Ask the Broker

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Q Are there new tax consequences for buying and selling a practice in the future?

Writing this in Mid-October, none

of us know what the outcome of the November election will be. One of the candidates promises to raise all of our taxes. The other one is promising not to, but who knows if no taxes on the “rich” will result in growing the GDP and increasing the revenues. Government revenues will have to go up to pay the amazing amount of debt we are acquiring every day. We do not know if the “Bush” tax cuts will expire, be extended or revised. Talk with your accountant to get his opinion and gain insight on what the best strategy or course of action is for your own personal situation.

Most folks believe the capital gains tax will go up. We just do not know if it will increase from 15% currently to 20 or 25%. Perhaps it will go up on a sliding scale. We also do not know if any change will be retroactive to the year the law is changed. (While most of us feel that a retroactive bill would produce a great outcry, the current president might embrace the obvious class warfare stance that would imply.)

This issue relates to the allocation of purchase price in a practice transition. There is usually a battle between the Seller trying to place as much of the asset in the capital gain category versus the Buyer trying to place as much of the asset into other categories that would allow them to depreciate the asset quicker. While this argument lessens if the capital gains rate goes up, there has always been an argument that the Buyer might benefit from saving some of his deductions for later years. Hopefully, the practice will grow more profitable over time and the owner will then be in a higher tax bracket due to the increased profit. Most of us feel that eventually we will return to some sort of increased progressive rate no matter who gets elected.

The buyer’s loan is also weighted much heavier in the early years with interest deductions. However, in the later years of the loan, the payments are mostly principle and there is no offsetting deduction. Therefore the deduction is more valuable in the later years to offset the increased tax rate. This also makes more sense now as inflation is so low. Ultimately, the argument between Buyer and Seller comes down to it costing the Seller a measurable amount of money which is burned up in taxes, compared to the Buyer who might even benefit from keeping some of the deductions for later.

We are currently exploring some ideas of placing a practice sale into a Deferred Sales Trust. My next article will explore the opinions of the accountants I respect as to whether that vehicle is worth exploring and what its effects are on both Buyer and Seller. .

Questions? E-mail wps@succeed.net

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