

## Save Tax by Incorporating Your Dental Practice



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“Every man is entitled if he can order his affairs so that the tax ... is less than it otherwise would be. If he succeeds then, however unappreciative the Commissioners of the Inland Revenue ... may be of his ingenuity, he cannot be compelled to pay an increased tax.”

*Lord Tomlin*

*Duke of Westminster v The Commissioners of the Inland Revenue*



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### More reasons to consider Incorporation?

- Reduction of the tax-free personal income tax allowance from 6 April 2010
- Introduction of a new higher rate 50% income tax band from 6 April 2010
- Restriction on tax relief for pension contributions from 6 April 2011 (*anti-avoidance provisions already in effect*)



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### Reduction of Personal Allowance (PA)

- Currently everyone has the benefit of a tax-free PA for income tax – 2009/10 £6,475
- From 6 April 2010 this will be reduced for those earning above £100,000
- For every £2 of income above £100,000 the PA will fall by £1
- E.g. income of £110,000 = £10,000 excess = £5,000 reduction in PA
- Based on the current allowance those earning above £112,950 will completely lose the PA




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### Effect of PA Reduction

Income (not dividends)	Tax Liability	
	2009/10	2010/11
£100,000	£29,930	£29,930
£113,000	<u>£35,130</u>	<u>£37,720</u>
Additional tax	<u>£5,200</u>	<u>£7,790</u>
Effective Tax Rate	40%	60%




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### Reduction of Personal Allowance

TAXABLE INCOME (£)	PERSONAL ALLOWANCE (£)	TAX INCREASE (£)
100,000	6,475	n/a
110,000	1,475	2,000
120,000	0	2,590




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### Main NIC Changes

- Additional ½% NIC employer contributions on all employees from 6 April 2011
- Additional ½% on your profits before superannuation, from 6 April 2011




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### Extra NICs

- For 'typical' Dentists surgery with £325k wages costs and one salaried GP – extra cost 0.5% = £1,625 p.a.
- And then on your own profits, for the average Dentist a further NIC hit of £500 p.a.




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### Is It Worth Working Harder?

Current Earnings	100,000
Opportunity to earn extra , say	15,000
Tax and NIC on 15,000:	
12,950 @ 60%	7,770
2,050 @ 40%	820
15,000 @ 1.5%	225
Net income available to spend from £15,000 earned (BEFORE superannuation deductions!) is just £ 6,185 (i.e. you get to keep less than 41.2%)	




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### When This May Hit Your Pockets

- Assuming you do not mitigate
- An "average" Dentist will have a tax bill in January 2012 £3,885 higher than January 2011
- An earner at say £175,000 p.a. will have a tax bill in January 2012 £7,635 higher than January 2011
- This ignores increase in NICs



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### Using a Company?

Personal tax rates 50% above £150,000  
(60% for income between £100k and £113k)

Company tax rate 21% up to £300,000



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### Incentives to incorporate (1)

- CGT Entrepreneurs relief
- Goodwill transferred into a company exempt from Stamp Duty (since 21 April 2002)
- Corporate intangibles regime (from 1 April 2002)
- Tax free motor allowance
- Increased Audit thresholds therefore reduced compliance cost



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**Sole Trader vs Company Comparison (1)** RA Accountants<sup>LP</sup>

*Sole trader with taxable profits of £40,000 in 2009/10*

		Tax/NIC	Retained
	£	£	£
Profits	40,000		40,000
Less: Personal relief	(6,475)		
Chargeable income	33,525		
Income Tax		6,705	
Class 2 NIC		125	
Class 4 NIC		2,743	(9,573)
Spend able income			£30,427




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**Sole Trader vs Company Comparison (2)** RA Accountants<sup>LP</sup>

*Assume business now via Company, director taking £6,475 salary*

		Tax/NIC	Retained
	£	£	£
<i>The Company</i>			
Profits	40,000		
Salaries (gross)	(6,475)		
Employers NIC	(0)		
	33,525		
Corporation Tax @21%	(7,040)	7,040	
Distributed as dividend	26,485		
<i>The Director</i>			
Remuneration (no tax/NIC)			6,475
Dividend (no further tax)			26,485
		£7,040	£32,960




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**Would you?**

- Does a tax saving of £2,533 outweigh the administrative burden?
- Would the protection of limited liability sway it?




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### Tax savings if incorporated

Profits	40,000	50,000	60,000	100,000	200,000
Tax saving 2009/10	2,533	4,028	4,807	4,907	5,157

Much reduced tax saving at lower profits

Assumes full distribution of profits (greater tax savings if retained profits)



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### Should I Incorporate?

- Advantages v disadvantages
- What is the balance?



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### Should I Incorporate?

- Advantages
  - Tax savings (greater if profits retained and tax efficient remuneration planned)
  - Protection of limited liability
    - Unless personal guarantees given
  - Ability to grant to a bank a floating charge on company assets



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### Should I Incorporate?

- Divorce ownership from management
- Enhanced status
- Creating a 'corporate' ethos
- Impact of accounts in a 'statutory' format on sale (easier comparison)



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### Should I Incorporate?

- Disadvantages
  - Published accounts
  - Separate entity – you own it but what it owns is not yours
  - New contracts (incl. Transfer of PCT contracts)
  - Company law - directors loans!
  - Greater formality (paperwork and culture)
  - IR35



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### Should I Incorporate?

- Cessation of unincorporated business for income tax purposes
- Increased Accountancy costs, should be outweighed by benefits



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### Incorporation

CGT:

- MV disposal of chargeable assets. Typically Goodwill/land & buildings/fixed plant & machinery
- CGT planning:
  - Incorporate to crystallise gain to 'bank' Entrepreneurs relief?



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### Incorporation

- Stamp Duty (SD)/Stamp Duty Land Tax (SDLT):
  - No SD/SDLT on goodwill/book debts
  - SDLT chargeable on transfer of land & buildings (+ fixtures) at MV – S.53 FA 2003
  - But think!!



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### Incorporation

- Inheritance Tax (IHT) - Business Property Relief ('BPR'):
  - Sole trader property used in business = 100% BPR
  - Partnership property = 100% BPR or, where partners own personally but used by partnership business = 50% BPR
  - After incorporation only 50% BPR if held outside company (and only then if individual controls company – otherwise no BPR)
  - Loan account balance created = no BPR



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### Incorporation

- Company is formed and shares issued
- Goodwill is sold (to utilise CGT annual exemption?)
- Other trading assets sold at book value



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### Incorporation

- Consideration is cash or left as a loan balance
- Popular - land and buildings can be retained outside company (no SDLT)
- No c/fwd of losses permitted (but why incorporate if you have losses!)



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### Sale of Goodwill at Full Market Value

- Establish a healthy loan account
- Goodwill all post 31 March 2002?
- CGT at 10%/18% with no SD/SDLT
- Subsequent extraction with no tax cost



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### Goodwill

- This might include:
  - transferable patient list;
  - brand name;
  - general reputation



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### Company – Profit Extraction

- Salary/Bonus
- Dividends
- Loans
- Interest on Capital
- Rent
- Pension Contributions
- Benefits in Kind



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### Incorporation - Administration

- Form a company and issue the appropriate share capital
- A new bank account will need to be set up for the company
- Discuss with the bank any changes required to borrowing and security arrangements as a consequence of the incorporation
- Legal documents



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### Incorporation - Administration

- Change over any PAYE scheme from the business to the company
- Change stationery to show the company's registered number and office
- Inform all suppliers, as necessary, of the transfer of the business to the company



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### Incorporation - Administration

- Consider the need to inform patients of the change in status to a limited company
- Either arrange new contracts of employment for employees, or inform them of the company formation and that this will not affect any of their statutory rights as there will be deemed continuous employment



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### Disclaimer

These presentation notes are for guidance only and professional advice should be obtained before acting on any information contained in them. No responsibility can be accepted for loss occasioned to any person as a result of action taken or refrained from as a result of reading these notes.



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**Incorporating your Dental Practice**

Good Luck

Please come and visit us at stand H4

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