Tax and becoming an associate: What you need to know

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In our last article, we marvelled at the behaviour of that most amazing species - the dentist – emerging from its cocoon of studies and venturing into the world of employed work for the first time. In this article following the dentist on its life cycle – truly a sight to behold in the natural world – we talk about becoming self-employed – blossoming into an associate, which for most of their kind, is a natural progression.

As we discussed last time, being employed is easy in the sense that you do not have to complete a tax return – all you need to do is to remember to claim tax relief on your expenses that are wholly, exclusively and *necessarily* incurred. You don't need to worry about setting money aside for tax, tax return filing deadlines, keeping adequate records. However, when you become self-employed, all that changes. It is not without its blessing – being self-employed gives you more flexibility to claim tax relief on expenses, for in the definition of wholly, exclusively and necessarily, the 'necessarily' is now dropped. But you do have to be mindful of several things. Let's try to break these down.

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Once you become self-employed, you need to register as such with HMRC and obtain a UTR. This UTR (unique tax reference) will stay with you until you die (or if you are unlucky enough to be declared bankrupt in which case you will also get a new one). You also need to ensure your Tax Returns are filed by 31 January each year and that you pay your self-assessment tax by 31 January and 31 July each year. Next year, there will also be additional deadlines to observe – for making tax digital.

Keeping proper records

HMRC are entitled to enquire into the tax affairs of any taxpayer that they wish to. If they did that, they would ask you for your records – invoices, pay slips, bank statements etc. Hopefully you will not be in that position, but it is a good idea to get into the habit of keeping adequate records in an organised way, from the outset, just in case. This has other benefits as well – you will find it easier to know where you are at, it will be easier for you to give your accountant details that they need for your tax affairs, you are less likely to leave out any business expenses that you could claim tax relief on, and it will make planning much easier. I always suggest to my clients to have a system of four bank accounts – a work account, a personal account, a tax savings account, and a personal savings account – to keep things easy and efficient.

Claiming tax relief on all allowable expenses

This also links back to point 1, as you need to know which expenses get tax relief so that you can ensure you put them through your work account. It is extremely important that you sit down with your accountant when you first start your self-employment to understand, in your own situation (as this will vary person to person) what will qualify as work expense. If you do not do this, it means you will either pay for expenses from the wrong account (and that could cause problems in the event of a tax enquiry) or you will not claim relief on all allowable expenses (and you will then be voluntarily paying more tax than you need to!)

Set aside money for tax

This is the one which, if you do from the outset, will make the biggest difference for you. When you first become self-employed, you do not pay tax until 31 January after the end of the tax year in which you started your self-employment. What does that mean? Let's say you start your self-employment in September 2023. That is in the 2023/24 tax year (as it falls between 06/04/23 – 05/04/24) and the first 31 January after that is 31 January, 2025. So, you would not pay tax for over a year after you start work. In that time, you will probably see your bank balance go up and up and up as, when you were an employed VDP, tax was already deducted from you but now, as a self-employed associate, no tax is deducted from you. It is important to remember and train your mind that all of that money sitting in the bank is NOT your money. A chunk of it belongs to HMRC. And that is where I would always suggest that you feed your tax savings account every month, so you are saving for your tax as you go along so as to not be caught short when you come to pay your first tax.

Check your structure serves you well

We have been talking as if you are self-employed – AKA a sole trader. However, it is also possible for you to trade as a limited company or even, in some cases, to trade as a limited company and a sole trader. There is not enough time here to go into the pros and cons of each and what you must consider before making the change (we will do that in the next issue), but it is essential that you review this very carefully with your accountant – not just when you start your self-employment but also regularly over the course of your self-employment as things (how much you earn, how much you need and a whole host of other things) change.

Two things that you should bear in mind linked to this are:

a. If you have your NHS income paid into a limited company, you will lose your entitlement to pay into the superannuation scheme. This is a heavily subsidised scheme and whilst I am not a pensions advisor, I do understand how much it is worth and that you need to think very carefully if you are considering forgoing this.
b. As above you will also lose entitlement to NHS maternity pay.

As Sir David Attenborough said, 'an understanding of the natural world is a source of not only great curiosity, but great fulfilment' and hopefully this article will have helped you to understand the second phase of our target species' life cycle much better. ◆

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