

# Conceptualising Self-employment Income in the UK





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# Executive summary

This exploratory piece of research investigates the under-analysed issue of how the self-employed conceptualise their income, in terms of their own cognitive measurement of their earnings derived from self-employment. As the literature review shows, this can cover a broad spectrum of issues:

- simple calculations of earnings
- preference for and relevance of accounting definitions
- the contribution of self-employment income relative to income from other sources
- the period over which income is conceptualised
- if, and how, reference comparisons are made with other wage-earners, both employees and self-employed
- the contribution made by non-pecuniary benefits accruing as a result of self-employment, and whether these compensate for relatively low monetary earnings
- the tendency to under-declare earnings or not to calculate hourly rates properly.

Using questions based on these issues, the methodology involved 30 interviews, held in mid 2008, with self-employed workers who had been trading for at least three years, spread throughout the UK and broadly stratified by age of owner and type of business. Interviewees were asked about their working definitions and components of income (employment, pensions, etc), comparators used in setting income targets, and metrics profiling the owner and business. Interviewees were also asked about their experiences of and ambitions for business growth, and how personal income had changed with increases in sales.

## KEY FINDINGS

Consistent with other surveys, our sample of self-employed business owners earned, on average, a lower income than achieved by those in conventional employment. Older owners worked fewer hours per week, and attracted lower returns from self-employment. Younger owners worked longer hours, principally because they were more exposed to risk, had a lower average level of savings, and fewer alternative sources of income.

Owners preferred different measures – such as drawings versus profits – and used different periods to measure income, but the most important measure was a highly practical one: income as declared on a tax return. Therefore, there were some practical distinctions between the conception of business performance and self-employed (and total) income. The formulation of such accounts varied considerably, depending on both the constitution of a firm (as a limited company, partnership or sole trader), and the business and personal objectives of the owner. The most important factor, however, seemed to be how interviewees used accountants – as simple

processors of year-end accounts or, alternatively, to optimise the legitimate opportunities open for the self-employed to avoid tax.

As a working definition of their income – a less formal benchmark than used on a tax return – two-thirds of the sample identified drawings from the business as their preferred measure. Most effectively treated drawings and profits as identical, by drawing all their profits from the business to function as their income. The remaining one-third used other measures, such as sales or profits. They often chose to suppress their current earnings in favour of investing in business development.

The use of drawings as a measure was preferred by male owners of business services firms, who worked fewer hours, but drew a higher hourly wage from their business. Sales turnover was favoured by females who operated in non-business-services firms with lower profit margins. Those who preferred profits as a measure tended to work the longest hours and drew the lowest wages, although their businesses tended to have the highest profit ratio.

The timescale across which earnings are measured may be as important to the conceptualisation of income as cognitive differences in the definition of earnings. Different timescales created different reference points for comparing earnings with employees (or self-employed peers), and/or to gauge productivity against an hourly rate. The period used depended on the sector and business model – eg whether the business involved cash transactions versus long assignments with distant invoicing arrangements.

Almost three-quarters of respondents failed to undertake an adequate process for calculating their hourly earnings, as it was difficult to estimate the amount of work actually needed to realise their annual or quarterly income target. This was at least partially attributable to the lack of incorporation of non-productive time (eg leisure, sickness, holidays) into calculations. This led to two of the younger interviewees earning, in effect, a rate below the National Minimum Wage and contributed to the observation that 60% of the sample earned below the average for employees. The corollary of this is that for 40% of the sample their income was greater than the average for employees.

A wider conceptualisation of income for the self-employed could take account of non-pecuniary returns. Although interviewees were adamant that their situation had improved since quitting regular employment, there was no clear evidence that the resulting non-pecuniary benefits adequately compensated for lower earnings.

There were no statistically significant differences between self-employed males and females in the sample. Timescales and preferred working definitions were similar, while expected differences in motivation failed to materialise.

Certain types of self-employed worker were more disposed to business growth, ie expanding the sales of and profits from their business activities. Younger owners were more keen to expand, but at some future date, while older owners were more interested in increasing the profitability of their activities. In addition to this age-related interest in growth there was some evidence that those favouring drawings as a measure of income were less interested in growth, while those using sales and profits as measures were more likely to favour growth and have longer-term plans for business development.

### **IMPLICATIONS AND POTENTIAL POLICY ISSUES**

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In order to resolve their unsystematic setting of fees, self-employed workers could be encouraged to follow simple flow chart instructions to calculate daily or hourly rates more accurately. The relevant factors of fee-earning time and non-fee-earning time should be stressed, alongside comparable salaries from employment. A full list of additional tax deductible expenses could also be included as part of the representation of costs.

The 2008–9 recession may prompt increases in the rate of business starts, in particular those ‘necessity entrepreneurs’ for whom starting a business was not their first choice. In response to this, business support agencies might also counsel start-up clients with advice about the likely level of earnings from self-employment, especially hourly rates, in order to provoke a direct comparison with employment. This would help avoid unnecessary exits from self-employment, where unrealistically high estimates of income are expected by the nascent and possibly naive start-up.

Accountants should be encouraged to make the best use of tax-deductible expenditure as this might enable clients to retain more income; especially so in the event of an economic downturn. Specific items should be included in business costs; eg pension provision. Pension uptake among the self-employed has been steadily falling and investment in pensions would be one such way to reduce tax liabilities, as well as providing for the future. There may be a role here for combining the business advice provided in preparing tax returns, with the advice on procuring pensions, rather than separating these two services.

Advice and counselling for self-employed business owners who aspire to develop their businesses should be targeted, given that younger owners may be prepared to increase their sales and employment, while older owners focus on increasing their profitability. All owners should also be reminded that there are strongly positive returns to income from sales growth.



# 1. Introduction

## 1.1 CONTEXT OF THE RESEARCH

There are nearly 3.7 million individuals classified as self-employed in the UK. It is believed that many of these self-employed workers are 'satisficing', or not performing optimally in terms of their profitability. Furthermore, self-employed individuals typically earn less than comparable employees. In both senses, earnings accruing to the individual and ultimately tax payments are lower than might be expected. As a result of the financial crisis starting in 2008, increases in unemployment might be expected to stimulate higher levels of business start-up, particularly increases in 'necessity entrepreneurship'. Therefore this study presents timely information to inform potential new starts of the level of financial rewards of self-employment, in particular drawing attention to relatively low earnings.

Self-employed owners, therefore, either suffer cognitive failure to discern these marked differences or find compensating non-pecuniary benefits in their self-employed work. Each of these reasons would justify continued self-employment as rational behaviour, but if these reasons are not substantive this may partly explain the decisions of many owners to quit trading in favour of a return to employee status. Policy-orientated research (Allinson et al. 2005) has addressed the systematic miscalculations of potential business start-ups, finding that belief in a series of myths is pervasive. The false proposition that earnings from self-employment are higher than those in employment may constitute a further myth. If this were true then business start-up advisers should counsel their clients with this cautionary advice, in order to address possible business failure.

A further, more fundamental type of intervention might also be appropriate for increasing the profitability of the business, or the income of the owner. Business advisers could encourage owners to adopt different measures of income (eg hourly rate) to obtain a better understanding of their income and make proper comparisons with paid employment. This awareness may, in turn, lead owners to consider how to develop the profitability of their business and seek some business advice. Similarly, if self-employed owners do not make the fullest use of tax exemptions to increase their income then there is also a role for accountants to help them. The findings of this report specifically address self-employed business owners with no employees, but would also have more general relevance for SMEs, especially micro-businesses. Therefore this exploratory study will develop further the understanding of the conception of income, as well as presenting policy-relevant recommendations.

## 1.2 AIMS AND OBJECTIVES

This research investigates how the self-employed conceptualise the returns, especially income, from business enterprise. Accordingly, the emphasis of the research is less concerned with the measurement of absolute levels of income; rather, it focuses on the perspectives of the self-employed on income.

The objective of the research is to understand how self-employed business owners conceptualise the trade-off between current income and future income/wealth accumulation, in the context of non-pecuniary returns and other constraints. The following are among the key questions concerned in this exploratory study.

- How do owners conceptualise the returns from business, especially income?
- Are non-pecuniary benefits important? What are they? How do they compare with actual income?
- How do owners define income in terms of profits and drawings?
- What are the different components of income?
- To what extent are long hours a concern? Are average 'wage' rates relevant? Are comparisons with paid employment important?
- To what extent is business income set at target levels (including satisficing)?

A key aspect of the study is the way in which conceptualisation of income is likely to vary according to (1) different sectors and (2) life-cycle stages, which is duly explored in the context of the above questions.

## 2. Literature review

Self-employment in the UK grew appreciably in the 1980s, with the number of those in self-employment doubling from 1.8 million to 3.5 million. After episodes of growth and contraction in the 1990s, the stock of self-employed increased, from a level of 3.2 million in 2000, to 3.7 million in 2006.<sup>1</sup> Increases in unemployment may give rise to higher rates of business start-up, although the evidence is somewhat mixed. Acs et al. (1994) and Cowling and Hayward (2000) find that self-employment increases with higher levels of unemployment, while Robson (1996 and 1998) find that self-employment decreases with rising unemployment. Although the literature is unclear, the recession may result in an increase in the supply of necessity entrepreneurs – those prompted to consider self-employment because of the ‘push’ from employment into unemployment.

There is substantial interest in understanding the circumstances behind this growth and the variables that affect it. Accordingly, much of the entrepreneurship literature is devoted to studying the supply of entrepreneurs, either by considering the population as a whole (Parker et al. 2005), or by focusing on differences between groups – for example, by ethnicity (Clark and Drinkwater 1998) or gender (Brown and Sessions 2001). Although income is among a host of variables used to model entry into or exit from self-employment, the literature lacks an appreciation of how self-employed business owners actually conceptualise their ‘income’.

### 2.1 HOW ARE EARNINGS CONVENTIONALLY MEASURED?

Most empirical literature does not specify adequately all the elements of income for the self-employed. Parker (2005) observes in the literature three means of measuring income from a business, and summarises their relationship in the equivalence:

Net profit = Revenue – Costs = Drawings + Retained earnings

Parker identifies net profit as the most common indicator of self-employment income. Another measure is drawings from the business, and a third is drawings plus growth in business equity. Each approach has different merits. The use of net profit has the limitation that it represents the trading position of the business, not necessarily the income of the owner – a situation most evident when the business is making a loss and the owner continues to make drawings. The use of drawings indicates the income of the owner, although these drawings may include monies retained from previous trading periods, rather than income earned in the current period. Official measurement (for example, through Her Majesty’s Revenue and Customs’ self-employment short form) tends to focus on profit and the trading position of the business, leading to tax liability.

Problems of synchronising information on the profitability of the business and drawings are therefore methodological issues for analysis, and of practical interest in terms of setting a level of drawings. Data integrity is a key issue since under-reporting of income by the self-employed is endemic (Parker 2004). Declarations to tax authorities are often understated, and owners are reluctant to reveal such information openly to researchers because they fear it could be linked to official government records. Independent studies suggest that less than four-fifths of gross income was reported to authorities in US datasets in periods studied (Clotfelter 1983 and Kesselman 1989) while under-reporting in the UK has run at between 14% (Smith 1986) and 20% (Macafee 1982). Williams (2005) observes that this tax evasion occurs among the most affluent as well as the more marginalised, although government action is often directed at recognising activities that are entirely in the informal sector, rather than simply under-declared business profits.

As well as inaccuracies in the raw data there are other factors that have led to high non-response rates. Wealthier respondents have less time available and value their time more, so participate less in surveys. A surprisingly high number of the self-employed actually do not accurately know their income, accounting for two-thirds of the missing income cases in the 1991 British Household Panel Survey (Meager et al. 1994). A further methodological issue concerns the appropriate transformation of data by researchers. Negative incomes are frequently either dropped altogether, or are given small positive values, imparting an upward bias to estimates (Parker 2004). On the other hand, very high incomes are capped at an upper boundary, leading to some downward bias.

Finally, most studies fail to include returns to capital. Such calculations are complex and usually avoided by researchers, although Headen (1990) provides estimates, suggesting a return of 84% to labour and 16% to capital. Over the longer term, some deferred returns are available in the event of the sale of a business, but as Stone et al. (2007) observe, business transfers are often not realised, despite owners’ expectations.

Most studies on the self-employed focus purely on income, without including the contribution of wealth. One exception is Parker (2003), which uses evidence from the Retirement Survey to describe the income and wealth of self-employed pensioners in the UK. Using the notion of lifetime wealth, Parker finds that among the self-employed, housing assets account for the greatest proportion of wealth (36%), followed by the state pension (27%), and financial wealth, including bank and building society deposits, equities and unit trusts (14%). Earnings from business amount to 11% and the value of the business as an asset just 1%. For this older self-employed group, income from a business thus represents only a small component of total wealth. Parker also finds that self-employed pensioners tend to have a higher lifetime wealth

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1. Office for National Statistics (2007).

than employees because of their greater financial and housing wealth, alongside higher earnings in retirement (but similar levels of pension income). Further research in this area would provide some indication of the changes in income and wealth across the life cycle, and how individuals plan their incomes even into retirement.

The cumulative evidence from these authors indicates that there are methodological difficulties that create problems in calculating self-employment earnings with any confidence and that this occurs for a variety of reasons, often in combination with one another. Not only are there methodological issues concerning the treatment of the data, but the data themselves may not be accurate, because of factors such as under-declaration to tax authorities. A frequent finding of research on self-employment incomes is that earnings tend to be lower than for employees. The next section explores the literature on comparisons, but the caveats on measurement apply to the general discussion.

## 2.2 WHY DO THE SELF-EMPLOYED WORK FOR SO LITTLE PAY?

Evidence indicates that US median income of the self-employed has lagged behind median incomes from employment for some time (Aronson 1991; Carrington et al. 1996). Aronson charts the difference over time, with a 48% income advantage to the self-employed between 1951 and 1954 progressively dwindling to a 20% disadvantage by the period 1985–88. Adjusting for the longer hours worked by the self-employed, their relative position worsens to a 70% disadvantage. Hamilton (2000) finds that self-employment in the US has lower financial rewards than other employment, after controlling for personal characteristics and wage distributions prior to entering self-employment. Evidence from the UK produces different results, with some studies indicating a positive advantage to self-employment. This advantage varies between 7% (Clark and Drinkwater 1998) and 35% (Robson 1997), although these studies do not take account of longer hours worked. On the other hand, Blanchflower and Shadforth (2007) look at earnings as expressed in HMRC records through the Survey of Personal Incomes (not controlling for prior circumstances, nor hours worked), finding that self-employed earnings are actually below earnings for similar employment.

Even though the self-employed in the UK may still have an advantage, this does not explain why they work long hours for relatively low average wages. Parker (2005) advances the idea that self-employment entails bearing greater risk, such that entrepreneurs self-insure by working longer hours, in order to raise their total earnings. It may also be the case that there are non-pecuniary benefits to self-employment, most often represented in the form of ‘being one’s own boss’.

Standard economic theory presumes that utility is based on absolute, rather than relative, income, while sociological

and psychological aspects of the literature indicate that earnings are perceived to represent relative deprivation (ie compared with those earning more), and thus lower overall satisfaction. In conventional employment literature, Clark and Oswald (1996) found that there is a negative impact of working longer hours and (perhaps surprisingly) also a negative impact of higher income on job satisfaction.<sup>2</sup> Equity theory (Adams 1965) suggests that individuals make ‘cognitive adjustments’ when confronted with ‘payment inequities’. This approach hypothesises that individuals have subjective views of their income relative to others. Any ‘cognitive differences’ in income may result in either redefining their reference group, or changing their perception of the skills involved in their job, its importance or intrinsic satisfaction. Self-employed workers may therefore have either have downwardly adjusted their expectations, or they may derive more satisfaction from self-employment, through non-pecuniary benefits, although analysis of these in the literature is often superficial.

Generally, the empirical literature focuses on additional financial benefits that are quantifiably measurable (on pensions: Schiller and Weiss 1980, or insurance: Hamilton 2000). Authors often invite their readers to consider ideas such as ‘being my own boss’ for their intuitive appeal, rather than attempting any analysis with these hard-to-quantify variables. There is a body of literature that moves away from rational wealth maximisation and considers non-pecuniary benefits. In general terms, self-employed workers are regularly shown to be happier in their work than those who are employed by others (Blanchflower and Oswald 1992, Weaver and Franz 1992; Katz 1993), although the reasons are not always fully explained. Evans and Leighton (1989) find that individuals preferring greater autonomy are more likely to become self-employed. Hundley (2001) confirms the idea of job autonomy, but also demonstrates that self-employed workers are more able to use their skills fully, more likely to prefer independence and that they feel less at risk of losing their ‘job’.

Although the evidence is mixed, there is some suggestion that the financial rewards from self-employment are lower than other employment. There are methodological problems in some of these papers, notably the failure to compare hourly wage rates, as well as making like-for-like comparisons of individuals’ skills and experience in both self-employment and other employment. Some studies (Robson 1997, and Blanchflower and Shadworth 2007) fail to make a proper comparison between the hours worked in self-employment and employment, such that hourly wage rates are not compared and indeed the self-employed themselves may be culpable of such errors in their perception of wages. The following section develops the idea that incomes are low for some groups, but that there is considerable variety within the distribution of income.

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2. This analysis uses the New Earnings Survey (Office for National Statistics 1991), as a basis for setting the reference wage, rather than an individual’s subjective view of that wage.

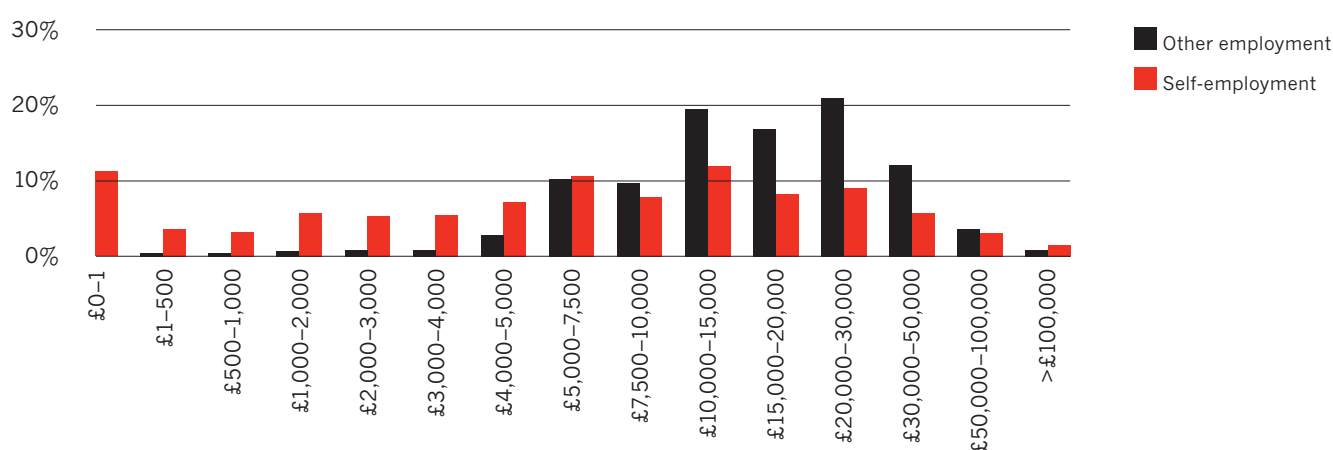
## 2.3 HOW HETEROGENEOUS ARE THE SELF-EMPLOYED?

Importantly, in the context of this study, Meager and Bates (2001) observe that the high degree of heterogeneity among the self-employed is often ignored. Economic studies of self-employment tend to treat the self-employed worker as a single ideal type, rather than as multi-dimensional individuals and businesses. In contrast, the sector in which the business is operating is often shown to influence the level of earnings significantly (Table 2.1).<sup>3</sup> For example, Parker (1997) describes the increase in income inequality in the 1980s, and explains it by the increasing heterogeneity of work undertaken by the self-employed.

The view of homogeneity is further questioned when considering different levels of income (Meager et al. 1994). Figure 2.1 shows the income distribution of the self-employed, revealing a highly skewed distribution relative to income from regular employment. As many as 11.3% of individuals recorded as self-employed earn nothing from self-employment, while the median self-employed income at the time of the research was just £7,500. Furthermore, the mean value of total income at this level is only £10,900 (or below the minimum wage for full-time employees).

Table 2.2 goes further in highlighting the fact that total incomes for many individuals who are self-employed are also low. This is especially true when self-employment represents only a small proportion of total income, such that those earning between £5,000 and £7,500 from self-employment earn a total of only £10,900 overall. As self-employment income rises to higher levels, it normally accounts for a higher proportion of total income and total income itself reaches levels comparable or better than full-time employment.

**Figure 2.1: Income distributions from self-employment and other employment 2005/6**



Source: HMRC (2007, Table 3.9: 2005/6).

3. HMRC (2007, Table 3.9: 2005/6). The HMRC classification differs from the more commonly used Standard Industrial Classification (SIC), although in many instances the categories are very similar (eg construction, manufacturing, wholesale, retail and repairs). Nonetheless, the 'Other Industries' category is less easily identified and relates to SIC classifications in Arts, entertainment and recreation, other services and activities of households as employers. The classification 'Unknown industries' relates to data where HMRC hold information on income but are not able to classify the sector.

**Table 2.1: Sector and mean income from self-employment**

Sector	Workers	Mean income
Legal and accounting activities	163,000	£72,393
Education, health and social work	335,000	£30,149
Other financial, real estate, renting and other business activities	800,000	£16,500
Construction	1,270,000	£14,331
Wholesale, retail and repairs	484,000	£12,831
Manufacturing	220,000	£12,773
Unknown industries	257,000	£12,062
Hotels and restaurants	212,000	£10,189
Other industries	622,000	£9,389
Transport, storage and communication	270,000	£9,222
Agriculture, forestry and fishing	346,000	£8,468

Source: HMRC (2007, Table 3.9: 2005/6).

**Table 2.2: Income distribution of individuals with self-employment income**

Lower limit of self-employment income £	Number of self-employed	Cumulative percentage	Income from self-employment £	Mean income (all sources) £	Self-employment as a % of total
0	539,000	11.4	–	22,000	0
1	163,000	14.9	239	16,200	1.5
500	139,000	17.8	741	14,000	5.3
1,000	246,000	23.1	1,492	12,700	11.7
2,000	224,000	27.8	2,491	11,700	21.2
3,000	230,000	32.7	3,491	10,700	32.6
4,000	239,000	39.0	4,548	9,350	48.7
5,000	532,000	50.3	6,203	10,900	56.8
7,500	395,000	58.7	8,708	13,000	66.8
10,000	589,000	71.2	12,326	16,700	73.6
15,000	394,000	79.6	17,310	21,500	80.4
20,000	439,000	88.9	24,374	28,900	84.1
30,000	282,000	94.9	37,589	45,200	83.2
50,000	140,000	97.8	69,214	85,600	80.6
100,000	102,000	100.0	233,333	270,000	86.7
Total	4,710,000		16,752	25,800	64.8

Source: HMRC (2007, Table 3.10: 2005/6).

Not only are there variations in the level of income within the self-employed population, but there are also different classifications of self-employment. The Labour Force Survey provides one such classification (Table 2.3), although alternative presentations exist in the Family Resources Survey and British Household Panel Survey, which use similar categories. Viewing these categories improves the understanding of the trading relationship with other businesses, as well as associations with employment for the self-employed. This begins to demonstrate that the way in which money is earned among the self-employed varies substantially.

**Table 2.3: Self-classifications of self-employed from Labour Force Survey**

	No. self-employed
Working for themselves	2,279,700
Running a business or a professional practice	604,705
Doing freelance work	459,435
A subcontractor	411,386
A partner in a professional practice	312,275
Sole director of their own limited business	243,975
Paid a salary or a wage by an agency	91,519

Note: All individuals are self-employed as a main job. Individuals are classified according to responses to four different questions.

Source: Office for National Statistics (2008).

## 2.4 INTERACTION BETWEEN GROWTH AND INCOME

The focus of many policymakers is to identify small businesses that create jobs (Robson and Bennett 2000; Amini 2004; Audretsch 2004), with a view to supporting these so-called ‘gazelles’ in their expected growth. Research suggests that modelling growth is too problematic and it is thus difficult to ‘pick winners’ (Davidsson and Henkerson 2002; Barringer and Jones 2004), although ‘descriptive’ approaches are widely used. The focus of research has thus been more upon identifying barriers to growth that may be amenable to policy action (Allinson et al. 2006). There is, however, a noticeable gap in the literature regarding identifying the returns on small business growth in terms of owners’ income. Where explanatory factors for growth are modelled, there are mixed opinions on the role of non-economic drivers, as compared with the motivation to maximise profit and income. This brings us back to the theme that the self-employed are ‘satisficers’, rather than necessarily profit- or income-maximisers.

Cassar (2007) uses US longitudinal data and measures the links between and changes in reasons for start-up and growth intentions, and the subsequent actual growth of the business. Cassar avoids the ‘recall bias’ caused by using retrospective accounts and investigates how views on income influence growth. His hypothesis suggests that high-growth businesses are associated with high rewards and vice versa. He finds that financial success plays an important role in explaining the intent to grow, as well as the actual growth achieved. In contrast to Cassar, Wiklund et al. (2003) claim that non-economic issues are very important in influencing growth intentions, possibly more important than expected financial outcomes. Although they find that there is a positive relationship between growth and the business owner’s income, it is by no means the most important factor that shapes the attitude to growth. In fact, this attitude is ranked joint bottom, behind work tasks, well-being of employees, control, independence, survival of crises and product-service quality. Wiklund et al. (2003) also find that the age of the owner is negatively associated with an attitude to growth (although the age of the business is irrelevant).

Greenbank (2001) provides some UK evidence that micro-business owners may be characterised as satisficers, reluctant to maximise business sales or profits. Underpinning this sub-optimal behaviour is a lack of systematic planning, rather than an explicit desire to restrict growth. Owners, he argues, pursue both economic and non-economic objectives relating to factors such as income levels, job satisfaction, working hours and control and flexibility. He emphasises that such a failure to set objectives effectively presents an opportunity to consultants and advisers working in the small business community. It was, in the view of Greenbank’s interviewees, very important to earn a ‘satisfactory income’ set according to household needs, but aspirations were very limited.



Business growth would appear to correspond with growth in owners' income, although this relationship is not always foremost in the motivation for growth. More typically, business owners have limited ambitions for growth and prefer to exercise control within the known parameters of the status quo, including satisficing behaviour regarding income. The next section elaborates on the contribution of this study to all the research presented in the literature review, including the location of changes in income in the dynamic situation of business growth.

## **2.5 CONTRIBUTION OF THE PRESENT STUDY**

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Whereas research typically considers causal relations between variables (income and education, income and sector, etc) little attempt has been made to address the more fundamental questions of how self-employed people view their own income. Accordingly, we have asked the self-employed for their practical working definitions, rather than their responses to formulae that, while technically correct, are irrelevant or impractical for most self-employed business owners. The method used by Parker (2003) allows a broad formulation of income, including a portfolio of wealth from different sources. Nonetheless, even this is prescriptive, imposing conditions on the data that may not accord with the true expressions of value attached to the portfolio by participants themselves. By contrast, the understanding developed in this study is based on participants' actual views. This study, therefore is sensitive to recording the perceptions and understandings of participating self-employed people, with respect to the balance between pecuniary and non-pecuniary benefits derived from the business. In doing this, the research project was particularly concerned to recognise the heterogeneity of self-employed people. This endeavour was achieved through attention to stratification of the sample, as well as the case study approach, and representation of views of individuals within the categories. Finally, the research addresses the relationship between business growth/development and self-employed business owners' understanding of self-employment income. This aspect of the research is more policy-orientated, addressing the government's agenda to promote business growth.

### 3. Method

The method chosen to achieve the stated aims of the research was in-depth interviews with self-employed business owners. This approach facilitated the exploration of complicated and interrelated themes in a dialogue between the researcher and the interviewee, leading to detailed case studies of different self-employed business owners, their individual circumstances and their particular conceptualisation of 'income'. The research instruments consisted of a short one-page questionnaire to collect standard information and a semi-structured schedule of questions and prompts derived from the literature review. Financial information was volunteered by most participants.<sup>4</sup> The financial data supplied were not necessarily drawn from audited accounts, but were often simply a recollection of the trading performance of their business. Interviews lasted from 30 to 120 minutes and were conducted across five months in mid-2008. The questionnaire and interview guide covered the following areas:

- profile of the owner (age, sex, years in business, highest educational qualification)
- employment history and route into self-employment
- information on business (sector, hours worked, employees, sales, profits, personal income) – covering the last three years of trading, creating a dynamic portrait of trading and personal income.

Questions addressed included the following.

- How do owners think about the returns for their business (hard measures, eg sales, or softer measures such as satisfaction)? Have these changed over time? How valued are the non-financial benefits?
- What working definitions (profits/drawings) are used for earnings from businesses?
- What are the different components of business income? (How many clients? How long-term are sales relationships? How variable are sales?)
- What are the different components of total income (eg business income, other employment, investments, pensions)? Is income viewed holistically? Are drawings from business treated separately?
- Are comparisons made with income from paid employment/self-employed peers? How are fee structures determined?
- Are long hours a concern? Are comparisons made with hours worked in paid employment?

- What growth ambitions do business owners have? To what extent does experience of previous episodes of growth determine present attitudes?
- Does experience confirm that sales growth corresponds with income growth? On balance do the benefits of growth outweigh the costs?
- What investment would be necessary to develop the business? Is growth constrained by a lack of investment funds?

#### 3.1 SAMPLE DESIGN

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The literature identified several concerns to be borne in mind in designing the sample. Parker (2005) indicates that the study of regional variation in incomes is a topic in itself and one that is somewhat in its infancy. Since it is known that regional variation does occur, this study sought to reflect geographical diversity rather than analyse regional differences. This objective was achieved to a large degree with representation from across most Government Office regions of the UK (North East, North West, South East, East, South West, London, West Midlands and Scotland).

The literature review also identified heterogeneity of businesses as a key component of income variability, and that the non-pecuniary benefits of moving from employment to self-employment were substantially lower for professional skilled staff. Accordingly, the sample was divided into two categories: professionals, represented by business services, and other businesses, including craft-based operations.

The sample was then further subdivided into age groups: young owners (under 40 years); middle-aged owners (40–55 years); and older owners (over 55 years). This permitted comparison between different types of self-employed person at different stages in their life cycle. Parker (2003) specifically focuses on the portfolio of income of retired self-employed workers, and we expected that further information on the portfolios of younger self-employed workers would build a more complete picture, both of income across the life cycle and of the different ways that individuals conceptualise income.

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4. 28 interviewees provided at least one year's worth of complete information, while 13 provided three years' worth of complete information.



In addition to the stratification of the sample given above, attempts were made to make the sample more homogeneous. The following guidelines were followed, in an attempt to restrict the majority of the sample to the following particular types of business and owner.

- Mature businesses. Differing surveys have used alternative measurements of maturity. This study used the GEM definition that fully fledged businesses are those that have been paying salaries for at least 3½ years.<sup>5</sup>
- Outright ownership. Multiple owners would not only complicate the situation for the individual, but hinder comparability between businesses.<sup>6</sup>
- First generation businesses. Business succession may also distort results owing to succession effects. Accordingly, the sample is restricted to owners involved in the set-up of the business.<sup>7</sup>
- Businesses where self-employment is the owner's primary job, rather than providing some self-employment income for an owner with a regular job elsewhere. The guaranteed wage of the latter was likely to create different perceptions of self-employment income, compared with those of the wholly self-employed workers, who are more reliant on the variable income from their own businesses.

### 3.2 LIMITATIONS OF THE RESEARCH

As an exploratory piece of primary research, this study is based on a small number of observations. The sample of just 30 interviews is relatively small and not sufficiently representative to suggest that these results reflect the general population of millions of self-employed individuals in the UK. The scope of the interviews is also wide ranging, covering the topics shown on page 14 and inevitably some topics are not covered in great depth. Accordingly, the findings of this study should be regarded as indicative of the types of thought process and behaviour of the self-employed in relation to how they conceptualise the income derived from their business, rather than as comprising definitive statements.

The selectivity of the method excludes certain groups of businesses, with the intention of focusing on mature and viable self-employment businesses. The consequence of this is that this research does not represent these excluded groups, although such groups may deserve their own specific studies. Partnerships attract different questions, because of the share of resources within the business, and would merit interviews with both partners. Similarly, husband and wife partnerships may produce different results and here the focus might involve examining household income more closely. The omission of 'new' businesses means that the experience of transition from employment to self-employment is not properly captured and these views are likely to differ from the retrospective narratives included in this study. Specific types of self-employment relationship, such as those described in Table 2.3, could also receive attention because, for example, subcontractors might be expected to exhibit differences to principal contractors.

Finally, there may be some limitations in the data themselves, because of the nature of the exchange of information in interviews. Interviewees may not have been entirely candid in their comments and the financial data may be susceptible to the reporting errors cited in the literature, although estimates were more readily provided than the two-thirds of missing income observed by Meager et al. (1994).

### 3.2 PROFILE OF ACHIEVED SAMPLE

The survey instruments were used to collect information on a number of different variables, the most important being the ages of the interviewees and the types of business they operated. Since the sample was relatively small, the respondents were not necessarily representative of the population of small business owners as a whole.

The final sample was achieved by snowball sampling. This method was chosen because it helped to overcome any suspicion that interviewees may have had in discussing very personal information about their income and the profitability of their business. This method has some disadvantages, most notably the representativeness of the sample and the inclusion of those with larger networks, while neglecting those with fewer contacts. A detailed summary of the interviewees is shown in the Appendix.

5. VAT data from 1995 to 2005 shows 36-month survival rates ranging between 65.6% and 71.3%.

6. In 2007 there were 2,984,755 sole proprietors in the UK.

7. Reliable estimates usually indicate that fewer than 5% of businesses are owned by a second-generation owner. (Stone et al. 2007).

### 3.3 PROFILE OF SELF-EMPLOYED OWNERS

A total of 30 self-employed people were interviewed, 18 male and 12 female. The age distribution of participants was roughly equally split between the three categories (<40, 40–54, 55+). The range of ages was 24–66 (mean=47, median=49), while their businesses had been established for between 2.5 and 30 years. The average age of the business was positively correlated with the age of the owner (correlation coefficient  $r=0.54$ ). Successive age groups had greater levels of experience in self-employment (Table 3.1). Although older owners had more experience of self-employment, they were also more likely to have entered self-employment when they were older – the middle-aged owners had all started their businesses following a period of employment. Older owners, on the other hand, had tended to defer starting their business until they were considerably older – some had retired or taken early retirement before starting-up. In addition, many younger owners had established their business straight after school or university, meaning that the difference in length of self-employment between age groups was not as great as may have been expected.

The employment history varied considerably and was not always directly related to the chosen self-employment activity. For three participants self-employment was their main occupation and had been since they completed their vocational training. More than three-quarters of the sample had worked in the private sector prior to self-employment, some in management and others in lower-level vocational or customer-facing roles. One-third of the interviewees had no prior occupational experience in their chosen self-employment field, and these were mainly the younger owners. Half of interviewees who had previous relevant experience in paid employment were older (Table 3.2), and several of these described this as ‘serving their time’, as well as recognising the skills and networks they had accumulated. Although nearly two-thirds of this group had quit paid employment to start their business, one-third were more circumspect, choosing to establish their business on a part-time basis while still employed, so that they benefited from the safety of a guaranteed salary. Five interviewees had a more mixed career, having owned multiple businesses or experienced periods of self-employment or company ownership sandwiched between spells of other employment.

**Table 3.1: Age of participants and age of businesses**

Age band	No.	Age of business in 2007/8 (years)		Age of entry into self-employment (years)	
		Range	Average	Range	Average
<40	9	2.5–18	5.4	16–33	24.6
40–54	12	3–19	9.6	34–46	39.1
55+	9	5–30	14.3	34–60	47.2

**Table 3.2: Age and relevance of work experience before self-employment**

Age band	Related to previous employment	Unrelated to previous employment
<40	3	6
40–54	5	7
55+	8	1
Total	16	14

### 3.4 BUSINESS PROFILES

Sole traders owned 20 of the businesses, while seven businesses were partnerships (mostly in name only – one person tended to undertake the majority of the ‘fee-earning’ work) and three were limited companies. Eleven traded under their owner’s name, and 19 under a business name, which may relate to different aspirations about the future shape of the business, or the impression given to potential clients. Only seven owners had separate business premises, the remainder operating from home.

In sectoral terms, the largest group operated in business services, including, for example, consultancy, training and Web design (Table 3.3). These owners were engaged in a number of different areas: finance, marketing, research and business support. Although other business owners were categorised together, they were a diverse group, including a general builder, tourist guide, taxi driver, artist, theatre designer and swimming instructor, among others.

**Table 3.3 Response rates by age and type of business**

Age band	Business services	Other
<40	3	6
40–54	6	6
55+	6	3

Owners of business services firms generally had direct work experience in their chosen field, whereas other business owners tended to lack this directly transferable background (Table 3.4). This is probably due to the low barriers to entry in other businesses, with a lesser reliance on networks or codified training.

**Table 3.4 Sector and relevance of work experience before self-employment**

	Related to paid employment	Unrelated to paid employment
Business services	11	4
Other	5	10
Total	16	14

Tables 3.5 to 3.7 show the sales turnover, income and hours worked.<sup>8</sup> In most respects, the businesses are biased towards the slightly larger end of self-employed businesses (see Table 2.2). The assertion of Meager et al. (1994) that many self-employed owners do not know their income was not found to be true among the interviewed sample. Most respondents were able to offer approximate figures for their most recent year, if not for the entire three years, without reference to their accounts.

**Table 3.5: Mean sales turnover**

Age band	Business services	Others	All businesses
<40	£49,000	£31,283	£37,188
40–54	£87,386	£118,400	£101,483
55+	£32,167	£21,000	£28,444
All ages	£57,621	£60,193	£58,862

There was a wide range of sales turnover among the sample, from a minimum of £3,000 to a maximum £400,000. Table 3.5 shows that the mean turnover among the sample was £59,000, while the median was £40,000.<sup>9</sup> Overall, while there was little difference between business services firms and other businesses, the most noticeable differences were instead between age categories: sales reached their highest levels among businesses owned by the middle-aged 40–54 group.

Since the businesses operated in diverse sectors, the composition of sales, in terms of type of customers, varied widely. This ranged from the briefest of contacts for a photographic website (one million unique page impressions and attendant income from sponsored advertising), to very close, long-term relationships for a swimming instructor and a tiler (who both had only a single client). More typically, the median number of paying clients among the sample was 15 per annum. Moreover, not only did the number of customers vary between businesses, but the fee structure within businesses could also vary for different clients. For example, the music editor attempted to charge higher rates when working on big budget films, while consultants would reduce fees for voluntary-sector clients.

Fees also varied according to the number of different services offered. Almost half (14) offered only one service and therefore generated only one income stream. By contrast, the remaining 16 businesses had multiple, though often closely allied, methods of generating income. Multiple income streams usually required a greater variety

8. Both age of owner and type of business are not statistically significant determinants of any of these relationships for this sample, but they are nonetheless used as part of the analytical framework to understand the responses of the sample with regard to their view of income.

9. This compares fairly closely with mean sales turnover for businesses with no employees of £64,266 for the UK (BERR 2007).

of skills and aptitudes on the part of the owner, and often commanded different fee levels, with interviewees seeking to maximise the number of sales of 'premium' services within their portfolio, which entailed the greatest fee. This was not always possible, however, and the least profitable activities continued to form part of their work. Examples of this include the tour guide who also operated as a tourism consultant; a market researcher undertaking street surveys and focus groups; an artist selling both originals and commissioned work for publishers was found to have royalty income. A further three interviewees disclosed two highly distinct business interests: consultant/author; taxi driver/gardener; and consultant/artist.

**Table 3.6: Average personal income from self-employment (2007/8 financial year)**

Age band	Business services	Others	All businesses
<40	£27,500	£10,629	£16,956
40–54	£34,320	£14,440	£25,284
55+	£14,000	£17,567	£15,189
All ages	£24,828	£13,696	£19,660

Among the sample, during the 2007/8 financial year, personal income from self-employment varied between £0<sup>10</sup> and £60,000.<sup>11</sup> Although technically self-employed, some interviewees were actually paid as temporary staff, through a mix of PAYE and business invoices (eg market researcher, stage manager). As indicated in Table 3.6 the average personal earnings from self-employment (ie excluding any other sources of income) among the sample was £19,660, with a median of £16,600,<sup>12</sup> which was above average for the UK self-employed population.<sup>13</sup> Despite this, earnings were still lower than the average income from other employment.<sup>14</sup>

10. The business earning £0 had had no sales for the year, as much for personal reasons as business reasons, although the owner had engaged in some backroom activities associated with keeping the business active. Up to 11.4% of individuals classified as self-employed earned nothing from self-employment activities according to *The HMRC Survey of Personal Incomes (2005/6)* (HMRC 2007).

11. This income includes income from multiple sources, not one business.

12. Some of the businesses were able to report higher profits (and therefore income), because their clients paid some of their expenses: market research (travel); music editor (travel, accommodation, subsistence, equipment).

13. *The HMRC Survey of Personal Incomes (2005/6)* (HMRC 2007) recorded a mean income of £16,752 and a median of slightly less than £5,000 from self-employment.

14. *The HMRC Survey of Personal Incomes (2005/6)* (HMRC 2007) recorded a mean income of £22,500 from employment. ASHE (2008) records a mean of £26,020.

Owners of business services firms earned considerably more than the others, and this is in keeping with other reported findings about earnings.<sup>15</sup> This result was also consistent for younger owners, but the relationship appears to break down among those aged 55 and above. The results from Tables 3.5 and 3.6 indicate that non-business services firms had considerably higher expenditure and lower profits than business services firms.

**Table 3.7: Average hours worked in a typical week<sup>16</sup>**

Age band	Business services	Others	All businesses
<40	52.5	51.7	51.9
40–54	42.5	49.2	45.5
55+	37.0	22.3	32.1
All ages	41.6	44.5	43.0

The amount of time spent working in a self-employed capacity ranged from 8 to 65 hours per week, with a mean of 41 hours and a median of 45 hours – a longer working week than most employees.<sup>17</sup> Five of the sample worked less than 15 hours and would be best described as part-time. Of these five, two worked fewer hours because they had full-time jobs, while the other three were retired. There were relatively few differences between business services and other businesses, indicating that labour inputs into the business in the two groups are comparable, even if personal earnings were lower for non-business services owners. Differences in hours worked were apparent by age – on the whole, the older the owner, the shorter the working week. This implies that hourly earnings may be a more relevant consideration than gross earnings and they are used throughout the subsequent analysis.

15. *The HMRC Survey of Personal Incomes (2005/6)* (HMRC 2007).

16. The two employees with self-employment as a second job are excluded from this table.

17. Employees worked on average 34 hours (ASHE 2008)

## 4. Results

### 4.1 RETURNS FROM SELF-EMPLOYMENT – DIFFERENT VIEWS

Before exploring the data in depth, it is worth commenting on the differences that can occur after the production of a trading profit, which can lead to varying informal calculations of personal income. These decisions are sometimes built on strategies for the future direction of the business or the owner's life, or even different ways of calculating costs (and therefore drawings). In addition, owners and their accountants often arrive at a formulation of income in terms of formally presented accounts, which can be at variance with the true income accruing to the self-employed individual. These different formulations of income also correspond with the owner's view of the most important line within their profit and loss statement.

#### Calculating personal earnings

Nearly two-thirds of the sample were very straightforward in their production of accounts, recording sales, cost of sales and operating expenses, and treatment of any positive balance as drawings. Others had chosen more complicated models, suppressing their level of drawings below the level of profits. In one case, for example, the owner of a limited company wanted to build a retirement fund, such that the company could pay dividends to him in his retirement. The owner of another limited company was building up share capital, with a view to selling the business.

Sole traders did not justify or explain their behaviour, except perhaps for a vague intention to create a safety net. Two such interviewees indicated that with a young business, they wanted to increase sales and profitability before drawing a more substantial wage.

A variety of methods were used to deal with costs when drawing up accounts, leading to a range of formulations of profit and, therefore, what would amount to different levels of drawings from the same raw turnover figures. All interviewees were aware that a 'good accountant' would be able to provide benefits to the business beyond simple year-end tax accounting, expecting him/her to be able to reduce tax liabilities by identifying the maximum legitimate business expenses.

There was varied use made of accountants with respect to tax minimisation, with the result that some interviewees benefited from declaring greater costs to the business. Almost half the sample conceded that they simply had not sought these services, and/or expressed dissatisfaction with the value for money provided by their accountant. A possible remedy was believed to be a more discriminating search for an accountant and/or better communication over the services that businesses sought. One interviewee knew that better service was available elsewhere, but had not made the necessary arrangements for change, as it

seemed a low priority for the use of his time: 'My dad is self-employed as well and he seems to have a better accountant and claims all sorts of things that I don't' (consultant economist).

The principle area of divergence in accounting practices was the inclusion of an office at home as a legitimate cost. Only five businesses fully exploited this possibility, including a share of utility bills and notional rent in their business costs. In one instance, an accountant advised increasing the value of the costs of a home office in high profit years, thus lowering their tax liability. Many, however, simply did not view this as an option, perhaps reflecting the group's natural conservatism: 'I think that's sailing a bit too close to the wind'. Indeed, the owner of a limited company actually paid himself as an employee, despite the higher levels of tax attached to paid employment, precisely because he wanted to contribute his 'fair share' of tax. Although not explicitly stated, other owners may have also had this sentiment – ie they already derive considerable fiscal benefits from self-employment and availing themselves to the utmost degree was perhaps being greedy.

Many interviewees saw the role of their accountant as 'rubber-stamping' their own, often comprehensive, records, and that was as much as they desired of this professional service. This does suggest that the self-employed demand for accountancy services is split between those owners desiring a more proactive client-focused service and those desiring simple, reactive 'year-end only' services. Moreover, it suggests that accountants could tailor their offering so they provide either or both of these services. It indicates that the role of the accountant is pivotal in determining the level of personal earnings from the business.

#### Working definitions of 'income'

Interviewees were asked which working definition of income they preferred; their answers included a mix of drawings, net profits, sales and Key Performance Indicators. Only five were more focused on the performance of the business (sales and KPIs) as a means of sustaining income flow, while a further five focused purely on the bottom line. Overall, drawings were the most preferred working definition of income, as indicated by the two-thirds of the sample who drew the entirety of the profits out of their business (subject to cash flow requirements). One of the interviewees elaborated on the theme of the closeness of drawings and profits in a small business in an accounting sense, compared with transactions in bank accounts: 'I've a business bank account and I transfer 20% of the profit to my tax account, 20% to my personal current account and 60% to ISAs and savings accounts, but in the end it's all the same because I'm a sole trader'. This group would vary drawings from the business in line with the performance of the business and relative to personal/household expenditure.

Those who suppressed drawings below the rate of profits still tended, nonetheless, to conceptualise business profit as analogous to income, thereby seeing any retained profit as deferred income. This group often opted to set drawings at a particular level every month (one proudly declaring they had kept drawings at the same level for 14 months in a row). One suggested that they used their tax liability as a measure of earnings; although this may relate closely to profit the picture was not always simple. The smallest group focused on sales or sales proxies as representing a scalable indication of income; ie when the business is seen to be performing at an above-average level in sales terms, they know their income will also be above average for the year.

Table 4.1 explores how different understandings of income are related to characteristics of the business and owner. Older owners were more likely to define income as drawings or profits, while younger owners preferred sales as a measure. Those who favour drawings as a measure earned the most, worked the fewest hours and consequently had the highest hourly rate. The differences between sales and income were due to the suppression of drawings as discussed above.

Table 4.2 shows some small differences between the use of definitions, but there is no significant difference between business services and other businesses.<sup>18</sup> Owners of business services firms referred to drawings slightly more often and seldom referred to profits or sales, while other businesses made more frequent references to either sales or profits. It was not possible to discern any implications of definitions affecting the earnings of these self-employed business owners, particularly because those who used measures other than drawings were suppressing current earnings and operating for the longer term.

**Table 4.1: Relations between business performance and working definitions**

Definition of income	Average sales	Average income	Average hours	Average hourly rate	Average age	Profit ratio
Drawings	£47,468	£22,070	36.4	£13.91	49.0	0.65
Profits	£116,800	£10,600	53.8	£3.97	48.4	0.60
Sales	£43,424	£19,537	46.0	£7.93	37.6	0.57

**Table 4.2: Business sector and working definitions**

Definition of income	Business services	Other businesses	Total
Drawings	12	8	20
Profits	2	3	5
Sales	1	4	5

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18. Chi-squared test  $p=0.246$

The sample also conceptualised their income across different timescales (Tables 4.3, 4.4 and 4.5). For example, the taxi driver and fruiterer both dealt in cash and worked to short timescales, based on the flow of sales directly earned in the immediate period. They could process daily differences in takings that made one day more profitable than another: 'I had a good weekend on the taxi'. More typically, however, quarterly or even annual timescales were preferred to gauge owners' income, since the length of assignments and subsequent cash flow were too varied to make comparisons across shorter periods valid. Other businesses were more likely to measure income across shorter timescales, while business services preferred longer timescales.<sup>19</sup> There were also observable differences between working definitions and timescales of measurement. Drawings tended to relate to longer timescales, while profits and sales used shorter timescales.<sup>20</sup>

**Table 4.3: Timescales across which earnings are measured, with average income and age**

Timescale	Number of owners	Average sales	Average hourly rate	Average income	Average no. years trading	Average age
At least monthly	10	£80,855	£8.87	£19,983	8	43.9
Quarterly	10	£42,131	£12.59	£22,992	11.7	50.3
Yearly	10	£55,800	£11.91	£15,633	10.6	46.7

**Table 4.4: Timescales across which earnings are measured and type of business**

Timescale	Business services	Other businesses
At least monthly	2	8
Quarterly	8	2
Yearly	5	5

**Table 4.5: Timescales across which earnings are measured and working definitions**

	Drawings	Profits	Sales
At least monthly	3	3	4
Quarterly	9	1	–
Yearly	8	1	1

19. Chi-squared test  $p=0.027$

20. Chi-squared test  $p=0.042$



Gathering together these different pieces of evidence it is possible to characterise the types of business and owner who define income in the following ways.

Owners who define income as drawings:

- are more likely to operate a business services firm
- are more likely to be male
- work the shortest hours (less than 36 hours on average)
- draw the highest hourly wage (about £14/hour)
- are more likely to have a single income stream
- measure income over longer periods (quarters or years).

Owners who define income as sales:

- are more likely to operate an 'Other' business
- are more likely to be female
- have a lower profit ratio (about 50%)
- measure income over shorter periods (weeks or months).

Owners who define income as profits

- work the longest hours (50 hours+)
- draw a low hourly wage (about £4/hour)
- have a higher profit ratio (about 80%)
- measure income over shorter periods (weeks or months).

## 4.2 WORKING PATTERNS AND REWARDS

There were some distinct life cycle aspects to the level and composition of income, and weekly hours worked, of self-employed workers. The clearest finding from the interviews was that the percentage of total income deriving from self-employment activities declined as the age of the worker increased, with younger owners more reliant on their income from self-employment (Table 4.6). For older workers, an increasing proportion of their total income was accounted for by earnings from other sources (interest and dividends, rental income from properties, pensions). The decline in income from self-employment with age at first stemmed from a decrease in the number of hours worked as the worker approached middle age, followed by a decrease in the hourly rate charged alongside further decreases in hours worked as they approach retirement (Table 4.7). Indeed, younger owners in the sample were increasing their hours worked per week as they built up their business and, potentially, because they feared that future work might not emerge, such that working harder was a form of self-insurance (Parker 2005).

Indeed, the work patterns of self-employed workers were rarely consistent. Hours were rarely even across different time periods, and there was an ebb and flow in terms of the number of clients being simultaneously engaged, different levels of success in winning contracts and deadlines to be met: 'I can work until 3am and get up and start all over again at 7am'. Such fluctuation in working routines was unavoidable, unless there were guarantees of repeat business (eg market research, tourist guide). The consequences of this unpredictable flow of work were some fallow periods with no work at all. This was especially true for the music editor, who engaged in long projects with uncertain end-dates and, as his component of the work was reliant on other stages of production, 'I'm just a cog in the wheel!' This also meant that future assignments could not be accepted until the current one was finished, owing to loyalty to the existing client. Younger owners generally lacked alternative sources of income and, having high levels of debt, the rationale for working hard when work was available to build up a safety net ('self-insurance') was clear.

**Table 4.6: Annual earnings from all sources**

Age band	Average % of total income from self-employment	Average total income (all sources)
<40	88.1%	£23,310
40-54	75.5%	£34,343
55+	63.9%	£24,837



Younger owners also expressed the view that they worked longer, because they had fewer health problems: 'I'm fit and healthy so I'm working while I still can' (general builder, 43). Financial commitments for household expenditure also suggested a deliberate longer-term plan to work longer hours in order to clear debts, as distinct from working harder simply to self-insure against fallow periods: 'I've only got eight grand left on the mortgage and after that I'm going to cut back the hours' (taxi driver, 38). Overall income (ie income from all sources, not just self-employment) was highest in the 40–54 age group, when there was the optimum balance between (a) commanding premium rates owing to experience and reputation; (b) working relatively long hours while still relatively fit and healthy; (c) working longer hours both to clear debts and build up a nest egg for the future; and (d) developing sources of income outside self-employment.

Older workers had lower levels of fitness and less willingness to work long hours, and were also likely to have cleared many of their debts, built up a suitable pot for their retirement and have steady, secure sources of income beyond self-employment, unlike younger workers (ie older people had less pressure to 'self-insure'). They thus tended to regard their self-employment activities as primarily satisficing behaviour to enjoy a more comfortable lifestyle. Their wage rates also tended to be lower, at least in part because their skills were somewhat outdated or they were less willing to take on stressful jobs that may have been higher-paying – few older owners mentioned working beyond midnight and they also had more holidays. Older owners were also more likely to mention refusing contracts and being more selective in choosing interesting work: 'I'm not a profit maximiser, I'm driven by the intrinsic interest of the assignment'. Some of this ability to pick and choose

lay in the fact that older owners were embedded in networks or had a reputation from being longer established in business (Table 3.1). The balance of income from self-employment and from other sources, combined with the trajectory of the owner's career and consequent fee-earning ability as he or she aged, led to an inverted-U shape curve in total income.

A different picture emerged when business sector was considered (Table 4.8). Business services owners earned substantially more than other owners, despite working shorter hours. The effects of total income or wealth did not offset this difference.

### Comparisons with paid employment

As noted in the profile of interviewees, the average earnings from the self-employed sample were nearly £3,000 lower when compared with those in employment. In fact, in the case of two recent graduates, hourly earnings from self-employment were actually below the national minimum wage (NMW). Younger owners justified these initially low incomes in terms of their expectation that they would benefit from higher incomes in the future. Such justification was expressed in terms of 'finding one's feet'. A Web designer (aged 25) reported: 'You pay the business in the first year, break even in the second year and the business pays you in the third year – I skipped that first stage!'. Despite this, he was still earning a wage slightly below the NMW.<sup>21</sup> Similarly, although the young stage manager interviewee earned comfortably above the NMW when in employment, she had long periods of inactivity between contracts, requiring family support to maintain her self-employed lifestyle: 'If my parents couldn't offer me a roof over my head between contracts I couldn't afford to do this'.

**Table 4.7: Age, average earnings and hours**

Age-band	Average hourly rate	Average weekly hours	Average change in hours (last three years)
<40	£12.20	47.2	+7.2
40–54	£12.51	42.8	+0.8
55+	£8.96	32.1	–6.0

**Table 4.8: Business sector and earnings from self-employment**

Sector	Average hourly rate	Average weekly hours	Average percentage of total income from self-employment	Average total income
Business services	£14.89	39.4	78.9%	£34,432
Other businesses	£7.13	42.4	72.6%	£20,869

21. At the date of the interview, the national minimum wage was £5.52 for those over 21.

Older owners with more mature businesses had higher hourly rates, but their process of comparison with paid employees to establish a reference wage was not precise. Often, they compared their current situation with an extrapolation of their prior employment: 'I now earn more than if I'd stayed in my old job. I'd reached the ceiling in middle management and let's say that 10% make senior management – I don't think I was one of them' (organisational development consultant, 58). Others indicated that self-employment, compared with their previous job, had improved their lives holistically, as opposed to simply in financial terms: 'As an area manager I'd be getting £22,000 and a car, but the hours are crazy and they call on you 24/7' (market researcher earning £20,000 for 25 hours per week). Similarly, another interviewee noted: 'Now I'm at a stage where I'm earning about the same – but there were frustrations at work and now any frustrations are ones that I've created' (business consultant, 42). Thus, these middle-aged and older workers generally felt better-off in self-employment compared with paid employment, even if the wage was not directly comparable.

In contrast with these views, however, the stage manager in her mid-20s very much hoped to secure a permanent post as an employee, being currently restricted to self-employment because theatres offered short-term engagements and were usually reluctant to take on permanent staff. Her view was that permanent employment provided superior terms, in particular with regard to sickness and maternity benefits (an argument linked to the points above about self-insurance and the motivations of younger workers).

In fact, the study showed that income comparisons tended to be more commonly made with reference to peers in self-employment rather than salaried employees. For example, locating the individual within the earnings spectrum of their profession: 'some of my old class are already working abroad, or working in films, so they're doing a lot better than me' (theatre designer, 25).

Comparisons focused on the appropriate levels of fees, in terms of hourly or daily rates. The interviewees made frequent reference to the advertised rates of self-employed competitors, or information from trade publications. Although some self-employed business owners were constrained by the model in which they operated (eg taxi fares are set down by local authorities) or their role in a supply chain (eg international development consultant limited by fee structures of large consortia that negotiate directly with foreign governments), the rate was usually negotiable, sometimes in consultation with the client: 'I ask them what they want to pay, if it's too much I probably haven't got the skills, if it's not enough then I'll try to direct them elsewhere' (consultant, 52).

Nonetheless, although more than half of the sample quoted a daily rate, there was little systematic consideration given to the incorporation of non-fee-earning time (eg downtime and holidays) into these rates. Equally, accurate estimation of the required days for completion of

a contract was often unsatisfactory, regardless of the age or experience of the owner: 'I have real problems pricing – they're buying a product – a website, not my time, so I can't charge them a daily rate' (Web designer, 24); 'I just don't know how long jobs take, sometimes they might be able to find a bit more money, which helps, but my first offer has to be competitive' (health consultant, 58). Others adopted pragmatic solutions that ensured they received fair remuneration: 'I price at the end of jobs when I finish so it's based on real costs' (general builder); 'for my latest project I asked for overtime if I went past midnight and they are buying my time at a daily rate, so if they run over schedule then they are paying me fairly' (sound editor).

The twin considerations of costing for non-fee-earning time and accurately estimating days thus complicated the devising of a simple daily rate. Only three tried to correct for this by monitoring earnings every quarter, while most treated quarterly monitoring as a paperwork exercise to produce accounts, preferring to make comparisons with paid employment to set their rates. Therefore, conceptualisation of income, and especially the fee schedule required to reach their desired income, often did not take explicit account of their own inputs and outputs, relying instead on less relevant external benchmarks.

### 4.3 EXPLAINING LOW INCOMES – THE VALUE OF NON-FINANCIAL BENEFITS

One of the factors accounting for acceptance by the self-employed of lower income from their activity than would be available if they were an employee, was the value of certain non-financial benefits. The literature recognises that such benefits are not realised in salaried employment and can potentially compensate for any shortfall compared with a salary (Blanchflower and Oswald 1992; Eden 1992; Weaver and Franz 1992; Katz 1993). Our sample indicated the sorts of benefit involved:

- engaging in activities not possible in paid employment (eg working free of charge or at discounted rates for sympathetic causes)
- modification of behaviour and work practices (eg flexible working, midday shopping, childcare)
- emotional and psychological benefits from self-employment through boosting perceptions of self-worth, personal fulfilment, etc.

It was not clear that all interviewees made comparisons with paid employment in this way, nor was it evident that they actually attempted to quantify the less tangible aspects of self-employment. Nonetheless, it was clear that they preferred being self-employed to salaried employment, viewing this choice as rational (ie the non-financial benefits did indeed compensate for the sacrificed salary).

Even in this relatively small sample, the breadth of responses to the issue of non-financial benefits was remarkably wide-ranging. Nearly half the sample (virtually all those in business services) emphasised the possibilities

of contributing to their local community as a direct result of their work – for example, pro-bono work for charities, reduced rates for social enterprises, serving on committees and working with students and the disadvantaged. Such activities would be less likely to be tolerated within the strictures of typical paid employment (or the choice and extent of activities would be strictly controlled by upper management). Owners often stated they were ‘giving back’, enabling others to benefit from their skills – effectively, a micro-business version of Corporate Social Responsibility (CSR). The architect, for example, mentioned possibly taking on an apprentice, harking back to his own training period. Generally, however, such training was not offered by business services owners; ‘old-fashioned’ apprenticeships and informal on-the-job training were more commonly mentioned by those in manual occupations, such as the general builder or the tiler. Therefore, both the frequency and nature of ‘giving back’ differed between those in business services and other sectors. The reasons underlying this were twofold: first, those engaged in business services do not generally need to be ‘on duty’ (taxi driver), nor work on site (general builder); secondly, those running business services firms had higher hourly rates of income. These factors facilitate a greater range and extent of CSR-type activities.

Although independence was often cited by the self-employed as one of their principal motivations, business services interviewees were quick to point out that they now often operated as a ‘hired hand’, and were expected to be responsive to clients’ demands on their time. Thus, workloads and the nature of work were – to a degree – externally determined by the needs of the client, although interviewees still emphasised the freedom of turning down unsuitable or less interesting assignments: ‘I like to be passionate about the work I take on’. This type of independence also lent itself to a more varied workload, and increasing the diversity of tasks led to greater satisfaction. With no recourse to using the skills of other colleagues and a reluctance to pay for support that would formerly have been paid for by their employer company, the interviewees took on most tasks themselves. The consequence of independent working led to a better use of existing skills, and a higher level of acquisition of new skills than in regular employment (Hundley 2001). There was also a trade-off, however, whereby the normal daily professional and social interactions with colleagues in regular employment were curtailed through working alone.

There were also psychological benefits from self-employment, often expressed as the corollary of independence. One interviewee went so far as to describe self-employment as ‘liberation’ from the patterns of work involved in paid employment. There was a general consensus that self-employment was more fulfilling than any prior salaried jobs, reiterating the findings in the literature (eg Blanchflower and Oswald 1992; Eden 1992; Weaver and Franz 1992; Katz 1993). Two interviewees indicated strong ‘push’ factors from employment to self-employment, citing their former unhappiness and stress. The acupuncturist, for example, was frustrated by his well-paid career job in the chemicals industry, but was

now very satisfied at being able to help people in distress. There was some recognition that this ‘liberation’ could be exaggerated – one interviewee observed that the short-term payoffs could be diminished with the realisation that self-employment was not a utopian solution. Nonetheless, the new status quo was still preferable to the old: ‘the honeymoon is now over, but I still enjoy self-employment more than work’.

Half of the sample regarded self-employment as a triumph, a personal achievement in which they took pride – being paid for services, as an individual, reflected the esteem in which the client held the self-employed worker, rather than the reputation of the larger company. Business services firms also emphasised their ‘sense of professional status’ derived from self-employment. Creative/healthcare interviewees were particularly inclined to note that their work was a part of their life (their ‘vocation’), compared with ‘onerous’ employment. Traces of this latter view were evident in other interviewees, albeit to a lesser extent.

Interviewees were not invited to rank their motivations, but personal earnings were almost invariably mentioned after non-pecuniary benefits. Only two expressed their motivation as primarily income-driven, and both of these were effectively full-time employees (and tended to define themselves as such) with a single client accounting for the majority of their self-employed income.<sup>22</sup> Although it may be presumed that having a single client rendered the individual more like an employee, most business owners in a similar position in fact shared the views of other owners in terms of non-financial versus financial benefits of self-employment. Therefore, it could be argued that the value of non-financial benefits was more relevant for those who defined themselves as primarily self-employed, than those who saw themselves effectively as employees, and that a mixture of self-employment and employment may not produce the same degree of payoff.

In Table 4.9 the extent of non-financial benefits among business services and other businesses are shown. The factors are similar to those often quoted as motivations for start-up, with personal achievement and flexibility being the most prominent. ‘Personal achievement’ corresponded to ‘being one’s own boss’, and pride at personal successes: ‘it was great when I won a Microsoft contract’ (consultant/trainer). ‘Flexibility’ related to work/life balance, with childcare or taking advantage of leisure opportunities at convenient times often cited: ‘I go into town to meet friends for a coffee in the middle of the day’. Such flexibility may offset the length of hours worked or low pay. Although only a small sample, it was noticeable that owners in business services cited a higher number of non-financial benefits than other owners.

22. It would also be true of both income-driven owners that they worked long hours (although no longer than the 60 hours cited by some self-employed businesses) and the work-leisure trade-off may be very different for these individuals than for those working for multiple clients in the more common self-employment model.

**Table 4.9: Non-financial benefits of self-employment**

	Business services	Other businesses
Personal achievement	10	6
Flexible working	8	4
Fulfilling contracts	8	4
New opportunities	8	2
Fun	3	4
Giving back	3	3
Using creativity	1	3
My vocation/calling	0	4
Money driven	1	1
Total	42	31
Average number of benefits	2.8	2.1

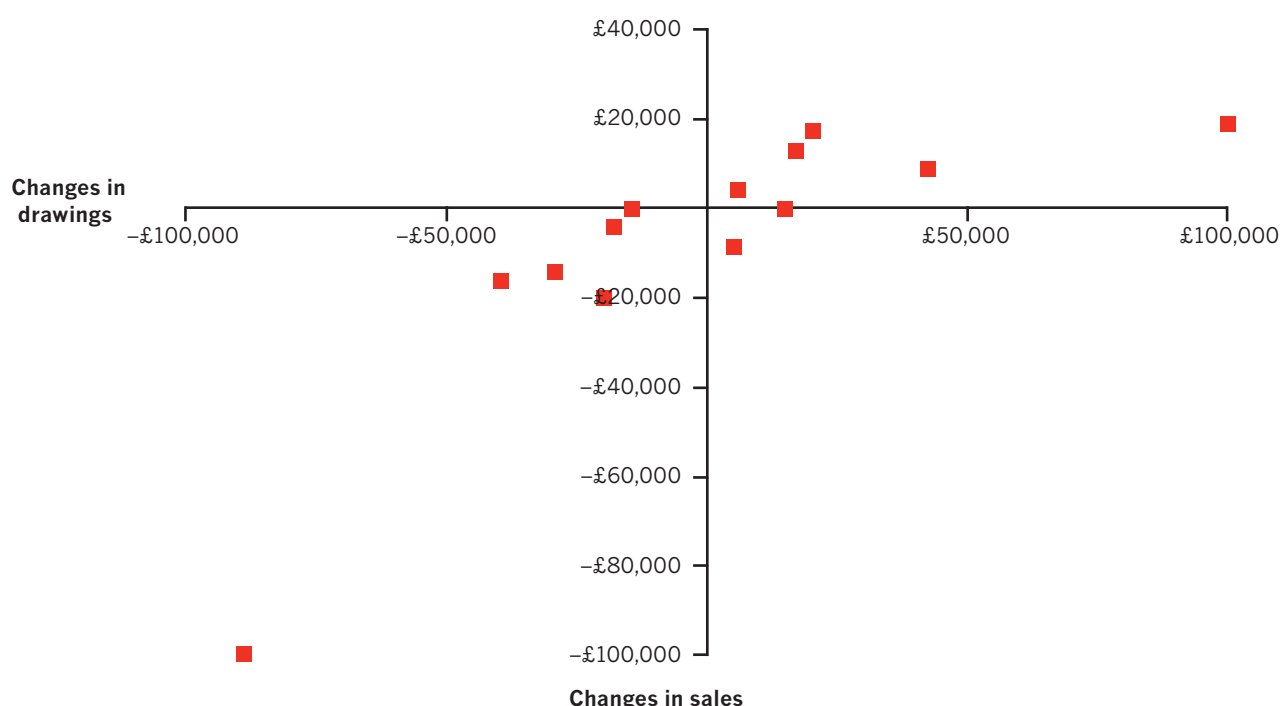
#### 4.4 RELATIONSHIP BETWEEN GROWTH AND PERSONAL INCOME

Interviewees were asked to provide figures relating to changes in sales and income over the past three years, in order to determine how growth (or decline) in turnover affected actual earnings. Only 13 complete observations of sales and income were available for the three-year period, with the changes in these variables shown in Figure 4.1. Although it was a very small sample, there was a clear

positive relationship between changes in annual sales and annual income (correlation coefficient  $r=0.81$ ). This relationship was less significant when changes in annual sales were compared with changes in hourly earnings (coefficient of  $r=0.60$ ), owing to the general increase in hours worked by the sample over the three-year period (an average increase of around five hours per person). Clearly, more research would be required to determine whether this relationship was maintained among a larger sample and in different sectors. In particular, the sensitivities of changes in income to sales growth could be tested, to respond to Cassar's assertion (2007) that high-growth businesses produce higher earnings, while low-growth businesses produce lower earnings.

As well as producing these quantifiable measures of growth, the research also explored, more qualitatively, how interviewees responded to growth in the context of their career history and previous experiences of expansion; and how growth affected income and leisure. When asked how their income responded to changes in the scale of the business, most separated their answer into two categories: (a) working longer hours as an owner and (b) taking on employees or subcontracting. Some clearly indicated they had experienced increasing returns, ie that their income per hour had increased as they increased their own hours. This is especially the case where variable costs were close to zero (eg Web designer, acupuncturist, economic consultant). On the other hand, all businesses that had hired staff expected diminishing marginal returns to personal earnings with sales increases; ie as sales increased, income also increased, but at a progressively slower rate.

**Figure 4.1: Changes in sales and income, 2005/6–2007/8**



Older self-employed workers were therefore especially cautious about expanding employment in their business, since the additional effort did not generate a proportionate reward, quite apart from a lack of ambition in their advancing years and worries about looking after employees. One interviewee noted, of his past employment as a company director: 'Some months the cash flow was so bad we made sure the staff were paid and we took nothing from the business'. These observations help explain the finding of Wiklund et al. (2003) that older owners are reluctant to increase their sales and number of employees. It also raises questions about the effectiveness of earnings strategies in later life – 'downsizing' may, in some instances, be an income-maximising strategy for the owner. For example, the consultant/author indicated that he now earned more in his self-employed capacity than when he directly employed staff: 'I'm not trying to grow a business, I'm trying to grow a brand – and that brand is me'. By contrast, younger owners, lacking such adverse experiences (or, perhaps, business experience in general) harboured growth ambitions, involving taking on staff, but often not in the immediate future.

Nonetheless, almost all the interviewees had made earlier investments to develop their business in some way other than expanding employment. They planned to continue to do so in the future as part of the strategic planning process; investing primarily in their own human capital, rather than physical assets, in order to be more productive and raise their level of income. For example, the tourist guide had thought about becoming a more highly remunerated 'driver guide', which would involve costs of £2,000, but was not sure that the market demand would justify this outlay. The Web designer had invested in the development of bespoke software, which he hoped would reduce the development time of subsequent projects. The common themes linking such responses were driving down costs and/or offering a better service to clients than competitors, with a view to becoming more profitable without the need to work longer hours. The photographer, for instance, felt that competition constantly drove innovation in his market, requiring continuous professional development: 'I'm getting into high-definition footage and I've begun exploring partnering with a Croatian business – but I'm doing this just to stand still'. The music editor was supplied with technology by his clients, but investment in technology could form part of a longer-term strategy to charge clients higher rates.

Growth thus required some forgoing of income in the short term. Interviewees were prepared to do this in principle, but required some assurance that their decision would actually be beneficial for their own incomes and the profitability of the business. Nonetheless, the monetary values involved were generally not substantial; owners generally expected to fund such growth through taking lower drawings, or even using their savings, in anticipation of higher returns in the future.

## 4.5 SUMMARY OF RESULTS

Two-thirds of the self-employed sample preferred drawings as a measure of their income, choosing not to retain money in the business, suggesting that they perceived earnings from their business as 'my money'. This group of responses was strongly associated with higher hourly rates, which would be expected from individuals choosing to draw maximum value from the business. Those using the working definition of drawings tended to measure income over longer periods (quarters or years), although there was no explanation for doing so.

One-third of the sample preferred measures such as profits or sales as measures of income and chose not to draw money from their business in the period in which it was earned. These responses were associated with lower hourly rates, corresponding with retaining money in the business, such that they perceived this as the 'business's money'. They also tended to use shorter timescales across which to measure income.

There were also some notable differences between groups within the sample regarding reported levels of income, but not how they conceptualised income. With regard to age there were some notable patterns. Younger owners relied more on their income from self-employment, with fewer alternative sources of income, while older owners could be observed to be 'downsizing' by consciously working fewer hours. Nonetheless, there were no observable differences between how the various age groups conceptualised income. Similarly, there were no statistically significant differences between self-employed males and females in the sample in terms of conception of income. Timescales and preferred working definitions were very similar and differences in motivation were not substantially different. Business sector was the only variable that appeared to determine how owners conceptualised income. Although working definitions were not influenced by business sector, timescales across which income was measured appeared to be related to business sector.

This study also found that there were returns to self-employment income as a result of a growth in sales. Not only did income rise as sales increased, but when sales fell, income also decreased. This relationship was also true, although to a lesser extent, when sales were compared with hourly income.



## 4.6 CONCLUSIONS

The results of this research largely correspond with established patterns among the self-employed shown by large-scale survey evidence. The sample earned, on average, nearly £3,000 less than those in paid employment (Hamilton 2000; Blanchflower and Shadforth 2007), and the older owners in the sample worked fewer hours (Cassar 2007) and attracted lower returns from self-employment (Parker 2003). Younger owners worked longer hours, as they were more exposed to risk, had fewer savings and no alternative forms of income (Parker 2005).

This research makes an original contribution in terms of insights into the ways in which the self-employed conceptualise their income. This study introduces the concepts of working definitions, as defined by interviewees, the timescales across which income is measured and the value of non-pecuniary benefits as a compensation for low wages (Weaver and Franz 1992; Katz 1993).

Although different measures – such as drawings versus profits and the use of different timescales – were observed among owners, the most important measure, in business terms, was a highly practical one: income as declared on a tax return. The formulation of such accounts differs considerably between businesses. Some differences emerged from the constitution of a firm (as a limited company, partnership or sole trader) and others from the business and personal objectives of the owner, but the most important factor seemed to be how self-employed business owners used accountants – as simple processors of year-end accounts or, alternatively, to optimise the opportunities open for the self-employed to avoid tax legitimately. To maximise their income, self-employed owners should therefore actively make requests for these services, and ensure they are making effective use of their accountant.

As a working definition of their income (ie a less formal benchmark than used on a tax return) the majority of the sample used their drawings from the business. Most effectively treated drawings and profits as identical, by drawing all their profits from the business to function as their income. Owners explained the use of other measures, such as sales or profits, as a choice made to suppress their current earnings in favour of business development.

Self-employed business owners also conceptualised their earnings across different timescales, from days to years, depending largely on their sector and business model, eg whether their business involved cash transactions or long assignments with distant invoicing arrangements. The timescale across which earnings were measured may, in fact, be as important to the conceptualisation of income as cognitive differences in the definition of earnings. Different timescales created different reference points for comparing earnings with paid employment (or self-employed peers), and/or gauging productivity against an hourly rate. Longer comparator timescales, for example, enable a comparison with salaries, but would disguise the effects of working longer hours.

The timescale over which self-employed business owners conceptualised income also had consequences for the derivation of an hourly or daily rate for their services. Many respondents failed to undertake this process of setting their own wage, as it was difficult to relate their annual or quarterly income target back to the amount of work needed to realise this amount. Hence two interviewees earned, in effect, a rate below the National Minimum Wage for employees and this contributed to the relatively low wages earned by a majority of the self-employed. Indeed, some 60% of the sample earned below the median hourly earnings for employees. The failure to calculate hourly rates correctly partially derived from the failure to incorporate fully the non-productive time spent (eg leisure, sickness, holidays). Although many consultants measured the hours of client contact, some slippage was evident, and explicit factoring of potential sickness or holidays into wage rates was rarely accomplished.

A wider conceptualisation of income for the self-employed would also take account of non-pecuniary returns. Although interviewees were adamant that their situation had improved since quitting regular employment, there was no clear evidence that the resulting non-pecuniary benefits adequately compensated for lower earnings; some of these attributions may be cognitive attempts to justify their preferred behaviour.

Although some differences in earnings and hours worked were evident between groups of self-employed workers, there was little evidence of differences in their conceptualisation of income. Although younger owners were more reliant on the income they earned from self-employment, older owners were deliberately working fewer hours. Nonetheless, there were no observable differences between age groups in their conceptualisation of income. Similarly, there were no differences between males and females in use of working definitions, timescales of measurement and non-pecuniary benefits. The only observable difference between groups was that the timescale across which income was measured appeared to be related to business sector.

Other research (Greenbank 2001) finds that self-employment may be characterised by satisficing, and the self-employed are therefore uninterested in business growth. This study anecdotally found instances in the work histories of the interviewees in which larger businesses had not produced proportional returns of income for their owners. This study also found, however, that there were returns to self-employment income as a result of a growth in sales. Allinson et al. (2005 and 2006) present myths that are widely believed among small-business owners. Further research might test whether the relationship between growth and income is misunderstood by the self-employed and test whether the revelation that sales growth produces income growth would modify satisficing behaviour and induce the ambition to grow.

## 5. Recommendations

This report makes recommendations for the intervention of business support agencies and accountants in order to help the self-employed realise higher levels of income, as well as issuing some caution in the area of low earnings. Some suggestions for future research are also proposed.

In order to resolve their unsystematic setting of fees, self-employed workers could be encouraged to follow simple flow chart instructions to calculate daily or hourly rates more accurately. The relevant factors of fee-earning time and non-fee-earning time should be stressed, alongside comparable salaries from employment. A full list of additional tax deductible expenses could also be included as part of the representation of costs.

The 2008–09 recession may prompt increases in the rate of business starts, in particular those necessity entrepreneurs for whom starting a business was not their first choice. In response to this, business support agencies might also counsel start-up clients with advice about the likely level of earnings from self-employment, especially hourly rates, in order to provoke a direct comparison with employment. This would help avoid unnecessary exits from self-employment, where unrealistically high estimates of income are expected by the new and possibly naive start-up.

Accountants should be encouraged to make the best use of tax deductible expenditure as this might encourage owners to earn more, especially in the event of an economic downturn. Specific items should be included in business costs; ie pension provision. Pension uptake among the self-employed has been steadily falling and investment in pensions would be one way to reduce tax liabilities, as well as to provide for the future. There may be a role here for combining the business advice provided in preparing tax returns with the advice on procuring pensions, rather than separating these two services.

Advice and counselling for self-employed business owners who aspire to expand should be targeted, such that younger owners might be prepared to increase their sales and employment, while older owners focus on increasing their profitability. All owners should also be reminded that there are strongly positive returns to income from sales growth.

Future research should be mindful of the methodological considerations that this paper raises in terms of the heterogeneity of the self-employed population and how large datasets such as Labour Force Survey, British Household Panel Survey or HMRC fail to identify how money is earned, neglecting contexts such as earnings constraints imposed by trade bodies or business-to-business/business-to-consumer transactions. Accordingly, future research should, where possible, involve primary data collection to capture such information, rather than relying on secondary datasets.

Following on from this more general study, other research could explore how particular groups conceptualise income. The newly self-employed could represent an especially interesting focus for future research.

Further research could test whether the revelation that business sales growth is likely to create net returns to income would modify satisficing behaviour and induce growth ambitions among the self-employed.

## Appendix: Detailed profile of interviewees

Self-employed occupations	Sex	Age	Self-employment				Total income (£)	Preferred measure
			Years trading	Sales (£)	Hours worked per week	Annual income from self-employment (£)		
Business consultant/ trainer	Male	40–54	3	200,000	60	45,000	45,000	Drawings
Tourist guide	Female	40–54	17	54,000	65	6,000	14,000	Profits
General builder	Male	40–54	8	12,000	13	10,000	40,000	Drawings
Consultant/author/landlord	Male	40–54	18	121,000	50	60,000	90,000	Sales
Photographer	Male	40–54	8	–	40	–	–	Sales
Health researcher	Female	40–54	7	25,000	20	27,000	41,000	Drawings
Economic consultant	Male	<40	3	85,000	10	30,000	66,000	Drawings
Web designer	Male	<40	8	22,000	60	15,000	16,000	Drawings
Consultant and trainer	Female	40–54	3	35,000	30	20,000	25,000	Drawings
Computer retailer	Male	<40	2	40,000	55	5,000	5,000	Drawings
Business consultant & trainer	Male	40–54	16	45,000	50	27,000	27,000	Drawings
Theatre designer	Female	<40	3	11,000	40	9,000	11,000	Drawings
Kitchen installer	Female	40–54	3	400,000	47	24,000	24,000	Profits
Public sector consultant	Male	55+	6	0	10	0	10,000	Drawings
Taxi driver/gardener	Male	<40	7	40,000	60	30,000	38,000	Drawings
Leadership trainer	Male	55+	7	70,000	42	6,000	30,000	Profits
Wall and floor tiler	Male	55+	25	5,000	12	5,000	20,000	Drawings
Music editor	Male	<40	3	55,000	55	–	–	Drawings
Financial consultant	Male	55+	10	20,000	60	12,000	27,000	Profits
Artist (publishing and originals)	Female	<40	18	30,000	50	0	4,000	Sales
Website developer	Male	<40	3	40,000	45	38,000	38,000	Drawings
Market researcher	Female	55+	26	30,000	55	12,000	12,000	Drawings
Swimming instructor	Female	55+	5	3,000	8	3,000	11,000	Drawings
Architect	Male	55+	15	55,000	47	45,000	53,000	Drawings
Research consultant	Female	55+	5	47,000	30	34,000	36,000	Drawings
Acupuncturist	Male	40–54	19	56,000	52	14,000	15,000	Drawings
VCS consultant and trainer	Female	40–54	3	98,000	45	27,000	30,000	Drawings
Market research	Female	55+	30	26,000	25	20,000	25,000	Drawings
Fruit and vegetable retailer	Male	40–54	10	70,000	42	18,000	28,000	Drawings
Stage manager	Female	<40	4	12,000	40	9,000	9,000	Sales



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