

Setting up a limited company for contracting

You're ready to start working for yourself as a contractor, and you've chosen the most tax-efficient format for it which is the limited company. What do you do next?

Understanding Limited Companies

The limited company is an organisation that is called a 'moral person' in law: this means that it has its own identity, and does business under its own name. It makes or loses money, can acquire debt, and pay taxes all by itself, just like a physical person.

It has its own bank account: "do not think that you can be paid to your company in your own name; revenues earned by the company must be paid to the company account," explains Rebecca Dawes of company formation specialist [Duport](#).

Understanding this is important because it explains why the legal formation of a limited company works the way it does. Just as a baby is registered in the birth rolls when it is born, a company is registered in the official list of companies when you start it. This list is kept by [Companies House](#).

What you need to get started setting up a limited company

Pick a [name for your company](#), decide where it is based, and decide who's going to be part of it. Pick a general name that isn't directly related to what you do just in case you plan on changing/expanding in the future. For example CarphoneWarehouse no longer sells car phones!

We'll use the hypothetical example of "World's Greatest Contractors Ltd." which is being set up by the imaginary contractors John and Joan Dunn. John and Joan both work at the company, and so they issue £100 worth of ordinary shares which they divide between them with each owning 50%.

In this division of ordinary shares, [dividends](#) paid out will have to be proportional to the shareholding division—but only for ordinary shares. In other words, in the example, each gets 50% of dividend income, but this would not be the case if a preferential share division is used. "[Income shifting](#)" legislation is also still under consideration in Parliament, and this could make [dividing up dividend income](#) dependent on services provided to the company, but watch this space for news of these developments.

Issuing Shares

But they could, if they so chose, include any other shareholders in the company that they might choose to, so long as the total amount of shares are divided proportionately to the capital. It's often helpful to sell one share to another person so that, in case John and Joan disagree about something, someone can be the tie-breaker. (Remember that when you sell shares to anyone, you must pay Stamp Duty at the local [HMRC](#) office on the sale.)

John and Joan also are not obliged to issue ordinary shares: there are many different types of shares, for example preference shares, which are linked to specific rules related to the company's operations. If you seek a structure of this kind, you should probably take advice from a professional as it has tax implications.

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Go Online At Companies House

Once you've made all the decisions above, you can then go online at Companies House and, for a fee of £20, set up your company. The online forms will guide you through the setup process. Companies House will check to see if the name you've chosen is not in use, and it will ask you to appoint a company director and a company secretary. In this case Joan takes the directorship, and John becomes the secretary, although one person could if necessary take on both roles. Being a director has certain [legal responsibilities](#) which you should be aware of.

Memorandum of Association

You will also need to file a Memorandum of Association with Companies House. This is a document that tells everyone why you've set up the company, and how you plan to run it. This document can have significant legal importance in tax disputes and any legal proceedings—for example, courts will look closely at this in an [IR35](#) case.

You can write this document yourself, but in that case, keep it simple!! State clearly what your company is for and how you wish to run it. But because this document can be quite important, you may wish to take professional advice before filing it. You can find many different models for a Memorandum online, for example at [Clickdocs](#).

Help from a Specialist

All of this is straightforward and simple, as it should be in our very liberal economy, but the devil gets into the details if problems arise while you are running the company. For tax purposes, and for your own protection, you may consider working with a company formation specialist. The cost is usually around £100

–it can be less—and you have the advantage of talking over what you want to do with someone before you do it. "A specialist will be able to suggest different structures which can affect tax, or add important conditions to your Memorandum of Association," Dawes adds.

Help 'from an Accountant

If you **choose an accountant** to set up your company, you get a bit more at the slightly higher cost of £250-£500 . The accountant will probably provide you with a formation package which usually consists of: setting up the limited company, **VAT** registration, bank account referral, corporate tax registration.

The accountant will then go on to handle your payroll and taxes. This is the route of least resistance, and of course an accountant can provide very useful advice for a growing company.

The company bank account

Getting a **business bank account** can be more difficult than you might think. The High Street banks can be suspicious of new companies, and they will worry you about your credit rating. If at all possible, try and work with a bank where you already have an account and are known. A referral from an accountant or a company formation specialist can spare you some pain in this regard.

Registering for VAT

This is the last but by no means the least step in starting your company. You can register online at the HMRC website and in general, handling VAT online is much easier than going the paper route. You may experience a delay in receiving your VAT registration, but don't worry as you can backbill your clients for it (just tell them you intend to do this). Some accountants will handle your VAT for you, but you can make the calculations yourself easily with the help of the online forms.

Start-Up Expenses

Any **start up expenses** when setting the company up can be claimed against future revenues your limited company generates.

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