

TAX MATTERS FOR DENTISTS

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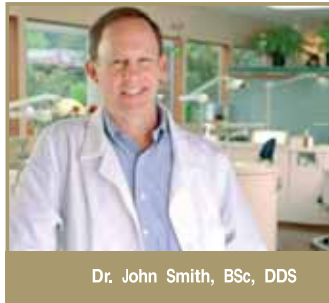
*Mike Lakhani
and his Team of Specialists.
Tax Advisors for the
Dental Community*



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Our Team of Contributors



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ENHANCE YOUR CASH FLOW

The feedback we have been receiving on our quarterly Tax Matters for Dentists, specifically the case studies, has been tremendous as readers can see the implications to their own situations. Other material covering changes in legislation and practice related matters have also been welcome.

Many dentists have taken us up on our "Tax Saver" plan in which we offer to do a comprehensive analysis of their situation. The huge savings and planning opportunities realized have repaid their initial cost for the plan many times over by structuring their affairs to impact their cash flow in a significant way. The 5 most common cash flow enhancements are:

1. Financing :

The traditional source for funds needed to start a new practice, expand to more operatories or purchase new equipment is mainly derived from leases or bank loans. Leasing had more attractive tax benefits when incorporation was not permitted, but now with a corporate tax rate of 19%, leasing is less desirable. Bank loans, normally structured over a 5 or 10 year repayment period, are a substantial drain on cash flow. Based on averages, we see \$5,000 to \$8,000 a month going to bank repayments. These can be reduced to \$2,000 to \$3,000 monthly with proper restructuring .

2. Deductible vs non deductible loans :

Following the financing issue, it is common to see practice related loans which, are tax-deductible, being paid before non-deductible loans (like mortgages). The impact here could be significant e.g. \$1,000 paid towards a tax-deductible loan costs \$1,235 before tax (at 19%) whereas \$1,000 towards a non-deductible costs \$1,850 before tax (at 46%).

3. Associates not incorporating :

The common advise given to associates and newer dentists to not incorporate needs more analysis. Incorporation may still make sense for an associate averaging \$120,000 to \$150,000 in annual income, and once most tuition fee write-offs have been used up. Choosing a proper year-end more than covers the initial costs involved.

4. Non-deductible expenses :

Personal expenses like life insurance premiums and club membership can be paid through the corporation. Although not tax-deductible, the combined personal and corporate cash flow improvement using such strategies can be significant.

5. Co-ordinating efforts of different professionals :

While the dentist is busy running the practice, we find the important

task of co-ordinating the advise from the bank, equipment vendors, accountants, lawyers and so called "financial advisors" (e.g. brokers) also ends up with the dentist. Significant dollars slip away in missed co-ordination opportunities.

Finding a trusted advisor to co-ordinate the professionals goes a long way towards meeting your personal and practice goals.

If the analysis of any of the above issues could help your own situation, please contact my office for a comprehensive "Tax Saver" plan. We will address the efficient use of cash flow, both personally and in your practice, to improve and build your Net Worth. For a tax-deductible fee of \$2,500, we guarantee the resulting benefits will more than cover the costs.

Please also visit our web site www.ddstaxes.ca to find out more about our service offering, tax tips, testimonials, and so much more. See how you can benefit from working with a specialist for the dental community.

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Case Study



Chris Molloy CFP

University Education Paid for Using Tax-Free Dividends

Dr. John and Susan Kordas (actual names changed) have always wanted to pay for all of their two son's education costs, just as their parents had done for them when they went through university. They want to give their two boys a good head start with their careers and not have them worry about student loans when they finish university.

Paul, who is 20 years old, is already attending university away from home. Peter is 18 and is going to start university this September. They need close to \$30,000 each per year to cover all their costs of staying away, for tuition, books, food, rent, car and so on.

Problem

Although Dr. John Kordas runs a successful practice producing \$750,000 per year, he is running into a negative cash flow every month and looking for ways to make up the shortfall. This shortfall arises after paying for all practice expenses, taxes, personal living expenses, servicing a mortgage and other loans, and paying for Paul's education costs. Both John and Susan are concerned their cash flow will get worse when Peter starts university this year and they will not have

anything left over to add to their retirement fund, which they expect to start using in 10 years.

Their accountant had advised them not to incorporate given they were spending everything they were making from the practice and incorporation would not help. This is a typical response from accountants, as they do not get involved with analyzing personal lifestyle cash flows or retirement funding.

Client Profile

- Dr. John Kordas, Age 53 with 22 years in practice
- Susan Kordas, Age 52 working as practice Administrator
- Paul, Age 20, university student
- Peter, Age 18, starting university this year

Net Worth	
Bank Accounts	\$2,500
Open Investments	\$165,000
RRSPs	\$514,000
RESPs	\$14,000
Home	\$700,000
Dental Practice	<u>\$450,000</u>
Assets	<u>\$1,845,500</u>
Liabilities Mortgage	\$140,000
Line of Credit	\$36,000
Investment Loan	\$150,000
Liabilities	<u>\$326,000</u>
Net Worth	<u>\$1,519,500</u>

Current Cash Flow		
	Sole Proprietor	Incorporated
Practice Gross Billings	\$750,000	\$750,000
Practice Expenses	(\$438,000)	(\$438,000)
Salary to Dr. Kordas	n/a	(\$188,000)
Salary to Susan Kordas	(\$50,000)	(\$50,000)
Earnings Before Tax	\$262,000	\$74,000
Corporate Tax	n/a	(\$14,000)
Dividends to Children	n/a	\$60,000
Cash Flow After Tax Dr. Kordas	\$162,000	\$121,000
Cash Flow After Tax--Susan Kordas	<u>\$38,000</u>	<u>\$38,000</u>
Total Family Cash Flow	\$200,000	\$219,000
Lifestyle Expenses	(\$72,000)	(\$72,000)
Mortgage/Loans	(\$44,000)	(\$44,000)
Family Cars	(\$34,000)	(\$34,000)
Children's Education	<u>(\$60,000)</u>	<u>(\$60,000)</u>
Cash Flow	<u>(\$10,000)</u>	<u>\$9,000</u>

Opportunity

With Dr. Kordas incorporating his practice, we can use the new regulations allowing his children as non-voting family shareholders. A significant improvement to his cash flow can be realized. Upon setting up a special class of shares, dividends of up to \$30,000 each can be paid tax-free to Paul and Peter from the practice (provided they do not have other income).

The substantial cash flow improvement (mainly due to the tax savings) will go a long way towards paying not only the education costs, but also to funding their longer term retirement plan.

Based on the suggested corporate structure, Dr. Kordas would realize \$57,000 of tax savings over four years by paying dividends to the children instead of to himself. The table below illustrates how this can be achieved:

Their accountant had advised them not to incorporate given they were spending everything they were making from the practice and incorporation would not help. This is a typical response from accountants, as they do not get involved with analyzing personal lifestyle cash flows or retirement funding.

them to keep their average tax rates around the same as the corporate tax rate (approx. 19%), while maintaining the personal lifestyle they are accustomed to having.

With their cash flow under control, they can focus on reaching their retirement goal of \$3 million in 10 years. An Individual Pension Plan could be set up (instead of continuing with RRSPs) to accumulate \$750,000 in that timeframe. Once the children complete their education, the surplus profits of \$60,000 per year can be invested within the Professional Corporation. With the growth of the existing portfolio, \$60,000 annual savings, the IPP, and the eventual sale of the dental practice, they will easily achieve their retirement goal.

All of this is made possible with proper planning, the efficient use of cash flow, and by coordinating efforts with one key professional.

Result

Dr. Kordas' personal lifestyle expenses would be substantially reduced after taking care of the children's education costs via the corporate dividends. Dr. Kordas could save more tax by immediately reducing his salary by \$17,000 (ie. \$9,000 after-tax) to offset the surplus personal cash flow.

In addition, Susan could increase her salary by \$25,000 and Dr. Kordas could further reduce his salary by \$25,000 resulting in \$3,000 more tax savings. With time, he and his wife can set salary levels that allow

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Tax Comparison				
Years	Dividend to Dr.Kordas	Personal Tax	Dividend to Children	Personal Tax
1	\$60,000	\$19,000	\$60,000	\$0
2	\$60,000	\$19,000	\$60,000	\$0
3	\$30,000	\$9,500	\$30,000	\$0
4	\$30,000	<u>\$9,500</u>	\$30,000	<u>\$0</u>
Total		<u>\$57,000</u>		<u>\$0</u>



Dr. Raj Arya DDS, LL.B.

HOW TO RESPOND TO A COLLEGE COMPLAINT:

ONE LAWYER'S PERSPECTIVE.

Receiving and eventually responding to a patient filed complaint at the RCDSO may be one of the most daunting professional tasks a doctor may have to undertake. A task, given our increasingly litigious society, a professional may very well likely have to face at least once or twice in his or her career. A patient can easily make a complaint against a dentist without any cost and the RCDSO is obligated to investigate the file to its eventual conclusion. Often feelings such as anger, depression, rage, guilt, frustration or the like enter into the doctor's mind as one may not understand or appreciate why this is occurring. The complaint package itself usually arrives via courier and contains detailed information on a seemingly complex and legalistic process that is to be followed. The

line. Second, make and safely retain clear copies of all records, correspondence and x-rays related to the patient file. Your lawyer will want to review these records carefully. You will also be required to send all original records to the RCDSO. Consequently, I strongly advise that you send the response and attachments by secure registered mail or courier. I also recommend that you do not contact the RCDSO directly once a complaint has been filed. If necessary, please let your experienced lawyer do so.

The response: Your lawyer should be able to guide you as to the various legal elements of the response and the time-lines contained therein. The lawyer should also ensure that you have covered all of the various allegations put forth in the complaint letter. Do not

One must handle all aspects of a complaint exhaustively, promptly and professionally right from the onset.

complaints package also spells out the various time-lines and the scenarios that may unfold including the various options available to the complaints committee in deciding the present case against the doctor including the possibility of referring specified allegations to a formal discipline hearing.

The question simply becomes — How does one properly respond to such a complaint? Is a complaint filed against a dentist really to be taken seriously or is this just a frivolous matter to be ignored? In my experience, from the doctor's perspective, one must handle all aspects of a complaint exhaustively, promptly and professionally right from the onset. Failure to do so may result in a negative finding against the doctor, or even worse, a referral of specified allegations to the discipline committee. This is something that a dentist would want to avoid at almost all costs!

My first piece of advice when you receive a College related complaint is to immediately retain competent legal counsel experienced in this field. A lawyer familiar with the process will be well worth the money spent as this is your professional reputation and/or license on

leave any allegation uncovered or unaddressed. They will not go away by themselves. Your lawyer may also recommend, given the facts of the case, whether you should retain expert opinion to be submitted along with your response.

There are certain common sense parameters to keep in mind when drafting a response. First, you should be fully aware that, at this time, the complaints panel consists of two dentist colleagues and one non-dentist layperson. Much like addressing a speech to a known audience, knowing your committee will give you an upper hand on how to appropriately respond to the complaint. You should also keep in mind that suggesting ludicrous or unbelievable clinical or standard of care choices in your defence to the complaint to the committee members who obviously know better will not help your case. The dentist members of the complaints committee are usually very familiar with day-to-day dental practice and will use common sense when deciding the outcome of a file.

Second, I always suggest to my clients to avoid any personal attacks in the response — despite how tempting it may be and how good it may feel!

Sometimes, the patient in his or her complaint letter will personally attack the dentist as part of the complaint. I would strongly recommend that the doctor remain completely professional throughout the entire response letter and resist the temptation to attack back. I am of the opinion that maintaining your professional integrity throughout the entire process goes a tremendously long way in supporting and bolstering your credibility. The patient is a lay person and is often quite irate or upset. You, on the other hand, are a highly trained and respected professional that should always focus on the bigger picture to come out of this ordeal relatively unscathed and without a referral of the allegations to the discipline committee. Reciprocal personal attacks or inflammatory remarks, in my opinion, bring the doctor a notch down in noted professionalism and this fact may even hurt the case. Always keep in mind that the committee members are also human and make decisions as such.

Third, respond thoroughly to the complaint using proper standard of care arguments to bolster your case. Often, but not always, the doctor is more familiar with the correct standard of care on a particular procedure than his or her lawyer. Be honest with your lawyer so that he or she can correctly guide and advise you. If there are supporting articles (e.g. located within peer

reviewed journals), bring them to your lawyer's attention so that he or she may elect to include them in your response, if appropriate.

The professional and thorough response will not only help you in your current defence matter but, in the event that you are successful and the patient elects to appeal the decision (again at no cost), then you can feel confident that your response was adequate and that you should win again. Again, focus on the bigger picture.

Patient complaints happen and are a reality of professional life. In fact, complaints can and do happen to the clinically best and most genuine dentists as well. Unfortunately, we must deal and respond to them in our professional careers. I have suggested a practical and concise manner in dealing with such complaints. Hopefully, following such a protocol will not only decrease your stress levels in the event you have to respond to a complaint but lead to a completely successful outcome.

Dr. R.K. Arya is a lawyer whose practice is focused on corporate/commercial transactions, privacy and regulatory work in the healthcare industry. Apart from being an Ontario licensed lawyer, he is also a licensed and practicing dental surgeon. Dr. Arya received his LL.B. from Osgoode Hall Law School and holds a D.D.S. degree from the University of Western Ontario.

UPCOMING ASSANTE PRESENTATIONS

- | | |
|---------------------|---|
| • January, 16/2007 | TISC Gala
Ontario Science Center |
| • January, 23/2007 | ADT Round Table
Meridian Banquet Hall |
| • February, 07/2007 | ADT Evening Presentation
Meridian Banquet Hall |
| • February, 08/2007 | SADA Evening Presentation
Payal Banquet Hall |
| • March, 06/2007 | TISC Evening Presentation
Ontario Science Center |

For information on these presentations call Assante at: **905.273.6605**

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Tax Saver Plan and Complete Annual Tax Implementation Plan are provided through ITCC Tax & Accounting Inc.

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