



## **Guidance on incorporation**

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Incorporation of dental practices has become more frequent over the past few years. Whilst many incorporations have been properly executed and for valid reasons, it seems that many more have not been. NASDAL specialists deal with a multitude of cases where only the short-term benefits and not the full and complete consequences of incorporation have been explained to the dentist. This guidance sets out how an incorporation should be carried out.

1. It is important to recognise, first and foremost, that the Limited Company (“NewCo”) is a separate legal entity and personality from the Sole Practitioner or Partnership (“Dentist”). It is not helpful to visualise NewCo simply as a wrapper around the Dentist’s profits, with everything else carrying on just as it was. The incorporation of a practice is better envisaged as an arms’ length sale from Dentist to a quite separate party, NewCo.

The fact that Dentist may be the sole Director and Shareholder of NewCo doesn’t alter the above advice.

2. For an incorporation to take place, the assets and liabilities of the practice must be properly transferred to NewCo. Assets which should be transferred may include, for example, dental chairs, equipment, such as cabinetry, more portable equipment, such as OPG, autoclaves, and stock.

Particular care needs to be taken with those assets held on finance, where the finance agreement is in Dentist’s name. Such assets cannot be transferred (sold) to NewCo without finance company agreement, and very often the finance company will not easily give this agreement, preferring for the liability to remain personally with the Dentist. In this case, a

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separate agreement must be set up between Dentist and NewCo essentially to rent the asset to NewCo. It is not enough for NewCo to merely take over the standing order – the ownership has not passed.

3. However, not every asset and liability needs to be transferred to NewCo. For example, Dentist would not usually transfer cars to NewCo, to avoid penal benefits-in-kind taxation.
4. Also, the Dentist's practice or property loans in his personal name may be left out of the transaction.

Interest payable on practice loans is generally tax deductible against the profits arising from that business. If the business profits are transferred to NewCo, then care needs to be taken to ensure that the interest on the related loan continues to be tax deductible.

Interest on property loans where the property is not transferred to NewCo needs special treatment.

As with equipment finance, it is not simply enough to change the standing order from Dentist's account to NewCo's account.

5. Another major asset which usually remains with Dentist on incorporation is the practice premises.

If the property is freehold, the Dentist would retain the freehold, then enter into a Lease between Dentist as the owner and NewCo as the tenant. However, this could create CGT problems, and restriction of Entrepreneur's Relief, which requires careful thought.

And if the property is leasehold, it would be normal for the Lease to be assigned by Dentist to NewCo. Dentist would be expected to guarantee the obligations of NewCo under the Lease.

6. The largest asset of the Dentist may well be his Goodwill. There are two aspects of this:
  - Its valuation
  - Its transfer

The valuation of Goodwill is a sensitive issue, leading as it does to a capital gains tax charge, which will normally be at a lesser rate than income tax rates (we do not comment here on the timing/saving/deferral arguments in this respect).

Goodwill needs to be valued at arms' length market value, and this must be done by a competent specialist dental accountant or valuer. Dental practices, whether private or NHS, are unlike other businesses, and there are particular approaches which apply.

You need to be aware that there is a risk of the valuation being challenged by HMRC; the tax savings are just as apparent to tax inspectors as they are to tax advisers. And, on a related note, the Sale Agreement should include a price adjustment provision, which requires careful drafting.

7. The Goodwill must be actively transferred to NewCo, which will be one of the matters addressed in the Sale Agreement. For an NHS Contract made between the Dentist and his

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PCT, this must be replaced by a Contract between NewCo and the PCT. This requires the PCT to re-issue the PCT Contract, and many clinicians avoid this on the grounds that:-

- 7.1 It is administratively unwieldy.
- 7.2 The PCT may choose to take the opportunity to renegotiate some terms in the Contract, such as the UDA/UOA rate.
- 7.3 There is a perceived risk that the PCT may not agree to make the transfer, thus blocking Dentist's perceived "tax saving scheme".

However, for the incorporation of the practice to be fully valid, the Goodwill must be legally transferred from the Dentist to NewCo.

8. It is not sufficient simply to assign the benefit of the Contract. The main reason for this is that clause 12 of the GDS Contract expressly prohibits assignment of the GDS Contract. It is therefore crucial to press the PCT to re-issue the PCT Contract in the name of NewCo.
9. Some PCTs insist on a clause in the new corporate contract which requires their approval when company shares are sold. This means that the practice/company can only be sold with the permission of the PCT. The danger of this is obvious.
10. The employees' employment must be transferred to NewCo. This entails a separate PAYE Scheme to be set up, and the employees transferred to it. The transfer of undertakings regulations (TUPE) need to be followed, which gives the employees the protection of continuous employment. However, P45s must be issued and a new Scheme started. On a related note, the contracts of self-employed personnel, that is associates and hygienists, must also be transferred to NewCo.
11. Superannuation will follow the provider, and if the Contract has been properly transferred into the name of NewCo, the NHS Pensions benefits will follow.

However, under the current guidelines (2011/12):

The "Principal" (ie any dentist who owns shares in the company) may only rank for superannuation to the extent of his aggregate dividends and salary derived from NHS activities. Therefore, problems arise if the company has any non NHS income.

- Incorporated associates will be excluded from the NHS Pension scheme

The interrelationship between incorporation and superannuation is in itself a complex area, and it is recommended you speak to a specialist dental accountant.

Incorporation of a dental practice should be done fully and completely, and it requires the use of a specialist Solicitor to draw up the Sale Agreement, the Lease, the transfer of the PCT Contract and the personnel and assist with any switches in security relating to finance changes.

The Dentist will need a formal valuation of the Goodwill, and accounting assistance and detailed tax advice from a specialist dental accountant. The Dentist's advisers should ideally work as a team to ensure that the Dentist reaps all the benefits available from incorporation, and avoids the pitfalls, which may take a few years to become evident.

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Most importantly, the Dentist must ensure that the decision to incorporate is made with a full and complete knowledge of the facts and consequences, both short and long term.

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