A cautionary tale

Ray Goodman discusses incorporating dental practices

In many cases, the practices were not using specialist dental lawyers or accountants. This was leading to incorporations, which may or may not have been properly conceived, being improperly executed. The necessary documentation was not being put in place to enable challenges from HMRC to be defended robustly and to avoid problems on sale or retirement further down the line.

Inevitably, we are now beginning to see the problems caused by such incorporations raise their head increasingly more frequently. The following case, that we have just completed after 11 months of difficult legal wrangling, is a case in point.

We were instructed to act for a buyer on the purchase of an NHS practice. So far as our client knew she was buying the goodwill, fixtures and fittings in the normal way. It was only when we received information back from the due diligence enquiries that we realised the seller had incorporated some 12 months earlier. The seller’s solicitor was not a dental lawyer and thus hadn’t realised the problems that flowed from the incorporation until we pointed them out.

The seller had two practices, one NHS and one private, and also a dental laboratory. All of these were transferred into the limited company on incorporation. The relevant PCT, having been persuaded to allow the principal to transfer his contract into the limited company on incorporation, was not inclined to allow any further transfer of the contract. As things stood the NHS practice within the limited company could not be transferred.

A transfer utilising the partnership provisions often used to enable GDS Contracts to be transferred is not available where one party is a limited company, as the drafting of the GDS regulations precludes partnerships between companies and individuals.

The only strategy to enable this contract to be sold involved all of the assets in the limited company, other than the practice to be sold to our client, being transferred out of the company to a new company. This involved significant additional cost, time and stress. As a result of the continuing potential risks to the buyer, it was necessary for the seller to discharge all debts of the business on completion, to have a significant proportion of the sale price held back by way of a retention against future claims, and to incur the further cost of preparing additional sets of accounts in able to ascertain the true balance sheet position on completion.

As a direct result of the lack of foresight on incorporating the practice both the seller and the buyer were subjected to a lengthy period of stress. The sellers were forced into a situation whereby they had to discharge all debt relating to their business, when they otherwise would not have wished to, and the legal and accountancy costs were increased significantly from what they would have been, had the practice not incorporated or been incorporated into a separate company from the other practice and laboratory.

Incorporation can, in the right circumstances, be highly beneficial to a practice. However, there are consequences other than tax saving. It is essential that before making the decision to incorporate, legal and accounting advice from dental expert lawyers and accountants is taken and that the incorporation is properly documented with all ancillary issues dealt with to avoid significant problems in the future.

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