

Dental Focus

A fresh approach to achieving lifelong prosperity



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An end to HMRC's goodwill on incorporation

This article explores the Chancellor's announcement in the Autumn Statement, which brought about an immediate change to the taxation of goodwill for business incorporations.

Latest goodwill values

Firstly, let's look at current goodwill values. The most recent NASDAL survey for the quarter to 30 April 2015 showed the following average values on a percentage of turnover basis:

NHS:	125%, down from 128%
Private:	99%, up from 90%
Mixed:	104%, down from 134%

.....
“These high values have helped create some significant savings on incorporation, which is why the rules have been changed. So, what has happened?”
.....

In the 'good old days'

Since the changes to the Dentists Act in 2006, many dental practices have chosen to

incorporate and run their business through a limited company. Such decisions were largely driven by commercial and legal reasons but tax, as always, also played a big part.

One of the main tax benefits of an unincorporated practice selling its trade and assets, including goodwill, to a company owned by the same individuals was that the sale proceeds could be left outstanding as a loan, which could later be repaid out of the profits generated by the company post incorporation.

Providing certain criteria were met, Entrepreneurs' Relief could be claimed on the disposal, resulting in tax at a rate of 10%. The company would then be subject to corporation tax at a rate of 20% on profits, the balance of which could then be used to repay the loan account with no additional personal tax liability.

This was a very tax efficient way to extract cash from the company, which would otherwise be subject to income tax if it were drawn as salary or dividends (with national insurance also

possibly applicable to salary payments). This route provided ongoing tax benefits when compared to income tax of up to 45% plus national insurance for the individual that would be payable had the business remained unincorporated.

In addition to the above, new businesses, broadly those established after 1 April 2002, could claim tax relief for the amortisation (depreciation) of any goodwill transferred to the new company, therefore reducing the company's corporation tax bill.

It's all history

In an unexpected move, the Chancellor changed the landscape for incorporations in respect of the taxation of goodwill, effective from 3 December 2014.

Firstly, goodwill acquired by a close company (broadly one controlled by five or fewer people) related to the seller no longer qualifies for Entrepreneurs' Relief. This change increases the tax payable by a business on a future

incorporation from the Entrepreneurs' Relief rate of 10% to the main rate of 28% (or possibly 18% to a limited degree).

With the tax rate on the sale increased to 28%, this makes the sale of goodwill, in exchange for the loan account, a less attractive proposition, particularly as the tax is payable up front and there are usually no actual sale proceeds from which to pay it. Whether a sale of the goodwill in this way is still a viable option will depend on whether the larger liability can be funded and if that liability will be outweighed by the annual savings in the longer term. Furthermore, there may be a more efficient method of extracting profits from the company, depending on each individual's personal circumstances.

Secondly, corporation tax relief on the amortisation of internally generated goodwill was withdrawn where the company acquires the goodwill from a related party, regardless of when the business commenced trading, resulting in the same tax treatment now for all related party goodwill disposals. As is normally the case with tax, the devil is in the detail, so specialist advice is imperative.

Is this the end?

There is no question that these two measures have reduced the tax benefits associated with goodwill, unless there is a sale to an unconnected limited company.

There are other reliefs available such that the capital gains tax liability on incorporation could be avoided, but these will generally not result in the creation of a loan account. However, with corporation tax rates reducing over the past few years (down to 20% for all companies from April 2015) and with no income tax or national insurance due on dividends paid out up to the basic rate band (currently £42,385) the on-going savings may still make incorporation worthwhile, depending on the specific circumstances of the practice and individuals involved.

In addition, other chargeable assets transferred into the business as part of the incorporation, such as property, are still eligible for the 10% tax rate. Stamp Duty Land Tax (SDLT) may also be mitigated by partnerships on incorporation, if the property is transferred in to the new company and not retained personally. Transfers

of property by a sole trader would prove less attractive as SDLT would likely apply.

What will HMRC look at?

If incorporation is still a viable option for you, it is important to ensure the correct paperwork is in place. Recently, HMRC has become more focussed on practice incorporations and there are standard questions they will ask. We know what these questions are and can help you get the correct documentation in place so, if there is an enquiry it can be dealt with as quickly as possible.

Conclusion

In conclusion, tax on incorporations can still be minimised if structured correctly and may continue to offer on-going benefits to the owners. Practices still operating as a sole trader or partnership should, therefore, not write off incorporation as a future option to run the business just yet. However, there are many other factors to consider and advice from a specialist dental accountant is essential.

The end of the tax return is nigh

Following speculation already breaking before the Chancellor's speech began, George Osborne made the headline statement that the annual tax return will be abolished, rounding off this statement with confirmation that the transition would start next year.

However, before we could book our skiing holidays for January, HMRC released what would be best described as their sales brochure, complete with a foreword from David Gauke MP, explaining that during 2016, five million small businesses, along with 10 million individuals, will have access to their own on-line tax account with HMRC.

.....
“The document promises that all users will have a tailored experience, including access to all taxes affecting them, the ability to pay taxes as they go and make single payments across all their tax liabilities, no matter what their source (PAYE, income tax etc.).”
.....

Importantly, the on-line account will include details of all the information which HMRC already have at their disposal, even where provided by third parties, giving the user an up to date and "dynamic" experience of their tax affairs. Users will even be able to upload details from their own accounting systems or provide further information, unknown to HMRC.



The proposal to consolidate all information held by HMRC in one easy to access place is welcome, but we operate in a regime of self-assessment, where the taxpayer calculates their own taxes (or appoints an expert to do it for them). Quite how this on-line platform gives the taxpayer the opportunity to interact with

omissions or errors is yet to be published. Before we pack our bags ready for an easy January we await the consultation, to be released later in the year, as to how this will be implemented and whether the annual tax return will truly be consigned to history.

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 2014.

The latest statistics show that overall profits are up, principally driven by increases in fee income. Whilst costs of sales have also increased, administrative expenses have been kept under control.

Here are some of the key figures:

- NHS average net profit per principal up by 2.8% to £129,054
- Private average net profit per principal up by 5.3% to £130,613
- Average NHS practice turnover up by 1.7%
- Average private practice turnover up by 6.6%

.....
“For the first time since 2004/05 a typical private practice's profit is greater than an NHS practice.”

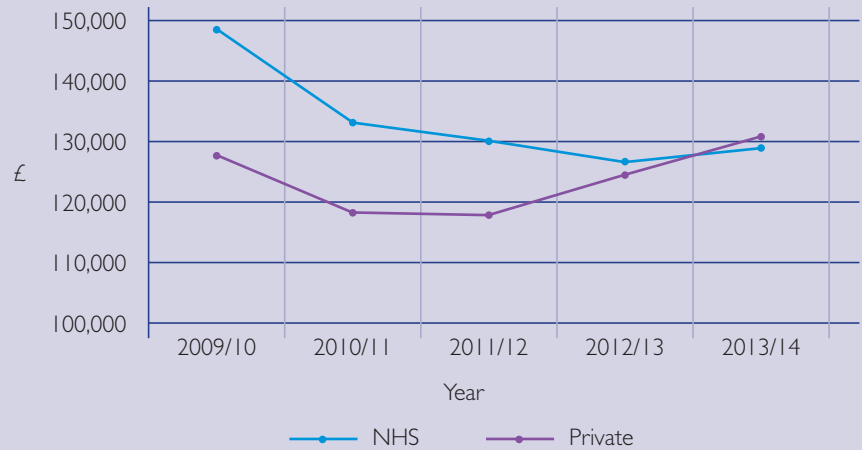
Associates have also seen growth, with turnover increasing by 2.3% to £83,311 and profit increasing by 1.1% to £68,544.

How is your business structured?

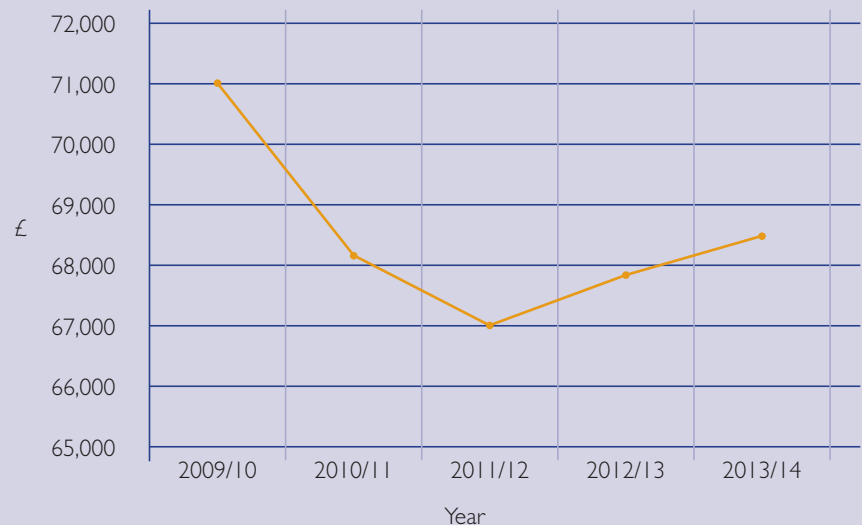
With the majority of practices operating as sole traders, have you considered whether your practice would benefit from incorporation? This is a complex area with many factors to consider and it is important to seek advice from a specialist dental accountant. A periodic review of your circumstances and longer term goals is sensible, so please get in touch if this is of interest.

The statistics show few dental associates trade through a limited company. One key issue is that associates are not eligible to be members of the NHS pension scheme if they are performing NHS work for a practice through their own limited company.

Practice Profit per Principal

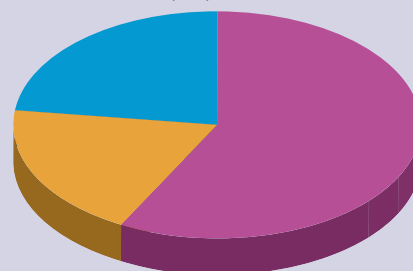


Associate Profit



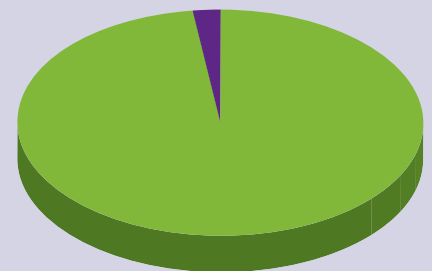
Practice Structures 2013/14

- Sole Trader
- Partnership
- Limited Company



Associate Structures 2013/14

- Sole Trader
- Limited Company



55% death tax abolished

PENSION

What has changed?

Previously, it was only possible to pass a pension on as a tax free lump sum if you died before the age of 75 and you had not taken any tax free cash or income. Otherwise, any lump sum paid from the fund was subject to a 55% tax charge. From April 2015 this has changed and this automatic tax charge has been abolished. The tax treatment of any pension you pass on will depend on your age when you die.

If you die before age 75 your beneficiaries can take the whole pension fund as a tax free lump sum or draw an income from it, also tax free, either by using income drawdown or by choosing to buy an annuity.

If you die after age 75 your beneficiaries have three options:

1. Take the whole fund as cash in one go. The pension fund will be subject to 45% tax, however, it has been proposed that this should be changed from 2016/17 to the

beneficiaries' marginal rate of income tax.

2. Take a regular income through an annuity or income drawdown. The income will be subject to income tax at your beneficiaries' marginal rate.
3. Take periodical lump sums through income drawdown. The lump sum payments will be treated as income, so subject to income tax at your beneficiaries' marginal rate.

Who will be affected?

Anybody who has a defined contribution pension, e.g. individual, group personal or stakeholder pensions, Self Invested Personal Pensions and Additional Voluntary Contribution schemes will all be affected.

What we say

The good news on pensions just keeps on coming. The abolition of the draconian 55%

pension death tax, together with flexible access to pensions from age 55, means that rigid pensions are a thing of the past.

.....
“A number of changes have been introduced from April 2015 and with the right advice pension planning can be beneficial to you and your beneficiaries.”
.....

Pensions can now offer possibilities to grow a fund in a tax free environment, having obtained a 40% tax deduction on the contributions, then being taxed at only 20% on withdrawal.

Our in-house Financial Planning team can provide independent financial advice. If you have any questions about pensions please contact Gary Cook at Hazlewoods Financial Planning on 01242 680000.

The single-tier pension

The single-tier pension will be introduced on 6 April 2016 and will apply to anyone reaching State pension age on or after that date, that is:

- men born after 5 April 1951; and
- women born after 5 April 1953.

Any State pension entitlement accrued in the years before the implementation of the single-tier pension will be recognised when establishing an individual's single-tier pension entitlement.

Anyone who reaches State pension age before 6 April 2016 will continue to receive their State pension in line with the current rules.

Calculating the single-tier pension

The full weekly rate of single-tier pension payable from 6 April 2016 will be set at a level just above the basic level of means tested support. £144 a week (in 2012/13 terms) was

used in the Government's White Paper for illustration purposes.

Under the new rules, an individual will need 35 qualifying years of National Insurance contributions (NICs) or credits to get the full weekly rate of single-tier pension. This is five qualifying years more than currently required to get the full basic State pension.

There's also a minimum. To get any single-tier pension at all you'll need at least 10 qualifying years. This is a big increase from the current minimum of just one qualifying year under the existing State pension rules.

.....
“Anyone with between 10 and 35 qualifying years will get a proportionate amount of single-tier pension.”
.....



Those who started their working life before 6 April 2016 may, of course, have built up some State pension entitlement already - this is protected by calculating a "foundation amount".

Spouses' pensions

The single-tier pension has been designed to ensure that, in the long term, the majority of people will be able to get the full single-tier in their own right. Eventually, the single-tier pension will purely be based on an individual's own record of National Insurance contributions and credits.

Further information is available on our website.

Annual Investment Allowance - a case of wait and see

At present, the Annual Investment Allowance (AIA) is set to reduce from £500,000 to £25,000 per annum from 1 January 2016. The AIA provides a 100% deduction against taxable profits in the year of purchase on qualifying capital expenditure, which includes plant and machinery, certain fixtures and fittings and commercial vehicles, up to the annual limit.

Where a business spends more than the annual limit on qualifying items, tax relief is still available but at a lower rate of either 8% or 18% per annum, dependent on the type of expenditure.

In the Budget the Chancellor commented that a reduction to £25,000 would be unacceptable but deferred making a decision on what the limit should be until the next Autumn Statement. This leaves things up in the air for businesses intending to make significant capital expenditure in the next 12 months.

The AIA is pro-rated for accounting periods ending after 31 December 2015 and therefore some businesses may already be in an accounting period where the available AIA is potentially less than £500,000. To illustrate, for a business with a year end of 31 March 2016 the total AIA available will be £381,250.

However, if no expenditure is incurred before 31 December 2015 then the maximum available AIA will be £25,000.

tax purposes is the date that the asset is brought into use.”

“Please also remember that if any expenditure is financed by hire purchase the acquisition date for

If you are planning any significant capital expenditure or property renovations and think that you might be affected by this, please get in touch for further advice.



Superannuation contributions

Superannuation rates have now been fixed for a four year period from 1 April 2015 to 31 March 2019. Other than a minor adjustment to a couple of tier bands, the rates are the same as for 2014/15.

Tax relief is available on the contributions paid. The calculation of net pensionable earnings (NPE) often causes confusion. Guidance for calculating NPE is available and if you would like a copy please do not hesitate to get in touch.

What benefits are available?

NHS dentists arguably have the best of both worlds, being self-employed from a tax perspective yet treated as employees for some aspects. As well as the pension benefits accruing from the NHS pension scheme, the following are available:

- Sick pay

Tier	2015/16 to 2018/19 pensionable earnings	2015/16 to 2018/19 contribution rate
1	Up to £15,431.99	5%
2	£15,432.00 to £21,477.99	5.6%
3	£21,478.00 to £26,823.99	7.1%
4	£26,824.00 to £47,845.99	9.3%
5	£47,846.00 to £70,630.99	12.5%
6	£70,631.00 to £111,376.99	13.5%
7	£111,377.00 and above	14.5%

- Maternity pay
- Paternity pay
- Death in service lump sum
- Survivor benefits

The above are all based on NPE, so it is

important to ensure you are declaring the correct level of earnings.

If you have any queries about pensions our colleagues in Hazlewoods Financial Planning LLP will be happy to help.

NHS dental prototypes

A new dental contract has been on the cards since 2011 and it has now reached the prototype stage. This is where whole versions of a possible new system are being tested, rather than parts of it, as was the case for the pilots.

There are three key elements to the new approach:

- Guidance on care
- Measurement of the quality of care
- Remuneration which supports continuing care and prevention as well as activity

All of the prototypes will be able to over deliver by 2%, however 10% of the contract value is at risk if there is under delivery.

The prototypes have two elements of remuneration, a capitation element and an activity element. The capitation element is based on a specified minimum number of capitated patients, with remuneration reduced if numbers are lower. The activity element works on a similar basis, with remuneration adjusted if activity levels fall below the target.



In addition, there will be a quality remuneration adjustment based on performance compared to the Dental Quality and Outcomes Framework (DQOF).

Two 'blends' of remuneration are being tested in the prototypes. Blend A uses capitation as the basis of remuneration for oral health reviews and preventative care (current Band 1 care), with activity payments used for all treatments (current Band 2 and Band 3 care).

Blend B uses capitation as the basis for current Band 1 and Band 2 care, with activity payments for more complex treatment in the current Band 3.

The next steps

Department of Health guidance states that if the prototypes are successful the final 'blend' could be decided in 2017/18. It is anticipated that there will then be a gradual roll out of the new contract.

Further tightening of Entrepreneurs' Relief rules

Entrepreneurs' Relief applies a reduced Capital Gains Tax rate of 10% to capital gains on certain eligible business assets, subject to a lifetime limit of £10m of gains. The main rate of Capital Gains Tax is now 28% and therefore Entrepreneurs' Relief can be extremely valuable to individuals disposing of qualifying business assets.

The December 2014 Autumn Statement included the unexpected announcement that the disposal of goodwill to a close company related to the vendor would no longer qualify for Entrepreneurs' Relief (see "An end to HMRC's goodwill on incorporation" article). The Chancellor has announced another two measures that further restrict the availability of Entrepreneurs' Relief on disposals of business assets in certain cases, increasing the tax payable on such disposals from 10% to the main rate of 28%.

Associated disposals must accompany a 'significant' withdrawal from a business

The first measure tightens the rules on claims to Entrepreneurs' Relief in respect of disposals of assets held personally by an individual, but used in the trade of their partnership or company. Subject to certain conditions, it is possible to claim the 10% Entrepreneurs' Relief rate of tax on such disposals, where they are associated with a full or partial withdrawal from the business itself. Withdrawal from the business was not previously defined, leaving open the possibility of a claim for Entrepreneurs' Relief on asset disposals at the same time as a very small

reduction to an individual's shareholding or partnership share.

To ensure that Entrepreneurs' Relief is only available where an individual has genuinely withdrawn from a business, it is now only available on disposals of personally held assets where they accompany a disposal of at least a 5% shareholding in a company or at least a 5% share in the assets of a partnership.

Clampdown on corporate partners

The second measure aims to restrict Entrepreneurs' Relief to those with a genuine stake in a trading business and prevents claims to the relief in respect of gains on shares in certain companies which invest in joint venture companies, or which are members of partnerships. Shares in normal trading companies should not be affected.

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Services

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. Our dental team is based at our Staverton office.

- 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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