

Business Reality

a real guide to getting your business going

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BUSINESS REALITY

A REAL GUIDE TO GETTING YOUR BUSINESS GOING

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TWD Accountants is the leading independent tax and accountancy specialist providing start up businesses with practical advice and planning.

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1. Starting your own business - Is this for you?

Self employment can offer you freedom and flexibility. It gives you the opportunity to manage your own career and take it in a direction you choose. It is both exciting and rewarding, but it is also full of challenges. The level of commitment that you will need should not be underestimated.

You will have to be disciplined, organised and in the early days be happy to be the Managing Director, Financial Director, HR Consultant, Marketing Manager and the person that gets the job done.

This guide looks at the day-to-day reality of starting a business and outlines the skills and qualities that you will need.

Are you?

- ✓ **Realistic** – Can your business idea really work?
- ✓ **Confident** – Do you have faith in your own abilities
- ✓ **Determined** – Some days will mean gritted teeth and a lot of determination
- ✓ **Committed** – You may need to work long hours, 7 days a week

It can take several months before a business becomes profitable and you will also need to look at how you will finance any outgoings during this period.

You will need to:

- ✓ Make a realistic forecast of your personal financial needs
- ✓ Prepare a business plan to identify how much you expect your business to make during the first year and what profit you expect to achieve.
- ✓ Manage your cashflow of money coming into and out of your business
- ✓ Look at other sources of income to finance your needs during the early days of your business
- ✓ Prepare a budget and stick to it. Don't risk overspending or running out of money

2. Market Research

Researching your potential market is essential. By taking your time to research your market, you will stop the risk of investing in a business which is not viable.

You need to know:

- ✓ Who your target market is?
- ✓ Does your product or service satisfy or create a market need?
- ✓ Who your potential customers are and how you know they will be interested in your products or services.
- ✓ What is your competition doing? Find out who they are and how they work and what share of the market they hold
- ✓ How will your business survive in the future? Anticipate any changes in the market and how you expect to react to them.

It is important to take time to answer these questions to increase the chance of your business becoming a success.

3. Business plan

A **Business Plan** will help you focus your proposed business venture, look at the financial aspects and help sell your vision to others.

By writing a business plan - you will help make your business become reality. Seeing your ideas in black and white will help you fine tune your product or service. By moving systematically step by step through your business process, you can help ensure you will get off to a flying start. It does not need to be an intimidating process - it will help you focus your mind - and it is vital for convincing your bank or other potential investors.

What should you include?

- ✓ **A Summary**
This outlines in a few paragraphs your whole business; it will create a feel for your business outlining your product or service and its advantages, the opportunity in the market, your team, how the business will be run and a brief overview of financial projections.
- ✓ **The Business and the Product**
Explain the background, your related experience, the proposed structure of the business. Add how your business will stand out from the competition; include your point of difference. Cover any threats to the business - it shows you are realistic.
- ✓ **The Market and Competition**
Your market research will be included in this section, including your customers, your competition and your understanding of how the business fits into the market.
- ✓ **Promotion and Pricing**
How will your customers know about your product or service - this is crucial to success. How will you position your product/service/how will you price it?
- ✓ **Management**
Include the structure and skills of your team. If you are going it alone, sell yourself, your skills, your experience, your history. It will give you the added confidence that you have the skills and expertise to make your idea work.
- ✓ **Operations**
Where will you be based?
What equipment/facilities will you need?
You also need to include in this section staff and supplier needs.
- ✓ **Finances**
Include a realistic sales forecast, your cashflow forecast, how much money you expect to be coming in and crucially going out of the business.
- ✓ **Financial Requirements**
What are you looking for? How much finance do you want, what will it be used for and here you need to confirm that your business can support any repayments.

Keep your business plan short and to the point and make it look professional. A well-presented plan will reinforce the positive impression you want to create of your business.

Most importantly, make sure your plan is **realistic**. Once you have prepared your plan, use it and update it regularly, it will help you keep track of your business' development.

4. Financing Your business

The amount of finance needed will vary from business to business, some will require a minimal amount of investment others significantly more. Sources of finance are varied and numerous, such as long or short term finance via loans or overdrafts provided by the Banks.

Raising Finance

- ✓ Seek professional help
- ✓ Go to your high street bank (they are still the main source of finance)
- ✓ Banks can usually offer tailor made solutions to meet your needs
- ✓ Finance provided by high street banks accounts for approximately 75% of all funding
- ✓ Can you invest your own savings, can your family help?

Other Sources of Income

Contact your local Business Link

They can offer guidance on any grants and financial incentives available to new businesses in your area.

Contact the Princes Trust

In 2009/10 the Enterprise Programme was launched to help young people who are interested in self employment to explore and test their ideas, write plans and start their own business.

Contact your Job Centre

If you are claiming certain benefits i.e. job seekers allowance, there may be assistance available from the benefits agency. For more detailed information contact your local JobCentre Plus.

You need to decide how much money you will need and draw up a budget based on the forecasts in your business plan. It is better to be realistic with your forecasts, don't be over optimistic about your sales in the first six months of your business.

Cashflow Forecast

A start-up business may spend more than it earns for the first couple of years and many businesses have seasonal sales patterns that lead to predictable cashflow peaks and troughs - all this needs to be taken into account when you are launching your business and the amount of money you will need.

Preparing a cashflow forecast will help you to plan your borrowing and will show you how much surplus cash you are likely to have throughout the year. You can identify the sources and amounts of cash coming into the business and where the cash will be paid out over a period of time.

Usually cashflow's are done for a year or a quarter in advance and divided into weeks or months. You should look at periods during which most of your fixed costs are going out, such as salaries or rents.

5. The Business Structure

Once you have decided you want to go ahead, you need to consider how your business will work and the legal implications that will have.

You need to look at which structure best suits the way that you intend to do business, as this will affect a number of factors such as:

- Who you need to notify that you have commenced in business
- What will you need to pay in tax and national insurance
- The records and accounts that you have to keep
- What will you be liable for if your business runs into financial difficulty

Setting up your business in the right way will help keep costs down and help prevent your working relationships breaking down.

Sole Trader

This is one of the most common and popular ways to launch a small business. If you are a sole trader you are self employed and have no special legal structure. As the name suggests you are the sole proprietor and fully responsible for all the business activity. It is the simplest business structure.

Once you have decided to trade in this way your only duty is to inform HM Revenue & Customs.

Once trading you will be responsible for the financial affairs of the business, including book-keeping. It is also your responsibility to ensure your sole trader profits are reported to HM Revenue & Customs on a Self Assessment tax return and any taxes due are paid on time. All of which an accountant can assist you with. It is important to note that in the eyes of the law you and the business are one and the same. That is you are responsible for any debts of the business and will be called upon to repay them if the business cannot.

Partnership

In a partnership, two or more self-employed people work together as partners and share the profits (or losses). The responsibility of running the business can be split between all the partners.

It would also be advisable to seek advice from a solicitor on a partnership agreement, this is a legal document, which sets out what each partner's responsibilities are and the ratios in which both profits and losses are to be shared. It will also make provision for resolving disputes between the partners in the event of any terminal disagreement.

Limited Company

The formation of a company can have two main effects. It separates in law your business and private affairs, offering you protection from any debts built up by the company other than those where the provider has insisted upon a personal guarantee, most usually a bank loan or overdraft. Secondly, there can be tax savings compared to that of a sole trader/partnership.

There are more formalities involved in both creating and running a limited company. For more detailed information on the responsibilities involved in running a company look at www.companieshouse.gov.uk. For cost implications your accountant will be in a position to outline both tax savings and costs comparisons.

6. Legalities

As a business owner, you need to have a working knowledge of the relevant legal issues and requirements.

This is one area where it is highly recommended you get professional help - ensuring you have ticked all the boxes could save you a lot of unnecessary expense later on in your business life.

In simple terms you need to be aware of laws affecting:

- ✓ employment
- ✓ the workplace
- ✓ insurance

Take advice on:

- ✓ recruitment
- ✓ terms and conditions of employment (the contract)
- ✓ wages and working conditions
- ✓ employee rights
- ✓ discrimination
- ✓ maternity and paternity leave
- ✓ sickness
- ✓ grievance procedures
- ✓ termination of contracts
- ✓ redundancy

Employment law is complicated - always take advice and be clear on your positions. Make sure you keep all relevant records and your staff have contracts.

Running a workplace - whether you are working from home, a mobile office or renting office space, means that you also have legal obligations. We would recommend you also take advice when setting up your business.

Ensure you have the relevant policies in place for:

- ✓ health and safety
- ✓ your business and the environment
- ✓ planning permission/building regulations
- ✓ licences
- ✓ data protection

Make sure you are insured, your workplace is insured and your people are insured. This is an expensive area and can be costly for a business if it is ignored.

Your insurance checklist:

- ✓ **Employers Liability**
This covers you against claims from employees for accidents or sickness
- ✓ **Motor Insurance**
All motor vehicles your company uses must be covered
- ✓ **Public Liability Insurance**
This covers damages payments and any legal costs to members of the public for damage caused by your business
- ✓ **Product Liability**
If you make or sell products, this would cover you for any defects in your products design or manufacture.
- ✓ **Professional Indemnity**
This covers you if you provide advice in a professional capacity.

7. Your Accounts

This section covers your book-keeping, credit, VAT, Tax, National Insurance and PAYE needs.

Keeping Records

From the moment you consider becoming self employed you must keep track of all financial transactions affecting your business. It may also be possible to claim tax relief for some expenses incurred prior to trading. This works on condition that the items of expenditure are used wholly and necessarily in your business, and were incurred in the 7 years prior to trading.

Typically such expenses could include:

- ✓ Market Research
- ✓ Designing and Testing Your Products/Services
- ✓ Computer Equipment & Software
- ✓ Website Design

Initial training costs are not normally tax deductible, however further guidance should be sought from your accountant on this matter.

Book-keeping

Good book-keeping is the key to effectively managing your finances and running a successful business. Keeping it simple is the key to understanding your business and doing it regularly makes the job easier.

If you are self-employed, you are responsible for reporting all your income and expenditure to H M Revenue & Customs in an accurate and honest manner. The key is keeping good records. Good record keeping does not necessarily involve employing a professional book-keeper or investing in expensive computer software - an account ledger, diary notes or a simple computer spreadsheet can be sufficient to record your income and expenditure.

It is recommended the new business opens a separate business bank account. If you prefer to use a credit card, then again, separating your business and personal transactions into two separate cards is recommended.

Separating your business and personal life will make the preparation of sole trader accounts easier and quicker, it also offers a limited amount of protection should H M Revenue & Customs wish to enquire into your business affairs.

Every month compare your bank statement with your cash book - both balances should be the same.

The forms of transaction that require recording:

- ✓ A record of every sale
- ✓ Bank transactions
- ✓ Cash payments and cash receipts for every purchase
- ✓ Credit card payments

When deciding on how to record your transactions you must make provision to identify which receipts/payments are cash, bank or credit card. With regards cash receipts you must also be able to identify any cash not deposited to the bank but used for sundry cash expenses or general living expenses.

Good record keeping is an essential part of running your own business. Failure to maintain good records could result in paying excessive tax.

8. Tax, National Insurance & VAT

Tax on Business Profits

If you operate your business as either a sole trader or partnership then you are liable to pay tax and National Insurance on the profits of the business irrespective of how much income you take as a salary - usually called drawings. Tax is generally payable in two instalments, these are known as Payments on Account.

Payments of tax are made in both January and July of each year and are based on the previous year's profits.

Limited companies currently pay their tax in full 9 months after the end of the accounting period.

Whatever your legal structure it is important to put money aside to pay your taxes. Late payment of tax will always incur interest charges and may lead to legal proceedings being taken if payment is not received at all. To determine what monies need to be put aside to cover your taxes speak to your accountant.

Case Study

Mr Smith's first year of business runs to 5 April 2011. His first year's profits are £15,000. The tax and national insurance due on these profits is approximately £3000. The tax due has to be paid in full on or before 31 January 2012.

In addition to this Mr Smith would also have to make a payment on account towards his profits for the year ended 5 April 2012. This payment is always 50% of the previous year's tax bill so would be £1,500. This brings the total payable on 31 January 2012 to £4,500. The rules also state that a further payment on account of £1,500 would be due on the 31 July 2012.

So when Mr Smith calculates his next year's tax bill he will have already paid £3,000 in advance to cover the 2012 tax bill. This system of tax payment will then continue as long as Mr Smith is self-employed.

National Insurance

As a sole trader or partnership you also need to make National Insurance contributions.

These fall into two categories:

- ✓ Class 2 contributions - these are paid as a fixed weekly rate of £2.50 (2011/12) From April 2011 if you're self-employed you can pay your Class 2 National Insurance either monthly or six monthly by Direct Debit, or pay in response to payment requests HMRC issue in October and April. The table below shows the due dates for payment of Class 2 National Insurance contributions for 2011-12.

You can also make one-off payments for any arrears you may owe.

Payment Request issue date	Period covered by payment requests	Number of contribution weeks	Due date of payment
October 2011	10/04/11 to 08/10/11	26	31/01/12
April 2012	09/10/11 to 07/04/12	26	31/07/12

- ✓ Class 4 contributions - these are profit based contributions and are charged at a rate of 8% of profits less an exempt amount of £5715 for 2010/11 subject to maximum contributions. Any class 4 contributions due are calculated as part of your Self Assessment Tax Return and will be advised by either your accountant or H M Revenue & Customs.

It is possible to claim either an exemption from or defer payment of these contributions. However, it is suggested that you speak to either your accountant or the H M Revenue & Customs before doing so.

8. Tax, National Insurance & VAT cont..

Value Added Tax (VAT)

If your business sales exceed the annual VAT limit, currently £73,000, then you must register for VAT. There are various rates of VAT information on which can be found in more detail at www.hmrc.gov.uk/vat/index.htm

You must issue VAT invoices which clearly state your VAT number and VAT details need to be entered separately into your accounts.

If you are required to charge VAT on your sales to customers, you are then entitled to reclaim any VAT you pay to your suppliers, the net amount only being paid to Customs & Excise.

Like all taxes you must register your business for VAT at the right time. Failure to do so will result in a penalty. As a rule of thumb at the end of each month you must look back at your sales for the preceding 12 months, if the income is in excess of £73,000 you must register immediately. If turnover is less than £73,000 but you think that it will exceed it in the coming month, then again you must register immediately. If you are in any doubt contact your local VAT office.

Of course like all taxes there are a number of schemes available to small businesses to reduce the administrative burden placed on them. For more detailed information please see the Customs & Excise website or contact your local office.

Top Tip -

Remember book-keeping records and supporting receipts should be retained for 5 years and 9 months after being submitted to the Revenue.

PAYE & National Insurance

Running your own business does mean you have a responsibility to not only pay taxes but also collect it on behalf of the government. Aside from VAT this takes the form of tax and National Insurance payments on behalf of any employees you may have.

If you employ people, you have a responsibility to deduct income tax and national insurance from all payments to employees. If you do take on employees you must inform H M Revenue & Customs immediately and they will send you a pack containing all the information you need along with calculations on how much tax and national insurance to deduct. As will all other tax payments there are time limits that must be adhered to or penalties will be charged.

Credit

Many businesses rely on credit control to run their business. When starting up your business you need to decide what credit you are going to give your customers, what your payment terms are and how you will manage chasing debts.

You can check other companies credit ratings online and it can cost as little as £50 - it is always worth asking your customers for trading references so you can check their trading history. By spending time doing your research, you will minimise the chances of dealing with bad debtors who could ruin your business

9. Key dates for Your diary

- 31/01** Final submission deadline for Tax Returns filed by internet.
- 31/01** The final date for payment of tax not being collected via your tax code.
Interest will start to accrue from 1 Feb if not paid
- 31/01** The last payment date for the first payment on account for the current tax year.
- 31/01** For any tax return outstanding for more than 12 months, you will be fined the greater of £300 or 5% of the tax liability, or possibly 100% of the tax due as a penalty
- 01/02** A late fixed filing penalty will be issued for any returns not filed by 31 January
- 28/02** 5% surcharge added to tax liability due by 31 January which is still outstanding.
- 05/04** Last day of the tax year
- 06/04** First day of the tax year
- 01/05** For any return that is 3 months late you will be fined £10 for each following day - up to a 90 day maximum of £900. This is as well as the fixed penalty above.
- 06/07** Final date for P11Ds and P9Ds to be issued by employers. This applies to employees' copies and submission to Tax Office.
- 31/07** Second 5% surcharge added to tax payable by 31 January just passed but still outstanding.
- 31/07** The final date to pay the second payment on account for the tax year just ended.
- 01/08** A second £300 fixed penalty or 5% of the tax liability, whichever is greater, will be imposed on all outstanding tax returns which should have been submitted by the previous 31 January.
- 05/10** Final date to tell your Tax Office about any undeclared income if you have not been sent a Tax Return.
- 31/10** Final submission deadline for paper tax returns.
- 30/12** Final date for submitting returns via the internet if you wish to have a tax underpayment (up to £2000) collected through your tax code.

10. Additional information

The numbers you need to know:

Business Registration

Companies House

0303 1234 500

www.companieshouse.gov.uk

Tax, VAT, PAYE and National Insurance

HM Revenue and Customs

0845 915 4515

www.hmrc.gov.uk

Consumer Rights

Office of Fair Trading

08454 04 05 06

www.offt.gov.uk

Education & Training

Department for Education

0870 000 2288

www.dfes.gov.uk

Health & Safety

Health & safety Executive

0845 345 0055

www.hse.gov.uk

Data Protection

Information Commissioner

08456 30 60 60
or 01625 54 57 45

www.informationcommissioner.gov.uk

Environment

Environment Agency

08708 506 506

www.environment-agency.gov.uk

Business Support/Grants

Business Link

0845 600 9006

www.businesslink.gov.uk

Princes Trust

0800 842 842

www.princes-trust.org.uk

Young Enterprise

01865 776 845

www.young-enterprise.org.uk

Grants

www.j4b.co.uk

Tax & Accountancy

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