Worth another look?

Alan Suggett takes a fresh look at incorporation.

Haven't we covered this before I hear you cry? Well, there has been plenty of good material written about dentists and incorporation over the past few years but I have returned to the subject as recently I have received a great deal of communication asking for my and NASDAL's advice in regard to what level of earnings are advantageous when one is considering incorporation. Many practice owners with NHSPS membership seem to be struggling with the annual allowance and incorporation looks to be their only saviour.

The benefits

Let us briefly remind ourselves of the potential benefits of incorporation. First and foremost in our minds must be the potential tax saving as well as limited company protection of personal assets. There used to be very attractive tax savings made by transferring goodwill to the new limited company with capital gains tax being paid at 10 per cent under Entrepreneurs' Relief rules. A loan account was then created that could be drawn down tax free.

Alan Suggett

is a specialist dental accountant and partner in UNW LLP.

But, for businesses transferred to a limited company after December 2014, Entrepreneurs' Relief will not be available where goodwill is transferred to a company related to the transferor. A related company will broadly be one owned by the dentist or any of his business partners or relatives. This means a tax charge at 20 per cent will now apply to any gain realised on the disposal of goodwill during an incorporation of a business. Despite this, incorporations may still be attractive for many dentists.

The NHS caveat

NHS contract holders considering incorporation should be aware of the barriers to NHS incorporation caused by NHS England incorporation policy. Unfortunately, most NHSE local area teams will either not cooperate with incorporation at all, or will impose such onerous terms and conditions that practitioners would rather not incorporate.

When to jump?

There are a number of factors that are particularly influential on the decision as to whether to incorporate or not:

1) Spouse – is there an advantage to be gained by splitting income with your husband or wife? For instance, if he/she is a basic rate taxpayer but not a GDC registrant.

2) Loan repayment – repaying loan capital out of lower taxed profits is a much more tax efficient solution. (The saving is the difference between income tax rate and corporation tax rate on the capital repaid.)

3) The ability to leave funds in the limited company as opposed to spending them personally – cash that is left to 'snowball' can be a great idea. On sale of the practice, cash can be returned to the owner with less tax than taking dividends – as much as 27.5 per cent less tax. Alternatively, the cash could be used to buy additional dental practices.

4) Directors loan account/income substitution – as already alluded to, this has gone out of fashion following the change to tax rules in 2014. It could still be a worthwhile tactic but Capital Gains Tax (CGT) of 20 per cent would be payable on gain on the sale of goodwill to the company. Most incorporations now sell goodwill at cost so that no CGT is payable.

5) The abolition of 'dividend tax credit' earlier this year – which imposed an extra 7.5 per cent income tax on dividends.

I would dearly love to deliver a rule of thumb but, as you can see, the sensible decision (to incorporate or not) can be different for the same profit level depending on which of 1,2,3,4 and 5 apply (and by how much). As always, my advice would be to seek specialist advice.