Business Start-Ups...Should You be a Sole Trader or a Limited Company?

If you are thinking of starting a new business then you may be wondering if you should be a sole trader or a limited company.

So what are the differences?

Here we look at both methods in more detail to understand the pros and cons of both.

According to the British Chamber of Commerce there are over 3.6 million people making a living from sole trading, which most certainly tells us how popular it is. Conducting your business this way is a viable easy option and it can be much more convenient. There are no set up fees, only one self-assessment tax return to file each year and it is easier to keep track of your finances and setting money aside for taxes.

It all sounds well and good but unfortunately there is one big catch.... A sole trader is not recognised as a registered business therefore any capital you put into the business is not protected by government laws. Personal assets such as your house or car could be at risk if your business fails and you are left with debts to clear. Limited companies do not have the same risk as they are seen as a separate entity to your personal finances and if things do go wrong then you will not be personally liable.

Which companies benefit the most form being limited?

When looking at which companies benefit the most from being limited, it really all comes down to how much money your business is making. Most businesses won’t benefit from the perks of incorporating until they are showing profits of around £25,000 a year. This is mainly due to the introduction of registration fees and corporation tax when a company is incorporated. Once these are deducted from your annual income, you could be left with very little.

However, for companies beginning to turn larger profits, forming a limited company can actually be more cost efficient. Tax reliefs are available on business expenses, so if you have paid for things like, equipment, machinery or uniforms then they are usually exempt from corporation tax. For small businesses producing profits of less than £300,000 a year, this can mean significant savings, especially if you pay your shareholders in tax-free dividends. If you are in doubt over the classification of an expense, then it is worth asking an accountant for their advice.

How will I know when to incorporate?

There isn't really a definitive answer to this question, but you can usually work this out by considering the above factors. Firstly, you need to consider your liability. Are you largely funding the company yourself? Do you stand to lose a significant chunk of this money if something goes wrong? Because this risk is so high if you are a sole trader, many businesses choose to go limited, even if they are not actually achieving large profits. For example, if you are running a company which involves the general public and one of your customers is injured then you could become liable for any legal claims. Although you can take out insurance policies to minimise the risk, one small mistake or misread clause in the paperwork could leave you vulnerable.
The main thing to remember is that you can incorporate at any time. If you begin to worry about the security of your finances, then going limited might be the right step to take.

For more help and advice on how to grow your business successfully

TALK TO US TODAY.

We have a team of dedicated professionals who are happy to assist you.

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