

## Should contractors with limited companies take salaries?

With the [pressure](#) coming from HM Treasury on [managed service](#) and [composite companies](#), many contractors are today investigating working with their own limited company incorporation.

If you are outside [IR35](#) — and this is the crucial factor, for if you are caught by it, you have no choice but to use the PAYE system — as the director of a limited company, you have the right to divide your contractor income between salary and [dividends](#). Your salary would necessarily be taxed for National Insurance and income just as any other full-time employees' salary would be.

But you need to decide [how much to pay yourself as Director](#) and whether to keep the salary very low, and to take most of your income in dividends, or to make it higher.

"The short answer is: yes, you should take at least some salary, although there is no legal requirement to do so," says Michael Moore, of the accounting and consulting firm [Deloitte & Touche](#) in London.

As Moore points out, if a contractor, working for a single contractee or agency, takes absolutely no salary he is quite likely to attract the attention of the Revenue.

"It's not so much a question of whether you make the salary very high, or very low, as it is whether or not you are securely outside IR35," adds Dominic Haslam, Deloitte senior manager, Tax. "However, taking a high salary may not prevent you from inviting questions."

"The result is that, if you are outside IR35, then you can take as much or as little in salary as you want, but you should review the matter with a professional," Moore adds.

[Dividend income is taxed](#) a lower rate than salaries, and is not subject to national insurance contributions. But certainly almost any contractor will want to ensure that his National Insurance contribution is covered, and may wish to cover a spouse by making that spouse an employee (although this can also attract the attention of the revenue as we've seen in the Arctic Systems [Section 660a](#) case to be judged by the House of Lords in March).

"Do ensure that you take at least the minimum wage," Moore reminds us.

According to the [Department of Trade and Industry](#), the main (adult) national minimum wage rate applies to workers aged 22 and over and is currently £5.35 per hour. The national minimum wage development rate is currently £4.45 an hour. This rate applies to 18 to 21-year-olds but may also apply to workers aged 22 and over during the first six months in new employment, who are receiving accredited training. For the training to apply there must be a written agreement between the worker and the employer, specifying that the worker will attend training on at least 26 days during the first six months of employment. (There is a further low rate for those under 20, but most contractors won't be dealing with that one).

Contractors at the high end of the salary scale will find that taking salary offers another advantage, as it enables flexibility with pension scheme payments. Since tax has already been paid on salary, it can be added to [tax-free pension schemes](#) without difficulty — although the amounts of pensions contributions are also under scrutiny currently as the "[Pension Simplification](#)" legislation is clarified.

**Published: Tuesday, February 13, 2007**

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