2024/25

TAX TIPS FOR COMPANY DIRECTORS

Jennifer Adams

tax insider
BUSINESS

Contents

‘Tax Tips For Company Directors’ – First published June 2016; second edition August 2017; third edition June 2018; fourth edition July 2019; fifth edition July 2020, sixth edition July 2021; seventh edition July 2022; eighth edition July 2023; ninth edition July 2024.

About Jennifer Adams

Jennifer Adams FCG TEP ATT (Fellow) has been a professional business author for over 15 years, specialising in corporate governance and taxation. She is also the proprietor of her own accountancy firm and, as such, is well placed to advise on tax problems that companies and their directors may face.

Jennifer has been a regular contributor to Tax Insider, Business Tax Insider and Property Tax Insider, is the author of the book titled '101 Property Tax Tips' and of the following Tax Insider guides:

- How To Use Trusts To Reduce Property Taxes
- Investing In Property – Personal Or Company Ownership

About this guide

This special guide has been written with the director of the small or medium-sized company in mind.

It looks at possible tax planning strategies for such directors at each stage of a company's life, from incorporation through to cessation when either the director leaves or the company closes.

Note that this guide is aimed at tax planning for private limited company directors only.

1 The beginning – Incorporation

When a limited company is formed, a new entity is created. Legally, this entity is separate from all other individuals, including the owners (shareholders), who may or may not be the same people as those who manage the company (directors).

It is invariably the case that a sole trader or partnership commences in business, and the business grows such that the matter of incorporation needs to be considered. Although the decision to incorporate should be for commercial reasons rather than tax savings, any tax savings that may result need to be factored into the decision.

There are tax costs relevant to incorporation that need to be taken into account when making the decision, not least capital gains tax (CGT) and possibly stamp duty land tax (SDLT) (land and buildings transaction tax in Scotland; land transaction tax in Wales) should property be transferred to the company. Although various CGT reliefs are available to reduce or defer chargeable gains made on incorporation (see sections 1.2 to 1.5), no such reliefs are available for the SDLT charge.

In addition, as well as deductions for income tax and employees' National Insurance contributions (NICs) through PAYE, an employer must also pay employer's NICs and (usually) pension contributions.

1.1. Incorporate or not?

Note: this section refers to the tax rates in England, which differ from the Scottish and Welsh tax rates.

Whether incorporation results in tax savings overall depends on a number of factors, not least the amount of salary and dividends the director-shareholder withdraws from the company. As ever, calculations will prove whether incorporation will be of benefit.

Calculations – Points to consider

- **Corporation tax rates 2024/25**

For 2024/25, the amount of corporation tax relief will depend on the corporation tax rate.

The rates of corporation tax for the year 2024/25 are as follows:

- Profits over £250,000 – the main rate of 25% applies.
- Profits of £50,000 or less – the small profits rate of 19% applies.
- Profits between these thresholds are taxed at the main rate of 25% subject to the marginal small companies relief (MSCR).

MSCR tapers the effect of the increased rate using the calculation:

(Upper limit – profits) x basic profits/profits x MSCR fraction where:

- upper limit is £250,000;
- basic profits are the company's trading profits or gains;
- profits are basic profits plus dividends from other companies; *and*
- MSCR fraction is 3/200.

Therefore, where there are no dividends from other companies, the marginal rate will be:

Profit band	Marginal rate
£0–£50,000	19%
£50,001–£249,999	26.5%
£250,000+	25%

The effective corporation tax rates at various profit levels will be:

Profits	£50,000	£75,000	£100,000	£150,000	£200,000	£250,000
Effective CT %	19%	21.5%	22.75%	24%	24.63%	25%

These increases in corporation tax rates will mean that tax-related reasons for incorporation are being further eroded, leaving issues such as image, separation and limited liability more prominent in decisions.

- **'Optimal' salary amount**

Those directors not subject to employment contracts are not 'workers' according to the National Minimum Wage legislation, so they are not restricted on the amount of salary they can withdraw, irrespective of the hours worked. The 'optimal' salary is the amount directors can withdraw tax efficiently from the company, taking into account the employee's tax bill and NIC both individually as an employee and for the company as the employer. The amount may also depend upon whether the employment allowance (EA) is available.

- **Impact of the employment allowance**

EA of up to £5,000 is available for those companies with more than one employee who are not directors of the company, capped at the employer's secondary NIC amount for the year where this is less. It is not given automatically and must be claimed. Companies with only one director and no other employees cannot claim EA. For 2024/25, the optimum salary whether EA is claimable or not is £12,570 (see below).

- **Interaction of NICs and employment allowance**

For 2024/25, the personal allowance is set at £12,570, as is the employee's primary threshold for NIC. The employer's secondary threshold for NIC is £9,100. Therefore, any director can withdraw an amount up to the secondary threshold of £9,100 (whether EA is available or not) without incurring tax or NIC charges for either the employee or employer. Any additional withdrawals can be taken as dividends which do not attract NIC.

Although NIC is not payable by the employee up to the primary threshold (PT) amount, if the EA is not available, the employer is liable for NIC on the amount greater than £9,100 (i.e., (£12,570 – £9,100) x 13.8% = £478.86). However, corporation tax relief is available on the whole amount such that by paying an 'optimal' salary of £12,570, the corporation tax deduction outweighs the amount of NIC due by as much as £867.50 per employee, as shown below:

Salary £12,570

Assuming corporation tax rate of 25%

- **EA not available**

Employer's NIC payment = £478.86

Corporation tax relief = £987.22 ((£12,570 – £9,100 + £478.86) x 25%)

Balance of additional tax relief over NIC payable £987.22 – £478.86 = £508.36

- **EA available**

Employer's NIC payment = £478.86

However, the employer's NIC element is cancelled out by the EA claim.

By taking a £12,570 salary, the company saves £867.50 in additional corporation tax compared with the £9,100 salary level (per employee).

Therefore, £12,570 is the most tax-efficient director's salary for the 2024/25 tax year whether or not EA can be claimed.

Practical tip

Assuming this extra saving is to be paid out as a dividend taxed at 8.75%, this reduces the tax saving to £464 overall where the director is a basic rate taxpayer, £337 for a higher rate taxpayer (33.75%) and £308 for an additional rate taxpayer (39.35%). Also, whereas the NIC payments are payable throughout the tax year, the corporation tax saving is not obtained until nine months and one day after the year end; this effectively reduces the benefit of the overall saving even further.

Despite any potential tax saving, many companies find that the practicalities and administration required in setting up a payroll scheme, making monthly or quarterly employer's NIC payments and then having to wait to claim the corporation tax relief is not worth the tax relief obtained. Instead, a salary equal to the NIC secondary threshold amount of £9,100 is taken so that no employee or employer's NIC is payable but with the year still counting towards state benefits.

To incorporate or not to incorporate 2024/25?

The table below compares take-home pay between continuing as a sole trader and incorporation for the tax year 2024/25. Note that the table is intended as a basic guide only.