

Social Security contributions and your new business

Requirements for your business

The Social Security Department (SSD) collects social security contributions from everyone so that benefits can be paid. When you are employed these contributions are deducted directly from your salary or wages and paid over by your employer. When you set up your own business this changes and the following sections will explain how this works in the first few years of trading.

Types of contributions

There are two types of contributions:

- Class 1: Paid by everyone working for an employer
- Class 2: Paid by everyone not working for an employer, so people who are self-employed or not working. Class 2 Contributions are calculated at 12.5% of earned income.

You must pay Class 2 contributions if you:

- Are over school leaving age
- Have been resident in Jersey for any continuous period of at least six months
- Do not work for an employer

Simply, everyone not working for an employer is liable to pay Class 2 Contributions. This means if you decide to start a business and become self-employed you will be liable to pay this level of contribution.

Before you start to trade

Creating a benchmark earnings figure

Because the business is brand new it doesn't have any

revenue history and so, in order to calculate how much a new business owner's Class 2 contributions should be once the business has started, Social Security needs to have a 'benchmark' earnings figure to work from.

The benchmark earnings figure is worked out by looking at the individual's previous earnings and he/she will therefore need to provide a copy of the Tax Assessment from 2 years before he/she started the business. The reason for asking to see the Tax assessment from 2 years before is because tax is collected in arrears so a Tax assessment from two years earlier will be the last finalised assessment.

Ways to calculate Class 2 contributions

Everybody must pay the earning related rate of social security contributions. However, it is recognised that when the business starts it might have lower sales than the individual earned before starting up and therefore there are two ways to calculate an appropriate contribution level in the early years.

The two ways to calculate the level of class 2 contributions are:

- Earnings related rate. This is the standard rate at which contributions, **must** be paid and is calculated at 12.5% of the actual earnings in the year
- Deferred rate. This is an annual concession and is calculated at 12.5% of £16,721

Note, the deferred rate is an annual concession that allows new businesses to help manage their cash flow by reducing contributions at the start. The reason, therefore, for a new business to choose to pay a deferred rate is to allow the new business to establish a client base and a steady stream of income whilst still benefiting from full entitlement to benefits and a full pension record for 2017.

However, because Social Security must charge the earnings-related rate for social security contributions, they

will continuously look back to make sure the right level of contributions has been made every year. By reviewing the actual annual earnings made from the start of the business and the level of contribution that has been paid, the department will be able to see if additional contributions are needed to catch up any under payment of social security contributions.

Contributions in the first year of trading

The following scenarios will explain how this works:

Mr A has decided to start a new business in January 2017 therefore his relevant year of tax assessment is 2015.

Earnings of less than £16,721 in 2015

- If Mr A has earned £16,721 or **less** in the relevant year of tax assessment (2015) then his earnings-related rate is 12.5% of his earnings, divided by 12 months.
- So, for example, if Mr A's tax return for 2015 showed he had earned £15,000 then he would pay a monthly contribution rate of £156.25.

Earning of more than £16,721 in 2015

- If Mr A has earned **more** than £16,721 in the relevant year of tax assessment (2015) Mr A. could pay the earnings-related rate but would also be offered the possibility to opt for the Deferred Rate whilst the business builds. The deferred rate is calculated at 12.5% of £16,721 divided by 12 so would be £174.17 per month.
- So, for example If Mr A's tax return for 2015 shows he has earned £40,000
 1. His earnings-related rate would be a monthly contribution of £416.67 for 2017.
 2. But he would still have the option to pay the deferred rate (12.5% of £16,721 divided by 12), therefore his liability becomes £174.17 per month for 2017.

Contributions after the first year of trading

The following scenarios will explain how this works:

Now Social Security will look back at Mr A's Tax assessment for 2017 to see what he actually earned in that year.

- So, if in 2017 (the year Mr A started his business) Mr A actually declared earnings of £50,000 to the tax office:
 1. His earnings-related contributions on £50,000 should have been 12.5% of £50,000 which is £520.83 per month or £6,249.96 for the whole of 2017
 2. But, if he opted to pay the deferred rate in 2017 Mr A already will only have paid $£174.17 \times 12 = £2,090.04$
 3. Therefore, Mr A's remaining liability for 2017 is $£6,249.96 - £2,090.04 = £4,159.92$
 4. This underpayment would be due on demand in 2019 although it might be possible to agree a monthly instalment plan
- If, in 2017 (the year Mr A. started his business) he declared an income of £12,000 to the Tax Office:
 1. His earnings-related contributions on £12,000 should have been 12.5% of £12,000 which is £125.00 per month or £1,500.00 for the whole of 2017
 2. But, if he opted to pay the deferred rate in 2017 Mr A will have paid $£174.17 \times 12 = £2,090.04$
 3. Therefore, Mr A is due a refund for 2017 as $£2,090.04 - £1,500.00 = £590.04$
 4. This would be paid back to Mr A on demand in 2019 and his pension record for 2017 and entitlement to benefit would remain fully accrued after the refund.
- If in 2017 (the year Mr A. started his business) he declared an income of £9,000 to the Tax Offices
 1. This is below £10,176.00 which is the lower earnings limit on which social security contributions are paid

2. But, if Mr A opted to pay the deferred rate in 2017 he would have already paid $\text{£}174.17 \times 12 = \text{£}2,090.04$.
3. Mr A can either get a full refund for $\text{£}2,090.04$ and lose his pensions accruals for 2017, or decide to leave his record as is and keep the benefit of a full pension accrued for 2017.

In subsequent years, this process will be repeated to make sure the right level of contribution is being paid each year.

Key points to remember

- Self-employed people are liable to pay Class 2 Contributions
- Class 2 Contributions are calculated at 12.5% of earned income and are the Earnings-Related Rate
- The Deferred Rate is calculated at 12.5% of $\text{£}16,720$ and is $\text{£}174.17$ a month
- The Deferred Rate option is available to every new business owner
- It is a yearly concession and re-evaluated every year
- It does not allow a business owner to request that any month of liability be waived
- If earnings in the Deferred Rate year are more than $\text{£}16,720$ you will be required to cover any shortfall
- If earnings in the Deferred Rate year are less than $\text{£}16,720$ you can receive a refund on demand
- If you earned below $\text{£}10,176$ you are exempt from paying Class 2 Contributions
- Sometimes there may be unusual or complex circumstances to consider and the [Social Security Department](#) will be happy to meet with you to discuss individual circumstances.

**All rates are as at 1st January 2017 and may be subject to change*

Calculating your earnings

The earnings that you will be assessed on are the earnings you declare on your Income Tax Return.

You can find lots of information about how to calculate your earnings on the [income tax for self-employed website](#).

Download the guide to Social Security Contributions and your new business here

Relevant Links

[Working for yourself tax guidance](#)

[Social Security Department](#)

[Starting up as a sole trader or partnership in Jersey](#)

[Setting up a limited company in Jersey](#)

[Guide to Writing a Business Plan](#)

[Business Plan Template](#)

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