<u>When is the right time to become a limited company?</u>

Being a sole trader is a good option for many small businesses, but there are various reasons why you may want to trade as a Limited Company instead. Every business is different and the right time to make the transition will depend on the business's specific circumstances.

Many believe that becoming a limited company will save them a lot of tax and while there are tax savings to be had they are not as good as they used to be. The amount of tax saved will depend largely on whether you need to withdraw all the profit from your limited company or whether you are leaving profits in the limited company to reinvest, and what tax bracket you are currently in.

It is useful to look at the main advantages and disadvantages of becoming a Limited Company.

Advantages of incorporation

- You have limited liability protection – This prevents individual company directors being personally liable for any of the company's financial losses. In a sole trade, owners are personally liable for all business debts and liabilities.
- Tax efficient – Profits from a company are taxed at between 19% and 25% depending on the level of profit compared to sole traders who pay 20%-45% income tax and are subject to National Insurance contributions. If you are a director and shareholder in the company, you can choose to take a small salary and withdrawal dividends from the company which are not subject to NI and have a lower income tax rate than a salary.
- Professional – In some industries, a limited company can provide a more professional image and encourage more confidence and trust among suppliers and customers.

Disadvantages of incorporation

- More compliance – A sole trader must only file a personal tax return to HMRC each year. A company must prepare and file accounts in line with Companies Act 2006 annually to Companies House, along with compliance statements, as well as file accounts and a company tax return to HMRC. This will incur extra costs.

- Losses – If a company makes a loss this can be offset against the previous year's profits or carried forward against future profits. This can be a disadvantage especially in the early years of the business, whereas if a sole trader makes a loss, this can be set against other income and save tax.
- Filleted accounts on public record – When you file your limited company's accounts and confirmation statement, these are available for anyone to see on Companies House.

It is usually the case that as your business grows there are more advantages to becoming a Limited Company. The tax savings in the company are likely to be higher and the financial risk of not having limited liability will also be higher. Deciding whether to incorporate your business should be a discussion that you have with your advisor at the outset. This should be reviewed regularly and certainly if your income or risks have increased.

For more help or advice about any of the ideas covered in this guide, Westcotts is here to help. To contact a member of our team for further advice please find the contact details of your local office on our website by following this link. https://westcotts.uk/contact-us/