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# Orange Genie

Accountancy  
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Guide to the UK Tax System for Small Limited Companies



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Running your own Limited company means you need to be aware of two tax regimes in the UK – Corporate tax that applies to your Limited Company and the Personal tax system as it applies to you.

This guide aims to de-mystify what many regard as a complex system and explain the bits you really need to understand.

## COMPANY TAXATION

As director of your company you are ultimately responsible for making sure you and your company file the correct returns, which is why you need some knowledge, but don't worry, your accountant is expert in all of these areas and will be there to remind, prompt and advise you.

As a director of a limited company, you are liable to ensure your limited company pays its Corporation Tax annually. Also, as a director you may need to consider VAT and PAYE.

### Corporation Tax

Corporation Tax is applicable to all limited companies, irrespective of profit levels. It's payable on your company's taxable profits.

At the most simple, taxable profits are calculated as the difference between your company's turnover and your tax deductible expenses, including any salary you pay yourself. Dividends are not tax deductible and are paid out of post-tax profits. The current rate of Corporation Tax is 19% in 2021/22.



### Your company's responsibilities are:

- File a set of accounts and Corporate Tax Return (CT600) annually by electronic means.
- Pay the right amount of Corporation Tax on time - within nine months of the company's year end.

If you are late filing or paying your Corporation Tax Return, i.e. you don't submit these within 12 months of your year end, or pay your corporation tax within nine months and day of your year end, you could find yourself facing fines of up to 100% of the tax owed, and £100 penalty.

As long as you keep your accounting records up to date, your accountant will be able to regularly advise you of how much corporation tax you may need to pay. Your accountant can also advise you of your potential liability throughout the year and will make sure that your accounts and returns are prepared in good time for your approval and submission.

An additional Corporation Tax charge may apply if you have an outstanding Directors Loan with your company. This is covered in our separate Guide to Director's Loans.

### VAT

VAT registration is compulsory, if certain turnover thresholds are met - £85,000 for 2023/23. Many contractors choose to register voluntarily, even if turnover is lower than the threshold.

This could be for a number of reasons such as:

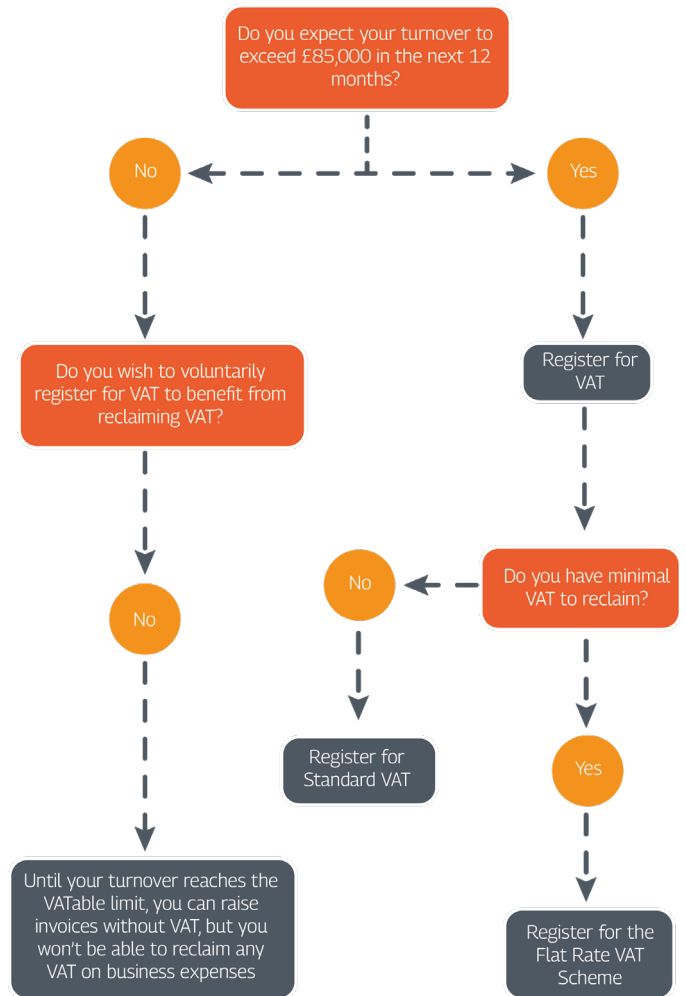
- Being VAT registered provides the company with a perception of being larger than perhaps it is.
- The end client may ask to only work with a VAT registered business
- Registration allows you to take advantage of the Flat Rate VAT scheme.



Once VAT registered you are required to charge VAT at 20% on all invoices produced by your Company. VAT is chargeable not only on the cost of your services but also on any expenses recharged to your client. For example if you invoice your client for a license for a piece of software, you would need to charge them for the license plus 20% VAT.

Charging VAT does not usually increase the cost to your agency/client as most businesses are VAT registered and can reclaim the VAT on your invoices.

VAT is due quarterly and traditionally on the value of the invoice raised, paid or not. In order to avoid the need to pay over VAT to HMRC before your invoice has been paid you can opt to use the cash accounting scheme and account for VAT on a receipts and payments basis. Don't worry, your accountant will advise you on payment systems and how much VAT you are due to pay and when.



### Flat Rate VAT

The Flat Rate Vat Scheme (FRS) is an alternative to standard VAT registration, open to businesses with an expected turnover of less than £150,000 (£180,000 including VAT).

Under the scheme, you charge VAT to your clients at the standard rate of 20% and you pay HMRC a lower percentage of your VAT inclusive turnover. Unlike standard registration, you do not offset VAT paid by your business. The percentage used depends on your business activity and the corresponding FRS category.

### Limited cost traders

In April 2017, the government introduced a new flat rate category of 16.5% for businesses who fall into the definition of a "limited cost trader". The government made this change because they believe that the Flat Rate VAT scheme has been abused in certain sectors



where a limited company is used solely for the purpose of accessing the Flat Rate VAT benefit for a worker who is caught by IR35. However, genuine contractors across all market sectors were impacted by the changes.

### Who is classed as a limited cost trader?

This Flat Rate percentage applies to "limited cost traders" HMRC guidance defines a business as a "limited cost trader" (LCT) if their VAT inclusive expenditure on relevant goods is either:-

- Less than 2% of their VAT inclusive turnover in a prescribed accounting period
- Greater than 2% of their VAT inclusive turnover but less than £1,000 per annum if the prescribed period is one year (if not the £1,000 is pro-rated)
- The meaning of relevant goods in this context is not defined in the legislation and therefore takes its everyday meaning and generally covers tangible items.

The legislation specifically excludes the following from the definition of "relevant goods":

- Capital expenditure on equipment
- Food and drink
- Vehicles, vehicle parts and fuel

For example:

John is an IT Consultant. In 2016 he registered for Flat Rate VAT and in his second year of trading he applied the rate of 14.5%

In his accounting period to 30 September 2016, John had VAT inclusive turnover of £140,000 and VAT inclusive expenses of:

Materials £600

Accountancy Fees £1200

Phone £350

Accommodation and subsistence £5,000

John made a surplus on the Flat Rate VAT scheme of £3,000

John now is classed as a "limited cost trader". His expenditure on "goods" is £600 including VAT and as this is less than 2% of the £140,000 VAT inclusive turnover he falls into the definition. His other costs are deemed to be services. Under the new rules, assuming John's business performs exactly as it did in 2016, he will make a surplus of £233

This is a reduction in profit for the year of £2,767



## De-registering for VAT

If you have voluntarily registered or are below the compulsory registration limit you can de-register from VAT at any time. You will need to confirm your exact date of de-registration and complete one final return. Once you have de-registered you will no longer charge VAT on your invoices but equally, if on the standard scheme, you can no longer reclaim VAT on your expenses.

## PAYE and P11Ds

If you wish to pay yourself or any other employee a salary, your company will need to register for PAYE. A payroll will need to be run for all employees and PAYE and NIC calculated. Each pay period will need to be reported to HMRC, via a Real Time Information (RTI) submission and the tax and national insurance deducted will need to be paid over by the appropriate due date.

At the end of the tax year, each employee will need to be issued with a P60, summarising their earnings and tax position for the year. In addition, if any benefits in kind have been paid to the employee a P11d will also be needed by 6th July.

## P11Ds

A P11D is the form used to report expenses and benefits paid to directors who own more than a 5% shareholding in the company and employees earning over £8,500 a year which have not been subject to PAYE tax.

These are likely to be items and services you may have received from your company in addition to your salary. For example an interest free company loan for a season ticket for travel or a company car. As they will increase your salary, they may attract National Insurance, however your company would pay this not you.

Your P11D will need to be filed by the 6th July following the year in question. For example, for the tax year 6th April 2022 to 5th April 2023 you would need to submit your P11D by 6th July 2023. If there is any Class 1A National Insurance owed, this must be paid by 19th July 2023 (in the case of tax year 2022/23).

If there are no benefits or additional tax to report then a return still needs to be filed with HMRC. We can do this for

you.

If you do file late or incorrectly, you will have about a fortnight to put things right, but if by the 22nd July you are yet to submit your P11D and pay any Class 1A National Insurance owed, your company will start to incur a penalty of £100 per month (or part month) per 50 employees. If you have submitted a P11D and you have filed it incorrectly you could also face a fine, though this is at the discretion of HMRC. If HMRC do think you took reasonable care and it's a genuine mistake, you're unlikely to face any fines. However, penalties of up to 100% of the tax owed can be applied if HMRC feel you have not taken reasonable care and/or are not being honest with your declarations.





## Personal Tax

As a director of a limited company, you will need to file an annual Self-Assessment tax return. This return summarises all your income throughout the year, such as:

- Employment
- Your limited company
- Rental income
- Investment income

The tax due on your total income, after allowances, is then compared to the tax that has already been paid during the year and then either a balancing payment may be necessary, or you could even be due a refund.

### Self-Assessment

Tax returns are issued shortly after the end of the fiscal year, which runs from 6 April to the following 5 April, so 2022/23 runs from 6 April 2022 to 5 April 2023. If you are registered for Self-Assessment you will be sent a notice advising the return is due. If you have not been issued with a tax return but know you have tax due it is your responsibility to notify HMRC who may then issue a return.

A Self-Assessment return is due to be filed by 31 January following the end of the fiscal year. If a completed return is not sent on time, HMRC will automatically issue a penalty of £100 irrespective of whether any tax is due or not.

### Payment of Tax

The UK Income Tax system has a payment regime in which the tax payments are usually made in instalments. The instalments consist of two payments on account of equal amounts: The first on 31 January during the tax year and the second on 31 July following.

These payments are set by reference to your previous year's net income tax liability. A final balancing payment may be due on 31 January following the tax year. In calculating your level of instalments any tax attributable to Capital Gains is ignored. All capital gains tax is paid as part of the final payment due on 31 January following the end of the tax year. A statement of account similar to a credit card statement is sent to the taxpayer periodically which summarises the

payments required and payments made.

#### Example 1:

George began to trade on 5 May 2018. His first Self-Assessment return was due for the period to 5 April 2019.

No payments on account were due on 31 July 2018, 31 January 2019 or 31 July 2019 since there was no previous years liability to reference these to.

All the liability was due on 31 January 2020 along with the first payment on account for 2019/20 set by reference to the liability for 2018/19.



#### Example 2:

Emma's income tax liability for 2017/18, after amounts deducted at source, is £8,000. This is her first year of trading. Her liability for the following year, 2018/19 is £10,500.

Date	Details	Amount
31.01.2022	Tax payment for 2020/21	£8,000
31.01.2022	First installment (50% pf 2021/22 liability)	£4,000
31.07.2022	Second installment (50% of 2021/22 liability)	£4,000
31.01.2023	Final payment (2021/22 liability less amounts already paid)	£2,500
31.01.2023	First installment (50% pf 2022/23 liability)	£5,250

## Interest and surcharges

Interest will be charged on any tax paid late. There will also be interest added by HMRC when tax overpaid is refunded. In addition there will be a 5% surcharge on any tax still outstanding on 28 February following the year of assessment, increasing to 10% if still unpaid at 31 July.

## Nil payments on account

Where there is only a small amount of income tax due, after tax deducted at source has been accounted for the two payments on account will be set at nil. This applies if income tax due for the preceding year, net of tax deducted at source is less than £1,000 in total or if more than 80% of your income tax liability for the preceding year was deducted at source.

## Claim to reduce payments on account

If you believe your current year's tax liability will be lower than the previous year's a claim can be made to reduce the payment on account. You should talk to your accountant if you are considering this.

## Corrections and enquiries

HMRC may correct a self-assessment within nine months of the return being filed in order to correct any obvious errors or mistakes in the return. You may also amend your return within 12 months of the filing date.

HMRC may enquire into your return by giving you written notice. In most cases the time limit for this is 12 months following the filing date.

HMRC cannot query an entry on the return without opening an enquiry. The main purpose of the enquiry is to identify errors, not all enquiries will determine that a return is incorrect.

## Capital Gains Tax

Capital Gains tax is a tax on the increase in value of assets over the period of time in which you own them. Assets can include investments, antiques, second homes and the shares in your company. The tax is due when you dispose of them, when selling or giving them away. There is an annual personal allowance against Capital Gains Tax, currently £12,300 (2021/22). It's also worth noting you don't normally pay tax on gifts to your husband, wife, civil partner or charities, and you do not pay Capital Gains Tax on NISAs, ISAs or If

PEPs, Premium Bonds or when you win money on betting, lottery or pools.

The rate of taxation you pay is based on your total personal income. If you are a basic rate taxpayer you will pay 18% on gains above the exempt amount and for higher rate tax payers it's 28%.

If the value of the gain is below £25,000 then HMRC do not need to approve it, and it can be simply reported on a self-assessment and Capital Gains tax rules applied. If the gain is in excess of £25,000 a liquidator will need to handle the closure before reporting the gain on a self-assessment.

You may also qualify for Entrepreneurs' Relief when disposing of your limited company. You can claim this relief if you control at least 5% of a company whose shares or assets you are selling, but you'll need to have owned the business for at least one year.



**Common examples of Capital Gains Tax applying are:**

- **On personal assets and possessions** - if you make again when you sell a personal possession for £6,000 or more e.g. jewelry or an antique, you may need to pay Capital Gains tax. There are special rules for items with a predicted life of 50 years or less, known as 'wasting assets.' These are free from capital gains tax so you may not be taxed on the sale of such items as vintage cars, pleasure boats, caravans and even some antiques.
- **On property** - whilst Capital Gains Tax is normally not payable on gains you make on the sale of your only or main home, because these qualify for private residence relief (PRR) there are taxable gains if you develop your home, for example by converting your garage into flats or if you sell a second property that is not your main residence.

If you have ever been a landlord and let part or all of your entire house, upon sale, the gain which relates to letting could be taxable. However, provided the house has been your main home at some time you can claim relief for the time it was your main residence.

- **When closing a company** - on a company closure the assets pass to the shareholder which means the assets have now been passed to you, so you will need to consider the Capital Gains Tax position. If the value of the gain is below £25,000 then HMRC do not need to approve it, and it can be simply reported on a self-assessment and Capital Gains tax rules applied. If the gain is in excess of £25,000 a liquidator will need to handle the closure before reporting the gain on a self-assessment.

You may also qualify for Entrepreneurs' Relief when disposing of your limited company. You can claim this relief if you control at least 5% of a company whose shares or assets you are selling, but you'll need to have owned the business for at least one year. This will reduce your Capital Gains Tax rate to 10%. We'd recommend you speak to a specialist liquidator, who will be able to help you close your company in the most tax efficient way possible.





## Inheritance Tax

Inheritance Tax is paid on an estate when somebody dies, if the value of the estate is over £325,000 (2022/23). The estate is valued by comparing the assets and liabilities of the individual. An estate can also include a share of jointly owned property and assets held in trust. If you pass your main home to your children or grandchildren, you will get an extended allowance against Inheritance tax. This will be £175,000 in 2022 to 2023

Tax is payable at 40% on the value of the estate over the allowable threshold. Inheritance tax can also be payable on lifetime transfers. If assets are gifted during the donor's life time and they are not deemed exempt, Inheritance tax will apply if the donor dies within 7 years of the transfer. The rate of tax paid reduces as the seven year time limit expires. Some lifetime gifts can be given exempt of Inheritance Tax, for example: spouse or civil partner exemption.

- **Spouse or civil partner exemption.** Your estate usually doesn't owe Inheritance Tax on anything you leave to a spouse or civil partner who has their permanent home in the UK - nor on gifts you make to them in your lifetime - even if the amount is over the threshold.
- **Charity exemption.** Any gifts you make to a 'qualifying' charity - during your lifetime or in your will - will be exempt from Inheritance Tax. A donation to charity in your will may also reduce the rate that tax is paid at.
- **Annual exemption.** You can give up to £3,000 away each year, either as a single gift or as several gifts adding up to that amount - you can also use your unused allowance from the previous year but you use the current year's allowance first.
- **Small gift exemption.** You can make small gifts of up to £250 to as many individuals as you like tax-free.
- **Wedding and civil partnership gifts.** Gifts to someone getting married or registering a civil partnership are exempt up to a certain amount.
- **Business, Woodland, Heritage and Farm Relief.** If the deceased owned a business, farm, woodland or National Heritage property, some relief from Inheritance Tax may be available. In most cases, you must pay Inheritance Tax within six months of the end of the month in which the deceased died. After this, interest



will be charged on the amount outstanding. You can pay in yearly instalments over 10 years if the value of the estate is tied up in property such as a house.

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