FINANCE UPDATES
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CAMPBELL & McCONNACHIE
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FINANCIAL PLANNING FOR SOLE TRADERS

Important considerations for the self-employed.

Being your own boss continues to appeal, with 3.5 million sole trader businesses registered in the UK at the start of 2019.

Sole traders, according to the Department for Business, Energy and Industrial Strategy in October 2019, account for around 59% of the UK's entire 5.9m private sector business population.

Being self-employed offers a range of benefits, from the opportunity to work wherever and whenever suits you to accepting as many jobs as you want or need.

Self-employment, however, comes with no health insurance, paid annual leave entitlement, workplace pension, sick pay or other benefits offered by an employer.

Whether you are a self-employed architect, a software developer or somewhere in between, the need for independent financial advice is patently clear.

RETIREMENT PLANNING

Most employees you know will have been automatically enrolled into a workplace pension, while no solution has been found to extend that to the self-employed.

With no employer paying into a pension on your behalf, saving for retirement falls on your shoulders.

According to the Office for National Statistics, self-employed people aged 35 to 54 are more than twice as likely to have no pension wealth than employees.

Most self-employed people, according to NEST, recognise the importance of saving for retirement – but few specifically save into a pension. The government-backed pension provider polled 2,000 sole traders and found only 24% contribute into a pension.

Instead, 76% of self-employed respondents admitted to using other options like ISAs, property and savings accounts to save.

Around three in four (74%) recognised the importance of saving into a pension, however.

An easy place to start would be through paying class 2 or class 4 national insurance contributions (NICs) to build up your entitlement to the **state pension**.

The state pension will not be enough to retire on and you will need other savings vehicles, while a minimum of 10 years of NICs are needed to qualify for the new state pension.

In order to get the maximum state pension, however, 35 years of NICs are required – and you need to wait until you reach your state pension age to start drawing it.

A **self-invested personal pension (SIPP)** allows you to choose how much you want to invest and when you want to invest it.

You can invest in mutual funds, cash, shares, exchange-traded funds or investment trusts, while HMRC provides 20% tax relief on any amount you pay in.

Only basic-rate tax relief is automatically claimed. If you pay a higher rate of income tax, you will need to reclaim relief through your tax return.

Unlike the state pension, you can usually start accessing your SIPP from the age of 55, while a range of options are available under pension freedoms.

Pension contributions from the profits of a limited company can be exempt for tax, while contributions paid by you as an individual may qualify for income tax relief.

SECURING A MORTGAGE

Depending on which sector your sole proprietorship operates in, your income can vary if your business is not in constant demand or lacks a steady workflow.

Many self-employed people also mistakenly believe their varied income or lack of three years' worth of accounts make them ineligible for a mortgage.

These are major misconceptions that have caused some sole traders to give up applying for mortgage without even trying.

Some have even been labelled 'mortgage prisoners' after becoming trapped with loans taken out before the recession in 2008.

With interest rates falling to and remaining at historic lows ever since that point, these homeowners have been paying interest above the market rate.

It should be much easier to switch to cheaper loans after the Financial Conduct Authority (FCA) reversed mortgage rules, which were introduced by the Financial Services Authority – a predecessor of the FCA.

Whether you want to secure your first mortgage, renegotiate an existing loan or are considering buying to let, we can point you in the right direction.

PROTECTION POLICIES

Protecting your income is one of the biggest headaches for the UK's army of sole traders and it may be worth arranging your own financial safety net.

This provides peace of mind in the event you miss out on income after becoming unwell or have an accident that stops you from working.

There are plenty of insurance products on the market, and we can compile a package to replace your income if you become seriously ill or incapacitated.

Three of the most common policies for the self-employed are income protection, life insurance and critical illness cover.

Income protection policies cover most illnesses and you can usually make as many genuine claims as you need over the duration of the policy.

You could also consider taking out life cover if you have any dependants, typically children or grandchildren.

Employers usually offer this as part of their workplace benefits, so it makes sense to think about setting it up for yourself.

If your business operates as a limited company, you may be able to put the cost of **life insurance** through your business much like other allowable expenses.

Regardless of your business structure, this is worth thinking about if you have any children or other loved ones who depend on you financially.

Typically, the person or persons named as beneficiaries of your life insurance policy will receive a lump sum or regular payments if you die.

Critical illness cover is a long-term policy that pays out a tax-free lump sum if you are diagnosed with life-threatening conditions like cancer, heart attack or stroke.

This cover can be used to pay off debts, including a mortgage loan, or to cover the costs of changes you need to make to your home as a result of your condition.

However, common ailments like a bad back or stress are not covered by this sort of policy, and it won't pay out to dependants if you die.

This document only touches on a few financial planning considerations for the self-employed, and you can contact us for much more detail.

Get in touch for independent financial advice.

IMPORTANT INFORMATION

The way in which tax charges (or tax relief, as appropriate) are applied depends on individual circumstances and may be subject to future change.

Pensions eligibility depends on individual circumstances, while your home may be repossessed if you do not keep up repayments on your mortgage.

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