
Remuneration Strategy for Owner-Managed Businesses

Aligning Salary, Dividends and Personal Thresholds

1. Why Remuneration Is a Planning Framework, Not a Payment Decision

For owner-managed businesses, remuneration is often treated as a mechanical decision. Salary is set, dividends are declared, and the process repeats each year.

In practice, this approach misses the real opportunity.

Remuneration is not simply about how profits are extracted. It is about how corporate and personal tax systems interact over time. Salary, dividends and pension contributions each operate differently, and the outcome depends on how they are combined rather than which is chosen.

A strategy that works in one year may not be optimal in the next. Changes in profit levels, personal income and thresholds can all shift the position.

The objective is therefore not to find a single “best” method, but to create a structure that can adapt.

2. Understanding the Three Core Extraction Routes

At a high level, there are three primary ways for a director to extract value from a company:

- Salary
- Dividends
- Employer pension contributions

Each operates differently.

Salary reduces corporation tax but introduces income tax and National Insurance. Dividends are paid from post-tax profits and avoid National Insurance but carry dividend tax. Pension contributions reduce corporation tax without triggering immediate personal tax, but funds are not immediately accessible.

The key point is that each route solves a different problem. Salary supports allowances and benefits. Dividends provide flexibility. Pensions offer long-term efficiency.

The role of planning is to decide how these should be combined.

3. Modelling the Combined Position: Why Salary Still Matters

It is common to focus on dividends as the primary extraction method. However, ignoring salary can lead to inefficiencies.

A modest salary can:

- Utilise the personal allowance
- Maintain National Insurance records for state benefits
- Reduce corporation tax

For example, paying a salary within the personal allowance range may create little or no personal tax exposure, while still reducing the company's taxable profit.

The benefit is not the salary itself, but the interaction it creates across the wider tax position.

4. Dividends in Context, Not Isolation

Dividends are often seen as the default extraction route because they avoid National Insurance. However, their efficiency depends entirely on where they sit within the individual's income profile.

A dividend taken in isolation may appear to fall within the basic or higher rate band. In reality, once salary, rental income or other earnings are taken into account, that same dividend may be taxed at a higher rate.

This is why dividend decisions should always be made in the context of total income, not company profits alone.

The difference between a dividend falling just below or just above a threshold can be significant.

5. The £100,000 Threshold: Where Structure Becomes Critical

The £100,000 threshold represents one of the most important pressure points in remuneration planning.

As income exceeds this level, the personal allowance is withdrawn. This creates an effective marginal rate of 60% within the taper range.

From a remuneration perspective, this creates a structural issue. Income that would otherwise be taxed at standard rates becomes significantly more expensive purely because of where it sits.

For example, a director with income of £98,000 may only need a relatively small dividend to trigger the taper. Once triggered, part of that dividend is effectively taxed at a much higher rate than expected.

This is why remuneration planning at this level becomes less about rates and more about positioning.

6. Pension Contributions: A Strategic Lever, Not an Afterthought

Employer pension contributions are often considered after salary and dividends have been determined. In practice, they should be part of the initial planning discussion.

Unlike other extraction methods, pension contributions:

- Reduce corporation tax
- Do not create immediate income tax
- Do not trigger National Insurance

This makes them particularly effective where income is approaching key thresholds.

For example, rather than taking a dividend that pushes income into the personal allowance taper, a pension contribution may achieve a better overall outcome.

The trade-off is access. Funds are retained within the pension environment, which means this route is most effective where immediate liquidity is not required.

7. Multi-Shareholder Planning: Expanding the Structure

Where more than one shareholder is involved, remuneration planning becomes more flexible.

Dividends can be allocated across individuals, allowing multiple allowances and tax bands to be utilised. This can reduce the overall tax burden compared to concentrating income in a single individual.

For example, splitting income between two shareholders may keep both within lower tax bands, rather than pushing one into higher or additional rates.

This is not simply about splitting income. It is about structuring ownership and extraction in a way that reflects the wider tax position of each individual.

8. Timing and Multi-Year Strategy

One of the most overlooked aspects of remuneration planning is timing.

Extraction decisions are often made based on available cash rather than tax position. However, spreading income across multiple years can significantly improve outcomes.

For example, taking a large dividend in a single year may push income into higher tax bands or into the personal allowance taper. Taking the same amount over two or three years may keep income within more favourable thresholds.

This does not reduce the amount extracted, but it can reduce the tax cost.

9. Bringing It Together: Why Remuneration Must Be Modelled

The common theme across salary, dividends and pensions is that they interact.

Changing one element affects the others. A higher salary reduces corporation tax but may increase personal tax. A dividend may be efficient in isolation but inefficient in context. A pension contribution may improve the overall position but affect cash flow.

Without modelling, these interactions are difficult to see.

In practice, the most effective remuneration strategies are those that are reviewed regularly and adjusted as circumstances change.

10. Key Takeaways

Remuneration planning is not about choosing between salary and dividends, but about understanding how all extraction methods interact.

Salary plays a role beyond simple income, supporting allowances and reducing corporation tax. Dividends provide flexibility, but their efficiency depends on the wider income profile. Pension contributions offer a powerful planning tool where immediate access to funds is not required.

Thresholds, particularly around £100,000, often have a greater impact than headline tax rates. Timing and multi-year planning can materially improve outcomes.

A structured, modelled approach will consistently outperform a fixed or formula-based strategy.

11. Talk to us

If you are extracting income from your company, we can help you structure that process in a way that reflects your full tax position.

We can model different remuneration strategies, taking into account corporation tax, dividend tax, National Insurance and personal thresholds.

As with most areas of tax planning, the earlier the position is reviewed, the more flexibility is available.

You can:

- **Email:** info@drs-tax.com
- **Telephone:** 020 8059 1891
- **Submit an enquiry** via our [Contact Us](#) page
- **Book a free 15-minute consultation**