Broadcast

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FACTSHEET: SMALL COMPANY DIVIDEND STRATEGIES

SPECIAL ISSUE

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As the end of the tax year approaches, small company directors and shareholders should take proactive steps to minimise their tax liabilities on dividend payments. Careful planning is essential to ensure that dividends are taken in the most efficient manner.

Tax-free dividend allowance

The dividend allowance was reduced to just £500 from April 2024, down from the previous £1,000 in 2023/24. This means that only the first £500 of dividend income will be tax-free, with the remainder taxed at the standard dividend tax rates. These rates remain unchanged at 8.75% for basic rate taxpayers, 33.75% for higher rate taxpayers, and 39.35% for additional rate taxpayers. This reduction in the dividend allowance makes it even more important to consider alternative tax-efficient strategies.

The impact of income tax bands

A key consideration is ensuring that total income remains within the most beneficial tax bands. The basic rate band extends up to £50,270, and dividends taken within this band will be taxed at the lowest rate of 8.75%. However, exceeding this threshold will push dividend income into the higher rate of 33.75%, significantly increasing the tax burden. Moreover, for individuals earning over £100,000, the personal allowance of £12,570 is gradually withdrawn, resulting in an effective marginal tax rate of 60% between £100,000 and £125,140. Careful dividend planning can help avoid this highly taxed income band

Timing of dividend payments

Dividends should also be timed strategically. Because dividends are taxed in the year they are paid, company directors have flexibility over when they declare and withdraw them. If a higher income is expected in the following tax year, it may be wise to take dividends before 5 April 2025 to use the lower rates while available. On the other hand, if a lower-income year is anticipated, deferring dividends may be beneficial.

Dividends or salary?

Balancing dividends with salary is another crucial aspect of tax-efficient planning. A common strategy is for directors to take a low salary up to the National Insurance threshold, which for 2024/25 remains at £12,570, and supplement income with dividends. This ensures that the personal allowance is used while minimising National Insurance contributions. For those wanting to extract additional funds from their company, employer pension contributions offer a tax-efficient alternative, as these are deductible for corporation tax purposes and not subject to income tax or National Insurance.

Avoiding directors' loan tax charge

Company directors should also be mindful of their Director's Loan Account. If money has been borrowed from the company, it must be repaid within nine months of the company's year-end to avoid a 32.5% Section 455 tax charge. Alternatively, if the company owes the director money, repaying loans instead of taking dividends can be a tax-free way to extract funds.

Making use of spouse's lower tax rates

Another key tax-saving strategy is to possibly make use of a spouse's tax allowances. If a spouse has a lower income or unused personal allowance, it may be possible to pay dividends through separate shareholdings (e.g., alphabet shares). This may reduce the family's overall tax liability by shifting income into a lower tax band.

Set up an initial planning session now

Every company is subject to its own set of circumstances that will determine planning options for 2024-25. While there is still time to act, please call so we can review your dividends v salary options before the end of the current tax year.

Call us on **01753 888 211** or email **info@nhllp.com** to discuss how these changes will impact your business.