

Financial year-end checklist for contractor limited companies

[Limited company contractors](#) have a range of tax efficient advantages as a result of being incorporated. However, they need to be on the ball to take full advantage of their allowances before the financial year ends.

Contractors can benefit from a number of allowances, and for those contractors with a spouse there are additional and legitimate tax advantages that enable them to manage their tax affairs to their maximum benefit.

And in cases where forecast tax payments are likely to be reduced, perhaps as a result of lower earnings or because of enhanced use of allowances, then there could be a strong case for a contractor to pay less to the taxman 'on account'.

Contractor dividends - now or in future?

Assuming the contractor's [limited company](#) is forecast to make a profit, the end of a financial year is always a key time to make decisions about [dividends](#). Contractors have a number of choices, which can be affected if they have a [spouse who is also a shareholder](#) in the business.

In essence, contractors need to decide whether they:

- o Should raise an additional dividend at year-end because they and their spouse have not earned enough to fall into the higher rate tax band
- o Should defer a dividend payment because they have already earned enough in the year to fall into the higher rate tax band, but might not earn so much in the following tax year.

Any decision about dividends should be taken by considering what the companies profit position at the end of the financial year is likely to be. Dividends can be taken at any time during the year, but by year end the numbers must add up such that all dividends taken were distributed from profits. And of course all [dividend paperwork](#) must be completed for any declared dividends.

To assist with making these decisions, contractors should either have software that enables them to produce regular and accurate management accounting reports, or they should be in regular touch with their accountant.

Directors' loan accounts

Contractors who have chosen not to take all the salary or dividend owed to them by their company will have a [director's loan account](#) in credit to them. Similarly, if a contractor has taken more cash from the business than its profits allow, then the contractor owes money to the business and has an 'overdrawn' director's loan account.

Technically, an overdrawn loan account, where the contractor has taken more cash out of the company than they are owed, is illegal according to the [Companies Act 2006](#). But for most contractor limited companies it is the tax liabilities that are potentially the biggest sanction.

“ Any decision about dividends should be taken once a contractor knows their profit position at the end of the financial year, because a company cannot declare a dividend unless it has made a profit. ”

The maximum a contractor who is a director of their limited company can take out of the business before incurring any tax liabilities is £5,000. If the debit balance of the loan is greater, the loan is classed as a benefit in kind and has to be reported on the contractor's P11D, unless the company charges interest.

The bottom line is that contractors should endeavour to clear any outstanding directors' loan balance at the end of the financial year to avoid any complications, especially as these complications might result in a 25% tax charge on the outstanding balance.

Salaries and bonuses

The end of the financial year is an ideal opportunity for contractors to use up any lower tax threshold allowances by paying the directors and any employees in the business the balance between the lower and higher tax rates as a salary and/or bonus.

This is especially relevant for spouses or partners working in the contractor's business who have been legitimately working on company affairs throughout the year, but who may not have taken the financial rewards owed to them.

Bonuses can also be used to clear director's loan accounts, as they count as an element of salary and are an overhead in the business and not a dividend that has to be declared out of profits.

Other allowances - personal and limited company

Contractors have a wide range of options that can reduce their tax liability if these options are taken before the end of the tax year; these options include personal as well as company decisions. For example, contractors can add contributions to their [pension](#) pots and invest in Individual Savings Accounts (ISAs).

To take full advantage of all the company and personal allowances, limited company contractors should check with their accountant and ensure that they have made full provision before year-end. In most cases, the costs of professional advice are greatly outweighed by the tax savings contractors can make based on the advice they receive.

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