Dental Focus

DRIVING LIFELONG PROSPERITY

Summer 2016

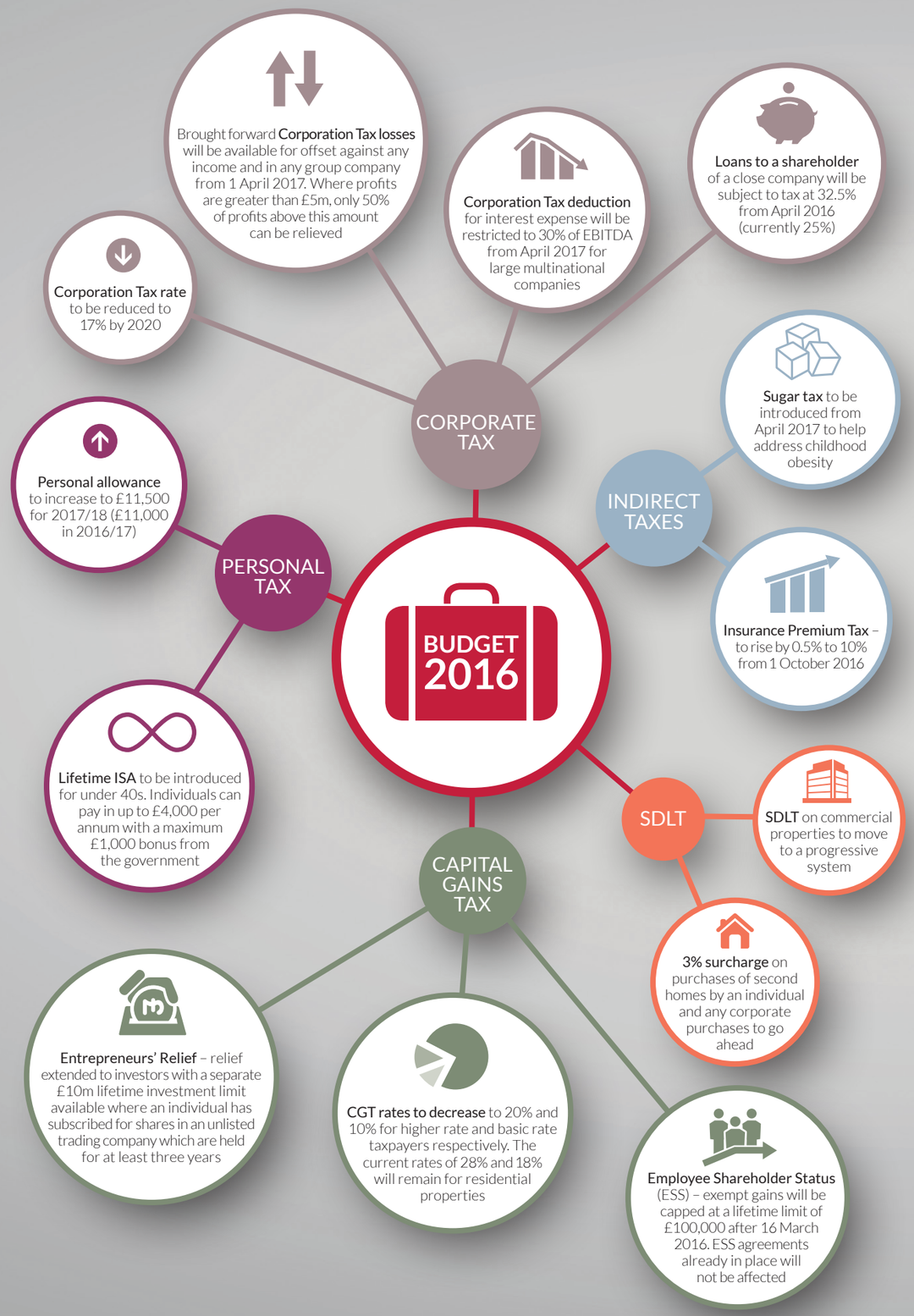
SPOTLIGHT ON CLOUD ACCOUNTING

Welcome...

Welcome to the latest edition of Dental Focus, helping to keep you up to date with the latest accounting and tax developments in the dental sector. In this issue we focus on cloud accounting and the opportunities this offers to dentists and practice managers. Don't miss our webinars introducing Xero cloud accounting software from June onwards.

INSIDE

HAZLEWOODS
DRIVING LIFELONG PROSPERITY



2016 Budget Update

PERSONAL TAX

There weren't many changes in the Budget relating to general personal tax matters which is not necessarily a surprise given the revolutionary changes to dividends and saving rates announced in the 2015 Summer Budget.

The government previously committed to raising the personal allowance to £12,500 over this parliament and made a move in this direction in the 2016 Budget by increasing it to £11,500 for 2017/18. The personal allowance was already set to rise to £11,000 for 2016/17 and that is still the case.

In addition, the Chancellor has reiterated his wish to remove more people from the higher rate tax band. The higher rate band will increase from £32,000 in 2016/17 to £33,500 in 2017/18. This, together with the personal allowance increase, will mean that in 2017/18 an individual will be able to earn £45,000 without paying higher rate tax. This is set to benefit 28.9 million individual taxpayers.

For the self-employed, the announcement of the withdrawal of Class 2 NICs will have been welcome. This will take effect from April 2018 and will save individuals that currently pay these contributions approximately £150 per year.

ISA LIMIT RISES AND NEW LIFETIME ISA FOR UNDER 40s

ISA SAVING LIMIT

The annual ISA savings limit is rising from £15,240 to £20,000 for all adults from April 2017.

NEW LIFETIME ISAS

Those between the ages of 18 and 40 will be able to save up to £4,000 per year in a lifetime ISA from April 2017 until they turn 50. The government will add a 25% bonus so that those who save the maximum each year will receive a state top up of £1,000. The fund is expected to be more flexible than a pension and it is possible to withdraw funds from the ISA at any time before reaching 60, though this will mean losing the government bonus and paying a 5% charge.

The ISA funds can be used by first time buyers for a home worth up to £450,000. The ISA accounts are limited to one per person so a couple can both receive the bonus when buying together. It can also be taken as a tax free retirement fund at the age of 60.

NON-DOMICILED INDIVIDUALS

Proposals had already been made to bring in significant changes to the deemed domicile rules for UK taxation with effect from 6 April 2017. Broadly, individuals who have been resident for 15 of the last 20 years, or are resident and have a domicile of origin in the UK, will be treated as if they are domiciled for all UK taxes.

Budget 2016 confirms that affected individuals will be able to rebase their non-UK assets to market value at 6 April 2017. All non-domiciled reforms will be legislated in Finance Bill 2017.

CAPITAL GAINS TAX

The headline grabbing Budget measure was a reduction in the rates of Capital Gains Tax, taking the maximum rate down from 28% to 20% and the lower rate from 18% to 10%, applicable from 6 April 2016. Those with buy-to-let properties and second homes need not get too excited however, as the measure will not apply to residential properties.

ENTREPRENEURS' RELIEF

Entrepreneurs' Relief (ER) was introduced in 2008 and allows individuals to benefit from a 10% rate of Capital Gains Tax (CGT) on the disposal of certain business assets. It has proved to be a very generous and popular relief, perhaps too popular, as the rules have been significantly tightened in recent years.

Amongst a raft of changes was the announcement that from 3 December 2014 the disposal of goodwill to a connected company would no longer qualify for ER, effectively ending the possibility of claiming it in respect of goodwill on business incorporations.

The March 2015 Budget restricted ER in respect of 'associated disposals' of privately held assets used in a business to those accompanied by a disposal of at least a 5% shareholding or 5% partnership share.

There has been much criticism of these legislative tweaks due to their impact on genuine commercial transactions. Anti avoidance provisions designed to stop people circumventing the new rules have meant that disposals of goodwill to a third party, where the consideration includes even a very small stake in the acquiring entity, have been problematic, as have disposals of privately held business assets where the accompanying business disposal is to family members.

In response to this criticism, the Chancellor has tweaked the rules again, recognising that this is necessary to reverse what were essentially unintended consequences of the original provisions; the changes will be backdated.

BACKDATED TO 3 DECEMBER 2014

It will be possible to claim ER on the disposal of goodwill to a close company (broadly one controlled by five or fewer individuals) where the claimant holds or acquires shares in the acquiring company, as long as that shareholding is less than 5%. This opens up the possibility of disposing of an unincorporated business to a third party, receiving both cash and a small amount of equity as consideration and still claiming ER.

A further welcome measure is the decision to allow ER on incorporation where this is undertaken as part of arrangements for the sale of the business to an independent owner.

BACKDATED TO 18 MARCH 2015

The anti avoidance provisions are to be amended so that ER should now be available on the 'associated disposal' of a privately held business asset when the accompanying disposal of shares or partnership interest is to a family member.

Another positive announcement, for family businesses in particular, was that the 5% minimum disposal requirement will be relaxed for 'associated disposals' where the claimant disposes of the whole of their interest and has previously held a larger stake.

STAMP DUTY LAND TAX (SDLT)

In addition to residential property SDLT changes (see the Buy-to -Let article), there were also changes to non-residential property. It seemed odd that back in 2014 the residential SDLT system was completely revamped from a cliff-edge structure to a progressive banding method whilst the taxation of non-residential property stayed the same. This has now been aligned from 17 March 2016 with the following new rates for purchases:

£0-£150,000 – 0%

£150,000 - £250,000 – 2%

Over £250,000 – 5%

The SDLT on leases on commercial property was already taxed on a marginal 'slice' basis but an additional rate has now been introduced for leases which have a net present value on the rent of over £5,000,000. These leases will now be subject to a 2% SDLT rate.

Cloud accounting – the way forward?

In the last couple of years there has been a rapid increase in the popularity of cloud based software, mainly due to the advantages it can offer to all businesses, including efficiency, connectivity, security and the ability to utilise real time information.

The Cloud is a platform that stores data and information which is accessible anytime, anywhere, from any device.

There is the opportunity for dentists and practice managers to use the Cloud as part of their everyday record keeping, ensuring all aspects of their financial records are totally up to date and providing them with the real time information they require to run the practice successfully.

THE ADVANTAGES OF USING CLOUD BASED SOFTWARE

- **Cost** - upfront costs are reduced. There is no initial start-up cost, but instead a monthly subscription cost. As accountancy and taxation rules and regulations change, the software will be automatically updated, at no additional cost.
- **Access** - just having one computer, with only one user being able to access the information, will be a thing of the past. Multiple users can access the information from smart phones and tablets, which will allow you to be connected to all your financial affairs at any time. Tailored user permissions allow you to give restricted access to users allowing a better flow of information. Different users could be given read-only access allowing them to retrieve information that is important to them.
- **Time** - bank statements can be automatically downloaded via a secure connection, eliminating the need to key in bank statements and reconcile using traditional methods. This frees up time that would have previously been spent entering each transaction.
- **Real time information** - a major disadvantage of traditional accounting software is that key advisers do not have access to the most up to date financial information that could be used to spot opportunities for the practice and nip any problems in the bud. When teamed up with your practice management software, cloud accounting software can be tailored to provide a snapshot of the information that is most important to you at the click of a button, giving you the ability to concentrate on other aspects of the business without feeling like you are tied to the practice.
- **Accountant relationships** - with multi-user access, your accountant can be logged in at the same time as you, providing live support and advice when you need it. Being cloud based eliminates the need to backup files and email them to your accountant giving increased protection over your data.

With up to date, meaningful financial information, key practice decisions can be made on an informed and timely basis; this changes accountant/client relationships from being purely based on compliance and allows better collaboration with other professional advisers.

FIND OUT MORE

To introduce you to Xero cloud accounting software and highlight the benefits and opportunities it creates, we are running a series of 20 minute webinars from June onwards.

To register, or for more information, please visit our website
www.hazlewoods.co.uk/sectors/dental-accountants.aspx

Company Corner

CORPORATION TAX

The main rate of Corporation Tax was due to fall to 18% from 1 April 2020, but the Chancellor announced in the 2016 Budget that this will instead fall to 17%. Corporation tax rates will therefore be:

Current Rate	20%
From 1 April 2017	19%
From 1 April 2020	17%

TAX ON DIRECTORS' LOAN ACCOUNTS

Under current rules, where a close company (broadly, a company with five or fewer owners) loans money to an individual associated with the company, typically a shareholding director, then a tax charge of 25% is due on the balance of the loan at the company year end. For loans made after 6 April 2016 the tax will be charged at an increased rate of 32.5%. As is currently the case, once the loan has been repaid, the tax paid may be reclaimed from HMRC.

ABBREVIATED ACCOUNTS FILING AT COMPANIES HOUSE

Small companies and LLPs currently have three options when it comes to filing their statutory accounts: file full accounts; remove the directors'/members' report and/or profit and loss account from the full accounts and file the rest (abridged accounts); or file abbreviated accounts.

The abbreviated accounts option is by far the most popular and allows a small company or LLP to prepare full accounts for its members, but then file abbreviated accounts with Companies House. These contain no directors'/members' report or profit and loss account, the balance sheet is less detailed and only a small number of notes are required (mainly the accounting policies and fixed assets notes).

The Government has approved new regulations removing the abbreviated accounts option for small and medium-sized entities. Instead, they will need to file the version of the accounts as prepared for their members, although small entities will still be able to remove the profit and loss account and/or the directors'/members' report. Whilst this may appear to be similar to abbreviated accounts, there will be more disclosure in respect of balance sheet notes.

The regulations also permit the accounts for the members to include an abridged profit and loss account or balance sheet, provided a statement is filed with Companies House confirming that the members consent to this.

The changes will come into effect for financial years beginning on or after 1 January 2016, although early adoption is permitted.

FREE COMPANIES HOUSE DOWNLOADS

Companies House has recently introduced a new public beta search service on its website, meaning that all public data held on the UK register of companies is now accessible free of charge.

This includes copies of filed accounts, annual returns and other forms dating back as far as 1995. Documents more than 20 years old are available for a fee of £3.

NEW UK ACCOUNTING RULES – FRS102

FRS 102 is a new accounting standard which replaces all of the current SSAPs and FRSs. It is a single standard, with 35 sections covering the various different items and is 350 pages long, compared to the 3,000 or so pages of current UK GAAP.

FRS 102 will become the standard for accounting for LLPs and unlisted limited companies in the UK. For small entities (which applies to most Dental Bodies Corporate) FRS102 applies to accounting periods commencing on or after 1 January 2016. Therefore the first financial statements to be affected will generally be 31 December 2016 year ends. The comparatives in those accounts will also need to be restated, meaning the opening balance sheet at 1 January 2015 (i.e. at 31 December 2014) will have to be recalculated in accordance with FRS 102.

The main areas where we believe may see significant differences between existing UK GAAP and FRS 102 are outlined below:

1. Directors'/members' loans. There may be a requirement to discount the book values of these loans where they carry no interest, or where interest is below market rate, unless it can be demonstrated that the loans are short term and repayable on demand.
2. Amortisation of goodwill. Unless practices can make a reliable estimate of the useful economic life of any goodwill, the default amortisation period will be ten years.
3. An accrual will need to be included for pro rata holiday pay not taken at the accounting year end. If your holiday and accounting year ends are the same there should be no significant impact.

There are other changes, however a lot of these are not commonly associated with small dental practices. We will be advising affected clients in due course.

Dividends taxation reform

A complete overhaul of dividend taxation took effect from 6 April 2016, introducing new rates of tax. Those most affected are owner managed businesses who, typically, take a small salary and large dividends to make up their remuneration package.

OUT WITH THE OLD...

Under the previous regime, the effective rate of tax for dividends was 0% for basic rate taxpayers, 25% for higher rate taxpayers and 30.56% for additional tax rate payers. Under this regime, it was possible to receive gross dividends of up to £42,385 (based on 2015/16 allowances and assuming no other taxable income) before being subject to income tax.

AND IN WITH THE NEW

The dividend tax credit has now been abolished and all individuals will be able to receive £5,000 of dividend income tax free under the new Dividend Allowance. As each person will be entitled to the allowance, regardless of whether they are basic, higher or additional rate taxpayers, incorporated dental practices should look to utilise both spouse's £5,000 allowance if possible.

This allowance will be taken into account when calculating taxable income and it will still count towards the basic/higher rate tax bands.

The tax rates on dividends in excess of the £5,000 allowance are now 7.5% for basic rate tax payers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers. Dividends will continue to be tax free in ISAs and pensions.

SALARY OR DIVIDENDS?

Dividends should still be more tax efficient than paying a large salary due to the National Insurance costs on salaries, although there will be an increased tax cost to the individual from next year.

For example, a director previously receiving a small salary of, say, £8,000 and dividends to utilise the basic rate band would not have been subject to income tax or National Insurance. However for 2016/17, tax of approximately £2,000 will be due if that director were to continue to receive the same level of net cash. The impact for dentists who need dividends to support their NHS pensionable earnings will be a 7.5% increase in tax on dividends over £5,000.

SOLE TRADE OR INCORPORATION?

With recent changes to the taxation of goodwill, the tax benefits associated with incorporating a dental practice have reduced somewhat. When also factoring in the impact of the new dividends regime, many people are asking whether this could be the final nail in the coffin for incorporation.

After running some initial calculations and based on our understanding of the new rules, we conclude that incorporation should not be discounted by dental practices; however, the potential tax benefits are going to be less. Incorporating a practice should continue to be a viable way to save or defer tax, especially when profits are retained in the business to fund growth or to pay down any bank debt. Reducing Corporation Tax rates to 17% by 2020 may also tip the balance in favour of a company structure. Of course, other non-tax commercial factors should also be considered.

If you would like any advice on how these changes affect you and/or assistance with a review of your remuneration strategy or operating structure, please get in touch.

Buy-to-let tax changes

If you own, or are considering the purchase of, a rental property, various tax changes should be considered.

STAMP DUTY LAND TAX (SDLT)

Firstly, if you buy a rental property or second home an additional 3% SDLT will now be charged. If, at the end of the day of the transaction, the purchaser owns two or more properties and has not replaced their main residence, then the extra tax will be charged. It is possible to obtain a refund of the additional SDLT if the previous main residence is sold within the following 18 months.

The rates of SDLT are therefore:

Band	Residential SLDT Rate	New Additional Property SDLT Rate
0 – £125k	0%	3%
£125k – £250k	2%	5%
£250k – £925k	5%	8%
£925k – £1.5m	10%	13%
Above £1.5m	12%	15%

Paying an additional 3% on even a modest sized property will increase the SDLT charge considerably.

For companies, the additional SDLT rate will apply to all purchases of residential property, not just on subsequent purchases. HMRC had consulted on exemptions for companies with large property portfolios (over 15 properties) but the Chancellor confirmed in his Budget speech that this would not be the case and all companies would be subject to the additional charge.

MORTGAGE INTEREST RELIEF RESTRICTION

Relief for mortgage interest costs on residential properties will be restricted to the basic rate of tax from April 2017, though this will be phased in over four years. From 2017/18, higher/additional rate relief will only be available on 75% of a landlord's mortgage interest, with the remaining 25% attracting basic rate tax relief only. This proportion will increase by 25% each year until 2020/21 when 100% of a landlord's mortgage interest will only get basic rate tax relief.

Who will be affected?

Any buy-to-let landlords with mortgages on their residential rental properties could be affected by the change. Even though the headlines were around higher rate and additional rate taxpayers being restricted to basic rate tax relief, basic rate taxpayers could be pushed into the 40% tax bracket as a result of these changes. This is because rather than a straight deduction of interest from rental profits, the new rules instead provide for a tax credit.

Below are a couple of examples of the potential additional tax payable for a higher rate and basic rate taxpayer. For the purpose of these examples we have assumed a personal allowance of £11,000 in both years and a basic rate band of £32,000. For simplicity, it has also been assumed that the only expense against the rental business is the mortgage interest.

Example 1

Emma, a higher rate taxpayer, owns a buy-to-let property worth £350,000, with an interest rate of 4% (i.e. interest cost of £14,000 per annum) and gross rental income of £18,000.

	Current Rules		2020/21	
Salary	£65,000		£65,000	
Rental profit	£4,000		£18,000	
Taxable income	**£69,000**		**£83,000**	
Tax rate	**Tax band**	**Tax**	**Tax band**	**Tax**
0%	£11,000	£0	£11,000	£0
20%	£32,000	£6,400	£32,000	£6,400
40%	£26,000	£10,400	£40,000	£16,000
Less 20% tax relief on interest			£14,000	£(2,800)
Total tax liability		**£16,800**		**£19,600**
Rental Tax liability		**£1,600**		**£4,400**

In 2020/21 Emma would have additional tax of £2,800 to pay as a result of the new rules. Emma's effective tax rate on her rental profits will be 110% (i.e. £4,400 tax on £4,000 profit).

Example 2

Karen owns a buy-to-let property with the same income and expenses as Emma but is a basic rate taxpayer and believes that she will not be caught by the new rules.

	Current Rules		2020/21	
Salary	£39,000		£39,000	
Rental profit	£4,000		£18,000	
Taxable income	**£43,000**		**£57,000**	
Tax rate	**Tax band**	**Tax**	**Tax band**	**Tax**
0%	£11,000	£0	£11,000	£0
20%	£32,000	£6,400	£32,000	£6,400
40%			£14,000	£5,600
Less 20% tax relief on interest			£14,000	£(2,800)
Total tax liability		**£6,400**		**£9,200**
Rental Tax liability		**£800**		**£3,600**

In 2020/21 Karen would also have additional tax of £2,800 to pay. In this example, Karen will have an effective tax rate of 90% against her rental profits (i.e. £3,600 tax on £4,000 profit).

The above examples show how the effective tax rate can be significant and quite unexpected.

FURNISHED PROPERTIES – WEAR AND TEAR ALLOWANCE

The wear and tear allowance has now been abolished. Rather than a straight 10% deduction against gross rents for furnished properties, landlords will instead be required to deduct the actual cost of replacing furnishings in the relevant tax year. This change could lead to fluctuating tax bills for the taxpayer and may result in an overall increase in tax for many landlords as they are unlikely to replace furniture each year.

The only landlords who are likely to be unaffected by the new rules are those that own furnished holiday lets. They can continue to claim capital allowances for furnishings and any loans relating to furnished holiday lets will continue to receive full relief for mortgage interest costs.

WHERE WE CAN HELP

We can help you to calculate the additional tax that will be payable and explore options in relation to the best holding for your property investments. There may be opportunities to mitigate the effects of these measures through the use of property companies, trusts or simply bringing spouses into the property business.

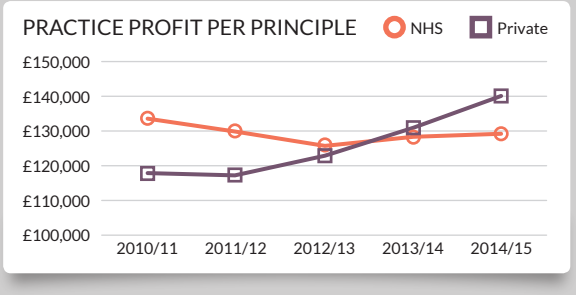
NASDAL STATISTICS – HOW DO YOU COMPARE?

The National Association of Specialist Dental Accountants & Lawyers (NASDAL) has recently published its annual report on the average income and profits of dental practitioners for the year ended 31 March 2015.

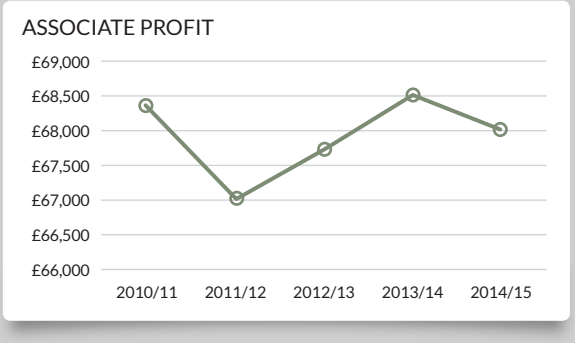
Here are some of the key figures:

- NHS average net profit per principal up by 0.2% to £129,265
- Private average net profit per principal up by 7.3% to £140,129

Average turnover per principal has increased by over 8% for private practices, far outperforming NHS practices. This has had a knock on effect on profitability.



Associates have seen marginal growth in turnover, up by 0.2% to £83,502. This has been offset by increased costs, resulting in a 0.8% reduction in profit to £68,024.



PRACTICE STRUCTURE

Whilst sole traders are still (just!) the majority, with 52% of replies (down from 58% last year), the proportion of limited companies has increased from 24% to 29%. This shows that the dental sector is becoming more corporate orientated and advice from a specialist dental accountant is critical, particularly if you are considering buying or selling a practice.

Copies of the detailed NASDAL statistics are available to our clients.

THE SERVICES WE PROVIDE

Our dental team is happy to discuss matters arising from this newsletter, as well as any other issues relating to your business or personal affairs.

- Accounting and bookkeeping
- Taxation and compliance services
- Management accounts
- Business planning and practice review
- Financial forecasts
- Capital allowances
- Computer software advice to include installation and training on Sage or Xero
- Financial planning
- Payroll assistance
- Advice on buying or selling a practice
- Due diligence on company acquisitions
- Benchmarking and practice profitability advice
- Partnership changes
- Incorporation
- Tax planning
- Capital gains

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