

Contractor Doctor: How much income should I save for holidays and sickness?

Dear Contractor Doctor,

I've just started my first contract as an interim marketing contractor. Until now, I've always been in a job, never been unemployed, and been paid for time off on holiday and for the few days I've been off sick.

I know that's all changed, and that now I'm running my own business I won't get paid for the days I don't work, whatever the reason. But I want to make sure I've put enough by to take time off for holidays, and in case I'm between contracts or get ill and can't work.

How much of my contracting income should I save for time off due to holidays and sickness?

Thanks

Meera

Contractor Doctor says:

Contractors are not employees and don't get paid for time off, whatever the reason for the absence. Some simple calculations and building up a cash reserve to act as a buffer for time off and resulting loss of earnings due to illness, prevents contractors from getting into financial difficulty.

Also, if market conditions are poor, resulting in an extended time between contracts, having money set aside for essentials such as household and travel expenses can fund the search for a new contract.

Once the contract is signed, create a monthly budget

For first-time contractors, or those reviewing their financial position, the first step once a contract has been signed is to create a monthly budget. This should take into account money put aside for tax, company expenses like travel, mobile phone and broadband, plus personal household expenses.

To calculate corporation tax liabilities, use ContractorCalculator's [interactive online calculators](#). A good rule of thumb is to set aside at least 20% of contract fees each month for corporation tax. The corporation tax rate is 21% (correct at the time of writing) but [business expenses](#) that can be offset against tax will bring the real rate down slightly.

Budgeting for holidays

For most contractors who are working on a contract without a break for three, six or twelve months, holidays are not a luxury. But they should be factored into a contractor's budget because contractors don't earn any fee when they are not working.

To plan for holidays, and to budget accordingly, bear the following in mind:

There are around 252 working days in the year (365 minus weekends, minus around eight bank holidays)

Most contractors would like at least six weeks holiday, which leaves around 220 working days, which is 44 working weeks

Most contractors find they take less time off sick than when they were permanent employees (see below for dealing with illness)

That means the income from 44 fee-earning weeks, or 220 fee-earning days, should be spread over 52 weeks of the year. Ideally, contractors should only take out of their businesses the cash they need during working weeks, so that they can still draw down cash left in their company during planned holidays.

How to manage unplanned time off

Unplanned time off can be needed for an illness, or the illness of a family member or friend who requires care, or for unplanned childcare responsibilities. A good contracting rule of thumb is to have at least three months, and preferably six months, of cash in the business or held personally, to cover short-term illnesses or other unplanned time off.

Ideally, all contractors should invest in an [income protection policy](#) to guard against loss of income from a more serious accident or illness. For example, a serious car accident or medical condition could leave a contractor unable to work for a year or more. Savings would cover the first three to six months, and then an income protection policy would cover all essential bills while the contractor recovers. It is very important to take expert advice when taking out such policies, as some 'off-the-peg' policies are designed for permanent employees, and so wouldn't pay out to contractors.

Having a three- or six-months savings buffer provides an income for contractors who are finding it difficult to win a new contract when market conditions are tight. And when market conditions are buoyant, it allows contractors a little more breathing space, so that they can wait until a better contract opportunity arises. And, if nothing else, having the money available for a rainy day is a good stress reliever.

Contractors who follow these simple tips are able to enjoy their contracting careers secure in the knowledge that they can enjoy planned holidays and are covered financially when the unforeseen forces them to take time off.

Good luck with your contracting!

Contractor Doctor

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