The Talking Law Podcast

Episode 104 – Top Tips in Business structuring for dentists and medical professionals, with Stephen Guthrie Part 1

Note: This has been automatically transcribed so will be full of errors! We are not providing it to you as a word-perfect version of the podcast but just as an easy way to provide you with a different way to be able to see or scan what kind of information that might be relevant to you if you are the kind of person that likes a transcript.

Transcript

Joanna: Hi, it's Joanna Oakey here and welcome back to Talking Law, a podcast proudly brought to you by a commercial legal practice Aspect Legal. Now in today's episode, we're talking about the top tips in business structuring for dentists and medical professionals with Stephen Guthrie. Now business structuring I know, hold the phone not necessarily the most exciting topic on everyone's lips. But we think it's so exciting. We're not just doing one show in this series, but we are doing two. That's right, we've got a two part series in the top tips in business structuring for dentists and medical professionals.

Now, obviously by the title, this is going to be particularly interest if you have a practice that is engaged in dentistry or medicine or related specializations, but this episode will also be just as relevant for you to listen to. If you have ever wondered about your business structure and wondered what the hell is the difference between a trust, a company or being a sole trader.

And while we're looking at trust, what's the difference between family trusts and unit trusts? What's the best investment structures to use as a business owner? When should we use SMSFs? To hold property? Is there a benefit of having a company see it as a beneficiary, in our trust structure? So many questions that I know are unanswered sitting out in our audience out there. And in this two part series, we're seeking to answer them all. So not withstanding that, we have a little bit of an emphasis on some of the intricacies of business structuring for dentists and medical professionals. It's super relevant to anyone who is in business who just doesn't quite get what trusts are or structures or has a question around that. Now, as I said, this is a two part series just because it's so exciting.

Actually, it's two part series because there's really a lot to cover. There's a lot to cover in terms of explaining some of the differences in different types of structure. But we also tried to make it super practical by giving you lots of examples so that you can understand where people have gone wrong and the example of what good looks like. So I have here on the show for these next two parts, Stephen Guthrie from Prosperity Advisers. Now, Stephen is no spring chicken in this area. In fact, he's got more than 20 years experience in providing strategic business advice and taxation services. So currently, he's a director in the business services and taxation division in Prosperity Sydney office, and he manages a team of professionals who deliver Business Advisory, taxation, corporate assurance and financial services. And he also leads Prosperity's Health Advisory practice and specializes in providing advice to medical and allied health professionals And then practices.

So of course is the obvious choice in talking about this topic today. So let's get stuck into it. Part One of our two part series was Stephen, let's go. Hi, Stephen, welcome to Tlking Law. We're really excited to have you on the show today.

Stephen: Yeah. Thanks very much for having me along Joanna. First time for me. So be interesting to see how this goes.

Joanna: Fabulous. Well, look, I think we're going to cover some really interesting topics here because obviously, you and we do a lot of work for dentists and medical professionals. And so there's a lot of people who are you know, advisors who deal with dentists and medical practices or the practice owners themselves who will be listening into this podcast. So I think it's going to shed a lot of light for them on this area of structure, because I think business structures for many people who run a business are a little bit confusing, and they really don't understand, you know, you go to your lawyer or your accountant, and and you end up in some sort of structure. But they don't necessarily understand A. the structure or B. why they're in the structure that they're in and see whether it's appropriate for the future and how to determine when those points are that they need to rethink structure for their future plans. Would you say? That's correct.

Stephen: Oh, absolutely. I mean, I was sitting with a client yesterday and looking at one of those lovely colorful drawings on a page with boxes and lines. And they were completely mystified as to why they had unit trusts and companies and family trusts and how it all worked and what it actually meant for them in the future. So it's really important not just to be thinking, what the immediate position, so what does it mean now, but planning for that next five or 10 years as to whether what they've got now actually works for them?

Joanna: Okay, wonderful. Yeah, I do want to do into some of these areas today of service trust as well, because, you know, as we know, this is the particular industry space where service trusts, you know, can be used quite frequently. So it's a really want to dig into some some of that area as well so that we can explain it because I think that's really the initial operating entity. But then sometimes in these areas, there's other complexity few other things going on around it. So let's see if we can demystify some of this area. But let's just start with, I guess, general comments on business and investment structures, what's the general approach that you take when when you're dealing with clients in relation to working out what structures are available and then what is most appropriate for them?

Stephen: Yeah, so I think it's, I take the approach that I need to do a lot of listening upfront. I need to ask a lot Have questions and really need to drill down with someone on not just what they're thinking at this point in time, but where they think their practice or business activities might take them. So, for example, there may be a sole practitioner at the moment. And so we could set them up in a structure, which works really well for them and their family. But if they have it in their mind that in two to three years, they want to bring in another owner into the business and we haven't explored that upfront, then we may find in two to three years, we have to go through an expensive reorganization, just to do something which we could have planned for at the start of the process. If we'd asked that question up front.

Joanna: And making this really real for our listeners. What is an example of a structure that might be really good for them initially, if it looks like They're only going to hold the structure themselves within their family versus something versus something that is more appropriate for bringing partners in in the future.

Stephen: Yeah, so it looks a very typical one we would see would be a family discretionary trust. So kind of almost a vanilla entity in Australia, everyone seems to have a family trust lurking in their group structure somewhere if I've been with an accountant for a while. So family trusts are great. In the sense they provide great flexibility to distribute income and assets within the family, but they don't work.

Because when you set up a family trusts, you have to nominate an individual within the family from whom the rest of the relationships and beneficiaries are linked. They don't work with two unrelated family groups. So you know, I've had a client in the state where they wanted to set up a business which They could see that in two to three years time, they would want to start bringing some of their associate doctors in as owners, but at the moment, they were just going to be within the family, they weren't quite ready to bring in other owners, we made the decision that we would set them up in a unit trust, rather than a family trust as the main practice entity even though at the start, all the units would be held within the family. But in two to three years time, we wanted a structure where we could start to bring in other owners and issue equity interests in the structure. So that's an example of one way that the standard, let's just use a truss structure doesn't work if you want to bring in other owners.

Joanna: And the interesting thing I find in dealing with business owners is that what they think the future plan is today is often quite different to what the future plan ends up being. I guess here is the difficult thing for advisors as well. It's not even just about and you know, absolutely, it's super important to understand what the client's plans are for the future, but also to arm them with the understanding that their plans might change. So how do you deal with that?

Stephen: Part of it is that initial discussion of making sure that we've canvassed as many of the options and kind of open their eyes to where the business might go, it's also been a part of our process that on a regular basis, we will revisit the structure. So whether it's annually or biannually, let's just look at where we're sitting. Does this make sense? We tend not to move from the left hand side of the page to the right hand side of the page, immediately there's a progression and so you can see if you look at the structure on a regular basis, you can see where you've perhaps moved your thinking, and we need to revisit, does the structure still work? It's impossible to forecast how profitable a business will be what it will be worth. And so whether you're qualify for things like small business CGT concessions, what future assets you may or may not have. And so you're going to constantly need to look at your structure and just run a fresh set of eyes over it, not just assume that what we set up three or five or 10 years ago was still the right structure for us.

Joanna: I think that's a really good point that and just having this point where you come back, you know, and it makes sense for that to be an annual review, because it's one of those things that you could then think of it at a particular time frame each year, but coming back in with some sort of regularity, to review, where you are, what you're in, what are your future plans now. And you know, how you're looking in terms of how you set up currently for those now, future plans,

Stephen: Particularly if you know you've got a if you're planning towards an equity event, you need to start 2-3 years out, make sure you put everything in place.

Joanna: Now I love how you say that because this is and we have a whole podcast show devoted to planning and buying and selling businesses The Deal Room podcast, but I spend a lot of time talking about the benefits of exit planning. But you know what? It's just sometimes I just feel like I'm flogging a bit of a dead horse because I don't know why but people don't want to know about exit planning until they're actually at the point mentally of exit. Do you find that... has that ever occurred to you? Do you have these issues?

Stephen: Yeah, absolutely. And there are some things that you can't fix on the spot. And if there is a good deal that's come to you and you know, don't be in the position where you feel constrained to take the deal if even if it means I haven't planned well for the tax consequences, for example, of that transaction.

Joanna: Yeah, absolutely. And you know, industries change we know dental is going through, you know, Interesting changes in evolution, I guess from a from a company in an acquisition and exit perspective. But I just think it's super important that that owners just think about exit well before it's time that they actually want to think about exit and just make sure everything's properly set up for that. But then I also often think maybe you're better off planning for your clients as though they are going to grow and exit in certain ways, even if they don't, because it just seems that there is this issue of businesses having this idea of small initially and then just not being ready for larger as it appears as the years go on. That seems to me to be one of the most common issues, would you say?

Stephen: Yeah, I always like the maxim of planning with the end in mind. So I typically try and think of what's the exit process for any structure that we're setting up because different structures to have quite significantly different outcomes at the end of the process.

Joanna: Yeah, absolutely. And can you maybe give us just a really quick snapshot or an example of what you mean by that

Stephen: So an example we would see reasonably regularly would be where someone's trying to qualify for these small business CGT concessions. And you'd appreciate that there are, there are some threshold issues, threshold tests that need to be satisfied before someone can qualify for those. And if you do qualify, then you can you can move from paying tax on half the game to paying tax on none of the gain that you make, and things like how many owners do you have in the business at the point you sell? Do you have someone who's over 20%? Or have we diluted ownership to the point where we've got too many owners and we don't qualify for small business CGT or we haven't thought about how we structure our assets so that we fall below the $6 million net asset test. Those kinds of things which you can manage. If you plan ahead, you can get to the point of the transaction and realize you've made a mistake and you've cost yourself tax on half your gain which you might not have needed to have done. That's an example.

Joanna: That's a great example. Yeah. Because they're interesting discussions, but because we do a lot of work at exit or acquisition. And but when clients come to us at the point in clients who referred in at the point of exit, one of the first questions we ask is, okay, you know, have you sat down with your accountant and plan this through in relation to what will be in your pocket at the end of the day, because from us having a look at it, maybe there's some other ways that you could consider dealing with business exit rather than, you know, how you you're proposing to deal with it at the moment? And they say, inevitably, they say no, and they go, then go through that process. And it's just, it's like, they continually, absolutely astounded at what the difference can be depending on you know, how that how that structure looks and what the approaches are that we're using, but it just makes me think you know, how often businesses just haven't been in close contact with our accountant as they're hitting into an exit event to really understand what the structure looks like what the options are for them what the differences are, at the end of the day in terms of what they're getting in their pocket,

Stephen: You're preaching to the converted. Clearly, you know, as an accountant and advisor to professionals and dentists, we love to be involved in the discussion and the planning process up front, rather than coming to the end and try and rescue a situation which may not be rescue doable. Yeah, absolutely.

Joanna: Well, this is what this is all about. Steven, isn't it? We're trying to give the warning signals so that, you know, people are listening to it now before they're thinking of exit because that's the point when you really should be thinking about it. Okay, so what are some of the things just generally, that you should keep in mind in relation to structuring and I'll kick it off - Asset protection is certainly something to have a think about. So what else from an accounting perspective for the sorts of things that you should be thinking about or bearing in mind, I guess.

Stephen: I guess it's most of the things are tax driven. So what are your long term versus your short term kind of tax expectations, the difference in tax on how your annual revenue is treated versus a long term gain you might make on on exiting the business, you know, revenue tax versus capital gains tax, the way the finances might work. So some structures are more easily have easier access to finance, you know, banks kind of understand some structures better than others. That's probably the key, the key areas and I guess, underlying all of that is the the way our tax system works in relation to kind of revenue that you're earning, and what that means for the structure you may or may not be able to choose to use.

Joanna: So what's an example of that? What do you mean the types of revenue?

Stephen: So if I'm an employee, you know, I turn up for work each day and earn a salary I can't turn around to my employer and say, here's an invoice from my company, which I've set up and you're going to be paying my company for my services because what I'm what I'm providing to my employer and my personal efforts, my personal services, and our tax system says that whether remuneration that's coming to someone is for their personal effort, then there's an expectation that is going to be taxed to the individual.

So this typically comes up with dentists and medical professionals who are clearly at work, seeing patients day by day, their income is being earned off their own personal efforts that we have in our tax system, a distinction between a business activity which is just earning income from that one person's activity versus a large medical practice, a law firm like yours and accounting practice like ours, where you've got a whole collection of people generating income in that circumstance. The profit that has been generated is what we call business income. And that is able to be split within our structure to other people other than just the owners of the practice. So understanding whether someone's generating personal services income, income from their own activity, or whether they've really got a legitimate business activity, they've got other people involved who are generating income as well. And for profit, therefore, is business income. That's a key distinction that chicken in the world of medical professionals we need to get over.

I go to conferences, a lot of talk to people a lot and quite often get approached about you know, my accountant said to me, it's okay that I've set myself up in a company and I'm only paying 27% tax even though they're just a sole practitioner carrying on business by themselves. The tax office looked at them the tax office would not be saying well done accountant. They would be subject to audit and probably penalties because the tax system will not allow them to operate through it. company in retained profits and pay tax on the company. So understanding that distinction is really important as part of that first choice of structured decision.

Joanna: And this is really something I think that is particularly important for medical and dental professionals isn't it? Why is it that it's so important or prevalent to think about these industries? Do you think Stephen?

Stephen: Well, because most medical professionals...unless they were an owner of a, or an owner or part owner of a medical practice with other medical professionals, most of the industry is set up as effectively sole practitioners, their contract is in someone else's business. But they have the typical industry structure is that they will be in receipt of 100% of the patient income from their buildings, and they will pay a fee across to whether it's a dental practice, the medical practice from which they're operating, and now we'll get to take home whatever the balance is as as kind of their their net income. And so most GPS who were other medical centers or dentists who work in someone else's practice are kind of running their own little business.

And it's really just, they're just they're the only ones generating the income. If they don't see patients that day, then there's no income being generated. And so the tax system would say, that's personal services income, that is income being generated solely from your own efforts. And therefore the expectation would be that you're going to pay tax on that in your own name. Even if you've set yourself up in a trust or a company, you won't be able to divert that income to your low income earning spouse or your parents or your children, you will be taxed on that as an individual.

Joanna: And you're absolutely right. This is one of the interesting things about this industry that is completely different. So someone came in from almost any other industry and came in and had a look at the way the industry works in terms of all of these dentists or you know, doctors out there sort of running their own little business. And having this, you know, service, this relationship with the service entities, you know, would sort of seem a little bit back to front to them. Again, it is it's a different approach, isn't it? And why is it that way? Do you think? I mean, it's an interesting reflection.

Stephen: The flipside is, what else would they be that they'd be employees? Yeah, that's right. And no one wants to employ a dentist or a doctor. Because of A. the perceived risk of I guess, litigation. The medical practice is trying to distance itself in a litigation sense from the activities of the medical professional, who's seen patients within its doors. And up till now, it's also been how do we minimize things like payroll tax, and there's a whole another discussion around what's happening in the world.

Joanna: Yes, that's right. But I do wonder, you know, if we take payroll tax out, there are if there is this continued movement or, you know, a confirmation of this potential movement with issues with the payroll tax side in the way that these structures have been traditionally set up. I just wonder, you know, is that the real driver rather than risk in and of itself, because it is interesting the way this industry is so different to most others. So anyway, I guess that's just a general statement and question out there. I just wonder, you know, maybe this is an area that we change quite a bit into the future.

Stephen: There are medical practices that are running different models, and are employing doctors. And taking away that kind of perceived pressure around. I've got to churn through as many patients in a day as I can, or I've got to fight with the Medicare system around billings, in order to maximize my income. It's a different model, but it's not all like that. There are some moves within the industry to see different kind of models in class.

Joanna: Interesting. Well watch this space as they say. But anyway, today we're just talking about today. The situation as it is currently.

Joanna: Well, that's it for part one of our two part series, all about the top tips in business structuring for dentists, and medical professionals with Stephen Guthrie from Prosperity Advisers. Now, if you'd like more information about this topic, then head over to our show notes or our website at talkinglaw.com.au. And at our website, you will get a free download on the transcript of everything that we talked about today. with Stephen and if you enjoy the content so much that you just want to read through it step by step. In fact, in areas that are complex like this, it can be really useful to see the transcript so that might be something that you find is useful for you if there's some things that we've talked about today that you found really interesting, perhaps a bit new, and you'd like to go and see more details about it.

Also at our website, you will be able to find out how to contact Stephen Guthrie and prosperity advisors. And you'll also be able to find out how to contact our lawyers at Aspect Legal, if you would like any help with any legal elements of the information that we covered today. Now, don't forget to come back to our next show, which is part two in this series, where we round off this discussion with Stephen and come to the end of our discussion on structures and really dig further into investment structures and premises ownership structures. So tune in to part two if you'd like to hear the rest of this discussion. And of course, if you enjoyed what you heard today, then please pop over to iTunes. And leave us a review we'd be ever so grateful. And don't forget to press that subscribe button. Well thanks again for listening in. You've been listening to Joanna Oakey and Talking Law, a podcast proudly brought to you by our commercial legal practice Aspect Legal See you next time.