



Do Not Buy or Sell a Dental Practice Until You Read This

Historically, Dental Practices have been selling for a premium in California for years. This has been a direct result of supply and demand, i.e.: more Buyers than Sellers which has driven the sale prices higher than ever. The reasons for more Buyers than Sellers is four fold: (1) More Graduates than Retirees, (2) CA State law was changed to allow a DDS to own as many practices as they wish. Previously, the law stated that a DDS could own a maximum of two practices, (3) CA State Law was again changed to allow out of state licensees to credential into the state of CA versus having to apply for and take the state dental exam, and (4) Many dentists took a bath years ago when stocks crashed and they were forced to postpone retirement. This and the after effects of 911 slowed the sale of dental practices for years...doctors simply couldn't afford to retire. The result has been a Seller's market. Now, many doctors have either attained their financial retirement goals or decided they've had enough time "in the mouth." The market is changing and the "seller's market bubble" is showing signs of deflation. The market is fast approaching an equilibrium situation with an equal number of buyers and sellers. Soon the market will have more sellers than buyers creating a Buyer's market.

Over the next 10 years there is an estimated 49,421 dentists that plan to sell their dental practice and retire. These are what the Economists call the "Baby Boomers". Over that same 10 year time frame the Dental Schools plan on graduating only 45,871 new dentists, leaving a shortfall of over 3,500 new dentists. The future is not that bright for sellers unless they either transition sooner than later or put a long term plan in place to prepare their practice for sale.

Now is still a good time to sell...or at least enter into a buy-out agreement. Although interest rates have fluctuated over the last couple of years, rates are still well below historical highs, Inventory is relatively low and buyer demand is still reasonably strong. These conditions will not last forever. More and more sellers are listing or calling to get appraisals in anticipation of selling some time soon. Rates have inched up and graduating classes are getting smaller.

Determining exactly what a dental practice is worth, and what it is capable of generating is vital to buyers. Understanding the value of all of the practice's assets is vital to the seller. This article will provide guidelines for both.

SELLERS:

As we have learned, the market will herald in a Buyer's market. Buyers will be able to peruse through a multitude of practices that will be for sale and they will be able to choose the pick of the litter when buying a practice. And they will also be able to dictate the sales price. Sellers can either get out and sell now or groom their practice for a later

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sale but understand this, grooming your practice doesn't mean esoterically increasing its perceived value...it means honestly increasing its value. This is something you may be doing without recognizing it. If your practice has hit a plateau or is in decline...then you are not doing this.

So...you either sell soon, which should be an option for you dentists who are presently on the fence, hanging on, or thinking of hanging on, or determine an exit strategy. Your exit strategy will include a) how long you plan on practicing for, b) generate a plan that creates a practice that will be in high demand in the future and then, c) implement the plan. In either case, you need a plan that will demonstrate the strengths of your practice and then implement that plan. If selling soon, you should review your practice the same way a lender would, evaluate it and perhaps even give it a face-lift. Kind of like selling a home...you might plant flowers or install an impressive new front door. Small things can make a big difference. Some of you may consider selling your practice yourself. Statistics show that For Sale By Owners (FSBO's) by and large fail to sell their practice and ultimately list with a Broker. Many FSBO's end up dealing with avoidable litigation. Doctors that do successfully sell their practice themselves usually get less than full value. FSBO's waste a lot of time, time that could have been productively spent doing dentistry while a professional takes care of the sale details. FSBO's often end up wasting valuable time with lookie-loos and wannabe buyers who are not pre-qualified and rarely end up buying anything. If you hire a professional to weed out the bad buyers from the good, show the practice, write up and close the transaction, help the buyer get financed, handle the lease transfer and numerous other things; you can do productive dentistry without the stress or liability that can arise from neglecting a particular issue. I will also point out that a dental broker is trained to minimize the many risks associated with selling one's practice. They work hand in hand with the seller's dental attorney to assure that all the legal aspects of the transaction are properly covered. If a FSBO makes one error, one wrong move, it could ultimately cost them many thousands of dollars and/or open them up to potential litigation. Finally, let me point out that one should consider whether to hire a full service broker or a discount broker. If you hire a discount broker, you must be willing to do most of the work yourself as most discount brokers charge extra to show your practice, to do the paperwork, to perform escrow functions, to generate the Buy-Sell Agreement, to transfer the lease etc. Most full service brokers include most if not all of these services and more in their quoted fee.

PREPARING YOUR PRACTICE TO SELL:

Preparing your practice for sale is much like preparing your house for sale. The Real Estate Agents tell you that you have to create "curb appeal" and that you need to generate the right impression, and that appearance is key. They tell you to remove the clutter, to make your home neat and clean, and to price your home right. That is great advice to sell your home, and it is great advice to sell your practice. Think esthetics, eye appeal and neatness. Buyers are as interested in the overall look and feel of the practice as they are in the financials and patient records.

CURB APPEAL (SPRUCING YOUR PRACTICE):

Start at your office front door. Is it worn, is the hardware old and tarnished, has your door signage seen a better day? Then paint or stain the front door, put on a new door

knob, and make sure signage is in good shape. 1st impressions with a Buyer are very important.

Next, take a walk through your office. Is the furniture in the waiting room worn and frayed? How's the paint on the walls? What about the carpeting? Are there burned out fluorescent lights? How is the lighting? Is the office clean? Really clean? Is the office cluttered? If the answer is yes, then get to work! Replace that worn out waiting room, paint the walls and replace some carpeting, change burned out bulbs and make sure that the office has good lighting. Lighting makes all the difference. Clean up the office. And I mean deep clean!! Come on, this is a place that renders health care! The cleaner the better. I have been in to many offices that I would be afraid to open my mouth in. Just imagine what a buyer thinks about a dirty office. Throw out the clutter. That means magazines, boxes, no longer used dental disposables, broken equipment, etc. Empty that op that you've been using as a catch all room. How's a buyer going to see the potential for an additional operator if the room is filled with junk??

....you have to create "curb appeal"

Now that you've tackled the facility and furniture, it is time to take a look at your equipment. Is all your equipment in working order? Are the chairs torn? Is your slow speed belt driven? Are you still hand dipping X-Rays? If you were a buyer would you buy your office with broken down, worn out, torn, antiquated equipment or would you be more inclined to buy a practice with equipment that is in working order, in good shape and manufactured in this century? Get a maintenance guy to come in and go through your equipment. Fix what's fixable, replace what is not. Make it work or replace it. You don't have to spend a fortune. If you replace it, you don't have to buy new. There are several reputable used equipment resellers that can replace an op for you with refurbished equipment at a reasonable cost. There are several companies who can reupholster your chairs and do equipment maintenance for you.

When all is said and done, do the final touches like air fresheners, fresh flowers, coffee in the waiting room, and I've even know a few sellers who have added a portable cookie maker in the waiting room.

Now that the office is ready to show, it's time to do your paperwork. Yes, paperwork. Many doctors dislike doing paperwork but if you do not have adequate records available for review, buyers will pass on your practice and move on to the next one. You need to have available the last three years of tax returns for the practice and a P&L for the current year. In addition, you will need to have available an Account Receivables (A/R's) Report, a copy of your Lease Agreement (if renting) and bank statements showing all bank deposits, (this info will be needed for the buyer's CPA to review after opening escrow). While you are looking at your account receivables, look at the delinquent accounts. Formulate a plan for collecting these A/R's and implement the plan. No one wants to buy delinquent A/R's, and unless you don't want to get paid for them, you must send out some kind of letter to the patients, preferably with some kind of motivational discount, in an attempt to get the

patients to pay. Other alternatives are to retain a collection agency or write them off.

Buyers love computers. If you are not computerized, think about doing so. Since you've implemented a plan 3-6 months before selling, you've got one recall before hanging up the hand piece. Get those patients into a computer with some kind of dental software. It will be a good jump start for the buyer, make your practice more attractive and not cost you all that much.

When you're ready to Sell - **PRICE IT RIGHT!** Each practice is unique and depending on the location, profitability, esthetics, type of practice, asking price and many other factors, some practices sell instantly while others require months. Understanding the positives and negatives of your office and placing a realistic price and time schedule to close an escrow on your practice is something your broker can explain once a comprehensive appraisal has been completed.

ADVANCE PREPARATION:

Ok, so you're not ready to sell right now. That doesn't mean that you shouldn't start taking steps that will facilitate the sale later. Major decisions that you make today will impact the sale of your practice in the future. Whether you are deciding to go high tech, remodel the office, or sign a new lease, you should weigh your decision based upon: (1) what is the impact to the practice now? and (2) what will be the impact to the practice when I am ready to sell? To demonstrate: many dentists today are looking at adding high tech dental tools to their practice such as lasers, Cerec machines, digital x-rays, and the like. If you are one of these dentists, you should not only consider the increased efficiency these items will bring to your practice and the cost to acquire them, but also how they will allow you to better enjoy dentistry and what these assets will add to the value of the practice when you execute your transition.

SOME OTHER CONSIDERATIONS INCLUDE:

Should you completely remodel the office? Maybe. If the office will look and feel better, or if it will make the office more ergonomic, then yes. Your patients will enjoy it, the staff will enjoy it and so will you. Just as in real estate, easy renovations can not only be self-liquidating expenses when preparing to sell, they can actually increase profitability. A little drywall and neon lighting to enhance the reception desk area can increase the value of your practice considerably.

Should you sign a new long term lease? That depends upon the terms, your plans and what the Assignment clause says. If you are planning on staying a while, you should not only secure a lease that covers the timeframe that you are planning to stay, but some additional time to cover a new owner. Practices are tough to sell with little or no lease time left and landlords are often ruthless in demanding rate increases for new leases, extensions and renewals. Make sure that your lease states that you, as the Assignor on a lease, are not held secondarily responsible should the Assignee fail to perform.

Should you hire additional staff? If the workload warrants it, then yes but only if it's absolutely necessary to maintain production. Remember, you want to keep your overhead

low. Generally, additional staff means more productivity, more revenues and therefore more net income. More net income means a higher sale price down the road. One way to value a practice is based upon it's True Net Income. The same goes for Gross Collections. Generally speaking...the higher the Gross Collections, the higher the sales price.

Should you slow down or sell while your numbers are higher? That depends on your situation. If you are not ready to retire and want to slow down and you can afford a lower sales price later, by all means slow down. Realize that you will be making some income while you do work, which will offset some of your lower sales price later. You should also consider bringing in someone to pick up the slack enabling you to maintain or even increase production.

Should you computerize if you are not computerized? **ABSOLUTELY!** It is unwise to think that you can efficiently run a dental practice today without the help of a computer and dental software of some kind. This single change will produce significant improvements in your scheduling, production, collections, and the ability to market the practice. All real pluses while you are still running the practice. Later, this single tool will help you to more easily sell the practice. You will be able to provide a buyer with all the information needed to adequately evaluate the practice and because the office is computerized, it will make it more attractive to a buyer looking at other practices that are not.

BUYERS: WHEN TO BUY?

As previously pointed out, the time is coming when the market will soon be a "Buyer's Market." Buyers will be able to pick and choose among many practice options. Whether a buyer purchases now or waits is an individual call based on his or her needs and goals. Regardless, one should not buy a practice until they feel comfortable with their hand skills and are ready to tackle the business end of a dental practice. There is a lot to know and deal with including: the EDD, employee-employer issues, OSHA, insurance billing, landlords, patient complaints, suppliers, equipment breakdowns and payroll, just to name a few. When you think you are ready to purchase a practice, you need to answer a few questions before you start looking. You first need to decide what area do you want to acquire a practice in. Next, what kind of practice do you want? A Fee for Service? An HMO? Will you accept PPO's? What about Denti-Cal? Next, you need to determine how large of an office do you want, both from a square footage standpoint and the number of operatories. Are you going to work by yourself or are you going to have a partner or an associate? This will determine how many ops you need. Next, you have to determine what kind of facility do you want the office to be in. A free standing building, shopping center or a professional building? The former two have visibility and exposure and tend to get walk-ins whereas the latter has a more professional look and feel and would tend to lend itself to more of a Fee for Service type practice. What do you need to earn? This question will determine how much the annual gross collections of your practice needs to be. You can use the following rule of thumb as a guide; "the average dental practice in the United States has an overhead of 60-65% which results in a net income of 35-40%." Please note that these

numbers are averages and the overhead number does not, I repeat...does **NOT** contain the Practice Acquisition Loan payments.

After you've determined what you are looking for, it's time to put your acquisition team together. Team?? Yes Team! Since most buyers are unfamiliar with the various aspects of a practice purchase, it would be wise to put a team together to help you in your practice acquisition. This team normally includes:

1) A Practice Broker - who can show you various practices, point out the pluses and minuses and generally provide you guidance thru the acquisition process.

2) An Equipment Technician - who can check out the dental equipment for you. He can tell you what's good, what's bad (or will go bad) and what's missing.

3) A Practice Management Consultant - who can independently check out the business end of the practice for you and determine how much gold is in the existing patient files or whether they've been already mined out.

4) A Practice Acquisition Loan Company - who can help you to obtain your loan(s).

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5) A Certified Public Accountant (CPA) - Preferably one that is versed in dental practice economics. The main purpose of the CPA is to verify that the collection numbers that are being reported are true and correct. The CPA will verify the records, look for any anomalies and help you with the Purchase Price Allocation (a breakdown of the total sale price by component of the practice). These components include the equipment, the goodwill, the covenant not to compete, the dental supplies and the patient charts and records. This allocation will have a great impact on both the buyer & seller's taxes so it is imperative to have some expert assistance in developing the numbers.

6) An Attorney - Only someone who is versed in Dental Practice Acquisitions. They will give you an independent legal review of the Buy-Sell Agreement (a detailed Purchase Contract), Covenant Not to Compete and the Office Lease.

Without a team such as this, a buyer is walking into a dark room without a light and will be clueless where he or she is going. Since dental practices cost hundreds of thousands of dollars, it is prudent that a buyer assemble this team to guide them in their practice acquisition process.

After you've determined what you are looking for and who your team is, it's time to go find your practice. You should find one that fits you like a glove. You've taken a long time to get to this point in your career. Use good judgment when selecting a practice and be honest with yourself. Does this practice meet my expectations? When you think you've found the right one, perform a thorough "Due Diligence" checklist. A proper "Due Diligence" checklist includes a review of: (1) The financial records of the practice, (2) The equipment, (3) The office lease, (4) The Yellow Page Ads and other marketing/advertising projects of the practice, (5) The Patient Files (Number and Type), (6) The number of new patients generated per month and how they are obtained, (7) Type and Number of Provider Contracts, (8) Practice Financing (Loan Acquisition and Working Capital), (9) Computerization, and (10) The Practice Acquisition Contract (Buy-Sell Agreement and Covenant Not to Compete).

Use your team to help you perform your "Due Diligence" checklist. When you've completed your reviews and you are satisfied that the practice checks out to your satisfaction and all of your purchase contingencies are met, then you can close your escrow and begin life as a Practice Owner. There are numerous advantages to being an owner and many doctors find the challenges and rewards greatly offset the added responsibilities. It's nice to be in the driver's seat and to be able to steer your dental practice in the direction YOU want to go. Just make sure the vehicle is priced right and capable of making the journey. Done correctly, the buyer and seller should both be happy and confident that they've made the right move without worrying about litigation later on.

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PRACTICE SALES AND LEASING

D&M Practice Sales and Leasing is a Full Service Dental Brokerage located in the San Fernando Valley. D&M specializes in the Appraisal and Sales of Dental and Medical Practices, Arranging Financing for Dental and Medical Practices and the Leasing and Sales of Dental and Medical Buildings and Office Space. The principle is Paul A. Maimone M.B.A. a CA licensed Real Estate Broker. He received his undergraduate degree from Northeast-

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