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The Start-up Brief

Tax Issues

This FAQ sheet forms part of a series prepared by postgraduate students from the University of Manchester's School of Law, in conjunction with the Legal Advice Centre. They are intended as an introductory guide to commonly asked questions by those approaching the Manchester Enterprise Centre when seeking advice on starting up new businesses.

These guides provide only a basic overview on key issues to be considered and do not constitute legal advice. Further detailed advice should be sought as necessary from appropriate professionals such as a solicitor or accountant.

This FAQ sheet tells you the key tax issues that you need to think about when starting up a business. So this includes the taxes a business needs to pay and how this relates to different business structures; how taxes are paid; VAT; tax and National Insurance when you are employing people; and international trading tax issues. If you are set-up, or will set-up, as a sole trader then this FAQ sheet doesn't apply to you. In this case, more information can be found at **https://www.gov.uk/set-up-sole-trader.**

This FAQ sheet specifically sets out to answer the following questions:

1. What are the principal taxes a business needs to consider?
2. How does the choice of business structure determine which taxes you need to pay?
3. What is VAT and who has to pay it?
4. As an employer what taxes do you need to pay on behalf of your employees?

Q1: What are the principal taxes a business needs to consider?

Capital Gains Tax

Capital Gains Tax is a tax on profits made when you are selling assets that have increased in value. You may have to pay Capital Gains Tax if you make a profit when you sell all or part of a business asset, including land and buildings, fixtures and fittings, plant and machinery, shares, registered trademarks and your business's reputation.

You pay Capital Gains Tax if you are a self-employed sole trader or in a business partnership. Once know Capital Gains Tax is payable, you have different ways to pay.

– straight away in the Report Capital Gains Tax online service. Under this choice, you do not need to wait for the end of the tax year and you can use this service as soon as you have calculated your gains and the tax you owe.

– annually in a Self-Assessment tax return.

Different methods have different time requirements, so make sure you pay HMRC by the deadline. Otherwise, you will be charged interest and may have to pay a penalty if your payment is late.

Corporation Tax

You must pay Corporation Tax on profits from doing business as a limited company or any foreign company with a UK branch or office.

If you need to pay Corporation Tax, the deadline for your payment will depend on the level of your taxable profits

Q2: How does the choice of business structure determine which taxes you need to pay?

Private and public limited company

You must pay Corporation Tax on profits from doing business as:

– a limited company

– any foreign company with a UK branch or office

– a club, co-operative or other unincorporated association, eg a community group or sports club.

You do not get a bill for Corporation Tax. There are specific things you must do to work out, pay and report your tax.

After you have registered your company with Companies House, you will need to register it with the tax authority Her Majesty's Revenue & Customs (HMRC) for Corporation Tax.

You must do this within 3 months of starting to do business and you can be charged a penalty if you register late.

You will need your company's 10-digit Unique Taxpayer Reference (UTR) before you register for Corporation Tax and this is sent to you after your company is registered. You have to file a Company Tax Return even if you make a loss or have no Corporation Tax to pay.

Partnership

Partnerships are not taxed on their profits. Instead, individual partners are liable to pay income tax on their share of the partnership profits, and to capital gains tax on their gains in respect of partnership assets. Corporate partners have to pay corporation tax on their share of profits and chargeable gains.

Once the partnership profit has been established, the partnership allocates a share of the profit or loss (calculated on the basis appropriate to the partner) to each partner in accordance with the partnership profit sharing agreement. This is the partner's share of the partnership profit.

A nominated partner is required to make a return on behalf of the partnership. This includes a statement that names all the partners, the taxable partnership profits or losses and the amount of profit or loss allocated to each partner.

A partner is normally required to include their share of the profits or losses in their personal or company tax return and pay tax on their share of profit.

Q3: What is VAT and who has to pay it?

What is VAT?

It is a general, broadly based consumption tax assessed on the value added to goods and services. It applies more or less to all goods and services that are bought and sold for use or consumption in the European Union

When to register

You must register for VAT when you go over the threshold, or know that you will. The threshold is based on your VAT taxable turnover. That is the total of everything sold that is not VAT exempt.

You must register for VAT if your VAT taxable turnover is more than a certain level (£85,000 for 2017-18) in a 12 month period or if you expect to go over the threshold in a single 30 day period. There are also other circumstances in which you will have to register.

You may have to register for VAT if you take over a business that is already registered.

There is no threshold if neither you nor your business is based in the UK, but you must register as soon as you supply any goods and services to the UK (or if you expect to in the next 30 days).

Late registration

You must register within 30 days of your business turnover exceeding the threshold. If you register late, you must pay what you owe from when you should have registered and you may get a penalty depending on how much you owe and how late your registration is.

Voluntary registration

You can register voluntarily if your business turnover is below a certain figure (£83,000 in 2017-18). You must pay any VAT you owe from the date you are registered.

You can apply to HMRC for a registration 'exception' if your taxable turnover goes over the threshold temporarily.

You may be able to reclaim VAT paid on goods or services bought before you registered for VAT if the purchases were made within certain time limits, but there is a time limit for backdating claims for VAT paid before registration.

Advantages of voluntary VAT registration

The threshold for VAT registration may seem high, but it is important to remember that this figure refers to 'taxable turnover', which is the overall income generated from all sales and not simply the profit made from those sales. For this reason, many small businesses and limited companies are legally required to register for VAT.

There are certain benefits of VAT registration, whether voluntary or because you have to register.

– VAT can be applied to the sale cost of almost all goods and services offered and VAT can be reclaimed on most goods or services purchased from other businesses.

– If you are sending goods to someone who is VAT registered in the destination EU country, you can zero-rate the supply for VAT purposes if certain circumstances.

– Small businesses can give the appearance of being bigger and more established, which can be appealing to clients, lenders, investors and suppliers, who will assume your turnover is high because you are VAT registered.

– A VAT number displayed on invoices, letterheads, websites and other forms of business stationery can be appealing to other firms, many of whom may be unwilling to get involved with a business that is not VAT registered and assumed to be small.

Disadvantages of voluntary VAT registration

VAT could deter the purchase of goods and services by customers who are not VAT registered, particularly if the final cost of the sale appears higher.

Your business could end up with a large VAT bill if you generate more VAT from goods and services sold than the VAT paid on goods and services bought from other businesses.

Extra paperwork and administration is an unavoidable consequence of VAT registration. Businesses have to keep all VAT invoices and receipts, maintain VAT accounting records, and file VAT returns every quarter.

Q4: As an employer what taxes do you need to pay on behalf of your employees?

PAYE (Pay As You Earn) is HMRC's system to collect Income Tax and National Insurance from employment.

If you are self-employed, which means you run your own business and are responsible for its success or failure, you are exempt from PAYE. But you still need to pay Class 2 or 4 National Insurance if you make profits of above certain levels in a year.

People who are employed by you and earn above a certain level will pay tax through PAYE. Otherwise, they are exempt from PAYE.

For those who qualify to pay Income Tax, you must, as the employer of these staff, make deductions from pay for tax and National Insurance from wages. You may also need to make deductions for things like student loan repayments or pension contributions.

These deductions are worked out using each employee's tax code and National Insurance category letter. You can use payroll software to work out how much tax and National Insurance you need to deduct from salaries during each pay period.

Q5: What are the tax issues if your business is based in the UK with main markets overseas?

If your company is based in the UK, it pays Corporation Tax on all its profits from the UK and abroad.

If your company is not based in the UK, but has an office or branch here, it only pays Corporation Tax on profits from its UK activities.

Taxable profits for Corporation Tax include the money your company or association makes from doing business ('trading profits'), investments and selling assets for more than they cost ('chargeable gains').

Q6: Do you have to pay tax on imported items at the border?

At the moment, the UK is in the EU Customs Union which means that there are no duties payable within the EU. This will however be likely to be affected by the Brexit discussions.

When goods cross into the UK and are re-exported within a certain time thereafter, outside of the EU, then duties are payable. The precise level of duty depends on the nature of the products.

You may have to pay VAT, Customs Duty or Excise Duty on items sent from outside the EU before you can collect them. However, you do not need to pay VAT or Customs Duty when your things are sent back to you – they must be described as 'personal belongings' on the customs declaration.

Please also refer to Start-up Brief: Issues to consider when operating across international borders.

Useful links:

- https://www.gov.uk/topic/business-tax/corporation-tax
- https://www.gov.uk/topic/business-tax/vat
- https://www.gov.uk/capital-gains-tax
- https://www.youtube.com/user/HMRCgovuk
  (a series of videos from the HMRC designed to help individuals and businesses get to grips with the basics of tax and taxation.