Top five tax tips for 2005

Income taxes are your biggest expense, and it is amazing how few dentists engage in serious tax planning. The tax savings generated can accelerate your mortgage repayment or boost your retirement savings.

These are my top five tax saving tips.

1. Deduct mortgage interest
If you have a sizeable house mortgage, you should look for creative ways to write off the mortgage interest. You pay $150,000 of interest on a $500,000 mortgage at 5% over 10 years. Deducting this amount on your tax return will result in a tax saving of about $60,000.

2. Use capital gains instead of dividends
If you are planning large cash withdrawals from your company in 2005, consider taking the cash as capital gains rather than dividends. On capital gains you only pay tax on one-half of the amount since only one-half of the capital gains is subject to tax. On a $200,000 cash distribution you can save about $20,000 of income tax.

3. Split income with family members
Income splitting is still the No. 1 tax shelter for B.C. dentists. With the small business deduction increasing to $300,000 in 2005, more dental income is taxed at the low corporate tax rate of 17.6%, and less income is subject to the 44% personal tax rate. You lose the benefit of the low corporate tax rate if all the income is paid out to you. The tax saving can be enormous by channelling corporate income to family members in a lower tax bracket.

4. Set up your corporate health plan
You can get almost a 45% discount on your medical expenses by setting

See TAX TIPS, page 4

Is your hygienist on the payroll?

The tax department is currently reviewing the role of hygienists in selected dental practices to determine whether the hygienist is entitled to independent contractor status, or should be treated as an employee. If the hygienist is considered to be an employee, then you, as the employer, will be assessed for failure to remit payroll deductions including employment insurance and Canada Pension Plan contributions. The assessment will likely cover the prior three years and will include penalties and interest.

To avoid the potential assessment and any ensuing arguments with the tax department, I suggest that you enforce a policy which requires all staff members, including hygienists, to be on the payroll. If you feel confident that your hygienist is an independent contractor, then I suggest...
Building Wealth: the G-E-M approach

Dental school gives you the skills to make money, but it doesn’t teach you how to spend it or save it. You may have seen the surveys which show that only 15% of dentists can look forward to maintaining the same standard of living during retirement as they enjoyed during their career. The message: Don’t leave your money matters to chance.

To ensure success in your financial planning, consider the G-E-M approach: Goals, Execution, and Monitoring.

Goals
What are your most important financial goals? Paying off your mortgage, financing your children’s university education, purchasing new dental equipment?

Make a prioritized list of your objectives, considering where you want to be 5, 10, 15 years from now. For example, it is a reasonable goal to plan to achieve financial independence within 17 years of starting or purchasing your dental practice.

Next, prepare a personal cash flow projection for the next 12 months. This should include anticipated practice income, tax payments, personal and living expenses, and the amount of any planned savings.

Don’t keep your goals locked away in your head. Write it down to give you visual reinforcement. One dentist I worked with made it his goal to repay his mortgage in four years – a very ambitious goal. He wrote his goal on post-it notes and posted them all over his office and even on his bathroom mirror. Although this is an extreme example of goal internalisation, it worked! Three years later he is on track to meet the four-year loan repayment deadline. The power of writing your goals down and reading them regularly cannot be overemphasized.

Execution
Execution is the true Achilles heel in financial planning because it requires you to overcome a common affliction – procrastination. Execution is the actual implementation of your goals; the time for “doing”, not “talking”. For instance, to start a serious savings program, get into the habit of automatically transferring surplus practice funds into your investment portfolio. Good habits need constant reinforcement, which requires discipline and a supportive environment. Your spouse and family are vital partners in this process. When you work together on executing a financial plan, you are on the right road to realizing your dreams.

Monitoring
As you implement the steps to reach your objectives, you need a mechanism to monitor your progress. If you plan to save $5,000 each month, prepare a monthly income and expense statement that compares the planned figures to the actuals.

Another excellent tool is the net worth statement, which tracks your wealth-building efforts. By subtracting your debts from the market value of your assets, you determine your equity or net worth. A rule of thumb to determine the required savings for retirement, if you wish to retire at age 60, use the factor of 25 times your annual after-tax living expenses. A goal of $60,000 of annual income would require $1.5-million in equity. Use the factor of 20 for retirement at age 65.

The G-E-M approach is a simple and effective tool for achieving financial independence.
Building wealth

Our approach to helping you build wealth is to integrate your practice financial management with your personal financial planning. After all, can you really separate the dentist from the dental practice?

We start by analysing your practice, and your professional and personal goals.

We give you the financial tools to control your overhead expenses and maximize your after tax cash flow. We review your tax returns to determine if there are any missed tax saving opportunities. We review your strategies to ensure that they are effective and consistent with your financial goals.

As dental accountants, we continue to monitor the success of your practice and the achievement of your personal financial goals. In fact, we build this right into our ongoing accounting engagement. Give us a call if you want us to help you build wealth.

Negotiating like a pro

Prospective purchasers often walk away from a practice purchase because they are unwilling to compromise on a relatively small price difference and, thus, miss the career opportunity of a lifetime.

I picked up the following exchange between students and established practitioners in a student forum, posted on the American Academy of Periodontology website, on the subject of purchasing and setting up your own practice.

A student posed this question to Dr. Nicholas Caplanis regarding his practice purchase.

Given what you know now, what might you do differently?

Dr. Caplanis replied: “There is not much that I would have done differently except that I probably would not have negotiated as hard regarding the practice purchase price. In my personal situation, the original asking price for the practice was approximately $400,000. The final negotiated purchase price was in the mid $300,000 range. In retrospect, given how successful I have been in this practice, I do not feel that the $50,000 that we were negotiating back and forth is as important today as it was back then. That amount of money could have been the deal breaker and I could have lost this practice to another buyer who was willing to pay it. In retrospect, an extra $50,000 for the price of the practice would have not really changed my financial situation that much. My advice, therefore, is “don’t be penny wise and dollar foolish”!”

Make your associate a successful partner

So you brought in the new associate as a future co-owner of your practice. How do you assist the new dentist in establishing a patient base quickly? How do you help her to become as successful as you are?

Putting the new associate, together with a novice assistant, in the old operatory down the hall is not a confidence booster for the dentist or the patients, who may think that the apprentice reality show has come to town.

Treat your new associate as a partner from the very beginning of the transition process. Ask your staff to respect the associate as if she were already a co-owner of the practice.

Abstain from using the name ‘associate’ in the presence of patients. Introduce the new dentist as “My new partner Al Dente” rather than “My new associate”.

Patients will be willing to accept treatment because they feel that the new dentist is a permanent addition to the practice and must be well qualified to be your partner.

Early patient acceptance is critical for the new dentist to build a patient base quickly, and your practice is productive only when both dentists have busy schedules. This will include sharing patients with one another.

With respect to managing the practice, have the new associate assume various ‘owner’ responsibilities during the transition period. For instance, by making her responsible for the hygiene recall system, purchasing of supplies or staff compensation, you will ensure that, once she has become a co-owner, she will be capable of sharing the burden of managing a successful practice.

Planning successful transitions —

Don’t bargain yourself out of the deal

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5. Maximize deductible pension contributions
Consider switching your retirement savings to an Individual Pension Plan, instead of the RRSP. You can make larger contributions to an IPP than to the RRSP, especially if you are over 50, and you are also entitled to a larger tax deduction for past service contributions.

Make tax planning your top priority in 2005 and put more money in your pocket. Give us a call if you want to find out how you can implement these strategies.

Reviewing controls—
Keep a close eye on the cash

Employee fraud in dental practices made headlines in a recent edition of Dental Practice Management. As reported by the Association of Certified Fraud Examiners, employee embezzlement in small businesses averages $100,000, and the percentage of funds recovered is very low.

A basic goal of internal controls is to keep track of your cash. Your cash disbursement controls help ensure the practice only spends money with proper authorization. Revenue controls ensure all treatments are billed correctly, collected promptly, and deposited into your bank account. Effective controls will dissuade employees with sticky fingers from diverting practice cash into their own pockets. Many dentists don’t pay attention to their front desk systems, but there is too much money flowing through your practice to ignore internal controls. Make review of your accounting system a priority for 2005.

We can conduct a review of your internal controls with our audit tools tailored to dental offices. Upon our review, we will provide you with recommendations and suggestions for implementation to strengthen financial controls of your practice.