JOHNSTON CARMICHAEL

Hospitality and Leisure News

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Closest to Your Business

Editorial

Welcome to our new edition of Hospitality and Leisure News. There's no pretending that these are easy times for the industry – consumers continue to tighten their belts, and recent changes to immigration law are having a heavy impact on businesses employing migrant workers (see Alessandro Riccomini's article, p6). But even in these challenging times, there are still opportunities to be had. Craig Mathieson might even argue that there's 'good news'. His article 'Paying too much VAT?' p8, brings the welcome news that the European Court of Justice has just confirmed that cancellation charges retained by a hotel when a guest does not turn up, are not subject to VAT. So check your records – it may be that HMRC owes you.

While everyone agrees that this is no time for unnecessary spending, it certainly is time to review your systems to see whether any improvements can be made. Good management of cashflow and stock is essential and Tina Buchanan has some timely advice as to how Sage software might help you.

One area of the industry which is benefitting from the current climate is the 'budget' sector. In his article 'Time to tackle the crunch', p4, Matt Henderson suggests how to take advantage of this and reminds us that we should all be thinking creatively. Could you subcontract out your catering, or outsource your housekeeping? It may be the key to your survival.

Another 'advantage' of today's situation is the weakness of sterling against the euro. This will attract more home-grown visitors which may in turn lead to a desire to improve your facilities. Gillian Cardwell, p9, urges you to carefully review your capital expenditure in order to maximise tax relief under the new rules. There's 100% tax relief on environmentally desirable assets which is worth keeping in mind.

Lastly, look after your people, says Scott McDonald, p10. They are your 'greatest asset' and without them 'your business could suffer serious financial loss or cease trading altogether'.

We hope you find these articles helpful. If there is anything not covered which you would like to discuss, please contact us. We take our responsibility to you very seriously and are here to help.

Contents

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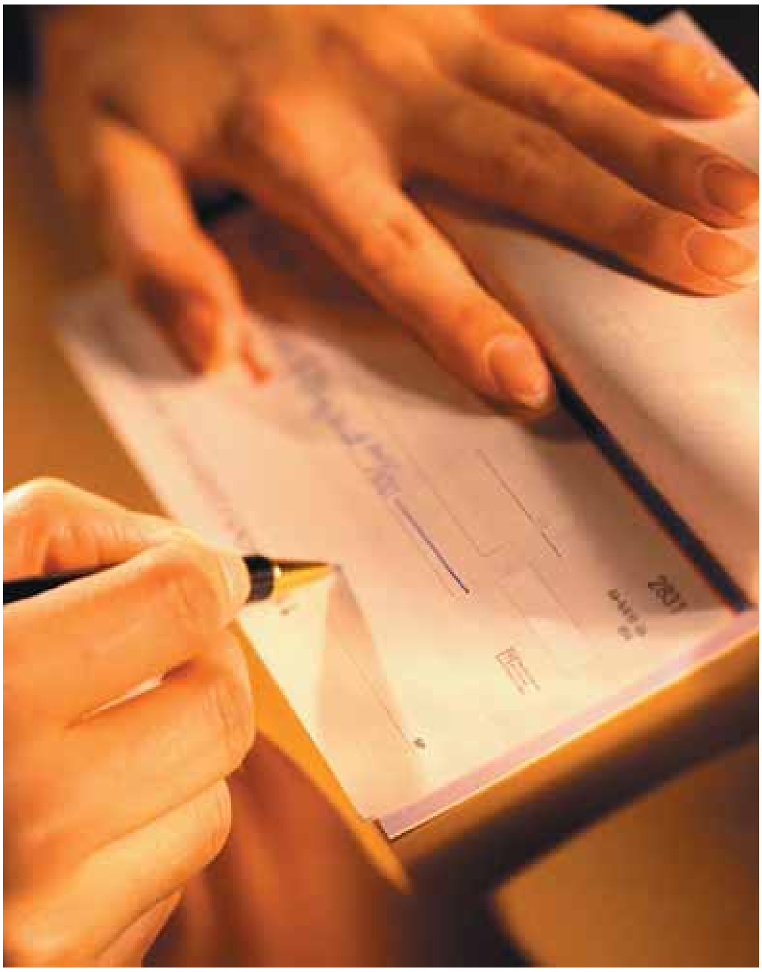
Controlling your cash

Margins in the hotel industry can be tight and in the current climate, cost control should be a priority. *Tina Buchanan* discusses how Sage Business software can help your business.



Management of cash flows in any business is important – no less so than in the hotel industry where margins can be tight and cost control a priority. The current state of the economy makes this even more important, so how can Sage Business software help?

A company's working capital consists of the amount of money owed to and by the business combined with stock held and bank and cash balances. Having up-to-date knowledge of the working capital is critical to managing cash flows.

By using Sage to record sales and purchase invoices, together with the bank transactions and by keeping records up-to-date and reconciled, it is possible to obtain an accurate understanding of the amount of cash available to the business. It will then be possible to see, at a glance, the amounts owed to, and by, suppliers and customers. This will help management decide which customers to chase and which suppliers to pay.

With correct procedures in place, the purchase order processing module within the Accounts Professional version of the software can be useful to control purchasing within the business. This module allows authorisation of purchases, checking of goods received and the ability to check the accuracy of purchase invoices received from your supplier compared to purchase orders.

Similarly, any business carrying a large amount of perishable stock will want to keep tight control of wastage and stock levels held within the business. The Sage Business suite has a Stock Management System included in the higher versions and providing it is set up correctly and regular stock takes are taken to verify records held, good control of stock levels can be obtained.

Sage software starts from £115 plus VAT and we can help install it, set up the appropriate systems and procedures and train your staff, if required. Should you wish to discuss how Sage can assist you gain better control of your cash then please contact your local Johnston Carmichael office for an informal chat.

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Time to tackle the crunch

The smoking ban, supermarket alcohol prices and the tightening of consumer spending have taken their toll on the hospitality and leisure industry in recent years. *Matt Henderson* addresses how to stay afloat in the current climate.

Hotels

One of the effects of the 'credit crunch' is that many businesses are looking for ways to cut costs. This is good news for budget hotels as they might be able to better serve the business travel sector. Those budget hotels with conference facilities, meeting rooms and leisure facilities might be able to increase business-related occupancy rates. Another factor is that UK short breaks – even in competition with budget airline destinations – are likely to be more attractive given the weakened purchasing power of sterling in the Euro zone. There are maybe some interesting opportunities, even in these difficult times, within the hotel sector.

Financial success for hotels is largely down to the ability to meet property costs, rent or lease payments, occupancy costs and – not least – finance charges. If contraction of a hotel business due to a downturn is needed then it is usually a problem. Hotels have a high fixed costs infrastructure and so they cannot readily respond to a reduction in demand in the same way that other businesses can reduce the supply to their customers. Some hotels offer very limited alternative uses, and in any event, local authority consent for change of use can be difficult to obtain. So there are real problems that face any hotel that is unable to find a way through difficult financial times.

However, aside from looking at serving business travel or UK short breaks, hotels might consider other ways to improve their finances. They could sublet the bar or the restaurant, or subcontract the entire food & beverage operation. Outsourcing of the housekeeping or laundry services might be a possibility. In this way costs can become variable on the number of rooms serviced. Labour costs can also be cut if staff are trained to do more than one job within the hotel.

In difficult times there is a temptation to delay property maintenance expenditure. This is not advisable as keeping the property in a good state of repair is crucial to maintain asset value, which in turn supports secured lending.

Public Houses

Just when some pubs have got over the effects of the smoking ban they now have to deal with increased home consumption of beer and the tightening of consumer spending due to the 'credit crunch'. Declining turnover is likely to continue for small "community" pubs, and so the demise of the traditional drinking pub is likely to continue. The worst problems will be faced by the small traditional pubs that have no catering or suitable space outside to accommodate smokers.

The pubs that do survive will have broadened their customer base or introduced new goods and services. Perhaps they will have adapted for competitively priced food, and an improved selection of drinks, or maybe they will offer live entertainment, special promotions, or the screening of sporting events. They might have changed by offering cocktails, wines and bottled beer to appeal to affluent young professionals.

To be profitable any public house must be well managed. Many publicans have little or no business training and this can lead to inefficiencies and lower margins. Margins can be adversely affected by a pub being tied to a

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supplier, so it is important to consider the overall financial implications of losing the independence of a free house when entering into "advance of discount" arrangements with a particular supplier.

Control over cash and stock is imperative for a pub to make money. The technology used at the point of sale is therefore important. A good system will allow a server to remain at the bar as a food order is relayed to the kitchen. It will also record the sale of individual items which makes stock reordering easier. Electronic point of sale systems can highlight the level of takings, and the level of corrections and voids being made by particular staff members and this greatly assists the efficient management and control of a pub business.

It is likely that the pub sector will continue to contract. Some hotels might also find themselves in a very difficult financial situation. For some of these businesses closure might be the sensible answer when all is considered. That might mean selling the building for residential development. Some pubs and hotels will close and the others will evolve to provide customers with what they actually want.

To optimise the outcome for a business that is either exiting the sector, or is looking to improve its business, specialist business recovery advice is best sought before it's too late.

Coping with the new VAT rate

The impact of the cut in VAT from 17.5% to 15% may only have a marginal impact on spending but it will leave many businesses, especially retailers, facing a serious logistical exercise and potential accounting system challenges.

Small business owners, accountants and other VAT registered businesses have had to decide what to do. Many businesses feel it is not worth the 'menu' costs of amending price lists, labels, catalogues, websites and other promotional materials, particularly because the rate change is only temporary. The result is that the rate cut will not be passed on to consumers.

One of the benefactors of the change is the financial sector and other businesses unable to recover most of the VAT on their costs. The costs of the change will be felt particularly by small businesses which do not have large accounts departments to manage the rate cut. Mistakes may be amplified by accounting systems which have not had to cope with a VAT rate change before. To dispel such fears HMRC have stated they will adopt a 'light touch' to mistakes made on the first VAT return after the changeover and, we hope, the change back to the higher VAT rate when it happens in thirteen months.

Flat Rate Scheme users will see a drop in the value of VAT inclusive receipts. HMRC has since introduced a reduction in the flat rates from 1 December 2008 for most industry sectors and, as a result, businesses on the scheme should once again decide whether it is still in their interests to remain in the scheme.

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Immigration: getting your 'rights' right

Alessandro Riccomini stresses the importance of ensuring both employees and employers are following the rules.

It is a well known economic fact that employers need to fill vacancies and the use of migrant workers is one solution. Many organisations, large and small, are increasingly contacting us to discuss the tax and NICs implications of employing someone from outside the UK.

There are various issues to be aware of such as pitfalls surrounding casual/part-time workers, tips/service charges, accommodation, uniforms, transport between home and work and the national minimum wage; however, there is a primary key issue.

Changes to the immigration system from 29 February 2008 have had a significant impact on employers in terms of their recruitment and employment procedures and practices. Further changes will be made during 2009. Work-based categories for eligibility to work in the UK will be replaced with a points-based system. Broadly speaking, these changes can be summarised as rules surrounding permission for foreign nationals, other than those of the European Economic Area countries and Switzerland, to work in the UK and an employer's responsibility to prevent individuals illegally working for them. Essentially, these rules revolve around where the individuals come from and the purpose of their visit. In order to prevent an abuse of these new rules, employers that illegally employ migrant workers face a range of punishments such as civil penalties from a maximum of

£10,000 up to criminal prosecution. They could also run the risk of being refused permission to recruit such workers in the future. At the same time, migrant workers without permission to be in the UK could face criminal prosecution and/or deportation in the most serious of cases.
Quite apart from the threat of a substantial fines, the potential loss of staff creates the very problem that the use of the migrant workers seeks to resolve in the first instance.

You might rightly ask why an employment taxes specialist is covering this type of topic. The reason is straightforward. In recent years, the profession has seen the use of the PAYE system to deal with all types of non-tax and NICs issues such as tax credits and student loans. It seems logical to expect that HM Revenue & Customs will take more than a passing interest, during their compliance visits, in the type of workers used by employers and make referrals to the immigration services.

Furthermore, there have been a number of recent employment law cases that dealt with whether a worker supplied by an employment agency could be classed as an employee of the end user for employment law purposes. The most recent case suggests this is unlikely to apply. However, I would strongly recommend you do not take any unnecessary risks in this area and ensure that any agency you use has a contractual obligation to check the immigration status of any migrant workers.

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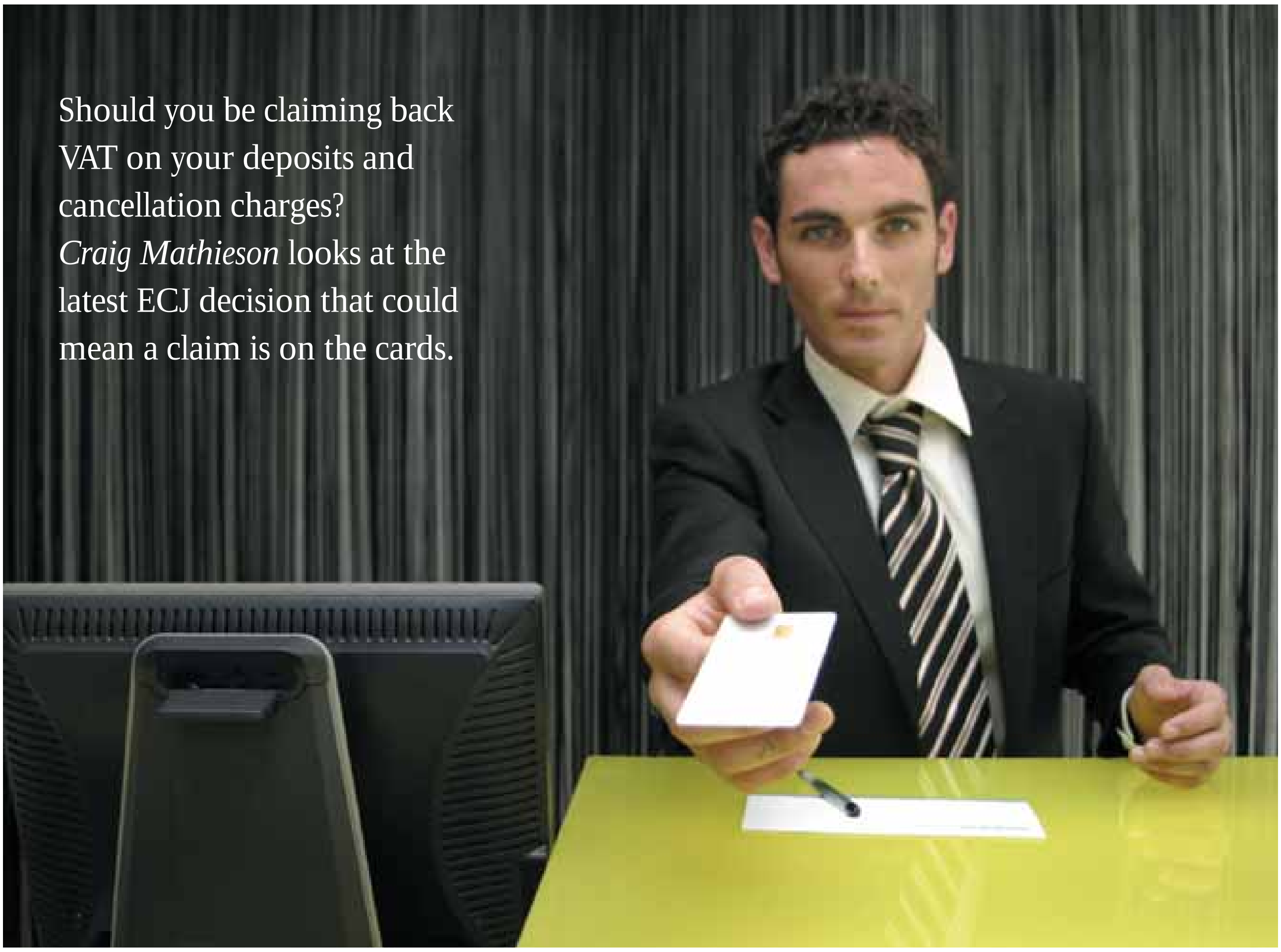

Should you be claiming back VAT on your deposits and cancellation charges? *Craig Mathieson* looks at the latest ECJ decision that could mean a claim is on the cards.

Paying too much VAT?

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Good news from Europe! A recent European Court of Justice (ECJ) decision has confirmed that hotel deposits or any cancellation charges retained by a hotel or restaurant when the guest does not turn up is not subject to VAT.

The reason behind this is that the payment is seen as compensation for the hotel/restaurant's loss rather than payment for services. HM Revenue & Customs (HMRC) agree that a hotel commences to provide hotel services at the point when a reservation is made and as a result VAT must be accounted for on receipt of the deposit. However, if the guest never turns up, the retained deposit is then seen as compensation and the VAT paid over can then be reclaimed. Please be warned, this HMRC policy doesn't extend to guaranteed reservations which are seen as a taxable supply no matter what happens and as a result, HMRC expect you to account for VAT on such payments when they are received.

My advice to you is, check your records, if you have overpaid VAT make a claim as soon as possible. Remember this can be back dated for the last three years.

At the same time, it has to be remembered that deposits are collected by many businesses in varying circumstances. Therefore opportunities may exist to recover amounts of overpaid VAT, or to review the existing deposit arrangements to see where they fall within the latest ECJ decision. If you have any questions, please contact a member of our VAT team.

Don't delay for as mentioned above you cannot make a claim if more than three years have elapsed since you initially paid the VAT.

Improvement benefits

New rules on tax relief introduced by the Government came into effect in April 2008. *Gillian Cardwell* talks you through the new allowances.

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As the impact of the credit crunch and the weakening of sterling against the euro hits the householder, opportunities exist within the hotel sector to attract new home grown visitors and now may be the time to improve facilities for these new consumers.

However, before embarking on a large capital spend and anticipating tax relief for money spent, be aware that the Government introduced new rules which came into effect after April 2008 regarding Capital Allowances. There are a number of changes which will have an impact on your business.

Hotel Allowances

The new rules will see Hotel Allowances being gradually phased out and being totally abolished by 2011. The scrapping of these allowances will not only affect any new projects but also expenditure completed before 1 April 2008.

Integral Features

A new category of 'integral features' is introduced from April 2008. This expenditure will attract 10% tax relief which previously may have attracted tax relief initially at 50% in the year of expenditure followed by 25% thereafter. HM Revenue & Customs have provided a prescribed list of items falling into the 10% category including:

- Electrical systems (including lighting systems)
- Cold water systems
- Lifts, escalators and moving walkways
- Space and water heating systems

> 'You should ensure that allowances have been maximised and possibly make a retrospective claim under the old rules'

The cost of replacing the 'integral features' (where either the whole, or more than 50% of the integral feature is replaced in a 12-month period) will now only qualify for tax relief at the new 10% rate. A revenue deduction can no longer be claimed for this replacement expenditure. However, on a more positive note, some of these items would previously only have obtained the 4% hotel buildings allowance.

Annual Investment Allowance

Another change is the scrapping of the 50% first year allowance on plant and machinery. It is being replaced with an Annual Investment Allowance. This new allowance allows the first £50,000 of expenditure on plant (including integral features, fixtures, fittings, furniture and equipment) to qualify for a 100% allowance with any excess above £50,000 receiving 20% or 10% relief.

So what do I do now?

These changes are fundamental to the hospitality and leisure sector. As the area of Capital Allowances is complex, many property owners may potentially lose thousands of pounds as a direct result of under claiming. It is important, when commencing a new project, that the expenditure is carefully analysed to maximise the capital allowances available to the business.

Changes to Capital Allowance rules provide a window of opportunity to review historical capital expenditure. You should ensure that allowances have been maximised and possibly make a retrospective claim under the old rules.

There are also generous tax breaks for investment in 'green' assets. There is 100% tax relief on environmentally desirable assets which are seriously worth considering when replacing existing ones.

The key to success is your people

The importance of protecting your business's greatest asset should not be overlooked says *Scott McDonald.*

Whether you are a sole trader, a new-start business or an established business you will no doubt understand the need to protect your premises, contents and vehicles. However, your business could be overlooking the protection of its greatest asset, its people. The importance of protection for a small business is just as great as that for a large company.

The unwelcome fact is, without certain key people your business could suffer serious financial loss or cease trading altogether.

However, you can take steps to safeguard your business against the affects of losing key people through critical illness or death. In this article, I will explain how it is possible to cover your business for:

- Key Person Protection
- Share Protection/Partnership Protection
- Business Loan Protection

Key Person Protection

In your business there will be a few individuals who make a major contribution to your profitability. Often, an individual's value to the business will be reflected in their remuneration package. This is usually a good indicator when you are trying to identify the key people within the business.

The loss of a key person can lead to the business suffering from some of the following:

- **Loss of profits**
  Loss of detailed knowledge/expertise necessary to run the business
- **Loss of goodwill**
  Problems in securing finance for new ventures, and; The need to recruit or headhunt and train a successor

Key Person Protection is life cover taken out to provide financial protection against problems like these. It is designed to give the company a cash injection if the key person covered dies or is diagnosed with a critical illness (provided that option is chosen).

Benefit levels are agreed at the outset and are usually guaranteed, based on multiples of salary, profits or the individual's contribution to profitability. There is no cash in value at any time.

Share Protection/Partnership Protection

The loss of a shareholding director or a partner can have a huge potential impact on the success of a business. Share protection can be designed to provide a sum of money to the remaining shareholder(s) if a business partner or shareholding director dies or suffers a critical illness (provided that option is chosen).

The issues that may affect a business if a shareholder or partner dies may include:

- The surviving business shareholders or partners having to re-allocate funds set aside for other purposes, so they can purchase the deceased's interest.
- The possibility of the deceased's interest in the business passing to beneficiaries who don't have the necessary skill and experience to make a worthwhile

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contribution to the business, or who would prefer a prompt cash payment.
- The possibility of the need to find a third party who can provide the cash to buy out the deceased's estate.

Share Protection cover is normally arranged by taking out life insurance, in conjunction with a suitable share purchase arrangement. These contracts should be made with business partners as individuals on an own life basis. The contracts should be made to the value of the individual's share for the benefit of the other business partners/shareholders.

The policies will usually be placed into a flexible business trust. The set-up of share protection requires attention to detail, as it is important to ensure there is no conflict with other business partner or shareholder arrangements in place.

Business Loan Protection

When a company takes out a loan, it needs to be sure the repayments can be met, no matter what happens to the business. By taking out Business Loan Protection, a company will have cover against events that could adversely affect its ability to repay its borrowings.

Loan protection is normally arranged with a term assurance policy. Before securing the funds, a business will often be told that Loan Protection (and its assignment), is a condition of arrangement with the lender. The reason for this is security.

If a key person suffers a critical illness, lenders know that a business may struggle to carry on with day-to-day operations and make timely repayments.

Confirmation will need to be provided that the loan has been drawn down with a request to commence cover, and Loan Protection will then provide cover to the value of the outstanding amount. A fixed term policy is put into place for the duration of the agreement.

This article is intended only to give a brief outline of areas that business owners should be looking at to make sure their business can continue in any unforeseen eventuality.

Directors and business owners cannot afford to say that 'it will never happen to us'.

The above article is based upon Johnston Carmichael Financial Services Ltd's understanding of current legislation. Johnston Carmichael Financial Services Limited is authorised and regulated by the Financial Services Authority.

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Hospitality and Leisure News

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