Finton Doyle
CHARTERED ACCOUNTANTS
Strength in Numbers
A Xeinadin Company

HOW TO PAY YOURSELF AS A COMPANY DIRECTOR

If you run your business through a limited company you have two roles – one as the owner or *shareholder* of the company and one as the manager or *director*. On a day-to-day basis the roles are one and the same, but when it comes to company law they are completely different, and this is what counts when it comes to paying yourself.

Shareholder

Owning a share or shares in a company gives you certain rights. Most shares are called *ordinary shares* and these give the owner rights to:

1. Control what happens to the company – in theory this is done through voting at a shareholders' meeting, but if you own all of the shares then you own all the votes
2. Profits earned by the company – these are paid out to the owners as *dividends*
3. Profits from selling your shareholding – just the same as any other asset, such as a house or car

Director

As a director of a company your role is to run the company for the benefit of the shareholders (often the same people). In this way you are an *employee* of the company, and as an employee you are paid a salary or wages under PAYE.

Which is Better?

Because you have this dual role you can decide whether you pay yourself dividends or salary, depending on your circumstances. But which is better? In most cases the answer is 'a bit of both'. Here's why:

Example 1

Company profit before tax	40,000
Corporation tax @ 19 %	(7,600)
Profit after tax	32,400

The profit after tax can be paid as a dividend. If the taxpayer has no other income they will pay tax on the dividend as follows:

Dividend	32,400
Less: Personal allowance	(12,570)
Taxable income	19,830

First £2,000 taxed @ 0%, balance @ 7.5%, income tax payable £1,337.25.

Total tax payable £7,600 + £1,391.25 = £8,937.25

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Example 2

Company profit before tax	40,000
Salary paid to director	(8,800)
Corporation tax @ 19 %	(5,928)
Profit after tax	25,272

Again, the profit after tax can be paid as a dividend and the tax computation will be:

Dividend	25,272	
Less: Personal allowance	(3,770)	- after allowing for salary
Taxable income	21,502	

First £2,000 taxed @ 0%, balance @ 7.5%, income tax payable £1,505.25.

Total tax payable £5,928 + 1,462.65.25 = £7,390.65 saving £1,546.60

Salaries paid at more than £736 per month start to become more expensive because of National Insurance contributions. These can add another 25.8% to the tax bill.

Practical Points

1. Salaries paid at more than £520 per month have to be paid through a payroll scheme and reported to HMRC when the payments are made (this system is known as Real Time Information, or RTI).
2. Even though there's no NI payable on a salary of up to £736 per month, HMRC will make the contributions on your behalf. This means that you don't lose out for state pension and other earnings-related benefits.
3. Dividends can only be paid from profits after tax. It's important to make sure that the company always has enough cash in the bank to pay its corporation tax bill. This can be done by transferring a regular amount into a savings account in the company name before dividends are paid.
4. You don't have to wait until the year end accounts are done to pay yourself. As a director you can 'borrow' money from the company and then when the accounts are finalised a dividend can be officially 'paid' to you as a shareholder – but in most cases you've already had the cash in advance. The dividend is often just a paper exercise to straighten out the books.
5. Don't forget that there's personal tax to pay on the dividends as well as corporation tax on the profits.
6. The company always pays its tax bill nine months after the year end. Personal tax is paid in January (and sometimes July as well) under self assessment.