

A man with glasses and a ponytail, holding a pen, looking at a laptop screen in a modern office setting. The background shows a window with a view of trees and a small potted plant on the desk.

Sole trader vs limited company – when should you switch?

by Lauren Hellicar

About Simply Business

We're one of the UK's largest business insurance providers. Since we started life in 2005, we've helped three million small businesses and self-employed people find the protection that's right for them, from builders to bakers and personal trainers (we cover landlords, too).

How does it work?

Answer a few questions about your business and we'll show you quotes from a range of insurers. After you buy, our Northampton-based team will be with you through every step of your cover, whether you have questions about your policy or you need to make a claim.

Sole trader to limited company

The decision to change from 'sole trader' to 'limited company' legal status can be tricky to call – especially if you're just getting to that point where you're making enough profit for incorporation to be a viable option.

To help you weigh up the pros and cons, we've created this handy guide on the benefits of incorporation versus staying as a sole trader.



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What's the difference between sole trader and limited company?

The sole trader legal structure differs from that of limited companies in several key ways. A sole trader is self-employed and owns and runs a business as themselves, whereas a limited company has its own legal identity.

You can read more about the [difference between sole trader and limited company](#).

How to become a limited company – and when?

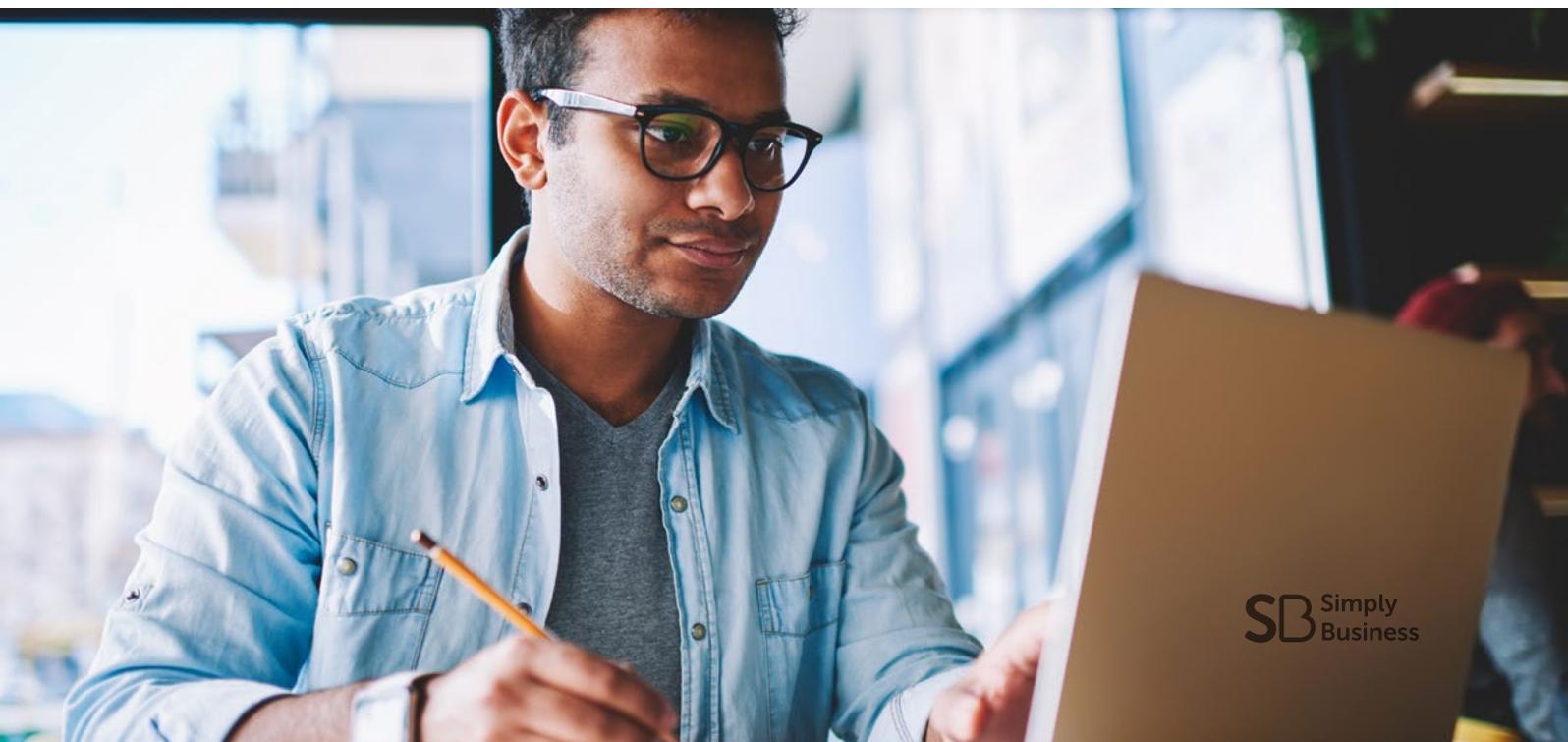
In time, the profits of a successful small enterprise will start to flow in. At this point, you may want to consider how becoming incorporated could lower your tax bill.

Speak to an accountant or financial advisor if you're unsure whether it's the right time for your business financially.

You can read all about [how to set yourself up as a limited company](#) in our step-by-step guide.

Here are the key steps you'll need to take if you're changing from sole trader to limited company:

- decide whether you'll be the sole director or whether you want to bring in others
- tell HMRC your legal structure has changed – this is very important because changing legal structure affects the amount of tax you need to pay
- choose a name for your limited company
- register your business with Companies House – to do this you'll need to [create your memorandum and articles of association](#)
- set up a new [business bank account](#) for your limited company
- tell your insurer your legal structure has changed



Sole trader or limited company pros and cons

If you're already a sole trader, incorporation might be a good step in certain circumstances.

Many small businesses and self-employed people start out as sole traders because it's the easiest legal structure to set up – especially when you're keen to get going with your new venture.

Reasons for changing to a limited company

Despite more admin, becoming a limited company can bring **increased tax-efficiency**, as well as **limited liability**, **greater borrowing power**, **improved reputation**, and **credibility** among clients and customers.

Another key benefit of changing from sole trader to limited company is what it could do to boost your business's image in the eyes of your customers. Incorporation may give you more of a professional edge by showing the world that you're a legitimate setup.

Depending on the nature of your business and the direction you want to take it in, you may also want to bring in other directors, or maybe shareholders. To do this, you'd need to be a limited company.

Reasons for staying a sole trader

If your earnings stay relatively low, you'll probably want to keep your tax and accounting as simple as it can be so you can do it on your own, or at least not pay the higher accountant fees that tend to come with being incorporated.

One thing to think about here is whether you need the limited liability aspect of incorporation.

You may want to look into forming a limited company if you increase your earnings. Things to take into account when you're making this decision include how much profit you're making and the current rates of tax you'll need to pay.

The costs associated with being a limited company rather than a sole trader will need to be lower than your profit to make it worth your while, so it's a good idea to do some calculations before you take this step.

It's also worth bearing in mind the time and effort involved in [bookkeeping](#) and other administrative tasks around being incorporated. However, if you want to [borrow money to grow your business](#), this is likely to be far easier if you change from sole trader to limited company status.



What are the other benefits of changing from sole trader to limited company?

There can be several benefits to switching from sole trader to a limited company structure, taking into consideration yours and your business's needs. Here are some of the key ones:

1. You're not personally liable if your business makes a loss or if someone makes a claim against it

This means you should have another bank account to keep all your personal finances separate from those of your business. This isn't a legal requirement but it's advised by experts.

Setting up a new account for your newly formed limited company, rather than simply using the one you used when you were a sole trader, will help you avoid any potential nasty tax surprises. You can read our article on [the best business bank accounts](#) to help you get started.

2. Your personal tax is based only on the salary and dividends you draw from your company

As a sole trader you pay tax personally on all the profit you make. It's generally understood that if you earn up to £30,000 you're better off staying as a sole trader. When you start to take in more than that annually, it's probably time to think about whether to incorporate.

3. You can claim tax relief on business expenses that you couldn't as a sole trader

If you're a limited company, you pay [corporation tax](#) on any profits you make – and you need to do this before you take any [dividends](#).

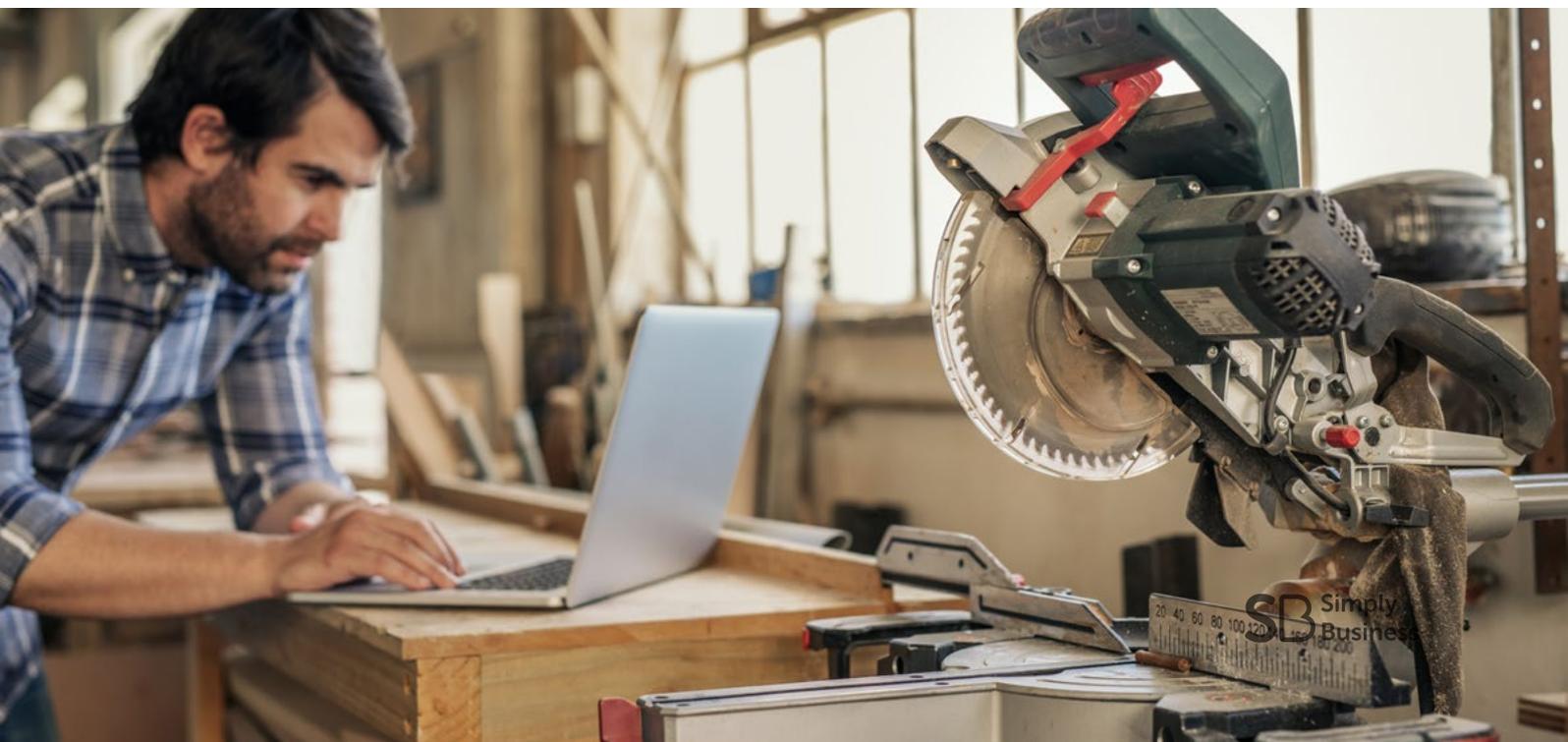
Claiming [expenses](#) reduces the profit you make and, therefore, your tax bill.

4. You can protect your business name

When you become a limited company you register your business name with Companies House. This means no other company can use it. However, it's worth noting that if you use a different trading name that's not registered, another company may use it.

Read more about [intellectual property law for small businesses](#).

Changing from sole trader to limited company can be a tough thing to get your head around on your own, so you may find it's worthwhile chatting it through with an accountant.



Related articles

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