IN BUSINESS

The Moore and Smalley magazine for owner managed businesses

'WHAT IF?'

RICHARD HALL EXAMINES THE BENEFITS OF FINANCIAL FORECASTING

SHAREHOLDER AGREEMENTS
CLIENT PROFILE: HAWKSHEAD RELISH
FINDING FINANCE TRUSTS BUSINESS STRATEGY IN A LOW CARBON ECONOMY
MOORE AND SMALLEY IN THE NEWS

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ISSUED IN AUTUMN 2010

MOORE SMALLEY
CHARTERED ACCOUNTANTS AND BUSINESS ADVISORS

Welcome

Welcome to the Autumn 2010 issue of In Business. With the first half of 2010 behind us, the big question is: 'what can we expect for the next six months?' Business owners may be worried about how the government's emergency budget measures will impact the region. Although there are signs of recovery and some opportunities available, businesses have to remain realistic and lean to ensure they maintain a competitive position in their sector.

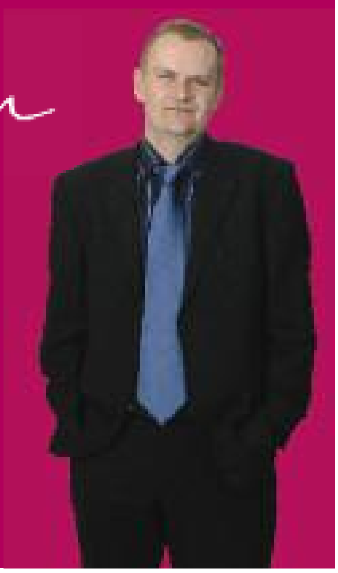
The Federation of Small Businesses (FSB) have recently released figures showing a quarter of small firms say they have 'little or no confidence' in being able to access the funding they need to grow. In this issue, Stewart Case addresses this concern and looks at some of the different funding options available to SMEs.

Richard Hall discusses forecasting and the importance of asking yourself 'what if?' in a variety of business scenarios. We also provide an overview of trusts and the benefits of using them, and examine the benefits of shareholder agreements. I would also like to say thank you to our clients Hawkshead Relish and GB Energy for their contributions to this issue.

I hope you enjoy reading this issue of In Business.

J. Treadwell

James Treadwell
Partner



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Shareholder agreements

Shareholders agreement are vital to protect the surviving shareholders and the family of the deceased

While it is an emotive subject, failure to have a shareholders agreement on death could have disastrous consequences for the surviving business owners, and indeed the deceased shareholder's family.

On the death of a shareholder their shares in the company would form part of their estate and be passed to the beneficiaries of their Will (usually family).

Without a shareholder agreement those shares may be retained by the deceased's family members who have little interest in (or ability to contribute to) the business, or potentially the shares could be sold to a third party. This can have serious implications especially if the majority shareholder dies.

It is important for owners and managers to have a shareholder agreement on death. The most commonly used is the 'cross option agreement'. This simply states that if a shareholder dies the surviving shareholders have the option to buy and the deceased's estate has the option to sell the shares within a certain time. Should either party exercise their option then the other has to comply.

The value of the shares is included within the agreement - either as a fixed amount (which should be regularly reviewed) or based on the value of the company at death.

The benefits of this are readily apparent – control of the business is retained by the surviving shareholders and the deceased's family receive 'fair value' for the shares being given up.

Should a shareholder die, the surviving shareholders will need the cash to purchase the shares. This could be funded from cash or bank lending, but a more cost effective option is for the shareholders to establish protection policies.

We have worked with our clients to ensure that they are aware of the financial impact of not having suitable shareholder agreements in place, but there are still too many businesses who overlook such an important provision. It can be a depressing topic but the consequences of failing to protect the business can be much gloomier.

Mark and Maria relish success

A Cumbrian food business born amid the turmoil of the foot and mouth crisis in 2001 has blossomed into a multi-award winning company serving global markets.

Hawkshead Relish, owned and managed by Mark and Maria Whitehead, has won 42 Great Taste Awards – the Oscars of the food sector – and been named Speciality Producer of the Year, the industry's most coveted accolade.

The company - which literally started life as a pot boiling venture – has also garnered widespread acclaim for its enterprising success, including the Cumbria UK Trade and Investment Award for Export in 2010, Cumbria Chamber of Commerce's Entrepreneur of the Year Award in 2009 and a nomination for the finals of the Manufacturer magazine's SME of the Year Award last year.

Not a couple to rest on their laurels, Mark and Maria are currently in the running for more high profile recognition.

Their success is driven by a range of 120 hand-made products whose star performers are raspberry and vanilla jam, beetroot & horseradish chutney, and red onion marmalade with pine nuts and balsamic vinegar.

Mark and Maria employ 18 staff at their production unit on the shore of Esthwaite Water, which produces 2,000 jars a day, as well as at their shop in Hawkshead, where visitors can sample jams and chutneys from a range of more than 120 products.

Times were not always this good for Mark and Maria, who have lived in the Lake District for 30 years. “We were running a small but busy café in Hawkshead – which we have since converted into the shop – and would use local ingredients and make our own condiments,” explained Maria. “This was always intended as a sideline and we didn't consider it to be a business in its own right.”

That was until 2001 when the foot and mouth epidemic struck. Visitors were told to stay away from rural areas and Mark and Maria were faced with substantial mortgage repayments and no income.

‘When the foot and mouth epidemic struck in 2001 visitors where told to stay away from rural areas’

Mark Whitehead, owner of award winning firm Hawkshead Relish

“We hatched a plan to take our condiments out to the wider public and two weeks later we had a small range of products that we trialled in local delis and shops,” said Maria. “Thankfully, they were well-received and the brand was born. Before long we doubled capacity and so it grew, through sheer determination, grit and ploughing every penny back into the business.”

The couple's entrepreneurial flair and perseverance has paid off as a result of constantly developing their product to suit changes in customer tastes.

“There is a huge amount of passion that goes into the company and this comes through not only in the products, but in the way we do business,” added Maria.

Find out more about the Hawkshead Relish Company at www.hawksheadrelish.com

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What if?

"What If?" is a question that we get asked a great deal.

The forecasting process enables you to look ahead and consider the impact of various business decisions before making any commitment, such as:

What would be the effect on my business if I...

- Recruited more people?
- Opened another branch?
- Expanded into new markets?
- Increased my marketing spend?
- Undertook a programme of capital expenditure?

Scenario planning allows you to prepare for situations where you have no control over the variables. For example what would happen if...

- A competitor cut their prices by four per cent?
- A supplier increased their costs by six per cent?
- Exchange rates changed?
- Customers or suppliers change their payment terms?

You can set the target that you would like your business to achieve, for instance sales value, debtor days, stock turnover and gross profit percentage. You can explore the various resource scenarios you will need to have in place to attain these targets and demonstrate the financial effect.

The financing requirement of the business can be ascertained or the effects of potential changes in financing can be modelled, such as variations to an overdraft facility, taking on new loans, invoice financing and trade finance.

It is important that an integrated profit and loss account, balance sheet and cash flow are prepared when forecasting so that the whole financial picture can be considered.

The two case studies associated with this article show how powerful business financial forecasting can be for external funding purposes and as an ongoing internal management tool – answering those "What If?" scenarios.

Case Study 1

Scenario

A business was expanding rapidly into a new market and part of the expansion required an increase in stock shipments from overseas. The timing of the increase in shipments and the funding gap needed to be ascertained.

As part of this planned growth, extra staff and associated increased costs needed to be budgeted for.

Additionally, the owner managers wanted to monitor actual figures against the budget to demonstrate a sound financial track record and calculate a monthly break even sales figure.

Outcome

We worked with the management to prepare two year integrated forecasts. These demonstrated when the increase in stock would need to be ordered, shipped and paid for.

The owner managers were able to discuss the trade financing need with funders in good time with polished, accurate and detailed forecasts.

The actual financial figures are imported to the budget each month to enable variance analysis. A forecasted monthly break even sales figure has been calculated and assists in implementing the timing of the increased overheads.

There are better ways of predicting the future of your business

Case Study 2

Scenario

A business needed increased finance to support the working capital requirement.

Additionally, the management wanted to set targets for debtor days, stock levels and gross profit percentage.

The business has several branches and the management wanted to set budgets for each branch.

Outcome

Working with the management, we prepared integrated forecasts, this time for a three year period. These highlighted the effects on the cash flow of the debtor days and stockholding targets as well as the increase in profits resulting from gross profit percentage improvement.

The demonstration of the financial effects of these targets was an effective management tool.

The financing need was ascertained and invoice financing offered by the funder. The financial viability of this was tested in the forecasts.

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Finding finance

One of the major problems that businesses face is obtaining finance. This was particularly the case when the banking sector came close to meltdown two years ago. Even though the worst of this should be behind us, the fallout has left an ultra cautious banking sector completely at odds with the often repeated mantra about being open for business.

In addition, the proposed tighter restrictions placed on banks from 2012 under the Basel Committee on Banking Supervision guidelines to meet higher liquidity and capital requirements will surely see bank lending even harder to come by for companies.

So, where does that leave businesses looking to expand or continue operations and needing finance in order to achieve this?

Typically, finance is either that of a term loan or overdraft, although the latter is becoming less common with overdrafts typically being converted to term loans at the banks' insistence.

A fund portfolio

Businesses have to think in terms of having a portfolio of funding sources as opposed to just obtaining finance through their bank.

The first and obvious solution to a funding requirement can be found close to home, via the directors themselves, either by way of loan or share allotment. This is usually the cheapest form of finance although the risk of losing personal cash if the company folds can be a deterrent.

Factoring and invoice discounting have become mainstream finance solutions enabling quick cash release on valuations and applications. In reality these forms of finance are taking over from the traditional overdraft facility.

Cash flow

Delayed payments to creditors and prompt ones from debtors, if handled with care, ease cash flow problems. Acquiring assets on a hire purchase or leasing basis also enables cash flow savings to be gained. Instead of depleting cash reserves financing a monthly amount, typically over a period of three to five years, is far less onerous.

Ensuring that applications for payment are made instead of raising sales invoices is simple enough to do and can ensure that large VAT payments can be avoided until the money has landed in the bank.

Finally, don't forget that the government's Time to Pay scheme will continue for the foreseeable future. Even spreading tax payments over a matter of months can have dramatic cash flow benefits.

In summary, while the banking sector is the first port of call for a business, it need not be the last!

'Factoring and invoice discounting have become mainstream finance solutions'

It is important to find the funding that matches your business needs best

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Trusts

Trusts are extremely useful vehicles for individuals with concerns about keeping the family wealth intact and mitigating inheritance tax and capital gains tax exposure. This article provides an overview of what a trust is, the circumstances in which you might use a trust and the benefits of doing so.

Where are trusts used?
The uses of trusts are wide and varied. Oddly enough, you may have one without even knowing it! If you have a pension scheme, you are likely to have a trust attached to it which will determine what happens to the pension when you die. The pension company is merely the trustee of your funds and you choose your beneficiaries.

A trust might be created because:

- Someone is too young to handle their affairs.
- Someone is not capable of handling their affairs.
- You wish to pass on assets while you are still alive (trust created by a deed).
- You wish to pass assets on under the terms of your Will (trust created on death).

Why should you use a trust?
The benefits of trusts fall into two areas:

1. Family wealth protection
2. Tax planning

A gift into a trust is often preferable to an outright gift. A gift into trust can avoid a capital gains tax charge while also making an effective gift for inheritance tax purposes. At the same time you can control the manner in which the recipient benefits.
For example:

- The beneficiaries may be too young to look after the gifted property themselves.
- You may wish to confer benefit on the individual beneficiaries in the light of their circumstances from time to time rather than giving each beneficiary an equal share at a given age.
- You may wish to provide benefit for an individual but at the same time protect the funds from that individual's creditors (in the case of a bankruptcy) or spouse (in the case of death or divorce).

What exactly is a Trust?
The following six points describe the principles of how a trust is created and managed:

1. A trust is an arrangement which enables you to give money or other assets to another person (the trustees) to look after on prescribed terms for the benefit of individuals of your choice (the beneficiaries).
2. Although you must hand over legal ownership of the trust assets to the trustees, they cannot be used to benefit the trustees – they are simply looking after the assets for the beneficiaries. If the trustee should die or wish to retire, the assets do not leave the trust. A new trustee is appointed.
3. It is usual to have two or three trustees (but not more than four).
4. You can include yourself as one of the trustees. This would allow you to influence the manner in which the trust is managed. You and your co-trustees would be able to decide how to invest the trust assets and, subject to the terms of the trust deed, you would be able to control the flow of wealth to the beneficiaries.
5. The trust deed itself describes how the beneficiaries are to benefit. The trust may give complete discretion to the trustees about how much money to pay to whom, or it may lay down fixed rules. It is up to the person setting up the trust to decide. Ideally, the trust deed should also give certain administrative powers to the trustees, for example;
   - wide power of investment
   - power to appoint investment advisors
   - power to use nominees.
6. Trustees must act jointly and decisions must be taken unanimously.

If you think a trust might be of benefit to you and your family, or you would like to find out more then please do get in touch.

'The uses of trusts are wide and varied. Oddly enough, you may have one without even knowing it!'

A gift into trust can be effective for inheritance tax purposes

Business strategy in a low carbon economy

Britain's shift to a low carbon economy has two main implications. Firstly, this new market will create a supply and demand for emission-reducing technologies, with companies in the energy sector having to adapt their businesses more than most. Secondly, as a result of government policy and changing social attitudes, businesses need to assess their exposure and decide what action is necessary.

The government has introduced legislation committing the UK to reducing CO2 levels by 80 per cent by 2050 (relative to 1990 levels) and government policy will play a big part in ensuring we meet this target, with several examples already in operation:

Climate Change Levy: a tax on electricity, gas and fuel oil use by business. Reduced levy rates are paid by businesses that deliver reductions in energy use in line with their sector's climate change agreements.

Carbon Reduction Commitment: from 2010 a compulsory requirement for businesses consuming 6000 MWh of gas and electricity (about £0.5 million). This mainly covers large firms but will include some SMEs in manufacturing and also has implications for tenants whose landlords have commitments of their own.

Climate change will inevitably affect the way we harness and use energy

Building Regulations Part L 2006: this revision of the building regulations requires all new buildings and renovations of existing buildings to meet energy performance standards for the whole building.

EU Directive on Energy Performance of Buildings - Article 7: this requires all buildings to obtain Energy Performance Certificates (EPCs) with information on the building's energy usage, and for all public buildings (such as hotels and large restaurants) to display them.

Energy prices continue to rise, affecting all areas of the economy. This only strengthens the business case for energy efficiency and associated carbon reductions. In the marketplace, consumers are feeling the pinch of rising energy and fuel prices and are searching for new products to lower energy costs, such as hybrid vehicles and energy-efficient appliances.

Companies that wish to take the next steps in reducing their carbon emissions must first develop a clear understanding of their 'emissions profile' and the risks and opportunities this profile creates. Sustainable climate-related strategies cannot simply be an add-on to 'business as usual'. Instead they must be integrated into a company's overall business strategy for success.

Sam Sinclair, Operations Manager at GB Energy in Preston works with a wide range of businesses who are keen to reduce their carbon footprint. He is seeing companies now starting to analyse their business practices in order to adapt to the new carbon economy. Here, he writes about the four main areas for business owners to consider:

1. Operational improvement

Energy efficiency is the first and central issue for any assessment of the economics of carbon reduction. An assessment of carbon emissions and reduction opportunities often reveals new insights into operational procedures which have previously been taken for granted.

2. Enhancing business reputation

Carbon reduction presents an opportunity to enhance a business' reputation. This can have an impact on a variety of issues such as investors, local communities and other stakeholders.

3.Identifying new market opportunities

Carbon reduction can expose important information and insights for guiding new strategic directions. Companies can exit increasingly risky business areas in favour of more secure options by measuring environmental costs and risks associated with product or process lines.

4. Enhancing human resource management

An often overlooked and underrated initiative is the engagement of the workforce. Implementing strategies for carbon reduction requires substantive changes, in both the structure and the culture of an organisation.

Smalleytalk

Friends go coast-to-coast for charity

L-R Dave Clarke, Michael Proudfoot and Mike Bolton at the end of their coast-to-coast bike ride

Three friends from Kendal have raised over £1,200 for a local hospice following a gruelling coast to coast bike ride.

Moore and Smalley's partner Michael Proudfoot, and his friends Mike Bolton and Dave Clarke, cycled the 140 miles between Workington and Tynemouth in memory of family members who have died from cancer.

The trio completed the journey in three days raising money for St John's Hospice, Lancaster, which cares for terminally-ill cancer patients.

Michael and Mike's mother-in-laws, Lorna and Margo, were both cared for by the hospice before losing their fight against cancer and Mike's brother Glenn passed away in June this year having spent some periods of respite at St John's.

Michael said: "Sadly most of us have experienced the loss of a friend or family member to cancer. Mike and I have had relatives that have been well-cared for by St John's Hospice where the staff do a fantastic job. We hope the money we have raised will help support the work they continue to do.

"The three of us all enjoy bike riding, but the second and third days were a bit of a challenge. Luckily we only had two punctures between the three of us. We'd all like to thank our friends, family and colleagues for their kind donations and their support of our cycle challenge."

Staff at local cycle store Wheelbase kindly donated special cycling shirts for the trio to wear on their journey.

Wacky races give £2,000 boost to cancer charity

Lancaster firms have raised over £2,000 for a local cancer charity by holding a race night with a difference at The Borough pub in the city's Dalton Square.

As well as horse racing, the Wacky Races night, hosted by Reid Hamilton Insurance Brokers and Moore and Smalley Chartered Accountants, even featured racing pigs.

The event raised £2,095 for Lancaster-based cancer support service CancerCare after local firms sponsored the eight televised races and guests donated cash in exchange for toy money to 'bet' on the contests.

Lucky 'punters' won raffle prizes including shopping vouchers, champagne, and weekend breaks kindly donated by local businesses.

Event organiser Duncan Woodcock of Reid Hamilton, said: "It is inspiring to see so many local businesses coming together to support CancerCare, a charity very close to our hearts. Thanks to everyone for giving so generously."

Joyce Tombs, partner at Moore and Smalley, added: "This was a race night with a difference with some very close contests and an exciting time was had by all our guests. We'd like to thank all our sponsors and guests for their generosity on the evening, raising a significant sum for a vital local charity."

Race sponsors were Bay Radio, Marshall Glover, Wagon & Horses, David Ian Skoda, North West Tyres, Ratcliffe & Bibby, DJ Cox Group, APC Overnight and C&G Recycling.

Making the news

Moore and Smalley was inundated with requests for expert analysis as part of the media's coverage of the recent emergency Budget.

Managing partner David Ingram, associate tax principal Stephen Adams, and tax partner David Bennett were all interviewed for broadcasts on BBC Radio Lancashire, while Colin Johnson featured on BBC Radio Cumbria.

David Bennett was heard on Radio Lancashire's Graham Liver breakfast show alongside client The Borough pub in Lancaster.

The interview was conducted live from behind the bar where David gave an insight into how the rise in VAT would impact retailers.

Meanwhile, tax partner Tony Medcalf took part in the Lancashire Evening Post's live Budget webcast, giving the newspaper's online readers his reaction to the budget announcements as they happened.

Corporate services director Mike Hardaker appeared in the Blackpool Gazette's review of the emergency budget discussing new measures to help entrepreneurs.

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