Buying an orthodontic practice

Accountant Mac Kotecha offers some guidance to those considering acquiring a new practice

If you are reading this you will probably already be pretty clued up on the issue of PDS contracts and the impact of this on you as a buyer, but in case you are not, let me give you a brief introduction on these points first. A PDS contract cannot be transferred using the partnership route. This means that the only way to buy a practice that has a PDS contract is for the PDS contract to first be transferred to a limited company and for you then to buy the shares in the limited company (when buying shares in a company, the due diligence process becomes even more important) - unless the PDS contract has some UDAs and is not just UOAs. It could be one little measly UDA, but that should enable it to be converted into a GDS contract which means that, if it is held personally, it should be able to be sold to you using the partnership route.

PDS contracts have end dates so once a PDS is converted into a GDS (assuming it can be) the expiry date should go out of the window.

If an NHS contract (whether PDS or GDS) is already held in a limited company, usually the only way you can buy it is to buy the shares in the company (as opposed to just buying the goodwill from the company).

At this point I need to say that I am not a dental solicitor and if you are looking at buying a practice, you will need to talk to a good dental solicitor who should be able to guide you through the process in the way that is most suitable for you. For the rest of this article, I am going to assume that you are in a position where you will be buying the shares in a company. I am going to give you three 'titbits' that will hopefully help you or at least, demystify limited companies a little.

What it means when you are buying shares

Think of the goodwill as your favourite Quality Street (the purple one for me). You want the purple one. You need the purple one. If the practice you were buying was totally private and there was no NHS contract but it was a limited company, you could, if you wanted to, buy the goodwill from the company. This means that you get the purple one but when you get it – it's not in its wrapper so it is just the chocolate. But that's fine, because you are going to eat it anyway and don't need the wrapper. You now own the goodwill direct. The company stays with its old owner, but it's just a shell now - just the empty wrapper.

Now, if it is an NHS practice and the NHS contract is held by the company, you can't separate the chocolate from the wrapper, which means you buy the actual wrapper containing the chocolate from its owner. You have bought shares and each one of those shares is part ownership of the

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wrapper (which owns the chocolate) so if you buy all the shares – you own the wrapper. You now own the company which owns the goodwill. You do not own the goodwill direct.

What tax will you pay?

I use the word 'you' loosely. When you own shares in a limited company, even if you own all the shares the limited company is still legally separate and distinct. The company pays corporation tax on its profits (20% for companies with small profits but will be 20% for all from April 2015). So the company pays this tax but that reduces the amount you can be entitled to so you are paying it indirectly.

What about you?

It depends. You will be able to extract income from the company broadly speaking in one of three ways (or a nifty combination of the three which your accountant will help you with).

Salary - You pay normally income tax on this at the normal rates. Also, don't forget you also pay employee's National Insurance on your salary (12%), and your employer (the company) pays employer's National Insurance at 13.8% (you don't have to pay the employee part after reaching state retirement age, but your employer still has to pay their bit). The company gets tax relief on the salary and employer's NI.

Dividends - The company does not get tax relief on the dividends it pays you, they come out of its profits which would already have been taxed at 20%. When you receive them, broadly speaking you pay no additional tax up to the basic rate band (but any salary you have eats into the basic rate band first - reducing this) and 25% at the higher rate (and 30.6% at the additional rate (that's over £150k). What does this mean in English? - I hear you ask. Well it means that if you have salary or self-employed income of say £40,000 already, any dividends you take out of the company will already have suffered 20% corporation tax and you will suffer an additional 25% tax on top of that making 45%. This is why it is important to get the planning right!

Draw-down of director's loan - If in the process of incorporation, you have loaned the company some money, this would be shown in the company accounts as a director's loan account. That money is owed to you so the company can, out of its taxed income, repay it to you. In your hands this is just repayment of capital so no further tax for you to pay.

Now that you are the proud owner of a company – you need to keep on top of the deadlines involved. There are deadlines for submitting accounts and deadlines for submitting company tax returns as well as company annual returns. If you don't comply - you will get stung by fines so best to keep up to date!

Mac Kotecha (FCA) is a chartered accountant, chartered financial planner and certified financial planner who deals exclusively with dentists. His company has been established for over 30 years and offers accountancy, taxation and payroll services in addition to invaluable advice on practice management, buying/setting up a practice and other dental issues. www.specialistdentalaccountants.co.uk