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OPTING TO GO IT ALONE

Joining the ranks of the self-employed has implications right across the spectrum for your personal finances and requires some very careful forward planning, writes **John Cradden**

LAST year around one-in-five people in Ireland were self-employed, according to the Central Statistics Office.

More people look set to join the ranks of the self-employed during 2010 and 2011 as increasing numbers are made redundant and/or decide to go it alone.

However, moving from an employed position to self-employment requires some careful financial planning.

Tax and VAT

One of the first issues will be whether you should set up as a "sole trader" or form a company. Setting up as a sole trader is simpler and easier, but setting up a company has some distinct advantages.

The main one is that it limits your personal liability. In other words, you will not be forced to sell any personal assets, such as your family home, if your business goes bust.

David Price, Principal of Taxmedic a tax and accountancy practice, Dublin , says it can cost as little as €300 to set up a company, and about €500 extra per year over what it would cost to run as a sole trader.

If your business is supplying goods and your turnover is more than €75,000, then you will have to register for VAT (value added tax). If you are supplying services, the registration threshold is just €37,500.

If you set up as a company rather than as a sole trader, you will have to pay PAYE (pay as you earn) and PRSI (pay-related social insurance) every month as you will be drawing a salary from the company in much the same way as if you were employed by someone else.

If you set up as a sole trader you will not need to pay income tax until after the end of your first year.

"For this reason, they will need to become more disciplined and remember to put aside an amount each month to meet the future tax bill," says Mr Price.

Expenses and record-keeping

When it comes to claiming all the expenses you are entitled to, the safest thing to do is to keep all expense receipts during the year, even if you aren't sure if you can claim on them.

You should also check out expenses or assets you already have to see if they can be attributed to business activity when the time comes to prepare your first set of accounts.

"For example, if working from home a portion of household utilities and existing home computer, desk, chair etc, as well as the family car, may all be deductible in part," says Mr Price.

In terms of record-keeping, you must, at the very least, keep a written record of all income showing the payer, date received, where lodged, or if it was received in cash.

If the business is VAT registered, record-keeping gets a bit more complicated, so it's worth asking a tax adviser to look after the paperwork – or show them how to, says Mr Price.

Insurance

As a self-employed person, you will not benefit from any of the insurance protection that you might have enjoyed as an employee if you were unable to work, such as income protection, serious-illness cover, or private health insurance.

In addition, you may need to insure yourself or your business against accidents, theft or damage.

If you are renting office premises and equipment, you will need contents insurance; liability insurance to cover injury or damage on the property; and employers' liability if you are employing anyone.

"Generally insurance companies offer packaged policies which are designed for SMEs (small and medium-sized enterprises) rather than the customer having to shop around for individual policies," says Jane O'Driscoll of the Irish Insurance Federation.

Pensions

Setting up a limited company gives you more scope in terms of pension funding, but whatever way you set up a pension, you need to make sure you have enough cash to make a pension contribution in the first place, particularly in the first few years.

"New start-ups should really only make pension contributions after they are 1,000pc sure they have enough cash to cover future issues, many of which won't be anticipated," says Michael Kiernan of Myadvisor.ie.

Mortgages

If you just become self-employed, you should know that banks will not entertain any mortgage applications until you have been in business at least three years, according to Karl Deeter of Irish Mortgage Brokers.

"Banks will often look for tax balancing statements to back up accounts and other supplemental information, so if you haven't been trading for several years, getting a mortgage will be extremely difficult," he says.

"Having said that, if one applicant in a joint application has secure employment, it makes the case better," said Mr Deeter.

New start-ups should only make contributions to pensions after they are 1,000pc sure they have enough cash to cover future issues