Financial Matters

Practice transition planning

This is part 1 of a two-part series on this topic

By Eugene Heller, DDS

For most dentists, ownership of their dental practice is the major focus of their energy expenditures, financial situation and professional lives.

Years of blood, sweat and tears, coupled with the relationships formed with both staff and patients, have caused dentists to form a deep-seated emotional attachment with their practice.

For many, the dollar value of that practice represents a significant portion of their financial assets.

For the new dentist, there is a definite value in acquiring the patient base that has taken the transitioning dentist years to develop and will provide an immediate and substantial cash flow.

All experience transition

Whether it is due to a change in career direction, a desire to cut back on the responsibilities of ownership while still enjoying the benefits of clinical dental practice or the desire to retire from dentistry, every practice owner faces an ownership transition.

Ownership transition can be a total sale or a partial sale, that is, the formation of a partnership. The level of success achieved as a result of this practice transition will be directly linked to the amount of detail given to, and the successful execution of, the "Transition Plan."

A buyer's market

Decreased dental school enrollments and other demographic factors have created an imbalance in the numbers of graduating versus retiring dentists.

This trend, which will continue for at least the next 10 years, has contributed to falling dental practice sale prices, and has created a buyer's market.

This dental work force shortage has made finding dentists to serve in more rural dental practices, which are difficult to market, almost impossible. These changes in the marketplace relative to practice transitioning have made advance, detailed transition planning mandatory.

Goals of a successful transition

Before discussing the development of a transition plan, a brief discussion of the goals of transition is required. In addition to identifying the actual goals, each dentist will need to assign an order of priority to these goals.

This prioritization will have a significant impact on certain aspects of the transition plan. The most common goals discussed by dentists include:

(1) In accordance with their preferred timetable, a desire to transfer patient care responsibility.

(2) Securing future employment for their staff and giving back to the profession by passing the baton to a new dentist.

(3) Maximizing their practice equity (financial gain from the sale).

There is no right or wrong order to the priority emphasis. The economic health of the transitioning dentist will usually determine the order of the priorities.

If the practice sale proceeds are a significant portion of the dentist's retirement assets, then maximizing the financial return will be at the top of the list.

If the clinician has a well-funded pension plan or other financial resources, and the sale proceeds will enhance the quality of retirement rather than providing the primary support for retirement, the order of importance will typically be the desire to provide continuity of patient care, ongoing employment and passing the baton, where maximizing the financial gain appears at the end of the list.

Factors affecting successful transitions

Prior to discussing the components of a transition plan, it will be useful to understand what is presently occurring in the transition marketplace. For a successful transfer of ownership, we must first have an interested new dentist.

Subsequently, location is at the top of the list relative to a new dentist's interest in a specific practice opportunity.

As previously discussed, rural practices, although typically more profitable than big city practices, are having serious recruitment problems.

Ninety percent of all practice sales today are in communities with populations of 50,000 or more, and 80 percent of these sales are in cities where the metro population exceeds 500,000.

The second factor is the practice’s ability to meet the financial needs of the new dentist. As a result of current levels of dental school-related debt, the new dentist must meet specific levels of production to pay for the practice acquisition, school loans and basic living expenses.

Therefore, a practice needs to provide, on the average, $500,000 worth of production for an employed dentist, and $400,000 worth of production if the dentist is purchasing a practice.

It is for this reason that 85 percent of total practice sales involve practices with gross receipts of $550,000 to $500,000.

While the highly productive and profitable practices of today frequently exceed $500,000 in annual receipts, the average new dentist (five years or less since graduation) does not possess the clinical skills required to produce this level of dentistry, and subsequently, sales trend toward the lower grossing practices.

After finding a suitable location and determining that the practice will provide for the financial needs of the new dentist, the new dentist will consider a multitude of other factors in selecting one opportunity over another.

The major factors considered include:

(1) the practice’s overhead to revenue percent,
(2) number of active patients,
(3) new patient flow,
(4) recall system effectiveness.

In addition:

(5) quality and length of the staff’s prior employment,
(6) practice history,
(7) types of procedures previously offered and/or produced,
(8) involvement in any discounted dental plans,
(9) appearance of the physical space occupied by the practice, and
(10) the age, type and appearance of the equipment and furnishings will play a major role in the selection process.

The 10 items listed above represent the major concerns and factors reviewed by the new dentist.

However, the owner dentist is concerned with:

(1) the ability of the new doctor to pay for the practice — obtain financing with all the school debt, the tax implications and subsequent net proceeds derived from the sale,
(2) the personality and ability of the new dentist to relate to patients and staff,
(3) the amount of post-sale relationship required between the seller and buyer, and of course,
(4) the new dentists’ clinical competence.

With the exception of the final concern, the other factors can be readily determined and resolved.

Today, 100 percent owner financing is readily available, the tax implications can be calculated and, typically, several meetings with the new dentist will address the communications skills and personality of the new dentist.

About the author

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