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the editor's corner

Prior to the advent of professional corporations, it was customary for orthodontists to count income in excess of practice costs as profit, which represented the orthodontist's net income. Thus, "profit" in 1978, in the average orthodontic practice was 52.3% of gross income. With the proliferation of incorporation of orthodontic practices and with the blurring of professional and commercial characteristics, this type of accounting will no longer do.

It is, and always has been, wrong to create the impression that orthodontic practice was that "profitable". There is no business on earth that does not include the chief executive officer's salary as a cost. The proper procedure is to allocate an annual salary for the orthodontist as a cost, along with the salaries of the other employees of the corporation. In a practice that has a gross income that is below average, it may well be that the doctor's salary will consume all of the net income after other practice costs. In that category, he will need all the income he can get to support a reasonable standard of living. However, once the practice income exceeds the average, then the net income after costs, including the doctor's established salary, can become a fringe benefit and contingency fund.

This fund permits adjustment of salaries at year-end, according to the amount of this net income, through bonuses; and it allows for fringe benefits for the doctor and for the staff. These include medical benefits, insurance benefits, auto benefits, uniform allowances, and retirement plan benefits.

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EDITOR'S CORNER

Many orthodontists refuse the discipline of incorporation and salary, even though they know that their salary is adjustable through bonuses at year-end and through retirement plan contributions and other fringe benefits; and that the structure of corporations is such that the doctor is eligible for a disproportionate share of the practice income. Many of these have merely had no advice or poor advice. Many are simply unable to discipline their spending and, indeed, have their expenditures exceed their income. They can even find solace in the often heard opinion that "a dollar saved is a dollar lost" due to the rate of inflation and increased costs, and the difficulty in finding investments which keep up with inflation after taxes.

It is precisely this difficulty with finding investments which keep up with inflation which recommends a retirement plan in a professional corporation. You don't have to be a genius. You don't even have to have any special knowledge about investment to come out better in your retirement plan than the most knowledgeable and sophisticated of investors. With no risk. You come out better, mind you. Not fantastic, but better.

Here's how. If you were to invest $10,000 a year in your retirement plan in a money market fund, it presently yields better than 10% a year. Let's say 10% a year. That means that in seven years, by the famous rule of 72, you would double your money. Now someone interrupts to say, "Yes, and when you take it out, it is taxed at 60%". That is correct. So, if the fund terminated in seven years, that first $10,000 would only be worth $14,000. If inflation during the seven years was 10% a year, you'd be left with only about $8400 in Year 1 purchasing power. That doesn't sound like a winner.

Maybe so, but everything is "compared to what". If you compare that to an investment yielding a long term capital gain, which is taxed at only around 30%, you'd possibly expect the long term capital gain to far exceed that measly retirement plan investment. Well, if my calculations are correct, it would take a long term capital gain of about 37% a year for the same seven years to equal the "measly" retirement plan. The reason is that the retirement plan investment is made in before-tax dollars and the long term capital gain investment in after-tax dollars.

You might say, "I was right the first time. I'm better off spending it, in that case". Maybe so, but I think it is a question of — Would you rather wind up at the bend in the road sorry that you had set aside money in a retirement plan or wishing that you had? □