

Financial and business intelligence

Spring 2008

SHIPSHAPE

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Chartered Accountants & Professional Business Advisers

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The gathering storm

Wobbling stock markets, a worsening credit crunch, inflationary pressures and talk of recession. Welcome to a new financial year. What can we do to weather the storm?

Grin and bear it?

With the collapse of US investment bank Bear Stearns, the problems in the banking sector have clearly moved from sub-prime to prime. Bear Stearns was the most exposed of all US banks to risky loans – and it became the first major bank to be undone by the market's jitters.

It's interesting to contrast the way similar crises were handled on either side of the Atlantic. After months of wrangling, the Northern Rock affair rumbles on. Whereas, just four days after Bear Stearns' Chief Executive Alan Schwartz assured Wall Street his company was not in trouble, the Federal Reserve and the US government swiftly approved an all-stock buyout, demonstrating the urgency of doing a deal before world markets reacted.

The investment bank was sold to rival JPMorgan Chase for an initial bargain-basement price of \$2 a share, or \$236.2 million. The Manhattan HQ alone is worth more than US\$1 billion. The move successfully averted Bear Stearns' bankruptcy and headed off a crisis of confidence in the global financial system.

Belt tightening

For most individuals and businesses the most immediate impact of all this will obviously be on lending. Many banks have already chosen to cut their mortgage offerings and people are now finding it harder to secure the funds they want.

The recent Budget hasn't made matters much better. True, the Chancellor has reduced the basic rate of income tax from 22% to 20%, but for some employees and the self-employed this will be more than offset by increases in national insurance contributions.

Mr Darling was never going to get any easy ride from the pundits and his hands have been somewhat tied by his illustrious predecessor. There was, however, an opportunity for him to make his mark, which he largely failed to grasp.

In fact, the Budget was more notable for what wasn't included, than for what was. Proposed changes to the capital gains tax regime had already been universally pilloried prior to the Budget, resulting in a climb-down and the introduction of entrepreneurs' relief. Non-domicile rules remain

hazy for the uninitiated despite initial proposals being refined following consultation. And, predictably, the Chancellor eschewed major tax cuts – ignoring calls for the abolition of inheritance tax for example.

Plotting a course

Amid worsening global economic data, the road ahead looks ever more uncertain. At Shipleys we'll be working hard to help our clients through this potentially challenging period. For our business clients, it's more important than ever to focus on working *on*, rather than *in* the business.

A new look

Finally, you'll notice that there's a new look to Shipshape. This follows last year's readers' survey and the many useful comments we received. We hope you like the results.

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Strengthening our team: meet our new Principals

We are delighted to announce the appointment of three new Principals at Shipleys. But who are the personalities behind the names?

Nancy Cruickshanks



“The challenge of my job is explaining VAT in words that clients can understand”

Nancy is a VAT specialist and her appointment as a Principal shows the increasing importance of VAT issues to Shipleys and our clients. Back in 1973 when VAT was first introduced, it was famously described by then Chancellor of the Exchequer Anthony Barber as being a “simple tax”.

VAT has now become very complex and the penalty regime is harsh. Nancy says her aim is to “help clients navigate the shark infested waters of VAT”.

Her advice covers both compliance and planning, mainly for businesses but also for private individuals. Her clients are from a variety of sectors, including land, property & construction, entertainment & media and financial services. They include all sizes of business from start-up, to those seeking a listing and PLCs.

Nancy secures zero rating certificates for individuals, which enable certain purchases of goods and services otherwise subject to standard rate VAT to be zero rated. She also advises on reduced rates of VAT for construction services

Making VAT as simple as ABC

“The challenge of my job is explaining VAT in words that clients can understand so that they can fulfil their compliance obligations and take advantage of planning opportunities. I think it’s important to earn the trust of a client so that they contact me about VAT before getting into a muddle.”

There have been numerous memorable moments in Nancy’s career: “Back in my Customs days, I once made some disparaging comments about some art which was being sealed for export. I later realised the artist was Don Van Vliet – also known as Captain Beefheart, for those old enough to remember!”

“More recently I met with the accountant to a financial services business who needed some help with specialist VAT planning. Before completing our journey from the client’s office to the owner’s home, we had to wait at the gates of the estate for a plane to land on the runway in the grounds before proceeding to the house where we took afternoon tea!”

Nancy has qualifications from CIMA, the Association of Tax Technicians and the Chartered Institute of Taxation.

Stewart Jell



“I’ve developed a particular expertise in the film, television and related industries”

Stewart enjoys looking after a variety of clients, most of whom are in the entertainment and media industry, or closely linked to it in some way. He has a wealth of experience in the sector ranging from sorting out the day-to-day business administration of the UK subsidiary of an overseas company, through to auditing the accounts of a UK PLC.

“What I like about my job is that no two days are ever the same. I get to meet an incredible variety of people through looking after a ‘mixed bag’ of clients. One day I may be setting up the system to keep the financial records or making sure the management accounts are ready for the board. On another I’m drafting a policy paper. I really enjoy taking an active part in getting things done.”



Shipleys' other Principals in the entertainment & media team, Ken Roberts and Steve Joberns, have built up a well-regarded and very busy department. Lead Principal Ken comments, "I am delighted with Stewart's appointment. He has the same ethos as the rest of our team and will make a major contribution to our plans for the future".

Homegrown talent

Stewart joined Shipleys straight from Birmingham University as a trainee and qualified as a chartered accountant with the firm in 2001. "Over the years I have developed a particular expertise in the film, television and related industries and I'm proud of the contribution I've made to growing the Shipleys entertainment & media industry team and building the reputation it enjoys."

Outside work, Stewart is an avid cricket fan and associate member of the MCC. He is married with two young daughters.

Joe Kinton



"One dream client was a motor racing team"

Joe's appointment recognises his outstanding technical ability and the contribution he has made to the firm's audit and corporate finance work.

He's a Cambridge Maths graduate and ICAEW prizewinner who trained with Shipleys and now sits on the firm's audit technical committee. "I've worked on everything from pure audits to projections. I really enjoy helping clients refine their business plans by showing how they impact on financial performance. This covers a variety of situations, from a listing, other fundraising, an acquisition or even sale of the whole business."

"My clients tend to be larger companies, quite often with investor shareholders who don't work full-time in the business, whether AIM or PLUS listed, or in private ownership." Joe's clients value his ability to help identify and model the key drivers to the financial success of a business.

The jet set

Joe has certainly had some enviable and glamorous assignments. He's audited a motor sport race team, visiting the factory, meeting the drivers, finding out all the race gossip and soaking up the pre-race atmosphere.

Joe has also worked on projects for a luxury yacht builder. "I now know what people mean when they refer to a floating gin palace!"

"For both these clients, attention to detail is quite astounding – the obsession with numbers and regulation is about as far as the comparison with the accountancy industry goes!"

When not working, Joe enjoys travel, snowboarding, socialising with friends and the occasional music gig.

... And fond farewells

Our fondest wishes to John McCuin and Sue Whiting, both of whom are leaving the firm. As we explained in the previous issue of *Shipshape*, John will focus on his heavy workload as Prime Warden of City of London livery company, the Worshipful Company of Blacksmiths, but will remain a Shipleys Consultant.

Sue Whiting recently married a partner in another accountancy practice and is looking forward to a well-earned retirement on the South Coast. We'd like to take this opportunity to wish them both the best of luck with their future plans.

Cars and capital allowances

Back in March 2007 the Government signalled that changes to the capital allowance system would be made to encourage the use of cars with lower CO₂ emissions. Capital allowances are the tax deductible allowances given for depreciation, which is not otherwise allowed as an expense in calculating taxable profits.

“The system for cars with higher CO₂ emissions will be reformed from April 2009”

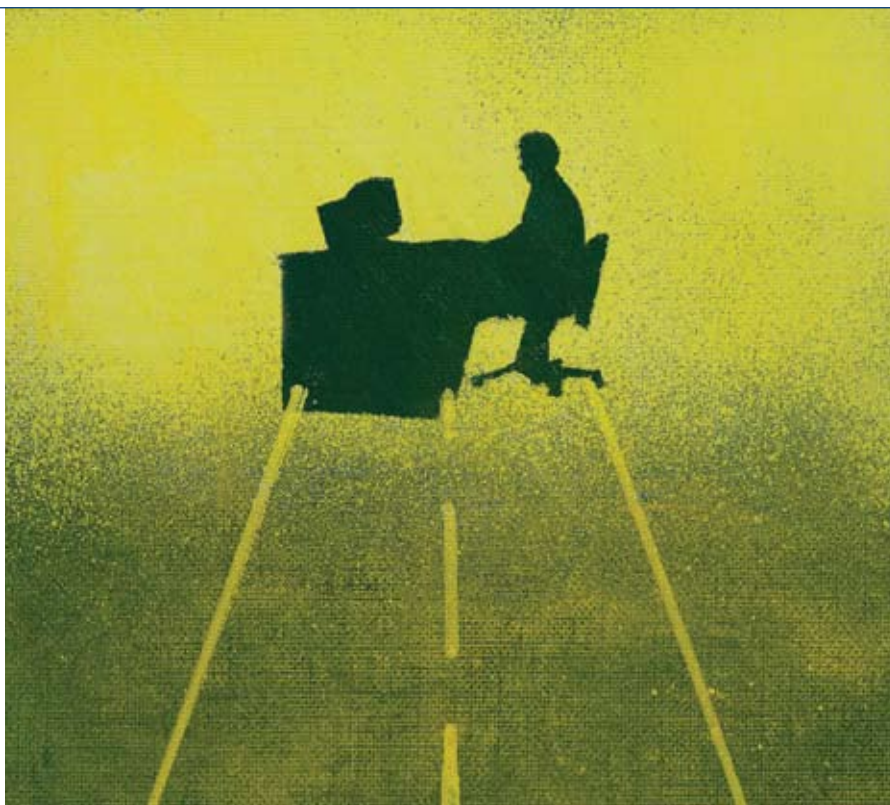
This year’s Finance Bill includes new provisions which extend the 100% capital allowances for cars with very low CO₂ emissions until 2013, but also cut the qualifying level from 120 to 110g/km.

From 6 April 2008 the annual writing down allowance (WDA) will be 20% rather than 25%. A distinction will still be made between cars costing up to and more than £12,000. So-called “expensive” cars are dealt with on an individual basis, so a balancing charge or allowance, calculated by comparing the sale proceeds with the written down value, is given when the car is sold. This means tax relief is given for the excess of cost over disposal proceeds during the period of ownership. Other cars go into the general pool of plant and machinery for capital allowances purposes.

Heavy polluters

However, it was announced on Budget Day that this system will be reformed for cars with CO₂ emissions in excess of 110 g/km from April 2009. Most notably, cars with CO₂ emissions above 160g/km will then attract only a 10% WDA.

The rules disallowing a proportion of car lease rental payments will also be reformed from April 2009 “in line with the new capital allowances rules”.



Companies Act – a reminder

The latest set of sections of the new Companies Act came into force on 6 April. Some of these sections will have a significant impact on many of our clients. There are two changes to be particularly mindful of.

Company secretaries

The appointment of a company secretary to a private company is now optional – provided the Articles allow this. If you are considering dispensing with the role of company secretary in your company, we strongly recommend you ensure that at least two directors are constantly in office. This will ensure that at least one company officer is available to deal with administrative and compliance issues, if the other is absent.

Filing of accounts

The rules for delivering accounts to Companies House have changed for all accounting years commencing on or after 6 April. Only nine months after the end of the accounting year – rather than ten previously – will be allowed for private companies to deliver their accounts to Companies House. For public companies, only six months will be allowed, instead of seven previously.

Overseas homes owned through companies

The Finance Bill does not go as far as had been hoped for those owning residential property abroad through a company or trust. It has long been a concern that an expensive annual benefit-in-kind income tax charge could technically apply on the basis that a property is made available by reason of employment – potentially including ‘shadow directors’. The announcements made at the time of the 2007 Budget suggested legislation would be introduced with retrospective effect to remove this problem.

Gaps in new rules

Although “time-shares” may now be included, the draft legislation does not appear to cover the common scenario where property is owned by a company which is itself owned by a trust. Furthermore, popular overseas entities such as a French société civile immobilière (SCI) are not obviously covered by the relaxation of the rules, although it is possible that HMRC may include them in practice.

Finally, the draft legislation does not apply to homes in the UK owned by companies – a common situation for non-doms.

Behind the Budget

On the face of it, the new Chancellor's first Budget speech was pretty dull, but further examination of the record-breaking number of detailed background papers provides much food for thought.

Some of the tax changes for 2008/09 were announced in Mr Darling's Autumn Statement in October, and others as long ago as March 2007. We have now had the benefit of seeing the Finance Bill, published on 27 March. As ever, changes and additions will occur during the progress of the Bill through Parliament, until it receives Royal Assent, probably in early July. We enlarge on some key aspects of the proposals below.

CGT – 10% rate limited in scope

Although the new rules for non-doms (see the *Current Issues* section of our website for a detailed note on this) have attracted a lot of attention, changes to capital gains tax are generally of much wider interest. Of particular note is the limited scope of the entrepreneurs' relief – the new 10% CGT rate – which will be confined to a lifetime maximum £1m of gains realised on certain assets.

Many who might have expected entrepreneurs' relief to mirror business asset taper relief and reduce their tax rate to 10% will not be eligible, and will face tax at 18% instead.

Disposals of shares

The main CGT relief is for interests in a business or shares – but in the latter case, only for employees and officers of a company who hold at least a 5% interest and have done so for a year. Many employees will fail the 5% shareholding test. Certainly many investors in AIM shares will not qualify.

'Associated' disposals

There is relief available for disposals of, for example, land used to carry on a trade – but only if the disposal is "associated" with a disposal of an interest in a business that would itself qualify for entrepreneurs' relief. Even then, the relief is only available to the extent that rent payable falls short of open market rent.

To be "associated", a disposal must be part of "the withdrawal of the individual from participation in the business carried on by the partnership or company" and the asset must have been in use for the purposes of the business throughout the 12 months ending with the disposal or, where appropriate, the earlier cessation of the business.

A similar rule applies in the case of a trust, save that the trust beneficiary must have ceased "participation" (personally owning at least 5% and

being an employee or director) in the business on the date of disposal or within the preceding three years.

Unlike business asset taper relief, entrepreneurs' relief will not apply to landlords of unquoted trading companies, partnerships or sole traders with no connection with their tenant.

'Settlor-interested' trusts

Aside from the above, the new 18% CGT rate applies to UK trusts and estates, as well as to individuals. Current rules, under which settlors suffer tax on gains realised by a trust from which they, their spouse or an infant child may benefit, are to be repealed.

This is a welcome simplification and should mean that such trusts will be able to use the annual exemption. However, it also means that the settlor may not set his or her capital losses against the trust's gains.

Annual Investment Allowance

There is a new allowance giving 100% tax relief on the first £50,000 a year of capital expenditure on plant and machinery (other than cars) available to individuals, partnerships, 'solo' companies and groups of

“Many who might have expected entrepreneurs’ relief to mirror business asset taper relief... will face tax at 18%”

companies, including those involved in commercial letting. It applies to expenditure from 1 April 2008 for companies, and 6 April for individuals and partnerships.

The AIA replaces the first year allowance, which was 50% for small enterprises and 40% for medium-sized enterprises (although available on all qualifying expenditure). Like the first year allowance, the AIA will not be available to a partnership with one or more members who are not individuals – i.e., they are companies or trusts. Otherwise, there is an annual writing-down allowance of 20% – or 10% for “special rate expenditure”, including long-life assets.

The AIA will not replace the pre-existing 100% regimes such as those for research & development and business premises renovation.

To avoid multiple claims, only one AIA will be available if businesses share premises or carry on similar activities.

‘Income shifting’

The Chancellor was notably silent on the subject of ‘income shifting’ (see *Money Matters* on the back page). We now know that any changes to the rules for this practice have been postponed for a year, pending further consultation. The Government is clearly finding it difficult to meet its

objective of preventing income being diverted to a spouse or partner with a lower tax rate, while providing certainty in the tax self-assessment system.

Motoring costs

VAT fuel scale charges have changed significantly. The amounts subject to VAT for prescribed accounting periods commencing after April 2008, which vary according to the CO₂ emission, are available at www.hmrc.gov.uk/budget2008/notes-pdf.htm

There have also been changes to Vehicle Excise Duty (‘road tax’) rates. The scale of rates may be seen at www.direct.gov.uk/en/Motoring/OwningAVehicle/HowToTaxYourVehicle/DG_10012524

Stamp Duty Land Tax

The Government has recognised a need for alternative finance structures – such as Shariah compliant finance – in place of conventional mortgage schemes to buy property. In response to this, measures were introduced in 2005 to give an exemption from SDLT on a purchase by a lender from a borrower, including where there is a re-mortgage.

According to the tax authorities, some financial institutions have secured these exemptions by “colluding” with vendors so that

ownership of a property is placed in a subsidiary company of the financial institution. The Finance Bill 2008 proposes that this relief from SDLT will not be available if there are arrangements for a person to acquire control of the relevant financial institution.

Offshore funds

After lengthy consultation, the Government is planning to introduce a ‘modernised and simplified tax regime for offshore funds’. Discussions will continue on a new definition of offshore fund to be included in next year’s Finance Bill.

‘Distributing’ funds, for which gains are subject to CGT rather than income tax, are to be re-named ‘reporting’ funds. Currently, if a fund does not have ‘distributing’ status throughout an investor’s period of ownership, the whole of any gain on disposal is taxed as income. Under the new regime, it is proposed that investors will be able to make a deemed disposal election when a fund ceases to be a ‘reporting’ fund. They would then be subject to CGT on the gain accrued, with only the subsequent growth taxed as income. This is likely to affect the growing numbers who invest in overseas mutual funds and Open Ended Investment Companies (OEICs).





Financial Assistance Scheme

Income tax payable on compensation under the Financial Assistance Scheme – which pays lump sums to those whose pension schemes ‘go under’ – will in future be linked to the relevant tax years to which the payments relate. It will no longer be treated as a single amount for the year of receipt, as was originally stated. Receiving a lump sum in one year representing several years’ arrears has sometimes pushed pensioners into the 40% tax bracket, whereas they might have only paid basic rate tax if the arrears had been received when due.

Further information

Our *Budget Summary 2008* booklet includes a full summary of the main proposals and is on the publications page of our website, www.shipleys.com, or you can request a free printed copy from Sandra Wyton at wytons@shipleys.com, T 020 7312 6547

VAT News

Commercial property – option to tax

The VAT rules relating to commercial property have become more and more complex and difficult to apply since the introduction of the option to tax in 1989. This has long been recognised by HM Revenue & Customs, which has now rewritten the legislation following consultation.

The final version of the legislation has yet to be published. What we do know, however, is that it will come into effect from 1 June 2008 and, rather than change the meaning of the law, is designed to make it easier to understand and administer. There will, however, be some minor amendments to deal with:

- opted properties held in a VAT group
- a simplified procedure for taxpayers who own a number of properties
- the opportunity for early revocation and a ‘cooling off’ period.
- automatic lapse of an option to tax six years after the taxpayer has ceased to have any interest in a property
- the ability to exclude a new building from a previous option to tax
- late applications for permission to opt to tax.

A new version of the VAT leaflet will be published and some parts will have force of law. It will be extremely important to become familiar with the new requirements once they are made available. Watch this space.

Three-year cap

Following the decision of the House of Lords in the *Fleming* and *Condé Nast* cases, a Revenue & Customs Brief (07/08) has been issued to let businesses know how to make claims for refunds of overpaid VAT. The full text is available at www.hmrc.gov.uk. The main points are as follows:

- the three-year cap no longer applies to claims for refunds of under-claimed input VAT relating to VAT periods ending before 1 May 1997
- likewise, claims for refunds of overpaid output VAT arising before 4 December 1996 are no longer subject to the three-year cap
- claims must be submitted to a special claims handling unit based in Liverpool (‘Fleming’ Claims Team (Leeds), Queens Dock, Liverpool L74 4AA)
- claimants should expect their claims to be subject to verification by HMRC, but there should be no undue delay in payment.

What has not been addressed is the thorny question of interest. Statutory interest is normally simple interest and at a very low rate, but there is some recent case law which suggests that compound interest may be available and at a much higher rate than previously used by HMRC. It’s important to bear this in mind, as it’s quite possible that the interest will be worth a great deal more than the underlying tax being claimed.

Construction services – 5% rate

With effect from 1 January 2008, the qualifying period for applying the 5% rate of VAT to renovations and alterations to empty residential properties has been reduced from three years to two years.

Comparing tax across Europe

Our global accounting association, AGN International, has published the results of the latest in its annual surveys comparing taxation in different European countries.



The surveys examine the comparative rates of various taxes from country to country, which vary considerably. Even among EU member states, tax is not harmonised, but governed by national legislation and numerous bilateral and/or multilateral agreements.

Rather than comparing headline rates (such as Gordon Brown's 10% rate of income tax, which only ever applied to a maximum £2,320 of income) the surveys take an example individual or business and compare the effective rates that would apply to them in each country. For example, the salary tax survey is based on an employee who is married with two children, on an annual salary of €100,000, with a company car which cost €40,000 when new and who pays mortgage interest of €7,500 each year.

Corporate taxes

The corporate tax survey examines effective corporate tax rates, which range from 7% in Malta, 10% in Cyprus and 13% in Liechtenstein, to 42% in the Ukraine. The majority of countries surveyed effectively levy corporate taxes between 28% and 41%. Some Southern and Eastern European countries such as Croatia and Hungary have become increasingly competitive. The Isle of Man, with zero tax, still appears to be a good place to locate a business.

Salary taxes, social security and expatriates

This survey shows that Liechtenstein leaves the most money in the pocket of the employee (89.7%) and the United Kingdom the least (54.31%). Cost of employment is highest in

France at 42% of employee salary cost, but France leaves 76.59% of gross salary in the hands of the employee. The total cost of employing someone in Sweden is almost 2.5 times net salary, compared to almost two times in the Netherlands and around 1.2 times in Russia.

VAT

Our survey demonstrates that the VAT picture around Europe is far from simple – in theory, VAT should be uniformly implemented, but in practice there are numerous local variations which can lead to costly errors, penalties and high compliance costs. Local advice at an early stage is clearly essential.

Parent companies and corporate structure

From a tax point of view, a non-resident taxpayer will gain most benefit from a parent company in

the Isle of Man, Gibraltar or Cyprus. However, our survey shows that it may be necessary to establish a combination of parent companies in different jurisdictions to achieve tax saving objectives.

Inheritance taxes

These taxes are often overlooked by the increasing numbers of people choosing to live or work outside their own country. The results of this survey show substantial variations in effective tax rates, from around 15% in the Netherlands and Spain to no effective tax at all in some countries including Cyprus, Estonia, Gibraltar and Sweden.

Full details of the AGN 2008 European tax surveys are available free of charge at www.agn-europe.org or contact AGN Europe: T + 44 (0) 20 8947 4888 E info@agn.org

Our friends down under

The opportunity to come to London and experience the UK way of life and work is something that many Australians seek. No different are Lauren Henderson and Aida Karup from Melbourne's William Buck's business advisory division, who have recently been on secondment to our London office.

"Our two months at Shipleys have passed very quickly. We've learned new systems and gained experience in audit, particularly in the film industry,

which would have been hard to come by in Melbourne", says Aida.

Lauren adds that the pair have taken every opportunity to experience UK culture. "Apart from the tea-making ritual, freezing cold rainy days and a few slang words, we have found many similarities between London and Melbourne. All in all, a great experience and one that will definitely be remembered and recommended to our fellow colleagues."

Saffron Insurance – a recipe for success

Shipshape talks to Richard Brown, Commercial Director at Saffron Insurance, about the company's thriving commercial business.

Saffron Insurance started life 53 years ago as Saffron Brokers, an offshoot of the National Farmers' Union. Still retaining a head office close to its roots in Saffron Walden, it is now one of the largest independent insurance brokers in East Anglia.

As Richard explains, "today we're one of the region's major players, with gross written premiums of between £15m and £25m, and commercial insurance is a major part of the business. But the company started more humbly and was run from a small office in what is now the gentlemen's lavatories of the local Conservative club!"

A vivid vision

The company's major shift took place in 2003. David Beswick took over the reins as MD and Chairman and, in the same year, Richard joined the group to develop its commercial business, drawing on 15 years' experience in commercial underwriting and development. At that time, the business had one office, seven staff and £2.5m in premiums.

"We had an ambitious vision to become a bigger broker and get the best products, pricing and service from insurance companies", says Richard. To achieve it, Saffron embarked on an aggressive drive to find experienced commercial staff.

Since 2003, Saffron has made 18 broker acquisitions and now has 63 staff and five offices across Essex,

Hertfordshire and Cambridgeshire, each offering commercial insurance services.

The right ingredients

So, what's behind this success? Richard puts it down to a deep understanding of clients' needs and the ability to negotiate the best products and prices whilst providing very high standards of service. A major factor in this has been the dedication, experience and hard work of the team, explains Richard.

Today Saffron is achieving policy renewal rates of over 90% – while other larger brokers work to renewal levels of around 70%-80%. What's more, with no call centres, no call waiting and high quality advice, Saffron have attracted a market that doesn't look to change their policies year-on-year based solely on price.

A steady hand

Richard is quick to point out that it's not a position Saffron has attained

"We had an ambitious vision to become a bigger broker and get the best products, pricing and service from insurance companies."

Saffron has invested in training for staff – encouraging them to take professional exams with the Institute of Insurers – to enhance their professional approach.

Saffron is not resting on its laurels. The company has recently invested in a team to manage the nitty gritty of the claims process, freeing up the commercial team to concentrate on developing client relationships.

It's also launching a series of white-labelled insurance schemes offering good policy cover at competitive prices for specific industries, as well as an enhanced product for residential and commercial property owners

without help. "Shipleys has been a valuable source of advice throughout our period of growth". The Shipleys team, led by Gary Haselton, has done more than just provide financial and management accounts and tax advice, acting as a sounding board, helping with acquisitions, group structure and how to handle deals.

Looking to the future, Richard is confident Shipleys will still be providing the kind of support Saffron needs. "We know we can be a demanding client, but Gary is no ordinary accountant – he's easy going, sociable and always there when we need him."

EIS broadens appeal

The changes in the capital gains tax rate provide an interesting opportunity for those considering the Enterprise Investment Scheme (EIS).

Most readers will be aware that a flat CGT rate of 18% has been introduced for gains realised by individuals, trustees and personal representatives after 5 April 2008. Previously, capital gains calculations took into account indexation allowance and taper relief, but the effective tax rate was normally between 10% and 40%.

Under the EIS, there is a 20% income tax credit on investments of up to £400,000 in a tax year. Once the shares have been held for two years, they should qualify for 100% relief from inheritance tax. In addition, gains made in the previous three years can be deferred without limit, but subject of course to the maximum that can be raised by any one company under the scheme. If the EIS investment

continues to qualify for the income tax credit, then any gain on its sale is exempt from CGT.

The performance of the EIS investment is key, so selection of the right scheme is crucial.

Shipleys LLP is not authorised to advise on the selection of individual

EIS schemes, which have historically been higher risk. However, we can introduce Independent Financial Advisers who specialise in selection of lower risk schemes designed mainly to preserve capital and bank the tax advantages, rather than to deliver investment growth or income.

Example

If a gain of £100,000 has been charged to tax at 40% in 2007/08, the net cost of investing £100,000 in an EIS scheme in 2008/09 might be £40,000 (£100,000 – £20,000 income tax credit – £40,000 CGT deferral). If the EIS investment is sold three years later for the original cost, the deferred capital gain is taxed at 18% rather than 40%, so the overall tax benefit is 42% of the amount invested.

The investor is left with £102,000 in all (£42,000 more than the £60,000 available if the investment had not been made) i.e. a 70% return.

'Income shifting' changes delayed

The Chancellor announced in the October 2007 Pre-Budget Report that legislation would be introduced with effect from 6 April 2008, following consultation, to thwart attempts at 'income shifting'. This affects those who arrange their affairs to gain a tax advantage by shifting part of their income, from dividends or partnership profits, to another person who is subject to a lower rate of tax.

This followed the taxpayer's House of Lords success in the *Arctic Systems* case, which concerned an IT consultant, Mr Jones, who hired out his services through a company owned jointly with his wife. Although she was responsible for some administration, Mrs Jones had limited input into the

income generating activities of the business. But the Revenue failed in its attempt to treat the dividends Mrs Jones received as Mr Jones' income for tax purposes.

However, in last month's Budget it was announced that there will be a further period of consultation to ensure "clarity and certainty for businesses and their advisers". Legislation is now intended to be included in the 2009 Finance Bill, so it seems likely to apply from 6 April 2009.

So, what should you do now if you might be affected? It seems that action is unlikely to be taken against those who shift income in the current year. For others, who may be targeted

at some point in the future, it would be prudent to start documenting the duties carried out by each spouse with a view to defending any attack from the Revenue.

Detailed advice should be obtained before taking action, or refraining from taking action, as a result of information in this newsletter.

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