Getting YOUR money out of YOUR company

Without paying 76% tax

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REMUNERATION TAX PLANNING

First point: company profits belong to the company. They aren't yours until you take formal steps to withdraw the cash. The aim of this guide is to outline how to extract money in the most tax-efficient way. You have three main options:

1. Salary
2. Dividends
3. Loans

Each has different tax implications. Paying yourself a large salary (even if you're worth it), will probably just hand the Chancellor a bigger cut.

One way to cut your tax bill is through permitted tax-free benefits or gifts. This route can help you extract value from your company in a non-cash way. We've put together a separate helpsheet covering some of the most popular ones. **Click here** for a copy.

SALARY

If you're employed by your company you'll be entitled to a salary. As the boss, you can decide how much to pay yourself.

Like any other employee you'll have a payslip showing your gross salary (before tax), various deductions for Tax and National Insurance (NI), and then the net amount (after tax), which is paid into your bank account.

You must submit the pay details to HMRC before you pay yourself, and pay any tax or NI to HMRC within three weeks.

Important points:

- You also pay employer's National Insurance contributions on your salary - HMRC gets two bites out of your salary!
- Only employees and directors are entitled to a salary - shareholders cannot receive a salary unless they are also employees.

DIVIDENDS

Retained profits after paying company expenses can be paid out as dividends to shareholders. There's a formal process through which the directors make a written record of their decisions to issue a dividend of £XX per share.

Please let us know if you'd like a copy of our Dividend Minute template.

No tax is deducted at source from dividends, nor is any NI payable. There's nothing to report to HMRC at the time. Each shareholder declares their dividends in their personal tax return where they may, or may not, need to pay Income Tax.

Important points:
A company cannot pay dividends if it has no retained profits. For example, if the company has a loan or overdraft, this cannot be used to pay dividends if it would make the company insolvent, regardless of the cash position. Use your management accounts to determine profitability! Relying on your bank balance alone is a bad idea. Trust us.

LOANS

If you don't want to pay tax on your dividends, why not 'borrow' the cash from the company as a loan, which you'll repay one (unspecified) day? This used to be common practice until HMRC got tired of it.

Now you have 'section 455 tax.' If you borrow money from your company and don't pay it back within 9 months, you'll be stung with a tax charge of 32.5% of the loan value. Ouch!

If you repay the loan, you get your money back. But you have to fight for it.

For most people, 32.5% is their top rate of dividend tax. So we'd almost always advise drawing dividends instead of borrowing. The tax charge will be the same, but dividends don't have to be repaid to the company.

Simple message: don't borrow money from your company unless you've got a really good reason.

WHAT'S THE 'BEST' MIX OF SALARY AND DIVIDENDS?

Ah, yes, the age-old question: what's the most tax-efficient combination of salary and dividends? Helpful hint: don't base your whole tax strategy on the opinion of 'Lisa from Nottingham' on Facebook.

Unless you've got identical tax positions, it's a recipe for disaster. Speak to a Chartered Accountant. Ideally us, of course!

But, whilst you're here, let's go through some of the main differences.

CORPORATION TAX TREATMENT

Wages are a normal business expense for your company. Paying your salary reduces the company's profits and tax bill - dividend payments do not. Paying dividends (or not) won't affect the company's tax position.

INCOME TAX

With a salary, your income will first be taxed at 0% (the best!), followed by 12% (not too bad...), then 32% and finally 42%. Those higher amounts - which kick in if your salary is more than c. £13,000pa - can start to hurt.

Your company ALSO has to pay National Insurance on its staff salaries. Broadly, this is 14% on everything over c. £9,000pa. For some employers there are potential reliefs against this 14% rate - we'll claim this on your behalf if we look after your payroll scheme.

Between you and the company, you'll have seen that the Chancellor might end up with a tax take of 56% (i.e. 42% plus 14%). In other words...the government is enjoying more of your income than you are!

DIVIDEND TAX

Dividend tax starts at 0%, then quickly goes to 7.5%. If you earn more than £50K the rates jump to 32.5% and then 38.1%!

Dividends don't get tax relief in the company. Sometimes it can be better to pay a salary (despite the higher personal tax), because the company is saving some Corporation Tax at the same time.

Oh, and one final thing - if you've had a good year and don't need the cash right now - who's to say you actually have to draw it anyway? Leaving profits in the company is a really tax-efficient idea, especially if the cash would only sit in your bank account (less the taxman's cut) rather than the company's.

WHAT'S THE ANSWER?

Ignore Lisa from Nottingham. There's a different answer for each person. When a new client joins Blue Penguin, we'll have an onboarding session where we provide personalised calculations for each person to consider the optimum mix of salary and dividends.

The savings can be quite significant. Our recent work for a client whose business makes £50,000 a year showed a gap of some £16,000 between taking all the profits as dividends, compared to a carefully tailored mix of dividends and salary.

For a one-person company with no other employees or shareholders, the optimum mix will be something like this:

AMOUNT	TYPE	TAX PAID (Between you and company)	TAX SAVED (By company)
First £9K	Salary	0%	19%
Next £1K	Salary	14%	19%
Next £3K	Salary	26%	19%
Next £2K	Dividends	0%	0%
Next £35K	Dividends	7.5%	0%

This works fine when it's just you and your company. If you have children or a spouse, then things can get really exciting with some legitimate ways for them to receive a share of the company's profits - especially if their own income is lower than yours.

THE COST OF GETTING THIS RIGHT

This helpsheet has been prepared as a general guide to the factors affecting your remuneration strategy. It's not exhaustive, and everyone's circumstances are different.

You don't need an accountant to run a payroll, or to draw some dividends. And you don't need a solicitor to buy a house. But why go it alone when so much is at stake? Please take professional advice from a Chartered Accountant...ideally us!

During your onboarding session we will look at a tailored plan for the family. This is complementary, and regardless of the size of the company or the fees they pay.

Alternatively, if you're not ready to switch accountant but would just like some advice, **book a consultation here.**

It's fair to say that our costs in Getting This Right are significantly lower than the costs in tax and potential penalties of Getting This Wrong.

BOOK A CALL TODAY

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