



A guide to contracting

By SG Accounting

FIRSTLY welcome

FROM SG ACCOUNTING

Do you have a burning desire to be your own boss? Have you heard about the financial benefits? Or, maybe you want to expand your skills and your current employer can't offer this? If this sounds like you, contracting maybe the right route to take.

We're sure you have many questions. So, we've put together this comprehensive guide to dispel any myths and to help prepare you for the journey ahead.

At SG Accounting we are proud to say that we take a different approach to accounting. When we start working together we like to arrange a face to face meeting; we come to you so we can discuss your needs in greater detail. Don't worry we are not scary and we'll try not to bore you too much by talking about tax!

We understand that all contractors' needs are different. But the one thing that stays the same is our promise to you: we guarantee you will receive a personal, professional and expert service - every time you speak to us.

Daniel Mepham
Partner

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MAKING THE MOVE

Pros and cons

People take the move to contracting for various reasons. They might:

- Be looking to take the next step in their career
- Need more flexibility
- Want to take home more money.

Whatever the reason, switching to contracting is a lot simpler than you may think. To help you to understand what to expect, we've set out the pros and cons of contracting.

“A mind that is stretched by new experiences can never go back to its old dimensions”

- Oliver Wendell Holmes, Jr

Pros

- You're no longer an employee. You are your own boss.
- You can expect to earn more money as a contractor (in some industries this can be two or three times as much as your employee counterparts)
- You can claim for more expenses that are related to working as a contractor
- You have greater control over who you work for, when and where
- Greater opportunity to expand your skills and knowledge
- You have the option to take extended breaks during contracts. Which may work better for your personal circumstances
- You get to work with different people on each project (avoiding the office politics that can come with permanent employment)

Cons

- Less job security (but the same can be said about permanent roles as well)
- If you don't work, you don't get paid
- It's your responsibility to find your next contract. Which means being proactive with job-hunting
- If you are not well, you don't get sick pay (although critical illness insurance is available)
- If you want to go on holiday you don't get holiday pay
- You're not entitled to receive company benefits, like pension contributions
- You may face a longer commute for the right contract



Swapping from permanent employment to contracting is not something that should be done on a whim. However, the rewards in most cases outweigh any downsides.

TIME TO TALK

Numbers

What does it take to become a successful contractor? Well, we certainly would say it takes determination, drive and hard work. Making it long term as a contractor also involves being able to make enough money to live off.

WHAT CAN YOU EXPECT TO EARN?

The contracting community is massive. It covers engineering and construction, accountancy and finance, healthcare, IT and so much more. On average, a first-time contractor can expect to charge a day rate between £300 - £500, depending on the industry and geographical location.

Contractors with niche skills are in greater demand and thus can charge more. For instance, some cybersecurity contractors are charging more than £500 per day. Similarly, contractors in London can charge more than their counterparts in other areas of the country, simply because there is a greater demand for them.

As a contractor working through a limited company, you should expect to take home between 70% - 80% of your contract value after you've paid any tax liabilities owed, VAT and accountancy fees.

THE FIGURES TALK FOR THEMSELVES

To show you what this means, we've put together an example that looks what a PAYE employee in IT and what an IT contractor working via a limited company will earn:

Assumptions:

£400/ day contractor rate
£1,858 Accountancy fees
£25/ day travelling & subsistence
£50/ month mobile phone

	SALARY	CONTRACTOR
INCOME		£96,000
SALARY	£75,000	£8,164
EXPENSES		(£1,858)
TRAVEL & SUBSISTENCE		£6,000
TELEPHONE		£600
PROFIT		£79,378
CORPORATION TAX (19%)		(£15,081)
DIVIDENDS AFTER TAX		£64,297
NET TAKE HOME PAY	£51,280	£79,061

WHICH IS BEST FOR YOU...

Umbrella or Limited Company

If you decide to become a contractor there are different ways you can operate. The two main options are through an umbrella company or via your own limited company.



WHAT IS AN UMBRELLA COMPANY?

Firstly, it's got nothing to do with umbrellas! An umbrella company (such as SG Umbrella) is a company that acts as an employer to agency contractors who work under a fixed term contract assignment. When you operate through an umbrella company you effectively become an employee of that company, and they in effect 'contract out' your services to end clients, usually through a recruitment agency.

A timesheet will need to be submitted each month to the umbrella company who will then invoice the client or agency. The umbrella company will pay you minus deductions for PAYE and NIC and their fees.

WHAT IS A LIMITED COMPANY?

A limited company (or personal service company, as it is sometimes referred to) is the most popular and tax efficient way to operate as a contractor.

In the process of setting up a limited company, you become the director. This means you are legally responsible for the running of the company. There are certain responsibilities that come with this. These are covered in further detail later in the guide.

The limited company is legally a separate entity to yourself. So, any contract is created between the limited company and the client. Not between you and the client.

Limited Company	Umbrella Company
Suitable For	
<ul style="list-style-type: none"> • Contractors who intend on making contracting a long-term career choice • Contractors who earn more than £25,000 p.a. • Contractors who work outside of IR35 • Contractors who want more control over their finances • Contractors who want to be their own boss and build their own business • Contractors who want to work in the most tax efficient manner 	<ul style="list-style-type: none"> • First time contractors who want the security that employment offers • Contractors earning less than £25,000 p/a • People who intend to contract for a short period • Contractors who don't want to take care of the admin that comes with running a limited company • Contractors working inside IR35
Advantages	
<ul style="list-style-type: none"> • In most cases it is the most tax efficient way to operate • Presents a professional image • You have complete control over the business • Higher take home pay • Can claim for a greater number of expenses • Choose how you want to get paid – usually a mixture of a small salary & dividends • Can join the VAT Flat Rate Scheme 	<ul style="list-style-type: none"> • Contractor receives full employment rights and benefits: sick pay, holiday pay, paternity / maternity pay • Tax and national insurance obligations are handled by the umbrella company • No paperwork – contractor only needs to submit a timesheet

SETTING UP A LIMITED COMPANY

If you are thinking of contracting for the long term, setting up your own limited company is one of the best ways to operate. The thought of forming your company may seem scary and complicated so we've laid out the steps that explain what is involved in setting up a limited company.

1. CHOOSE A BUSINESS NAME

Every limited company needs to have a unique name. Ideally, the business name should reflect what your business does.

As you may use your business name for marketing purposes, it is advisable to choose a name that is easy to remember and spell. Before you incorporate the business, it is also worthwhile checking that the name is available as a web domain, in case you decide to create a website for your business. Once your business is incorporated you must include Limited or LTD at the end.

2. APPOINT A DIRECTOR & SHAREHOLDER

A limited company must have at least one director, probably yourself.

The director is responsible for running the company in accordance with all relevant legal requirements, and for completing all the necessary paperwork for HMRC.

Ownership of the company is issued through shares. As the director of the company you will likely be the main shareholder as well. Unless you decide to share ownership with someone else such as a spouse.

3. REGISTERING THE COMPANY

Once you have decided on a business name, you can incorporate the company by registering it with Companies House. This can be done through the post or online. Once the incorporation is complete you'll receive a Certificate of Incorporation, this typically takes 24 hours.

A third party can also incorporate the company on your behalf. We offer this service for free as part of our monthly accounting packages. Please refer to our website for further information.

4. INFORMING HMRC

You must inform HMRC that you have incorporated a limited company. This must be done within three months of starting any business activity (for example advertising the business).

HMRC will ask for the:

- Company's name
- Company's registered number
- Company's start date
- Details on the type of business you will be conducting
- Address you do business from

HMRC also need to know the date up to which you are preparing your first set of accounts.

After informing HMRC, they will forward you by a post a Unique Tax Reference number (UTR). It's important to keep this safe. You will need it to set up an online account to pay Corporation Tax and for completing an online tax return.

5. OPENING A BUSINESS ACCOUNT

It's important to understand that the finances of the limited company are separate to your personal finances. As the director of a limited company you are legally obliged to open a separate business bank account for the company.

There are lots of options available to choose from. However, it is worthwhile taking your time to research which account can offer you the best value.

Some things to consider, include:

- Is online banking available?
- Can you see an account manager (if needed)?
- What transaction fees are applicable?
- What interest fees are charged?

6. FIND A GREAT ACCOUNTANT

We have spoken to thousands of contractors in our over 20 years in business. It's been a regular occurrence for us to take on clients from other accountants - our clients are often surprised at how little tax planning was done previously.



Not only can an experienced contractor accountant help you to operate in the most tax efficient manner, they can save you time and also reduce the stress of running your own business. We are proud to say that most of our new clients come from recommendations. Once you join the SG Accounting Family, one of our partners will come to meet you to discuss it all in further detail.

A woman with blonde hair, wearing a dark blazer, is looking upwards and to the right with a thoughtful expression, her hand resting on her chin. To her left, a large black thought bubble contains a calculator icon. The background is a textured, light-colored wall.

Explaining expenses

What is a business expense?

An expense is defined as something which is made ‘wholly and exclusively for the purposes of your business’, as these can be offset against income and so will help to reduce your tax bill.

As a contractor, working through a limited company (outside of IR35) you may be able to claim for things such as those in the list below.

- Computer equipment
- Company bank charges and interest
- Clothing (branded uniform or protective work clothing. Jeans and T-shirts aren't allowed we're afraid!)
- Pension contributions
- Accountancy fees
- Business travel and hotels
- Branded stationery (letterheads, business cards etc) and postage
- Phone and internet costs
- Business entertainment
- Equipment for business use
- Motoring expenses
- Software
- Technical books and journals
- Some professional subscriptions
- Use of a portion of your home as an office

Expenses

WHAT'S NOT ALLOWED

If it is not intended for the sole and exclusive use of the business, the rule of thumb is that it is not an allowable business expense.

Examples of what is NOT allowed might be: gym membership, medical expenses, parking fines (make sure you put enough money in the meter!) and speeding tickets. If expenses such as this are put through the company, you can end up paying even more in tax than you saved as a “benefit in kind”.

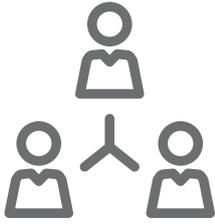
HOW TO CLAIM FOR BUSINESS EXPENSES

If you paid for it from your business account, you'll need to keep a record of the purchase as proof. This can be in form of a receipt.

If you made the purchase using your personal account, you will need to transfer the amount from your business account to your personal account, typically on a monthly basis.

You need to keep all of your receipts for at least six years so that you can prove the purchase was made. This is to cover yourself in the unlikely event of a tax inspection.





YOUR RESPONSIBILITIES

Running a limited company means that there are certain things you must do. Don't worry, these responsibilities aren't complex, but you need to be aware of what they are. Plus, a good accountant (like ourselves) will be able to help you with these.

ANNUAL ACCOUNTS

These need to be submitted on an annual basis to Companies House. This is typically done within nine months of the year end date.

CONFIRMATION STATEMENT

Submitted to Companies House on an annual basis. It provides them with up to date information on your limited company. Such as details on directors and shareholders and the company address. Companies House charges a fee of £13 for this.

REAL TIME INFORMATION

Information must be sent to HMRC about an employee's salary and associated deductions before, or at the same time as the payment is made.

CORPORATION TAX RETURNS

This needs to be submitted to HMRC with a set of year end accounts. It is easiest to submit this at the same time as sending documentation to Companies House.

VAT RETURNS

This can be done online with HMRC or through an appointed third party. We can help you with this. Payment can be made via BACS or via direct debit.

PAYING PAYE AND NIC

If payroll is run on a monthly basis, you need to inform HMRC via RTI of any PAYE and NIC payments due. Payment should be made by bank transfer. Most Directors would receive a salary from their company as well as dividends.

ONLINE SELF ASSESSMENT AND PAYMENT OF TAX LAIBILITIES

Self-assessment tax returns need to be submitted and any tax liability paid in full by midnight on 31st January, following the tax year-end. There are fines and penalties for late submission and payment. Plus, interest will be applied to any outstanding amount. This can soon add-up so it's important to get it done on time.

This can be done via HMRC online services (if you have registered). It is also possible for a third party to do this for you. We offer this service as part of our monthly accounting packages.

VAT or Not?

One of the most frequent questions we get asked, is “Do I need to be VAT registered?”

The answer is quite simple. A business must register for VAT if at the end of any month its taxable turnover for any consecutive 12-month period is more than the VAT threshold (£85,000 from 1st April 2017).

If your turnover is below the threshold but you expect to receive a large income payment in the next 30 days which will take you over the threshold, you must register straight away.

Even if you don't expect to exceed the VAT threshold, you can voluntarily register for VAT. Some of the reasons for this are:

- In some industries and professions, it is expected that businesses are VAT registered
- It looks more professional to be VAT registered
- If you make a lot of purchases for the business, it may be beneficial to be VAT registered as you may be able to claim the VAT back (only if they are eligible)



If you decide to become VAT registered, you may find it beneficial to use the Flat Rate Scheme (FRS). This scheme is available to small businesses whose VAT turnover is £150,000 or less (excluding VAT).

This scheme allows you to charge VAT at 20% to the company you are contracting for, then pay it back to HMRC at a lower rate (depending on which trade sector your business falls into).

By becoming VAT registered you can also benefit from cash accounting. Cash accounting means you only pay VAT to HMRC once you have received it from your customer. This can be very helpful for company cash-flow. With accruals accounting, you must pay HMRC based on when the invoice has been raised.

WHAT IS IT ALL ABOUT?

IR35: In or Out.

Ask any contractor, the one word that fills them with fear, and the majority will reply 'IR35'.

IR35 is a piece of legislation that was introduced in April 2000. Its sole purpose is to guard against what HMRC refer to as 'disguised employment'. A simple example of this would be where an employee would leave their job on a Friday and return the following Monday as a contractor. They would essentially be doing the same job but would benefit from the 'perks' of working via their own limited company.

DETERMINING IR35 STATUS

Unfortunately, it is not as simple as saying "I work through a limited company and I am a contractor". Therefore, I must be outside IR35. HMRC is cracking down heavily on disguised employment, particularly in the public sector.

New rules were passed in April 2017, which saw the responsibility of determining the IR35 status of a contract move away from the contractor to any third party who is closest to the limited company contractor' - so in effect, the organisation that pays you.

EFFECT ON INCOME

If your contract is deemed to be inside IR35, then effectively you are classed an employee of the company and must pay the full amount of tax and National Insurance contributions from your income. Thus, reducing the benefit of working via a limited company.

You also have a reduced allowance for expenses, meaning that you can only claim tax relief for certain things. The rules surrounding the IR35 legislation are incredibly complex. Most genuine contractor contracts are ok but we'd still recommend that you speak to an expert, like ourselves, before signing any contract to get clarification if the contract will place you inside or outside IR35.

SETTING IT STRAIGHT

True or false?

There are some people who may warn you against becoming a contractor, believing that it's a risky business move. To help you to decide if contracting is the right option for you we thought we'd dispel four common myths about contracting.

CONTRACTOR INCOME IS LOWER THAN PERMANENT INCOME?

False: The average contractor can expect to earn between £300-£500 a day. Contractors in niche sectors and major cities, like London, can earn much more. Yes, there may be periods where you aren't working (between contracts, for instance) but you can reduce risk by taking a proactive approach to finding contracts and building up cash in the company.

ONCE YOU BECOME A CONTRACTOR YOU CAN'T GO BACK TO 'PERM'?

False: There is no stigma attached to contracting. If you do decide that contracting isn't for you and want to return to permanent employment, the likelihood of an employer turning you down for a role because you were a contractor is unheard of. Additionally, being able to show that you are adaptable and can take ownership of projects is a plus for any employer. In fact, we find that most contractors never want to return to permanent work again out of choice!

CONTRACTING WILL TAKE OVER MY LIFE?

False: Being a contractor gives you the freedom to work for who you want and when you want. Some contractors work hard on a project and then decide to take an extended period of leave once the contract ends. They may spend this time travelling or choose to spend this time with their family.

Employees don't have this luxury. They are generally given a fixed number of leave days each year which they can't go over.

MY SKILLS WILL BECOME OUTDATED?

False: A common myth about contracting is that your skills can become redundant after a year or so. Contractors in some sectors may have this problem, but this can also happen to permanent employees as well.

As long as you keep your skills updated, you won't have this problem.



CV TIPS FOR CONTRACTORS

You're hired!



As a contractor, your chances of getting hired largely depends on the quality of your CV. On average, a recruiter or employer only spends around 20 seconds looking at your CV. So, your CV must be able to pack a punch straightaway. If you haven't looked at your CV for a while, or if you don't have one, these tips can help you to stand out from the crowd.

TAILOR YOUR CV

It is essential to adapt your CV to suit the role that you are applying for. It is not uncommon for contractors to have three or four versions of their CV that they use for differing roles. A recruiter or hiring manager will easily be able to tell if it is a generalised CV. If it is, it will likely end up in the bin.

MAKE IT PERSONABLE

As we mentioned earlier, someone typically looks at your CV for 20 seconds or less so the first impression counts. If your CV contains spelling or grammar mistakes, it may swiftly end up in the 'No' pile.

If you are struggling to put your CV together, it may be worthwhile getting it professionally written. If you prefer to do it yourself, make sure you get one or two people to look over it for mistakes.

LENGTH MATTERS

The standard length of a CV is two pages (A4 size). However, as a contractor, you may have a wider range of work experience. In that case, it is acceptable to increase the length of your CV to 4 pages. However, be careful not to exceed this as the reader may deem it to be too long and may discard it.

MAKE IT EASY TO READ

A recruiter or hiring manager doesn't have the time to read reams of information. To make your CV easy to skim read, break it up using sub-headers and bullet points.

It can be tempting to make your CV more interesting by presenting it differently, such as an interactive presentation or as a web file. However, most people, especially recruiters still prefer to receive a CV as a word document or pdf file.

CV layout

FIRST PAGE:

Personal details: name, contact number, email address and postal address.

Profile: a short summary (three - four lines is adequate) detailing who you are, what you do, what you are looking for and your core skills.

Expertise: using bullet points list your areas of expertise that matches the requirements of the contract. Try to expand on these areas by relating it back to numbers. Such as, how much money you saved the company over a specific timeframe.

Skills: list your skills (or key technological skills) and explain how these can be an asset to the company.

SECOND PAGE:

Work experience: list the name of your employer, date or time-frame you worked for them and a short-detailed description of the project you worked on.

Additional information: such as details on languages spoken or type of driving licence held.

References: state that these will be available at the interview.

A contractor CV differs to a standard CV as the employer is more interested in your skills and expertise and how these can benefit the company, rather than your previous work experience. By following the layout described above, your chances of being offered your ideal contract are increased.

Glossary of terms

Annual Financial Accounts

Annual Financial Accounts often referred to as Company Accounts or Annual Accounts. They include an income statement, a balance sheet and a directors' report. Annual Financial Accounts need to be submitted to HM Revenue & Customs (HMRC) and Companies House.

Companies House

This is the UK Registrar of Companies where you must incorporate your limited company. Each registered company is required to file Annual Financial Accounts and Confirmation statements with Companies House.

Confirmation statements

Confirmation statements must be filed annually with Companies House. It gives details of directors, secretaries, the registered office, share capital and shareholding.

Corporation Tax

Corporation Tax is a tax levied on company profits. Corporation Tax is calculated as a percentage of your profit at the end of the company year.

Dividends

Dividends are payments made by a company to its shareholders from company profits.

Payroll Year End Returns (FPS)

Each tax year (6 April - 5 April) requires a final payroll return to "close off" the year's PAYE (pay as you earn or salary tax) submissions to HMRC by all companies that pay staff salaries, by 19 April.

Expenses

Expenses arise during the discharge of company business; they are wholly and exclusively for the business and have been paid for personally. These expenses can be claimed back from the company. Expenses paid out by the company reduce the company profit and corporation tax liability.

Flat Rate Scheme (FRS)

A scheme that was designed to simplify VAT compliance for small businesses. Businesses can charge VAT at the standard (20%) rate and pay it back to HMRC at a lower rate based on their trade sector.

HM Revenue & Customs

Her Majesty's Revenue and Customs (HMRC), also referred to as "HM Revenue & Customs", is the government body responsible for the collection of taxes.

IR35

IR35 is a piece of legislation that allows HMRC to collect additional payment where a contractor is an employee in all but name.

Limited company

A separate legal entity incorporated with Companies House.

National Insurance

National Insurance (NI) contributions are made based on earnings or profit.

PAYE

Pay as You Earn (PAYE) is a tax on income deducted at source by employers on behalf of HMRC.

Real Time Information payroll returns

Also known as RTI. These are monthly payroll returns that need to be submitted to HMRC declaring what salaries your company has paid yourself and/or your employees.

Turnover

Your business turnover means the total sum invoiced by your company (excluding VAT).

VAT

Value Added Tax (VAT) is an end-user tax added to products or services. Output VAT is added to invoices and collected on behalf of the government. Input VAT is what is paid to suppliers. The difference in output VAT less input VAT is required to be paid quarterly to HMRC.



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