



Incorporation of Medical Practices

In recent years various changes in tax legislation have increased the tax cost for individuals. Combined with the reduction in personal pension funding reliefs, the burden of personal taxation for individuals has increased. With personal Tax rates of up to 55% as opposed to a low rate of corporation tax of 12.5% the attractions of operating through a company is obvious.

Currently most medical practitioners operate in a personal capacity or as partners in a medical practice. Consequently their income is subject to Income Tax at rates of up to 55%. Over the last four years the reliefs that an individual could claim to reduce their taxable income, and ultimately their tax liabilities, has been significantly reduced. With the reduction in the earnings cap for personal pension contributions the ability for medical practitioners to pension fund in a tax efficient manner has also been greatly reduced.

With further changes expected for both taxation and pension reliefs, individual's annual tax liabilities are expected to rise. Many medical practitioners have availed of the option of incorporation of their private practices as it can offer a number of advantages.

It is important to understand that as each individual's personal circumstances are different, incorporation may not suit all individuals. It is also important therefore that any decision is not taken lightly and that proper professional advice is obtained in relation to all the aspects of incorporation, some of which are outlined below.

Corporation Tax

An Irish company is liable to Corporation Tax on its profits. Whilst there are many similarities in the calculation of taxable profits under income tax and corporation tax rules, the rates and administration requirements are different. In addition companies can offer greater tax planning opportunities both on incorporation and on dissolution.

Irish companies are liable to corporation tax at a rate of 12.5% on their trading profits. When compared to the personal tax rates of 55% there is a significant difference. However, where the company retains its profits the profit is subject to an additional surcharge. Irish companies that are controlled by five or fewer participators are known as "close companies". Under Irish tax legislation close companies are liable to a surcharge on their undistributed income with the result that the effective rate of corporation tax for trading profits retained by the company is circa 19%. However even when the surcharge applies there is still a substantial differential between the corporation tax rate and personal tax rates.

Where a company invests surplus funds then it is liable to corporation tax at 25% on any non trading income. For close companies there is also a surcharge that will apply which would give an effective rate of corporation tax on such non trading income of 40%.

Increased cash flow

Taking a 19% effective rate of corporation tax on trading profits in a company as opposed to paying up to 55% on personal profits there is a tax saving of €3,600 for every €10,000 of profit earned and retained by a company. Where the company uses these profits for pension funding there is essentially a tax saving of €5,500 for every €10,000 pension contribution.

With the lower rates of corporation tax it is clear that the level of after-tax profits that a company can retain is significantly higher than that of an individual. This gives the company greater opportunities to utilise its after tax income for working capital/debt management or to pension fund, invest, etc.

The use of companies to acquire property and assets can be a useful strategy as it can greatly reduce the personal cash requirement for an individual. This can be particularly advantageous where there is goodwill attached to a practice. As a company will have less tax on its trading profits its ability to pay for the asset or repay the capital element of borrowings is significantly greater than for an individual.

Income from Company

Whilst the company may carry on a trade it is important to remember that it is the individual who has to be registered as a medical practitioner with the Medical Council and not the company. However the income earned by the company belongs to the company and any funds taken by the owners from the company would be taxed in the owner's hands.

Where funds are extracted from the company the nature of the payment to the owners will determine the tax treatment of the income. For example on incorporation of a business where assets are sold to the company then the payment by the company to the individual for these assets can be subject to Capital Gains Tax at the rate of 25% where the amount paid is in excess of original cost of the assets. Similarly on the dissolution of the company any retained income available to the shareholders would be subject to Capital Gains Tax.

Whilst Capital Gains Tax can arise on transactions connected with both the incorporation and dissolution of a company it can be significantly reduced where "retirement relief" can be claimed. In broad terms retirement relief is a relief given to an individual on the disposal of all or part of the qualifying assets of their business, provided they are aged fifty-five years or more at the date of disposal. It should be noted that it is not necessary to retire in order to claim this relief.

Where salary is paid then the company must operate payroll taxes on the salary. It is important therefore where you carry on your trade through a company that you identify annual income requirements so that the salary paid by the company is sufficient to meet this. Any remaining income can then be retained by the company for alternative uses.

Pension Planning

Companies can offer individuals the ability to avail of enhanced pension funding opportunities. The level of pension funding available to individuals is now restricted based on an earnings cap, currently

€115,000. However employers' contributions are not subject to the same cap. Therefore through the use of a corporate structure an individual becomes an employee of their own company which gives them significant enhanced pension opportunities. Pension funding will depend on various factors such as age, income levels, salary, position, etc and therefore needs to be considered carefully.

Company Law

When a company is registered with the Irish Companies Registration Office it takes on its own separate personality in law distinct from that of its shareholders. The company becomes a separate legal entity that has rights, obligations and duties that are different from those of its owners.

Whilst the shareholders are the owners of a company it is the directors who are charged with the task of managing the company. In Ireland most private companies are owner managed so that the shareholders and directors are the same people. Directors of all companies have duties and responsibilities and therefore it is important that each director is aware of his duties and responsibilities.

Conclusion

The incorporation of a private medical practice can achieve tax savings and provide better planning opportunities in relation to pension planning, retirement relief and working capital/debt management. The optimum structure will depend on what you want to achieve from incorporation.

It is possible to organise your affairs such that some activities of a private medical practice may be dealt with through a company and therefore it is important that a review is undertaken to ensure that any activities that should not be incorporated are retained personally.

DHKN is the leading advisor to Medical Consultants in Ireland. We pride ourselves on our professionalism in this specialist area. We are to the forefront in relation to the efficient Incorporation of Medical Practices. Our dedicated medical practice team is Partner led bringing a wealth of experience and practical solutions to our clients. This enables DHKN to work closely and deliver a high quality, professional service.

This article is intended for information purposes only and looks at some of the aspects of incorporation. Professional advice should be sought before acting on any issue covered in the article.

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