Family Business Insight

2018




ArmstrongWatson®

Accountants, Business & Financial Advisers

Image by CN Group
David Hayton - Carlisle

Contents

Welcome

Welcome to the third annual Armstrong Watson family business survey report and our insight into the opportunities and challenges faced by family businesses across the UK.

Family Businesses are the lifeblood of our communities, and with a record response to our research, the results provide us with a unique look into the inner workings of arguably the most important sector within our economy.

Last year Armstrong Watson celebrated 150 years of supporting, advising and protecting clients and, just as our firm has evolved during this time, we recognise that it is essential to understand how family businesses develop during their life cycle. By analysing current thinking and realising the concerns and aspirations of family businesses, we are able to help achieve prosperity, ensure financial stability and perhaps most importantly, increase longevity, securing futures and providing peace of mind.

Paul Dickson, Chief Executive

Introduction

Welcome to the 2018 Armstrong Watson Family Business Survey.

In the course of contributing to this survey, I have been privileged to meet and learn about a range of family-led enterprises that are engaged in fantastic activity across the United Kingdom. It strikes me that the values, the trust, honesty and support that you find within a family unit are perfect ingredients for many kinds of successful activity. When these elements are built into the operations and systems of a business, it seems to me that the chances of business success increase.

Of course getting this structure "right" isn't simple. The family dynamic can sometimes make life a bit more complicated than for other businesses, especially as greater numbers of family members become involved. Or when there are changes imminent.

There are some big issues in this survey, many of them linked to change. Our hope is that this report will provide equal measures of food-for-thought, reassurance and challenge.

The analysis has been compiled by a range of experts from within our organisation and network. We want you to take that and use it to the best effect in your organisation.

I would like to express a huge thank you to all of the businesses that responded to this survey. At Armstrong Watson we have a core purpose "to support, advise and protect companies and individuals for the long term". This Family business survey is a very important exercise in our commitment to that purpose. It wouldn't be possible without your time and enthusiasm. Thankyou.

The results from this survey help us to know what you think. Please contact your local Armstrong Watson office if you'd like to discuss any of these issues further, or learn about events in which you can discuss the topics in the company of other business owners.

Nick Palmer
Strategic Business Adviser

Nick Palmer works in the business advisory arm of Armstrong Watson. Prior to joining the firm he ran his own business for a period of ten years, and managed someone else's family business for 2 years. Having an understanding of the challenges facing owner-managed, family businesses, Nick is well-placed to support the key decision makers as they try to balance the big and small issues of being in business.

Nick works across the North of England and South of Scotland helping companies to identify and build the best versions that they can be.

Executive Summary

The Armstrong Watson Family Business survey has benefitted from a strong response rate since the first report in 2016. 2018 saw a 13% increase in overall responses, taking the completed survey number to just under 500.

We are very grateful to everyone who took time to complete the survey; the increasing numbers of respondents, tracked over time, help to deliver "statistical relevance" that validates any trends and the reassurance those trends give to participants and readers.

We have also increased the size of the survey this year. There are a greater number of questions than last year, in part to allow us to track certain topics on a longitudinal basis, and in part to reflect the changing business landscape. For example this year's survey included new questions on GDPR, talent recruitment and digitalisation which we hope will add relevance to our audience.

We were keen to look at key trends and future proofing. The questions we posed were deliberately set to challenge thoughts on preparation. To this end, there are a number of interesting results to appear from the survey and some serious concerns highlighted as to how equipped family businesses really are for the imminent changes ahead, both within their own business life cycles and the economic climate they operate within.

Just under
500
respondents

Up from
last year by
18%

Contributors

We are very proud to have an experienced team of advisers who have taken the time to analyse the survey findings and applied their specialist knowledge to reflect on the results. Their commentary offers an insight into current thinking, looks at developing trends and provides direction on many of the areas examined. If you would like to speak to a member of the team about any of the issues discussed, please refer to our contact details at the back of this report.

Karen Thomson,
Payroll Director

Karen has worked in the HR, finance, pensions and payroll industry for most of her career, focussing on the payroll and pensions industry for the last 20 years. She sits on a number of government consultation forums representing employer and client views.

She is qualified to Masters level and lectures for the Chartered Institute of Payroll Professionals (CIPP) in partnership with Derby University for the Masters programme and is one of only 10 people to be appointed as a Chartered Member of the CIPP. In addition she is also a qualified tutor for the CIPP teaching their Foundation Degree in Payroll Management.

Whether a business is a customer now or not, she values them. Karen insists that no-one is treated as a number, only as a person. Customer service is at the forefront of everything she does. She uses the knowledge she has to help employers keep their employees happy, by providing an excellent payroll service.

Sally Jones,
Accounting Senior Manager

Sally joined Armstrong Watson in 2003 and qualified as a Chartered accountant shortly after. Throughout her career she has supported entrepreneurial start ups through to large, well established businesses.

As part of her role, Sally supports the independent retail sector. Her passion and enthusiasm for hospitality and leisure means she builds close relationships with her clients and also with the wider network.

Taking time to get to know her clients, Sally gains an understanding of their challenges and goals and gets great satisfaction from providing solutions in a friendly and supportive environment.

Emily Harrison
Tax Consultant

Emily joined Armstrong Watson in 2008 in the Skipton office. She qualified for membership of the Association of Taxation Technicians in 2011, achieving the highest mark in the country in her sitting for the Business Compliance paper and received the Collingwood medal in recognition of this.

She moved to the Leeds office in 2012 and qualified as a Chartered Tax Adviser in 2013. Emily now assists the tax consultants with the provision of proactive tax planning for our clients. She specialises in residency tax issues, inheritance tax and estate planning.

Olivia Rawlinson
Senior Tax Consultant

Olivia joined the tax consultancy team at Armstrong Watson in January 2018. Olivia graduated from the University of York where she studied Accounting, Business Finance and Management. She qualified as a chartered tax adviser at Grant Thornton where she was a Manager in the Tax Investigations team. Olivia has a vast amount of experience in dealing with HMRC enquiries and resolving on-going tax disputes. In addition, she has successfully prepared and submitted a number of voluntary disclosures to bring her client's tax affairs up to date.

Olivia enjoys working with entrepreneurs. Her favourite part of the job is meeting with clients to discuss their business, available opportunities for future growth and assisting with any current hurdles they are encountering.

Contributors

Nick Heaney
Accounting Director

Nick joined Armstrong Watson in September 2017 as a Director based in the Dumfries office.

Nick oversees the provision of the wide-ranging services and advice offered by the Dumfries office to the Agricultural and Rural business sectors and the wide-variety of owner managed businesses.

Having bought a smallholding in Cumbria, Nick has integrate back into the rural community of Cumbria and the South West of Scotland and applies his no-nonsense, plain speaking approach to his advice, to current and prospective clients.

A keen horseman, who show-jumped before turning to accountancy, Nick has lived in the countryside for most of his life and shows a true understanding of issues faced

Richard Askew
Partner

Richard became a qualified accountant in 2005 and has lived in West Cumbria all his life. He joined Armstrong Watson in 2006 as an audit senior and from 2008 Richard spent four years as Corporate Services Manager at Penrith. In October 2012, he became Corporate Director based at our West Cumbria office in Workington and in 2015 Richard became a partner of the firm and continues to lead the West Cumbria office.

Richard supports and advises clients across a range of industries and those in nuclear, construction and hospitality in particular, and prides himself on providing an accurate, timely and value adding service to his clients. Richard focuses on working with owner managed businesses to help them achieve their business objectives, supporting them in growing and protecting their wealth for the long term, creating lasting relationships built upon honesty and trust.

Helen Robinson
Accounting Senior Manager

Helen works closely with family owned and owner managed businesses in a variety of sectors. She takes time to get to know her clients, understand their challenges and where they want to get to. Helen works with them to achieve their goals and strives to deliver a quality service.

Having worked within accounting since 1997 and qualifying in 2005, Helen builds strong, long lasting relationships to support growth and help secure the future of business through practical and commercial advice.

Jonathan York
Director

Born and raised in Leicester, Jonathan started his career in accountancy on leaving school in 1989 and has enjoyed working successfully across a variety of different areas of business ever since.

He relocated to the North West when he got married and has worked at Armstrong Watson for over 10 years

Having trained initially in accountancy and personal tax compliance, Jonathan moved into tax on a full time basis in 2001 where he focussed particularly on trust work. He has acted for farmers throughout his career and plays a key role in our Agricultural team.

David Jones
Employment Solicitor, Myerson Solicitors LLP

David specialises in all aspects of employment law, acting for a range of employers, senior executives, and individual employees. He trained and qualified at Walker Smith Way solicitors in Chester, then Slater and Gordon Lawyers in Manchester, before joining Myerson in 2016.

David also provides advice to HR professionals, which includes reviewing and drafting a variety of employment related documents such as employment contracts, policies, handbooks, disciplinary and grievance procedures and settlement agreements. We utilised David's knowledge and experience to assist us with the analysis of our question relating to GDPR.

Respondents

Our geographical heartlands are Cumbria, Yorkshire and Scotland; these areas accounted for 78% of the overall respondents. The remaining respondents were based across the Rest of the UK.

The responses came from a good mix of sectors. Agriculture (23%) and Retail and Hospitality (19%) led the way, there were contributors from Property and Construction, Manufacturing, Motor and Haulage as well as Science and Technology. Finding no match from that list, 28% of respondents identified as "Other".

These industry figures are slightly changed from last year when 29% of respondents were "Agriculture". Retail and hospitality were listed separately last year (when collectively they accounted for 18% of respondents). But otherwise the data was consistent.

Limited Company status (51%) was the most commonly occurring company structure, with Partnership (33%) Sole Trader (14%) and LLP (2%) making the balance. Although there were some differences with last year's figures, they are not significant, and the relative numbers from these industries was consistent.

47% of respondents identified as 1st Generation family business, with 28% for 2nd Generation, 14% for 3rd and 11% for 4th generation of greater. This represents a slight change from last year where 1st and 2nd generations "scored" 53% and 15% respectively.

The average number of owners fell slightly (for a second year in succession) to a figure of 2.5 (down from 2.69 last year and an average number of 3 the year before that). As we noted last year, this figure is highly relevant to the questions relating to how an organisation plans for succession, retirement of previous owners.

The average number of employees rose in this year's survey from 19 last year to 26. Perhaps this is an indicator of economic confidence across the region? The greatest share of respondents (60%) employed fewer than 10 people. Only 3% of respondents employed more than 500 employees.

As with last year, we can make a calculation that the respondents to this survey employ in the region of 12,000 people. Using the ONS figure for average salary in 2017 (£26,730), this suggests an amount around £320 million entering the economy through these respondents. The figures for 2016 were an average salary of £26,500 across 8,000 employees giving £212 million.

Generations in Existence
1st 47%
2nd 28%
3rd 14%
4th 11%

Limited Company
51%

Partnership
33%

Sole Trader
14%

LLP
2%

Agriculture
23%

Motor & Haulage
4%

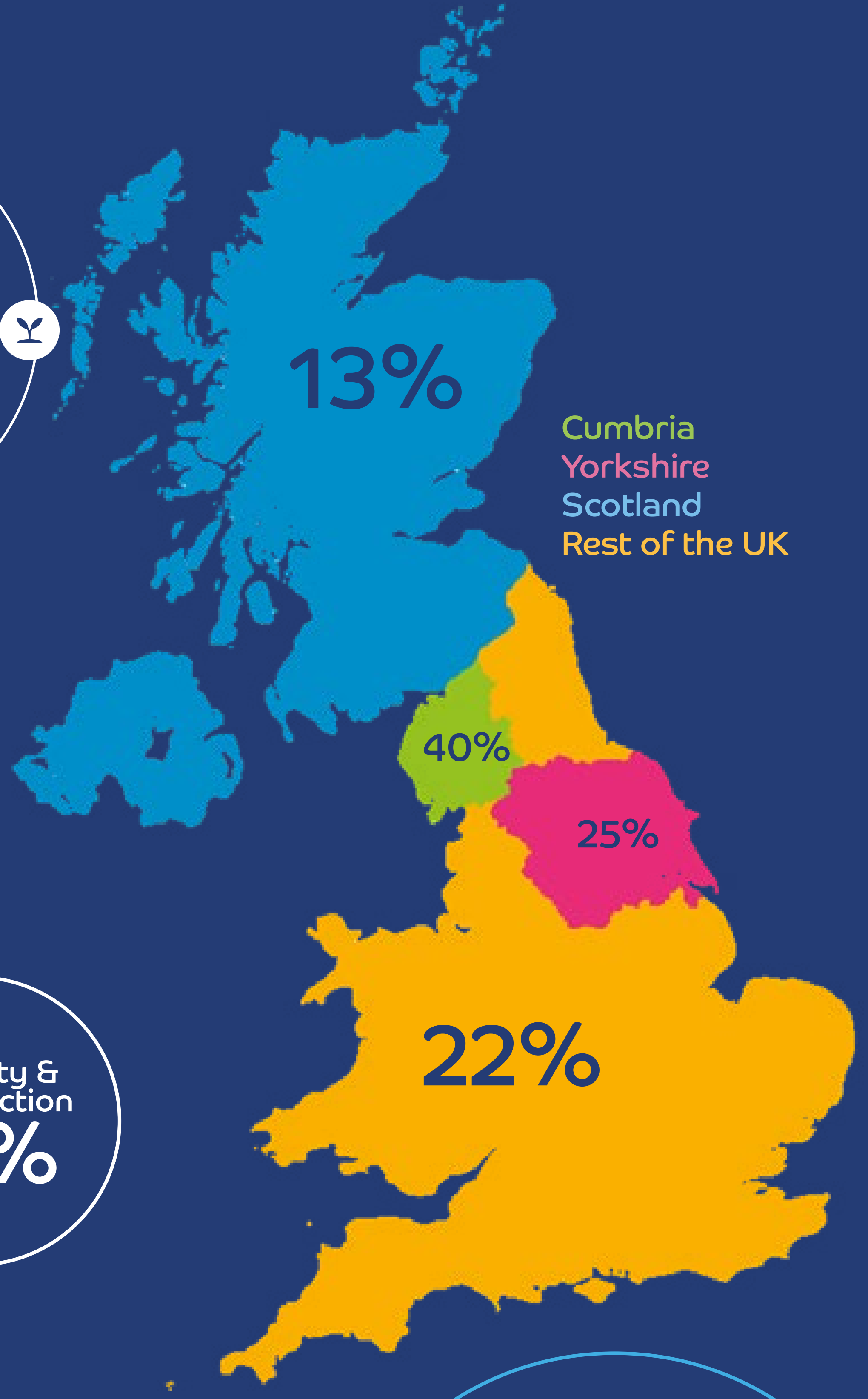
Science & Technology
4%

Property & Construction
12%

Manufacturing
10%

Retail & Hospitality
19%

Other
28%



People

Over 300 hundred businesses indicated they were 'employers' and subsequently responded to the employment related questions.

When looking at the total businesses participating in this research there was an average of 26 employees per business compared to 19 employees last year. However, looking at the specific employment areas to follow, with those who stated they employed one or more employee the average increased to 38 employees. By far the largest number of responses came from family businesses with 60% employing less than 10 employees, 37% employing 11 to 250 employees, and 3% employing more than 500 employees. The feedback from those who employ people was across all industry sectors, from agriculture to manufacturing and domestic services to name but a few. The people section also benefits from responses from different regions in the UK from Wales right up to Aberdeen in Scotland, Yorkshire, Cumbria and Lancashire.

26
Average number of Employees

Up from **19** in 2017 report

Average number of owners
2.5

People Management

How will the following considerations impact your business in the next 12 months?

Key

- P Positive Impact
- N Negative Impact
- NI No Real Impact
- X No Comment

Commentary by Karen Thomson
Payroll Director

70%

believe automatic enrolment will either have no impact or will be positive

Auto Enrolment

P 20% N 25% NI 55%

Pensions have dominated media platforms for some years now, but still there are employers who don't believe automatic enrolment impacts them; it does! As both payroll director for Armstrong Watson, and sitting on the Pensions Regulator for payroll bureau round table consultation forum, I've seen first hand how businesses are coping with automatic enrolment. As the final staging comes to an end for existing businesses, and percentage rates set to increase from April, we felt it was appropriate to ask family businesses for their latest views; so what did we find out?

With over 75% believing automatic enrolment will either have no impact or will be positive, this should be very good news for the Government and their continued endeavour to ensure people save for their retirement. For those businesses that said it would have an impact, up from 10% in 2016/17 to 20% for 2017/18, evidence suggests this will be due to the increasing costs but not only in percentage of contributions that are set to increase, but also in the administration.

For those who use a payroll bureau such as Armstrong Watson, administration costs are part of the payroll processing, as it relies on payroll data to administer correctly, but those who run their own payroll will need to ensure their systems are updated with the new increases and will face re-enrolment after three years of staging. They will also likely see an increase in queries from employees who see their deductions go up, and for those living in Scotland who might be impacted with increased tax costs, it may be too much to bear. This could potentially lead to more opting out, resulting in automatically re-enrolling in three years and so on. We will see what the results show next year as to whether the business views were on the money!

60%

think that any new changes will either have no impact or a positive impact

Changing Employment Law and Legislation

P 11% N 35% NI 53% X 1%

With more than 260 pieces of legislation directly impacting payroll - and therefore any business with employees - constant changes to payroll and employment law can have a huge impact on a family business, especially those who have to monitor it themselves! So what did our family business owners tell us?

Although the survey results show that 64% of business owners believe that any new changes will either have no impact or a positive impact, this also raises concerns. Larger family businesses have had to cope with the Gender Pay Gap legislation and should have reported their findings on their website, and all businesses will also have to cope with the new General Data Protection Regulations (GDPR).

Changes to agency workers, the GIG economy, IR35 (employment status) and of course holiday pay are still to come, amongst what will no doubt be more legislation coming through the courts. It isn't all doom and gloom of course, and those who believe changes will have a positive impact may have identified the drive of the Government to encourage flexible working, especially for working parents. The new childcare credit scheme may mean an end to salary sacrifice schemes for childcare vouchers; are you aware if you have one of these schemes, you will not be able to permit new entrants after 4th October 2018 and anyone who leaves will not be able to return to it?

I'll be covering many of these changes in our forthcoming monthly Inspired e-newsletters and via our payroll website, but whatever family businesses use to keep up to date it is important they do and, if needing help, seek professional advice.

Concern up by

10%

Last year 20% felt this legislation would have a negative impact, compared to 30% this year.

National Living Wage

P 9% N 30% NI 59% X 2%

As the media continue to discuss how businesses are struggling to retain people and offer decent pay-rises, the National Minimum and National Living Wage (NLW) can have a real impact on employer costs, sometimes numbers employed and subsequently productivity, and our survey respondents' views appear to reflect this concern.

As the Government continues to increase the NLW and also come down hard with compliance and naming and shaming, businesses are clearly concerned. Last year 20% felt this legislation would have a negative impact, compared to 30% this year. When taking into account the rise in the rate of the National Living and National Minimum Wage, along with the start of automatic enrolment for many small businesses over the last year, it may explain why it has resulted in a 10% increase on the impact this legislation will have.

Of the 59% who said they wouldn't feel any impact, these were made up mostly of less than 10 employees. When talking about pence on less than 10 employees we can understand it won't play a massive part in the bottom line, but for larger family owned businesses it will. As the Government continues to increase these rates, some under the age of 25 years may feel they are treated unfairly as their pay-rise may not match those who are paid on the National Living Wage. In addition, as the department for Business, Energy and Industrial Strategy (BEIS) looks to introduce hours and rates shown on payslips from April 2019, data will also be more transparent to HMRC. This new legislation won't impact those who have regular pay e.g. monthly salary but will impact those who only show fluctuating amounts on a payslip.

Going forward, for every hour worked the rate of pay will need to be shown. Payroll software will for the most part take care of this, but it does mean employers will need to be vigilant in ensuring they are paying the correct rates. No longer can a business pay an amount that includes X, Y and Z as part of someone's hourly rate, they will need to show items separately.

Image by CN Group
Laylocks, Skipton

21%

don't know what salary sacrifice is

9% are currently reviewing their options

53% are not considering it

14% have a scheme in place

3% no comment

Do you operate a salary sacrifice scheme in relation to pension contributions?

Despite increasing automatic enrolment contribution costs, it was surprising to see so few family businesses have a salary sacrifice scheme for pensions in place.

Too few businesses understand what a salary sacrifice scheme is to even consider one. The nuts and bolts are, employees sacrifice some of their salary in exchange for pension contributions (these must meet the automatic enrolment rules and no-one can be forced to join one), the employer also contributes and the two amounts combined become an employer contribution to the pension scheme. These are calculated before tax, thus tax relief is provided directly and National Insurance is only paid by the employee and the employer on the reduced gross salary; therefore it is puzzling as to why so many are not implementing one, or considering it. There are of course rules, for example, no-one can enter a salary sacrifice scheme if it takes their pay below the National Minimum Wage, but there will be many others that could benefit. If you do want to implement a salary sacrifice scheme and need some help, please ensure you approach a qualified professional to advise you.

54%

find it sometimes difficult to retain talent

19% do not find it difficult to recruit staff

26% find it very difficult

1% no comment

How difficult do you find recruiting and retaining new talent?

Family businesses have in the past said it is difficult to recruit good people, and with a worrying 80% of respondents in this year's report stating they find it 'difficult' or 'sometimes difficult' to recruit and retain new talent, sadly there's been no improvement over the last 12 months.

Many in the Cumbria region – particularly - have expressed concerns over what impact Brexit might have, especially in the hospitality, manufacturing, professional services and agriculture industries. Is the UK failing to invest in the recruitment of good people, providing the skills needed for family owned businesses, or is there something else causing these difficulties? With the media implying the labour force will have more influence on what they will accept in pay and conditions, this may make the situation worse if employers cannot offer what workers want.

Apprentices

We asked family businesses to share with us their knowledge and actions regarding apprentices. There are two groups of respondents; those who employ apprentices and those who do not, and for those who do employ apprentices, we looked at their knowledge of the Government's flagship apprenticeship levy scheme.

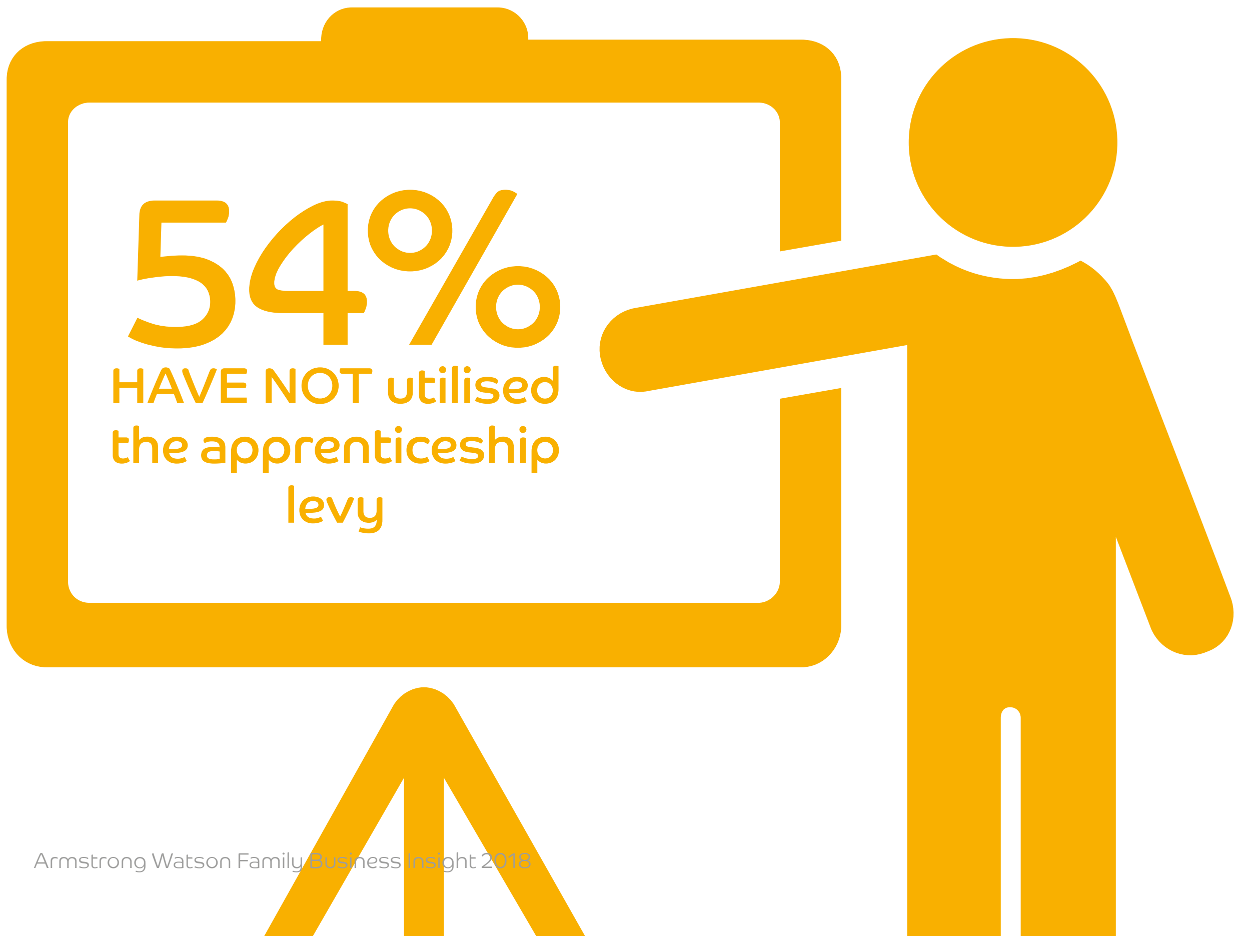
Why are so many family run businesses not employing apprentices and for those who do, why are they not using the new scheme to help them with their training costs? This is a question that is also being asked by the media and the Government, with many saying they do not understand how the scheme works, or whether they can use it. Some professional bodies are calling on the government to have a complete overhaul of the scheme as it doesn't appear to be working. So is it down to its complexity or something else? For more information on how the scheme works contact your payroll adviser or visit the GOV.UK website.

63% DO NOT employ apprentices

37% DO employ apprentices

24% DON'T KNOW what the apprenticeship levy is

43% HAVE utilised the apprenticeship levy



Digitalisation

Making Tax Digital

HM Revenue & Customs are in the process of implementing Making Tax Digital (MTD) which the Government states will "make it easier for individuals and businesses to get their tax right and keep on top of their affairs - meaning the end of the annual tax return for millions."

Some businesses will be mandated to use MTD from April 2019 (this has been extended from the original date of April 2018) and therefore it is important that businesses are aware of this and able to meet the requirements, which include submission of quarterly returns.

Of those who responded within the survey, almost 20% didn't know what MTD was, and a further 37% did not know what the impact on their business will be.

Of those who were aware of how this may impact their business, only 34% intend to pass their records to their accountant to deal with. Over half intend to deal with the new requirements in-house, either with HMRC free software (6%), cloud accounting (17%), or other recognised software (32%).

It is clear from the results, that many of those surveyed have not yet accessed the many benefits that online/cloud/digital accounting software can bring to a business. Not only does it ensure that you will be compliant under MTD, but it is quick and easy to use, improves cash flow and allows instant access to your business anywhere in the world.

1 in 12

businesses have not considered what they plan to do to comply with MTD

1 Making Tax Digital will be introduced across the UK from April 2018, do you understand the impact this will have on your business?

44% Yes

37% No

19% Don't know what making tax digital is

2 How will you approach your record keeping to comply with Making Tax Digital?

17% Use cloud accounting within the business

32% Use recognised software within the business

6% Use HMRC free software

34% Pass records to our accountant to deal with

8% I haven't considered this

56%

of respondents are unsure of the impact Making Tax Digital will have on their business

19%

don't know what making tax digital is

Sharing of Digital Information

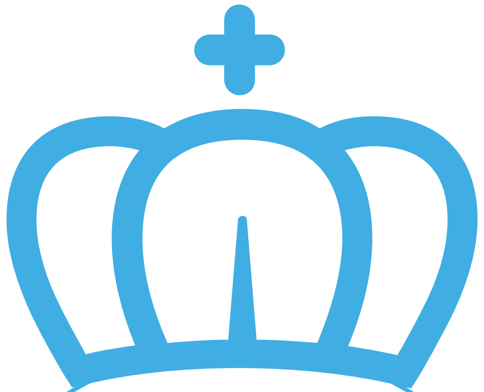
3 With access to digital information increasing, did you know that HMRC now receive information about you from all UK institutions and some foreign governments?

53% Yes

47% No

It is surprising to see that nearly 50% of respondents were not aware that HM Revenue & Customs now receive information about you from all UK institutions and some foreign governments. This is an area which is continually developing and the amount of information available and shared is continually increasing, as are some associated reporting requirements, such as the FATCA or CRS regulations. This could be a potentially concerning area for family businesses, with 19% believing this may increase the likelihood on a HMRC enquiry, and 25% uncertain whether this may impact the likelihood.

With the number of HMRC asset seizures having increased by 23% in 2016/17, it has never been more important to ensure that family businesses look to take professional advice to structure their affairs correctly to avoid breaking the law.



1 in 5

businesses believe their business will be more susceptible to an HMRC enquiry

4 With real-time digital access to business information, how do you believe this will impact on the likelihood of an HMRC enquiry into your business?

8% Less likely

19% More likely

48% No difference

25% Uncertain

GDPR

Regardless of the Brexit issue, the EU's General Data Protection Regulation ('the GDPR') comes into effect on 25 May 2018. It has been designed as a response to the increased use of technology and personal data and the need to protect consumers, employees and their privacy. Although GDPR will represent "another obstacle" for many businesses, it is a long overdue response to our changing world.

The ICO (Information Commissioner's office) will have increased powers to police this matter from May. The potential costs and inconvenience have also increased.

Our family business survey shows that 13% of businesses consider that the new regime will not apply to their business. At the point of survey (Q4 2017) 36% of respondents hadn't heard about GDPR at all. 46% of respondents are only "thinking about" or are partially prepared for the changes. Only 6% of businesses considered themselves to be fully prepared.

When we ran these numbers past business partners in the legal profession, they were "very surprised". David Jones from Myersons told us "the ICO acknowledges that organisations, especially small businesses, will take some time to transition to the new regime, but with the May deadline looming, businesses should not delay preparation further".

5 How prepared are you for the new data protection legislation (GDPR) which will be introduced in May 2018?

36% Never heard of it

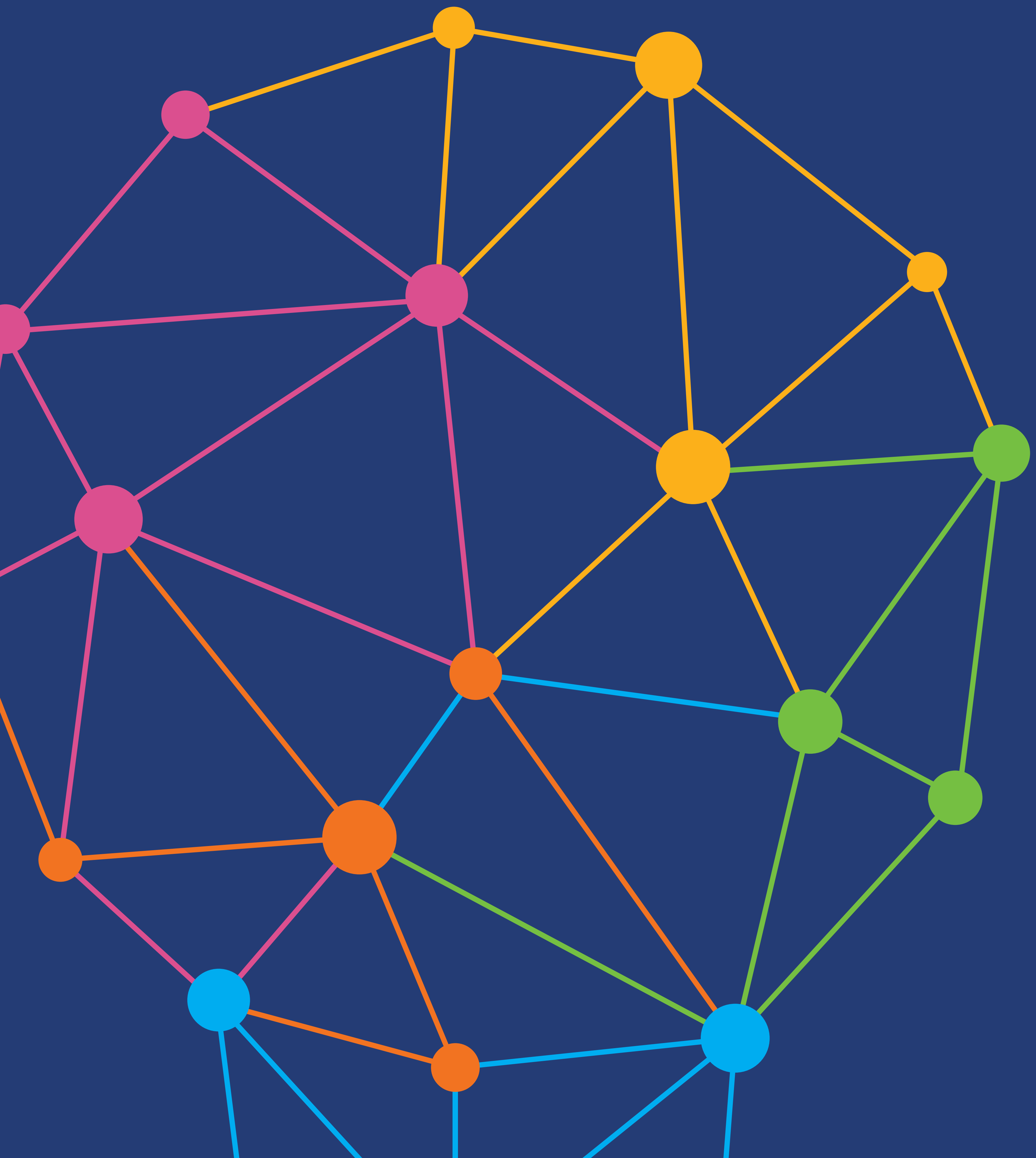
22% Thinking about it

23% Partly prepared

6% Fully

Only 6%

of businesses are fully prepared for GDPR



Innovation & growth

Pressure to Adapt & Change

6 As a business do you find yourself under pressure to adapt and innovate to keep up with the ever changing environment?

51% Sometimes

38% Always

11% Not at all

On a day-to day basis businesses are faced with, and overcome, a variety of challenges. However, businesses also need to look to the future, understand what challenges they are likely to face and plan how they will overcome them. This is innovation.

Innovation is sometimes misunderstood (indeed finding a clear-cut definition is a challenge in itself). Innovation doesn't have to be the invention of something new, for example it can also be enhancing or streamlining a production process to make it more efficient. It is reported that innovation accounts for between 25-50% of productivity gains, and firms that innovate are more productive than those who do not.

The survey highlights that family business owners understand the importance of innovation with less than 11% of respondents not feeling any pressure to adapt and innovate to keep up with the ever changing environment.

The pharmaceutical and technological sectors boast reputations as leaders of innovation. Nevertheless, innovation is important across a wide range of sectors. The survey demonstrates that the respondents in the retail and manufacturing sectors feel under the most pressure with 44% stating they 'always' feel under pressure to adapt and innovate (compared to an average of 38% across all sectors). In addition, of the respondents in the agricultural sector, 92% stated that they either 'sometimes' or 'always' felt the pressure to adapt and innovate.

The UK Government are, and have been for a number of years, investing in innovation across all regions and sectors. This comes in a variety of forms from the provision of grants to fund projects to tax credits and reliefs. With increasing frequency, we are having conversations with our clients and reducing their tax liabilities through claims to Research and Development Tax Credits.

89%

of businesses feel under pressure to adapt and change

Image by CN Group
Brian Welch, Hexham

Financing Growth & Innovation

7 **Business growth and innovation are essential to achieve longevity and a secure future. What is your primary plan to finance growth and innovation in the future?**

50% Own Capital

19% I don't intend to grow

15% Bank Loan

10% Don't know

3% Debt financing/capital

3% Equity Financing

The survey highlighted that the retail and manufacturing sectors felt under the most pressure to adapt and innovate. Therefore it is quite surprising to see that 24% of the retail businesses responded stating that they do not intend to grow (above the 19% average). On the other hand, it is less surprising that only 4% of manufacturing businesses had no intention to grow

There is continued uncertainty surrounding Brexit and what it will bring to each of us. Brexit is likely to be a key driver in the differing results across each sector. For example, there has been press coverage predicting that rising inflation and a depreciation of sterling will squeeze household incomes and depress consumer spending. I have no doubt that those in the retail sector who stated they do not intend to grow and innovate despite feeling the pressure to do so, are wary of this reduced consumer spending prediction.

With over 89% of respondents feeling the pressure to adapt and innovate, it is clear to see that the family business owners surveyed understand that growth and innovation is essential in achieving longevity and securing their future. However, growth and innovation comes at a financial cost that could make it unachievable for some. Therefore, the key question is, how will growth and innovation be financed?

Interestingly, over 50% of respondents planned to finance growth and innovation by using their own capital and only 15% would obtain a bank loan. However, financing plans tended to vary from sector to sector. In the construction sector 54% of respondents would use their own capital to finance future growth and innovation. In comparison, in the retail sector this reduced to 41% and in the agricultural sector only 32% of respondents planned to finance growth and innovation by using their own capital.

Challenges to Business Growth

8 Which of the following will be the main challenge to your business growth in the next three years?

35% Having the right people in the business

25% Marketplace competition

12% Not enough time

11% Lack of funding

4% Business Infrastructure

13% None of the above

In addition to finance costs there are a number of other challenges to businesses. In fact, less than 11% of respondents considered their main challenge to be a lack of funding.

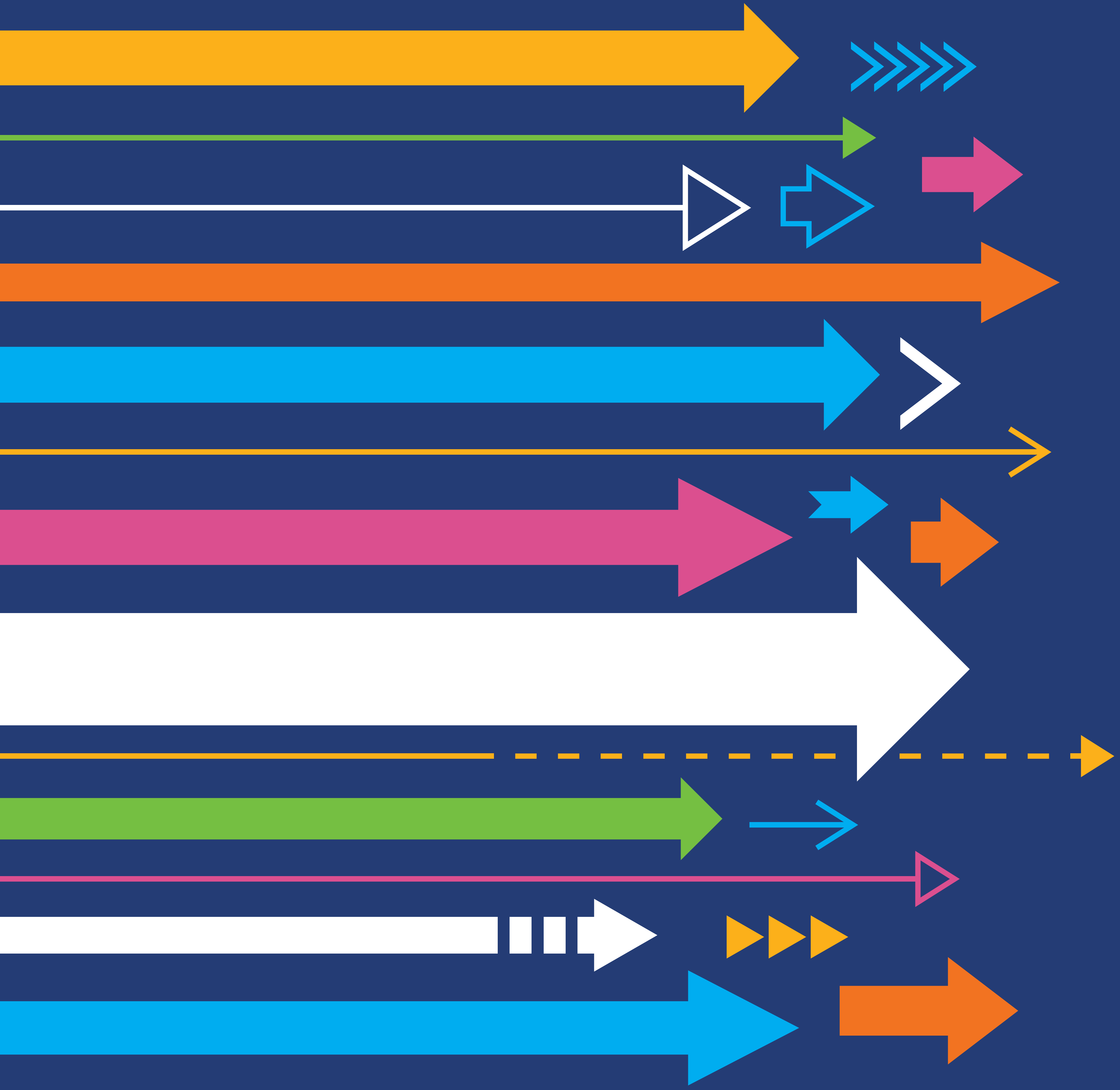
The main challenge to businesses over the next 3 years, as identified by 35% of respondents, was having the right people in the business. However, some sectors found this more of a challenge than others, 25% of agricultural businesses saw this as their biggest challenge, whereas 38% of construction businesses saw this as their main challenge.

If having the right people in your business is seen as a significant challenge, employers must consider how to attract and retain key employees. One way of retaining employees which is becoming increasingly more popular is the introduction of tax efficient share schemes such as Enterprise Management Incentives (EMI). By providing employees with an equity stake in the business, EMI is not only tax efficient for the employee, it aligns the employees objectives and interests with that of their employer.

Of the companies that identified having the right people in the business as their main challenge, over 50% did not operate a salary sacrifice scheme in relation to pension contributions. Offering a salary sacrifice arrangement in respect of pension contributions can be an effective tool in retaining staff as any contributions made by the employee reduce their income tax and National insurance contributions payable.

35%
believe having the right people in the business will be the biggest challenge to growth

Image by CN Group
Judy Bell, Northallerton



Planning to let go

9 Age?

18 – 24 = **less than 1%**

25 – 34 = **4%**

35 – 44 = **14%**

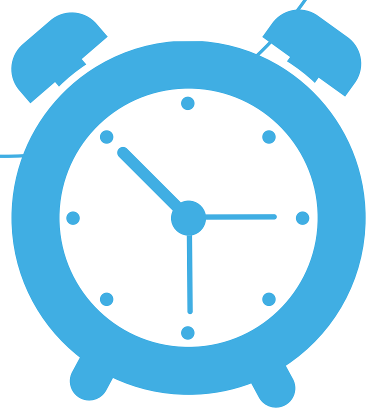
45 – 54 = **31%**

55 – 64 = **31%**

65+ = **20%**

51% of respondents were aged 55 or over

41% intend to leave their business in over 10 years



10 Timescale for leaving the business?

13% Within 2 years

19% Within 3 to 5 years

27% Within 5 to 10 years

41% Over 10 years

11 How do you see yourself leaving the family business?

32% Pass/Sell to my children

8% Pass/Sell to other family members

7% Exit following a management or employee buyout

12% Sell to highest bidding third party

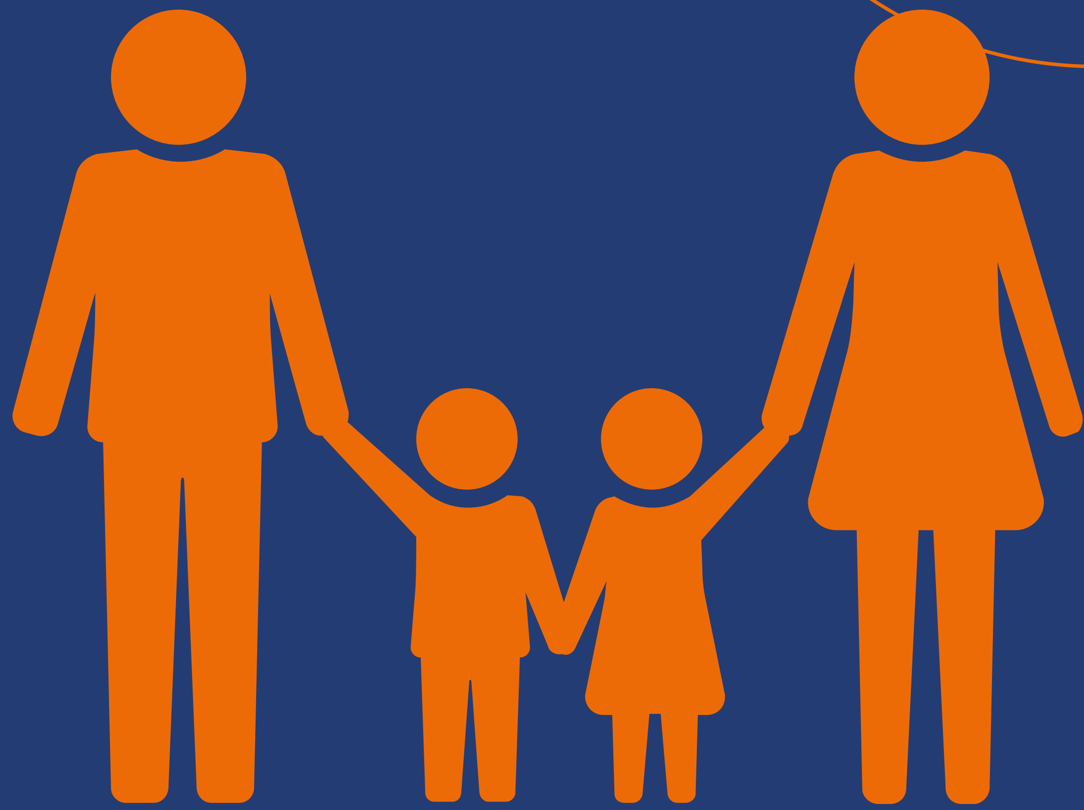
8% Sell to third party who will carry on my values/ethos

13% The business will cease

8% I don't plan to leave

12% I haven't considered this

32% Pass/Sell to my children



12 Are the next generation already in the business?

58% Yes

42% No

42%

Have discussed their intentions with the next generation to pass the business to them

13 Have you discussed with the next generation your intentions to pass to them?

58% Yes

42% No

FOR SALE

51%

of businesses either aren't structured correctly or don't know if they are for future sale

14 Do you consider your business to be structured correctly for you to maximise your return from future sale?

49% Yes

26% No

25% I don't know

Exit

The survey results for "Exit" threw up some interesting variation. Whilst the ownership and control data indicated a majority of owners are over the age of 44 (as you might expect), it was a surprise to see that 5% of owners under 44 were planning to leave within 10 years. This sounds like ambitious business owners with a clearly defined plan. This sounds promising for the economy.

41% of family business owners expect to leave after 10 years, making this the most popular option. Those planning to leave within 5 to 10 years add another 27%. Therefore 68% of owners are staying put for at least 5 years.

My direct personal experience is that intention and events don't always align. Sadly "events" can skew even the best laid plans. The important thing, regardless of the timescale is to have discussed and anticipated contingency plans, such that everyone knows your "Plan B"? This investment of time is a valuable insurance against a worst case scenario. Again, my personal experience is that the best way to do this is via a constructive long term strategy for your business.

When we look at the responses from those intending to leave in more than ten years time, it is perhaps unsurprising that the greatest number answered "I haven't considered this" (the exit route). Thinking about and planning that far in advance can seem like wasted effort, but even if passing ownership to a family member sounds easy, it still needs doing correctly.

Of course, business planning isn't only about the issue of exit, but there are clear benefits to anticipating differing circumstances as part of any business review. The reality is that an exit will require the business to be attractive enough for someone to want to pay for it. What work is being done now to ensure purchaser demand at the appropriate moment?

Perhaps unsurprisingly for a Family Business survey, the largest single response to method of exit was to pass or sell to children (32%). Passing or selling to other family members accounted for a further 8%, giving a family retention rate of 40%. It says something for the self confidence of our business owners that 8% don't plan to leave. 13% of owners anticipate that the business will cease at the point of exit. I'm sure there might be circumstances where this is the best solution, but 13% seems too high? Especially as only 12% think they'll be selling to a highest bidding third party.

For those businesses with family succession in mind (178 companies) 43% did not currently have the Next Generation in the business. Obviously working "somewhere else" first can be invaluable for the family business and I'd be delighted to catch up with anyone who has stories to share about this benefit. Somewhat surprisingly, an equivalent number (42%) hadn't yet discussed with the individuals concerned the plans to transfer the company to the next generation. As Mike and the Mechanics noted, the best time for this conversation is "in the living years".

This reminder is brought further into focus by the fact that only 49% of companies felt that the business was structured correctly for the current generation to maximise their return from a future sale. 26% didn't think the business was structured correctly to maximise a return (and this can sometimes be deliberate, a family transfer isn't necessarily about maximising return). However 25% of businesses didn't know if their structure was correct to maximise a return. This ratio held true across those planning to leave within 2 years, 3-5 years, 6-10 years and beyond 10 years. My observation would be that it's never too early to discuss this with a business advisor.

The next 12 months...

Impacting issues over the next 12 months

The daily drama of the Brexit negotiations are guaranteed to keep the journalists busy for the next 12 months, but what does this unique situation mean for family business owners?

The ratio of people who think Brexit will have a positive or negative effect has remained approximately the same between 2016 and 2017. In both years, roughly twice the number of people believe Brexit will have a negative rather than positive effect.

This year's results also give a picture of uncertainty and indifference on the Brexit issue. A quarter of people do not expect any impact from the United Kingdom leaving the EU. The greatest response (34%) came from those who were uncertain about the outcome. The negotiations might not have finished by the time we next run this survey, so the ongoing comparison will be interesting to note.

There was a marked change in the perceived impact of exchange rates. In 2016, the number of those who were expecting a negative impact from fluctuating exchange rates was 50% higher than the number expecting a positive impact. In this year's results, the number of those expecting a negative impact was nearly three times higher than for those expecting a positive impact.

34% of respondents expected fluctuating exchange rates would have no impact on their business, and 27% of people were uncertain about any impact.

The question about the impact of low interest rates showed a significant variation compared to the previous year. In 2016 roughly two-thirds expected a positive impact and one third a negative impact. By 2017 the ratio was four fifths positive and one fifth negative.

In addition, this year 33% expected no impact from low interest rates, and 15% were uncertain. One point to note was that the survey was "open" in the week that the Bank of England raised interest rates for the first time in 10 years. It might only have been a slight rise, but it will have been current at the time of survey response. Again, it will be interesting to see how this reaction changes over time.

14 What impact do you believe the following issues will have on your business in the next 12 months?

Brexit

14% Positive

27% Negative

25% No impact

34% Uncertain

34% are uncertian what effect Brexit will have

Low Interest Rates

43% Positive

9% Negative

33% No impact

15% Uncertain

43% thought low interest rates would have a positive effect

Fluctuating Exchange Rates

10% Positive

29% Negative

34% No impact

27% Uncertain

34% thought fluctuating exchange rates would have no impact

Summary & Conclusions

Summary

Selecting the balance of questions for this survey is a difficult task. A great deal of effort goes into the precise wording and logic of each question. The reason for this deliberation is so that our results can give something meaningful back to those businesses who, quite naturally, want to know how they compare to their peers.

To that end, perhaps the most interesting trends from this survey are those questions which reveal respondents to be under-prepared for what might well be imminent changes. This isn't intended to "scare", but it allows us a polite cough in order to highlight some important issues.

The question regarding salary sacrifice suggests that a number of businesses are not taking advantage of something that could help them. Indeed 21% of respondents didn't know what salary sacrifice is and 53% are not considering the scheme. If you haven't considered this scheme and its benefits yet, it might well be worth your while to do so.

The questions on Apprentices also threw up some interesting results. Only slightly more than a third of businesses are employing apprentices, and of those that are, 44% do not use the Apprentice levy. 19% of those employing apprentices don't even know what the Apprentice levy is. Given these results, I think it's safe to say that the Apprentice levy, and the support available to those who employ apprentices is worth knowing more about.

The questions around Digitalisation, and in particular the issue of "Making Tax digital", is another surprising result. Making tax digital will be introduced in April 2019, and yet at the time of the survey 37% of businesses did not understand the impact of the changes and 19% didn't know what it was. Under these circumstances it is unsurprising that 56% of respondents were unsure about the impact this change will have on their business.

Equally, 47% of respondents were not aware that HM Revenue & Customs can now receive information about businesses from all UK institutions (and some foreign Governments). 19% of respondents thought that this might make their chances of an HMRC enquiry more likely.

At the point of the survey (Q4 2017) 36% of respondents hadn't heard of GDPR (General Data Protection Regulations) at all and only 6% of businesses considered themselves fully prepared. In a delightfully British way, our business partners from Myersons (solicitors) told us that they were "Very surprised" by this result. GDPR is happening in May 2018, and companies would be well advised to get "up to speed" on the implications of this change for their business.

The questions around innovation and growth threw up some interesting results. 11% of respondents never felt any pressure to innovate in order to keep up with the ever-changing environment, yet 38% of respondents always felt pressure to innovate. There was interesting variation on these numbers across the different sectors.

The issue of financing growth and innovation produced some interesting variations across sectors too. Sadly we don't have data of our own from before the banking crisis, but the fact that 50% of respondents intended to "self-finance" growth, in contrast to 15% who would take a bank loan, could potentially indicate a change of habit brought about by the changed funding landscape since 2007.

Conclusions

Our respondents told us that lack of funding wasn't actually the biggest challenge when trying to grow a business. The leading challenge was in fact not having the right people in the business. This is a perennial problem. Again there was some variation on this ratio across the different sectors.

Given that this was a family business survey, it was perhaps surprising that Passing or selling the business to children only applied to 32% of the respondents, with a further 8% intending to pass or sell to another family member. 27% of respondents indicated an intention to sell outside the family.

42% of business owners who intended to pass or sell to a family member had not yet discussed with the next generation their plans and intentions. This is a high number, especially given the stark reality that we don't always get to time departures to our liking. In addition, 51% of businesses aren't structured correctly or do not know if they are structured correctly for any future sale. In the constant state of urgency that often accompanies a business, it is perhaps worthwhile to invest the time to think about what happens in three or five years' time.

These highlights, and other data from the annual survey will, I hope, give you that mix of food-for-thought, reassurance and challenge that I mentioned in the introduction. If nothing else this survey should outline the fantastic achievements of the family business sector. You are significant contributors to the national economy and an inspiration to lots of people who will follow your lead.

If you would like to discuss any of the issues raised in this report, please do not hesitate to contact your local Armstrong Watson office.

Contact Us

If you would like to discuss any of the topics explored within the Family Business Insight 2018 or to find out more about how our family business experts can advise and support your family business, please get in touch.

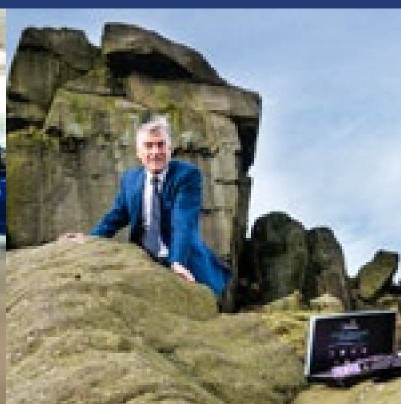
www.armstrongwatson.co.uk/family-business

0808 144 5575

Family Business Insight

2018



ArmstrongWatson®

Accountants, Business & Financial Advisers