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Bankrolling education through corporate loans

Most dentists finance their children's education by making them shareholders in the dental corporation and paying them a dividend. Here is an alternative financing vehicle of lending company money to the kids directly. Depending on your situation, this strategy may work even better for you than the traditional family trust dividend.

The "corporate loan" strategy is best explained by way of an example.

Dr. Bob needs to support his son Andrew in the amount of \$30,000, which includes \$15,000 for tuition fees. In fairness to Andrew's siblings, Dr. Bob tells him that a portion of the financial support will be in the form of an IOU, which he is expected to pay back once he is established.

According to the shareholder loan provision under section 15(2) of the Income Tax Act, a loan by the company, unless repaid within a short

time, is treated as income to the debtor. The income is not allocated to the shareholder. What a great income splitting opportunity this represents! Here is how it works.

Dr. Bob's Dentalco lends \$30,000 directly to Andrew. He reports the loan as income; assuming no other income, his estimated income tax is only \$2,000.

When Andrew eventually pays back the corporate loan to Dentalco, he can write off the full amount against his income, according to section 20(1)(j) of the Act. A \$30,000 repayment is likely to save another \$13,000 of income tax. Alternatively, if Bob were to pay Andrew from personal funds, and Andrew pays him back, then there is no tax relief for Andrew.

The savings become more dramatic for larger loans. Suppose Andrew

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Problems with GST refund?

Until recently, the dental community and GST bureaucracy lived in peaceful co-existence. Input Tax Credits were usually refunded promptly. GST refunds were granted on the basis that dentists provide two kinds of services: a "multiple service" which is an exempt supply and not eligible for the refund, and a "zero-rated supply" that is eligible for the Input Tax Credit.

About two years ago, the GST auditors started to aggressively reassess dentists and denying any GST refunds on the basis that dentists are no different from medical practitioners because they only provide exempt services and, therefore, are no longer eligible for the Input Tax Credit.

The provincial dental associations and the CDA have been active in

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clarifying the GST policy with the GST Head Office. We have filed appeals for all our clients who were reassessed and have been dealing with the GST Rulings Division directly. We are finally showing some success in recovering the GST refunds for our clients.

The current GST policy basically confirms the established GST treatment, which is as follows.

- A dentist who performs cosmetic services, such as bleaching, is performing a taxable supply; this means that 7% must be charged to the patient on the treatment.
- A zero-rated supply occurs when the patient is not charged the GST, but you are eligible to claim a refund of the GST you paid.
- The zero-rated supply occurs when the dentist charges the patient for the cost of the lab component of items such as crowns, bridges, dentures and implants – called “supply of artificial teeth” in GST lingo.
- Crowns that are fabricated to replace 50% or more of the existing teeth are considered “artificial teeth”. Partial crowns or veneers, as long as they meet the 50% criteria, are unconditionally zero-rated. Onlays and inlays are not considered artificial teeth and, therefore, are tax exempt rather than a zero-rated supply to the patient. When onlays or inlays are supplied by a commercial lab, the lab must charge GST to the dentist.
- According to the GST Ruling Division, the documentation the patient receives is important in determining whether or not the dentist has provided a zero-rated service eligible for the refund. This means that the lab component of the service must be clearly identified on the patient’s invoice.

Here is how you calculate the GST refund.

1. You determine the refund percentage by dividing the lab fees into the total office production, consisting of exempt and zero-rated supplies. If this ratio is less than 10%, you are not eligible for any GST credit. If the percentage is, say, 15%, then you are eligible to claim 15% on the GST paid on dental supplies and other overhead expenses.
2. With respect to claiming the Input Tax Credit on equipment purchases, it is an ‘all or nothing’ rule. If your equipment is used more than 50% for the provision of zero-rated supplies, such as lab equipment, then the full GST paid is recoverable. If use of the equipment is primarily for the supply of exempt services, then no refund can be claimed.

If the GST office is still not willing to part with your refund, and you need some help, please feel free to give us a call.

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enrols in dental school, requiring \$60,000 of income to pay \$40,000 for tuition costs. A \$60,000 loan will trigger a \$7,000 personal tax for Andrew. Once Andrew deducts his \$60,000 repayment to Dentalco from his professional income, his tax benefit is likely to be \$24,000.

In summary, under the corporate loan arrangement the child reports the loan as income when in the low tax bracket and receives a tax deduction on repayment when in the high tax bracket.

Give us a call if you need assistance.

Manage energy, not time

The number of hours in a day is fixed, but the quantity and quality of energy available to us is not.

This fundamental insight is the main theme of the book *The Power of Full Engagement*, authored by Jim Loehr and Tony Schwartz, and published by Simon & Shuster. I highly recommend it.

Facing crushing work loads, we try to cram as much as possible into every day. Time management is no longer a viable solution.

The book describes how managing energy, not time, is the key to your enduring high performance, as well as to your health, happiness and life balance.

The authors are running a corporate athlete training program for elite athletes, and they provide readers with a practical step-by-step program on how to mobilize your energy and expand your capacity in a systematic way, just as Olympic athletes do. It also shows you how to create positive energy habits.

You will find this book an easy read and a source of inspiration and renewal – just what you need to get a jump start on the busy fall season in your practice.

The secret to lasting success lies in how we manage our energy. It is an insight that most of us ignore.

Disability Insurance: what you need to know

“Disability results in all the disadvantages of death, but it lets you live to enjoy it,” says my insurance agent Frank Allen when explaining the need for a disability policy.

The ability to work in your chosen profession is your biggest asset. One of the most important financial decisions you will make is to select appropriate disability insurance in order to protect your income. If you are 35 years old, there is a 30% chance that you will become disabled for more than 90 days during your lifetime. A 35-year old dentist, earning \$150,000 annually, is estimated to generate \$5.5-million by age 60, assuming a 3% inflation rate. That is an enormous amount of financial stability to protect from disability.

Here is a checklist to determine if you have the best disability protection.

How much coverage do you need?

I recommend that you purchase sufficient coverage to replace at least 60% of your earnings, assuming that the disability income is not taxable. Prepare an analysis of your income needs, taking into consideration current living expenses as well as future needs, such as education financing, in order to confirm that coverage is sufficient. Whether or not the disability benefits are taxable will depend on whether or not the premiums are paid with after-tax dollars or written off as a practice expense. Paying the premiums with after-tax dollars ensures that the disability benefits are not taxed.

Does your policy have an “own occupation” clause?

“Own occupation” coverage is the best you can have because you receive the disability benefits if you are unable to perform the usual and substantial duties of your profession, even if you choose to work in another occupation. Compare that to the “regular occupation” definition, which pays the benefits while you are unemployed but ceases to pay if you choose to work in another occupation. Avoid the “any occupation” clause, which basically states that if you qualify to work at any job (including as a greeter at Wal-Mart) the insurance company is off the hook.

How long should you have to wait for benefits?

All disability policies define a waiting or elimination period, which is the amount of time that elapses before payments start. During this waiting period, ranging from 30 to 180 days, you are expected to provide self-insurance. Premiums decrease drastically if you opt for a 90-day waiting period, rather than 30 days.

Is your policy “non-cancellable”?

This provision means that the insurance company must continue to insure you as long as you pay the premiums. Your policy cannot be cancelled for any reason, nor can your premiums be increased.

Should the maximum benefit be to age 65 or lifetime?

All policies have a length of time during which they will continue

paying monthly benefits (2 years, 10 years, to age 65, or lifetime). Most doctors should choose the ‘age 65’ option.

Does the policy offer partial or residual benefits?

This is an important feature to look for. If you cannot carry on your job full-time, but you can work part-time, then the insurance company will pay benefits equal to the drop in your income. Many policies require a drop of 20% of your income and a continuous disability of at least 30 days before you are eligible for residual benefits.

Are there COLA and FIO options?

The cost of living adjustment (COLA) clause will provide increased benefits in the event of a very long disability. Its purpose is to protect the purchasing power of your disability income. The Future Income Option (FIO) clause will allow you to increase coverage as your income increases, without having to provide evidence of good health. This rider is important for young dentists, who are initially unable to receive the level of coverage they will require in future because of insufficient current practice income.

Did you fully disclose your medical history?

The insurance company will not hire investigators to verify all the details of your application. When you complete the application form with your agent, make sure you understand all the questions and disclose all ailments and illnesses, even

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Obstacles in buying a practice

You want to be your own boss, yet are you continuing to work as an employee or associate. What is holding you back? Here are the major hurdles that prevent many dentists from making the move to ownership.

The "money" factor

With ballooning student loans and a big house mortgage, the idea of borrowing an additional \$400,000 to purchase a practice is really scary. But consider that the extra income you can earn as an owner, rather than an associate, is sufficient to pay back the loan within seven years. In other words, purchasing a practice is a great investment. If the bank is reluctant to lend you the full purchase price, don't be afraid to ask the vendor to finance the balance of the purchase.

The "self confidence" factor

You shy away from buying a practice because you feel you don't have the entrepreneurial talent of a Donald Trump. All you need is a dose of common sense, lots of hard work, and a desire to put the needs of your patients and staff ahead of your own. There are also plenty of advisors to assist you.

The "fear of failure" factor

While buying a practice involves an element of risk, many dentists over-estimate the risks. Many perceive a greater loss of patients in a transition than occurs in reality. You can reduce the risk to an absolute minimum by carrying out a thorough due diligence investigation prior to purchase.

The "spouse" factor

Never buy a practice in a location that your spouse doesn't particularly care for. The decision to buy must be made jointly. Having your spouse on side will save you lots of grief.

if you think they are insignificant. It would be a tragedy if your claim were denied because of a lack of full disclosure.

Don't 'go for cheap' when purchasing disability coverage. You need quality coverage which is, of course, reflected in a more expensive policy.

Make sure you find a knowledgeable advisor who can help guide you through the jungle of disability contract definitions and who will find the best coverage at the most reasonable cost.

Practice Opportunities

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Surrey, BC

Well-established family practice in professional building; 3 ops; excellent cash flow; well maintained; principal retiring.

E-mail: practice@telus.net

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