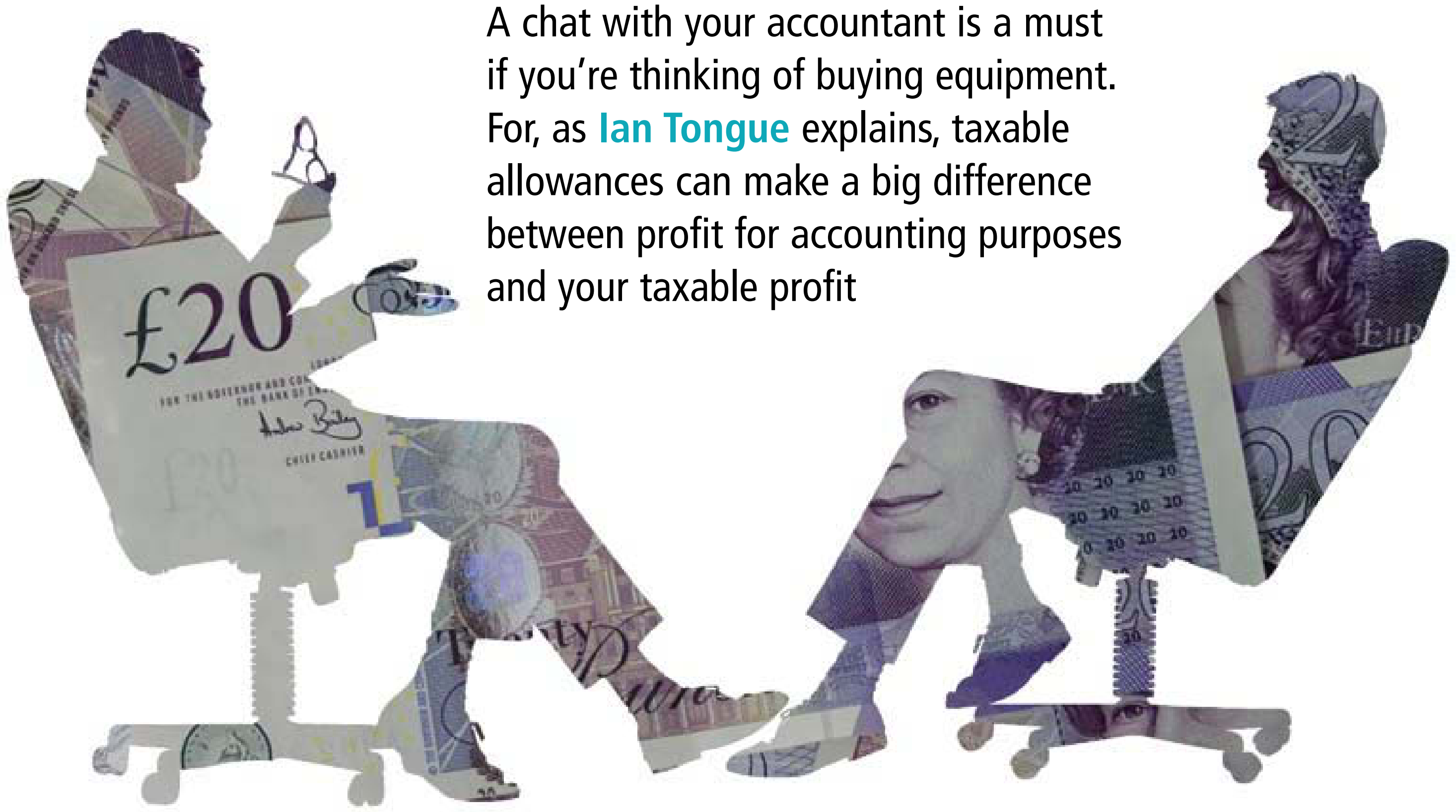
STARTING A PRIVATE PRACTICE

Making allowances

A chat with your accountant is a must if you're thinking of buying equipment. For, as **Ian Tongue** explains, taxable allowances can make a big difference between profit for accounting purposes and your taxable profit



CAPITAL ALLOWANCES are often referred to as the tax form of depreciation. While there are similarities, the application of capital allowances is very different to the accounting depreciation you will see in your private practice accounts.

Unlike accounting depreciation, tax relief is available on capital allowances and this can be a benefit to a doctor who is buying capital items, such as medical equipment.

Capital allowances are a tax allowance for the purchase of capital items and do not relate to the day-to-day running cost-type expenditure.

The idea of both a depreciation charge and capital allowance is to spread the cost, because a capital asset usually will derive economic benefits over a number of years.

However, for many years the Government has been encouraging capital investment by offering generous allowances for the purchase of certain capital assets.

This inevitably leads to a difference between the depreciation expense in your accounts and the capital allowance claim made.

When preparing your computation of tax, your accountant will add back the depreciation expense and claim capital allowances. So there can be a significant difference between your profit for accounting purposes and your taxable profit.

What qualifies?

The most common types of expenditure that most independent practitioners engaging in private practice will come across relate to 'plant and machinery' and privately-owned 'motor vehicles'.

However, those that may have bought or leased premises are likely to have incurred expenditure integral to the building or on long-life assets which also attract allowances, albeit at differing rates due to their usual long-term nature.

In practice, the term 'plant and machinery' would cover medical equipment and most fixtures and fittings.

How much is the allowance?

This depends on the level of capital expenditure in the year. At the time of writing, there is a generous allowance available known as the 'Annual Investment Allowance' or AIA for short. This provides a 100% allowance in the year of purchase for the first £100,000 of expenditure on plant and machinery. But this allowance is not applicable to cars. And it was announced in last month's Budget that this £100,000 will fall to £25,000 in April 2012.

Once the £100,000 has been used up, the rate reverts to the standard rate known as the 'writing down allowance' which is currently 20% on a reducing balance basis. The Chancellor announced in his Budget that this will change to 18% in April 2012.

The best way to view the AIA is that it is an acceleration of the tax relief that you would have received over the life of the asset to the year of purchase. This can be helpful from a cash flow perspective, but there is obviously going to be a delay between purchase and seeing the benefit of the tax relief.

The capital allowance rate for long-life assets or integral fixtures is 10% on a reducing balance basis, but this will drop to 8% in April 2012 as a result of the Budget.

Investing in capital expenditure attracting the AIA can be of particular benefit now following the 50% tax rate introduced on 6 April 2010.

For example, a doctor purchasing medical equipment of £30,000 would be given capital allowances of £30,000, thereby reducing their tax liability (including National Insurance) by £15,300 for a 50% taxpayer or £12,300 for a 40% taxpayer.

Tax relief on cars

The quick answer for most consultants is not a great deal. Motor and travel claims are heavily under fire at the moment, as reported in recent issues of *Independent Practitioner Today*, and therefore any capital allowances available are restricted to the business use element only. Therefore, while the initial relief may seem high, in real terms it is restricted to a much lower amount.

Capital allowances on vehicles are now based on the CO_2 emissions, with less polluting cars attracting more tax relief. Care must be exercised when choosing a vehicle with one eye on the tax relief available, as you may be left with a car which you did not want or depreciates faster – and that will ultimately cost you more.

The rates for vehicles purchased on or after 6 April 2009 are:

- Cars with CO_2 emissions up to 110g/km: **100% (one off)**
- Cars with CO_2 emissions between 110 and 160g/km: **20% p.a.**
- Cars with CO_2 emissions over 160g/km: **10% (a year)**

Cars bought on or before 5 April 2009 attract annual capital allowances of 20% subject to a maximum of £3,000.

The actual capital allowances claim made for the above vehicle rates are scaled back for private use.

Usually, the vehicle is privately owned which results in a 'balancing allowance' should the above rates not be sufficient come resale time. However, this works both ways and some tax relief may have to be paid back known as a 'balancing charge' if the tax written down value is less than the sale price on resale. This is an important consideration if buying a low-emission vehicle, as some of the initial benefit may have to be paid back.

It is worth noting that leased cars do not attract capital allowances. But the lease rentals can be treated as an expense subject to a restriction for private use and a 15% reduction if the car's emissions are greater than 160g/km.

The above rates also apply to companies, but the private use element restriction is removed to be replaced by a 'benefit in kind'. Again, this is emissions-based and results in an income tax charge on the individual using the vehicle.

If you are trading as a limited company, you should discuss this area with your accountant in more detail.

Timing of purchase

This can be an important consideration. Your accounting year-end could end on any month and therefore the timing of asset purchases can lead to tax relief being enjoyed earlier or spread. You should discuss your individual circumstances with your accountant.

Capital expenditure of various types attracts differing forms of tax relief. Discussing your plans with your accountant before you commit to purchase is important to ensure you are aware of the tax relief available and timing of the benefit.

With the introduction of the 50% tax rate, now might be a good time to consider investing in capital.

■ **Next time: Choosing an accounting year-end**

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