Planning Partnership Changes

A Guide for GP Partnerships

Authors
Neil Mason Associates
Michael Hill Partnership
Grant Thornton UK LLP

In this Guide

Authors

Tom Mason
RICS Registered Valuer

Tom is a partner at Neil Mason Associates, chartered surveyors specialising in the healthcare and commercial property sector. He advises clients on surgery valuations, Notional Rent Appeals, third party rental valuations and the disposal and acquisition of property. Tom is currently advising LMCs how NHS changes will affect practices occupying NHS owned premises and is an active member of the Primary Care Premises Forum.

Jeremy Hill

Jeremy is a solicitor and managing partner at the Michael Hill Partnership. He specialises in commercial property, partnership and primary health care matters advising GP, pharmacy and dental practices and groups throughout England. Recent presentations to LMCs and GPs include 'The viability of incorporation of GP practices' and 'Health Centre Practices - the effects of the transfer of property from PCTs to NHS Property Services Ltd'. He is an active member of the Primary Care Premises Forum.

Steve Cosford

Steve has worked at Grant Thornton for 25 years and leads a healthcare team specialising in general medical practitioner clients. He works extensively with the team and clients on accounting and business issues affecting GPs as well as other entrepreneurial businesses. He presents to GPs and connected professionals on a range of topics including partner succession, the impact of tax changes relating to pensions and considerations for using different business structures for GPs' practice and private income.

Partnership is a long term relationship of mutual trust and shared interests

Although it is a relationship based on professional practice and business, for both the potential and continuing partners the starting point is to be sure they can work together and share values and objectives.

It is not a good idea to leap into a partnership without thinking through the potential consequences. Often likened to a marriage - but with multiple partners - you need to take time to get to know your future 'spouses' before tying the knot. Open communications and careful planning at the outset will avoid costly and possibly acrimonious disputes further down the line.

> Often likened to a marriage - but with multiple partners - you need to get to know your future 'spouses' before tying the knot.

The parties involved in a planned partnership change will fall into one of three categories; the continuing partners, the outgoing partner (unless the partnership is expanding) and the new partner.

This guide is intended to provide an outline of some of the major factors that all the parties should consider. It is based on the assumption that to ensure continuity, patient care and the development of the practice, the retirement of one partner will inevitably be an opportunity to recruit and appoint a replacement partner. It is worth noting that all parties will necessarily need to look at the same issues but from different perspectives. Although this briefing note is divided into sections for current, retiring and new partners, it would be worth reviewing all sections for a fuller picture of the considerations involved.

Ensuring continuity during a change in the partnership

Assuming an existing partner has indicated they intend to give notice or the decision has been made to expand, this section outlines the issues that current partners and the management team should consider early on in the process.

Management of the process

Almost above all else, ensure that one partner or the practice manager (or a small committee in a larger practice) has ownership of the day to day role of liaising between the accountants, solicitors, surveyors and any other professionals and has simple and timely lines of communication to the remaining partners.

There will be numerous issues to manage and changes to implement which will require considerable time commitments. Some redistribution of other workloads and allowances may be necessary between all the partners and management staff. Clear open communication and reporting, both internally and to your professional advisors, will be vital to reach agreement in a timely fashion.

Partnership agreement

It is vital at this early stage that you check the partnership agreement and note all factors relevant to a partnership change. If there isn't a partnership agreement, this must be rectified as a matter of urgency. Without a written agreement detailing how the partnership will operate, the partnership becomes a relationship that can be terminated almost at the whim of any partner (a 'Partnership at Will') and uncertainties are left to be decided by the Partnership Act of 1890. This leaves an uncertain and insecure future for all parties.

The partnership agreement should provide guidance on notice periods, property valuation procedures, methods and timings of payments to any retiring partner and continuity arrangements to ensure the NHS contract is preserved.

Draw up a timeline which should include all absolute dates, notice periods to partners and CCG, year end, any other trigger dates (such as payment dates to outgoing partners) and any requirement for a probationary period for a new partner.

Funding and taxation

Take accountancy advice as completion accounts may need to be drawn up, taxation will inevitably feature and payments will need to be timed. Simple advice taken early can affect the structure of any negotiations saving time, cost and tax and avoid having to unravel a hastily made agreement.

Clear open communication and reporting, both internally and with your professional advisors, will be vital.

Premises valuation

Premises will usually be the practice's single most substantial asset (and possibly liability) and will be a key issue both in negotiations with any incoming partner and in calculating payments to an outgoing partner.

It is important, when there are changes to a property owning partnership, that the value used when assessing the worth of each share is as up to date as possible.

> Bear in mind that the premises valuation process could take between four to six weeks from start to finish.

As such, you will need a full valuation which takes into account all parts of the property and any income associated with it. As such, the valuation report must be up to date to ensure that you have a true picture on which to base the calculations. You must decide early on in the process when you require your property valuation report by. Bear in mind that the process could take between four to six weeks from start to finish.

Once you have settled on the surveyor you are intending to use, which may take a week or so in itself, it will take a couple of weeks for them to arrange to visit the premises. Once they have carried out their inspection, it generally takes a week or two to prepare the report and post out a copy. Bear in mind that inspecting the property requires access to all parts and as such, it is easier to inspect when the property is empty or at the very least quiet. This could be on a training day or perhaps on a lunchtime when the premises may be between surgeries. In larger practices, where there is very little down-time, you will need to discuss with your surveyor how this can be done with minimal disturbance to staff and patients.

If a partnership agreement is in place, this will set out how the property is to be valued and any valuer you instruct will be required to follow this direction, unless you specifically ask them to carry out their valuation on an alternative basis.
In general when there is a change in partnership, it is likely that you require the valuer to value the surgery premises 'assuming continuing use as a medical centre and with vacant possession given on completion'.

However, depending on the nature of the building, you may need an additional valuation on an alternative basis such as 'assuming an alternative use such as residential or commercial'. If you are unsure what you require, discuss it with your surveyor.

The BMA/GPC recommend the use of a specialist medical valuer to value the premises. It would be advisable to appoint a surveyor who is not only a member of the Royal Institution of Chartered Surveyors (RICS) but is also a RICS Registered Valuer who has the specialist knowledge required when valuing surgery premises. When the surveyor visits the property, it will speed the process of preparing the valuation if relevant documents are available prior to their arrival. Plans of the premises will be very helpful; these need not be to scale but should give an indication of the layout. Details of the notional rent and any associated abatement should also be to hand. If there are any leases in place to third parties such as a pharmacist or dentist then copies of these should be given to the valuer as these will help to properly assess the value of the income these generate.

Surveyor visit checklist

- **Plans of premises**
- **Details of notional rent and any abatement associated with this**
- **Details of leases in place to third parties**

The main terms to negotiate

It is important that all existing partners agree the main terms that need to be discussed. This includes profit shares, any probationary period and the timing of payments and receipt of funds managed, particularly with any property (freehold or leasehold) transfers and mortgage arrangements. Agreed terms should be 'full and final' set out in retirement agreements and amendments or addenda to the partnership agreement. Lawyers familiar with GP procedures should be consulted to ensure transitional arrangements are understood and enforceable.

Creating firm foundations for an incoming partner

Many of the same issues need to be looked at by an incoming partner but from a completely different viewpoint. New partners will be investing time, effort, and often considerable amounts of money into what will probably be a lifelong relationship.

Each aspect of the proposal needs careful consideration. Unpicking an ill thought out and hastily arranged partnership will be costly in time, money and energy.

Partnership agreement

This should be the first thing you look at. If there isn't a partnership agreement, insist on one. Without a written agreement detailing how the partnership will operate, the partnership becomes a relationship that can be terminated almost at the whim of any partner (a 'Partnership at Will') and uncertainties are left to be decided by the Partnership Act of 1890. This risks an uncertain and insecure future for all parties. If the practice hasn't taken the time to get an agreement in place, it may indicate other issues regarding practice management.

You will then need to consider the main terms of the existing partnership agreement. This should include key issues such as automatic continuation, sickness and other leave; premises ownership; decision making, voting and meetings; suspension and retirement.

Any uncertainties should be clarified with advice from the partnership's solicitors and if the situation is still unclear, you should take independent advice.

How is the practice performing?

The next step is to assess whether it is a well run practice. Check informally with the LMC and any other contacts you might have as to the practice's reputation and record. Does the practice have a proper business plan? What is the patient list size? Are there other practices which will be competing in the local area? Are there training arrangements and career development opportunities? Meet with the partnership accountants and ask for a copy of any accountants' reports or written advice. Do some due diligence on the financials so that you can understand the overall profitability of the practice.

Ensure that you understand how your income tax liabilities will be calculated and the timing of when tax payments will be due, including whether the practice will save for this on your behalf or whether you will be expected to do this for yourself.

You will need an indication of your expected monthly drawings and how much of this you will need to save towards tax if the practice does not pay this on your behalf. You should also understand how the practice deals with the NHS pension scheme including the monthly on account payments that will be paid for you, the annual balancing payment / refunds that are due each March and the related tax relief implications.

It is also important to understand how partner capital accounts are calculated. These will usually be based on the last valuation less any practice balance sheet loans. The net equity buy-in requirement will be based on this subject to an up to date valuation, any off balance sheet practice loans and the timing of when this is expected to take place as defined by the partnership agreement.

At this stage you should also discuss partner current account balances including the expected level that you will be required to contribute and the period you will have to do this.

Considering the terms of the Partnership

- **Should a salaried role be considered first to test out the relationship?**
- **What are the time scales: is there to be a probationary period and what will be the notice periods?**
- **What are the proposals for profit share and progression to parity over time?**
- **What about any capital payments and premises obligations (see below)?**
- **How will the capital be funded?**

Premises valuation and ownership

If a valuation is being used in the negotiations between parties, you should ensure that this valuation is up to date. Valuations that are more than a year old should be updated to ensure that you have a true picture of the value of the premises. It is also advisable to request a copy of this report and read it thoroughly; do not just turn to the page that gives the capital value of the property! The report will contain important information including an assessment as to the suitability of the fit out of the premises and whether the income on any leases is correct.

If you are negotiating using a valuation that has already been carried out by the practice you may wish to be advised by your own surveyor as to the value of the premises. This could be in the form of an opinion on the contents of the report or could involve a second valuation being carried out if there are concerns about the first.

Are you fully aware of the structure of ownership of the premises? It's important to understand how the premises are held; ownership and occupation could be based on any number of combinations as to the freehold and leasehold. In some practices, the partners have set up a separate company to act as a property owning vehicle, leasing the premises to the practice. While both entities may involve the same individuals, it is important to be clear that, in the eyes of the law, they are two separate entities and as such, the lease should reflect that. Any lease that is in place should be relevant to the healthcare market, and tie in with the Doctors Rent and Rates Scheme.

Suitability of the premises

Whilst it is possible to come to an opinion of the current value of the premises, it is important to be aware of the future use of the building. Bearing in mind that an investment of this nature is long term, are the premises of a size to accommodate future levels of demand? Is there, for example, any planned residential development in the area which will dramatically increase patient numbers? Is there an ability to extend the existing premises to cope with any future demand? Does the building comply with current legislation set out by the Care Quality Commission and the Disability Discrimination Act? If not, it would be advisable to consult a surveyor to get specialist costings of the works that would be required to bring it up to current standards.

Is the specification of the fit out of clinical areas up to modern standards? Although current standards cannot be back dated on existing premises, there is a need to ensure that clinical areas conform as closely as possible. Older converted buildings will have greater difficulty in getting to this standard than newer purpose built premises.

Are there any large cost items within the premises that would need replacement or repair over the next few years? This could include items such as the boiler, the roof or any other internal services. Once again, if there is a concern in this area, it would be advisable to ensure that costings are to hand prior to completion. If you have any concerns about issues to do with the fabric of the building or the internal fit out, then it would be sensible to discuss them with the surveyor and to include any questions in your initial instructions to them.

> If a valuation is being used in the negotiations, you should ensure the valuation is up to date.

Specific financial questions

When will I be required to buy-in?

The partnership agreement will determine the timescales. The most common periods are at the date of joining the practice, on completion of the mutual assessment period or on achieving parity.

Why is the amount I am being asked to pay different to my share of the valuation?

There may be existing practice loans that you may be required to take a share of. You will only be required to buy into the net equity ie your share of the gross valuation less your share of the practice loan at the date that you buy in on.

I understand how the net equity has been calculated but how do I raise funds to finance this?

You will not normally be restricted to using the existing practice lender, although you may be able to obtain a preferential interest rate and terms by doing so. It is worth contacting your personal bank to find out what they are prepared to offer and your accountant should have the contact details for banks with a healthcare specialism who may also be able to offer preferential interest rates and terms.

What period should I take the loan over and what sort of interest rates can I expect to pay?

If it is an unsecured loan (which is likely to be the case if you are not using the same lender as the practice loan) then most lenders would prefer to lend based on a maximum 15 year term with a minimum commitment period of 5 years, but some are prepared to offer 20-25 years depending on your circumstances. Terms, interest rates and arrangement fees do change on a regular basis and so your accountant should be able to give you an idea of what is currently being offered, but it is of course up to you to decide on what is right for you and to understand the terms being offered.

Do I receive any additional monies to contribute towards the loan repayments?

You will receive your share of the cost / notional rent that the practice receives from the NHS, less your share of the repayment costs of any practice loans. This may not fully cover the repayment costs of your personal buy-in loan and so this may be a factor in deciding how many years you wish to take the loan over in order to achieve the required level of monthly repayment. You may also need to borrow additional monies to cover the cost of buying into the partner current account depending on how much this is likely to be and the timing of when you have to pay it. There will be no additional income to cover this cost and it will simply have to be funded out of your drawings.

What are the income tax implications?

Your taxable profit allocation will increase by your share of the rent received less your share of any loan interest on the practice loan (not the capital repayment element). Income tax and class 4 national insurance will be payable on the net amount at the highest rates applicable to you based on your overall net taxable income. You do not get tax relief on the capital repayment part of your loan arrangements as this is simply repaying the amount that was borrowed. You will also get tax relief on the interest element of the repayments on your personal buy-in loan. Any additional tax and national insurance due is payable with your six monthly self employed tax payments each January and July.

How and when does Capital Gains Tax become applicable?

Capital Gains Tax (CGT) is only payable at a future date when you sell all or part of your share of the building. CGT is payable on the difference between the cost that you acquired the share of the building that you are selling, and the amount that you actually sell it for. You have an annual exemption amount to cover any gains that you make each year up to a certain limit before you have to pay CGT. This applies to all aggregated gains in a tax year and not to each individual disposal. Any remaining surplus is subject to CGT at the applicable rate. It is important to ensure that you keep a record of the date and amount paid for any additional increases in share or improvements made to the property as this information is required when calculating the gain.

Capital Gains Tax (CGT) is only payable at a future date when you sell all or part of your share of the building.

What rate of CGT is likely to apply?

The rate of CGT will depend on your income tax bracket for the year in which you make the disposal and on your own personal circumstances. If you are selling a share of the surgery premises in connection with leaving the practice or reducing your hours then you may be eligible for entrepreneurs relief which could be a substantial reduction on any capital gain. Your accountant will be able to confirm if this is applicable to you.

Preparing a smooth transition for an outgoing partner

More than any of the other parties involved in partnership changes, the retiree should have the time to prepare and discuss options with trusted advisers and family. Then, in discussion with the other partners, a plan can be put in place taking into account the considerations set out below.

Check the partnership agreement

The partnership agreement will set out the notice periods required and terms applicable. Plan the remaining requirements around these terms. If there isn't a partnership agreement, it may be too late if the intention is to end it! In these circumstances, giving notice could have drastic consequences so you should seek legal advice as to the effects of the Partnership Act 1890.

Consider 24hour retirement or other options

It will depend on the partnership agreement as to whether this can be done unilaterally. Other options might include reduction in sessions or altering the profit share to enable a more flexible and gradual handover.

Financial tax and pension

Advice from your accountant and financial advisers regarding retirement and pension planning will be imperative. This should be an ongoing re-evaluation and not left until a few months before retirement. Organising your pension and budgeting for retirement will involve a full financial planning exercise to ensure the right products are exploited at the right time to maximise benefit and minimise current and future tax consequences. You should ensure that you are fully aware of any potential Capital Gains Tax liability (as highlighted on page 7).

Premises arrangements

As the most significant partnership asset, care needs to be taken in understanding what the effects of retirement from the practice will have on any interest in the premises. Is there a mortgage (or other loans) charged against the premises? What value will come out, how will it be paid and with what tax consequences?

Again, it is vital that you discuss the situation with your professional advisers in the run up to retirement.

However, it is sometimes the case that the best laid plans take a rather different course. Ill health, a sudden death or a partnership fallout can precipitate urgent and unforeseen discussions. If an urgent and unexpected decision is needed, professional advice will prove invaluable.

It is vital that you discuss the situation with your professional advisors in the run up to retirement.

Summary

A well-run and organised practice should always be ready for change.

Early discussion and planning will ensure that making partnership changes will be less challenging and onerous. Every practice should review and understand their existing partnership arrangements, how their premises are owned and managed and the basic terms applicable on a partnership change.

It's also important you review these arrangements on a regular (say three yearly) basis, to ensure that your arrangements fit within the current legal and financial structures, and within the NHS systems. This will simplify planning when change is required, minimising delays and the costs of 'last minute' panic measures.

Checklist for buying into a partnership

Partnership agreement

- **Is there one?**
- **Consider the main terms including**
  - automatic continuation
  - notice periods
  - property valuation procedures
  - method and timing of payments to retiring partners
  - profit shares
  - continuity arrangements
  - decision making, voting and meetings
  - suspension and retirement

Practice performance

- **Review the practice's business plan.**
- **What is the practice's reputation?**
- **Are there career development opportunities?**
- **Review the accounts.**

Tax

- **How will income tax be calculated?**
- **Will the practice handle this on your behalf?**
- **Take advice on tax reliefs and capital gains liabilities.**

Finances

- **Do you understand how the buy-in amount has been calculated?**
- **How are the partner capital accounts calculated?**
- **Review options for raising the buy-in funds and decide on an appropriate loan period.**
- **What are your expected monthly drawings?**
- **Review the NHS pension scheme arrangements.**

Premises

- **Is there an up to date valuation?**
- **What is the structure of ownership of the premises?**
- **Suitability of premises against CQC, DDA, NHS requirements?**
- **Will the building cope with future demand both for new services and increasing patient numbers?**

Planning Partnership Changes

Neil Mason Associates
The Byre
Spring Hill
Harborough Road Pitsford
Northampton NN6 9AA
01604 799010
info@neilmasonassociates.co.uk

Michael Hill Partnership
Top Hat Terrace
119 London Road
Leicester LE2 0QT
0116 204 6302
jmth@michaelhill.co.uk

Grant Thornton UK LLP
Grant Thornton House
Kettering Parkway
Kettering Venture Park
Kettering
Northamptonshire NN15 6XR
01536 315496
steve.cosford@uk.gt.com

This publication has been prepared only as a guide. No responsibility can be accepted by the authors for loss occasioned to any person acting or refraining from acting as a result of any material in this publication.