NEWS FROM THE LATCO TEAM AT
ENSORS CHARTERED ACCOUNTANTS

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LOOKING AT LATCOs

Going concern issues for LATCOs

The past few years have bought a raft of financial uncertainties. Starting with the effects of the Covid pandemic, and more latterly the conflict in Ukraine, rising inflation rates, the tight labour market, the supply chain disruption and increasing energy prices. The list of potential obstacles for any entity is a long one.

Fortunately, most LATCOs have the support of a Local Authority and are willing to put pen to paper in this regard to support the going concern assumption in the accounts. However, it is wise to have these conversations with them early on if needed.

Continued overleaf ➤

Ensors

Making you more than just a number

As auditors, we are looking for support for a period of at least twelve months from when the audit report is signed, and we need evidence that the Local Authority has the resource if needed to provide this support.

ISA 570 – The auditing standard on Going Concern, requires auditors to obtain sufficient audit evidence regarding and concluding on:

- Whether a material uncertainty related to going concern exists; and
- The appropriateness of management's use of the on Going Concern basis of accounting, in the preparation of the financial statements

Reverse stress testing is a useful tool to enhance the robustness of the going concern assumption. It involves identifying scenarios which would make the business model unviable and also assessing the likeliness of those scenarios occurring.

Other accounting considerations include:

LOAN COVENANTS

Many LATCOs have loans with the Local Authority and it's not uncommon for these to have covenants. Long-term liabilities would need to be reclassified as current, if there has been a breach in loan covenants during, or at the year end, that could trigger immediate repayment of borrowings. It is possible to obtain a waiver of the covenant, but this needs to be agreed in writing prior to the year end.

BAD DEBTS

Like the covid effects, the current economic climate could have ramifications for investment property companies whose tenants are unable to pay. Persistent issues could also have an impact on lease receivables and consequently fair values of properties.

ONEROUS CONTRACTS

The supply chain impact and labour shortage could also mean that some contracts may now become loss-making, meaning that a provision may be required. In addition, some contracts may make provision for compensation to be paid for delays or non-performance.

Carrying values of assets, recoverability of deferred tax assets, stock write downs, the capitalisation of interest costs on paused projects and the estimation uncertainty in significant judgements, are all areas to consider too.

We are in turbulent times and understanding the key risks for your LATCO in a volatile economy is a challenging one, and almost involves the constant reappraising of budgets and cash flows to understand the current situation.

Don't ignore your Transfer Pricing

Without transfer pricing legislation, it would be relatively straight forward to manipulate the profits of connected parties, so that they fell into companies/organisations/structures where there was either no tax, or very low tax rates. This would deprive a government of the necessary funding to enable it to fulfil public needs.

The object of transfer pricing is therefore to analyse all transactions that take place between the connected parties and determine an amount that each of those transactions would take place at, if the parties were unconnected; the 'arm's length basis'. These transactions will not only include goods and services, but also financing arrangements/loans etc. The issue with financing is not solely the interest rate charged, but also would the recipient of the loan have been able to secure that level of finance from an unconnected lender, without the support of its parent undertaking.

By carrying out the transfer pricing analysis, adjustments can be made to arrive at an appropriate allocation of profit/risk for each type of transaction between the connected parties. Where the actual transactions do not take place on this arm's length basis, appropriate adjustments must be considered for corporation tax purposes.

For UK purposes, transfer pricing generally only applies to large entities. A large entity is one that meets one of the following:

- It has more than 250 employees or,
- Where there are less than 250 employees then a large entity must also have a turnover of more than €50 million and gross assets of more than €43 million.

The figures above must be looked at on a group basis. For transfer pricing, identifying the group will include not only the more usual 51% ownership criteria, but can also involve looking at what are known as linked enterprises and partnership enterprises.

Although transfer pricing has traditionally been considered to only apply where there are cross-border transactions, for a number of years now it will also apply between UK resident connected parties, providing they meet the size criteria.

Taxpayers must keep sufficient records to make a complete and correct return; there is guidance from both HMRC and The Organisation of Economic Co-operation and Development (OECD) as to what transfer pricing records should be maintained.

This brings us to local authorities and LATCOs.

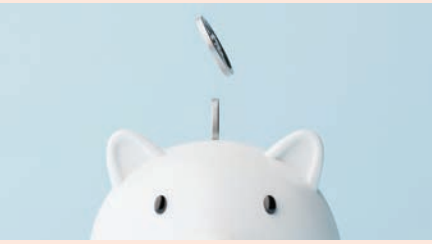
Although a local authority has a corporate tax exemption, it needs to be considered when determining whether or not the size criteria has been met. It is likely that a local authority will be largely using the criteria above and, therefore, so will the LATCOs that it owns. It is important that the LATCO has robust transfer pricing documentation to evidence the prices used for transactions with the local authority, so that HMRC will have confidence that the profits are allocated to the correct entities.

Payroll: Is it time to outsource?

Historically, and somewhat inaccurately, payroll has been misinterpreted by many as simple data processing, often tagged onto the responsibilities of internal finance or HR teams. But with huge legislative changes in recent years; Real Time Information (RTI) reporting, Auto-Enrolment Pensions and numerous holiday pay rulings to name but a few, is now the time to outsource?

We've considered the advantages and disadvantages, of making the leap to an outsourced payroll function.

Advantages



Financial savings: The financial savings to be made in software alone can be enough to make outsourcing look a more attractive option! Many software providers operate on a monthly subscription basis linked to employee numbers, often based on turnover within the tax year rather than just current active employees (meaning a business can be paying to maintain the records of employees it no longer has). With additional costs for module add-ons to deal with extra requirements such as auto-enrolment pensions; this can all add up to a hefty price tag.

Time savings: Passing the payroll responsibility onto a third party can free up valuable time that can be spent on growing your business, or focussing on other important internal processes if payroll currently falls in the remit of internal finance or HR teams. It also eliminates the need for time spent keeping your own teams up to date with the frequent legislative changes; the responsibility and cost of this would all lay with the third party provider for their own staff.

Expertise: Outsourcing can give your business access to qualified and experienced payrollers. The Chartered Institute of Payroll Professionals (CIPP) estimates that there are only 15,000 qualified payroll professionals working in the UK – an asset that can be expensive and difficult to come by in-house. Payroll is of paramount importance to any business; issues with pay can quickly lead to issues in staffing and retention, so best left to the experts.

Cover, efficiencies and segregation of duties: Outsourcing your payroll function passes the burden of ensuring there is cover and continuity of service entirely to the third party provider, meaning no more holiday headaches, or worries if there are internal unexpected absences. Many payroll providers also offer BACs payment services too which can alleviate time pressures on the finance team usually required to make payments, as well as utilising autonomy to minimise the chances of input error or fraud.

Robust systems and security: A diligent payroll provider will have invested time and money in choosing a robust, reliable and secure payroll system; just be sure to enquire about your chosen provider's GDPR policies. A strong reporting package will come hand in hand with this, often with the ability to tailor reports to individual needs.

Disadvantages

Data access: You may lose instant access to employee or financial data and statistics which may previously have been easy for you to retrieve quickly, instead having a small delay while your provider collates this and responds.

Staffing decisions: If your business currently has an in-house payroller, you may need to consider if there are enough other responsibilities for them to maintain employment. This may be the right decision for the business, but of course never an easy one to make.

Stricter timescales: Some flexibility may be lost with regard to timescales, and you may need to consider being stricter, or potentially bringing forward cut-offs for overtime claims and similar items… though some may consider that an advantage!

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LATCo™ network
enabling innovation

Ensors are proud to be working closely with the LATCO network – "the first membership organisation founded entirely by LATCOs for LATCOs to provide a sector voice and enable support to members delivering public services commercially."
https://latco.network/

We are providing the Network's members with initial free-of-charge meetings from across our comprehensive range of accounting and tax professionals.

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