



1st Contractor
Accountants

Guide to Running a Limited Company



Who we are

1st Contractor Accountants are a specialist online firm of accountants for contractors, freelancers and small businesses. The founders of 1st Contractor Accountants have nearly 30 years combined experience dealing with contractors accounts making us experts in this industry.

We pride ourselves on our high service levels. By embracing the latest technology we can deliver a consistently high service wherever you are in the country.

What we do

We offer accountancy services that aim to save you as much time as money as legally possible. We do this through a combination of easy to use online software, expert accountants and 1st class customer service.

Why choose us?

- You own dedicated account manager
- One of the lowest prices in the market
- Unlimited expert support and advice
- Easy to use online software
- Simple, expert accounting!

Call us now on **0207 156 7875** or email us at [**support@1ca.co.uk**](mailto:support@1ca.co.uk) to speak to one of our experienced advisors and find out exactly what we can do for you.



About This Guide

This guide has been written to provide anyone who is considering setting up a limited company, with enough information to cover the basics. We hope you find it useful.

This guide provides general guidance only, specific advice should be sought from your accountant regarding your individual circumstances before any action is taken.

All of the rates and allowances in this guide are for the tax year 2012-13. After the 5th April each year we will release a new guide with up to date rates and allowances, contact your account manager or visit our website for the latest guide.



Company Set-up

When you decide to start a limited company you have to register (incorporate) the company at Companies House.

Before you incorporate your company you will need to decide your company name, who the director will be and who will be the shareholders.

There are certain rules you have to abide by when choosing your company name. It can't: be the same as an existing company, be offensive, include "sensitive" words. You can find a detailed description of what isn't allowed [here](#).

Tip – Make sure the company name you have chosen has a web domain available before going ahead. There is nothing worse than setting up a company and realising you can't setup your website!

Shareholders own limited companies but they don't run them. That job is given to the directors. All limited companies must have at least one director, which will most likely be you.

You will also be a shareholder however it may be in your interest to appoint other shareholders as well in order to operate as tax efficiently as possible. You should talk this through with us before setting up your company.

Previously there was a requirement for all companies to appoint a company secretary, this is no longer necessary.

Once incorporated, you will receive a certificate of incorporation showing your company name, company number and date of incorporation.

For a fee of just £75+VAT we can handle the whole set up process for you including:

- Company incorporation & all paperwork
- Help setting up a business bank account
- Registering for PAYE, Corporation Tax & VAT with HMRC
- Advice on best business structure



Directors Responsibilities

As a director of a limited company you have certain responsibilities you should be aware of. Simply put the main ones are:

- Always act in the best interest of the company
- The day-to-day running of the business
- Preparing & filing accounts and annual returns
- Reporting changes to Companies House

You are also responsible for ensuring the company obeys the following laws:

- Tax Law
- Company Law
- Employment Law
- Health & safety Law

You will be responsible for ensuring that the limited company meets its obligations and is run in accordance with the Companies Act 2006



Business Bank Account

Once you have setup your limited company one of the first things you will need to do is setup a bank account. It is important that you setup a separate business bank account in your company name and do not use a personal account.

Virtually all high street banks will offer a business bank service with varying benefits and charges. Lots of banks offer free business banking for new businesses for a set period but it is important to look closely at what charges may apply after this period.

Some people prefer to setup an account with their current bank or if you prefer we can recommend one of the banks we have a close partnership with who can set you up quickly and give you a great deal.



PAYE

Before you can pay yourself or any employees a salary you will need to register and set up a PAYE scheme with HMRC.

Once registered, you will receive 2 unique reference numbers and you will now be required to deduct tax and national insurance from salaries paid to employees/directors.

As an employer you will have to:

- Deduct & pay to HMRC, tax and NIC from any salary payments
- File annual returns to HMRC by 19th May after the tax year end
- Report benefits & expenses paid to employees by 6th July after the tax year end

Included as part of our service we will setup your PAYE scheme, run monthly payroll for you, advise you how much and when to pay over to HMRC and complete the necessary end of year forms.

Facts and Figures

Under PAYE there are three main types of tax you will be required to pay HMRC: Income Tax, Employers National Insurance and Employees National Insurance.

Income tax – This will be deducted from the employee's salary. Currently the first £8,105 is tax free (if your total taxable income exceeds £100,000 then this allowance is gradually withdrawn). The next £34,370 is taxed at 20%, any income above this, up to £150,000, is taxed at 40% and any income over £150,000 is taxed at 50%.

Employees NI – This will be deducted from the employee's salary at the rate of 12% on any salary above £7,605 (below this amount there is no NI to pay) up to £42,475. Above this NI will be deducted at the rate of 2%.

Employers NI – As an employer your company has to pay this at the rate of 13.8% on any salary above £7,488.



VAT

You don't have to register for VAT until your taxable turnover reaches the registration threshold (currently £77,000).

Even if your turnover does not exceed the registration threshold then you can choose to register for VAT voluntarily if you wish. You may choose to do this if you incur a lot of business expenses with VAT on, as if you are VAT registered you can reclaim the VAT element of these expenses.

The other reason for voluntarily registration may be to take advantage of the VAT Flat Rate Scheme.

It is important to remember that once you are VAT registered you will be required to add VAT on to all of your sales invoices. If you are selling to members of the public, rather than VAT registered businesses, then this will increase the cost to them as they cannot claim back the VAT.

The current rate of VAT is 20%, if you charge a client £1,000 you will have to add £200 (20%) VAT on top making the total invoice £1,200.

If you register for VAT you will be required to submit a VAT return every three months and pay any VAT due to HMRC.

If you are unsure whether you are required to, or whether you could benefit from, registering for VAT then contact us.

Included as part of our service, we can setup your VAT scheme and calculate your quarterly VAT returns



VAT Flat Rate Scheme

If you are VAT registered you have the option of joining the Flat Rate Scheme (FRS). The Flat Rate Scheme is designed to help small businesses by letting you calculate your VAT payment as a flat rate percentage of your turnover (including VAT).

You will still charge VAT to your clients at the standard rate (currently 20%) but the percentage of VAT you pay to HMRC will be lower. The actual percentage depends on your business trade sector.

Under the scheme you are not allowed to claim back VAT on individual expenses (unless over £2,000).

If you have very few expenses with VAT on (travel typically does not have VAT on) then the Flat Rate Scheme may be beneficial to you and you could even make some money from it (which of course then has to be taxed!)

Note – You cannot join the scheme if your annual turnover (excluding VAT) will exceed £150,000.



Corporation Tax

Shortly after incorporating your company HMRC will send you a "Corporation Tax – New Company Details" form. When you receive this simply send it on to us and we can complete it for you and register your company for Corporation Tax.

Corporation tax is the tax your company pays on the profits it makes. The current rate for small companies is 20%.

You will be required to submit a Corporation Tax return, along with a set of accounts, yearly to HMRC. These are due 12 months after your company's year end.

You will be required to pay your Corporation Tax within 9 months and 1 day from your company's year end.

Included in our service is the calculation and preparation of your Corporation Tax returns. Instead of springing your tax bill on you a few months before it is due, our online software will give you an accurate up to date estimate of your Corporation Tax at a glance to avoid any nasty surprises.

Included as part of our service we will prepare and submit your annual accounts and Corporation Tax returns



Invoicing

In order to get paid you will need to send invoices to your clients. There are certain things that must be included on an invoice including:

- The word invoice
- Unique invoice number
- Invoice date
- Company name and address of the customer
- Description of goods/services
- Breakdown showing rate, period & total owed
- VAT amount (if applicable)

There are certain things that are not legal requirements but are still a good idea if you want to get paid! Such as how you want to receive payment, your business bank account details are a good idea if you want to get paid quickly. Also don't forget to state your payment terms e.g. 30 days.

Our online software will help you create a perfect invoice in seconds with you required to enter just a couple of pieces of information.



Expenses

No matter what your business does you will incur some expenses as a result of running your business. You will only pay tax on your profit (income less expenses) so the more expenses you are able to claim the lower your tax bill.

As a general rule, if an expense has been “wholly and exclusively” incurred for carrying on and earning the profits of your business, it will normally be allowable.

It is important to remember that HMRC could ask you for proof of these expenses so it is important that you keep copies of all receipts. It also means you can forget about making up expenses simply to lower your tax bill, you have to actually incur them to claim them!

There are lots of complicated rules surrounding expenses but that’s what you pay us for.

As a rough guide some of the typical expenses you can claim are:

- Business travel & Subsistence
- Accommodation while away on business
- Accountancy Fees
- Mobile telephone
- Postage & Stationery
- Computer equipment & software
- Internet
- Bank Charges
- Pension contributions
- Books & Publications
- Home office costs
- Subscriptions to approved professional bodies

Contact us for a copy of our expenses guide for a more in depth description of what is and isn’t allowed.

If you have any questions as to whether an expense is allowable or not speak to your account manager.

Note: if you are inside IR35 (see IR35 section) the expense rules are different, call us to discuss.



Insurance

The three most common types of insurance required by Limited company contractors are:

Employer's Liability Insurance – Protects against claims from employees injured due to an employer's negligence. This is a legal requirement for all business, however there is an exception if the company only has 1 employee and that employee owns 50% or more of the shares – which will be the case for most of our clients.

Public Liability Insurance – Protects against injury caused to members of the public and damage to their property caused by your company/ employees.

Professional Indemnity Insurance – Protects against claims where a client has suffered financial loss as a result of errors or negligence in the service you have provided.

Other types of insurance – Freelancer legal protection, Personal Accident & contract review.

Please note that as we are not authorised by the FSA we cannot provide you with any of the above Insurances but we can provide you details of companies who can, simply speak to your account manager if you want any further information.



IR35

IR35 is a complex tax legislation that, simply put, is in place to stop contractors using Limited companies to save tax working for a client where ordinarily they would be classed as employees.

When deciding whether you are classed “employed” or “self-employed” several factors need to be looked at within your contract and working practices. If you are deemed to be “employed” then you fall inside the IR35 legislation.

If you are inside IR35 then you have to operate the majority of your pay as “deemed salary”, this attracts tax & NI at the same rate as a regular salary. The expenses you can claim are also limited.

If you are outside IR35 you can pay yourself a smaller salary, with any further profit paid to you as dividends. You can also claim any allowable business expenses. This will give you a much higher take home than operating inside IR35.

Ensuring you get your IR35 right is so important. Getting it wrong could cost you a lot of money in fines, interest and backdated tax. For this reason we strongly recommend that you seek the advice of a tax status specialist who specialise in IR35. They can review your contract and your working practices and advise you whether they believe you fall inside or outside IR35. We can recommend some very good firms for this.

Contact us for a copy of our IR35 guide for a more in depth description of the details of IR35.



Salary

If you fall outside the IR35 legislation then the level of salary you pay yourself is completely up to you. There are three possibilities when setting your salary level, these are:

- 1) NIC Free Allowance** – Setting your salary level at the NIC free allowance (currently £7,488) is the most tax efficient salary as you pay no tax or NIC on your salary
- 2) National Minimum Wage (NMW)** – Currently £6.08 an hour, for a whole year will equate to an approximate annual salary of £11,000. As this would exceed the tax & NIC free amounts you would have to pay some tax and NIC on this salary.
- 3) Market Rate Salary** – You may decide to pay yourself a much higher salary based on what you would expect to obtain in the market place. This would mean a higher tax and NIC bill

In the majority of cases the NIC free allowance salary is chosen as it is the most tax efficient however there may be other factors that affect your choice such as IR35 insurance policies or pension contributions.



Dividends

If you fall outside the IR35 legislation then you will pay yourself dividends. A dividend is a distribution of profits after tax, from the company to its shareholders.

Before you declare a dividend you must make sure there is enough profit in the company to do so (not simply enough money in the bank). After this the dividend can be paid providing all of the necessary paperwork has been completed

Our online software will provide you with a running calculation of the amount available to distribute as a dividend. It will also take care of all of the paperwork when you pay the dividend.

As your company pays Corporation Tax on its profits before a dividend is paid you will not have any tax to pay personally unless you are a higher rate tax payer. For 2011/12 that means your total gross income (gross salary, gross dividends and any other income) is above £42,475.

If you are a higher rate tax payer you will have further tax to pay when you complete your self assessment tax return each year. Contact us for an estimate of your tax bill.



Personal Tax Return

As a director of a limited company, HMRC will expect you to complete a personal tax return (also referred to as a self-assessment tax return) each year.

The deadline is 31st January (providing you file online) after the end of the tax year. E.g. for 2012-13 tax year your return would be due by 31st January 2014. This is also when any outstanding tax is due to be paid.

A tax return will include details of your salary, dividends, and any other income you may have, such as property rental.

To be able to file your return online you need the 10 digit UTR number which can be found on the front page of the tax return. If you do not receive a tax return and do not already know your UTR number you will need to contact HMRC.

You must register in advance to file online with HMRC. There are strict penalties for late submission of your return or if you fail to pay your taxes on time so make sure you don't leave it too close to the deadline.

The tax return is not included in our monthly fee however we will be more than happy to take care of it for you, our prices start from £100+VAT



Payments on Account

Payments on account can be confusing to understand at first but are important as they can have a big impact on your pocket.

A payment on account is made twice a year and is effectively paying for next years tax in advance.

On the 31st January you will make a “balancing payment” settling any unpaid tax for the previous tax year. On the same day you will also be required to pay your 1st payment on account for the current tax year. The amount is calculated at 50% of your tax bill for the previous year.

Your second payment on account will be for the same amount and be due 31st July.

If you expect your income to be less next year then it is possible to reduce your payments on account.

Something to watch out for – In your first year of paying tax in this way you will have 1.5 times your tax bill to pay in January as you would not have already made any payments on account!



Payments on Account—Example

Example – Your first tax bill for the 2010/11 tax year is £10,000. As you haven't yet made any payments on account you will have to pay the whole £10,000 on the 31st January 2012. You will also be required to make your 1st payment on account of 50% (£5,000) towards 2011/12.

In total you have £15,000 to pay on 31st January 2012

*£10,000 for 2010/11

*£5,000 for 2011/12

Your second payment on account of £5,000 towards 2011/12 is due by 31st July 2012.

Your tax bill for the 2nd year, 2011/12 is £12,000. You have already paid £10,000 on account (£5,000 on 31st January 2012 & £5,000 on 31st July 2012) therefore you need to make a "balancing payment" of £2,000 by 31st January 2013. You also need to make your first payment on account of £6,000 (50% of your £12,000 tax bill) towards 2012/13.

In total you have £8,000 to pay on 31st January 2013

*£2,000 for 2011/12

*£6,000 for 2012/13.

Your second payment on account of £6,000 towards 2012/13 is due by 31st July 2013



Timetable

Some important dates for your diary.

Company year end - will be the last day of the month your company was incorporated on. Example, if your date of incorporation is 15/01/2011 your first year end will be 31/01/2012

Tax year end – 5th April

Annual Return – yearly on the anniversary of the date of incorporation.
Due within 30 days.

Company Accounts – Due with Companies House 9 months after your company year end

Corporation Tax return – along with your accounts need to be with HMRC within 12 months of your company year end

Corporation Tax payment – to be paid to HMRC within 9 months and 1 day of your company year end

VAT return and Payment – due with HMRC quarterly on the 7th of the month after (approximately 5 weeks) your VAT quarter end

PAYE/NIC deductions – due to be paid to HMRC by 19th of every quarter (July, October, January & April) – may be required monthly depending on the amount of tax due

Payroll Year end forms – P35 & P14 due with HMRC by 19th May

Payroll P11d form – due with HMRC by 6th July

Personal tax return – due with HMRC by 31st January

1st Payment on account – due to be paid to HMRC by 31st Jan

2nd Payment on account – due to be paid to HMRC by 31st July

Find out more

If you would like to find out more about how 1st Contractor Accountants will save you time and money, contact us today!

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