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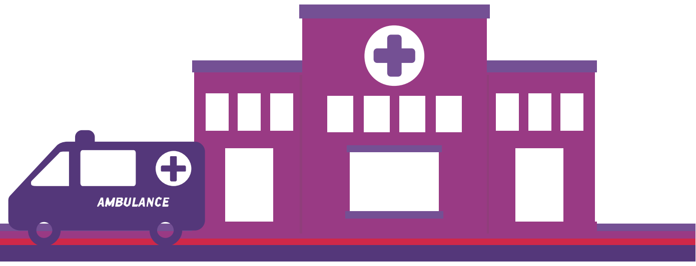
Understanding tax in the healthcare sector

Healthcare insights | Autumn 2016



Having faced unprecedented changes, with increased regulation and rising cost pressures stemming from the recent uplift in the National Minimum Wage and the newly introduced National Living Wage, the healthcare industry is experiencing challenging times.

In a sector where demand is certainly not an issue, operators will no doubt be thinking about ways to optimise efficiency and savings within the business. One of those areas is tax - both understanding the obligations and available opportunities.

Careful management of a business' tax affairs can reduce the compliance burden and maximise available reliefs to generate real cash savings, whilst ensuring all applicable tax law is considered. In this issue of Healthcare insights, we explain what steps can be taken to help unlock the potential hidden value within healthcare businesses.

Delivering on-going cash savings

VAT is a significant cost to healthcare operators with the majority incurring a 20% rate on most day-to-day running costs of a business. While these costs will normally be budgeted, operators will often incur unforeseen 'one-off' costs during the year on items such as temporary staff, repairs to heating/electrical systems, ad hoc maintenance and improvements. Careful VAT planning from the outset can help mitigate VAT and ensure that it does not become a burdensome cost to the business.

Operators should ensure that any budgeted capital expenditure is properly reviewed in order to take advantage of statutory reliefs such as reduced and zero-rated VAT. Historically, zero-rate relief has only been seen to be available on the construction of new care homes on new sites, or where existing homes have been demolished. In our experience, this view is changing and projects which may previously have been treated as standard-rated may now be zero-rated. Furthermore, architects and contractors are often unaware of the numerous reduced rates which apply to certain works, such as conversions, the renovation of empty premises and the installation of some energy saving materials. Sometimes small changes can be made at the planning stage to the building design or areas of spend which could fundamentally improve the VAT position.

Case study

Grant Thornton recently reviewed the details of an ongoing refurbishment project which was being invoiced by the contractor at the standard rate of VAT. The VAT costs payable by the company on construction and professional fees were projected to be £1.1 million.

Following a review of the scheme and negotiations with HMRC, we were able to agree in writing with HMRC that the contractors costs were subject to the reduced rate of VAT. Further re-structuring of the way in which the project was delivered to the business enabled us to reduce the VAT cost to £275,000.

Healthcare providers could also benefit from restructuring their business operations to enable recovery of VAT on ongoing running costs as well as capital spend. Restructuring business activities in this way must be carefully considered in conjunction with commercial objectives and be in line with strategic goals.

It is important to note that the UK is currently bound by EU rules and is unable to significantly extend the reliefs which are currently available to the healthcare sector. The impact on the VAT rules could be substantial once the UK exits.

Maximising reliefs

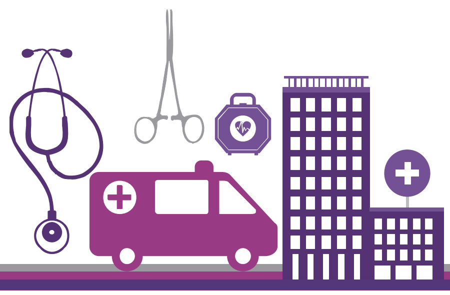
Aside from VAT, capital allowances are a valuable form of tax relief available on capital investment that can generate real cash flow benefits. Market research has shown that there are two fundamental areas of capital investment commonly undertaken where tax relief is often overlooked: property acquisitions and energy efficiency improvements.

Property acquisitions, including new developments and renovations of care homes, can give rise to advantageous tax reliefs through the capital allowances regime. The rules changed substantially for transactions on or after 1 April 2014, which mean newer acquisitions should have the capital allowances position clearly defined at the point of sale. However, older transactions and specifically those acquired from local authorities or NHS alike, could contain considerable levels of unclaimed allowances. In some cases, this could be up to 40% of the expenditure which presents an opportunity to make a claim.

Typical rates for capital allowances and VAT *

	Capital Allowances (%)	*VAT (%)*
Acquisition of building	Up to 40	20 / 0
Historic acquisition from a Local Authority or NHS	20 - 40	Review recommended if VAT at 20% paid
Refurbishment	Up to 80	20 / 5 / 0
New Development	Up to 60	0
Land purchase	0	20 / exempt
Extension	60 - 80	20 / 0
Energy efficient costs	Up to 100	5

**the rates above are a guide and can vary depending on specific circumstances*



Statutory obligations to improve energy efficiency are resulting in increasing costs to property owners and operators as various new requirements now in force require significant capital investment.

To counter the cost to business of this investment, the Government operates Enhanced Capital Allowances (ECAs), allowing the full cost of investment to be relieved immediately. The requirements of ECAs are unusually onerous and prescriptive, particularly around repairs and thermal insulation. As such, seeking professional advice before investment is recommended to ensure the tax and accounting position are optimised from the outset.

With the healthcare industry braced for financial challenges ahead, it is imperative that businesses take advantage of the tax reliefs available by assessing what value can be unlocked on current, future and historic projects. To that end, an outside perspective may help to navigate complex rules and to identify necessary savings.

Case study

Grant Thornton uncovered a substantial under claiming of Capital Allowances on a series of historic healthcare property acquisitions.

As a result of a grass roots review of historic accounting records and a re-classification of leasehold and building expenditure, our analysis identified additional tax relief of £1.5 million.

Other tax considerations…

1 Potential interest deductibility restrictions

From 1 April 2017, new rules will be introduced that may limit tax deductions for net interest expense to 30% of the EBITDA for UK corporation tax payers.

2 The Apprenticeship Levy

The levy will come into effect from 6 April 2017 and requires all employers operating in the UK, with an annual pay bill of over £3 million, to pay a 0.5% levy on the pay bill. The levy must be spent on training apprentices and optimising this expenditure (while remaining compliant with government guidelines) will be crucial.

3 Employment issues

Investment in attracting and retaining staff is vital to maintaining standards and lowering agency costs. The right incentive plan could motivate employees and in turn boost business.

4 Rationalising your group structure

Seeking advice as early as possible could be advantageous to realise potential tax benefits and make the structure tax efficient.

Grant Thornton's Tax services

Our team of highly experienced tax professionals advise healthcare clients across both the public and private sector on a wide range of issues. Our clients range from family owned care home businesses to GPs, healthcare funds, REITs and specialist healthcare investment companies. We help them to navigate the complex world of tax across a range of matters on an ongoing basis.

Our tax experts, specialising in areas such as direct tax, VAT and capital allowances, can guide you through the minefield of continually changing regulations to help you mitigate costs and realise your commercial ambitions.

Please get in touch if you would like to find out how we can help your business:

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Grant Thornton's Healthcare team

Grant Thornton has considerable experience of working with the Healthcare sector. Over the last year, our team of Healthcare specialists have been particularly active, advising the shareholders and management teams of dynamic businesses at various stages of their lifecycle.

The Healthcare team provide a holistic approach to solving our clients' problems. Alongside our excellent corporate finance, restructuring and due diligence services, we also have more bespoke offerings, such as CQC reviews performed by an experienced nurse practitioner, our Place Analytics team which provides demographic and geographic data analysis and mapping to social care businesses to assist them with strategic decision making and our Business Consulting team which provides performance improvement, working capital advisory and operations advisory.

The key to our offering is our ability to provide the 'best team' to match each client's individual needs. Our team is made up of highly experienced professionals, with a combination of financial, operations and clinical skills – combining robust professional services knowledge alongside colleagues with years of experience in industry as practitioners.

Please contact our experienced Healthcare advisory team to find out how we can help your business:

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