

Guide to running a limited company - 2012



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- It should not be relied on or treated as a substitute for specific advice relevant to particular circumstances.
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Limited co's – the basics

- A company is a separate legal entity controlled by its members
- It is “limited” if the members are not liable for any of the company’s debts unless:
 - they have given a guarantee to the company
 - they owe unpaid share capital
- So a company can enter into legal contracts, open a bank account, become a tenant or own property & other assets.
- Whilst the members control or own the company, the directors manage the company (can be same people)

Limited co's – the basics

- The company needs to have capital in order to operate as a business, so the owners will purchase shares in the company
- An owner managed company could be setup with the same person as both shareholder and director, and with 1 share valued at £1 (but seek advice first!)
- Companies also need to have Articles of Association that set out what a company can and cannot do. (The standard Model Articles are generally suitable for startups, but can be individually tailored)
- Companies can be incorporated online for £18 at www.companieshouse.gov.uk

Limited co's – key requirements

- The key legislation is the Companies Act 2006 and related Statutory Instruments which fill in specific details
- These set out various requirements including for company constitutions, director duties, shareholder transactions and reporting
- Small companies have to prepare a full set of annual statutory accounts under UK Accounting Standards
- A set of accounts have to be filed with Companies House within 9 months after the year end. These will be publicly available, but small companies can file abbreviated accounts which omit a P&L

Limited co's – Authorisations

- Directors and shareholders need to authorise certain transactions & events
- Model Articles give directors power to declare interim dividends using an ordinary resolution
- Directors can pay at intervals any dividend payable at a fixed rate if it appears to them the profits available for distribution justify the payment
- Shareholders also need to approve final dividends
- Unpaid dividends cannot be accrued in the accounts without shareholder approval prior to the year end
- Directors also need to authorise the accounts

Directors duties & services

- s.170 – 178 CA'06 mention a director's duties, mainly to act within company's constitution, with due skill & care, for benefit of the company
- The Model Articles mention a director can undertake any services, and be paid as the company sees fit
- Best practice to have a director's service agreement setting out terms or could have a written memo
- A company with a sole director/shareholder without additional staff could mean the director is also acting as an employee, as well as an office holder. This has implications for minimum wages
- Without a written contract, difficult to prove if e'ee

Accounting

- It is important to keep proper records to comply with Companies Act 2006 and also for tax purposes
- A paper ledger, spreadsheet or accounting package should be used to show and explain the company's transactions and to record assets and liabilities
- Keep the accounting records along with supporting receipts, invoices, bank statements and contracts to for at least 6 years
- Regular preparation of accounts can allow you to analyse key performance indicators and to make better decisions
- Monitor systems regularly to track credit control and manage cashflow

Accounts

- Accounts mainly consist of 2 parts:
 - Profit & Loss (or Income Statement)
 - Balance Sheet
- The P&L shows the trading history for a given period of time, normally 1 year, and shows turnover less costs as gross profit. Admin expenses, interest and tax are then deducted to arrive at net profit or loss
- The B/S shows the accounting value of a business at the end of the period. Assets (company owns or is owed) less liabilities (company owes to creditors) gives equity (share capital plus retained profits/losses from previous years)

Accounts

- Statutory accounts are those that apply generally accepted accounting principles and other rules and regulations as laid down in statute or accounting standards, and make disclosures as required
- As well as P&L and B/S, also need directors report and explanatory notes
- Management accounts can be of any format, and are generally prepared on monthly or quarterly basis
- Cashflow forecasts and budgets are also important as they estimate the sales, costs & other outgoings expected in the future, and can predict a cash shortfall or be used to appraise business decisions

TAX

- Companies mainly face the following taxes:
 - Payroll taxes
 - VAT
 - Corporation tax
- **Payroll taxes** – for an understanding of how wages are taxed please refer to our separate Wealth Extraction Strategies guide.
- In the following pages we discuss IR35 which is a potential payroll type problem for contractors, freelancers and locums.

IR35 – Personal Service co's

- Legislation for substance over legal form of a relationship between a contractor (or freelancer or locum) and client
- Some contractors use limited companies to invoice “clients”, but the overall facts suggest they are actually employees
- In particular:
 - Substitution
 - Right of control
 - Mutuality of obligation

Factors suggesting IR35

No Substitution

- Worker cannot delegate or substitute without client's consent
- One person companies, unless evidence to contrary

Lack of control

- Worker engaged for period, not specific tasks
- Client can move worker to other tasks
- Client directs, supervises and quality controls work

Mutuality of obligation

- Engager obliged to pay a wage/remuneration
- Worker obliged to provide own work or skill
- Notice period irrespective of breach could be an indicator

Potential indicators of employment:

- work on the client's premises
- use the client's equipment
- work standard hours
- be paid at an hourly rate or use of timesheets, no fee retention for performance
- be subject to a right of control & take direct orders
- Part and parcel of organisation
- No financial risk, client obliged to give work, worker has to accept
- Notice period to terminate, not at end of project
- Right to receive e'ee benefits: sick pay, holiday, staff canteen, Xmas party

Contract should reflect reality

- The actual working practices are the most important factor. So if the written contract does not reflect these, it will be ignored
- HMRC have been known to interview both the contractor and the client to verify the working practices
- Contract terms should be consistent, eg use company & supplier, not alternate with agency and contractor
- HMRC may also have previously made a Status ruling at the client

What if IR35 applies?

If IR35 applies, the consequences are that:

- Income in form of deemed payment under Sch E
- S.336 expenses can be claimed for travel, subsistence, PII, benefits in kind (& E'ers NI) etc
- An additional 5% of turnover can be claimed as expenses
- Deduct salaries + E'ees NI + E'ers NI paid in yr
- The income left over will be subject to income tax and national insurance at the same rates as normal employees, ie 20/40% tax and 12/2% NI
- E'ers NI also has to be paid 13.8% by contractor (client doesn't pay)

VAT

- VAT has to be added to sales invoices for **taxable supplies** made by a **taxable entity** in the course of business (s.4 VAT Act 1994)
- Taxable supplies are a supply of:
 - goods or services that are not exempt
 - made in the UK
 - for consideration (ie money)
- Not all sales are taxable, eg health professionals such as qualified doctors, optometrists or dentists etc involved in protecting, maintaining or restoring a person's health are exempt

VAT Registration

- A taxable entity is one that is compulsorily or voluntarily registered for VAT
- Compulsory registration is required if turnover:
 - for previous 12 months > threshold of £73,000
 - for next 30 days alone is expected > £73,000
- If customers are VAT registered, voluntary registration could be worthwhile as can claim back input VAT on suppliers' invoices.

VAT invoices

- Once registered for VAT, a company must give a VAT invoice for taxable supplies to other registered businesses
- Must show
 - Invoice no.
 - Name, address, VAT no.
 - Tax point (& issue date if different)
 - Customer's name & address
 - Description of services (quantity, rate, charge)
 - Net charge, VAT, total charge with & w/out VAT
- Need to keep copies of invoices issued

Tax point

- VAT is charged at the tax point which is the earlier of the date services are provided vs date invoice issued (unless invoice issued < 14 days after service provided)
- If a continuous supply of services, under Regulation 90 of VAT Regulations 1995, can delay tax point by:
 - issuing "Request for Payment"
 - write "This is not a VAT Invoice" on request
 - issue tax invoice once payment received

Reclaim VAT

- Can reclaim input VAT attributable to taxable supplies in the course of business
- Expenses like computer costs, phone, stationery etc
- Can't reclaim entertaining
- Ensure that wherever possible, suppliers invoice using the correct company name and provide a VAT receipt, as HMRC could ask for this
- Can reclaim input VAT borne by a business 3 yrs prior to VAT registration, including pre-incorporation expenses if not a taxable person, and re-imburse full cost

Vehicles & VAT

If not a company car, can only claim VAT on mileage allowance fuel element which is 15p to 26p

If company car:

- Reclaim ALL the VAT on repairs & maintenance and other expenses for car as long as:
 - Used to some extent for business purposes
 - Company pays for the work done
- Reclaim VAT on petrol:
 - All the VAT if only business purposes, or if private then pay qtrly fuel scale charges (only good if high mileage or low emissions)
 - Business element only, but need detailed logs
- May not be worth it, need consider P11d benefits

VAT administration

- Complete the VAT registration form – not very long, give details of business & estimate turnover
- HMRC will provide a VAT number and certificate
- VAT returns will need to be submitted electronically every month, quarter or year depending on the scheme chosen
- Return is 1 page and provide amounts of net & VAT elements of turnover and expenses in UK and EEC
- If output VAT > input VAT, pay difference to HMRC
If input VAT > output VAT HMRC will refund you
- Need to keep record of input & output tax for each period for 6 yrs

Annual VAT scheme

- Company makes interim payments during year and only 1 return with last payment +/- balancing payment for any difference
- Interims payments are:
 - 9 mths x 10% each between mths 4 to 12 OR
 - 3 qtrs x 25% due by end of mths 4, 7 and 10
- Pro's:
 - 1 return for whole yr
 - 2 mths to complete it & send in balance
- Con's:
 - If turnover falls, interim payments based on prior year's actual payments, so pay more than necessary

VAT Flat Rate Scheme (FRS)

- Net turnover has to be < £150k for the next year to be eligible for FRS
- Add output VAT at 20% as normal on sales invoices
- Calculate amount due to HMRC differently:
Gross sales (ie including VAT) x flat rate %
- Don't reclaim any input VAT on purchases
- Can also claim VAT on capital goods if purchase >£2k

VAT Flat Rate Scheme (FRS)

- Each industry has a different FRS %, but get 1% discount in first year
- Eg IT contractor with 14.5% FRS and income £80k
 - Receive from customers: $£80k \times 20\% = £16k$
 - FRS has $£80k \times 120\% \times 14.5\% = £13,920$
 - £2,080 “profit” on VAT (20% - 14.5%) is liable to corporation tax
- So need to have $< £2,080$ of input VAT to be worthwhile ie $£2,080 / 20\% = £10,400$ net expenses

Corporation tax

- Companies need to prepare corporation tax returns based on the accounting profit in the statutory accounts, but making various adjustments eg:
 - increase it by adding back disallowable items for tax purposes such depreciation, entertaining or general bad debt provisions (see next page)
 - reduce it by claiming capital allowances on fixed assets (eg furniture or computer equipment)
- Multiply the profits chargeable to corporation tax (PCTCT) by 20% for small companies and 26% once PCTCT > £1.5m (with marginal relief £0.3m-£1.5m)
- If there are losses, carry these forward against future profits from the same trade, or sometimes backwards

Expenses for corporation tax

- Can claim tax relief on expenses wholly & exclusively incurred in the course of business:
 - Travel & subsistence – not between home & “fixed” place of business or if contract > 2 yrs
 - Rent, rates & office costs (or use of home £156)
 - Computer costs
 - Telecommunications & utilities
 - Specific provisions for bad debts
 - Many others (eg a dress for movie premiere!)
- Make sure expenses invoiced to business wherever possible and keep all invoices for 6 yrs

Company Car

- Company gets corporation tax deduction running costs & capital allowances
- P11d benefit on car & fuel
 - Benefit on car is list price x CO2%
 - Benefit on private fuel is £18,800 x CO2%
 - Company pays e'ers NI at 12.8%
 - E'ee pays income tax on benefit but no e'ees NI
- No car benefit if no private use, but this not possible if kept overnight at home.
- No fuel benefit if private use is repaid during tax year
- If not a company car, can claim 45p per mile 1st 10k miles, and 25p thereafter to cover wear & tear & fuel

Caveat for corp tax & acs

- We have only given brief details here of corporation tax and statutory accounts as opposed to 15 pages for IR35/VAT
- This is because corporation tax and statutory accounts are based on a vast number of principles and rules from a variety of legislation and sources. Complex issues and problems can often arise so unless you have a very simple business.....please.....



Forms & red tape - Startup

- 1) Complete form CT41G to give HMRC details of the business
- 2) Register as an employer by ticking box in CT41
- 3) Register for VAT & submit VAT returns quarterly/annually, along with payment
- 4) Can apply for Annual Accounting & Flat Rate schemes with the same form VAT 600 AA/FRS
- 5) Apply for online gateway & HMRC services for VAT, payroll etc

Forms & red tape - Monthly

1. Spend time inputting expenses and sales etc into a cashbook or accounting package
2. Decide on salary & dividends level
3. Process payroll and pay yourself/staff and also pay tax/NI to HMRC by 19th of following month if by cheque, or 22nd if electronically
4. Check if sufficient profits & pay dividends, also need to sign a dividend minute and voucher
5. Every quarter, take total income, expenses, output VAT and input VAT and file VAT return online & submit payment to HMRC within 1 month of quarter end

Forms & red tape – Year End

1. Prepare full statutory accounts upto YE
2. Use full a/cs to calculate and pay corporation tax liability within 9 mths of YE
3. Submit abbreviated acs to Companies House within 9 mths of YE
4. File corporation tax return CT600 within 12 mths YE
5. Deliver annual return to Companies House < 28 days of return date
6. File P35 (total) and P14 (indiv e'ee) annual returns for payroll details by 19 May each year
7. File P11d giving details of staff benefits & expenses by 6 July each year

let us take care of it all.....



Our Services

- Statutory audit & accounts preparation under IFRS & UK GAAP.
- Corporation and personal tax planning/returns.
- Monthly management accounts
- VAT returns, payroll and bookkeeping from source documents and incomplete information.
- Building cash flow models, including for funding proposals.
- Business and strategic advice, with guidance on future plans.
- Preparation for due diligence.
- Systems design and reviews to mitigate weaknesses and risks in controls & processes.

The MAH method

- We delve deep into the business to understand the:
 - client, its industry and laws & regulations
 - internal goals and external pressures and the interactions between them
 - systems & controls
- We then use our technical expertise and rich experience to identify the key risks and choices where professional judgement needs to be exercised and critical estimates made
- This means we can offer tailored advice to your problems and help you to meet financial objectives within the boundaries of generally accepted practices

Benefits of choosing MAH

- City firm with technical expertise
- We act with integrity and honesty, whilst helping you achieve your objectives
- As a valued client you will never be overlooked
- Fast response within 24 hours to calls / emails
- We do whatever it takes to meet a deadline, and can regularly email you to warn of impending deadlines
- No shortcuts – our budget will never outweigh the importance of providing a high quality service
- Face to face meetings at least once a year
- Fixed fees for standard work and we accept instalments / standing orders. No hidden surprises!

Gains from choosing MAH

You could do all the work yourself, but we can:

- Save you time, so you can focus on your business, whilst not spending your leisure time on accounts/tax
- Ensure all the tax, VAT and accounts are reasonable, reducing stress and giving you peace of mind
- Save you money with tax planning, so you get to keep more of your hard earned cash to spend as you please

MAH

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