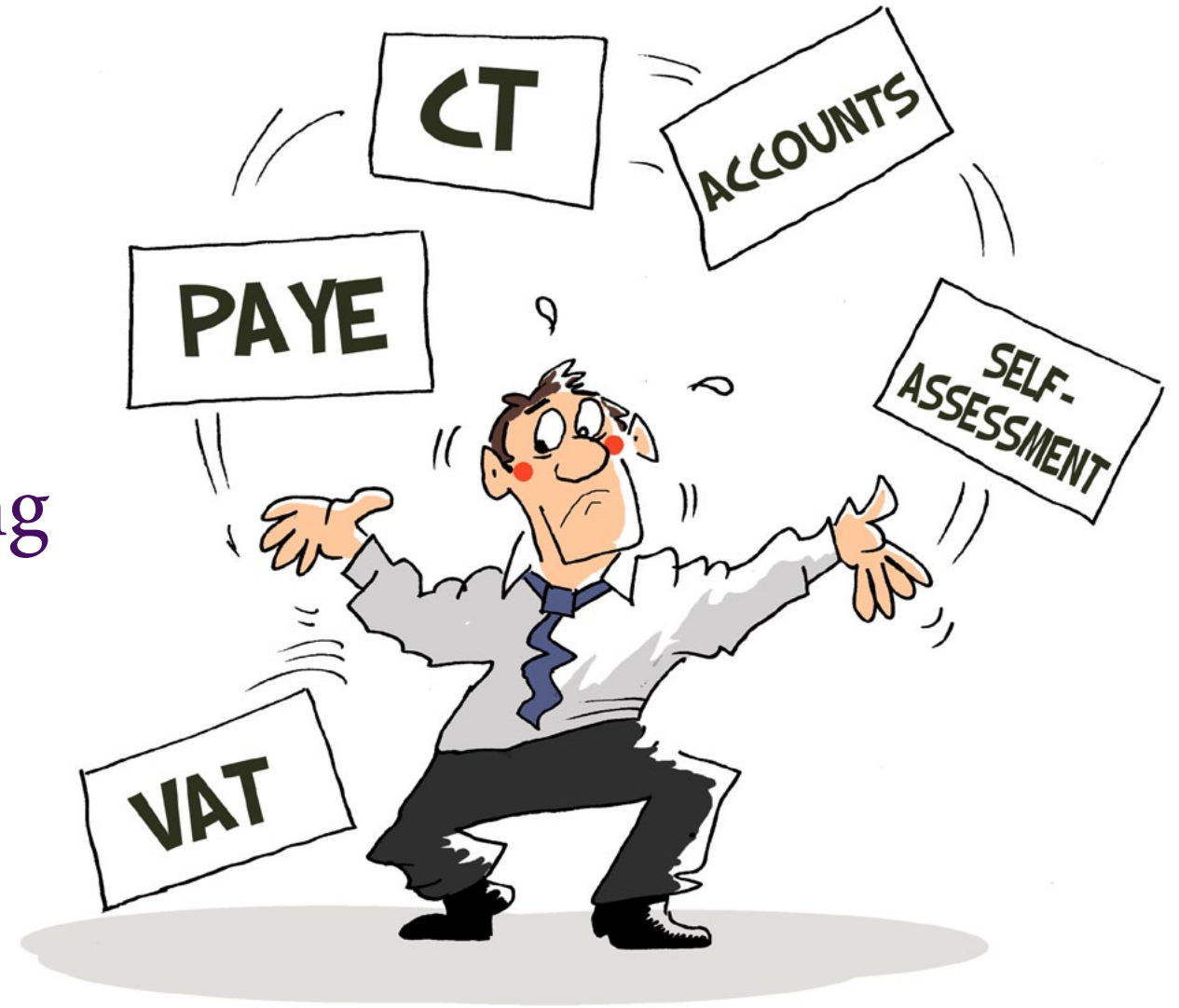


# A Comprehensive Guide To Operating As A Contractor



**YOU NEED A HELPING HAND FROM CONTRATAX**

# Interactive Contents Page



# Introduction

We want to give our clients the best value for money they can achieve whilst knowing they are receiving the best advice, customer service and quality of accounts in the market place.

## Firstly, who are Contratax?

As this guide has been written by Contratax we felt it only fair to explain who we are and what we do.

Contratax is a collaboration between two chartered accountants (one of whom is also a chartered tax advisor) and a chartered certified accountant. We only employ staff that have specialist knowledge in areas affecting contractors meaning we are at the leading edge of contractor accountants.

2013 saw the launch of Contratax and this builds on the wealth of experience and knowledge the directors have gathered from the 20+ years running and owning their own accountancy practice, specifically servicing small and medium sized entities, including detailed working knowledge of all areas affecting contractors.



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## HOT TOPICS



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## What Contratax will do for you?

We don't want to bombard you with different service levels and different prices so our service is simple, one price to cover everything! So, for just **£75+VAT per month** we will cover the following:

- Initial company setup with Companies House;
- Registration with HMRC for VAT (including Flat Rate VAT where applicable), PAYE and Corporation Tax;
- Assist in opening a company bank account with Cater Allen;
- Monthly payroll for up to two employees with full RTI submission;
- Monthly management statements including profit figures and dividends available;
- Quarterly VAT calculations with submission to HMRC;
- Annual P11d's for up to two employees prepared and submitted to HMRC;
- Annual accounts prepared and submitted to HMRC in iXBRL;
- CT600 and associated calculations prepared and submitted to HMRC in iXBRL;
- Abbreviated accounts prepared and submitted to Companies House;
- Basic self assessment for the directors each tax year.

### We also cover the following for no extra charge:

- Prepare dividend vouchers and board minutes as required;
- Prepare and submit the annual return to Companies House (including the filing fee);
- Provide a registered office facility for your Company;
- All company secretarial work i.e. change of addresses, appointment of directors etc;
- Mortgage/tenancy references or income confirmation letters;
- Reviewing all HMRC/Companies House correspondence;
- Unlimited support from a personal accountant by email, phone, post or face to face.

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# What Contratax can do for you?

## And just for completeness, the following is not included:

- IR35 contract reviews – we specialise in accounts and not law. We obviously understand IR35 and the complexities it involves, however, you wouldn't pay a lawyer to do your accounts so why pay us to review your contract, leave it to the experts instead!
- Company dissolution/winding up – prices start from just £100+VAT.
- Dormant/inactive companies – prices start from just £50+VAT
- More complex self assessment returns – these would include multiple capital gains, rental property where bookkeeping/accounts are needed etc. – price on application.

## What we need from you...

In order to provide you with the above service we need a few details from you as follows:

- Invoices raised for the month;
- Details of all 'out of pocket' expenses;
- Bank statement for the month;
- Anything received from HMRC/Companies House.

It really is that simple, provide us with the above each month and we do the rest!

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# How to Operate?

There are a number of vehicles available to contractors to trade through, each have their advantages and disadvantages. Contratax only offer services to Limited Company contractors and on the odd occasion, sole traders/partnerships (these are quite rare in the contracting world) but for completeness and for a balance of fairness we will touch on the other vehicles too.

## Limited Company

For contractors, trading through a Limited company is generally the preferred route to take. It has the benefits of an increased take home pay compared to using an Umbrella company (even if the IR35 legislation applies) and gives most flexibility around withdrawal of funds. You can also benefit from being able to claim a wider variety of expenses and can benefit from certain VAT schemes to boost your turnover.

## Umbrella Company

If you work through an Umbrella company you become an employee of that company. The advantage to this is that you don't have to worry about running your own company, IR35 or insurance.



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# How to Operate?

However, this comes at a cost and that cost is tax efficiency. When using an Umbrella company your earnings are generally 10-20% lower than using a limited company (outside IR35) because the majority of your earnings are taxed under PAYE using an Umbrella company. You also have to pay both employee and employer national insurance which is something often overlooked by new contractors.

## Sole Trader/Partnerships

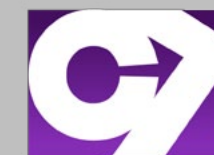
Generally, you cannot work as a sole trader/partnership in the contract market. This is because it opens up agencies and clients to employment risks if you aren't genuinely self-employed, they could also become liable for your taxes if you failed to pay them and for these reasons not many people can contract on a sole trader/partnership basis.

The main benefit of being a sole trader/partnership is that there are less reporting requirements because you can simply submit a tax return each year (and a partnership return where necessary). However, as with Umbrella companies, the downside comes in the form of tax efficiency.

This is because any profits are subject to tax and National insurance (something that is avoided by taking dividends from a Limited Company).

You could also choose to use an offshore arrangement, typically one involving loans or double taxation treaties. However, these are being widely targeted by HMRC and so are generally not a recommended vehicle to trade through.

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# The First steps to running a Limited Company

## Step 1

It is generally advisable to appoint an accountant straight away, and ideally one that is a contractor specialist. You can then be assured that you are using a professional who you can trust and rely on to give you first class quality advice. Contratax are expert contractor accountants and only deal with limited company contractors. If you want to discuss our services our contact details can be found at the back of this guide. We will also cover steps 2-5 as part of our normal service to you within our all inclusive price.

## Step 2

Choose a company name and decide on who the director(s), secretary (if desired – it's no longer a requirement for small companies) and shareholders will be. It is wise to discuss your personal tax situation with an accountant at this stage so you can ensure the correct company setup; if you are thinking of a split share holding (normally with a spouse or civil partner) then now is the best time to implement it. Once this has been decided the company needs to be formed; most contractor accountants, including ourselves, will form a company for you free of charge and it can normally be done on a same day service.

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# The First steps to running a Limited Company

## Step 3

Once the company is registered with Companies House it is its own legal entity so it needs its own bank account. You can approach any bank for this provided the account is opened in the company name, however, you want to be aware of banks charging you for business banking. We can assist in opening an account with Cater Allen, our recommended banking partner, giving you the benefit of free business banking for up to 30 transactions a month along with no minimum balance requirements.

## Step 4

Register the company with HMRC for Corporation Tax. This needs to be done within 3 months of trade commencing and should be done online once you have received a letter from HMRC confirming the company's unique taxpayer reference (UTR) which will be 13 characters long. Normally, the company will also register for PAYE (needed if a salary will be paid – more details further on) and VAT (again, discussed further on), all of these can be done by an accountant if required.

## Step 5

This step may or may not be required depending on personal circumstances. All directors in the new company now need to register for personal self assessment (if they aren't already registered) because they will be required to submit a Self Assessment Tax Return to HMRC each year. This registration can be done using form SA 1 or electronically online with HMRC. Again, a good accountant will do this as part of the initial setup process.

## Step 6

Some may consider this an obvious step and some will have already done this but you need to find yourself work in the form of a contract role. Some clients prefer to get the company set up and ready to go before securing their first contract; some prefer to secure the first contract and then get the company set up. We generally recommend setting the company up around 4 weeks before the estimated start of a contract so you can allow plenty of time to complete the necessary registrations, but it's not the end of the world if things need pushing through quite quickly due to an imminent contract start date.

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# The First steps to running a Limited Company

## Step 7

So, you have a company, all the necessary registrations have been done and you've been offered your first contract role. What to do next? You now really need to give some thought to IR35 and not just brush it under the table. IR35 is discussed in great length further on in this guide, however, it basically determines how funds can be extracted from a limited company and is dependent on your contract and working practices. As it is dependent on the contract you would be wise to get this reviewed before signing; there are many specialists who can do this (Qdos Consulting, Bauer & Cottrell to name a couple) for a very reasonable fee and it will give you some peace of mind that you have carried out due diligence with respect to IR35.

## Step 8

With everything signed and the contract underway, you will now start to think about how to extract money from the company in a tax efficient manner. This is where a good accountant will be indispensable as they should look at your personal circumstances and advise on the most tax efficient setup for you. Normally this will be with a combination of a relatively low salary (assuming IR35 doesn't apply) and dividends. But it could also include splitting shares with a spouse or civil partner, using childcare vouchers and even making pension contributions from the business account.

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# The First steps to running a Limited Company

## Step 9

Most accountants will deal with you on a monthly or quarterly basis (we work on a monthly basis) and will want details of your invoices, expenses and bank transactions. Here at Contratax we simply ask you to send these to us each month and we will do the rest, which involves processing a salary, advising on profit levels and ensuring all returns and submissions are made on time and accurately.

## Step 10

Each year you will have to submit accounts and corporation tax returns to HMRC, abbreviated accounts to Companies House and a personal tax return to HMRC. Most good contractor specialists will include all these services within their standard package and they should be completed in a relatively short space of time. We aim to have all accounts out to clients within a few weeks of receiving their information so they aren't waiting any longer than is necessary for company information.

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## Top 5 tips to when starting out

Over the years we've seen contractors come and go; some are in it for the long haul whereas others use it as a stop gap between permanent jobs – often due to redundancy. Whatever the reasons behind you choosing to contract to earn your living, we have 5 top tips that in our opinion should never be forgotten.

### 1. IR35 – Never forget it!

Like it or not IR35 is here to stay for the foreseeable future and is the single most important piece of legislation that all contractors trading through a limited company need to consider. With this in mind our tip to you is to always be vigilant in this respect. Get all new contracts reviewed, not only for what is written down but with respect to what happens in practice too (your working practices) and think like a contractor not an employee!

### 2. Get insured

Generally insurance is relatively cheap for the risks it covers so in our opinion it's a must have. We generally recommend professional indemnity insurance along with public liability insurance and employer's liability insurance and each can be purchased for a relatively modest fee if you shop around. It may also be worth considering IR35 insurance as this can cover you for the fees involved in defending a case. Some policies will cover the additional liabilities as well if you were to lose your case with HMRC, well worth the £300 (approximately) that the policies normally cost!

## HOT TOPICS



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# Top 5 tips to when starting out

## 3. Build a warchest

The term warchest is used in this context to refer to a pot of money, or available funds, that can be drawn upon in times when you are out of contract (also known as 'benched'), off sick or even on holiday. You should always remember that as a contractor you do not receive holiday pay or sick pay etc. from your client like permanent members of staff, and you may not always be lucky enough to be in contract so you need to save for when this happens.

As a rule of thumb, when contracting you should try and build up a pot of money (whether in the company or not) to cover 6 months + of outgoings to cover you in case you cannot secure a new contract quickly. This is personal preference though, some clients will like to build up between 1 – 2 years worth of funds before they feel 'comfortable' and others like to spend it now and live 'hand to mouth'.

## 4. Consider joining the PCG

The Professional Contractors Group (PCG) represents contractors across the country and lobbies the government and various other bodies on behalf of contractors. Membership starts at just £120+VAT per annum for a standard membership and £220+VAT for the 'plus' package and in our opinion the 'plus' package is preferable. Not only does it provide you with a free legal and tax helpline, professional assistance against HMRC compliance checks and a number of template contracts, it also provides some fringe benefits like jury service insurance, client/agency default insurance and many many others. Check it out at [www.pcg.org.uk/join-us](http://www.pcg.org.uk/join-us)

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## Top 5 tips to when starting out

### 5. Stay in touch with your accountant

This is so often overlooked but is vital if you want up to date advice, help and guidance from your accountant. We've seen it so many times where clients, despite numerous attempts to contact them, do not get in touch or provide us with information (even though they are still paying us) and they get into trouble with late returns, penalties, interest and normally a large overdrawn director's account meaning no way to pay company liabilities. You pay your accountant to provide a service so let us do this for you.

### 6. Remember your responsibilities

Ok, I know I said it was a top 5, but this one had to be mentioned too. As a limited company director you take on certain responsibilities that have to be adhered to. You are ultimately responsible for your company and must ensure it submits all returns on time, pays all liabilities as they fall due and maintains proper accounting records for inspection by HMRC at all times. Yes, a good accountant will help you with all this and should normally save you more in tax than you pay them, but never forget that at the end of the day it is you, as company director, who is responsible for running the company.

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# Forming a Company

Although forming a company is relatively straight forward there are a few things you need to ensure you get right and these include:

- **Appointing the correct directors** – You need at least one director that is a natural person (not a company) and over the age of 16;
- **Appointing a company secretary** – This is no longer a legal requirement for private companies so is generally optional. However, if you are allocating shares to a spouse or civil partner it is often wise to make them the company secretary so that they become an officer and thus meet this part of the criteria for Entrepreneurs relief;
- **Registered office** – This is the legal address for the company. If you don't want your personal address on the public record why not use your accountants address as your registered office (and service address);
- **Service address** – This is the correspondence address where the directors can receive correspondence from third parties about the company. Combine this address and the registered office as your accountants address and you can keep your personal address off the public record;
- **Residential address** – This has to be given to Companies House and is the usual home address of the director concerned. It will however be shielded from the general public (although certain predetermined organisations can access it).
- **Share allocation** – Generally you will form a company with 100 ordinary shares (although you are free to choose any number and type as you see fit). If you are looking to allocate some shares to a spouse or civil partner now is the best time to do it.

Although all of this is pretty straight forward and reasonably cheap to do yourself, why not let Contratax take care of this for you. New clients taking up our accountancy service will receive a free limited company setup where needed.

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# Setting up a bank account

One of the first things that needs doing once the company is formed is the setting up of a business bank account. As the company is its own legal entity it requires its own bank account. Most high street banks will be able to accommodate this without any problems however most will now charge for business banking.

## Why not try Cater Allen?

Cater Allen are part of the Santander Group and all deposits held by Cater Allen are unconditionally guaranteed by Santander UK PLC.

They offer free business banking for up to 30 day to day transactions a month (with no minimum balance requirement) when opened through ourselves as introducer, and in our opinion have an excellent customer service team!

Full details of their standard reserve account can be found at <http://www.caterallen.co.uk/reserve-account>



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# Registering for Corporation Tax

All new companies are required to register with HMRC for corporation tax, usually within 3 months of starting to trade and details of this will be sent out to the company's registered office by HMRC within a few weeks of incorporation. The letter sent out is a 'CT41G' entitled Corporation Tax – Information For New Companies and explains how to register with HMRC online.

It is important to get this right because penalties can fall due if you don't register at the correct time. All Contratax clients get this service included as part of the standard setup process so let us take care of this for you.

Once registered the company becomes liable to submit a corporation tax return (CT600) along with annual accounts to HMRC each year, and these are due 12 months after the period end to which the return relates. In certain situations two returns will be due (normally in the first year of trading when the accounts cover a period in excess of 365 days).

The company will also be liable to pay corporation tax on its profits. This is roughly calculated as income less expenses, multiplied by 20% and is something Contratax calculate as part of the annual accounts completion. If profits exceed £300,000 per annum or you have associated companies then the rate you pay may increase to a maximum of 23% (FY2013).

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# Registering for Pay As You Earn (PAYE)

If you want to take a salary (over the lower earnings limit) from the company then you need to register a PAYE scheme with HMRC. Again, this is quite a simple process which can be done online. However, if done incorrectly or at the wrong time can cause numerous problems and even lead to penalties so leave it to Contratax as we cover this free of charge for all new clients.

Once registered HMRC will allocate the company a PAYE reference and an accounts office reference meaning the company has to calculate and deduct tax and national insurance from all wages paid at the appropriate rates.

As a PAYE registered company you must also submit payroll information to HMRC in real time (RTI); this normally entails the submission of a Full Payment Summary (FPS) or an Employer Payment Summary (EPS) on or before payment of the related wages.

You will also have to pay any tax/national insurance due to HMRC; this is normally done on a quarterly basis where the average liability is less than £1,500 per month.

Finally, you will need to submit a P11d & P11d(b) to HMRC each year to report any benefits/expenses received by the employees.

All the necessary payroll procedures are included in our all-inclusive monthly service.

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# Registering for VAT

If your turnover exceeds £79,000 (2013/14) in any 12 month period, or, your turnover is expected to exceed £79,000 in the next 30 days alone, you must register for VAT. Once registered you must charge VAT on your standard taxable supplies at the current rate of 20%.

Even if you are not required to register for VAT we normally advise you to do so because it is normally beneficial from a tax saving point of view to be registered. Likewise, if you do not expect your turnover to exceed £150,000 per annum you can join the flat rate scheme.

This is a simplified method of accounting for VAT where you simply pay over a flat percentage of gross sales to HMRC and typically produces savings of anywhere between £1,000 and £4,000 per annum depending on turnover and trade sector.

As a VAT registered entity you should remember though that you have certain responsibilities to meet otherwise you could incur financial penalties.

The main ones being:

You have to submit a VAT return electronically to HMRC, normally on a quarterly basis;

You have to pay any VAT due as calculated on the return electronically to HMRC;

Contratax can register all new clients for VAT as part of the joining process and we will also calculate and submit VAT returns for all clients in our monthly all-inclusive service.

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# Registering for Self Assessment

Once you become a company director you should submit a self assessment tax return to HMRC each year. In order to do this you need to register and obtain a Unique Taxpayer Reference (UTR) which can be done by sending an SA1 form to HMRC or registering online. As part of the sign up process Contratax will take care of this for you and we will include the completion of a basic tax return for all directors each year within our standard monthly fee.

As an individual liable to complete a return you have the responsibility of submitting a self assessment to HMRC each tax year. The tax year runs from 6th April to 5th April and the tax return is due with HMRC by 31st October following the end of the tax year if submitted on paper or by 31st January if done online. You also have to pay any tax due by 31st January and possibly payments on account by 31st January and 31st July.

The self assessment must contain details of all income received within the tax year it relates to, be that salary, benefits in kind, dividends, bank interest, rental income or any other source of income you may have received. Failure to submit the return on time or failure to submit an accurate return will leave you liable to penalties and interest.

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## About IR35

Like it or not IR35 is here to stay for the foreseeable future and is the single most important piece of legislation that all contractors trading through a limited company need to consider. It has been around since April 2000 and with the current government prioritising against tax avoidance and evasion it is more prevalent than ever.

Although the rules surrounding IR35 are complicated and open to much interpretation we have tried to summarise the key points in this short guide.

The IR35 legislation can apply to anyone providing their services via an intermediary (normally a limited company/ personal service company). In particular, where the income received would be treated as employment income if the individual providing the services had received the income personally without the intermediaries' involvement.

It was introduced to stop the 'Friday to Monday' contractor where an employee would leave their employment on a Friday and return to work for the former employer on Monday, but this time, as a contractor trading through a limited company. The benefit of this was that the former employer saved on employers national insurance (currently 13.8%) and the former employee could now structure their tax affairs much more efficiently to pay less tax, and notably, little or no national insurance.

The scope of IR35 is huge, and it cannot be defined in this guide alone. It is subject to interpretation and this is always changing, mainly because there is no statutory definition of what a contract for service (self employed or outside IR35) or contract of service (employed or inside IR35) actually is.

As a result, we have to use the normal employment indicator tests and common law (past cases heard in the courts which set precedents for further hearings) to generate an indication to someone's IR35 status.

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# About IR35

Ultimately however, it is down to the director to make a judgement, normally guided by professional help, as to whether IR35 should apply to a particular engagement or not and proceed on that basis. It would then be up to HMRC to challenge that and possibly take the case through the tribunal and even the courts because neither the director, nor HMRC themselves, can decide whether IR35 does actually apply (or not); only the courts themselves can.

We shall now look at some of the main indicators to be considered in determining whether or not IR35 applies to a particular engagement:

**Direction & Control** – Does the client have control of the contractor in the sense that they can direct them to do any work as the client sees fit or has the contractor been brought in to complete a specific set of deliverables?

Does the client determine how the work has to be done or does the contractor choose how to carry out the set tasks?

Does the client determine the time and place of work or does the contractor have a choice in when and where they carry out the task?

The latter in each example is preferable from an IR35 point of view; ideally, the client should have as little control and direct the contractor as little as possible to help put the contractor outside of IR35.

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# About IR35

**Right of substitution** – Does the contractor have to complete the work personally (personal service) or do they have the choice to engage another individual or company to complete some of the set tasks? Personal service is indicative of a contract of employment so if the contractor has a reasonably unfettered right to substitution then this points to being outside IR35.

**Mutuality of Obligations** – This normally appears in all contracts, an obligation on both parties to provide something as part of the contract and HMRC's own guidelines suggest that they ignore this test when reviewing a case for IR35.

However, it should still be considered from an IR35 point of view. Is there an expectation on both parties to offer and accept work or is each party free to not offer work/ refuse work as they see fit? If there is an obligation on each party to offer/accept work then this would be indicative of employment and thus inside IR35.

**Being part and parcel of the organisation** – Although this isn't defined in statute, IR35 is all about disguised employment and contractors becoming part and parcel of the organisation, therefore, to be outside IR35 you want to try and maintain a professional but distant relationship to the client. Try to avoid going on 'team building' exercises, Christmas parties and the likes; do not participate in staff benefit schemes. Where possible, be identified as a contractor on all internal documents, name badges, emails etc. and try to avoid internal processes that only apply to employees.

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# About IR35

There are also other indicators, that although are not the main areas to consider, have some bearing when looking at the picture as a whole. They would be as follows:

1. **Provision of equipment** – If you have to provide your own computer, mobile phone etc. (i.e. your own tools of the trade) then this is a pointer to outside IR35.
2. **Financial Risk** – Do you take any financial risk within the contract i.e. having to correct defective work at your own expense. This would point to outside IR35 as employees don't generally have to cover the costs of fixing their errors.
3. **Length of engagement** – Although not a major indicator the length of engagement may carry some weight in an IR35 investigation. Generally, the longer the contract the more likely you are to become integrated into the company and may start acting like an employee. There is also more tax at stake if you have been at one client longer i.e. 3 years as opposed to 3 months.

All this may be a lot to take in but it is worth researching and understanding IR35 as it can have a significant impact on your tax efficiency if your contract and working practices are seen to have fallen within the scope of IR35. This is because the large majority (95% less qualifying expenses) of your income from the relevant engagement has to be taxed under PAYE; you even end up paying the employers national insurance contributions too!

## Get a review

You may have done your research, read your contract and tried to determine your IR35 status and are still unsure as to where you stand, or, you may think you know exactly where you stand in relation to IR35. Either way, we would always advise getting your contract reviewed by a suitably qualified person so they can advise on whether or not they feel IR35 would apply to the particular engagement. Taking professional guidance on this matter is a good step, not only should it give you peace of mind that you have some assurance as to your IR35 status, it shows you have acted diligently in the matter which is important if HMRC do investigate and win.

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# Non-Compliance

HMRC are trying to crack down on non compliance in this area and are increasing the number of compliance checks to identify companies not complying with the IR35 rules. They have specialist IR35 teams in place to conduct reviews and it has been said they will be opening more checks than ever (this will only become clearer with time though).

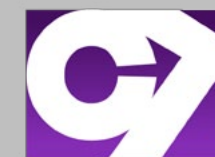
If they were to investigate and deem the IR35 rules to apply, subject to any appeals etc., then they would recalculate the tax that should have been paid in accordance with the rules and issue a demand for this outstanding tax. On top of this would be interest at the statutory rates and most likely a penalty at a set percentage of the outstanding tax.

This is determined by how the company has acted, have they been reasonable and acted diligently or have they not given IR35 a second thought. If you have had a contract review it would seem reasonable to think that any penalty will be lower than if you hadn't as you can show you were acting reasonably/diligently.

## Contract Review services

Just to clarify the matter here, Contratax do not advise on whether an engagement would be subject to IR35 or not, we refer this on to the experts in this field. You wouldn't ask a legal professional to do your accounts so why ask your accountant to review what is a legal matter! Yes, we understand IR35 (quite well we would like to think) but it just isn't worthwhile offering a contract review service when there are companies that specialise in this field, Qdos Consulting and Bauer & Cottrell are generally well recommended.

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## Business Entity Tests

The Business Entity Tests (BET's) were designed to try and give some guidance to IR35 by applying a number of tests, with a scoring system, to identify if you are high, medium or low risk in terms of IR35. Some have commented that the scoring system is badly weighted with most 'average' contractors falling into the medium or high risk categories but you should seek advice on this and make up your own mind. Further details can be found on the HMRC website, <http://www.hmrc.gov.uk/ir35/guidance.pdf>

### Further reading

If you want to read more about IR35 and in particular the latest developments in this area you may want to research the following:

1. IR35 forum minutes;
2. Dragonfly Consultancy Ltd v HMRC (2008);
3. ECR Consulting Ltd v HMRC (2011);
4. Marlen Ltd v HMRC (2011);
5. MBF Design Services v HMRC (2011).



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# Income Shifting (Settlements legislation)

## About Income Shifting

Income shifting is the common name given to the settlements legislation and behind IR35 is the second most commonly discussed piece of legislation affecting contractors. It is a piece of anti-avoidance legislation, just like IR35, that seeks to tax individuals who seek to gain a tax advantage by making arrangements to 'shift' their income onto someone else to pay a lower marginal rate of tax.

For contractors earning £100,000 per annum the savings to be made by 'income shifting' could be as much as £9,000 - £10,000 where they have a non working spouse or civil partner.

To consider if the settlements legislation applies we have to ask ourselves 5 questions.

1. Has there been a settlement – a transfer of an asset from one subject to another which causes a shift in who receives the income from said asset?
2. Is there a retained interest – does the person that originally held the income generating asset still receive a benefit from the income it generates?
3. Was the transaction bountiful – was the transfer done at below market value i.e. contained an element of bounty?
4. Were the transferor and transferee unmarried – were the original owner and the new owner unmarried/not in a civil partnership at the date of transfer?
5. Is there wholly or substantially a right to income – was the main attribute of the asset transferred a right to income i.e. a right to receive dividends over and above everything else (voting rights, capital upon winding up etc.) in relation to shares?

## HOT TOPICS



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# Income Shifting (Settlements legislation)

If the answer to each question is yes then the transaction is likely to be caught by the settlements legislation, however, if you are able to answer just one question with a no then the settlements legislation is unlikely to apply.

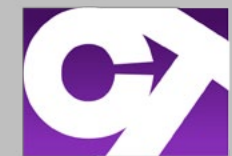
If the settlements legislation does apply then in simple terms the person who gave away the asset will be taxed on the income it generates even though they don't actually receive some or all of it.

## What about husband & wife?

The husband and wife (or couples in a civil partnership) setup is quite a common setup whereby one of them works through a limited company but both of them own shares in the company so that the income generated can be split between them. This gives a tax advantage where the 'non-working partner' can receive dividends to utilise their basic rate band where dividends are tax free and thus lower the overall rate of tax paid as a whole.

But is this not covered by the settlements legislation? Well to decide this we must refer back to the Arctic Systems case of 2007 where HMRC took Arctic Systems Ltd and Mr & Mrs Jones (each a 50% shareholder in the company) through the courts. They sought to apply the settlements legislation because Mr Jones generated all the company's income but Mrs Jones received 50% of all dividends paid as she had taken up 50% of the shares when the company was formed.

## HOT TOPICS



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# Income Shifting (Settlements legislation)

## What about husband & wife? (continued)

This case was ultimately decided by the House of Lords where the judge found that there was indeed a settlement of income from Mr Jones to Mrs Jones but the settlements legislation didn't apply because of the spousal gift exemption. This was basically because there was an outright gift (Mr Jones gifted half the shares to Mrs Jones at incorporation) and this was not wholly or substantially a right to income (the shares included voting rights, rights to capital upon winding up etc. and not just a right to dividends).

The Jones' were entitled to this exemption because they were married and living together and it is this final point that is one of the key points to consider!

If you are thinking of splitting shares with an un-working spouse or civil partner then you should ensure that your setup mirrors that of Arctic Systems as the decision handed down by the House of Lords sets a legal precedent, and binds all lower courts to come to the same conclusion given an identical set of circumstances.

### Remember:

1. Ensure you are married/in a civil partnership and living together;
2. Try and split the shares at incorporation, ideally before a contract has been secured;
3. Ensure dividends are declared and paid in relation to the shareholding;
4. If making payment to a joint bank account then ensure two separate payments are made in relation to each share of the dividend.

## HOT TOPICS



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## Other things to consider...

### 1. Dividend waivers

A shareholder can 'waive' or give up their right to a particular dividend payment and in legitimate commercial situations they can be used without any adverse tax implications. However, given the outcome of Buck v HMRC it is not something that is recommended for contractors where the shareholders are connected because HMRC have successfully argued that a waived dividend can cause a settlement that isn't covered by the Arctic System precedent. Thus, the settlements legislation can apply.

### 2. Different classes of shares

Different classes of shares can be used to manipulate dividend payments so that different shareholders could receive different amounts of dividends. Although different classes of shares can have the same rights attached to them the Arctic Systems precedent only covered 'ordinary' shares of the same class and because of this multiple share classes would not be recommended for the standard contractor setup.

### 3. Multiple share transfers

Try to avoid transferring shares more than once because if you start manipulating the share splits to keep one or more of the shareholders below the high rate threshold, HMRC may argue that the transfers are actually a right to income and as such apply the settlements legislation. You should also try to avoid declaring dividends shortly after a transfer has taken place, this is because HMRC may argue that at the point of transfer there was an expectation of the dividend payment and again this would lead to a right to income and therefore the settlements legislation would apply.

## HOT TOPICS



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## Other things to consider...

### 4. Transfers in high value companies

Where the company whose shares are being transferred holds a high level of reserves, or a high expectation to a high value of reserves in the future, HMRC may argue that there is an expectation to this income when the transfer takes place. They could then seek to apply the settlements legislation on the basis that the transfer is transferring right to income from one person to the other.

## HOT TOPICS



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# Temporary Location – The '24 month' rule

## About the 24 month rule...

We've covered IR35 and the Settlements legislation so let's now move on to the '24 month' rule.

The '24 month' rule is the common name for the legislation surrounding travel expenses and temporary locations. It is designed to allow tax relief on expense claims for travel and associated costs of an employee travelling to temporary locations whilst still employed by the same employer. It enables the employer to pay the employees travel costs tax free without crystallising a benefit in kind charge.

## What is a temporary location?

A temporary location is one at which you perform a task of limited duration or for a temporary purpose. Normally this would be a location at which you are not present for more than 24 months, nor do you expect to be present for more than 24 months.

## What can be claimed?

If you are contracting at a temporary location then you should be able to claim for the following expenses:

**Travel (including mileage) to and from the temporary location** – this must not include any 'ordinary commuting' i.e. travel between home and a permanent workplace;

**Accommodation** – this could be claimed if you had to stay overnight at the temporary location for business purposes;

**Subsistence** – this would cover breakfast and evening meal when staying away from home for business purposes and also the cost of lunch at, or on the way to, a temporary location. It would not cover the cost of making a packed lunch at home and taking it to work;

**Personal incidental expense allowance** – this can be paid to an employee (this is an un-receipted claim) when staying away from home at a temporary location at the rate of £5 per night (£10 if overseas) to cover incidental expenses like laundry and newspapers.

## HOT TOPICS



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## Temporary Location – Other Considerations

### Only one workplace during the employment

If you only work at one site during your employment then this would not be seen as a temporary location and as such no travel/related costs could be claimed.

### Multiple sites within one location

Multiple sites could be viewed at the same location if the journeys involved to get there are substantially the same. An example would be the city of London and the financial sector, moving from one bank to another down the road would more than likely be seen as the same location and as such it would be the total time spent at both banks that counts towards the 24 months.

### Working at more than one site

If you work at more than one site and don't spend more than 40% of your time at a particular site (over a rolling period of 24 months), the duties performed are of a temporary nature. The site isn't a permanent location therefore travel expenses to that particular site can still be claimed, even if attendance exceeds 24 months.

### Returning to a previous site

In order to 'reset' the 24 month clock there needs to be a substantial break in attendance at that site. This substantial break would have to exceed 15 months (60% of 24 months) to ensure that the clock is reset. Breaks shorter than this would fall foul of the 40% rule as mentioned above when working at multiple sites over a 24 month period.

There is a wealth of information on this issue, including detailed examples in the HMRC helpsheet 490 – Employee Travel on the HMRC website here: <http://www.hmrc.gov.uk/helpsheets/490.pdf>.

## HOT TOPICS



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# Temporary Location – Other Considerations

## Further information on expense claims

Having determined that the location you are travelling to meets the criteria to be treated as a temporary location and noting what can be claimed as above we will provide some further information on these claims.

## Travel expenses

Travel could include that by train, plane, bus, taxi or any other form of transport. In general HMRC cannot argue on the amount spent on travel i.e. deny relief for first class travel unless the travel was seen as a reward for service but this would be rare. The use of taxis should be restricted, ideally to times where it is only necessary to use one or where public transport is not available i.e. early mornings or late at night.

You should obtain a receipt for all travel claims as proof that the expense has been incurred otherwise HMRC could deny relief.

## Mileage claims

When travelling in your private vehicle to a temporary location you can claim Approved Mileage Allowance Payments (AMAP's) at HMRC set rates to ensure they are tax and national insurance free, the current rates being:

1. Motor Car – 45 pence per mile for the 1st 10,000 miles, 25 pence per mile thereafter. The 10,000 limit resets on 6th April each year;
2. Motor Cycle – 24 pence per mile, no mileage limit;
3. Push bike – 20 pence per mile, no mileage limit.

To justify the claims in the event of a HMRC compliance check you should keep detailed mileage logs of all trips claimed. These logs should include a date, start and end location (including postcodes), reason for the journey and total miles travelled.

## HOT TOPICS



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# Temporary Location – Other Considerations

## Accommodation

If claiming for accommodation because you have to stay away from home due to business commitments then you should ensure the standard of accommodation is reasonable and in line with your normal standard of living. Lavish or expensive hotels or rented flats could be seen as a reward for service rather than a legitimate business expense. If this was the case a benefit in kind could arise. Claims may also be restricted if the employee is accompanied by family or the reason for the accommodation is not 100% business related. Remember to obtain receipts for all accommodation claims.

## HOT TOPICS



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## About Dividends

Dividends are a return to shareholders from the profits of a company in which they own the shares.

Typically, contractors operating outside IR35 will take a relatively low salary leaving a relatively large amount of profit in the company. Once this has had corporation tax deducted it is available to be distributed to its shareholders. This is a more tax efficient way of operating because dividends falling within the basic rate band are tax free to the individual and they are also free of National Insurance.

To declare a valid or legal dividend the directors of the company need to hold a meeting to determine the value of dividend to be declared. They should consider the levels of retained profit in the company as these must cover the value of dividend being declared. The correct paperwork needs to be drawn up (minutes of the meeting and dividend certificates).

Once the dividend has been declared it should be paid to the shareholders in relation to the shares they hold i.e. if you hold 50 shares and a dividend of £10 per share has been declared the shareholder would receive £500.

## HOT TOPICS



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## Dividends

## How are dividends taxed?

To understand how dividends are taxed we need to appreciate how dividends are received. Dividends from UK companies are received net of a 10% tax credit; this means that for every £900 of dividends received you will be taxed on £1,000, the £900 being the net dividend and the £1,000 being the gross dividend.

If your total gross income does not exceed £41,450 then there will be no further tax to pay on the dividends received; this is because the gross dividend is subject to a 10% tax rate which is covered by the tax credit as mentioned above. Dividends in excess of the high rate threshold are subject to 22.5% tax (32.5% less the 10% tax credit), this equates to an effective rate of 25% on the net dividend, and dividends in excess of the top rate threshold are subject to 27.5% tax (37.5% less the 10% tax credit).

Assuming a standard salary of £7,692 and no other income for 2013/14 then you can receive net dividends of £30,382 before paying any additional tax on them but to help you calculate this at any point in the year you should use the following pro forma calculation:

High Rate Threshold	£41,450.00
---------------------	------------

Less

Projected salary for the year: (£7,692.00)

This could be from your company or other employments

Projected gross bank interest:(£ XXX.XX)

This would be estimated bank interest for the year

Any other income: (£ XXX.XX)

This could include rental profits or gross foreign dividends

Gross dividends available: £ XXX.XX

Multiply by 90% \*90%

This eliminates the tax credit from the calculation

Net dividend available: £ XXX.XX

## Dividends you can receive before paying High rate tax

## HOT TOPICS



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# Dividends

## continued...

Dividends taken in excess of this figure will be subject to further taxes at a rate of 25% of the net dividend, on the assumptions your total income does not exceed £150,000. However, if your total income exceeds £100,000 you will lose your personal allowance at a rate of £1 for every £2 your income exceeds £100,000, to a point where your income exceeds £118,880 you will have no personal allowance.

Also, if you or your partner are in receipt of child benefits then these will be withdrawn in part if your income exceeds £50,000 to a point that they will be withdrawn in full if your income exceeds £60,000.

If you can structure your income so that it doesn't exceed the £100,000 threshold you can avoid losing some or all of your personal allowance. If you ensure it doesn't exceed £50,000 you won't lose any child benefit payments (where applicable) and if it doesn't exceed the high rate threshold (£41,450 2013/14) you won't have any further tax to pay on the dividends.

Whatever you do, make sure you know how much income you are drawing and what the personal tax implications will be, you don't want to become liable for tax in January that you can't afford to pay. If you want an easy, simple to remember rule, just save 25% of any dividend received from the company and you should have sufficient funds to pay any resulting tax liability.

## HOT TOPICS



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# Student Loan Payments

## About Student Loan Payments

If you have a student loan that needs to be repaid this will need to be declared on your self assessment return each year. You need to remember that it is the gross dividend that counts towards your income when calculating how much your repayment will be, as when your gross income exceeds £16,365 you will be required to pay 9% of the 'excess' income to HMRC to pass on to the Student loan company.

## Payments on Account

Many first time contractors get caught out with payments on account that become due following the first year of being within self assessment. Once you have completed the first self assessment to 5th April you may have a tax liability that will be due for payment by the following January and if this liability is over £1,000 you will also be required to make payments on account to HMRC.

The payments on account are calculated at 50% (each) of the previous years liability and are due for payment by 31st January within the tax year and 31st July following the tax year.

To illustrate this with an example, say for 2012/13, the first year you did a self assessment, your liability was £4,000, this will be due for payment by 31st January 2014. At the same time you will also be due to make two payments on account against any potential liability for 2013/14, these will be due at a rate of £2,000 each and due for payment on 31st January 2014 and 31st July 2014.

## HOT TOPICS



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## Employer Liability Insurance

This covers the employer against claims brought against it by its employees for injuries at work etc. Legally it is no longer required if you are the only employee and hold at least 50% of the share capital but is generally available as part of a package with Public Liability Insurance at no extra cost so may as well be taken.

## Public Liability Insurance

This covers the company against claims made by a third party in the case of claims for injury, death or damage to their property as a result of the company's, or its employees actions.

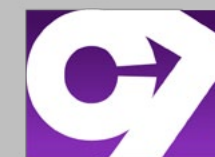
## Professional Indemnity Insurance

This insures the company against claims made against it by a third party as a result of defective work etc. A common example of this would be where a client suffers a financial loss as a result of poor work or negligence by your company.

## Professional Contractors Group (PCG)

The Professional Contractors Group (PCG) represents contractors across the country and lobbies the government and various other bodies on behalf of contractors. As part of their membership packages they offer group insurance policies that may be worth looking at. Check them out at [www.pcg.org.uk/join-us](http://www.pcg.org.uk/join-us).

## HOT TOPICS



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There are also a number of other companies that offer insurance at competitive prices, a couple to be recommended are Qdos Consulting and Hiscox. You may also want to consider the following insurance, although some may give rise to a benefit in kind:

## Private Medical insurance

The Company can pay for insurance to cover its employees in the case of medical conditions. However this will always be a taxable benefit and in some cases must be taxed via payroll so it's generally not tax efficient to do this via the company.

## Life insurance

The company can pay for life insurance for its employees and depending on how the policy is written, who pays for the policy and who the beneficiaries are will determine the tax treatment of this. Generally, the only policies that can be taken out tax free are 'relevant life' policies.

## Critical illness / income protection policies

These provide cover in the event that services cannot be provided by either the company or the employee. If the policy covers the company and is paid from the company account then it's not normally a benefit in kind but any pay-out is received by the company.

If it covers the employee and the proceeds of a claim would go to the employee then a taxable benefit is most likely to arise.

If you were thinking of taking out any of the three preceding policies we would recommend you speak to a financial advisor to ensure your needs are fully accounted for.

## HOT TOPICS



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## About Expenses

There is one question that gets asked more than any other by contractors, new and old, and that is 'what expenses can I claim?'. Quite frankly there isn't a definite answer to this because all contractors will have different businesses and thus different expense needs. As a golden rule, if the expense is 'wholly and exclusively for business use' it can be claimed through the company.

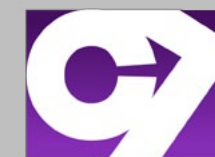
Now what does 'wholly and exclusively for business use' actually mean? Broadly speaking this means that there is no duality of purpose i.e. it only has one purpose and that purpose is for business use. For example, if you incur postage costs sending a business report to your client, this is 'wholly and exclusively for business use' and it only has one purpose (getting a business report to a client) and as such the postage costs could be claimed through the company.

Having established that anything that is 'wholly and exclusively for business use' can be claimed through the company we can now look at some of the more common expenses that are claimed and outline any particular areas that you need to be aware of in making a successful claim.

Before going further, remember that, any expenses claimed from the company aren't freebies, they still ultimately come out of your pocket because there will be less profit in the company. In reality you are only saving 20% on the expense (and arguably the high rate tax on the income used to pay for them) so you should question whether it really is worth trying to justify some of the more 'dubious' expense claims. In my opinion it's not, especially when it's just one more thing HMRC could question, by all means claim everything that is legitimately for business use but be sensible about it too.

And finally, always remember that it should be the company, not the individual, that commits to any contract and that all invoices whenever possible should be in the company name.

## HOT TOPICS



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## Annual Events

The company can take out all its employees on an annual event each year, most commonly a Christmas party but any annual function is acceptable, and the costs of this will be deductible for corporation tax purposes. You can also hold more than one annual event each year, provided they are indeed annual events so this could also include a function on the anniversary of incorporation along with a summer ball for example.

However, for these to avoid a benefit in kind charge the following need to apply:

1. The total cost (including VAT) must not exceed £150 per person per year. Exceed this and the whole amount will be subject to tax and NIC;
2. All staff need to be invited, however, this is normally just yourself.

Partners can be invited, but if they are, all employees must be allowed to bring a partner. Each partner will then be counted as a 'head' for the £150 allowance.

## Childcare Vouchers

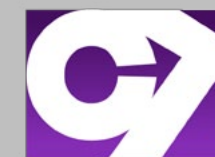
If you are paying for childcare personally then you need to consider how the company can contribute to these costs in a tax efficient manner.

Providing you are a basic rate tax payer from a salary/benefits point of view then you are eligible to receive up to £243 per month in childcare vouchers from the company free of tax/national insurance (this amount is proportionally reduced for high rate/additional rate taxpayers). There are two ways the company can provide this.

They can contract directly with a voucher provider (Busy Bees and Kiddivouchers seem to be highly recommended) to issue physical vouchers to the employee who can then use them to pay for childcare at their registered provider.

This is normally the easiest method of provision but the voucher providers normally charge up to 10% admin fees for the service.

## HOT TOPICS



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## continued...

Alternatively, the company can make a direct agreement with the registered childcare provider to purchase childcare and provide this to their employee. All that is needed is a letter of agreement between the company and the childcare provider stating how much childcare will be purchased each month and details of the employee this will be provided for.

Regardless of the method you choose you need to consider the following:

- The childcare vouchers must be paid directly from the company bank account. They cannot be a reimbursement to the employee directly;
- The child/stepchild for whom the childcare is provided must be yours and they must live with you;
- The child only qualifies up to 1st September following their 15th birthday (16th birthday if they are disabled);

- The childcare vouchers can only be used at registered/ approved childcare providers;
- The childcare provider must not be related to you unless they run their own childcare business and also look after unrelated children.

Overall childcare vouchers are a great way to increase your tax efficiency when operating through a Limited company.

## HOT TOPICS



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## Client/Business Entertaining

Unfortunately business entertainment is not an allowable expense for corporation tax purposes so putting these expenses through the company will not give rise to a corporation tax deduction. That said, it is still worth putting any genuine business entertaining through the company as it saves having to pay it out of your personal income which may have been subject to tax.

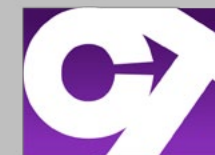
Excessive business entertaining may be questioned by HMRC so you need to ensure you keep detailed records of whom you are entertaining, the reason for the entertainment and what you hope to get out of the entertainment to justify it as a genuine business expense.

## Clothing

The area of clothing costs is a commonly misinterpreted area because for clothing to be allowable, without giving rise to a tax charge on the employee, it must be either protective in nature or constitute part of a uniform that cannot be worn outside of work. It is normally quite obvious if the clothing is protective in nature (a hard hat, steel toe capped boots etc.) but it is much more subjective as to whether something constitutes a uniform or not. As a rule of thumb something bearing the company logo would constitute a uniform, but general office clothing would not.

Therefore, suits, ties, shoes etc. would not be allowable through the company without giving rise to a benefit in kind charge.

## HOT TOPICS



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## Company Cars

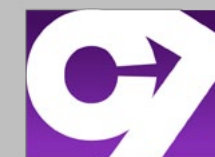
A common misconception amongst contractors is that Company Cars are appropriate to put through the company because they save tax, but this is generally not the case! This is because you effectively end up paying both the employee tax and also the employer tax.

In the majority of cases company cars will actually cost you tax compared to owning/leasing the car privately so you really do need to give it some consideration before committing to a company car. Normally, company cars are only beneficial if they are very low emissions, you do a large private mileage or you are brought within the '24 month' rule (as explained previously).

To clarify some of the most commonly confused areas:

- VAT cannot be reclaimed on the purchase of a new car and it's not normally charged on second hand cars so in most cases there is no VAT to reclaim on the purchase of a company car;
- VAT on car lease costs can only be claimed in part, 50% on the vehicle lease and 100% on the maintenance costs. However, this assumes you aren't on the flat rate scheme, if you are no VAT can be reclaimed in any situation;
- The company does save corporation tax but this won't be as much as you think. If you purchase the car you can only claim capital allowances at 8% or 18% depending on the CO2 emissions of the car. If it's leased you get relief on 100% of the cost, provided the CO2 emissions are below 130 g/km, over this relief is restricted to 85% of the cost.

## HOT TOPICS



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## Company Cars continued...

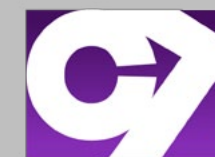
If you do decide to get a company car you will be in receipt of a benefit in kind, calculated as follows:

- Work out the benefit in kind percentage – roughly speaking this is the CO2 emissions less 95, divided by 5, rounded down to the nearest whole percentage with 11 added to it (if it is diesel you then add on 3%). Please note the maximum this can be is 35% and special percentages apply to cars with CO2 emissions below 95g/km.
- Multiply the list price of the car, including any optional extras but less any capital contributions (maximum £5,000), by the percentage calculated above. This will give you the benefit in kind value of the car.
- From the calculated benefit in kind deduct any personal payments to the company to cover private usage of the car and this gives you the taxable benefit in kind figure.

If fuel is also provided for private use then you will be liable to the fuel benefit which is calculated at a flat rate of £21,100 multiplied by the benefit in kind percentage. This is regardless of the value of fuel provided so in most cases it's very unwise to provide fuel for private use.

The major disadvantages to a company car are that the company has to pay class 1A national insurance (13.8%) on the value of the benefit and the employee will pay tax on this benefit at his marginal rate. For most contractors on the low salary/high dividends setup this will result in an extra 20% tax. However, it also means that more of their basic rate band is consumed leaving less available for tax free dividends and in most cases they end up paying the equivalent of 42.5% on the benefit in kind value (20% tax and 22.5% tax on the dividends now in the high rate band).

## HOT TOPICS



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## Company Vans

As an alternative to a company car you could be provided with a company van. These are more tax efficient compared to company cars, although they do still give rise to a benefit in kind. However, you can't simply cover up the back windows of an old car, the van must be purpose built and meet the strict HMRC criteria (a goods vehicle with a maximum legal laden weight of 3,500 kilograms).

If you were thinking of a company van it has the following benefits compared to a company car:

1. Flat rate benefit in kind value of £3,000 p/a regardless of CO2 emissions. If fuel is provided for personal use this is increased by £564;
2. VAT can be reclaimed on the purchase of a company Van, even when you are on the flat rate scheme (assuming the cost exceeds £2,000);
3. No restriction on capital allowance claims based on CO2 emissions. This means that the van will normally receive 100% corporation tax relief in the year of purchase utilising the AIA.

As with company cars the same tax treatment then applies, the company pays 13.8% class 1A national insurance and the employee pays tax at their marginal rate.

## HOT TOPICS



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## Computer Equipment

If you need any equipment, normally a computer or laptop to carry out your trade then you will be fine putting this through the company. However, you do need to ensure that any private use is insignificant to avoid a benefit in kind charge arising.

Most Limited Company contractors will be on the flat rate scheme so can only reclaim the VAT on any equipment if the total cost (including VAT) exceeds £2,000. If you were considering purchasing equipment for £1,667 then you would be no worse off if you purchased a few ancillary items or increased the spec to bring the total cost up to £2,000 (provided it was all from the same supplier on the same invoice) so that you could reclaim the VAT. A simple but effective tip to get improved equipment for the same effective cost!

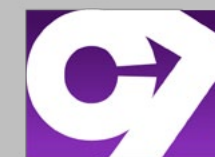
## Homeworking expenses

If you provide equipment, services or supplies, for business use only to an employee that works from home then these are fine to claim with no benefit in kind arising providing any private use is insignificant. Things that could be provided would include a computer, office furniture, pens and paper, internet connections (see below) etc.

You can also reimburse additional household expenses i.e. gas and electricity provided that the employee is required to work from home and the facilities aren't available at the normal workplace. This being the case, provided the amount reimbursed does not exceed the additional household expense there will be no benefit in kind arising from the transaction.

In reality, it is probably not wise to make a claim in this way as it could be open to question by HMRC and for the costs involved probably isn't worth it. Instead why not just claim the flat rate allowances that need no record of household expenditure, the current amount being £18 per month or £208 per annum. This is quite often more than the actual additional expenditure incurred from working from home anyway.

## HOT TOPICS



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## Internet Connection

You can put the cost of an internet connection at your home through the company provided you take out the contract in the company name and pay from it direct from the company account. However, you do need to ensure that any private use is insignificant to avoid a benefit in kind charge arising.

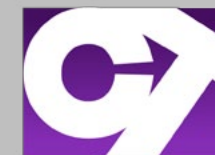
The same applies for a landline connection, however, in order to get the contract in the company name you may well need a second line installing and given the normal costs involved with this it is normally cheaper to simply keep any landline connections outside the company.

## Mobile Phones

One mobile phone can be provided to an employee, free of tax and national insurance provided the contract is taken out by the company and is paid direct from the company bank account. It will also receive a deduction for corporation tax purposes even if there is private usage. This exemption covers the initial cost of the handset (including smartphones), the monthly line rental and the additional cost of any calls/texts/data etc.

This can be a great exemption for the company as it means that you can effectively cover the cost of your day to day mobile phone through the company. However, you should make sure that you don't end up paying more for a business contract than you would do for a personal one. You are only saving the corporation tax so if the personal deal is 25% or more cheaper than the business deal you may be better off going taking the personal contract and avoiding the company altogether.

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## Training Costs

If you are considering improving your skills or just refreshing yourself then you may be considering putting these costs through the company. However, you will be surprised at just how little in terms of training costs can be claimed as a tax deductible item in your accounts but this doesn't mean you shouldn't still claim them, you just might not get corporation tax relief.

Firstly, in order to avoid a benefit in kind on the training costs the training must be work related. This means it must be designed to impart, instil, improve or reinforce any knowledge, skills, or personal qualities which:

- are, or are likely to prove, useful to the employee when performing his/her duties or
- will qualify or better qualify the employee to undertake the employment, or to participate in charitable or voluntary activities arising through the employment.

The training must relate to the employee's current employment or to a "related employment".

Assuming that the above qualifies, then the training costs, along with any associated costs such as travel and accommodation, will be deductible, for corporation tax purposes, if they are designed to enhance a current skill rather than develop a new one. If the training is to impart a new skill then this may not be eligible for corporation tax relief.

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# Pension Contributions

## About Pension Contributions

Depending on your personal circumstances, making contributions through your Limited Company can be a great way to increase your tax efficiency.

Provided that the contributions are 'wholly and exclusively' for the purpose of trade then the contributions will be allowable against tax in the year they are paid (take note they cannot be 'accrued' into the accounts for tax purposes). In practice, for one person Limited Companies, HMRC should accept that pension contributions form part of the overall remuneration package of the fee earner and shouldn't look to disallow them if they don't cause the company to make a loss and are within the annual pension allowances each year.

As a rule of thumb, it is normally most tax efficient to make personal contributions up to 100% of your salary (it is the gross contribution that counts) with any additional payments coming from the company. However, the tax saving between the two is normally less than 1% so in practice most contractors chose to make all payments direct from the company as company contributions to avoid the administration of two different payments. Doing it this way also has the added benefit in that it effectively IR35 'proves' the money because company pension contributions are an allowable expense when working out the IR35 deemed salary.

Unfortunately Contratax isn't authorised to give specific pension advice (only the tax implications of making contributions) so if you are considering setting up a new pension, or contributing to a current pension we would recommend you speak to a suitably qualified pension advisor.

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## Wages – Main fee earner

The wages paid to the main fee earner should automatically be deductible in calculating taxable profits. The only time this would not be the case is if an abnormally large salary was paid which caused the company to make a loss in a given accounting period.

The 'average' contractor (if there is such a thing) normally takes a salary up to the secondary national insurance threshold, which is £7,696 for 2013/14, as this is the level at which the salary should be free of tax and national insurance. This is on the basis that they are outside IR35.

However, taking such 'small' salary does come with a few caveats:

1. Be aware if you are making personal pension contributions as these are normally capped at 100% of relevant earnings (normally gross salary). You may want to consider company pension contributions to avoid this issue;
2. Is your IR35 insurance linked to your salary level? Some insurance products specify a minimum salary that must be paid so check your policy documents carefully;
3. You cannot have a written contract of employment in place between yourself and the company. If you do you will be subject to the National Minimum Wage (NMW) legislation and as such a higher salary must be paid (currently around £11,500 per annum).
4. You also need to remember that the level at which national insurance first becomes due may be lower in the first tax year of trading. This is because director's national insurance is calculated on a cumulative basis and the thresholds are reduced if you become a director part way through the tax year (although they aren't if you cease to be a director part way through the tax year). You will also need to ensure that your salary exceeds £5,668 (2013/14) as this is the current lower earnings level at which you get a years credit for national insurance purposes.

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## Wages – Secretary or admin assistant

You can pay wages to a secretary or admin assistant and these will be allowable provided the overall remuneration package is in line with the work they do and the responsibilities they hold. Normally, however, the person you are paying this to will be a spouse, dependant or relative and this is where HMRC may start questioning as they may see the payments as not 'wholly and exclusively' for business purposes.

If you do want to pay someone in this way you should ensure that the wages paid are in line with market rates and that they comply with National Minimum Wage and you have a contract of employment in place to cover things like holiday pay and sick pay. A good way to gauge whether the remuneration is reasonable would be to ask yourself, 'would you pay the same wages to a random third party to do the same job?' If you can honestly say yes then it should be acceptable paying this to a connected person.

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