

C TODD & CO

CHARTERED CERTIFIED ACCOUNTANT

NEW BUSINESS KIT

A guide to starting your own business.

C. TODD & CO
CHARTERED CERTIFIED ACCOUNTANT

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because your business.....is our business

BEFORE STARTING UP

It is the ambition of many people to run their own business, but a number of dangers exist.

A major concern is the risk of business failure despite considerable effort and finance having been put into the venture. Time spent in making the decision and thinking through your plans now will minimise the risk of failure in the future.

Think carefully about ceasing to be someone else's employee.

Certainty of income, both in terms of quantity and regularity, disappears, whilst fixed outgoings, such as mortgage repayments, remain. Similarly, other benefits of employment may be lost, such as life assurance cover, a company pension, medical insurance, a company car, regular hours and holidays.

Success in business depends on many factors; most important is the need to critically review all aspects of the business proposition before progressing too far.

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SELECTING A LEGAL ENTITY FOR YOUR BUSINESS

One of the first decisions you will have to make is the form of legal entity it will take. This decision may be determined by the way you have organised your operations and whether you intend to work on your own or in conjunction with others.

The form of entity you choose will impact on the way you are protected under the law and are affected by taxation rules. There are three basic forms of business organisations and each is treated differently for legal and tax purposes.

Sole Proprietor Business

A sole proprietor business is typically a business owned and operated by one individual. A sole proprietor business is not considered to be a separate legal entity under the law, but is an extension of the individual who owns it. The owner has possession of the business assets and is directly responsible for the debts and other liabilities incurred by the business. The profit or loss is combined with the other income of the individual for income tax purposes.

This is the easiest form of business to own and operate as it does not require any specific legal organisation, except, the normal requirements such as licenses or permits. The business decisions are solely the result of the owner's abilities.

Partnership

In a partnership, two or more individuals join together to run the business enterprise. Each of the individual partners has ownership of company assets and responsibility for liabilities, as well as authority in running the business. The authority of the partners, and the way in which profits or losses are to be shared, can be modified by the partnership agreement. Partnership creditors typically have recourse to the personal assets of each of the partners for settlement of partnership debts.

The rights, responsibilities and obligations of partners are typically detailed in a partnership agreement.

A partnership is a legal entity recognised under the law and, as such, it has rights and responsibilities in and of itself. A partnership can sign contracts, obtain trade credit and borrow money. When a partnership is small, most creditors require a personal guarantee of the general partners for credit.

A partnership is also required to file an income tax return. A partnership typically does not pay income tax; the information from the tax return is combined with the personal income of the partners to determine their overall tax liability.

Limited Company

A limited company is a separate legal entity that exists under the authority granted by statute. A limited company has substantially all of the legal rights of an individual and is responsible for its own debts. It must file tax returns and pay taxes on income it derives from its operations. Typically, the owners or shareholders of a limited company are protected from the liabilities of the business. However, when a limited company is small, creditors often require personal guarantees of the principal owners before extending credit. The legal protection afforded the owners of a limited company can be useful.

A limited company must obtain approval from Companies House to use its proposed name. A limited company must also adopt and file a Memorandum and Articles of Association, which govern its rights and obligations to its shareholders, directors and officers.

A limited company must file annual tax returns (corporation tax returns) with H M Revenue and Customs.

Incorporating a business allows a number of other advantages such as the ease of bringing in additional capital through the sale of share capital, or allowing an individual to sell or transfer their interest in the business. It also provides for business continuity when the original owners choose to retire or sell their shares.

Tax laws have tended to favour the limited company route as a means of paying less tax, however the potential savings of a company do need consideration. It is necessary to consider factors such as the company car as savings from incorporation can soon be totally eliminated if a company car and fuel for private use are provided.

BUSINESS STRUCTURE - THE PROS AND CONS

There are also other factors beside the tax implications that should be borne in mind.

Company

- A company must be formally incorporated with a written constitution in the form of a Memorandum and Articles of Incorporation. There is, therefore, an initial setup cost.
- Companies are governed by the Companies Act.
- A company must keep accounting records, file accounts and an Annual Return with the Registrar of Companies. This information is available to the public, suppliers and customers to view.
- A company must keep Statutory Books.
- Companies may have greater borrowing potential. They can use current assets as security by creating a floating charge.
- Shares in a company are generally transferable, therefore ownership may change but the business continues.
- Incorporation does not guarantee reliability or respectability but gives the impression of a soundly based organisation. Personally, there may be prestige attached to directorship.
- Tax is payable on directors' remuneration paid via PAYE on the 19th of the following month after payment.
- Corporation tax is payable 9 months after the year end.
- Losses in a company can only be carried forward to set against future profits.
- For profits up to £300,000 tax is generally charged at 21%.
- There is both employers' and employees' national insurance payable on directors salaries and bonuses. The NI charge is greater than that paid by a sole trader/partner.

Sole Trader / Partnership

- There are no formation costs, but a written partnership agreement is advised.
- Sole traders and partnerships are not required by law to have annual accounts nor to file accounts for inspection. However, annual accounts are necessary for the H M Revenue and Customs tax returns.
- Sole traders and partners are unrestricted in the amount and purpose of borrowings but cannot create floating charges.
- The unincorporated business does not carry the same prestige as a limited company.
- For a sole trader or partnership, tax is generally paid by instalments on the 31 January in the tax year and the 31 July following the tax year.
- Losses generated by a sole trader or a partner can be set against other income of the year or carried back to prior years.
- Profits are taxed at 40% on taxable income in excess of around £41,000.
- A partner / sole trader will pay Class 2 NI of £2.30 per week and Class 4 NI of 8% dependent on the level of profits.

REGISTERING WITH THE TAX AUTHORITIES

A significant task for the new business owner is assuring that the business is properly complying with the extensive tax and information filing requirements imposed by the various authorities. Problems and penalties could arise if the new business is not registered with the appropriate tax authorities in a timely fashion.

This section summarises some of the more prominent filing requirements common to most businesses.

H M Revenue and Customs

It is necessary to notify H M Revenue and Customs of your existence by completing forms CT41G (companies) and CWF1 (sole traders / partnerships).

The form notifies the H M Revenue and Customs of your accounting date, your accountant, and also enables a PAYE (Pay As You Earn Scheme) to be set up, which is a requirement if you are to be an employer.

Once an accountant is registered as acting for you H M Revenue and Customs will discuss the traders or companies tax affairs with the accountant.

If you fail to register within the first three full months of self employment a penalty of £100 may be levied.

H M Revenue and Customs NI Contributions Office

Depending on the level of profit, sole traders and partners have a liability to Class 2 NIC. These are payable either quarterly or monthly by direct debit.

Class 2 contributions are at a weekly level of £2.30 (where annual earnings are £4,825 or more) and the necessary form to collect Class 2 contributions should be completed at the same time as the form CWF1.

H M Customs and Excise

You need to consider if it is beneficial to be VAT registered from the outset.

If you are registering for VAT, form VAT 1 needs completing, and if you are a partnership, form VAT 2 needs to be completed giving details of all the partners.

ACCOUNTING RECORDS AND RECORD KEEPING

A question that the owner of a business must answer is “Who will keep the books of the business?”

Will the receptionist or a secretary double as a part time bookkeeper, will you have a bookkeeper that comes in periodically, or will the volume of activity be such that a full time bookkeeper will be required?

Very often the owners of a business decide to keep the books themselves and underestimate the commitment they have made to other phases of the operation and the time required to maintain a good set of financial records and books of account.

As a consequence, record keeping is often low priority and must be caught up later. This approach, though rarely planned, can require a substantial expenditure of time and money. While it is important for the owners of a business to maintain control and stay involved in the financial operations of the enterprise, this can be achieved by maintaining close control over the cheque signing function and scrutinising certain records. Your company's accountant can help develop a good programme of record keeping duties for you, your employees and any outside bookkeepers or accountants you may engage.

A Word About Computers

The computer is probably the single, most valuable, invention for bookkeeping and accounting since the advent of double entry bookkeeping. If your business includes any of the following, then a computer would be a useful tool in your business:

- Many repetitive or routine tasks.
- Lots of paperwork, i.e. suppliers' cheques, sales invoices, purchase orders, mailing labels.
- Lots of general correspondence.
- Written reports, contracts, newsletters, catalogues or brochures.

There are a number of very good easy to use accounting software systems which are commercially available. If you want to use a computer based accounting package, either in your own business, with a service bureau, or through your accountant, it is imperative that you generate accurate information to be entered into the system.

The real value of the computer becomes apparent once it is running smoothly in your business. Your accountant can then function in the capacity for which he was trained, not as a “number cruncher”, but as your business adviser, consultant and strategist. Both of you can focus on analysing your business to make it more profitable.

Internal Control

Internal control is the system of checks and balances within a business enterprise that helps to ensure that the company's assets are properly safeguarded and that the financial information produced by the company is accurate and reliable.

When your company grows to the size where you must delegate some of the functions, it becomes more difficult to ensure that all the transactions are being accounted for properly.

No matter the size of your business, you should always be able to answer “YES” to the following questions:

- When my company provides goods or services to our customers, am I sure that the sale is recorded and the debt is recorded in accounts receivable until the cash is collected?
- When cash is expended by my company, am I sure we received goods or services?

The method used to ensure that these two questions can be answered affirmatively will be widely varied. They are essential stepping stones to maintaining good control in your business. The solution in your particular instance may be as simple as numbering the sales tickets and being sure ALL TICKETS ARE ACCOUNTED FOR or reviewing all invoices and timecards before signing company cheques. These are fundamentals in a well run business. As the company grows you will need to consider concepts such as segregation of authority as well as employee fidelity bonds or controlled access storerooms.

No matter what the size of your enterprise, you should consider controlling your business and safeguarding hard earned assets as a priority from the outset.

VALUE ADDED TAX

VAT is a tax on consumer expenditure and is ultimately paid by the final customer. Most business transactions involve the supply of goods or services and VAT is payable if they are made:

- in the United Kingdom;
- by a taxable person;
- in the course or furtherance of business and are not specifically exempted or zero rated.

VAT is collected by H M Customs and Excise and is normally payable quarterly.

Registration

There are two different types of registration - compulsory and voluntary.

Compulsory

A person who makes taxable supplies becomes liable to be registered if:

- At the end of any month, the value of his taxable supplies in the period of one year then ending has exceeded the registration limit, which is £67,000.
- At any time, there are reasonable grounds for believing that the value of his taxable supplies in the next 30 days will exceed the £67,000 limit.
- If, where a business carried on by a taxable person is transferred as a going concern, the taxable supplies for the twelve months prior to the transfer exceed £67,000.

In most situations, the person must notify Customs and Excise of the liability within 30 days of the end of the month in which the value of the taxable supplies first exceeded the VAT registration threshold.

Voluntary

The main situations in which a voluntary registration might be beneficial, even though supplies do not exceed the VAT registration threshold, is where the supplies are all issued to other VAT registered traders, or where all supplies are zero rated and no VAT is charged on the transaction.

All VAT suffered by a VAT registered trader on business expenses can be reclaimed from Customs and Excise.

Taxable Persons and Supplies

Taxable Persons

It should always be remembered that it is a person that is registered for VAT and not a business. If a person has two separate different businesses, both with taxable supplies of £40,000, then that person will be required to be registered for VAT and account for VAT at the appropriate rate on the total supplies of £80,000.

It is possible to mitigate the effect of VAT by having one of the businesses operated by a limited company or by a partnership with a relative, but professional advice needs to be taken since Customs and Excise have the power to still treat the two businesses as one if strict criteria are not met.

Taxable Supplies

Taxable supplies are all supplies made by a business either to a third party or to the trader himself (goods for own use), which are not exempt supplies. Taxable supplies therefore include zero rated supplies.

The major categories of exempt supplies are:

- Land (but not buildings);
- Insurance;
- Postal services;
- Betting, gaming and lotteries;
- Finance;
- Education;
- Health and welfare.

It is important that at the outset of a business, a trader establishes the VAT status of any supplies being made to avoid mistakes, e.g. the services of a physiotherapist are exempt, whilst the services of an acupuncturist are standard rated.

Tax Rates

There are three rates of VAT:

- a standard rate of 17½%;
- a reduced rate of 5%; (for certain supplies of fuel and power and sanitary goods)
- a zero rate.

The four main areas of zero rated goods are:

- Food and agriculture (but excluding pet food and most catering);
- Printed matter, including books and newspaper;
- Young children's clothing and footwear;
- Passenger transport (but excluding hire cars, taxis and parking).

Any VAT charged by the business, whether at 17½% or 5% is known as Output VAT and the total charged or collected in the VAT quarter is payable to Customs and Excise.

Input VAT

Input VAT is the VAT that you are charged on your business purchases and expenses (the other persons Output VAT) and is normally recoverable in full by a trader who makes standard rated or zero rated supplies. Businesses that make some exempt supplies (known as partially exempt businesses) have different recovery rules.

The total Input VAT suffered in the quarter is deducted from the Output VAT charged or collected and the difference is either the amount of VAT due to Customs and Excise or the amount repayable by Customs and Excise.

The majority of Input VAT is recoverable but there are special rules for:

- cars;
- petrol supplied for private usage;
- business entertaining;
- goods sold under a VAT second hand scheme.

To reclaim VAT you have been charged as input VAT, you must hold valid evidence that you have received a taxable supply, which normally means a valid VAT invoice from a registered trader showing his VAT number and the amount of VAT charged.

Special Events

It is not always possible to calculate each quarter's VAT liability by merely deducting input VAT incurred from 7/47's of the sales income and professional advice needs to be taken in the following situations:

- Importing and Exporting - either within or outside the European Union;
- Partial Exemption, i.e. where a business makes some exempt supplies, all the input VAT incurred is not necessarily recoverable;
- Retail Schemes, i.e. where both zero rated and standard rated supplies are made which cannot be separately identified at the point of sale;
- Land and Property;
- Cash Accounting;
- Self supplies;
- Second hand schemes for motor cars, used boats, antiques, horses and ponies and others.

Penalties

The impact of penalties has been considerably reduced since the early 1990's and the possibility of any business suffering a serious misdeclaration penalty for an innocent error on their VAT returns is low.

The two most important penalties still in existence which every business should be aware of are:

- Late registration penalty for not registering for VAT at the correct time. The penalty is based on a percentage of the VAT due between the date of registration and the date that the person was required to be registered and the percentage increases dependent upon the lateness of the registration. The penalty is in addition to the VAT that is due.
- Default surcharge for traders that are persistently late in either submitting VAT returns and/or making payment of the liability due. The penalty is based on a percentage of the VAT due and is on a sliding scale.

VAT Checklist

Registration

- Should the business be registered?
- Are details on registration certificate correct?
- Review position at regular intervals.

Preparation of Returns

- Has return been received? If not, then obtain duplicate from VAT Office or consider registering for online filing.
- Review sources of information.
- Prepare VAT return and check for accuracy and completeness.
- Make payment (if Outputs exceed Inputs)

Input Tax

- Do any restrictions on Input VAT reclaims exist?
- Are invoice additions and calculations checked?
- Is Input VAT claimed at the earliest tax point?
- Are all claims properly supported with valid tax invoices?

Output Tax

- Is all income reflected for VAT accounting?
- Is VAT captured at the correct tax point?
- Is VAT correctly applied where appropriate?

PAYROLL TAXES

Irrespective of the form of business in which you operate, if you are going to have employees then you will have to contend with payroll taxes.

Do you Have Employees?

Whether an individual is an employee or not is a question of fact depending on the terms on which he works. The question of whether an individual is employed or self employed is very important for the business "employing" him or her, as that business has to comply with the reporting requirements.

In certain areas the H M Revenue and Customs has placed emphasis on reclassifying individuals claiming to be self employed as employed. If you have treated someone as self employed and subsequently after a routine visit from the DSS or H M Revenue and Customs it is clear that they were employees, then the tax and NIC which should have been paid will be assessed on you. Therefore it is important to ensure when using the services of self employed people, that they are in fact self employed.

The Operation of a PAYE Scheme

Upon registration the H M Revenue and Customs will send to you guidelines on operating PAYE, National Insurance, Statutory Sick Pay and Statutory Maternity Pay (employer's pack).

In order to calculate the amount of tax and national insurance due by an employee, the H M Revenue and Customs will supply you with sets of tables. By reference to the "tax free" tables and an employees tax code you will be able to calculate the amount of salary that is not subject to tax. The difference between this figure and the gross amount is the employee's taxable pay.

The employer's and employee's national insurance is calculated by reference to the gross pay with another set of tables. Special rules exist for the calculation of national insurance for directors.

The tax and national insurance should be paid to the H M Revenue and Customs by the 19th of the month following that in which the salaries were paid.

In most businesses, the directors, and often the employees, have benefits that are not immediately taxed through the PAYE system, the most usual being the provision of a car and possibly fuel. Class 1A national insurance contributions are due on the taxable value of these benefits in kind and are due on the 19 July following the fiscal year in which the benefits are made available.

In addition, the H M Revenue and Customs requires on an annual basis, a form P11D (Return of expenses payments and benefits) for all directors irrespective of income and all employees receiving remuneration including the benefit in excess of £8,500. For those employees earning less than £8,500 but who receive expense payments and benefits, a form P9D is required.

A form P46(Car) needs to be completed quarterly on 5 July, 5 October, 5 January and 5 April if any employees have been provided with or have changed their company car. Further details are given on the taxation of company cars in H M Revenue and Customs leaflets IR132 and IR133. The H M Revenue and Customs will still require form P11D to be submitted annually in addition to the P46 (car) forms.

INCOME TAX AND CORPORATION TAX

Eventually you will have to deal with income or corporation taxes. The taxation legislation is extensive and can be confusing for an individual starting a business. A Chartered or Chartered Certified Accountant should be consulted when you are dealing with the taxation affairs of the business. The payment of taxation has a direct impact on your cash flow.

Tax Returns

Companies

Companies are charged corporation tax at the rate applicable during the financial year (1 April to 31 March). Where a company's accounts period spans two financial years the profits for the period are apportioned between the years.

There are special rules to calculate the tax rates applicable for profits falling between the small companies and normal rates, and are such as to ensure that the tax charge rises progressively.

A company is required to calculate its own liability to corporation tax and pay that liability by the normal due date, nine months after the end of the accounting period, without an assessment being raised.

The company is required to send its completed tax return (form CT600), accounts and tax computation to the Inspector by the filing date, which is 12 months after the end of its accounting period. Penalties will be charged if it is late.

Once the company agrees its liability with the Inspector, there will be a settlement of any balance due or overpaid. Interest will be charged or paid from the normal due date on the balance.

Sole Traders / Partnerships

Sole traders and partnerships are charged income tax at the rate applicable during the fiscal years (6 April to 5 April).

There may also be a liability to Class 2 and Class 4 National Insurance Contributions, depending on the level of profit in each fiscal year.

Class 2 contributions are at a weekly stamp rate of £2.30 (2008/09).

Class 4 NI is payable by the self employed on profits.

Class 4 contributions are levied at 8% on profits between £5,435 and £40,040 for 2008/09 plus a further 1% charge on profits in excess of the upper limit.

For the self employed and those that pay tax on other income such as rents, tax is normally payable in three instalments - the first two instalments are based on the tax paid on the previous years business tax liability.

Therefore half is paid by the 31 January in the year of assessment, the other half by the 31 July in the year following the year of assessment. The third instalment will be any balance due (payable the following 31 January) or any amount repayable by the H M Revenue and Customs if your final liability is lower than the amounts paid on account.

Under self assessment your income tax return, which encompasses your trading results, needs to be filed by 31 January following the tax assessment year. This date is moved forward to the end of September if you wish the H M Revenue and Customs to calculate your tax liability.

CASH PLANNING AND FORECASTING

CASH IS KING!

The lifeblood of any business is its ability to collect cash and pay bills as well as pay its employees, particularly its owners. Far too often small businesses are profitable, but they do not have enough operating capital to meet their current needs. Consequently, they may be forced to sell out to a stronger competitor or close the doors and put the company out of business.

The ability to forecast cash resources is by no means a well defined science. None of us have a crystal ball and any cash forecast which is prepared can be no more than an educated guess as to when the customers pay and when your business will pay its obligations.

Starting the Analysis

One of the most significant factors to be considered in your cash flow forecast is the volume of sales that will be generated in the period for which you intend to forecast. A sales forecast needs to be based on specific facts. These might include your sales history or the history of similar businesses you have owned or operated or the competition. In your area, what has been the experience of similar operations?

Some of the questions that should be addressed include what other factors could I control such as adding new product lines, deleting unprofitable operations, adding a new salesperson? In preparing a forecast, you must also take into consideration items such as the seasonality of your business, the relative state of the economy and the period over which you will forecast.

Cash Collections

Once you have determined your level of sales, you must address questions such as: what percentage of my sales are received in cash, and what portion are credit sales for which I will have to carry amounts in debtors? For those that are debtors based, how soon is the cash collected?

If you are relying on customer payments for collection of debtor balances you must determine what portion of the debts will be collected in thirty days, sixty days, ninety days and thereafter, and what portion, if any, may never be collected. To assume that 100% of your sales will ultimately be converted to cash is probably unrealistic especially considering the current economic environment and the tight cash situations that may face some of your customers.

Other sources of cash may be available in addition to sales. Do you expect to bring in a partner or other investors, or can you borrow money from a bank? Part of your cash flow analysis may be to determine how much investment money or borrowings will be required to operate your business.

Once you are comfortable with the cash receipt side of your business, and the timing of the collections of funds from your sales and other sources, it is necessary to consider the expenses and other cash needs of your business operation.

Cash Outlay

If your business entails sales of stock, you will have to purchase the merchandise or the component parts and pay employees to assemble it. This may require a significant outlay of cash before the first pound of sales is generated and received. You should consider how often and in what amount your employees must be paid and when their payroll taxes must be paid over.

Additionally, you need to know the credit trade terms your creditors are willing to advance to you. Do you have to pay for stock items on a cash n delivery basis or can you pay for them thirty or forty five days after receipt? What expenses must be paid to allow you to convert purchased merchandise to saleable stock? If your production requires utilities to run machines or supplies that are required, such as consumable chemicals or packing materials that must be purchased prior to the sale of the stock, you should consider the timing of these payments.

In addition to the cost of manufacturing, you should consider whether your productive capacity would allow you to generate enough stock to support the level of sales that you are predicting. If the volume of sales you forecast is above your ability to

produce today, what changes in your operating environment must be made to meet the production levels. Will you need additional employees, if so, how much will they cost? Do you have to acquire additional machinery for your shop operations? What is the cost of the machinery and when will you have to pay for it?

Once you have determined the cost of operating your production or service facilities, you need to consider what other expenses you must pay to keep the doors of your business open. You typically will have to pay rent for your office or manufacturing facility. You must consider how much the monthly payment is and when it has to be paid. Will there be other cash requirements such as a deposit on first and last month's rent. If you are opening a new business, you must consider what your cash requirements are to make your facility ready for your specific needs and purposes. Will you have to buy or rent furniture? Will you need to make tenant improvements or pay deposits for utilities and other services?

You also need to consider overhead items and costs to open a new business that will hopefully be one off expenses. This may be a solicitor's fee for drafting partnership agreements or incorporating your business, the cost to obtain business licences, setting up an accounting system, stationery costs, and costs of signs or logos.

It may seem like the list of costs and expenses to be incurred is endless. However, it is imperative to make the list as detailed as possible to ensure that you have sufficient funds to make your operation ready for business prior to running out of cash. The more detailed the list and the more sufficient information you can provide, the less chance there is of unpleasant surprises as you open your business.

In addition to determining the amount and volume of expenses and cash outlays you will have to make, it is critical to determine the timing of such payments. There may be a variety of financing alternatives that are available to you. Most of the start up cost which you incur can be delayed or deferred until you can generate the cash from your operation to help pay them. This needs to be carefully analysed and built in to your cash flow analysis. However, a good rule of thumb is to assume that you are going to have to pay your expenses sooner than you think and that you will collect your cash slower than you anticipate. If you work with this attitude, any surprises should be favourable ones.

The following tax matters require consideration as part of the preparation of your cash flow forecast:

VAT and Other Taxes

If you are VAT registered (compulsory for businesses with sales in excess of the statutory limit), your sales receipts will include "Output" VAT and some of your costs will include "Input" VAT.

The net receipt of VAT has to be paid over to the Customs and Excise each quarter. If, however, your sales are zero rated, you will be able to claim back the VAT on your purchases.

The basic calculation is not as difficult as is often made out. Typically, adding up your sales receipts for a quarter, multiplying the figure by $17\frac{1}{2}$ and dividing by $117\frac{1}{2}$, gives you your output VAT. Do the same for your purchase invoices to calculate Input VAT. Deduct Input from Output and put this figure into your cash forecast in the first month of the next quarter.

PAYE

If you employ people you will have to deduct tax from their pay and pay it to H M Revenue and Customs in the following month. For a forecast it is sufficient to put the gross figure in the cash flow forecast as it automatically includes PAYE.

Schedule D

If you are the proprietor of a business that is not a limited company, your wages are part of the profit of the company and referred to as "drawings". The tax that you pay will be based on the profit of the company not the amount that you take out. It is advisable to pay a sum into a deposit account each week to provide for this tax that will be due after your year end.

Many businesses go bust because they fail to provide for the taxes that are payable. Make sure that it does not happen to you!

OBTAINING CREDIT AND FINANCING FOR YOUR BUSINESS

At some stage you will probably need to obtain some outside capital for your business. You may need to obtain capital for the initial expenses prior to opening your business or for expansion.

Generally business financing takes two forms, debt or equity. Debt means borrowing money. The loans may come from family, friends, banks, or professional investors. Equity relates to selling an ownership interest in your business. Such a sale could be admitting a partner or, if you are in a company, issuing of additional shares to investors. It is typically a prudent idea to consult with your accountant, as there are many significant legal ramifications to such a step.

How Do I Get the Money?

There are several questions that must be answered during the course of raising money for your business. The ability to answer these questions is critical to your success in obtaining financing as well as the overall success of the business. Remember, in raising capital you have to sell the ability of your business to potential investors in much the same way as you sell your product to your customers.

1. How much Cash do I Need?

To answer this question you will have to do some cash flow planning, which will require estimates of future sales, the related costs, and how quickly you must pay your suppliers. You will also have to build into your planning when you will generate enough cash to pay the money back. However, if you raise cash through equity your investors will want to know how the value of the business will grow and how they will benefit through dividends or selling their shares.

2. What Will You Do With The Money?

One of the most important questions you will have to answer for a potential investor is how the money will be spent. Will you use it for equipment or to hire additional employees or perhaps for research and development for a new improved product? Again, part of the answer on how you spend the money is how it will benefit the company.

3. What Experience Do You Have in Running Your Business?

One of the primary reasons for business failure is lack of experience of management. You will need to convince your investors that you have the knowledge, experience and ability to manage your business and their money at the level at which you expect to operate.

4. What is the Climate for Your Type of Business and Your Location?

Few investors will want to put money into your business if you don't have a reasonable chance of success. If your business is based on existing economic or legal conditions that are subject to change in the near future your risk is substantially increased. If the local economy is sluggish you need to be aware of this before moving ahead.

Once you have developed answers to these questions, you can begin to look for financing. One of the first steps is to determine whether to raise funds through debt or share capital. The cost to your company of each type of funding is different, as is the way in which they are treated for tax purposes. The interest on borrowed money is deductible by a business for tax purposes, which reduces the effective cost to your company. Dividends which you might pay on the same investment in shares would typically not be tax deductible. In selling shares there usually is no firm commitment by your company to pay the money back but your shareholder will want, and generally will have, a legal right to have a voice in the management of your company.

Business Plan

Typically, a potential lender will want to know all about you and your proposed venture. Many of these details will have already been provided, but are best provided in a logical consolidated format. This format, or business plan, is a document that enables the investor to readily obtain an understanding of your proposal. It follows that in order to successfully raise funding, the business plan should be commercial and realistic.

Financing Alternatives

Whether you determine that debt or equity financing is the best choice for your company, there are a number of alternative types of financing available. Depending upon the nature of your business, the financing may be a combination of debt and equity and may be tailored to fit the specific needs of your company.

Debt Financing Sources

1. Banks

The first source of funds, which typically comes to mind when borrowing money, is a bank. Banks typically lend to small businesses on a secured basis using equipment, stock or debtors. The more liquid and readily saleable the assets you have to offer as security, the more acceptable they are likely to be a banker.

Loans from a bank may take several forms such as:

An overdraft limit which is reviewed annually and allows you to borrow up to a predetermined maximum as you need it and pay it back as funds from sales and receivables are collected.

A short term loan, usually between 3 and 5 years, for the purchase of a specific asset such as a computer or a machine.

2. Lease Financing

In today's business environment it is quite common to acquire equipment through lease agreements. Leasing packages come in a variety of types through many sources. Leasing companies typically will accept a somewhat higher degree of credit risk because they are looking to the value of the equipment for collateral if your business cannot make the agreed upon payments. For this reason, leasing companies generally prefer to finance new equipment of a general purpose nature which can be resold if necessary. Leases often run for a period of three to five years and because of the risk that leasing companies are willing to take, they are somewhat more expensive than commercial bank loans.

3. Trade Credit

A very important source of financing for your company may be from the creditors and suppliers with whom you do business. Many suppliers will originally ask for cash on delivery or, in some instances, they want payment before starting on your order, depending on the nature of your purchase. Most suppliers will quickly establish trade credit with you once you have gained their confidence by continuing to do business with them and paying as requested. Establishing good relationships with trade creditors is essential because it allows you to use the goods and services in your operations and sell your product to your customers, in some instance before you pay for them. The trade credit you build today will be relied upon by other suppliers as you attempt to establish yourself with other suppliers in the future. Trade credit terms will vary depending on the type of purchase you make, the industry you are buying from and the industry you are in.

INSURANCE

Sufficient insurance can be as critical to the success of your business as a good product or service. Without proper insurance you could lose all of the money, time and effort you put into your company. The types and amounts of coverage you purchase must be evaluated on a cost benefit basis like any other commodity that you purchase. Usually, you will want to insure against risks that could have significant detrimental impact on your business. This normally would include such items as fire, storm damage, theft, general and product liability.

Depending on the nature and size of your business it is often a good idea to self insure for all or a portion of certain losses. Self insurance can be accomplished by not buying coverage for incidental risks or increasing the deductions on policies that you do buy. Often, raising the deductible can have a very favourable impact on policy premiums. The administrative cost to the insurance company to process small claims is quite high, consequently the rates typically go down substantially if they are relieved of this expense by insuring for losses in excess of a sizeable deductible amount.

Required Policies

Very little insurance coverage is mandatory. The only insurance coverage typically required by law is public and employers liability. Your insurance agent can explain the required coverage, the rating systems, and help you purchase a policy.

You must also be aware that the terms of your building, office lease or mortgage may require you to carry certain kinds of insurance coverage in specified minimum amounts. If you have leased equipment or have borrowed money from a bank or other lenders, there will usually be insurance requirements in the agreements relating to these transactions. There are many other types of policies that you may wish to consider. The specific coverage provided by each and a qualified insurance broker can explain the related costs in depth.

Insurance is like any other product that you purchase. Before purchasing it you should consult with more than one broker as to your needs for protection. You should discuss insurance needs with acquaintances in the same or related business as yours. Before buying coverage you should check out the reputation of the company that is underwriting the policy.

C. TODD & CO
CHARTERED CERTIFIED ACCOUNTANT

COMPUTER ACCOUNTING SYSTEMS FOR FIRST TIME USERS

Introduction

A business user choosing a computer system for the first time has to give detailed consideration not only to the purchase of the hardware and software but to the installation of the system and the training of staff. The proprietor of the business will need to make a solid commitment in both time and money in order to reap the benefits.

Software

Accounting software, like hardware, is now very powerful and comparatively inexpensive. Integrated software includes Sales, Purchase and Nominal Ledgers with Sales / Purchase Order Processing and Stock Control in a single suite of programs.

Microsoft and their Office software package and Windows operating system is practically universally used on PC's nowadays. Accordingly, most other software producers have now produced Windows versions of their own packages. Microsoft Office includes word processing, spreadsheet and database software and will be suitable for most business environments.

E-mail and the Internet have had a great deal of publicity in recent times. There can be no doubt that development in these areas will significantly impact on our lives, both socially and commercially. Getting on to the Internet is a relatively simple and inexpensive process.

Developing and maintaining a website can be as complex and expensive as you care to make it. A great deal of careful thought needs to be given before significant time and expense is incurred as to how this aspect of technology be best implemented to suit your business.

Planning and Implementation

Planning and implementation must cover the layout of your accounts, control over the information going in and verification of the information coming out of the system.

Where advanced management information is involved, such as profit and loss by departments, more detailed planning is required. Development of a system can only take place at the pace at which staff are able to increase their own skills.

Even at the first stage the system should produce Aged Debtors and Aged Creditors reports on a regular basis to enable the business to improve its cash flow.

Security

The popular press would have you believe that it is only a matter of time before a virus attacking your hard disk eats up your data!

The most frequent reason for loss of data, however, is not taking backups.

Proper procedures should be in place to ensure you make regular backups of your data and then to make your backups as secure as is practical, from both accidental damage or theft.

USEFUL CONTACTS

H M REVENUE AND CUSTOMS

New Employer's Helpline	08456 07 01 43
Subcontractors Helpline	08453 00 05 81
Helpline for the Newly Self Employed	08459 15 45 15
Working Families Tax Credit	08457 14 31 43

www.hmrc.gov.uk

NATIONAL INSURANCE

National Insurance Contributions Office
Longbenton
Newcastle upon Tyne
NE98 1ZZ

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Companies House
Crown Way
Cardiff
CF4 3UZ

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