WARR & CO
CHARTERED ACCOUNTANTS

A Guide To Financial Planning For
PARTNERSHIPS

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The Importance of Financial Advice

Having entered into business as a Partnership, aside from obviously striving to be successful, there are endless different matters that will be encountered and make demands on time. Amongst these are the many financial planning issues, both on a personal and a business level.

Find the time

NHoearly always, individuals that run successful businesses find that time is precious and generally very limited. After all there are only 24 hours in a day and 7 days in a week. When striving to run a business effectively and profitably, setting time aside to broach financial planning issues is often put lower down the list of daily priorities. Where the inclination or motivation exists to do so, there is the time to be set aside to undertake research. However, it need not be time consuming. Even a complete overhaul can be broken down into a series of smaller steps.

Understand the cost of poor planning, understand the benefits of good planning

Failing to set aside the time or financial resource is often a false economy. We regularly encounter clients that continue to pay premiums to unnecessary or uncompetitive insurances or invest into products that deliver sub par performance. However, those same clients would be reluctant to allow a poorly performing employee or inefficiencies in their business model to reduce productivity or have a negative impact on profit.

Whilst proprietors are very focused on the day to day activities of their business, the need to address financial planning should be considered an equally important part of their business plan. Consider it another fundamental business process. Planning effectively can ensure that resources are working as hard as they are.

Why seek the assistance of a qualified Independent Financial Adviser (IFA)?

First and foremost, an IFA can do the ‘donkey work’, overcoming the first hurdle which is that of limited time. Once a client relationship is established, they can work behind the scenes to bring together comprehensive information regarding a client’s existing financial arrangements. Together with detailed record keeping, this ensures that ongoing advice can be a painless affair.

The Importance of Financial Advice (ctd)

Secondly, an IFA can provide a detailed assessment of an existing provision. This outlines the cost of ineffective financial planning and conversely the benefits of sound plans where these exist, thus instilling confidence where appropriate.

Whether the adviser is remunerated by commission or fees, these are worth paying as the benefit of good financial planning often outweighs the cost.

Why Warr & Co

Recognising that clients seek financial planning advice that works cohesively with accountancy & tax advice, Warr & Co set up a financial planning division in 1997. We have been offering independent financial advice that we believe to be complimentary to the accountancy and tax advice we provide our personal and corporate clients.

Regulated directly by the Financial Services Authority and acting as Independent Financial Advisers (IFAs) and Independent Mortgage Brokers, our Financial Services Partners, Jeff Crewdson, Steve Prosser & Chris Raggett undertake financial planning on behalf of a wide range of clients. These include sole traders, partnerships, professional practices such as solicitors and fellow accountants, and small to medium Limited Companies. Through a combination of expertise and various software systems, we believe we have the ability to provide informed advice across a wide range of financial planning areas.

We are proud to convey that we already have one Chartered Financial Planner and our other two advisers are presently working towards that status through a rigorous course of professional examinations.

Treating Customers Fairly (TCF)

Warr & Co. accepts TCF as an integral element of our financial services work ethic and helps determine the success of our firm. The interests of our clients are paramount and central to our business plan. We therefore strive to perfect our service standards and continually improve the transparency with which we act for our clients.

This will be achieved by way of the on-going review of our work practices and advice processes so that we have a working model that is fair to all our customers, and be proved to be so.

In conclusion, we believe we offer a highly effective combination of a professional approach together with a friendly attitude that ensures the whole process of financial planning need not be considered a daunting affair.

Review Existing Provision

We consider it imperative to review existing financial arrangements. The financial services market is constantly evolving. Whenever we undertake planning for a client for the first time, before taking steps forward, we feel it a necessity to firstly look back. Here are just some of the reasons why one should not assume that, because these areas of financial planning have been addressed, there is no need to review them.

Financial Protection

Adequacy – just because sufficient insurance was effected last time around, it is unsafe to assume that it remains so now. Even allowing for no change in circumstances, inflation will likely have eroded the true value of any provision.

Smoker status has changed – thousands of people give up smoking each year. After a period of just 12 months, many insurers consider an individual to be a non-smoker. The differential between smoker and non-smoker premiums can be substantial.

Medical status has changed – just because one insurer determined a client to be a poor risk, it does not mean that a rating need continue to apply. The condition may have been temporary or the insurer may have had a specific view that other insurers may not embrace.

Cost – the cost applied a few years ago may not be the true cost today. If nothing more, a review should be undertaken to determine the competitiveness of the premium being paid. In particular regard to life cover, the cost of this has reduced over the years due to improving mortality experience and increased market competition. There can be a wide discrepancy between a competitive provider and one who is not.

Pensions & Investments

Adequacy – is current provision on track to reach set financial objectives? Is the funding level sufficient?

Attitude to investment risk – are investments in keeping with the desired investment approach? Is the asset allocation suitable?

Performance – are funds performing to expectations?

Personal Provision

This is generally a starting point when addressing this area of planning and generally encompasses 3 different types of cover; income protection, life cover and critical illness

Income Protection – designed to replace earnings in case of an individual being unable to carry out their occupation, due to long-term ill health or disability. Particularly important is the insurers' definition of earnings and of disability, i.e. own occupation, any occupation, etc.

Life Assurance – cover to provide financial stability in the event of death. This may be utilised to fund the redemption of a mortgage or financial liabilities or to provide capital or income to meet expenditure. A key point of review is to replace lost death in service benefits enjoyed from a former employment. There are a variety of structures available to suit different needs.

Critical Illness – Designed to primarily pay a lump sum in the event of contracting any one of a wide range of critical illnesses such as cancer, heart attack, stroke, paralysis, blindness, and brain tumour. A good policy covers in excess of 25 serious illnesses.

Key Planning Provision ~ Financial Protection

Business Provision

Debt protection – This is often effected upon the instruction of the bank with a view to covering overdrafts and commercial loans and is usually effected on the Partners.

Key person cover – Key person insurance is effected where the long-term absence through accident or ill health, or death of an individual, will have a severe detrimental effect on the profits of the business. It is effected to cover the cost of replacing the intellectual or physical skills that contribute to the success of the business and the financial impact the loss of such skills would create. Clearly such cover may be considered for Partners, as they are often founders of a business and are in essence 'what make the business tick'.

As the situation arises, key employees should be protected, to provide the business 'breathing space' and the ability to endure the downturn in profits that could ensue. This allows time to seek out the right replacement and to cover recruitment costs, which alone can be quite high.

Partnership protection – with appropriate legal assistance, decisions should be made regarding the basis of valuation of the shares of the business and how the business would be restructured in the event of the death, ill health or retirement of one of the Partners. This would usually be contained within a partnership agreement, which also contains provisions for how the business is run and the obligations of each Partner.

In regards to the death of one of the Partners, provision should be effected to either: -

compensate the deceased's estate for the loss of goodwill or share of assts if this is cancelled or absorbed by the business,

or

where goodwill remains and / or there are business assets, to enable the remaining Partners to make good this to the deceased's estate. This would also apply to any capital account that may have been built up.

Key Planning Provision ~ Financial Protection (ctd)

In the case of the latter, a cross option agreement (also known as a double option agreement), rather than a buy & sell agreement, should be effected. This is worth considering, as the former does not constitute a binding contract for sale. Because of this, any Inheritance Tax Business Property Relief is protected. An option to sell the deceased's shares is granted to the executors and an option to purchase the shares is given to the remaining Partners. Either side may exercise the option, which is then binding on the other party.

The purchase can obviously be financed either by self-funding out of business assets or cashflow, or by raising debt. If either of these are not viable or preferable, a highly cost effective alternative is to effect life assurance in respect of each Partner.

Effective planning in this area avoids shares being sold to external parties or a spouse or partner of the deceased being able to participate in the running of a business.

In conclusion, the key benefits of a partnership protection arrangement are certainty and control. Certainty comes from knowing that the business can finance a prospective purchase and that the business can survive the death of a Partner. Control is provided as the surviving Partners can decide whom they continue to run their business with.

Group risk – a key constituent to the growth or prosperity of a business is the employees. In order to attract and retain good staff, provisions such as sick pay entitlement, death in service (life cover), private medical insurance (PMI) and critical illness are appropriate as part of a voluntary or standard employee benefit package. These can of course be self-insured by the business, although this may not be desirable, as this can leave it exposed to a substantial liability. Therefore, it maybe preferable to insure and provide the benefits by way of group risk arrangements.

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Key Planning Provision ~ Pensions

Existing Arrangements

An important starting point is to investigate existing policies. As a consequence of new legislation that became effective 6th April 2006, it is appropriate to establish the structure of any existing provision. This can strongly influence the way in which future planning is carried out.

A number of issues arose out of the new legislation, the impact of which should be assessed as a priority.

Where pension commencement lump sum (PCLS), formerly known as tax-free cash, under the old rules exceeds the 25% limit now permitted under the current pension legislation, there is the opportunity to protect this. However, due care should be taken as this is a complex area of planning and one which also has time constraints attaching to it. Upon inception of the new rules, the Government allowed a 3-year time period, i.e. until 5th April 2009 for higher entitlements to be recorded.

Furthermore, for those with higher levels of benefits, which are in excess of, or approaching, the Lifetime Allowance (£1,500,000 2006/2007, £1,600,000 2007/2008), we would urge that further planning is undertaken with caution. Where such pension funds have been accumulated, primary and enhanced protection planning also be considerations.

Regardless of legislative changes, the ongoing performance of pensions is a fundamental point of consideration, to ensure the provider / fund manager is providing satisfactory returns and the asset allocation still meets the clients requirements.

New Provision

For many, the new pension rules now permit funding to a pension to a much greater level. Thus, the decision regarding which pension wrapper to utilise has never been so important. The personal pension wrapper has become more prevalent due to its administrative simplicity. However, the utilisation of a Stakeholder or Self-Invested personal pension, or perhaps a hybrid version, is an important area upon which to take advice.

Equally, advice should be taken with regard to funding levels to ensure objectives are met.

Key Planning Provision ~ Pensions (ctd)

Business Provision

As with employee protection provision, a key benefit to attracting or retaining good quality employees is an appropriate pension arrangement.

Whether an employer chooses to fund it or otherwise, a minimum requirement where the number of employees, including partners and part timers, is 5 or more is to provide access to a Stakeholder scheme. Failure to ‘designate’ a registered Stakeholder scheme when required to do so could lead to financial penalties of up to £50,000 for the business and fines of up to £5,000 on individuals i.e. partners.

Certain employers will be exempt from such a requirement if they offer an occupational pension scheme or a group personal pension that meets certain conditions.

It is our experience where non-employer sponsored Stakeholder schemes are set up, the take up rate is very poor. In many instances, this is little more than a shell, with no actual members.

The Government’s review of future pension provision is almost complete. As such, there is every expectation that the legislation shall be passed to introduce Personal Accounts, as they are presently known. Whilst not ‘compulsion’ in the strictest sense of the word, employees will, unless opted out, become members of the scheme through auto-enrolment. Even where opted out, employees will be opted back in after 3 years. It is intended that the scheme be funded by a 3% employer contribution (to be phased in) and 4% employee contribution, with a further 1% in tax relief.

It is intended that the legislation becomes effective from 2012 and like Stakeholder schemes, exemption shall be granted providing existing schemes meet specified criteria.

With this in mind, it is perhaps appropriate to begin the process of effecting a suitable pension scheme with a view to phasing it in, thereby alleviating the financial impact to both the business and the employees.

Other Planning

Whilst not intended to be an exhaustive list, we hope we have provided a useful guide to the key areas of planning which business proprietors operating as a Partnership may wish to consider. However, without going into detail, listed below are some other areas with which we may be of assistance.

Mortgage Planning

Residential purchases and remortgages

Investment property purchases and remortgages

Commercial funding

Personal Investment Planning

Onshore and Offshore Bonds

Individual Savings Accounts (ISAs)

Unit trust / OEICs

Inheritance Tax (IHT) Planning

Wills / Trusts

Provision to meet liabilities.

Retirement Income Planning

Annuities

Phased retirement / Unsecured Pension (USP)

Regular Reviews

If not derived already from earlier comments, the most important part of any plan is the need to regularly review ones financial affairs. Circumstances and situations change and needs and requirements evolve as time goes on. This can be as a result of a multitude of different changes; earnings increase, earnings decrease, needs increase, needs reduce, optimistic attitudes become more cautious, etc, etc.

Whilst there is no hard and fast rule, we would expect such reviews to take place at least annually, perhaps even more regularly. And these need not be formal meetings either, with email and telephone providing more than adequate lines of communication.

Warr & Co is regulated in the conduct of all financial planning business activities by the Financial Services Authority (Reg No. 169591). Whilst the information detailed here is updated regularly to ensure it remains factually correct, it does not in any way constitute specific financial advice and no responsibility shall be accepted for any actions taken directly as a consequence of reading this. If you would like to discuss any of the points raised and / or engage our services in providing independent financial advice specific to your personal circumstances, please feel free to contact Jeff Crewdson, Steve Prosser or Chris Raggett on 0161 477 6789 or email us at finserve@warr.co.uk.