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Should I incorporate my business?

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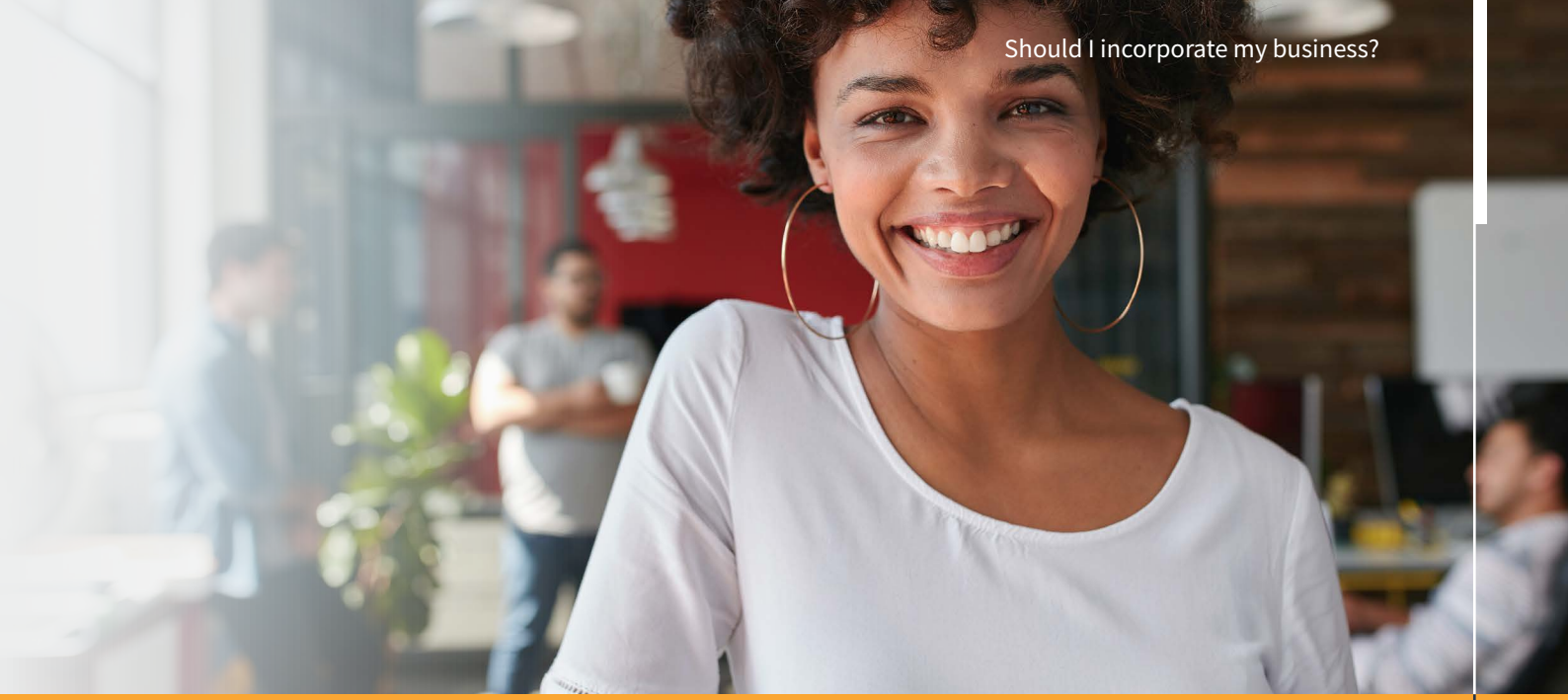
We're regularly asked about the benefits of incorporating a business into a limited company, from current clients who are sole traders and from new clients just starting out in business.

What is a Limited Company?

- A limited company is a type of business structure which is registered at Companies House as a legal entity in its own right and is completely separate from its owners.
- Legally it can enter into contracts in its own name and is responsible for its own actions, finances and liabilities.
- It must appoint at least one director who will be responsible for managing the company.
- The owners of the company are known as the shareholders and own the shares which are issued by the company.
- The same person can be the owner and director, so you can set up a company by yourself, or with other people if you prefer.

To help you decide if a limited company is the best option for you, we've examined the key differences between operating as a sole trader versus a limited company, highlighting the tax treatment and extra responsibilities you'll need to consider before making your decision.



Key differences of Sole Trader vs Limited Company

Structure

As a sole trader you're a one man band; you are the business, the owner, and the manager.

In comparison, if you decide to incorporate your business, it becomes a separate legal entity, you become a shareholder, and you serve the company as a director.

Protection

In the unfortunate event that the business has a legal dispute, or worse still, if the business fails and owes money, as a sole trader you would be sued personally.

As a limited company is a separate legal entity, the company finances are separate to your personal finances, so your personal assets and credit rating are safe.

Tax on Business Profits

As a sole trader you'll pay Income Tax and National Insurance on your business profits in the year that they're earned.

A limited company pays Corporation Tax on the business profits in the year earned.

Company tax rates are currently lower than Income Tax rates.

Paying yourself

As business profits for a sole trader have already been subject to Income Tax, you'll have no further tax to pay when you withdraw money from the business.

However, any monies withdrawn from a limited company would be subject to Income Tax and National Insurance at the time payment is made.

Note: as a director of a limited company you can decide when payments are made, which may allow you to gain a tax advantage.

Business Accounts

There's no requirement to prepare formal business accounts as a sole trader, although we'd recommend some form of accounts are kept to help you successfully run your business, or to secure funding.

As a limited company director, each year you are obliged to prepare and submit financial accounts which meet criteria set by the Companies Act, to Companies House. A company tax return, along with your financial accounts must also be filed online with HMRC.

Privacy

There are no formal requirements to publish business information as a sole trader.

Information about your limited company, including the financial accounts will be in the public domain. Each document filed at Companies House is readily available to be downloaded by any third party. However, you should be able to use your accountant as your registered office address if you're concerned about making your home address public.

Costs

You should expect to pay more in accountancy fees when you incorporate your business. You can expect to see an increase in your fees of 50-100% compared to a sole trader; this is because of the extra work your accountant will need to do on your behalf. However, this cost is usually outweighed by potential tax savings.

Legal Responsibilities

You'll have certain legal responsibilities as a limited company director, laid down by Companies House. Failure to meet these responsibilities can lead to disqualification, fines, or in the worst case, a criminal prosecution.

Key benefits of incorporating

As well as the differences already noted, here are some of the benefits of incorporating your business.

PROFESSIONAL IMAGE

Being a director and shareholder of a company can provide you with kudos as it can portray the success of your business. The reputation of your business will be enhanced, hopefully attracting more customers.

FINANCE

Whilst obtaining funding is difficult for most businesses, having a company separate from yourself may make it a little easier.

PENSIONS

As an employee, the company could provide you with a pension. This would be a tax-deductible expense, giving you a tax advantage over a sole trader.

SUCCESSION PLANNING

As a shareholder, should you wish to retire, sell your business, or in the unfortunate event of you passing away, it's much easier to transfer the business ownership than with a non-registered business.

There are many factors to consider before incorporating your business, so we'd always advise you to speak to an accountant to find out what's best for you.

Contact us now at **hello@danbro.co.uk** or call **01253 600150**

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