Dental Wealth

Helping Successful Dentists Make Work Optional.

Top Tax Saving Tips for Dentists

Here is a list of tax-saving ideas you may wish to consider:

Incorporate

Consider creating hygiene or a technical service corporation to administer hygiene revenue. A professional corporation (PC) may be used to operate your dental practice. This could result in tax savings and/or a tax deferral, because corporations are taxed at 18.62 percent on the first $250,000 of taxable income for calendar year 2004 compared with the top combined personal federal and provincial tax rates that range in Ontario of 46.41 percent.

Be aware that this strategy only works if money is retained within the PC or if the dentist elects to withdraw the money personally by way of dividend. If you need all the corporate income generated from your practice for everyday living expenses, then the PC may not earn a sufficient profit to justify the annual legal and accounting fees for corporate maintenance and tax filings.

Pay Dividends

If you have a hygiene or technical service corporation with your children as the shareholders, you may pay a dividend to your children over 18, especially those attending university. Children over 18 without income are in lower marginal tax brackets, and dividend income is taxed at a very low rate.

Here's the advantage of paying dividends: an individual who earns regular income up to $33,375 per year pays a combined provincial and federal tax rate of 22 percent. When this money is received as dividend rather than regular income, the tax rate is 12 percent. Adopting this strategy reduces the tax burden by a full 10 percent.

Make Mortgage Interest Tax Deductible

If you have a mortgage on your home and happen to have excess capital in your practice's bank account, consider writing a cheque from the practice to yourself, depleting this capital balance. Use this money to reduce or eliminate your home mortgage, ask the bank for a personal investment/business loan and invest the money back into your practice. This strategy converts the non tax-deductible mortgage interest into a tax-deductible interest on a business or investment loan. An added plus is that it can help protect your money from creditors.

Hire Family Members

If you employ family members in your practice, prepare a written job description for each individual and pay a reasonable salary and bonus for services rendered. By having some income, children over 18 will accumulate RRSP room for future earnings. Canadians earning less than $8,148 for 2005 qualify for a personal exemption and pay no provincial or federal taxes.

Take Advantage of Depreciation

Consider buying and installing big-ticket items for your practice - equipment, renovations, computer software - before year-end. This has the effect of increasing tax-deductible expenses by way of the increased capital cost allowance (depreciation).

Create a Health Spending Account

If you have a PC consider creating a personal Health Spending Account (HSA). An HSA is a bank account whose deposits are spent exclusively on health-care expenses. By having an HSA, you may convert health-care expenses into 100 percent business deductions and a nontaxable benefit for yourself. You determine both the amount of the annual contribution and how the benefit dollars are spent. Best of all, unlike traditional medical and dental plans, any unused funds remain in the account for your future needs.

Suppose an incorporated dentist in Ontario who earns $100,000 of net income incurs a $10,000 medical expense. The dentist would have to in effect withdraw $18,416 in pre-tax income from the PC to pay this bill. By using a Health Spending Account the company would pay only $11,000.00 - including the 10 percent administration fee - an amount that is fully tax deductible from the PC and a non-taxable personal benefit. The overall tax savings would be $7,416.

All the highly successful people I have worked with had very clearly defined and written plans - for life, career and money. They believed implicitly and unshakably in their plans and were undeterred by external circumstances. If something unexpected occurred, the plans possessed built-in contingencies to help adapt to new circumstances.

Maximize Retirement Savings – IPPs vs. RRSPs

As an unincorporated dentist, you may contribute the maximum amount permitted each year to a Registered Retirement Savings Plan (RRSP).

However, if you are employed by your PC and are earning a high income, consider creating a "super-RRSP" in the form of an Independent Pension Plan or IPP. Contribution limits to an IPP exceed the maximum allowable RRSP limits and are fully deductible by your PC and are a non-taxable benefit for yourself. This will allow for an increase in the total value of assets that is tax-deferred until withdrawal. IPPs offer significant amounts of additional tax-deferred income to be set aside for your retirement.

Consider this example of two dentists, each 45 years old, both with net incomes over $100,000, but one is incorporated and the other is not. For the next 24 years, both make the maximum allowable contributions, the first to an IPP and an RSP, the second only to an RSP.

At age 69, assuming an annual return rate of 7.5 percent, the incorporated dentist will have accumulated $4,800,101 in the combined IPP/RSP compared with a total of $3,310,822 in the RSP alone. This works out to an annual annuity income of $362,819 versus $250,251.

The decision is clear: the incorporated dentist who contributes to both an IPP and an RSP may have an additional $1,489,279 of tax-sheltered assets in his or her retirement plan, as well as an extra $112,568 in annual retirement income!

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