

Should I buy a practice?

In the second of his two-part article, **Paul Kendall** assesses tax and finance issues.

Most associates will not have the funds to buy into a practice outright and will need to raise funds from an external source to finance the purchase. There are a number of banks that historically have been keen to provide finance to dentists and offered discounted rates to those investing in a practice; however the ongoing credit crunch has resulted in an increase in the rates being charged. Prior to the recent financial crisis most specialist lenders would finance up to 120 per cent of the purchase price, unsecured up to a maximum of £320,000, at an interest rate of one per cent above Bank of England base rate. Currently, those lenders are looking at each case on an individual basis, and no longer offer fixed priced deals. However

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low rates of interest are available to those who are willing to shop around. Secured borrowings are currently available at one to 1.5 per cent above base rate, with unsecured borrowing available from 1.5 per cent to 1.75 per cent above base rate.

Advice needs to be taken as to the length of the loan period as there is no point in repaying a business



● Work out your finances before embarking on buying a practice.

loan (with interest eligible for tax relief) over a short period of time, when the borrower also has personal borrowings (for example, a mortgage). In that instance it would be better for the borrower to take the maximum loan repayment period offered, and use up the extra income this will free up to pay off his personal borrowings.

The associate should consider whether an interest only arrangement should be undertaken in the early years of the loan, as

this will reduce the initial monthly cost at a time when cash flow may be tight due to investment in the practice.

Specialist advisers will usually have contacts with the main bankers and can assist to ensure that only the lowest interest rates are charged. It is important that the banks' specialist lenders are approached as high street bank managers are often not aware of the cut price deals available to dentists. ➔



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☉ Taxation issues:

The transition from associate to principal is treated as a cessation of the associate business and a commencement of the principal's business for tax purposes by HM Revenue and Customs. This can lead to cash flow problems for those associates who have been in practice for some time and whose accounts year end is not March 31. The reason for this is rather complicated; suffice it to say that an additional amount of tax will be payable by those associates.

There are a number of tax planning opportunities, though, to deal with this and specialist advice should be sought to reduce the amount payable.

If the practice that the associate is joining has an accounts year end other than March 31 there may be additional tax liabilities to pay upon a future retirement from that practice and advice should also be sought on that matter.

The fixtures, fittings and equipment and stock element of the purchase price of the practice will attract a deduction for income tax purposes and assist in reducing the tax liability in the early years in practice. Unless there is an incorporation of the practice, tax relief on the goodwill element of the purchase price will only be available on the eventual sale of that goodwill on retirement.

Income protection

Associates will usually not have large business liabilities and can often survive a period of time on a reduced income as a result of illness. Principals, however, cannot, as they will often have their share of the practice overheads to contribute to as well as a monthly bank loan to pay. A principal will therefore need to make the following provisions:

Locum cover – to ensure that funds are available to pay a locum to undertake dental treatments in the

principal's absence. This will ensure that the patients' needs are dealt with and an income is received by the practice so that the practice overheads and an income for the dentist can be provided for.

Practice expenses policy – should a locum not be available an alternative arrangement would be to provide for the practice overheads to be paid. This type of policy would normally pay a fixed amount based on the level of expenses in the latest set of practice accounts. It would not be usual for this type of

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policy to provide an income to the dentist in addition to the overheads.

Critical illness policy – to provide a personal income in addition to the above. These policies will provide for a fixed level of monthly income for life (or until receipt of pension), the amount of which would usually be based on the after tax level of drawings of the dentist.

Life cover – to repay the practice bank loan upon death should the practice consider the short term repayment of capital to the partner's executors a problem.

The premiums paid on locum policies and some types of practice expenses policies will attract tax relief, but the proceeds received upon a claim will be subject to tax, whereas premiums on the other policies, mentioned above, do not attract tax relief but their proceeds can be received tax free.

The more usual arrangement of cover would be for the dentist to take out a locum policy that would cover a period of one year, and a critical illness policy to cover the period thereafter.

Record-keeping – usually the practice manager will keep a

record of the joint income and expenses and the contributions by the principals to the joint account, so the principal will usually only need to keep records of personal income and expenses, along with lab bills incurred by the practice that will need to be prior charged to him or her. A large number of practices use computerised accounting packages, such as Sage, and can provide detailed accounts that are useful to the practice for management purposes and also keep the year end accountancy costs down.

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Incorporation – there are substantial tax benefits to incorporation for some practices, but for others the benefits are small and the administration burden of incorporation too high to make the exercise viable. The tax benefits can be derived from restructuring the way that the practice profits are drawn. But given that an incorporated company can claim corporation tax relief on the amortisation of the goodwill each year, whereas an unincorporated principal cannot, it is an area that needs to be examined as part of the purchase process.

As can be seen from the above there are a considerable number of issues that require advice from specialists in the field of dental finance and associates are strongly advised to approach them. The author has seen a number of unsuccessful practice purchases which have resulted from a disregard for the issues above. ■

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