

Business Matters

News & Information from **Hammonds** Chartered Accountants and Business Advisers

Autumn 2004



Hammonds

Chartered Accountants and Business Advisers

The value of an audit to your business

With the audit thresholds now raised from £1 million to £5.6 million for financial years ending on or after 30 March 2004, you may be wondering whether your company should dispense with the audit.

However, although the change is of course welcome for many businesses, the 'cost/benefit analysis' does merit some careful consideration, as audits do have benefits that can outweigh any savings made.

Some examples of these include:

• Additional credibility

Where there are a number of shareholders who do not work directly in the business, an audit adds credibility to information provided to them in the financial accounts. This also applies to customers and suppliers who may be looking at these statements as well.

• Reassurance and reliability

While an audit is not a guarantee that the accounts are free from fraud or error, audits can, and do, detect and deter material fraud or error in the accounts.

• Attracting investors

An audit makes it easier for a business to attract outside investors or a buyer as it reduces the amount of work that they need to do to satisfy themselves that they are making a sound investment. The regular performance of an audit and publication of an unqualified audit report for a number of years prior to a sale provides additional reassurance to a purchaser.

• Easier bank finance

Banks may include the requirement for a company to be subject to an audit, irrespective of size, as a condition of lending money to it. The fact that a company may already be subject to an audit can reduce the cost of borrowing. Some companies could find themselves in breach of existing covenants by automatically dispensing with an audit.

• Peace of mind

There is no clear evidence that the absence of an audit increases the likelihood of a company being the subject of a tax investigation. However, the introduction of the Corporation Tax Self Assessment regime has transferred the responsibility for correctly calculating the tax liabilities to the company. Mistakes and errors in the accounts themselves can lead to an accumulation of unpaid tax, interest and penalties. An audit helps to reduce the incidence of such costly errors.

• Uncovering opportunities for improvement

Work undertaken by us as auditors involves an assessment of the accounting and internal control systems. It is normal practice for auditors to report to the directors on any perceived weaknesses and recommend improvements.

So even if your business now falls below the compulsory audit threshold, be wary of making any hasty decisions to discard an audit. The costs of dispensing with this service could far outweigh any short-term savings.

Burnhill Business Centre
Provident House
Burrell Row
Beckenham
Kent BR3 1AT

Telephone 020 8249 6328
Fax 020 8249 6329

Email info@hammondsaccountants.co.uk

www.hammondsaccountants.co.uk

Geoff Miles FCA

Consultants:

Glen Vaughan ATT CTA
Sandy Kinnear FCA FTII

Registered to carry on audit work
by The Institute of Chartered
Accountants in England
and Wales

IN THIS ISSUE

The PAYE puzzle



A wealth management plan



Disability discrimination



Five essential ingredients of
your business plan



Taking the stress out of VAT

The PAYE puzzle

Pay As You Earn is the Inland Revenue's system to ensure that as many people as possible pay the right amount of tax by deduction from their salaries and pensions each year. But for many, PAYE remains something of a mystery.

A PAYE code goes up when you have more than the standard allowances – for example, you might be paying into a personal or group pension scheme – and goes down when the Revenue are collecting unpaid tax from an earlier year, or tax on this year's company car benefit.

How does it work?

Suppose you are an employee. Your code will start with your personal allowance – usually £4,745, but increasing to £6,830 or £6,950 for many older clients. The code is used by your employer to calculate the amount of tax to deduct each month, and a code of 599, which rounds to £6,000 of tax-free pay for the year, means that the first £500 of your income each month will be paid free of tax. Your employer then uses Tax Tables (or software) to work out the tax at 10%, 22% and/or 40% to deduct from your salary in excess of the month's tax-free figure.

PAYE is a cumulative system, which allows for fluctuations in your income over the year. Essentially, by setting your PAYE code at the right level, the Revenue can rely on your employer to deduct the tax due from your year's salary.

New uses for PAYE

Recently, the Revenue have used the PAYE code to reduce the amount of tax people have to pay over and above tax deducted at source. To put it another way, they have improved their cash flow.

If you have rental income, or a substantial investment income (taxed at source, usually at 20%, but potentially taxable at 40%) you would expect to include the income in your self-assessment and pay the tax over to the Revenue in the usual three-payment cycle:

- **First payment on account**
31 January in the tax year (so 2004/05 = 31 January 2005)
- **Second payment on account**
31 July after the tax year (so 2004/05 = 31 July 2005)
- **Any balance**
31 January after the year (so 2004/05 = 31 January 2006)

However, the Revenue are increasingly making adjustments to PAYE codes. This is ostensibly to make tax simpler for taxpayers,

but it has the effect of ensuring that tax is collected sooner. So in circumstances like those mentioned above, tax due for 2004/05 would be collected by making a minus adjustment to your PAYE code, and therefore increasing the amount of tax you pay each month. So the tax is instead paid by monthly instalments between April 2004 and March 2005.

Where there is a balance of tax due at the end of the year, the system can sometimes work to your advantage. If the balance is less than £2,000 and you submit your Tax Return by 30 September, you can opt to have this amount collected through PAYE in the following tax year.

This means that a 2004/05 underpayment will be collected by monthly instalments between April 2006 and March 2007, rather than as a single payment on 31 January 2006. This also eliminates payments on account in 2006.

Is there a limit on the extra PAYE tax I can pay?

If you are an employee, the Inland Revenue can use what are called 'K' codes to instruct your employer to deduct up to 50% of your salary or pension in tax. After NICs, that might mean that you are left with less than half your gross salary!

Can I stop them from doing this?

It is likely that if you have a tax liability of up to £3,000 over and above the tax you pay through deduction at source, the Revenue will try to make a coding adjustment to collect it this year or next. You have the right to ask them not to collect your tax this way, but it cannot be guaranteed that an Inspector will be willing to remove an adjustment once made.

The Revenue are duty bound to tell employees and employers (or pension payers) when a PAYE code changes, but although they are supposed to tell us too, documents can go astray. So it is important that you send copies of PAYE code notices to us. We will be able to spot when tax is being collected on other income and, if you agree, ask for the adjustment to be removed. We can also correct any errors before the end of the year.

Send copies of PAYE code notices to us as soon as they are received, so we can make PAYE as painless an experience for you as possible.

Business Legislation Watch Disability Discrimination Regulations

What are the regulations?

The final stage of the Disability Discrimination Act 1995 (Amendment) Regulations, covering the issue of physical access and employment for disabled persons. The regulations come into force on 1 October 2004.

What do they cover?

The duty of all service providers to make 'reasonable adjustments' to their premises so that disabled people do not face barriers to access, and the new obligation for employers with fewer than 15 staff to ensure fair treatment of disabled workers.

What do they mean for your business?

- Anyone who provides a service to the public or a section of the public will need to make 'reasonable adjustments' to their full range of physical features, such as kerbs, steps, doors and toilet facilities.

- Small businesses, which have previously been excluded from the Disability Discrimination Act, will have to comply with the legislation, and must ensure that they don't discriminate against a disabled person at any stage of the employment process, from recruitment to promotion and dismissal.

Action to take

In addition to reviewing your employment policies to ensure there is no discrimination, you must make sure that your business premises are accessible to people with disabilities. You should take into account all aspects of your business premises, both inside and outside. Draw up an access plan to allow time to implement any necessary refurbishment. It may be advisable to arrange for a professional access audit.

**For more information on the new obligations for businesses, visit www.drc.org.uk/open4all
Further guidance on the Disability Discrimination Act 1995 is available at: www.disability.gov.uk/dda**

Preserve your peace of mind ... with a wealth management plan

Failing to plan, whether for income or capital taxes, education costs or retirement, tends to create unpleasant surprises. A neglected succession strategy or insufficient insurance can seriously damage your wealth.

That's why it doesn't pay to avoid confronting such financial challenges until they arise. Instead, you should establish and review an overall wealth management plan, to minimise the occurrence of unexpected costs. Besides tax planning, here are some other critical elements of an overall wealth management plan:

Succession planning

All business owners should have a strategy to sell their business or to pass their business interests on within their family. If no action is taken, taxes can dramatically diminish the value when the owner dies – perhaps even forcing the family to sell the business. Integrating an exit strategy into your estate plan is essential to protect your assets and your company's ongoing success. We can assist you in reviewing or developing your plans in this important area.

Investing

While tax efficiency may be a key factor when investing in a pension or an ISA, there are many other issues that influence a strategy to make your money work as hard as you do. These will include establishing your investment horizon, finding a comfortable risk level, and marshalling your assets among stocks and shares, unit trusts, bonds, cash and cash equivalents, property, life insurance, and other investments.

Protecting assets

Being prepared to shield your assets is more important than ever before, and the key is to execute plans before claims arise. Potential strategies to discuss with us include transferring assets to your spouse, the use of trusts and even your retirement plan.

Life insurance

Life insurance takes many forms - including term, whole life and mortgage protection, as well as serious illness and disability insurance. Along with protecting your family's financial future, a well-conceived life insurance policy can provide liquidity to pay inheritance tax, equalise estates passing to children who are not involved in a family business, and efficiently pass funds on to succeeding generations.

Wealth management is not something you can afford to ignore or put off until tomorrow. Call us if you would like advice and assistance.



What's the Plan? Five essential ingredients of your business plan

It is not only start-ups and large companies that need business plans. Every business needs a 'blueprint' – not just for the benefit of potential investors, but so that the people who work in it can have a clear idea of its direction, and can commit to its future.

A good business plan serves various functions, but it must have a practical structure. Here are five essential ingredients:

1 A business description and mission statement

Every business needs a clear declaration of why it exists, and a basic description of how it intends to meet its primary objective.

It need only be a few sentences, and might be something like 'Our company aims to provide outstanding solutions and service to the x industry in and around the area of y'. Think of your mission statement as the heart of your business plan. All your goals and activities should flow from it.

Having prepared your mission statement, you next need to comprehensively describe your company. Provide a brief history and then explain what it does, identify the marketplace niche it fills, and assert why you and the business will succeed. You may also wish to reveal why your business chose its location and show how you are benefitting the local community.

2 A management profile

Potential investors, lenders and even employees are not interested in a faceless corporate entity. They need to know that competent, experienced people are steering the ship.

Provide an outline of your organisational structure and management team, giving solid reasons why your staff are competent to succeed. A chart illustrating the roles and relationships of key employees can work particularly well.

3 A financial portrait and strategy

Prospective investors and lenders need a good idea of the financial aspects of your business. Include basic data such as current and projected balance sheets, a profit and loss account and an analysis of cash flow. If you are a start-up, project this information as accurately as possible. It is important not to cut corners with these calculations. Do ask for our assistance with this.

Above all, make sure your numbers demonstrate that you and your management team have considered the key 'drivers' that will determine your success or failure. Don't fill the business plan with overly optimistic financial projections that could ultimately depict your company in a bad light.

4 Sales and marketing objectives

Expertise and past success mean little without an up-to-date strategy for bringing your products or services to market. Describe your intended market, giving specific details of its size and how much of it you mean to serve. What is your market's growth potential? What specific geographic and economic factors play a role?

List your five largest competitors and explain how you can serve your market better than these rivals. Do not conceal your weaknesses: recognising the challenges you must overcome shows that you are realistic.

5 An executive summary

A concise, readable overview may be necessary to get your 'foot in the door' with many potential lenders. An executive summary should show the highlights of each section of the business plan, providing a clear synopsis of who you are, what you do and where you're heading.

An ongoing process

Like keeping a 'To Do' list, writing a business plan is an ongoing process. Yours must adapt to changes in your company, its market and the economy – and that means regular reviewing and updating.

For help with developing a business plan or improving an existing one, do please call us.

Taking the stress out of VAT

How would you like to be able to simplify your VAT accounting procedure into a single calculation? And how about paying regular set amounts, and only having to prepare one simple VAT Return each year?

That may sound too good to be true, but help could be at hand in the form of the VAT Flat Rate Scheme (FRS). This allows eligible businesses to calculate their net VAT liability as a flat rate percentage of their total turnover.

How it works

Tax invoices are issued to registered customers in the normal way, using the standard VAT rate of 17.5% (*not* the trade sector percentage) where appropriate. The VAT liability is calculated by taking the total quarterly turnover (including VAT), and multiplying it by the trade sector

percentage, which will lie within the range of 2% to 13.5%. Because the flat rates are an average, some businesses will pay less on the scheme and some pay more.

You can find your rates and much more information on the Customs and Excise website at www.hmce.gov.uk.

Incentives

As a special incentive, if you join FRS when you first register for VAT, you can take 1% off the published flat rates until your first anniversary of registering for VAT.

Under FRS, you cannot normally claim tax paid on purchases, as this is taken into account in setting the trade sector percentages. However, input tax can be specifically reclaimed on single capital assets costing £2,000 or more (including VAT).

Cash accounting

The FRS has its own form of Cash Accounting, as the quarterly turnover can be on the basis of either invoices issued or cash received. To enhance the simplicity even further it can be used in conjunction with the Annual Accounting Scheme. This allows predetermined payments to be made by 3 or 9 interim instalments. Any balance is payable when the return is due, two months after the end of your annual accounting year.

Are you eligible?

You can apply to join the FRS if you expect that your taxable turnover in the next 12 months will not be more than £150,000 (total turnover not more than £187,500). Once you are in the scheme, there is a tolerance, allowing you to remain in provided your total VAT – inclusive turnover for the year just gone does not exceed £225,000.

If your turnover is too high for the FRS, you may still be eligible for Annual Accounting and Cash Accounting if it is below £660,000 (exit tolerance level £825,000).

Talk to us if you think you could benefit from the Flat Rate Scheme. We might be able to help you take the stress out of VAT.

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.



WEB WATCH ESSENTIAL SITES FOR BUSINESS OWNERS

Age Positive www.agepositive.gov.uk

Information and advice on recruiting, training and retaining a mixed-age workforce.

Intellectual Property www.the-key.biz

New website, managed by the Patent Office, offering information to businesses on protecting their valuable intellectual assets.

Chip and PIN www.chipandpin.co.uk

Information for businesses and consumers on the new Chip and PIN credit card system.

Enterprise Insight www.starttalkingideas.org

Encouraging young entrepreneurs to develop their business ideas.

REMINDERS FOR YOUR DIARY

September 2004

- 30** Deadline for submission of the 2004 Tax Return if you wish the Inland Revenue to calculate the tax or, if you are an employee, you wish to have a 2003/04 balancing payment of less than £2,000 collected through your 2005/06 PAYE code
End of CT61 quarterly period

October

- 1** Due date for payment of Corporation Tax for period ended 31 December 2003
5 Individuals/trustees must notify the Revenue of new sources of income/chargeability in 2003/04 if a Tax Return has not been received
14 Due date for income tax for the CT61 quarter to 30 September 2004
19/22* Quarter 2 2004/05 PAYE remittance due

November

- 1** Please ensure you are retaining your documents for the 2005 Tax Return.
2 Last day for notifying car changes in quarter to 5 October – P46 (Car)
30 Extended deadline for submission of Form 42 (transactions in shares and securities) if a form was not received from the Inland Revenue

* With effect from 6 April 2004, all employers with more than 250 employees must make their payments of PAYE Tax and NICs electronically, by either BACS or CHAPS. Payments previously due by the 19th must now be clear by the 22nd, but if the 22nd falls on a weekend or bank holiday, payment must clear by the last preceding working day.