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CHARTERED ACCOUNTANTS

BUSINESS


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Is your financial risk strategy up to date?

If the pandemic – and now the Ukraine war – have taught small and medium-sized business owners anything, it is the value of staying agile in changing circumstances. Regular assessment of financial risks, and your strategies to meet them, will help to mitigate their short and long term impact.

Financial risk

Financial risk might best be described as any potential future situation that could cause your business to lose money. A business will have more control over some risks than others, but that doesn't mean risks outside a firm's control, such as energy and fuel prices, can simply be ignored.

For example, if part of your business involves visiting customers, fuel costs might be contained by reorganising service areas to reduce travel time for each journey.

> *Risks are inevitable, but businesses should do their best to be prepared for the unexpected; and the key to this is agility.*

Cash flow

If you focus primarily on sales and profitability your business' overall financial position could get overlooked. However, cash flow is critical; poor cash flow has led to many business failures.

- Prepare regular cash flow statements so that future liquidity issues can be identified early.
- Where there is a lot of uncertainty, this can be built into cash flow projections.
- If customers regularly pay late, you could consider applying a late payment fee.

Conduct more frequent reviews

Weekly – or even daily – cash flow monitoring could be appropriate given current economic conditions. Risks are inevitable, but a business will be better prepared to deal with them if it has a financial risk strategy in place. Since it is impossible to see the future, businesses should do their best to be prepared for the unexpected; and the key to this is agility.

Think about your business as a series of moving parts, not static fixtures and ask questions such as: What else can this asset be used for? Does this expense scale down if revenue falls? Can we quickly scale up if an opportunity presents itself?

PROPERTY

Eviction law set to change

Reform of the private rented sector in England has been on the agenda for some time, but it looks like the end of section 21 evictions might come later this year. Landlords will no longer be able to evict tenants without giving a specific reason.

Most residential tenancies in England are assured shorthold tenancies lasting for a minimum six months. After this initial fixed term period, a landlord can – subject to sufficient notice – currently end the tenancy without giving any reason. Many section 21 evictions are, of course, because of rent arrears. The proposed reform mirrors the system already in place in Scotland.

The alternative

As an alternative, a landlord can evict using section 8 of the Housing Act. Such evictions can happen at any time during a tenancy – including the initial fixed term – but only if a tenant has broken the terms of the tenancy agreement such as rent arrears, unsociable conduct or property damage. This process carries no certainty of regaining possession and can be more expensive.

The reform should include strengthened repossession grounds when a landlord has valid cause.

If the reform is introduced, the average landlord with just two or three properties will need to be more careful than ever about who they take on as tenants. They might consider asking for several months' rent paid upfront or for a guarantor to be provided.

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TAX

Making the most of business disposal reliefs

If you are a company owner planning to sell your business in the future, you can make sure that the chargeable gain on your shares is taxed at 10% rather than 20% – in other words that the disposal qualifies for business asset disposal relief (BADR).

There are several conditions for the relief and one of them has recently been the subject of a decision in the Upper Tribunal. As a result, HMRC has had to rewrite some of its guidance.

Trading companies qualify

A company must be a trading company for its shares to qualify for BADR. A trading company is one whose activities do not include “to a substantial extent, activities other than trading activities”. Previously HMRC defined ‘substantial’ as “more than 20%” of a company’s income, assets, expenses incurred and time spent by its officers and employees on trading and non-trading activities.

The Upper Tribunal rejected such a prescriptive test and the application of a strict numerical threshold. ‘Substantial’ should be “taken to mean of material or real importance in the context of the activities of the company as a whole”. One must look at the nature of the company’s activities and consider how best to measure their extent. The test is both qualitative and quantitative.

The Tribunal decision may create some uncertainty where companies have some non-trading activities. Business owners may prefer to keep any significant non-trading activities separate from their trading company.

If you do not intend to dispose of your business, your heirs will want its value to qualify for business relief for inheritance tax, given at 100% for unlisted company shares or a business or interest in a business. Businesses that consist wholly or mainly of dealing in securities, stocks or shares, land or buildings or making or holding investments are excluded. If there is a mixture of activities, there is no single test for determining whether its activities are ‘wholly or mainly’ excluded. As with BADR, careful advance planning should avoid any unpleasant surprises.

BUSINESS

Managing employment costs

The National Minimum Wage and Living Wage increased from April, alongside the rise in national insurance contributions (NICs). Employers need to plan for the changes.

National Living Wage

The hourly rate of National Living Wage that must be paid to workers aged 23 and over has gone up to £9.50; a 6.6% increase, equating to extra annual salary of at least £1,000.

The minimum rate going up nearly in line with the expected rate of inflation puts pressure on employers to match this when it comes to settlements higher up the salary scale. Small and medium-sized businesses in particular could find the higher rates of minimum pay a strain on their finances.

National insurance contributions

Higher paid employees will see a big drop in their take-home pay from April following the 1.25% increase to the rate of NICs, even though the starting threshold is going up. For example, someone earning £100,000 annually will have take-home pay of nearly £91 less in April compared with March, but an increase of nearly £32 in July compared with June. July is when the starting threshold will see another, more substantial, raise to match the personal allowance at £12,570.

- Employers will also see a broadly similar increase in what they have to pay (with no reduction from July). It will be expensive if there is a team of highly paid personnel unless costs can be passed on to clients.
- Make sure additional costs are reflected in financial projections.

Salary sacrifice

The higher rates of NIC make salary sacrifice arrangements more attractive than ever, especially regarding employer pension contributions. A company car salary sacrifice arrangement also works well for full electric and certain hybrids.

Salary sacrifice will not, however, suit everyone. Employees need to be aware that a lower base salary will normally mean a lower level of potential mortgage borrowing — a real problem given current property prices.

TAX

VAT claims on electric cars

New rules apply for claiming VAT on electricity used for charging vehicles.

If an employee charges a vehicle at a public charging point, the supply of electricity is made to the employer, who can then recover the VAT on the cost, just as where the employee charges the car at work. Sole proprietors and partners in a business partnership can also recover VAT when they charge vehicles at home. In all cases, only the VAT relating to business use of the vehicle can be claimed, calculated by reference to mileage records.

However if an employee charges a vehicle at home, the supply of electricity is made to the employee not the employer. The employer therefore cannot recover the VAT. HMRC is reviewing what evidence could be provided to allow employers to claim the VAT where an employee is reimbursed for the cost of charging vehicles at home for business purposes.