A matter of TRUSTS

Wei Xu, CPA, from Physio Accountant writes about the importance of trusts in the operation of physiotherapy businesses.

Trusts originated in England and have been in existence for hundreds of years. They offer the perfect structure for physiotherapists to build both their business and family wealth. In particular, trusts offer asset protection, wealth building features and tax flexibility. The most commonly used trust for running a sole-trader physiotherapy business is a family trust, and the most commonly used structure for running a multi-partner practice is a partnership of family trusts.

Asset protection

Every trust requires a trustee to run that trust. The trustee has the powers to make financial and legal decisions on behalf of the trust; in the absence of a trustee the trust will be inoperable. The trustee can be a company, or it can be an individual or several individuals. For physiotherapists running their businesses via trusts, it's important that you have a corporate (company) trustee. As a physiotherapist, you have professional indemnity insurance; however, if you are running a business, there are other threats to your financial and professional life. Having a corporate trustee of your trust to run the business will limit the potential financial liability that you, as a person, encounter.

A quality commercial solicitor will be an important part of your team of advisers when running the business, and that person will most likely advise you to not hold capital growth assets in your own name because of potential legal threats. If you have a personal partner who is not in business and so doesn't face the same risk, then that person may have some assets in their name.

You need to understand that it's the trustee that will be sued if there is a disaffected person trying to attack your growing business that is running under the trust. Therefore if a company is that trustee and it does not have any assets, your business is not at risk of losing its well-earned financial status or its physical assets.

Wealth building features

I mentioned above that developing your wealth as a practising physiotherapist can involve buying growth assets in your personal partner's name. Your personal partner will be one entity that can hold capital growth assets for the benefit of your family and not have those assets at risk. In addition, further wealth should be distributed from your business to an investment trust, which would also operate with a company trustee for asset protection.

An investment trust is established so that investment properties, managed funds, publicly listed shares and publicly listed units can be brought in, further protecting the assets of the physiotherapy business and developing wealth. This investment trust is another family trust that has all the asset protection and tax flexibility features of the trading trust that is running your business.

It is important that the paperwork is established correctly when setting up these wealth building and asset protective structures. Therefore make sure your advisors know what they are talking about with regards to trusts and also make sure that your advisors understand the required features of these trusts as they relate to physiotherapists.

Tax flexibility

For many people it seems far too complicated to be running a business from a trust. However, physiotherapists are very good at taking them on and know that, with the correct advice, they will have a number of features that offer tax flexibility. The risk lies in incorrect advice.

For example, if you are running your physiotherapy practice in a trading company structure, you will run into significant problems on a number of fronts. First, distribution of yearly profits is fixed via the share structure of the company, whereas with family trusts you can distribute profits in varying amounts to varying people each and every year. You cannot distribute profits to a child under eighteen years of age in a company structure, whereas in a family trust you can. These profit distributions to minors (effectively dependants who are under eighteen) from a trust each year are tax free and help to pay educational and child-rearing costs. This offers significant cash savings and needs to be understood by the business owner.

Traditionally the profit at the end of each financial year in a trust is distributed around the family to provide for education (as mentioned above for minors), living expenses and private mortgage payments. Then any excess profit is distributed to a company beneficiary. This builds the family wealth but also results in a low average tax rate to the physiotherapist and his/her family. The company that receives distributions only pays 30 per cent tax and allows the business to thrive and grow without getting too highly taxed.

Recently the Australian Tax Office (ATO) implemented changes to the way family trusts are run to build businesses in Australia, altering and making more complex the distribution of excess profit to a company beneficiary of the family trust. This has had a vital effect on physiotherapy practices so practitioners need to take heed.

Despite this, it is important to trust (pardon the pun) the tax and business advice of quality professionals who know the physiotherapy industry and can handle the paperwork behind this law change. It is also important to know that trusts are still by far the best structure to run a growing and thriving physiotherapy practice.

The final point to make on tax flexibility is that a trust structure is best if you want to sell your practice to a third party in the future, because of the capital gains tax flexibility. Third party buyers will not want to buy your tax/business structure; they will want to buy your business. So 'Acmetown Physio Centre' the business will be bought by a third party, but the structure that it runs from—'Bill Smith Pty Ltd' as trustee for Bill Smith Family Trust—will not be bought by that third party.

As a result, that third party buys the business of Acmetown Physio Centre and its owner, Bill Smith, will receive the full proceeds of the sale of the business through his Bill Smith Family Trust bank account—and it's likely that he won't pay any tax. This would not be the case in a trading company structure, in which the proceeds of the sale of Acmetown Physio Centre would likely be taxed at between 30 and 40 per cent.

It is important to understand trusts from an operational perspective, and to have trusted advisors to guide you in order to reap the asset protection, wealth building and tax flexibility features that these business structures can offer.

Physio Accountant is Australia's first accounting team specialising in providing accounting and financial solutions to the physiotherapy services industry. With our extensive knowledge and understanding of the industry, we can provide leading edge financial help and client service for every stage of your physiotherapist career. Visit www.physioaccountant.com.au.