




SPECTRUM ISSUE: 9 | APRIL 2010

# spectrum

THE NEWSLETTER FROM RITSON SMITH



The answer  
is blowing  
in the wind

Increasing revenue from farmland the green way



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## Introduction



**The waiting is over and as this edition of Spectrum lands on your desk we will be coming to terms with a new Government and the effect it may have upon us. Challenging times lie ahead for any new Government and certain commentators are asking if this is an election you really want to win. The Chancellor in his last budget of this Parliament played a fairly straight bat on March 24, but there remains a real concern that there will be an increase in either or both VAT and Capital Gains Tax in the inevitable post election budget.**

There was some good news in the budget for small business owners in the form of the doubling of the Annual Investment Allowance (AIA) for expenditure on plant and machinery from £50,000 to £100,000, and the doubling of the lifetime limit for Entrepreneurs' relief from £1million to £2million. What did not receive much publicity was the fact that the special 40% FYA, which was only introduced last year, came to an end on April 1 2010 which is to the detriment of larger companies or those with greater capital expenditure.

There is still uncertainty about obtaining credit from banks and, although they are stating that they are "open for business", the focus of the banks' lending decisions is increasingly on those businesses that are able to clearly demonstrate a strong case for accessing debt facilities. These will be businesses that have a strong management team that know and understand the fundamentals of their business, the market in which it operates and can provide robust management information. The perception may have been that this tightening of credit decisions may have gone too far, but there are early signs that a more balanced view is returning with a return to a more traditional and prudent approach to lending.

The challenge facing us as business advisers is to work with both clients and banks to ensure the correct level and quality of information is shared both ways; educating banks and clients in order that the correct lending decisions are made. What was possible, and perhaps the norm, two years or 18 months ago should no longer be considered usual today and we must recognise and adapt to that change.

I hope you find something of interest within this edition of Spectrum. We are always trying to improve our communications with clients and would be pleased to hear from you with any specific questions you may have.

**Niall Farquharson** Managing Partner

# Demise of the personal touch

HM Revenue & Customs are making changes to the way that they carry out enquiries, or 'checks' as they are now known.

For corporation tax and income tax where they are checking all of a tax return, they are likely to carry out a cross tax check, i.e., consider other taxes at the same time. Any check will look at the corporation tax or income tax return, the PAYE and National Insurance position as well as the VAT returns.

This will have obvious resource and cost implications for the taxpayer in terms of dealing with the enquiry and involving their advisors but will reduce the requirement for multiple visits looking at different taxes.

It has also become apparent that there is a more regimented approach to enquiry or check work. Newly introduced rules mean that HMRC will be less flexible when looking at reducing any penalties that are based on the tax involved where an error is identified. Previously reductions were available for the level of disclosure, co-operation, and seriousness and there was more scope to negotiate.

In the event of an enquiry or check, Inspectors or Officers will be adopting a more formal approach, and the days of individually

penned letters may well be over. Any requests for information will follow a more regulated format. It will be interesting to see if this results in a significant increase in the type and level of information and documents required as the more individual approach is phased out.

Inspectors or Officers are likely to have less discretion compared to how some may have operated in the past. This would appear to be an attempt to ensure that any agreement reflects departmental policy and is consistent regardless of the Inspector who deals with your case.

The result of this is that officials will be less likely to negotiate. Prepare yourself - old style enquiries may well be a thing of the past.



**If you have any concerns about how this may affect your business then please get in touch for advice.**

**Dave Smith** Tax Manager

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# TIS rules prove taxing



David Dowell - Senior Manager, Corporate Tax

Tax legislation isn't exactly child's play. The anti-avoidance legislation on transactions in securities (TIS) is an example of that despite the HMRC's best efforts to explain it. With an eye on the proposed changes recently intimated in the 2010 Budget, Ritson Smith's tax specialist, David Dowell makes an attempt to initiate the un-initiated.

The current Transactions in Securities (TIS) anti-avoidance legislation seeks to prevent taxpayers converting income into capital therefore creating a tax advantage. It is topical in light both of the increase in the higher rate of income tax to 50% from April 6 2010 compared to a historically low Capital Gains Tax (CGT) rate of 18%, and the Government's announced intention to replace the existing legislation affecting transactions where a tax advantage is obtained on/after March 24 2010.

Like many anti-avoidance provisions, the rules have sometimes caught innocent transactions as well as those they were intended to forestall - it will be interesting to see if the new provisions avoid this. Clearly, someone expecting a tax bill of 18%, and perhaps 10% if Entrepreneurs' Relief is available, would not be pleased if HMRC demanded 50% from them!

## The existing TIS rules apply where there is:

- A transaction in securities (including share sales):
- The taxpayer obtains a 'tax advantage' (i.e. where potential income has been converted to capital or income tax has been avoided or reduced):
- The tax advantage arises as a result of the transaction falling within a 'prescribed circumstance' - for owner-managers this will generally be 'unacceptable' or Circumstance D transactions.

If the above features are present, HMRC will issue a counteraction notice. Generally speaking, there should be little to worry about under current legislation on a simple sale of shares for cash to a third party. Potential problems can arise however, where either in addition to cash there is a debt or loan note in the purchase consideration or a connected party purchaser is involved.

Care also needs taking when a company buy-back of shares is involved or one company has been liquidated with the majority shareholder continuing the trade in a new company. Finally, secondary buy-out transactions involving newcos and the replacement of existing venture capitalists with new investors can be affected by the current provisions.

The existing legislation does offer an important escape clause - counteraction notices are not issued where it can be shown the transaction was motivated by genuine commercial reasons and not entered into for tax avoidance.

While, disappointingly, drafts of the proposed new legislation have not yet been published, it is understood the new legislation will apply only to close



## Keeping it in the family

**Figures suggest that about three quarters of all businesses within the UK are family businesses and they employ around half the entire workforce. Disturbingly, however, relatively few survive longer term – with only one in eight getting through to the third generation.**

Family businesses possess a number of characteristics that set them apart from other business models. Perhaps the most obvious of these is that there is a need to balance the interests of the family with those of the business.

With the recent economic difficulties so many businesses have been facing there has been an underlying need for management to be prepared to change and adapt. Within the family business this introduces an added difficulty because many family members depend on the status-quo for psychological comfort – even if the status-quo is not healthy. However, one of the many competitive advantages of the family business is the ability to make decisions quickly because access to the business leader is easier.

There is a need to ensure that the company's business plans are integrated with the family's plans for leadership and ownership, and both of these must be aligned with the family's personal financial plans and their estate planning. If this isn't happening, then it is time to seek professional assistance.


In most businesses, owners or investors can come and go based on financial expectations. Within the family business it is not uncommon to find that it is the continued support of family members who are not involved in the business that is often critical to continuity. These family members may have a large financial and emotional stake in the business. It is important to recognise their role in both the governance as well as business strategy.

One of the peculiar anomalies of the family business is that they are often not driven by profit alone. This is generally because they do not have plans to "cash out" by selling the business after several years. Preserving the business for the long term can appear more important than current economic reality.

I am not suggesting that these characteristics are applicable to every family business – rather they provide an insight into why the factors facing family businesses are different.

It is by developing this greater understanding of the elements which are unique to these companies that has ensured Ritson Smith has become a leading provider of advice and support to the family business sector.

**Ewen Alexander** Partner



companies (including both UK and overseas companies), will clarify how the tax advantage should be quantified and include a new income tax advantage test. The new legislation will also introduce a new exemption to cover fundamental changes in ownership and remove obsolete tests where tax advantages are no longer considered to arise.

Clearly, the concept of tax avoidance is a nebulous area which is why we recommend that clients entering into the situations described contact HMRC for advance clearance – at the very least until the new legislation is published.

Not seeking advance clearance exposes the taxpayer to uncertainty over a lengthy period, remembering the reduced discovery assessment time limit of four years does not apply to TIS counteraction assessments which retain a six year time limit.

Clearly, the message is that if in doubt about the tax efficacy of a particular transaction, especially given the new anti-avoidance legislation to be issued in this regard, speak to your tax advisor as a matter of urgency.

# Funding is out there but is your business ready for investor scrutiny?



Graham Alexander - Partner, Corporate Finance

The slow recovery from the global economic downturn and the ongoing lack of debt funding and liquidity means that companies are continuing to find accessing funding for the development and growth of business opportunities extremely challenging.

Having your business well prepared for investment is therefore key for all businesses who wish to secure the equity funding that is available.

Investors, both institutional and private, are likely to have a variety of possible investment opportunities to consider at any one time and differentiating your business or opportunity is vitally important to attract investment with the desired terms and structure.

### Three fundamental areas to focus on as part of this preparation include:

- Management team
- Business model
- Intellectual Property (IP)

The strength and experience of the management team underpins the quality of any opportunity. The challenge is to assess whether the team includes the requisite technical, commercial, and financial skills combined with experience and strategic leadership.

Enthusiasm for the opportunity is key. Management teams who are very clearly excited by their business or technology can often make an impact on prospective investors.

Sometimes, young companies won't have given enough thought to what their business model is and how they do business. Are

they operating in the most efficient way? Is their model suited to attracting investment and delivering the best returns? Time should be taken pre the fundraising process to consider the current structure, to challenge whether there are alternatives and to consider what structure is best suited to attracting investment.

In technology based businesses, which are prevalent in the oil and gas industry, Intellectual Property is, often, the key differentiator and where investors can see real value. Companies need to ensure their IP is well understood and thought through and, most importantly, protected - ideally via formal and registered patents rather than well guarded and confidential "know how" which can be difficult to 'sell on'. Companies need to assess what competing IP is out there and how this compares with their own.

Taking time to assess what the current position is in each of the above areas *before* commencing a fund raising process allows businesses to consider what steps can be taken to address any deficiencies, and only then should opportunities be presented to potential funders with the aim of accessing funds on the most advantageous terms possible.

**Graham Alexander**  
Partner, Corporate Finance



# Client profile: St John's Wells Windfarm

**For the Sleigh family the answer to increasing revenue from their Aberdeenshire farm was, quite simply, 'blowing in the wind'. The Sleigh family have farmed the land at St John's Wells, Fyvie, for four generations since 1903. In addition to arable farming, the family have beef cattle, pure bred Suffolk sheep, a commercial flock and over 40 Shetland ponies which they breed and export all over the world for showing purposes.**

It was about five years ago as farming revenues decreased and the outlook was uncertain that the Sleighs began to think about diversification.

"We have an ideal site here for a wind farm. It's a large area with good exposure to the elements," explained John Sleigh. "We are not only investing in our own families' future but we are producing clean energy for local use."

The brothers experienced little in the way of objections to proposals for the £3 million investment in three 80 metre turbines which will be in situ for the next 20 years. The energy is sold to Good Energy in Bristol, the only UK electricity company whose fuel mix is 100% renewable coming from wind, water, and sunlight.

Recently, St John's Wells has joined forces with another four Aberdeenshire farms to provide energy to Good Energy for a ten year term. "It's going well," said John Sleigh. "We hope to get a reasonable return on our investment and are delighted to be involved in this exciting and developing market."

John Laing, Partner of Ritson Smith, has supported the Sleigh family business since 1992. For both farmer and professional advisor, the move into renewable energy has been a learning curve: "This was a substantial investment for the Sleigh Family," commented John Laing. "It was important to ensure that existing farm assets were protected and financial risk to the family was limited to an affordable capital contribution.

We assisted the family from the outset with preparation of projections, advice on the correct financial and taxation structure for the venture, advice on currency exposure during the development stage and negotiation and agreement of banking facilities.

"The wind turbines have been fully operational for some months now and it is pleasing to note that the business is on course to meet our projections."



One of the St John's Wells Wind Farm turbines under construction

## News in brief

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### Avoiding the 50%

**If your annual income is above £150,000, the tax year April 6 2010 to April 5 2011 will see the new 50% rate of income tax increasing your tax liability and, unless prompt action is taken, the costs could be considerable.**

Even where your income is between £100,000 and £115,000 you could be liable to an effective tax rate of over 60% on the income above £100,000 as a result of the withdrawal of personal allowances.

Combined with increasing National Insurance costs for employees and employers, now would be a good time to look at where your income comes from and consider whether any changes to your current arrangements could lead to smaller tax bills.

Visit [www.ritson-smith.com](http://www.ritson-smith.com) (News section) for tips of how to minimise the effect of the 50% tax rate and other tax increases.

### Late payers penalised

**HMRC have introduced a new and more severe penalty regime for late payments of PAYE and NI which will apply to all payments due for the 2010/11 tax year. If you have previously delayed payment for cash flow or other reasons, then be aware of the cost implication.**

For monthly or quarterly payments, no penalty will be charged for the first late payment in a year as long as it is paid within six months of the due date. For the second and subsequent late payment a tax geared penalty of between 1% and 10% of the amounts paid late will be applied, depending on the number of tardy payments and the lateness of the payment.

For annual or occasional payments the tax geared penalty will be from 5% and 15% of the relevant amount, again dependant upon the degree of lateness.

HMRC will generally send out their penalty notification after the end of the tax year which means that you could face a hefty bill next Spring or Summer if you have accrued late payments.

As always, inability to fund a payment is not an acceptable excuse. While the Business Payment Support Service can agree payment plans for all taxes, there is evidence that they are adopting a tougher approach.

Proactive action to contact HMRC is usually advisable to avoid enforcement action through the court, and we can assist in negotiating if needed.