The incorporation process

Michael Lansdell aims to answer the basic questions about incorporation that all dentists operating as sole traders or in a partnership should be asking.

Ev er since the General Dental Council (GDC) amended the regulations to allow dentists to trade through limited companies from July 2006, the issue has been clouded with speculation and misinformation that has deterred many practitioners from investigating the possibilities.

While it’s true that incorporation will not suit every practice, the decision should at least be made in full knowledge of the facts. Individual practice circumstances vary widely, and objective, professional advice should always be sought before a change of status is contemplated. This article is dedicated to answering the basic questions about incorporation that all dentists operating as sole traders or within a partnership should be asking.

What is incorporation?

Incorporation is the process that transfers the ownership of an existing sole trader dental practice or partnership to a limited company (usually newly formed). Incorporation is now an option for practice principals and partners, and also for self-employed associates.

What is a limited company?

A limited company is a separate legal entity, with its own legal identity, which is owned by one or more shareholders and managed by one or more directors. In a sole trader or a partnership, both ownership and management vest in the sole trader or partners.

What does ‘limited’ mean?

Assuming the company has not traded fraudulently or recklessly, and the directors or shareholders have not given creditors any personal guarantees, their liability for the company’s debts is limited to their original investment in the company. This is usually a nominal sum between £1 and £1,000.

Are there any special rules for dental practices?

Yes. The GDC requires that a majority of the directors in a dental practice limited company are registered with the GDC, but there is no GDC restriction on who can be a shareholder.

How will I be paid?

Directors in a limited company may become employees and be paid a salary as well as receiving both taxable and tax-free benefits. Taxable benefits could include private medical insurance, a company car, and pension contributions (within certain limits) include child care vouchers and pension contributions.

Shareholders in a limited company receive dividends, which represent their share of some or all of the company’s net profit after Corporation Tax has been paid.

How does the limited company work?

Because it is a separate legal entity, the company has its own bank accounts, assets and liabilities, employs staff in its own name and enters into contracts in its own name.

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Some limited companies have a company secretary who is responsible for keeping the statutory records of the company up to date and filing fiscal returns. In smaller companies, such as dental practices, these duties are usually carried out by the practice’s accountants.

How do I convert my sole trader business or partnership to a limited company?

1) Set up a new limited company at Companies House (usually done by accountants), with you and any partners as director(s) and shareholder(s). The share- holders can also include any one else involved in the business, family members for example.

2) Open a bank account in the name of the new company.

3) Sell your practice assets and goodwill to the new company (freehold land and buildings are usually excluded) using a sale agreement prepared by a solicitor. Capital Gains Tax, normally 10 per cent, is payable on any profit on the original practice purchase price.

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5) Decide whether the limited company should immediately borrow the money to pay you for the practice, enabling you to repay non-tax-deductible personal debts, a mortgage on your home for example; or maintain a loan due to you, which can be drawn on free of tax until it is paid off to defray your nor- mal living expenses. If you choose deferred payments, the terms should form part of the sale agreement.

6) All your existing contracts, including PCT contracts, should be transferred into the name of the new company; PAYE registrations should be reeregistered to the new company; and direct debit and standing orders switched to its bank account.

7) You have now ceased trading as a sole trader, and your practice is trading as a limited company.

Of course, this is only a brief summary of the incorporation process and cannot take into account individual practice differ- ences. As we stated at the outset, a limited company may not be the ideal trading vehicle for every- body, and the value of professional advice cannot be overstated, but for those who do choose this route, the mechanics of con- version are straightforward. In later articles we shall be assess- ing the potential benefits.