

The Engine

Issue 4

Keeping You Up To Date With Manufacturing & Engineering News

May 2019

Now, for tomorrow

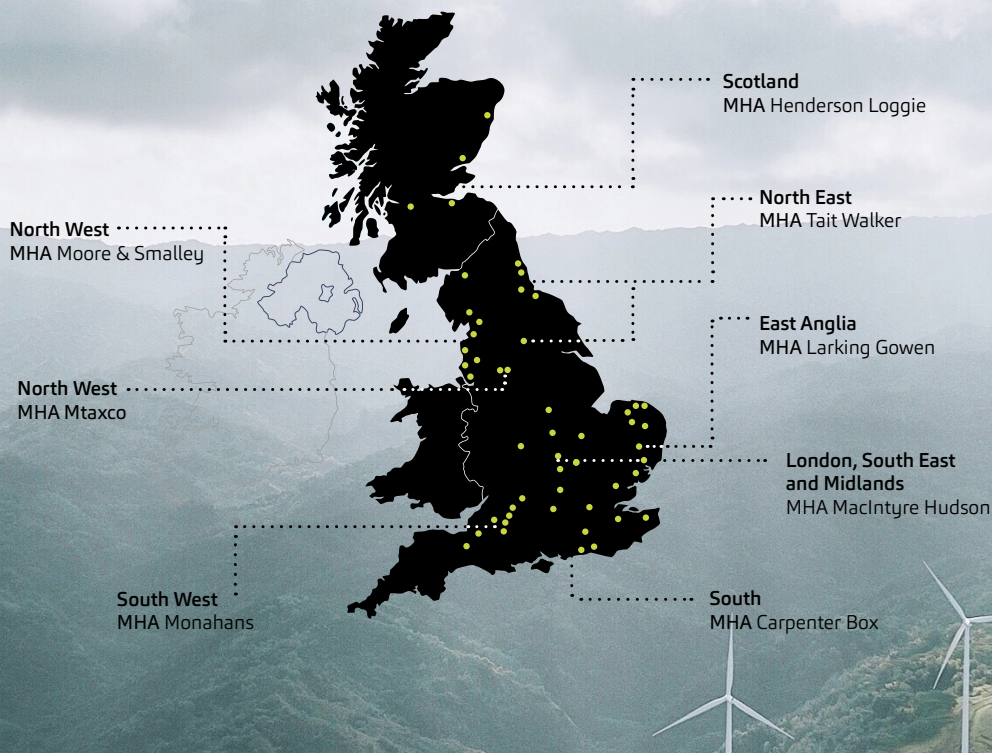


About MHA

MHA is an association of progressive and respected accountancy and business advisory firms with members across England, Scotland and Wales. Our member firms provide both national expertise and local insight to their clients. MHA members assist clients with their needs wherever they are in the UK, as well as globally through our membership of [Baker Tilly International](#), which has a network of trusted advisors covering 145 territories worldwide.

Our Sector Approach:

MHA allows clients to benefit from in depth sector knowledge in addition to specialist accountancy services and expert business advice. Manufacturing and engineering is a key sector for MHA, and we are committed to assisting both our clients and the sector as a whole by promoting manufacturing and engineering in all of its forms throughout the UK.



National Reach

50+
Offices
nationwide

8

Independent
accountancy
firms



Combined
turnover of

£143m



International Reach

125

Member firms
in 145 territories



10th

Largest network in
the world by combined
revenue



US\$3.6bn

Combined
member firm
revenues





Foreword

Welcome to the fourth edition of The Engine, our Manufacturing & Engineering Newsletter.

At MHA, we're passionate about UK manufacturing and engineering. MHA members act for thousands of businesses across the country, including OEM's, those in the supply chain, as well as engineering companies and tech businesses.

As we head towards the post Brexit world, we think it's more important than ever to champion our UK sector, which is why we look to share best practice right across our client base. As well as delivering accounts, audit and tax solutions, we also support skills initiatives, run forums and hold seminars, all aimed at helping our clients in the sector to do better.

Along with others such as Lloyds Bank, Innovate UK, the High Value Manufacturing Catapult and Autodesk, we're a member of the Future of British Manufacturing Initiative (FOBMI).

FOBMI is a collaboration between leading UK industry organisations focused on increasing the competitive advantage of UK Design and Manufacturing companies, by removing the barriers to true productivity and innovation.

Do get in touch if you think we can help your business in any way.

What's Inside:


- MHA Manufacturing & Engineering Survey Report Launch Event
- An interview with Arthur Hodgson from the Advanced Manufacturing Forum
- Sustainable Manufacturing
- IR35
- Manufacturing Research & Development

Thought Leadership

Nationally, we produce an annual respected Manufacturing & Engineering Survey Report which has become a barometer of how the sector is faring and how it thinks it will do in the future. The report looks at financial considerations, business confidence, innovation, employment, exporting and future considerations and was launched in February 2019:



<https://mha-uk.co.uk/insight/knowledge/2018-19-manufacturing-engineering-report/>



MHA Manufacturing & Engineering Survey Report

There could be few more fitting locations from which to launch a 'state of the nation' manufacturing report than the Institution of Mechanical Engineers HQ in Birdcage Walk, London.

The MHA Manufacturing and Engineering Report 2019 has become a real go-to document for anyone looking to understand the opportunities and challenges facing SMEs up and down the country.

The launch event itself, held in February, was chaired by MHA manufacturing group lead Chris Barlow. Chris gave a summary of some of the main findings of the report including the fact that manufacturers and engineers remain broadly optimistic and confident about future growth, despite the uncertainties around Brexit and the fact that they face rising production costs and skill shortages. Chris handed over to the afternoon's first speaker Richard Smith.

Richard is the Engagement Director with TRS (Talent Retention Solutions) whose role is around one of the major issues facing the sector – recruitment and retention. With a brief that has evolved over time, TRS continues to evolve and is developing a suite of services supporting the attraction, development and retention of people and skills across UK manufacturing, engineering and technology industries.

Also involved in the launch event and putting forward some interesting facts around global economic trends, with a particular focus on the UK was Rhys Herbert, Senior Economist at Lloyds Commercial Banking. Lloyds Bank has partnered with MHA over a number of years to sponsor the report as part of their extensive support for the UK's manufacturing sector.

Lucy Sutcliffe, MHA's Senior Customs Duty Manager spoke to the audience about preparing for Brexit from a customs perspective. Lucy advises clients on customs and excise duty issues, assisting them to understand and utilise the various and often complex customs and excise regimes and procedures. The audience benefitted from Lucy's extensive expertise in advising on the potential benefits and obligations of the Authorised Economic Operator (AEO) regime. Her advice on some of the options open to businesses around imports and exports was both timely and focussed.

The final speaker, Matt Rooney who is Engineering Policy Adviser at IMECHE rounded the formal part of the event off by highlighting elements of the report that he found interesting. Matt's commentary is an integral part of the report which is freely available to anyone interested at:

<https://mha-uk.co.uk/insight/knowledge/2018-19-manufacturing-engineering-report/>



Arthur Hodgson - Advanced Manufacturing Forum

What is your role at the AMF and why is manufacturing so important to you and the region?

My role as Forum Manager with the AMF is to develop the membership offering to ensure we deliver relevant information and services to our North East members. I visit member and non-member businesses to find out what they do, how they are innovating, what they do across the whole of the business to help identify areas of support and reasons to be part of the AMF, as well as helping to sign post them to other areas to help with business improvement and success.

I plan and implement events to inform, educate and engage with the sector, on topics/subjects that are relevant from feedback I receive when visiting companies. The role is very varied and allows me the opportunity to meet with a diverse range of manufacturing and engineering businesses, finding out the amazing things we are making in the North East. The technology and innovation in even small manufacturing companies is so interesting and I love learning about what they are doing, where their products are sold around the world and helping them to share their story.

We have a heritage going back centuries in the region, from the glass building monks of the seventh century to the designers of augmented world's of tomorrow. I myself have worked on the production line at Nissan, something a lad from Sunderland has to do otherwise I can't be called a Mackem (slang for people from Sunderland)!

Manufacturing has always and will always be a huge part of our makeup. Like my father before me and so many to come, families have links going back decades in this sector. We have a workforce of skilled and semi-skilled people who are vital to the sector and passionate about making things and I want to help to champion that as best I can for the future.

How do you feel North East manufacturers are responding to Brexit? What do you think manufacturers in the North East could do to work better together? How do you think forums support this sector?

Following a recent visit to an MHA event in London to hear from a number of speakers and regions across the UK in relation to our sector, I have to say that in the North East we are still relatively optimistic about the future. No one, as yet, knows what is going to happen and therefore, we are getting on with things. There will be opportunities coming from Brexit, either way, whatever happens. On-shoring has already begun to happen for a few, companies are looking at supply chain and "what if" situations and in the short term, if not the long term, there are requirements for our members and the manufacturing sector in the North East to supply the region and further afield. The AMF as the manufacturer forum will be helping our members to source those opportunities with each other and also explore opportunities outside of the region and the EU.



Sustainable Manufacturing

Whilst the phrase “sustainable manufacturing” is one many are familiar with, pinning down what it means is less easy.

To some, it is as simple as being “green”, but the growing consensus is that the concept extends much further than that.

For example, the US Department of Commerce sums it up as: “The creation of manufactured products that use processes that minimize negative environmental impacts, conserve energy and natural resources, are safe for employees, communities, and consumers and are economically sound.”

This could therefore encompass areas as diverse as minimising emissions, paying tax responsibly and operating good working conditions as detailed below:

Economy

- Investing in infrastructure
- Combating bribery and corruption
- Creating jobs
- Paying tax responsibly
- Driving innovation
- Generating sales and profits
- Contributing to local economy

Society

- Good working conditions
- Treating suppliers fairly
- Complying with the law
- Good community relations
- Respecting human rights
- Ensuring product safety

Environment

- Minimising waste and emissions
- Minimising use of hazardous substances
- Using energy and resources efficiently
- Using environmentally sound materials and energy
- Protecting biodiversity

What are the Benefits of Sustainable Manufacturing Practices and Why Should Small and Medium Sized Enterprises (SME's) be Embracing Them?

The key is to recognise that not only are there tangible, monetary benefits, such as reducing energy costs by investing in energy efficient plant and machinery, or increasing use of renewable energy sources, but there are also significant intangible gains to be had from improved relations with employees, suppliers and customers.

For example, a 2016 Cone Communications study reveals:

- 75% of millennials would take a pay cut to work for a socially responsible company.
- 76% of millennials would consider a company's social and environmental commitments before deciding where to work.
- 64% of millennials would not take a job if a potential employer did not have strong corporate responsibility practices.

As a result, in the dynamic, challenging, global economy which UK manufacturers are currently operating in, the gains from developing a culture of sustainability will be a key tool to their survival. With their appetite for innovation and ability to react more swiftly than their larger competitors, UK SME's are ideally placed to do so.

However, in order to build a sustainable manufacturing business that generates real gains, there are several hurdles to overcome:

- Firstly, is the need to identify which sustainable initiatives will generate the greatest gains and more importantly how these will be measured.
- Secondly, an action plan should be drawn up to prioritise initiatives and deliver them.
- Thirdly, the results of the activities should be measured and fed back into the start of the process to generate a culture of continuous improvement.

Measurement is important and there are many indices, ratings and standards that aim to do this. Tools such as the OECD's Sustainable Manufacturing Toolkit are a useful place to start.

In summary, not only is introducing a culture of sustainability into all areas of the business model a means of safeguarding the long term future of UK manufacturing businesses, but it can also generate both financial and non-financial benefits if carefully implemented and monitored.





A Warning to the Private Sector – IR35 is Coming

The October 2018 budget bought confirmation that IR35 rules changes will come into force for “medium” and “large” private sector businesses from April 2020.

The definition of medium and large remains unspecified. For manufacturers, this could impact on the use of off-payroll workers to support things like special projects where project managers, or marketing specialists or other consultants are required. It may also impact on the use of flexible workforce solutions and the use of agency workers. This is because the legislation will impact on the arrangements where any intermediary is used to supply off-payroll workers.

It does not apply where the off-payroll worker is genuinely self-employed.

Since April 2017, the public sector e.g. NHS Trusts and the BBC, have been required to examine the arrangements they have with workers who supply their services through intermediaries, including agencies, partnerships and personal service companies (PSCs). Where but for the existence of the intermediary the arrangement would be one of employment, public sector engagers are required to operate PAYE on all amounts payable to the worker either directly or via an intermediary.

The main focus of Government is to extend the current public sector IR35 rules to the private sector. Experience suggests that private sector businesses will require all of the time afforded to them to prepare for the change. Failure to prepare and be ready for April 2020 could result in significant:

- Labour supply issues;
- Business continuity issues;
- liabilities to tax;
- Liabilities to national insurance,
- And interest and penalties.

The private sector ought to benefit from the lessons learned from the public sector and will have had nearly 18 months to prepare. In particular, companies could take full advantage of HMRC's online “Check Employment Status Tool” (CEST).

However, CEST has caused problems in the past because converting something as subjective as employment status into algorithms, perhaps unsurprisingly, proved more difficult than expected. A lot of work has been done, though doubts about CEST's reliability remain. One key issue is that the concept of “mutuality of obligation”, an important test in deciding employment status, has been omitted from the tool.

It is strongly recommended that any business paying workers through intermediaries should review their arrangements to assess those off-payroll workers that are:

1. Genuinely self-employed;
2. Definitely caught by IR35;
3. Potentially less certain and require detailed review.

An early intervention to embark on a programme to identify those contracts that are at risk, to plan how to manage any potential changes and ensure that steps are in place to make sure that PAYE is operated where appropriate from 6 April 2020, or introduce required changes, will be essential.

Experience suggests that private sector businesses are likely to require all of the extra time afforded to them to prepare for the change. Getting it wrong could result in significant liabilities to tax, national insurance, interest and penalties.

The overuse of intermediaries is a concern to the Treasury, with HMRC estimating as many as 90% of PSCs were failing to operate the rules correctly, costing the public purse £400m. Companies must be prepared for scrutiny ahead.

IR35 Event

Off Payroll Workers – Time to Review Existing Arrangements



12 June 2019



Milton Keynes

[Register Your Place Now!](#)



Manufacturing Research & Development

For the first time since Research & Development (R&D) tax credits were introduced, the annual tax savings claimed by UK manufacturing companies topped £1 billion according to the Office of National Statistics' (ONS) latest report.

The increase in R&D claims results from more manufacturing companies realising that the product and process improvements they make may qualify for relief. There was a 21% increase in the number of claims made by manufacturing companies compared to the previous year. The average tax saving within the sector was over £90,000 per claim.

However, there are still many firms that are not claiming the tax relief that they are entitled to. R&D tax credits might be claimable for relatively common activities such as:

- Attempting to develop a new or improved product or manufacturing process.
- Improving product or manufacturing processes to take account of changes in legislation, such as health and safety laws or environmental regulations.
- Working with new or alternative materials.
- Reducing tolerances.
- Overcoming technological problems and challenges.

How Much Tax Relief can be Claimed?

R&D tax credits work by reducing a company's corporation tax bill or by generating a cash repayment to the company if it doesn't have a tax liability. There are two schemes for claiming relief: the Small or Medium sized Enterprise (SME) Scheme and Research and Development Expenditure Credits (RDEC) Scheme.

Under the SME Scheme, a company can deduct 230% of its qualifying R&D costs from its taxable profits instead of the normal 100%. This can result in significant tax savings, as shown in the illustration below for a company with £750,000 of qualifying R&D expenditure.

	With R&D Claim	Without R&D Claim
Sales	£10,000,000	£10,000,000
Costs of Sale	(£5,000,000)	(£5,000,000)
Gross Profit	£5,000,000	£5,000,000
Qualifying R&D Costs	(£750,000)	(£750,000)
Other Expenses	(£2,000,000)	(£2,000,000)
Net Profit	£2,250,000	£2,250,000
Less Additional 130% R&D Relief	(£975,000)	N/A
Taxable Profits	£1,275,000	£2,250,000
Tax due at 19%	£242,250	£427,500

The level of R&D expenditure does not need to be this high. In fact, according to the ONS, most claims for R&D tax credits involve less than £50,000 of qualifying costs.

The effective saving offered by the SME Scheme is approximately 25% of the qualifying R&D costs. The RDEC scheme is slightly less generous, as illustrated below for a company with £750,000 of qualifying R&D expenditure. Under the RDEC scheme the company is paid a 12% credit by HMRC. However, this credit itself is taxable, resulting in a net benefit of circa 10% of the qualifying R&D expenditure.

	RDEC Claim
Qualifying R&D Costs	£750,000
12% Above the Line Credit	£90,000
Corporation Tax on Credit at 19%	(17,100)
Post Tax Benefit to the Company	£72,900

What Costs Qualify?

The legislation only permits certain costs to be claimed.

- Staff costs relating to R&D activities. This is often the largest area of a company's claim.
- Externally provided workers, such as those provided by an agency.
- R&D activities that are subcontracted to another party.
- Software license costs.
- Consumable items (heat, light and power, and materials and equipment used or transformed by the R&D process).

The costs can only be claimed if they are attributable to qualifying R&D activities.

Is my Company Small, Medium or Large?

A SME is a company with fewer than 500 employees and either of the following:

- An annual turnover not exceeding €100 million; and
- A balance sheet not exceeding €86 million.

Companies in excess of these limits are large for R&D purposes. If the company is in a group or has external investors, it may be necessary to include their figures when considering if the company should claim under the SME Scheme or the RDEC Scheme.

Most SMEs will be entitled to claim under the more generous SME Scheme, but some have to make RDEC claims, where for example their expenditure has been subsidised by a government grant.

If you would like to review whether you are eligible to make an R&D claim, please get in contact with us.



About MHA

Services

- Compliance: audit compliance, accounting and financial reporting. Our audits reassure stakeholders and identify risk.
- Taxation: particularly around international tax, employment issues, R&D Tax Credits, Patent Box, Capital Allowances and tax mitigation.
- Business planning and support.
- Accessing public and private funding.
- Maximising the efficiency of your supply chain: reducing costs and improving margins.
- Mergers & Acquisitions: We have advised on many engineering transactions, including a number of cleantech investments.
- Due diligence ahead of funding and grant applications.
- Risk management: We advise on both governance issues in order to best attract investment and on minimising fraud and corruption risk.

MHA is a UK wide association of progressive and respected accountancy and business advisory firms. Each MHA member firm offers a broad range of services including accountancy, tax and corporate finance, as well as sector specialisms.

We are the UK member of the international network, Baker Tilly International. Through our membership of Baker Tilly International we are able to provide premier accounting, assurance, tax and specialist business advice worldwide, drawing on internationally recognised industry and service line experts in 145 territories.

Contact Us

If you require any further information or advice regarding these topics, then please feel free to contact your local MHA member firm contact.

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