

STARTING A PRIVATE PRACTICE

Winning the tax game

Tax doesn't have to be taxing. **Martin Murray** explains what you need to know

STARTING A PRIVATE practice means you now run a new self-employed business, so tax is not deducted at source through PAYE as with NHS employment.

Financial accounts are the starting point for calculating what tax is to be paid. They are a summary of income less expenditure. The net figure is profit.

But special rules are applied by the accountancy bodies and the taxman to calculate what is income and what is allowable as expenditure.

Basically, income is anything earned in the private practice which has not suffered tax at source. Note that I said 'earned' and not 'what has been paid'.

This difference is important, as HM Revenue and Customs (HMRC) taxes the self-employed on what is earned – or in other words billed – as opposed to what is paid in any financial year. At the year-end there may be patients who have not paid, but you must pay tax on what they have been billed for.

This seems unfair. But this apparent travesty of justice is alleviated by what can be claimed as non-taxable expenses against income.

An employed NHS consultant can only claim an expense against income for tax provided it was 'wholly, exclusively and necessarily' incurred in respect of that employment. This means the inspector of taxes can mostly argue successfully that an expense was not 'necessarily' incurred.

He may say the NHS employer should have provided the computer equipment, if it was so necessary for the job, and the books could have been obtained from the library.

But for the self-employed the requirement to prove an expense

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was 'necessarily' incurred is dispensed with. Expensive equipment can be bought within reason, provided it has some use in the practice. This is good, as it greatly expands what can be claimed against income and ultimately cuts the tax you pay.

Pre-trading

What is often missed by new consultants and their accountants is the fact that expenses on certain items incurred before the private practice commenced can be claimed as if they were spent on the first day of the business. This can even relate to items bought several years before starting up.

The most common type of expenses are computers/laptops and surgical glasses. A restriction takes account that they will have diminished in value from when bought until their ultimate use in the private practice.

Year-ends

Most consultants believe accounts must be prepared to a 5 April year-end to be co-terminus with the fiscal year. They and their accountants miss the fact that accounts can be prepared to any year-end.

HMRC normally seeks to tax a 12-month period, but this year can, within certain parameters, be chosen by the consultant. Take,

for example, two consultants who have year-ends that differ only by 25 days. What are the consequences for each?

The first consultant A has a year-end of 5 April 2008 and his colleague B has a year-end of 30 April 2008. The main difference is that A will pay tax on his income in the tax year 2007-08, whereas B will pay his/her tax in the tax year 2008-09.

This is important as, in the first three to four years, income rises sharply in the new private practice and the choice of year-ends can reduce and delay the tax payment. The choice of year-ends also allows one to be forewarned of any large tax payments and to plan appropriately.

Tax payment dates

The NHS deducts tax by PAYE on behalf of the Revenue. Consultants

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with private practices must pay it to the taxman themselves. This sounds simple, but there are pitfalls for the unwary.

Take, for example, a consultant with a tax bill of £20,000 for 2006-07 and £30,000 for 2007-08. The way HMRC collects the tax – on 31 January and 31 July together with a balancing payment the following January – means that the tax payment at 31 January 2009 will be £25,000 followed by a payment on 31 July 2009 of £15,000. For the unwary consultant this can be financially distressing, to say the least, if he has not been forewarned.

Revenue inquiries

If anything in this world can be guaranteed it is that the majority of consultants will be selected for a HMRC inquiry. This is because the Revenue finds it unusual for

someone to be employed and self-employed, and earnings from both sources can be large.

Fortunately, most inquiries are straightforward and sorted reasonably quickly. Most accountants run an insurance scheme to cover any additional accountancy and legal costs. These policies are relatively inexpensive in comparison to a full-blown inquiry.

In the brave new world of self-employed private practice it is best to sit down with your accountant to go through all aspects personally to you, not just the main points detailed above. ■

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READER PROMOTION

Plan here for a comfortable retirement

Consultants get excellent benefits from the NHS Pension Scheme, but it takes no account of private earnings. So you should seriously consider how your retirement will be funded, writes Stuart Smith.

The NHS pension may underpin your retirement planning, but it usually needs building up to avoid a significant income drop when you finally decide to call it a day. Fortunately, these days, both pension rules and pension contracts tend to be flexible.

Pension rules changed in April 2006. One relaxation means you can claim tax relief on contributions of up to 100% of annual earnings, subject to an annual allowance, which this year is £235,000.

There is now also the lifetime allowance (currently £1.65m) – a maximum pot you can accumulate in your pension plan, but which is subject to sizeable tax penalties. Rules differ for calculating the value of a defined benefit pension, such as the NHS, or a personal scheme.

Pension contracts are more flexible these days. Examples are:

■ Stakeholder pension – with strictly controlled charges, these tend to have a limited range of funds to invest in and are suitable for those paying relatively low contributions and for smaller funds;

■ Personal pensions – offer a much wider range of funds, usually including some from 'external' fund managers such as Invesco, Fidelity and Jupiter. They offer excellent value and are more suited to those paying in higher contributions and/or with bigger funds;

■ Self Invested Personal Pensions (SIPPs) – give you access to a full range of investment funds, as well as share dealing and the ability to own a commercial property within your pension fund. Likely to be most suitable for those with funds worth £100K plus.

Before deciding, you should take account of your own personal circumstances, such as existing benefits and your attitude towards risk, and also the features of the chosen pension contract.

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