ADVICE FROM THE MANUFACTURING TEAM AT
**ENSORS CHARTERED ACCOUNTANTS**

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# MANUFACTURING MATTERS

## Time to dig in

By **Chris Barrett** – Manufacturing Partner

I am struggling to remember the number of times I have re-written this article due to continuous changes both politically, but also with the rates of taxes and the future outlook for the UK markets and interest rates.

*Continued overleaf* ➤

Making you more than just a number

# Time to dig in *continued*

However, as I finish this article, a 3rd Prime Minister in the last three months is due to be in place and their job is undoubtedly to tackle a huge economic challenge with high inflation and a cost-of-living crisis, plus to build our economic growth back to a level we so desperately crave.

The Bank of England's pursuit of rising interest rates to try to curb inflation, has yet to slow it down – though with 0.5% added in September and the next prediction to further increase in November, we may start to see its effect.

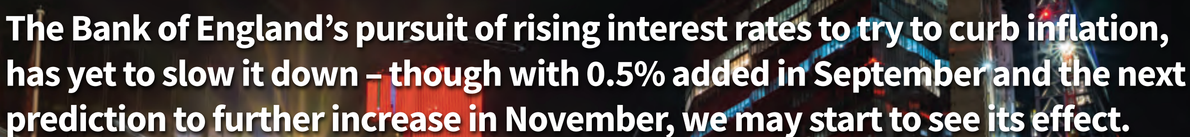
Alongside this, the ongoing impact of the Russian invasion of Ukraine has meant energy costs have risen to eye-watering levels. Whilst the government has stepped in with support both personally and for businesses for the next six months, this is clearly not long enough and makes budgeting extremely difficult, as businesses are planning now for beyond this period, but are struggling to with a lack of information. The concern is the number of businesses in the UK that may not be able to continue after this period, if further support is not granted.

All these factors are starting to show a fall in gross margins, as the continuous rise in cost prices is beginning to take hold and the difficulty to pass these on in full to customers. Output and order levels are slowing in certain sectors too, yet the continuous demand for skilled staff still appears to be unavailable to obtain in the market. A perfect storm you may say!

Whilst COVID was an unexpected headwind for businesses to face, the UK appears to be set for a deeper recession similar to the 2008 financial crisis. It is therefore a time to dig in and hold on for many manufacturers until the storm passes and consumer confidence is rebuilt in the market both within the UK and globally, as we are not facing these challenges alone. A strong Prime Minister will help to shape the path through these challenges ahead – let's hope they are up to the task.

Leading on from these challenges included within our edition, is our Research and Development (R&D) Manager, Sasha Talbot, outlining current issues faced in making R&D claims, plus the new rules due to commence in 2023. Also, our Corporate Finance Associate Partner, Simon Martin, outlines the more recent transactional structure of Employee Ownership Trusts and if these may be suitable to you for consideration.

I hope you enjoy reading this edition and wish you all a successful finish to 2022 and a prosperous 2023.



For many years the UK Government has been encouraging companies to carry out investment on innovative projects. In return, companies are able to claim R&D tax relief in respect of qualifying expenditure, which either reduces their corporation tax liability, or provides the company with a payable tax credit.

# R&D Tax Relief Scheme

# CURRENT ISSUES AND UPCOMING CHANGES

By **Sasha Talbot**
Research and Development Manager

However, during recent months there has been a lot of negative press regarding the relief, so is the relief still worth claiming?

In April 2022 HMRC paused the repayment of R&D tax credit payments. The main reason for this was due to a significant increase in the volume of fraudulent claims being submitted. This has led to HMRC introducing additional scrutiny processes, which has increased the processing of claims from 28 days to over 40 days.

In addition, there are proposed changes to the legislation which are being introduced for accounting periods starting from 1 April 2023.

What are the proposed changes from 1 April 2023?

## Overseas workers

At present, it is possible to claim for subcontractors and externally provided workers carrying out activities overseas. This will no longer be possible under the proposed changes, unless it is not possible to carry out the R&D activities within the UK. This may apply due to geographical, environmental or social conditions. There may also be legal or regulatory requirements which prevent the R&D being carried out within the UK. It will not be possible to claim for overseas subcontractors or EPWs, due to a lack of workers being available within the UK, or due to reduced costs being available overseas.

This is likely to have an impact on companies if they are currently claiming for workers within overseas group companies, or overseas third parties. For example, many software development companies use external developers from around the world and this may no longer be possible under the proposed changes.

## Data and Cloud costs

It is not all doom and gloom with the proposed changes, as cloud computing costs should be eligible for relief from 1 April 2023. This is a welcome change, as for a long time the R&D legislation has not kept up with the fast moving pace of software development. There has also been a large amount of confusion amongst tax advisors as to what expenditure is eligible, so the proposed changes will provide some clarity.

The following new categories of expenditure are being introduced:

- Licence payments for datasets;
- Cloud computing costs that can be attributed to computation, data processing and software.

Payments for datasets will only be eligible if used for R&D purposes, so relief will not be available if the datasets can be resold at a later date, or have a lasting value to the business following completion of the R&D project. It will be possible to apportion costs, where the licence payments cover multiple data sets.

Whilst cloud computing costs will be eligible, it will still not be possible to claim relief for servers and data storage. We await further guidance as to how this will work in practice, as licence payments often cover a range of costs, so suitable apportionments may have to be claimed.

The R&D tax relief still remains beneficial to companies, but the impact of the changes, together with the tighter scrutiny measures being imposed by HMRC, means that it is important to submit robust claims to HMRC to help reduce the risk of enquiry.

# Time to sell?
# Time for an EOT?

By **Simon Martin** – Associate Partner

An Employee Ownership Trust (EOT) is a form of employee ownership where a Trust acquires a majority stake in a business on behalf of all employees. Over recent years the EOT has become a much more widely used tool to sell a business and has also become a valuable way to engage the workforce.

EOTs were already on the rise pre-pandemic fuelled in part by a generous 0% tax structure for sellers in transactions of this nature. And, in recent years, their popularity has continued to soar.

Not all businesses will be suitable for an EOT. There needs to be a genuine desire for long term employee ownership. If this is embedded in an organisation, then an EOT can provide a controllable, tax efficient vehicle to sell, as well as providing a great catalyst for fresh optimism, commitment and, most importantly, engagement from staff.

EOTs have more benefits for vendors than just the very attractive 0% tax rate on proceeds. Although some EOTs can be structured below market value, it has become more usual for the sale to take place at a market rate determined independently by accountants.

An initial valuation can provide the vendor with an idea of the consideration which they would achieve, allowing this option to be assessed before advising staff and letting the proverbial genie out of the bottle.

Although the market for buying and selling businesses remains buoyant, there has been a noticeable shift in their characteristics, with many deals now comprising of elements that require harder negotiations. One of the more common and more challenging characteristics being a greater prevalence of Earn-Outs (contingent consideration) in trade deals. This means that business performance must continue to achieve a set level even after the deal has been completed, in order for all proceeds to be received. An EOT exit is generally a less stressful method to realise the value of a business, compared to a trade sale and comfort is drawn from the fact that it is the trusted management and employees of a business, that will be given the opportunity to share ownership, in the business that they have helped to build.

The deal needs to be fair and affordable, with the independent trustees needing to be satisfied that the deal is in the interests of the employees. Clearance regarding the tax implications is also required from HMRC.

If you would like further information on how an Employee Ownership Trust could help you realise the worth of your business, please contact our Corporate Finance team. They have a proven record in advising on successful EOTs, including structuring the deal and securing funding.

**www.ensors.co.uk/corporate-finance-team**

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***"Kalsec is an ingredient supplier for the food and beverage industry and have worked with Ensors for the last 20 years. We have found their service and advice professional and efficient, particularly valuing how Ensors know our business and people. We are a private and sustainable business operating in complex financial environments. In recent years, our European trading activities have increased, and we now work under several European jurisdictions. Ensors have provided comprehensive advice on several key areas such as corporation tax planning, joint venture incorporation and VAT compliance. As a thriving UK-based international business with strong capital investment and robust future growth planned, we firmly believe Ensors' continuous support as the independent and dependable financial adviser and auditor plays an important part in our ongoing success."***

James Smith – Managing Director, Kalsec Europe Ltd

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