FUNDING YOUR SURGERY PREMISES

To buy or to lease your surgery premises? In the third article in his series on financial management, accountant Ian Tongue discusses the pros and cons of each approach

The modern GP practice faces a variety of options when it comes to funding the surgery premises. In the past, GPs normally owned the premises in proportion to profit share. Now, many GPs are not property owners even though they are partners.

The influx of private money into primary care has created fresh opportunities for funding surgery premises that are treated differently from an accounting and taxation perspective.

Why buy?

Buying a share in a surgery has historically been the most common approach, with many partnership agreements requiring new partners to buy out a retiring or leaving partner.

This is still very common. But it can act as a barrier for new entrants, as many GPs nowadays are looking for flexibility. It is not unusual for retiring GPs to retain their ownership of the surgery and receive rent, which is treated as a cost to the practice.

Where a surgery comprises propertyowning and non-property owning equity partners, adjustments are made in the accounts to accommodate this. This would be focused on identifying the income and expenditure streams attributable to the property and making a first division of profit.

Where a change to the norm is made in a practice, it is worth updating the partnership agreement accordingly. Some partnership agreements also have restrictive covenants for continued GP surgery use or specific methods of valuation. A review of these items can sometimes benefit the equity-owning partners and should be considered. It may increase the value of the premises.

The main benefits of purchasing are:

- capital growth
- purchase is usually 'self-funding' from notional/cost rent
- creates a 'nest egg' upon retirement
- GPs have control of the building
- potential for joint arrangements such as an on-site pharmacy or other primary care services.

Disadvantages are:

- lack of flexibility
- responsibility for upkeep
- capital growth is not usually as high as other investments because of the specialised nature of the property.

The recent changes to capital gains tax are also an important consideration. Previously, most GPs selling their share of the surgery premises would have paid little or no capital gains tax. The reason for this was that the share of the surgery was regarded as a business asset and given beneficial capital gains tax relief based on the length of ownership. From 6 April 2008, this relief is to be withdrawn for individuals. It will be replaced by a single rate of capital gains tax of 18%. According to the initial proposed changes, GPs who have owned their share of the surgery for many years will be worse off, in many cases by several thousands of pounds.

However, there may be light at the end of the tunnel as the Government appears to be bowing to pressure and may introduce a form of 'retirement relief'. Details are sketchy at present and have not been formally announced, but the expectation is that somewhere in the region of £100,000 of tax-free gain may be exempted from capital gains tax upon retirement for qualifying disposals. Your accountant should keep you up to date with developments in this area.

Why lease?

Leasing allows GPs more flexibility and is commonly the method adopted when private funding is being introduced.

'Leasing' is another term for renting a property and a long-term agreement is usually required, typically 10 to15 years. The surgery premises do not belong to the partners and the rent paid is usually recorded as an expense in the surgery accounts.

Frequently, GP practices are required to make a significant capital contribution to the new surgery. This is usually recorded as a contribution towards fixtures and fittings but could be as an upfront lease rental, commonly known as a lease premium.

Care must be taken to understand the nature of any payments made, as the accounting and tax treatment is very different. Your accountant will be able to advise you further in this area.

The main benefits of leasing are:

- greater flexibility
- premises are usually purpose-built or heavily bespoke
- lease rentals should be met by notional rent received
- GP tenants are not usually responsible for the upkeep of the building itself
- cost is allowed as an expense in the accounts
- if sharing premises, GPs should experience cost savings.

Disadvantages of leasing are:

- GPs do not own anything other than the fixtures and fittings
- lease commitment may be long
- GPs don't share in any capital growth of the premises
- the premises will be subject to periodic rent reviews
- the landlord may not act in the best interests of the practice
- there can be no direct benefit from joint arrangements with, for instance, a pharmacy or dentist
- possible problems of sharing premises with other surgeries.

In some new-build properties, the PCT may seek the practice to be VAT-registered as this may have some cash-flow advantages for the PCT. Before doing this, seek specialist advice.

Where a PCT or private investor is bringing together primary service providers, they can sometimes require the GP surgery to hold the main lease, known as the 'head lease'. The holder of the head lease would sub-let to the other service providers. This should be considered carefully as it may adversely affect cash flow.

Stamp duty can be significant on new leases and is dependent on the rent paid and the rental period. Your accountant will advise you on this area.

Where a lease is taken out, it should be ensured that the lease accommodates changes in the partnership, otherwise one person could ultimately be responsible for the lease after everyone has retired. Your solicitor will be able to advise how best to go about this.

Ultimately, each GP practice will face very different factors in deciding how to fund the surgery premises. There are several options and they should be discussed further with your professional advisers to determine the most suitable option.

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