businesses in all sectors, nor even to all businesses within a sector. Instead, an accurate valuation will depend on consideration of a number of factors. These include:

- **The size of the business –** larger firms tend to be viewed as less risky and so attract a higher price, even if they are less efficient than smaller competitors
- **The prospects for future growth –** buyers sometimes pay more for businesses with high growth rates because they repay the investment more quickly. You might consider selling before turnover and profits level out
- **Diversification –** if you have a wide 'business mix' it can affect the sale price, since buyers may only be interested in one area or market
- **Customer base –** the size of your customer base is important, but so is the quality of your customers and the cross-selling opportunities
- **Profitability –** although generally the higher the profits, the higher the value, some buyers might prefer a business with areas in which large efficiency savings can be made
- **Cashflow and financial management –** the size and certainty of cashflow, and the strength of the balance sheet and financial management are all vital factors.

While you will obviously not wish to undervalue your business, it is also important not to overvalue it. An inflated asking price will dissuade buyers, or make them think you are not serious about selling.

Ultimately, the value of your business will be determined by the laws of supply and demand. If there are plenty of willing buyers for your type of business and few sellers, you will get a good price, and if you can allow buyers to set a price through competitive bidding, so much the better.

While a business is only ever worth what a prospective buyer is prepared to pay for it, there are steps you can take to increase the value of your business, and ways to make a reasonable estimate of that value. Call us to discuss your particular circumstances.

HELPING YOU AND YOUR BUSINESS TO STAY AHEAD

We can help you make the most of your wealth and your business. Call us to discuss:

- Valuing your business and preparing it for sale
- Keeping business taxes and overheads to a minimum
- Developing a plan for tax-efficient profit extraction
- Strategies to improve your bottom line
- Reducing the tax on your estate
- How the Spring Budget announcements affect you

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Change of view for home-working expenses

If you work at home, you will want to claim the extra costs of running a home office on your tax return, or from your employer. HM Revenue and Customs (HMRC) has recently changed its view about what employees can claim, but there are also different rules for different types of taxpayer.

What can you claim?

As a self-employed person you can claim costs in your accounts that are incurred wholly and exclusively for the purpose of your business. Having somewhere to do your business paperwork is essential. If you don't maintain a separate office, you can claim a reasonable proportion of those household running costs that represent the space and time in which your office operation occupies your home. This includes a proportion of your rent, council tax and water rates.

As an employee you can only claim the additional variable expenses incurred by working at home. These costs amount to the increased energy needed to heat and light your property for longer, and the extra water used if that is metered. You can also claim the cost of business related telephone calls, but not a proportion of telephone line rental, or part of your mortgage or insurance costs. These amounts are considered to be fixed whether or not you work from home, so you can't reclaim any part.

HMRC prefers employees to reclaim the costs of home-working from their employers. If you have agreed with your employer that you will work at home for all or part of your working time, your employer can reimburse you for the extra energy used during that time. If you want to claim more than £2 per week, excluding telephone calls, you must be able to demonstrate that your energy bills have increased by more than this amount.

The new view

HMRC's previous view was that employees who were obliged to work at home could also claim a proportion of the fixed costs such as insurance, but now that claim is limited to just the variable costs. Also if your employer does not reimburse your costs there are some extra conditions to be met before you can make a claim for home-working expenses on your tax return:

- The duties performed at home must be 'substantive' – that is, they must represent 'all or part of the central duties of employment'
- Your work must only be possible with certain facilities, such as a specific item of hardware or computer software
- Those special facilities must not be available for you to use at the company's offices
- You must have no option but to work from home.

Your claim will fail if you have any choice about working from home. HMRC's new announcement says that you are deemed to have had a 'choice' even if your employment contract stipulates that you must work from home, if you were also offered a different contract without that stipulation. In that instance, you can't claim any expenses. This might seem very harsh but it is the latest interpretation of the law given in the HMRC Tax Bulletin number 79.

The best approach might be for your employer to reimburse you directly for the additional costs of working from home. Contact us for more specific advice.

Alternative ways of extracting profit

Your company pays corporation tax on its profits, but you are only taxed personally on what you draw out of the company as a salary, bonus, or by other means. The dividends you receive from your company are effectively tax-free in your hands, if your total income for the tax year is less than about £37,000. Once you reach that limit you may want to think about extracting profits in different, more tax-efficient ways. Here are some alternative approaches:

Maximise allowances

Make sure you are using any tax-free allowances available such as mileage paid for the business journeys you drive, paid at the approved rate. This mileage rate varies according to the number of miles driven in the tax year, and whether you drive your own car or a company car. A low emissions company car can still be a tax-efficient way of providing a smaller car for you or another member of your family.

Keep it in the family

If you have young children, your company can provide you with £2,600 of tax-free childcare vouchers per year. This is doubled if your spouse or partner also works for your company. When you pay your spouse between £82 and £94 per week (2005/06 rates), they may pay no national insurance or tax on that income (depending on their circumstances). However, a wage at this level will count toward their entitlement to a state retirement pension. The company should pay at least the minimum wage of £5.05 per hour, and keep a record of the work done to justify the cost on business grounds.

Pay attention to pensions

The company can pay very tax-efficient pension contributions into your own (or any employee's) personal pension scheme, or into a self-administered pension scheme. The new pension rules effective from 6 April 2006 increase the limit of the pension contributions you and your company can make. Care should be taken to ensure that the individual's total remuneration package, including the pension, is justifiable for the work performed.

Property concerns

If you own a property that the company uses for its business, perhaps land used as a car park, a lock-up garage, or even an office building, the company can pay you a market rent. This rent should be declared on your personal tax return and you will pay income tax under self-assessment. You can offset a range of costs connected with the property and there is no NI payable on rental income. When you come to sell that property it will qualify for a higher level of taper relief to reduce the capital gains tax due.

There are other tax-efficient ways of extracting profit, such as short-term loans, or interest, which may be appropriate. Contact us for more advice.

The end of the zero company tax rate

It has been announced that the 0% starting rate of corporation tax is to be increased to 19%. How will this affect you?

The zero rate

When he introduced the 0% starting rate for corporation tax in 2002, Chancellor Gordon Brown suggested that this would encourage small companies to retain profits to invest in the future – typically in plant and machinery (for which a 40% first year allowance was also then available). The rate applied to a company's first £10,000 of profits.

In fact, the move opened a tax loophole for some business owners. By managing the owner's remuneration mix of salary, bonus, benefits and, in particular, dividends, considerable savings of tax and national insurance contributions were possible. The result was that many new companies were formed purely to take advantage of the zero rate.

Anti-avoidance legislation

To counter this avoidance of tax, in April 2004 the Government introduced a tax on non-corporate dividends, with the result that a company paying a dividend to non-corporate shareholders out of profits which had been 'taxed' at the 0% starting rate had to pay 19% of the dividend over to the Inland Revenue. The legislation gave us what is known as the 'non-corporate distribution' rate (NCDR).

That resulted in a highly complex set of rules and calculations – a situation somewhat at odds with the Government's claims to be committed to reducing the burden of red tape for businesses.

The new rate

Against this background it is perhaps easy to understand why in his Pre-Budget Report on 5 December 2005, the Chancellor announced that the starting rate of corporation tax will be increased to 19%. The removal of the 0% rate means that the NCDR and the complicated rules on non-corporate distributions will become redundant.

It is expected that confirmation of this change will be announced in the Spring Budget and that it will apply from 1 April 2006.

What are the implications for you?

The good news is that the simplification of the rules brings a welcome cut in the amount of red tape surrounding corporation tax. The change is certainly less welcome from a tax point of view for those businesses that incorporated just to take advantage of the 0% rate.

However, although this change increases the amount of tax a small company will pay, you should not make a knee-jerk decision to disincorporate. There are many other benefits to running a limited company, and owners of small companies still stand to save tax through incorporation.

Contact us to discuss your particular circumstances.

WORK ISSUES

A smoking policy

The laws on smoking in public places are becoming ever more stringent. The Republic of Ireland implemented a full ban on smoking in workplaces in March 2004, and similar anti-smoking laws look set to be introduced in the UK over the next few years. How might this trend affect your business, and should you implement a new company policy on smoking?

The debate

A key element of the debate is over the harmfulness of passive smoking. Under section 2 of the Health and Safety at Work Act (1974), employers must provide their staff with a healthy and safe working environment. With passive smoking increasingly (if controversially) viewed as contributory to ill-health, there is a real danger that employers could face compensation claims if they allow smoking in the workplace.

Many employers are therefore considering banning smoking altogether. However, before you decide upon this course, you should think carefully about how to proceed.

Introducing restrictions

If you impose a blanket ban on smoking in your workplace overnight, you may end up with some very disgruntled staff. It is wise to conduct a thorough consultation on your business's smoking policy with staff (both smokers and non-smokers), and to have a substantial notice period before introducing restrictions.

If you do not wish to completely alienate the smokers among your staff, or to send them outside the building for their cigarette breaks, one option is to have a designated smoking room. However, even here a balancing act is required. Non-smoking staff can become resentful if it is perceived that smokers are having preferential treatment with longer and more frequent breaks.

State your policy

Make sure that your staff handbook and terms of employment clearly state company policy on breaks and rest periods, as well as any areas where smoking is permitted. If any member of staff contravenes this policy, take disciplinary measures and ensure that you keep a written record of the dates of any warnings given, as this will be vital should a case ever come before an Employment Tribunal.

Finally, if any member of your staff is in the process of trying to stop smoking, be aware that their withdrawal symptoms may make them irritable and contribute to substandard performance for a time. Again, try to be sympathetic, within reason, since any disciplinary measures that don't take these symptoms into account could cause problems if the employee appeals.

It is always best policy to seek professional advice from your legal advisor.

Company Law Reform: reducing the burden on business?

The Company Law Reform Bill was introduced into Parliament on 1 November 2005, and includes proposals aimed at simplifying company law and reducing the burden of red tape for smaller companies, making it easier to set up and develop a business.

It is hoped that the new measures will save businesses an estimated £250m a year, with small companies benefiting by around £100m.

What the proposals mean

'Thinking small first'

Under the proposed reforms, those parts of the law most relevant to private companies will be listed first, rather than being expressed as exceptions to the rules applying to larger public companies. This has the aim of making it easier for small companies to identify the requirements that apply to them.

Improving clarity

The coverage of the Companies House 'plain English' guidance will be increased, making the regulations easier to understand. The legislation will also be supplemented with comprehensive guidance, including a new 'checklist' of the basic company law requirements, and small businesses will be consulted on developing this.

Widening electronic resources

Companies House is planning to develop its web-based resources. During 2007 it will offer web incorporation, and companies will be able to access their details via an online portal.

Key legislative changes

The key legislative changes include the following:

- Proposals to bring forward the deadline for private companies to file their annual reporting documents – currently 10 months after the year-end – are being considered
- Separate model articles of association for private companies, which will contain the minimum key rules on the internal workings of the company, and will be shorter and clearer
- Abolishing the need for private companies to have a company secretary, and to hold an annual general meeting. In addition, written resolutions may be carried with a simple or 75% majority of eligible votes, rather than requiring unanimity. Companies will also be able to make greater use of electronic means for communicating with shareholders
- The provisions on accounts and reports have been restated, to make them easier to understand. Small and medium-sized companies will retain the option to file abbreviated accounts with Companies House
- The rules on providing financial assistance to potential or actual shareholders are being abolished, and it will become easier for private companies to make capital reductions.

The Bill also aims to clarify the duties of directors, and will allow directors to file a service address on the public record.

Further information on the Bill can be found on the UK Parliament website: **www.parliament.uk**

REMINDERS FOR YOUR DIARY

March 2006

31 End of corporation tax financial year
End of CT61 quarterly period
Filing date for Corporation Tax Return Form CT600 for period ended 31 March 2005

April

5 Last day of 2005/06 tax year
Deadline for paying retirement annuity premiums to be carried back to 2004/05 and for 2005/06 ISAs

6 Pensions 'A-Day' – significant changes to the pensions system come into effect

14 Due date for income tax for the CT61 period to 31 March 2006

19/21 Quarter 4 2005/06 PAYE remittance due

20 Interest will begin to accrue on unpaid PAYE/NI for 2005/06

30 Normal annual adjustment for VAT partial exemption calculations (monthly returns)

May

3 Last day for notifying car changes in quarter to 5 April 2006 – P46 (Car)

19 Last day for filing forms P14, P35, P38, and P38A – 2005/06 PAYE returns, without incurring penalties. Also last day for filing contractor's returns, including CIS36

31 Last day to issue 2005/06 P60s to employees

A look ahead to Budget 2006

March is traditionally the month when the Chancellor gives his Budget speech.

It is always difficult to predict what will be announced, but in addition to the removal of the 0% starting rate of corporation tax (see page 3), key measures to look out for might include details of rules for UK Real Estate Investment Trusts (REITs), which allow investment in a spread of properties. In particular, there might be an announcement on the 'conversion charge' which companies must pay to put property into a REIT.

Another area where businesses will be hoping for clarification is income recognition. In certain circumstances, accounting standards now require the sale value of work in progress to be included in revenue. In the Pre-Budget Report, the Chancellor acknowledged that the change – which means that the top and bottom line are increased without any additional cash receipts – is likely to cause serious cashflow problems for some businesses, as a result of the acceleration of tax liability. He announced that legislation will be introduced to allow the tax charge to be spread over three years, with an extension of up to six years for those businesses most severely affected.

One thing that is certain is that the Chancellor is not afraid of creating surprises. In his Pre-Budget Report he announced an intention to prevent tax advantages in holding certain assets, such as residential property, in Self Invested Personal Pension schemes. This removed what had been seen as one of the most important advantages of the new pension rules coming into effect in April 2006, in terms of encouraging people to invest for their retirement.

Make sure you contact us after the Budget for details of how any new announcements might affect you.

Business and personal planning need not be left until the end of the tax year – talk to us now about tax and financial strategies for you and your business.

We are sometimes asked if we are able to help additional clients. We are a growing firm and do appreciate your referrals. We consider it a compliment when you recommend us to your friends and business contacts.

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