PLUS OTHER TAX EFFICIENT
PROFIT EXTRACTION STRATEGIES

SALARY VERSUS DIVIDENDS

TAX Cafe®

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Salary versus Dividends

& Other Tax Efficient Profit Extraction Strategies

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and
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Important Legal Notices:

Published by:
Taxcafe UK Limited
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Kirkcaldy KY1 1TL

Email: team@taxcafe.co.uk

ISBN 978-1-911020-97-4

Twenty-fifth edition, Revised November 2024

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About the Authors & Taxcafe

Carl Bayley is the author of over twenty Taxcafe guides designed specifically for the layperson and the non-specialist. Carl's particular speciality is his ability to take the weird, complex, and inexplicable world of taxation and set it out in the kind of clear, straightforward language taxpayers themselves can understand. As he often says himself, "My job is to translate 'tax' into English."

In addition to being a recognised author, Carl has often spoken on taxation on radio and television, including the BBC's It's Your Money programme and the Jeremy Vine Show on Radio 2.

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Nick Braun founded Taxcafe.co.uk in 1999, along with his partner, Aileen Smith. As the driving force behind the company, their aim is to provide affordable plain-English tax information for private individuals and investors, business owners, accountants and other advisers.

Since then Taxcafe has become one of the best-known tax publishers in the UK and has won several business awards.

Nick has been involved in the tax publishing world since 1989 as a writer, editor and publisher. He holds a doctorate in economics from the University of Glasgow, where he was awarded the prestigious William Glen Scholarship and later became a Research Fellow. Prior to that, he graduated with distinction from the University of South Africa, the country's oldest university, earning the highest results in economics in the university's history.

Contents

Introduction

This guide answers one of the most common questions asked by company owners: "What's the best way to take money out of my company if I want to pay less tax?"

In Part 1 we kick off with a plain English guide to how *companies* are taxed.

Corporation Tax rates increased on 1st April 2023. Calculating your company's tax bill also became more complicated. As a result, new tax planning opportunities have arisen.

In Part 1 we also explain how *company owners* are taxed. As a director/shareholder you can choose the best **mix** of salary and dividends. We examine the pros and cons of each type of income.

Company owners can also choose the most tax efficient **level** of income. We will see how, by smoothing your income or varying it significantly from year to year, you may be able to cut your tax bill considerably.

Tax-Free Salaries & Dividends

In Part 2 we reveal how much tax-free salary and dividend income you can withdraw from your company this year. You'll discover how to calculate the 'optimal' tax-efficient salary and how couples in business together can receive £26,140 this year without paying any Income Tax.

In Part 3 we explain how much dividend income you can take taxed at just 8.75% and how to avoid paying tax at 33.75%.

This part of the guide also contains important tax saving strategies for parents who want to avoid the Child Benefit Charge. This now kicks in when your income exceeds £60,000 (previously £50,000) but many company owners will be able to avoid it completely or in part.

There is also important tax planning information for high income earners (those with income over £100,000) and for *really big* earners, who may actually benefit from reversing the strategy that usually benefits everyone else.

Income from Other Sources

In Part 4 we turn to company owners who have income from other sources (e.g. pensions, rental income, interest income, income from another business and stock market dividends).

We explain why you may need to adjust your company salary or dividends to avoid the higher tax rates that kick in when your income reaches certain key thresholds (£50,270, £60,000 and £100,000).

We also examine some tax planning techniques that can be used to reduce or eliminate the tax payable on your income from other sources.

Company owners who are also landlords need to be aware of the restriction to tax relief on mortgage interest. Fortunately, company owners have more flexibility than other landlords when it comes to avoiding some of the worst effects of this additional tax charge.

Company owners can also enjoy much more tax-free interest than most other taxpayers (up to £6,000 per year).

Splitting Income with Family Members

Part 5 explains how company owners can gift shares in the business to their spouses, partners or children and save over £10,000 in tax this year, with similar savings every year.

We also show how additional savings can be achieved by paying tax-free salaries to family members, including your minor children.

There are, however, many traps to avoid when it comes to splitting income with family members and these are fully covered in this part of the guide. For example, we examine the danger of gifting shares that have fewer rights than ordinary shares and the danger of using dividend waivers to divert income to your spouse/partner.

Alternative Profit Extraction Strategies

Part 6 looks at alternative profit extraction strategies:

- **Directors' loans:** How they can be used to reduce or postpone tax.

- **Rent:** Why getting your company to pay you rent is more tax efficient than a dividend in many circumstances.

- **Interest:** How to receive up to £6,000 of tax-free interest from your company.

- **Charity:** Who should donate: you or the company?

- **Pension contributions:** Why they're better than dividends, who should make them (you or the company), plus a chapter on putting property into a pension.

- **Capital gains:** How to pay Capital Gains Tax at a reduced rate when you sell or wind up your company; How to pay 0% tax when you sell your company to an employee ownership trust.

In Part 7 we turn to some of the practical issues and dangers that may be experienced when extracting money from your company:

- How to avoid the minimum wage regulations
- How to make sure your salary is a tax-deductible expense
- Making sure your company has sufficient distributable profits to declare dividends
- How to declare dividends properly and avoid an HMRC challenge
- When HMRC might try to tax your dividends as earnings

Finally, in Part 8, we look at some other tax saving strategies for company owners, including how they may be able to reduce the amount of Capital Gains Tax payable when assets like rental properties are sold.

In this part we also explain how you may be able to completely avoid tax by emigrating.

Using This Guide & Limitations

This tax guide deals primarily with the 2024/25 tax year, starting on 6th April 2024 and finishing on 5th April 2025. Unless expressly stated to the contrary, all references, examples etc, are based on the tax rates, thresholds, and allowances applying for 2024/25.

There are some references to other tax years, for example when discussing the advantages and disadvantages of postponing income to a future tax year. In these cases, we will take account of what we know about the future tax regime, including the increase in employer's National Insurance from 2025/26 onwards.

However, the tax rules that will apply in future years are not known with any degree of certainty: and the further one strays into the future, the more uncertain the position becomes!

The reader must bear in mind that tax laws (and HMRC's interpretation of them) are continually changing.

Please note that, although small company owners are this book's main target audience, this is NOT supposed to be a do-it-yourself (DIY) tax planning guide. Our purpose in writing this guide is to explain in plain English how companies and company owners are taxed and provide some tax planning ideas that can be taken to an accountant or other professional adviser for further discussion.

We do not recommend 'going it alone' when it comes to this type of tax planning and there are several reasons for our cautious approach. Firstly, although the guide covers a fair amount of ground, it does not cover every possible scenario: that would be impossible without making the guide much longer and possibly much more difficult to digest.

In other words, in places we have had to sacrifice definitiveness in favour of making the guide a manageable and hopefully enjoyable read for the average small company owner.

Companies come in many different shapes and sizes, as do their owners, so it is possible the information contained in this guide will not be relevant to your circumstances.

In particular, please note this guide is aimed mainly at UK resident director/shareholders who own and work for UK resident companies.

Secondly, the main focus of this tax guide is *Income Tax* planning: helping company owners pay less tax on their salaries, dividends and other income. There are, however, other taxes that often have to be considered, including Capital Gains Tax (CGT) and Inheritance Tax.

Steps that you take to reduce one type of tax can have an adverse impact on your liability to pay other taxes. While some mention is made of other taxes in this guide, we cannot guarantee that all interactions are covered.

Thirdly, there are potential risks involved when it comes to structuring your affairs to reduce the tax payable on salaries, dividends and other payments made by your company.

While most of the tax planning ideas contained in this book are widely used by many accountants and other professional advisers, and have been for many years, this does not mean they have the blessing of HM Revenue & Customs!

There are some grey areas when it comes to this area of tax planning and some tax savings may not always be guaranteed. In other words, we cannot be certain that some of the tax planning ideas contained in this book will not be subject to some sort of attack from HMRC, even if only at some point in the future.

For example, in the chapters that follow, we will show that the most tax-efficient mix of income for most company owners is a small salary coupled with a larger dividend. While this is a well-established, reasonable form of tax planning which, if carried out correctly, is generally accepted, even if grudgingly, by HMRC, there are circumstances under which they might seek to tax dividends as earnings.

We'll look at this potential threat further in Chapter 42, but it's also worth pointing out that, *at present*, such attacks are rare and generally only occur where aggressive tax avoidance schemes are involved. For the vast majority of small company owners, the danger is remote and lies firmly in the future.

Fourthly, there are also *non-tax* factors that have to be considered when deciding how much money you withdraw from your company and in what form. In some instances, other considerations will outweigh any potential tax savings.

For all of these reasons, it is vital that you obtain professional advice before taking any action based on information contained in this guide. The authors and Taxcafe UK Ltd cannot accept any responsibility for any loss that may arise as a consequence of any action taken, or any decision to refrain from taking action, as a result of reading this guide

Corporation Tax Rates

Much of the planning and analysis in this guide is dependent on the company's Corporation Tax rate. As we will see in Chapter 1, under the new Corporation Tax regime, a company's overall tax rate could be anything between 19% and 25%.

However, it is generally a company's *marginal* Corporation Tax rate that matters for the purposes of this guide, rather than its *overall* tax rate. A company's marginal Corporation Tax rate will be either 19%, 26.5%, or 25%. It is these three rates we will use in our illustrations, examples, etc, throughout most of this guide.

Matching Up Company and Personal Tax Rates

It is *most likely* that a company owner who is a basic rate taxpayer will have a company paying Corporation Tax at 19%, while higher or additional rate taxpayers will have companies paying Corporation Tax at higher rates. We will generally follow these principles for our main examples throughout this guide.

However, we will also cater for the possibility that higher or additional rate taxpayers may have companies paying Corporation Tax at only 19%, while basic rate taxpayers may have a company paying Corporation Tax at a higher rate as, for various reasons, all these combinations are possible.

Scottish Taxpayers

The Scottish Parliament can set the Income Tax rates applying to most types of income received by Scottish taxpayers, but not interest or dividends. The vast majority of the information contained in this guide is relevant to Scottish taxpayers. However, unless stated to the contrary, all examples, tables and calculations assume the individual concerned is not a Scottish taxpayer.

Despite this general assumption, there is a great deal of information in this guide specific to Scottish taxpayers, as we want to include them as much as we can without making the guide too complicated.

It's also worth pointing out that, where a director needs to be a basic rate taxpayer for a particular strategy to work (see Chapters 10 and 11, for example), a Scottish intermediate rate taxpayer can be included. To be a basic or intermediate rate taxpayer for 2024/25, a Scottish taxpayer needs taxable income excluding dividends, interest, and savings income, of no more than £43,662 *and* total taxable income of no more than £50,270.

Spouses and Civil Partners

Under UK tax law, all legally married spouses and registered civil partners are treated the same. Hence, when we refer to a 'spouse' in this guide, it includes a civil partner. For tax purposes, a spouse does not include a common-law partner or co-habitee. Where we are discussing a partner who may either be a legally married spouse or a common-law partner, we will use the term 'spouse/partner'.

Furnished Holiday Letting

At present, for the 2024/25 tax year, furnished holiday letting businesses meeting specific qualifying criteria are treated as trading businesses for the purpose of a number of key tax reliefs, including business asset disposal relief and holdover relief, which we will discuss in Chapters 1, 27, 28, and 36.

Profits from furnished holiday letting are also currently treated as earnings for pension purposes, and mortgage interest and other finance costs can be properly deducted in full.

However, as confirmed in the October 2024 Budget, from April 2025, furnished holiday letting will be treated as an investment activity for all tax purposes, in the same way as other property letting. The key CGT reliefs discussed in Chapters 1, 27, 28, and 36 will generally no longer be available, profits will not be classed as earnings, and mortgage interest and other finance costs will only attract basic rate tax relief in the same was as other residential lettings (as discussed in Chapter 26).

For more information on how to plan for these changes, see the Taxcafe guide *Furnished Holiday Lets: Big Tax Changes Ahead*.

Some Assumptions

Unless stated to the contrary, we will assume throughout this guide that directors and company owners are:

i) UK resident individuals
ii) Not subject to the 'off payroll working' rules (sometimes known as 'IR35': see Chapter 43)
iii) Not subject to the Child Benefit Charge (we will look at this in Chapter 17 however)
iv) Not Scottish taxpayers (see above)
v) Not claiming the marriage allowance (see Chapter 4)
vi) Not subject to the minimum wage rules (see Chapter 38)

We will also assume, again unless stated to the contrary, that companies:

i) Have no associated companies
ii) Are UK resident
iii) Have a twelve-month accounting period
iv) Are not close investment holding companies

The relevance of these assumptions is explained in Chapters 1 to 3.

In this edition, we will also ignore the possibility, which may still exist in a few circumstances, that payments to directors will attract Corporation Tax relief in an accounting period commencing before 1st April 2023. For guidance on this issue, see the previous edition of this guide.

Part 1

How Companies & Company Owners Are Taxed

Chapter 1

How Companies Are Taxed

Companies pay Corporation Tax on their income and capital gains. From 1st April 2023, there are two official tax rates:

- Small profits rate 19%
- Main rate 25%

The practical effect is that companies pay tax as follows:

- **Profits £50,000 or less** – Company continues to pay 19% tax on all its profits

- **Profits between £50,000 and £250,000** – Company pays 19% tax on the first £50,000 and 26.5% on the remainder

- **Profits greater than £250,000** – Company pays 25% tax on all its profits

The new Labour Government has published a *Corporate Tax Roadmap* which states that the main Corporation Tax rate will not be increased, and the small profits rate and relevant thresholds will not change, for the duration of this Parliament. Hence, the above rates are expected to apply until at least 2029/30.

A company with profits of £100,000 will pay 19% on the first £50,000 and 26.5% on the final £50,000. The total tax bill will be £22,750 which means the company will have an overall tax rate of 22.75% (£22,750/£100,000).

A company with profits of £150,000 will pay 19% on the first £50,000 and 26.5% on the remaining £100,000. The total tax bill will be £36,000 which means the company will have an overall tax rate of 24% (£36,000/£150,000).

A company with profits of £20,000 (i.e. less than £50,000) will simply pay £3,800 (19%). A company with profits of £300,000 (i.e. more than £250,000) will simply pay £75,000 (25%).

TABLE 1
Overall Corporation Tax Rates

Profits	Corporation Tax	Corporation Tax Rate
£50,000	£9,500	19.00%
£60,000	£12,150	20.25%
£70,000	£14,800	21.14%
£80,000	£17,450	21.81%
£90,000	£20,100	22.33%
£100,000	£22,750	22.75%
£110,000	£25,400	23.09%
£120,000	£28,050	23.38%
£130,000	£30,700	23.62%
£140,000	£33,350	23.82%
£150,000	£36,000	24.00%
£160,000	£38,650	24.16%
£170,000	£41,300	24.29%
£180,000	£43,950	24.42%
£190,000	£46,600	24.53%
£200,000	£49,250	24.63%
£210,000	£51,900	24.71%
£220,000	£54,550	24.80%
£230,000	£57,200	24.87%
£240,000	£59,850	24.94%
£250,000	£62,500	25.00%

Non-Resident Companies

Only UK resident companies are able to benefit from the 19% small profits rate. A non-resident company that earns rental income from UK properties, for example, has to pay 25% Corporation Tax on all its UK rental profits.

Accounting Periods vs Financial Years

A company's own tax year (also known as its accounting period) can end on any date, for example 31st December, 31st March, etc.

Corporation Tax, on the other hand, is calculated according to financial years. Financial years run from 1st April to 31st March. The 2024 financial year is the year starting on 1st April 2024 and ending on 31st March 2025.

This doesn't matter most of the time, but does when Corporation Tax rates change. For example, on 1st April 2023, the main rate of Corporation Tax increased from 19% to 25%. A company with profits of more than £250,000 whose accounting period ran from 1st January 2023 to 31st December 2023 will therefore have been liable for Corporation Tax as follows:

- 3 months to 31st March 2023 19%
- 9 months to 31st December 2023 25%

The company will therefore pay 19% Corporation Tax on roughly one quarter of its profits (3/12) and 25% tax on roughly three quarters of its profits (9/12). (It doesn't generally matter at what point during the year the profits are actually made.)

This means the company's overall Corporation Tax rate for this year will be 23.5%. (In practice, Corporation Tax is calculated using days not months and this will result in a small difference.)

Because the Corporation Tax increase is now in full force, the above calculations are no longer necessary for current accounting periods. For example, the above company will simply pay 25% Corporation Tax on all its profits for the accounting period running from 1st January 2024 to 31st December 2024.

However, if Corporation Tax rates change again in the future, these split-year calculations will become relevant once more.

Marginal Tax Rate Planning

The Corporation Tax increase means many companies are paying more tax on their profits. The good news is many companies are also enjoying more Corporation Tax relief on their spending.

Before the increase companies enjoyed 19% Corporation Tax relief no matter how much profit they made or when they spent their money. A company incurring an additional £1,000 of tax-deductible spending would reduce its taxable profits by £1,000, saving it £190 in Corporation Tax.

The Corporation Tax increase means the amount of tax relief a company enjoys now depends on its profits. The position is as follows:

- A company with profits of £50,000 or less has a marginal tax rate of 19% and continues to enjoy 19% tax relief on its spending.

- A company with profits of between £50,000 and £250,000 has a marginal tax rate of 26.5% and enjoys 26.5% tax relief on its spending. (However, if the company's spending pushes its profits below £50,000 it will start to receive just 19% tax relief on any additional spending.)

- A company with profits of more than £250,000 has a marginal tax rate of 25% and enjoys 25% tax relief on its spending. (However, if the company's spending pushes its profits below £250,000 it will start to receive 26.5% tax relief on any additional spending.)

In Table 1 we listed the new *overall* tax rates companies face. For example, a company that makes a profit of £100,000 has an overall tax rate of 22.75%.

However, this overall rate is NOT used for most tax planning purposes, for example calculating the amount of tax a company will save if it spends some more money. Instead it is the company's marginal tax rate.

This makes sense when you consider a simple example. A company that anticipates making a profit of £100,000 and incurs an additional £10,000 of tax-deductible expenditure will reduce its taxable profits by £10,000. This will reduce its tax bill by £2,650 (26.5%). The company's overall tax rate of 22.75% does not tell us how much tax the company will save.

The Marginal Tax Rate Bands

Companies now effectively have three marginal tax rate bands:

Profits up to £50,000	19%
Profits between £50,000 and £250,000	26.5%
Profits over £250,000	25%

These bands apply in the majority of cases, but can be affected by factors such as whether the company has any associated companies (see Chapter 2). They are an important concept in tax planning for companies, so watch out for references to the company's 'marginal tax rate band' later in this guide: it is these bands we are referring to.

(A director also has his or her own marginal tax rate band for Income Tax purposes. We'll get onto those later but, for now, it's important to emphasise that the ***director's*** marginal rate band and the ***company's*** marginal rate band are different things: although both of them are critically important.)

Should My Company Postpone or Accelerate Spending?

Where a company's profit level changes from one year to the next, it may be able to save more Corporation Tax by postponing or accelerating some of its spending. For example, a company with profits not exceeding £50,000 in the current year will be taxed at 19% but, if it expects to make profits between £50,000 and £250,000 next year, its marginal tax rate will increase to 26.5%.

A company expecting this sort of increase in its marginal tax rate would enjoy an additional 7.5 percentage points of tax relief on spending it can postpone, saving £750 for every £10,000 postponed.

In other cases, where the company expects its marginal tax rate to *decrease* next year, accelerating expenditure could produce similar savings.

But not all types of expenditure are suitable to be postponed or accelerated. Furthermore, in many cases, the timing of the tax relief is not dependent on the date the money is spent. For more information on this type of planning, which can yield almost 40% greater tax savings on deductible expenditure, see the Taxcafe guide *Putting it Through the Company*. Naturally, the commercial implications of postponing or accelerating business expenditure always need to be considered.

As far as most of the issues covered in this guide are concerned, it is generally the *director's* marginal tax rate that is far more important as this can vary by a great deal more.

Nonetheless, there are exceptions where the company's marginal tax rate alone is the key factor in determining the optimal time for it to spend money: pension contributions on the director's behalf are a prime example (see Chapter 33).

Tax Relief on Salaries etc

If your company pays you a salary, rent, interest, or makes pension contributions on your behalf, these are generally tax-deductible expenses for the company.

As we shall see in the chapters that follow, when deciding how much salary or other income to pay yourself, the amount of Corporation Tax relief your company receives on these payments is an important factor.

If your company's marginal Corporation Tax rate doesn't change, the amount of tax relief it gets is clear. Assuming the payment does not itself alter the company's marginal Corporation Tax rate, it will provide relief at 19%, 26.5%, or 25%.

In the vast majority of cases, it's as simple as that, and you can safely ignore the rest of this chapter.

In fact, we're going to ignore it for the majority of the guide ourselves and, unless stated to the contrary, will assume the company obtains Corporation Tax relief at 19%, 26.5%, or 25% on all its tax-deductible expenses, including payments made to, or on behalf of, directors.

Example: *Angela takes a salary of £12,570 out of her company, which makes an annual profit of around £80,000 and thus has a marginal Corporation Tax rate of 26.5%. Her salary produces a Corporation Tax saving of £3,331 (£12,570 x 26.5%).*

One quirk to watch out for though, is that the expense itself can sometimes lead to the company's profits dropping into a different marginal tax rate band.

Example: *Belinda also takes a salary of £12,570 out of her company, but its annual profit before paying her salary is just £60,000. The Corporation Tax saving produced by Belinda's salary is thus:*

£10,000 @ 26.5%	*£2,650*
£2,570 @ 19%	*£488*
Total	*£3,138*

For the sake of illustration, we've ignored employer's National Insurance in these simple examples, but we will, of course look at that later in the guide, as well as examining whether £12,570 was the best salary for these directors to take.

Changing Marginal Corporation Tax Rates

Things can get a little more complicated when a company's marginal Corporation Tax rate changes during the course of the *Income Tax* year.

Where the company's marginal Corporation Tax rate changes from one accounting period to the next, the exact amount of tax relief it will enjoy in respect of payments made during the *Income Tax* year will depend on its accounting date and profit level, on whether the payments are made monthly, annually, or as a 'one off', and on how the payment is recognised in the accounts.

Companies must operate the accruals basis of accounting, which means any periodic cost must be spread over the period to which it relates. For example, a company with a 31st December accounting date may make a single annual rental payment of £20,000 to its owner/director, who owns the company's trading premises personally. Whenever the payment is made, the director (who we will assume, for the time being, is not using the cash basis) will have taxable rental income of £20,000 for 2024/25.

But the payment that suffers Income Tax in the director's hands in 2024/25 will need to be recognised on a time apportionment basis in the company's accounts. Hence £15,000 (9/12ths) of the rent will fall into the company's accounting period ending 31st December 2024 and attract Corporation Tax relief at its marginal rate for that year; and £5,000 (3/12ths) will fall into the accounting period ending 31st December 2025 and attract Corporation Tax relief at its marginal rate for that year.

Let's say the company's profits turn out to be £200,000 for 2024 and £300,000 for 2025. Hence, it will have a marginal Corporation Tax rate of 26.5% for the year ending 31st December 2024, and 25% for the year ending 31st December 2025. The Corporation Tax relief for the rent on which the director pays Income Tax in 2024/25 will therefore be:

£15,000 @ 26.5%	£3,975
£5,000 @ 25%	£1,250
Total	£5,225

The overall effective rate of relief is thus 26.125%.

The director will pay Income Tax on £20,000 of rental income in 2024/25; the company will enjoy Corporation Tax relief of £5,225.

Where something is a periodic cost, it's important to appreciate that, for Corporation Tax purposes, it is generally spread over the period to which it relates, regardless of when it is actually paid. Hence, the rent payment above would attract the same amount of Corporation Tax relief, and in the same accounting periods, even if it was not paid until after 5th April 2025.

There are some exceptions to this rule, however. Companies cannot claim Corporation Tax relief on:

- Salaries or bonuses that are still unpaid nine months after the end of the accounting period
- Interest charged by the company's owner that is still unpaid twelve months after the end of the accounting period

In these cases, relief can only be claimed when payment is actually made: credits made to the director's loan account count as payment though.

On the other side of the equation, directors are generally only taxed on payments from their company when they receive them (again, a credit to the director's loan account counts as receipt).

This applies to salary, bonuses, and interest paid to the director (as well as dividends, although these do not attract Corporation Tax relief). The only potential exception is rent, where the position depends on whether the director is taxed on their property income under the cash basis, or under traditional accruals basis accounting (see the Taxcafe guide *How to Save Property Tax* for detailed explanations of both methods and when they are available).

So, where does all this leave us with the effective rate of Corporation Tax relief for payments made to, or on behalf of, directors in 2024/25?

Generally, if something is paid monthly, it will be a periodic cost. Some things are always a periodic cost, even if paid annually.

Rent and interest are always periodic costs and thus will generally attract Corporation Tax relief at the rates for the relevant accounting period or periods, as in our example above.

Salaries and pension contributions paid monthly will usually also be periodic costs, attracting Corporation Tax relief at the rates for the relevant accounting period or periods.

Salaries, bonuses and pension contributions paid annually or as a one-off may not be periodic costs, but this depends on the circumstances. The position for salaries is discussed further below, pension contributions are discussed in Chapter 33.

Where payments are not periodic costs, they will generally attract Corporation Tax relief at the company's marginal rate for the accounting period in which they are paid: although, as we shall see later, there are exceptions to this.

Salaries in the Current 2024/25 Tax Year

The current tax year for *individuals* runs from 6th April 2024 to 5th April 2025. For most companies, whose marginal tax rate does not change, it will be simple to calculate the Corporation Tax relief on salaries and other regular payments made to directors: generally 19%, 26.5%, or 25%. Where the company's marginal Corporation Tax rate changes during the 2024/25 Income Tax year, the calculation becomes more complex.

Example: *Average Company Ltd has an accounting period that runs from January to December. It makes monthly salary payments to the directors. For the accounting period ending 31st December 2024, the company makes a profit of just £50,000 and hence will enjoy Corporation Tax relief at just 19% on the salary payments it makes.*

For the accounting period ending 31st December 2025, the company makes a profit of £100,000, and hence will enjoy 26.5% Corporation Tax relief on any additional salary payments.

The 2024/25 tax year falls into both of these years, so the company will enjoy the following tax relief on its salary payments:

April to December 2024	*9/12 x 19%*	*14.250%*
January to March 2025	*3/12 x 26.5%*	*6.625%*
Total Corporation Tax relief		*20.875%*

The company will enjoy a total of 20.875% Corporation Tax relief on salary payments made during the current 2024/25 tax year.

Note this assumes the payment of the salary does not itself alter the company's marginal Corporation Tax rate for either accounting period.

The outcome may be different where the director's salary is paid in a single annual lump sum, rather than monthly.

Example: *Annpay Ltd has an accounting period that runs from January to December. In the year ending 31st December 2024, it makes a profit of just £50,000, but in the year ending 31st December 2025, its profits increase to £100,000.*

The company's director, Anne, takes her salary in a single lump sum in March each year. The salary she takes in March 2025 is accounted for as an expense in the company's accounts for the year ending 31st December 2025 and will thus provide Corporation Tax relief at 26.5%.

If we compare the results in the last two examples, we can see that a single lump sum payment (as for Annpay Ltd) may produce a different overall rate of tax relief to regular monthly payments:

Average Company Ltd (monthly pay):	Relief at 20.875% on average
Annpay Ltd (lump sum):	Relief at 26.5%

In both cases, we are talking about salary falling into the same *Income Tax* year: 2024/25.

However, such single annual lump sum payments are not always accounted for as an expense of the company accounting period in which they are paid.

It would have been equally acceptable for Annpay Ltd to have accrued part of the cost of the salary paid to Anne in March 2025 as an expense of its accounting period ending 31st December 2024, with the remainder treated as an expense of the accounting period ending 31st December 2025. The split would be done on a time apportionment basis, with the end result being that the Corporation Tax relief for Anne's salary would be the same as for the monthly payments made by Average Company Ltd.

The proper accounting treatment of a lump sum payment like this is really a question of whether Anne's lump sum salary paid in March 2025 is seen as a reward for her efforts as company director over the period from April 2024 to March 2025, or as a bonus paid in recognition of her continuing service to the company.

In many cases, the decision on how to treat the director's annual lump sum salary in the company's accounts will have been made some years ago. If so, it could be difficult to argue for a different treatment this year just because the company's marginal Corporation Tax rate is changing.

There is, however, a way to control the timing of relief for a director's salary (when paid as a lump sum), which may be beneficial where the company's marginal Corporation Tax rate fluctuates from one accounting period to the next.

Securing Optimal Corporation Tax Relief for a Director's Salary or Bonus

For tax purposes, a director's bonus is effectively the same as a lump sum salary payment. For the purposes of this technique, it is better to refer to it as a bonus, however.

It is possible to secure Corporation Tax relief for a director's bonus in an accounting period that has already ended before the director is paid (or deemed to be paid: see Chapter 4).

The first step is to hold a directors' board meeting before the end of the old accounting period and minute the fact that the directors have agreed to pay themselves a bonus in respect of their performance during that accounting period. The amount of the bonus is not specified at this time (as we will see in Chapter 4, this could trigger an immediate Income Tax liability, which the company would have to put through the payroll and pay via the PAYE system).

However, while no Income Tax liability or payroll reporting obligation under PAYE has been created yet, the company now has a commitment to pay the bonus in respect of that accounting period.

As long as the director is then paid (or deemed to be paid: see Chapter 4) within nine months after the accounting date, the company can accrue the cost in its accounts and secure Corporation Tax relief in the earlier period.

Let's say, for example, a director's optimal salary (or bonus) for 2024/25 is £12,570 and they plan to take this as a single lump sum in March 2025. The company has a 31st December accounting date and usually makes profits somewhere between £45,000 and £75,000 before taking account of the director's salary.

Once the company's profits for the year ending 31st December 2024 are known, it can decide how much bonus to pay. In the scenarios that follow, 'profit' means the company's profit before taking account of the director's bonus or salary (for 2024/25). We'll also ignore employer's National Insurance for the sake of illustration.

Scenario 1: The company's profit for the year ending 31st December 2024 turns out to be £50,000 or less. The company pays a bonus of £1 to honour its commitment in respect of that accounting period. A further £12,569 can then be paid, as a separate, routine lump sum salary payment, later (but by 5th April 2025) and this will obtain Corporation Tax relief in the year ending 31st December 2025, possibly at 26.5%.

Scenario 2: The company's profit for the year ending 31st December 2024 is between £50,001 and £62,569. The company pays a bonus equal to the amount of profit in excess of £50,000, thus obtaining Corporation Tax relief at 26.5% on this amount. A further sum to bring the director's total salary and bonus (combined) for 2024/25 up to £12,570 can then be paid, as a separate, routine lump sum salary payment, later (but by 5th April 2025), which will obtain Corporation Tax relief in the year ending 31st December 2025, possibly also at 26.5%.

Scenario 3: The company's profit for the year ending 31st December 2024 is £62,570 or more. The company pays a bonus of £12,570 and obtains Corporation Tax relief at 26.5%.

Again, all these actions should be minuted as part of a directors' board meeting: this technique requires formality to succeed!

Under scenarios 1 and 2, the company could, instead, choose to go ahead and pay the full bonus of £12,570. This would mean some or all of the bonus only attracts Corporation Tax relief at 19% but, if the company is not confident of making profits in excess of £50,000 in the year ending 31st December 2025, it may be better to get Corporation Tax relief in the earlier period as at least this provides a cashflow benefit.

Under scenario 3, there may be instances where a salary of more than £12,570 becomes optimal for the director (we'll see these later in the guide). This technique can again be used to pay the optimal salary by way of a bonus.

The technique can also be used to fix the director's salary at the optimal level in other scenarios, such as when following the large salary strategy covered in Chapter 21.

Salary versus Bonus

Many directors prefer the simplicity and certainty of a regular monthly salary. However, as we have seen, when it comes to maximising Corporation Tax relief, it will often be better to take an annual lump sum as a bonus. But it's up to you!

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